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# Timing your dividends to perfection

**Dividends come in two types: interim and final. If you don't get the procedure for paying each of them spot on you might face an unexpected tax bill. How can you dodge this trap?**

**Tax on dividends**

Because dividends are usually the most tax-efficient way to extract profit from your company it's important to understand the procedure for paying them. However, the first point to note is that regardless of whether a dividend is interim or final, the tax treatment is the same for you and your company. So to that extent the difference is irrelevant.

**Interim dividends**

The distinction between the two types of dividend is one of company law - tax law doesn't play a part. The **Companies Act 2006** says *"The Company may by ordinary resolution declare dividends, and the directors may decide to pay interim dividends"*.

**Final dividends**

By comparison, company law requires final dividends to be approved by shareholders following a recommendation from the board of directors. In other words, directors can, on their own, set the amount of dividends while shareholders' approval is required for final dividends.

**Trap**. Whatever the type of dividend, it can only be paid to the extent your company has profits. No profits means no dividends. There are potentially nasty tax consequences of paying dividends in excess of profit, including retained profits brought forward from previous years.

**Why the fuss?**

The bottom line is that HMRC doesn't really care what sort of dividend it is. Its interest is more fundamental, i.e. whether a payment is genuinely a dividend or not. Its argument is that if company law procedure hasn't been followed then a payment that purports to be a dividend won't actually be one. And if it isn't then it must be salary, a bonus or a loan to the director or shareholder who receives it. This can mean higher taxes and NI costs. Now you can see why HMRC is so interested.

**In practice**

Contrary to HMRC's lengthy advice to its inspectors and the plentiful articles you'll find on the subject in tax reference books, the truth is that HMRC has until now rarely made challenges regarding the nature of dividends. However, there have been a few recent tribunal and court cases which indicate that HMRC is becoming more willing to challenge the validity of dividends. Therefore, HMRC is paying more attention to the timing, and thus the nature, of dividends.

***Tip. Keeping to the dividend rules isn't difficult, but it does involve following a procedure and quite a bit of paperwork. That said, if you set up a routine for voting and paying dividends it will simplify the process.***

# Writing off a loan can save you tax

**If you owe your company money you could repay it out of your net salary. However, writing off the debt might be a better option. How can you ensure maximum tax efficiency?**

### Year-end planning

It's a typical situation; your company has paid for goods and services on your behalf plus you've drawn money over and above your salary to pay for the family holiday and a few extra necessities. Come the end of the financial year you're indebted to the company to the tune of several thousand pounds. To avoid the tax problems associated with this your accountant has in the past suggested the company pays a dividend to clear the debt. But this year the company doesn't have sufficient reserves to do this.

### Write it off

The usual alternative to paying a dividend is to pay yourself extra salary (or bonus). Obviously you don't draw this; it's simply credited to you in the company's books in order to clear the debt. The trouble is this costs a small fortune by the time you've factored in the tax and NI payable, and this is the last thing the company needs right now. Another option is for your company to write off the loan.

### Corporation tax deduction

Until 2010, where a company wrote off a director's loan, the corporation tax (CT) position was arguable - well HMRC thought so even though tax experts were certain that write-offs were deductible for CT purposes. But HMRC doesn't like being proved wrong so it cajoled the government into changing the law with effect from 24 March 2010. Since then the write-off of a loan to a director shareholder definitely doesn't qualify for CT relief.

### Director's tax bill

On the face of it writing off a loan from the company doesn't look like a good deal for the director shareholders either. The employment income rules say that the amount written off counts as salary which, as we've already mentioned, is a costly option. However, the good news is that this rule is trumped by another one, which HMRC has no choice but to accept. This says that the write-off of a loan made to a director, where they are also a shareholder, must be taxed in the same way as a dividend.

**Trap**. Companies often record sums they pay for or on behalf of a director over and above salary as a loan, e.g. settling personal bills. However, HMRC thinks transactions of this type should be subjected to PAYE tax and NI and not taxed like a dividend. It will help your counter argument to have a written loan agreement with your company which states such payments must be debited to your loan account.

***Tip. Despite the loss of CT relief for loan write-offs, they can still be a tax and NI-efficient alternative to a bonus and equally efficient as a dividend. For example, a loan write-off of £30,000 can save over £3,000 in tax and NI between you and your company. And unlike a dividend, which can't be paid where your company doesn't have sufficient reserves, loan write-offs are permitted.***

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## Bitesize Points

### Company accounts rejection rate is 2.5%, says Companies House

A surge in rejections of company accounts prepared under the new UK GAAP rules, identified by ICAEW, has been refuted by Companies House, which reports that only 2.5% of accounts have been returned, despite hitting the peak reporting period. However, a spike in calls to ICAEW helplines have been related to rejection of accounts filed under the new FRS 102 Financial Reporting Standard, although this may be a sign of first-year adoption teething issues.

### Business rates revaluation will hike bills for one in four

The Government has recently launched a four-week consultation on the long-delayed revaluation of business rates and details of transitional arrangements for businesses hit by substantial rises, which are likely to result in higher rates for one in four businesses.

From the 30 September 2016, anyone in England and Wales who pays business rates, can go online to check their new draft rateable value using a new tool which will provide an estimate of what their business rates will be from April 2017.