

Hornbeam Taxation Services for Growing Businesses

The tax system can be harnessed in a number of ways to help growing businesses.

Tax Credits

Consider Charlie who is works for himself selling and maintaining commercial batteries. Charlie believes that he has invented a more efficient battery and is spending a lot of time working on this project. As a result, his income drops considerably. Hornbeam help Charlie make a claim for tax credits, and this income enables Charlie to survive this difficult stage.

Incorporation

Charlie's plan shows the business exploding into profitability, but he is determined to keep the business growing and his investment plans will eat all the available cash flow. Growing a business out of profits taxed at 42% or 52% is quite a challenge. Hornbeam are able to demonstrate the by incorporating the business Charlie is able to reduce the tax rate to 20% and that by managing the investment pattern the maximum use is made of Capital Allowances and in particular the Annual Investment Allowance.

Enterprise Management Incentive

Charlie patents his technology and outsources his manufacturing. He starts to become successful in selling the new product. However, he is convinced that the design can be improved further. Charlie is friendly with Steve who is a design engineer employed as a reader in battery technology at a nearby university. Charlie cannot really afford to recruit Steve, but Steve believes Charlie's battery technology and agrees to join the business in exchange for Share Options. Hornbeam register an Enterprise Management Incentive (EMI) share option scheme which entitles Steve to buy 25% of the shares in Charlie's company for a nominal sum in 3 to 5 year's time, with no tax cost to Steve or Charlie.

Development Tax Credits

Steve devotes essentially all his time to improving Charlie's battery technology, and soon new patents are issued, and new more efficient models are rolled out. Hornbeam claim for Development Tax Credits. These allow the company to claim for double the actual cost of Steve's salary, creating useful tax losses which give the company working capital to pursue its development. The company may choose to claim some of the tax credits back as a cash refund, effectively repaying the tax and national insurance that the company has paid.

The Enterprise Investment Scheme

The business is growing so rapidly that new Capital and new connections are needed. After getting Hornbeam to prepare a valuation Charlie (and Steve) sell a minority stake to a strategic investor. After Liaising with the investor Hornbeam set this up as an Enterprise Investment Scheme investment and the investor is able to obtain 20% income tax relief against his investment!

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The “New Goodwill” Scheme

Charlie decides to produce a new line of megabatteries, the purpose of which is to store the electric power produced by Wind Turbines. At Hornbeams advice this new business is created as a partnership between Charlie and Steve. In just a couple of years this is an extremely successful business and the team undertake a programme sell this business back into the Limited Company. The payments out of the company are of course subject to Capital Gains Tax at 10% but as all of the owners are higher rate taxpayers this is considerably better than the 25% or 35% tax payable on dividends. Better still the company is buying “New Goodwill” which it can claim as an expense against corporation tax.

Imagine the new business is making £100,000 profit. It might be valued at £500,000. The sale of 20% of the business back to the company puts £100,000 in the hands of the partners for £6970 tax (saving at least £18,030 personal tax). The company can claim capital allowances as it depreciates the goodwill, so £100,000 of allowances over 5 years saves at least a further £21,000 corporation tax. Overall, we have used £100,000 of profits to SAVE £39,030 of tax!

The Pension “Scheme”

As Charlie’s business matures, he looks for a permanent head office, factory and training centre. Having taken Hornbeams advice and set us a “potentially self-managed” pension scheme for himself and his family several years earlier, Charlie is able to make substantial tax-free contributions from the company. The pension scheme buys the business premises and is able to enjoy all rents and capital gains free of tax. Eventually, Charlie will be able to take 25% of the scheme value out free of tax and enjoy a very substantial pension (sadly not free of tax) in his retirement.

The Budget

The last budget contained quite a few provisions to encourage growth businesses, many deliberate, some perhaps less so. The reduction on the corporation tax rate, the improvements to the R and D tax credits scheme, and last but not least the increase in Entrepreneurs relief for Capital Gains Tax are just a few of the things that well-advised clients can and should be taking advantage of.

Please call Phil Needham 01603 720424 or email phil@hornbeam-accountancy.co.uk to find out more about using any of these schemes to reduce the tax of your business.



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