TaxTalk

Simplifying the complexities of Tax

October 2023

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Are you up to date and maximising your Capital Allowances?

Capital allowances have always provided a valuable tax relief for businesses to enable them to reduce their taxable profits or increase losses for future benefit - both resulting in more cash in your business. With the increase in corporation tax to 25% from 6 April 2023 and the current economic conditions, are you maximising your claims?

As a business, when you incur expenditure it will either be capital or revenue in nature. Capital revenue as a starting point is not deductible for tax purposes, however relief is provided by way of capital allowances. Capital allowances can be claimed on items which you keep to use in your business – plant and machinery (P&M). There are different types and rates of capital allowances, some of which are more favourable than others. It is important to note that generally the relevant assets must be owned by the business; any assets leased or under hire purchase have their own special rules.

Annual Investment Allowance

The headliner for the past few years has been the Annual Investment Allowance (AIA) which provides 100% immediate tax relief on assets which qualify as P&M. When it was first introduced in 2010, the threshold was only £50,000, however this eventually reached £1,000,000 in January 2019 initially as a temporary increase, then becoming permanent and still stands today. In a partnership, AIA is only available where all the members are individuals. If your business is in a group, you are only entitled to one AIA allowance.

There is also the First-Year Allowance (FYA) which permits 100% deduction of the cost, but with no limit. This is commonly seen in respect of electric cars and those with zero CO2 emissions.

Super-deduction

2021 saw the arrival of the super-deduction, the then Chancellor Rishi Sunak announcing it as “the biggest business tax cut in modern British history”, although arguably a way of softening the impact of the soon to be hike in Corporation Tax.

The super-deduction provided a FYA of 130% for main pool and 50% for special rate (SR) P&M expenditure incurred between 1 April 2021 and 31 March 2023. For those of you who know your allowances, the special rate includes ‘integral features’ (i.e. items such as electrical power and lighting, hot and cold water, heating, ventilation and cooling).

Most businesses are currently finalising their tax returns with their final super-deduction claims at the moment. A key point to be aware of is that not all expenditure on plant and machinery will qualify for either the super-deduction or the SR allowance.

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For example, expenditure on assets which are purchased in order to be leased out will not generally qualify. In addition, the contract for the purchase of the asset must have been entered into after 3 March 2021.

Full expensing

As the era of the super-deduction was drawing to an end, many businesses faced with increasing costs started to wonder what the Government would do to stimulate investment. Full expensing was announced by the Chancellor in the 2023 Spring Budget and applies to expenditure incurred from 1 April 2023 to 31 March 2026, to companies (or corporate partners of partnerships) only.

Main pool assets will be eligible for 100% relief and a 50% first-year allowance will be available for qualifying special rate assets. For example, if a business spends £1 million of qualifying expenditure, under the full expensing regime, this would offset against income, saving tax of up to £250k at a 25% rate of corporate income tax. Full expensing is only available for expenditure on P&M; there are also some notable exclusions, such as cars, as well as many assets used for leasing.

Writing Down Allowances

No capital allowance article would be complete without a quick mention of Writing Down Allowances (WDA). WDA will apply if assets do not qualify of AIA or FYA, or when the maximum limit has been reached. The WDA enables your business to offset a % rate every year on a reducing balance basis.

Assets must be allocated to the correct pool; main rate pool attracts a rate of 18% and special rate pool (integral features) attracts a rate of 6%.

Property and capital allowances

Property and capital allowances has always been a complex area. If you are acquiring, building, fitting out or refurbishing commercial property be sure to seek advice to maximise any claims. Claims are also possible for the communal areas in apartment blocks that are held as investments, or serviced apartments and furnished holiday lets held as investments. If you are buying a commercial property take advice before the purchase.

As well as having access to the range of allowances previously mentioned, there are a couple of other additional mechanisms for relief with property:

SBA

The Structures and Buildings Allowance (SBA) was introduced in 2018 and provides tax relief for expenditure incurred on certain assets that would not previously have qualified for capital allowances. This includes works on structures, walls and ceilings.

Relief is available on a straight-line basis currently at 3% per annum and is not available for expenditure incurred on buildings which are in ‘residential use’. When SBA is claimed there is a reduction in the base cost of the property for Capital Gains Tax purposes when the asset is subsequently sold.

Land Remediation Relief

Companies that acquire contaminated or derelict land for the purposes of their trade or UK property business can claim an enhanced deduction of 150% for clean-up costs.

It is available to developers, investors and occupiers, and for both commercial and residential property. The relief is not available to partnerships; however, a company that is a member of a partnership can claim.

What now?

With businesses starting to adjust to the increase in corporation tax to 25%, access to capital allowances is increasingly valuable. Planning is key. Before you undertake large items of spend, seek advice to ensure that any claims can be maximised, to reduce the amount of tax that you pay and increase cash flow.

If you’d like more in-depth guidance and advice, please contact Catherine Heyes.

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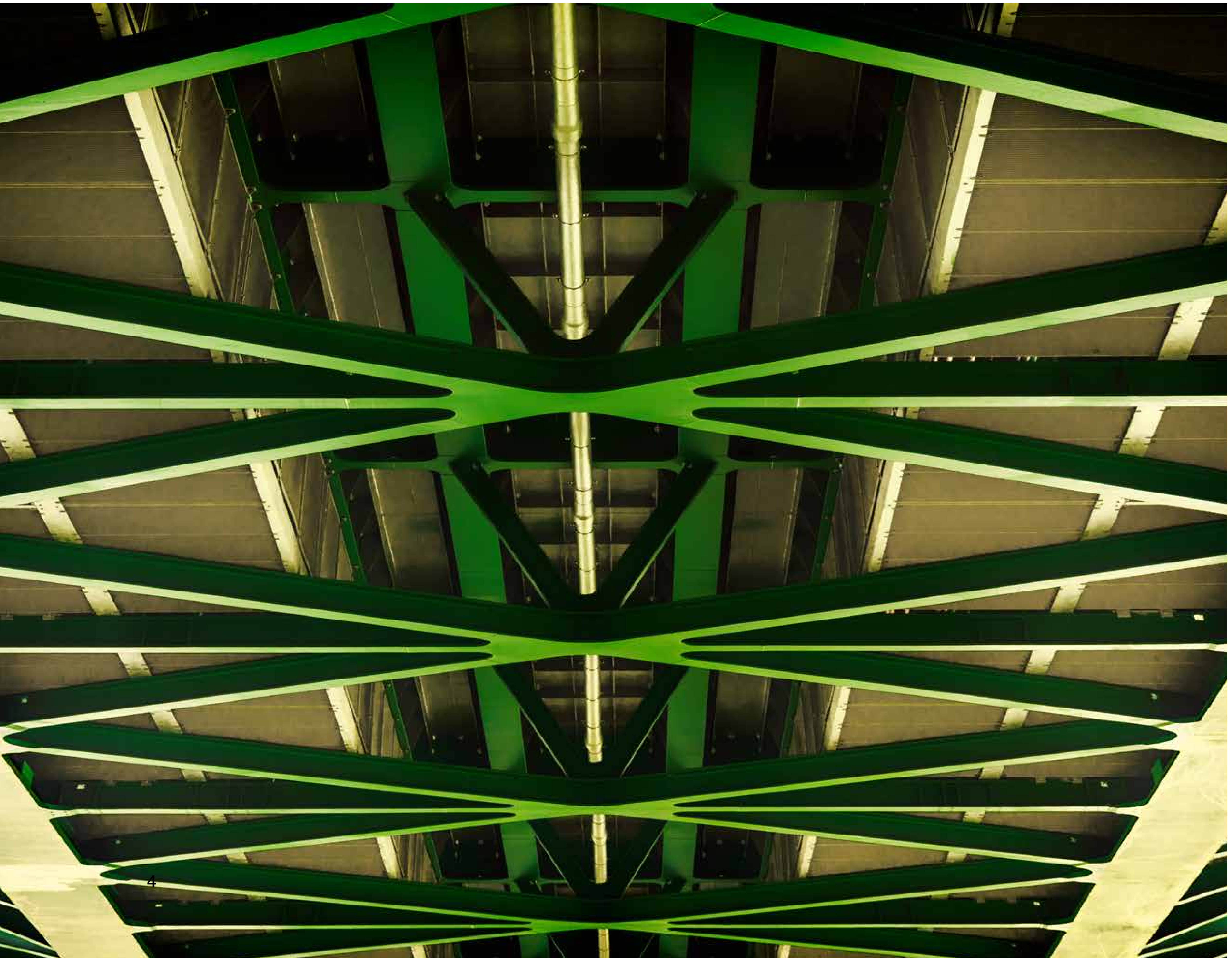
Transfer pricing matters – for start-ups and SMEs seeking to grow internationally

For many start-ups and SMEs, international growth is a strategic priority. Alongside the commercial drivers for business planning, the impact of doing business cross-border on the business's international tax and transfer pricing position need to be considered. Failing to do so can mean the misreporting of profits (or losses) and taxes by group entities in different markets, tax adjustments and penalties, as well as brand and reputational damage.



Business model for international expansion

Start-ups and SMEs can be driven to expand internationally to access new consumer markets, employee talent pools, and low-cost or specialised manufacturing hubs.

A UK company's presence overseas, however small, may trigger the taxing rights of the local market country. This may take the form of an overseas permanent establishment, for example, if local personnel act as dependant agents (e.g. sales representatives) or operate a fixed place of business (e.g. office, factory, shop) on behalf of the UK company. If an overseas branch or subsidiary is established, these are also clearly subject to international tax and transfer pricing as well as local tax rules.

Intra-group transactions and transfer pricing

When expanding internationally, start-ups and SMEs typically provide significant support to an overseas entity in its early years or continually. It's important that this is on arm's length terms and priced accordingly.

Transfer pricing issues and disputes often arise in relation to a local market entity and other group entities, the following being common:

- Provision of management and support services: A local market entity receives strategic guidance from the business founders / management and support services (such as finance, HR, IT) from an overseas parent or other group entities, without charge
- Sale of products: A local market (limited risk) distributor buys products from a group entity (e.g. at fixed prices for on-sale to local customers) with volatility in profit margins or resulting losses
- Use of intangibles: A local market entity uses trademarks, technology (such as internal platforms), patents, copyright, or other intangibles (such as supplier lists) that are owned and developed by another group entity, without charge
- Advance of funding: A local market entity receives a loan from a group entity, either favourable in amount or at a low or nil interest rate that is beyond what a third party would provide

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In the early years, an overseas entity is also likely to incur additional expenses to establish a new business in the local market. The bearing of risk can be acute, typically seen in large outlays on sourcing skilled personnel, customisation of products and services, and marketing campaigns tailored to domestic cultural and consumer preferences.

As a result, a key transfer pricing matter to usually address is whether the local market entity takes entrepreneurial risk and should bear the risk of operating losses, or if this resides in an overseas parent or another group company. If losses accumulate in the local market entity, a matching expectation can arise that it should retain entrepreneurial profits in the future (rather than pass these on through intra-group charges).

When start-ups and SMEs plan international operations, it is the important to manage the cross-border tax implications.

If transfer pricing policy considerations are addressed after the event, there can be misalignments between the substance of the business arrangements and tax positions reported by group entities in different countries. Tax adjustments can not only deny an entity's claims to tax losses but attribute income and profits, resulting in double economic taxation. Interest and penalties can apply depending on the level of non-compliance.

In determining the nature and pricing of intra-group cross-border transactions, withholding taxes, VAT and customs duties should also be managed.

Transfer pricing related business considerations

The transfer pricing arrangements of international groups are increasingly subject to greater reporting, documentation, information sharing, and scrutiny by tax authorities. Tax authorities are generally well attuned to and take action against any perceived tax avoidance by multinational businesses.

In the UK, SMEs should consider cross-border transaction reporting and documentation requirements in their overseas markets. The UK's major trading partners, namely the US and EU Member States, typically have relatively low thresholds for tax compliance purposes.

As businesses grow internationally, tax transparency increases. Apart from demonstrating tax compliance by aligning value creation with profit and tax outcomes across group entities internationally, a robust transfer pricing strategy can facilitate international growth. Investors, whether through venture capital firms, IPOs or otherwise, seek confidence in business governance and compliance processes to provide funding and management buy-outs. Brand and reputation management are enhanced as well.

Transfer pricing matters – for start-ups and SMEs seeking to grow internationally

A transfer pricing strategy for start-ups and SMEs should recognise their specific requirements and circumstances. Entrepreneurial businesses can change rapidly, and transfer pricing policies need to be designed to be commercially adaptive, balancing cost and ease of implementation.

Our experienced Transfer Pricing team has the deep knowledge and insights to develop, document and help your business to implement appropriate transfer pricing policies in the UK and internationally. We work closely with our international network of professional advisory firms across PKF Global.

If you would like further guidance, please contact Farhan Azeem.

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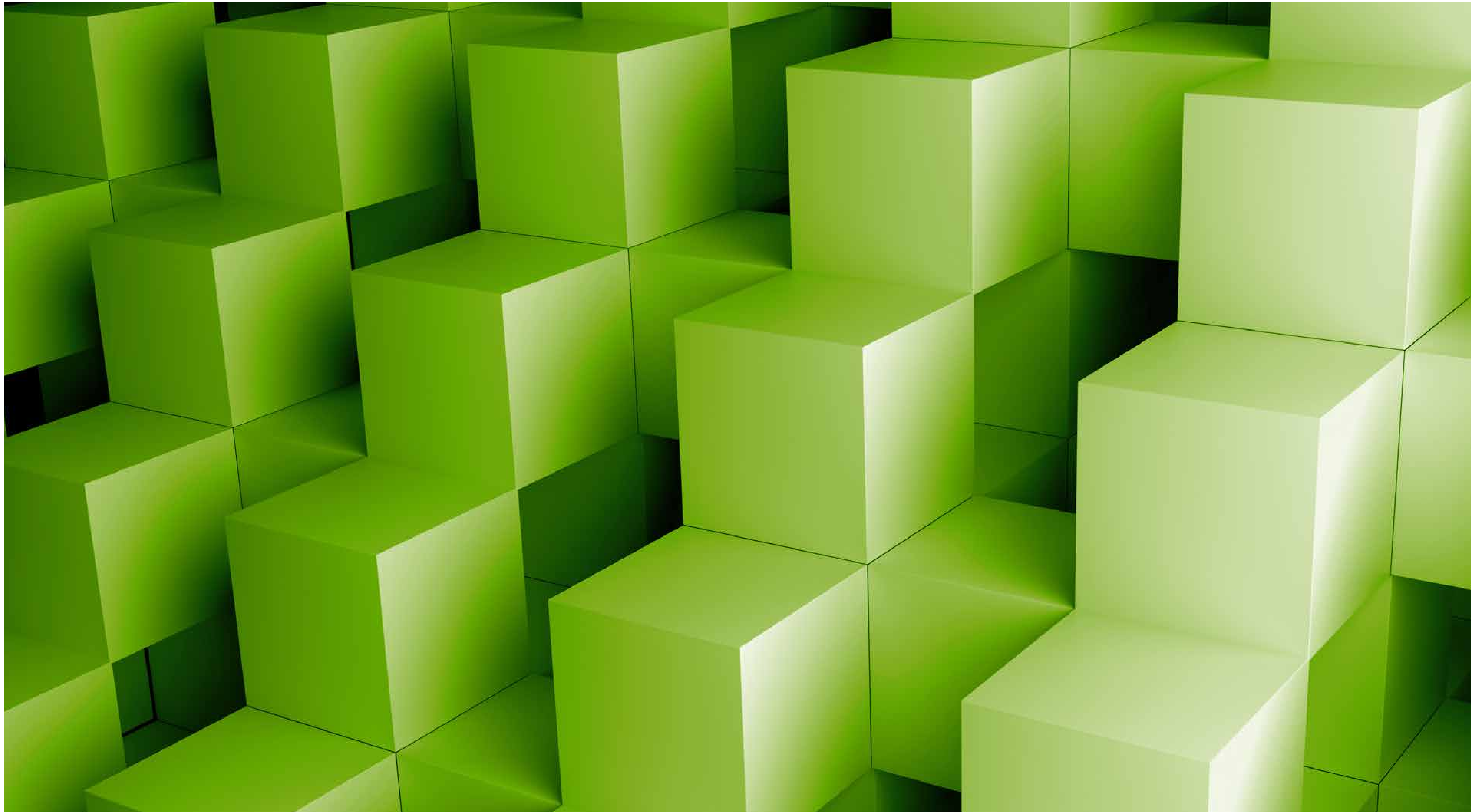

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Simplifying complexity for our clients

PKF is one of the UK's largest and most successful accountancy brands.

We provide a full range of audit, accountancy, tax and advisory services, and are experts at simplifying complexity – we're particularly well-known for working with large, high-profile businesses with challenging issues in fast-moving and highly technical areas.

We are also an active member of PKF Global, an international network of legally independent accounting firms that gives us an on the ground presence in 150 countries around the world.

PKF in the UK

11th largest Tax practice in the UK

£153 million annual fee income

1450+ UK partners and staff

5th ranked auditor of listed companies in the UK

Our tax services At a glance

"By bringing together the extensive expertise and experience of our tax specialists we can provide a fully rounded service that offers excellent value for money."

We offer comprehensive tax compliance and advisory services to a range of clients, both in the UK and globally, helping them find their way in the increasingly complex world of tax.

We find practical solutions that we use to our clients' advantage. Our team of experts supports individuals, and businesses ranging from start-ups and SMEs to large international groups, both listed and privately owned.

Where understanding of our clients' sector makes the difference, our experts invest their in-depth industry expertise to provide invaluable support and insights.

We offer the following specialist tax services:

Corporate and business taxes

Our Business Tax team will ensure that you are both tax compliant and efficient.

We provide specialist corporate and business tax advice on both a local and international level, which includes senior accounting officer and large business compliance, transfer pricing, transaction services, due diligence, R&D tax relief, employer solutions and global mobility. We also support both the personal and business affairs of partnerships and LLPs.

Read more

Personal tax and wealth management

Our team will guide you through the complex world of taxes, helping you meet all filing requirements and identifying risks and opportunities to help mitigate tax liabilities.

We advise individuals, the self-employed, partners, trustees and executors with their UK and international tax affairs. Our services include all aspects of tax, including Self Assessment, Capital Gains Tax, Inheritance Tax, property (both residential and commercial), trusts, family wealth and estate planning, residence and domicile issues.

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VAT and Indirect taxes

Our indirect tax team will support you in meeting your VAT compliance objectives and advise you on any VAT issues that your business faces.

We can ensure that your VAT risk is assessed and managed, and that your VAT recovery is optimised. We can also provide advice and compliance services on other indirect taxes, such as Insurance Premium Tax, Customs duty, and Air Passenger Duty.

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Tax disputes

HMRC is increasing the number and scope of tax investigations into both individuals and businesses, covering all aspects of potential underpayments of tax, including offshore investments, personal and corporate Self Assessment Tax Returns, PAYE and NIC compliance and VAT.

If an issue arises, our trusted advisors will match the right specialists with your needs to provide you the necessary support – whether for a routine HMRC enquiry or a more complex investigation.

Read more

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