

## Associated companies

NOTE: The main corporation tax rate dropped to 20% from 1 April 2015. This reduction to 20% has resulted in the unification of the main corporation tax rate and the small profits rate from April 2015. The introduction of the unified rate removes the requirement to determine which rate of corporation tax a company should be paying and should make the corporation tax system more straightforward to administer. We have left this article available for companies that still need to refer to the old rules when calculating taxable profits for FY2014.

The 'associated company' rules govern how companies are associated for the purposes of access to the small profits rate of corporation tax and marginal relief (previously known as marginal small companies' relief).

In FY2014, a company paid corporation tax at 20% on taxable profits up to £300,000, and at 21% on profits above £1.5 million. If a company has profits between £300,000 and £1.5 million the main rate of corporation tax is charged, but a marginal relief is allowed.

Where a company is deemed to be associated with other companies, the corporation tax thresholds are reduced accordingly. The associated company rules seek to restrict the ability of separate companies being established to take advantage of the small profits rate of corporation tax. This is achieved by dividing the main rate by one plus the number of associated companies which the company has in the relevant accounting period. For example, if two companies are deemed to be associated, both companies would pay the main corporation tax rate of 21% at half the usual threshold, namely at £750,000 rather than £1.5 million. There is no corresponding relief for losses.

It is important to note that companies controlled directly by a person(s) and grouped companies will remain associated for tax purposes.

New rules introduced in 2011 created a new 'substantial interdependence test' which basically ensures that companies are only seen as associated where there is a connection between the companies.

The purpose of the rule was to take the existence of other companies into account for the purposes of the small profits rate, only where there is a substantive relationship between the relevant companies. However, where there is an association by 'accident', the companies will not necessarily be associated. For example, a husband and a wife could each control their own company, and each company will no longer be associated.

The legislation which governs whether or not there is substantial commercial interdependence is contained within *The Corporation Tax Act 2010 (Factors Determining Substantial Commercial Interdependence) Order 2011*.

Substantial commercial interdependence is determined by taking the following three factors into account:

The degree to which the companies are:

- Financially interdependent - Companies are "financially interdependent" if one gives financial support (directly or indirectly) to the other, or each has a financial interest in the affairs of the same business
- Economically interdependent - Companies are "economically interdependent" if the companies seek to realise the same economic objective, the activities of one benefit the other, or the companies have common customers
- Organisationally interdependent - Companies are "organisationally interdependent" if the businesses of the companies have or use common management, common employees, common premises, or common equipment

Each decision as to whether there is substantial commercial interdependence will depend on its specific circumstances. It should be noted that for substantial commercial interdependence to exist, it is not necessary for all three types of links to exist. For example, even where there is no sufficient financial link, a company can be an associated company of another if sufficient economic or organisational links exist.