



Associated Companies and the Marginal Rate

In between the small companies rate of corporation tax (21%) which applies up to profits of £300,000 and the main rate (28%) which applies to profits over £1,500,000, lies the 'marginal rate zone'. This is the band where an effective composite rate of 29.75% is applied to ensure a smooth transition between the 21% and 28% thresholds. This can be demonstrated by calculating the tax at different levels of profit:

Profit	£600,000	£900,000	£1,200,000	£1,500,000
£300,000 at 21%	£ 63,000	£ 63,000	£ 63,000	£ 63,000
Balance at 29.75%	<u>£ 89,250</u>	<u>£178,500</u>	<u>£267,750</u>	<u>£357,000</u>
	<u>£152,250</u>	<u>£241,500</u>	<u>£330,750</u>	<u>£420,000</u>
Overall rate of tax	25.375%	26.833%	27.563%	28%

Companies are understandably anxious to avoid having any of their profits tripping over the £300,000 threshold and therefore being taxed at the marginal rate of 29.75%. Some time may be spent in attempting to control the timing of sales and expenses, especially near the accounting year end.

The thresholds are annual limits and they are scaled down for accounting periods of less than a year, but they are also scaled down if there are 'associated companies' carrying on any trade or business at any time during the accounting period.

If the company has one associated company, then the thresholds are halved with the lower limit becoming £150,000 (and the higher limit £750,000). For companies with two associated companies the thresholds are divided by three and the lower limit reduces to £100,000, and so on.

This can present real problems when the companies are likely to have fundamentally different profit levels. So, for example, three companies associated with each other could have profits totalling £270,000, split as follows:

Profit	£20,000	£200,000	£50,000
First £100,000 at 21%	£4,200	£21,000	£10,500
Balance at 29.75%	<u>£ -</u>	<u>£29,750</u>	<u>£ -</u>
Tax	<u>£4,200</u>	<u>£50,750</u>	<u>£10,500</u>

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The total tax is £65,450, compared with a single company paying £56,700 on profits of £270,000.

So what are associated companies? They may be either members of the same group or companies controlled by the same persons. In determining whether any person (or persons) has control, the rights and powers of certain other persons may be attributed to them. These include:

- spouses, civil partners
- other blood relatives
- business partners (only where relevant tax planning arrangements are or ever have been in place)
- certain trustees.

By concession, the only blood relatives taken into account are minor children unless there is substantial commercial inter-dependence between the companies.

The moral of all this is 'think twice before you set up a lot of separate companies'. There may be compelling reasons for doing so, but it's worth considering operating a number of 'divisions' within a single company.

Do call us if you would like further help or advice in this area.

