

# ACTIVE PRACTICE UPDATES

FEBRUARY 2023

tc accounts · tax · legal · financial planning

## CORPORATION TAX IN 2023

How the April tax rise affects SMEs.

After multiple policy U-turns and much uncertainty, the main rate of corporation tax will rise from 19% to 25% from 1 April 2023, affecting companies with profits of £250,000 and over.

The legislation provides that small companies with profits up to £50,000 will continue to pay corporation tax at 19%, with profits between the two limits being subject to a tapered rate.

All UK companies must pay corporation tax on the profits they generate, while the profits of non-incorporated businesses, such as sole traders and partnerships, are taxed via self-assessment.

---

### CONTEXT AROUND THE MEASURE

The April 2023 corporation tax rise was first announced by the then-Chancellor of the Exchequer, Rishi Sunak, in March 2021 during his Spring Budget.

At the time, the Government's fiscal policy had been to reduce the annual deficit and deliver "sustainable public finances" after Sunak signed off on £400 billion more spending than planned in 2020, owing to the Covid-19 pandemic.

The Treasury estimated the changes to corporation tax would increase tax by an additional £17.2bn a year by 2025/26.

However, after Boris Johnson resigned as Prime Minister in July 2022 and was replaced by Liz Truss, the Government's approach to fiscal policy changed radically.

Kwasi Kwarteng, the third person to serve as Chancellor in 2022, delivered his 'mini Budget' on 23 September, where he announced a range of tax cuts and cancelled the planned rise in corporation tax.

However, following a strong negative market backlash to the mini-Budget, the Government was forced into a U-turn, with Truss confirming on 14 October the corporation tax rise would in fact go ahead as planned.

In documents accompanying the Autumn Statement by Jeremy Hunt, who replaced Kwarteng after he was sacked as Chancellor the day of the corporation tax U-turn, the Treasury upgraded its estimate of the value of the tax rise to £17.9bn per annum by 2026/27.

Despite the increase, the UK will remain the country with the lowest effective corporation tax rate in the G7.

---

### NEW RATES & THRESHOLDS

The corporation tax hike will be applied on profits exceeding £250,000 a year, which means around 10% of all UK companies will pay the full higher rate, according to Spring Budget 2021 documents.

The Government will also establish a 'small profits rate', which will hold corporation tax at 19% on profits of £50,000 or less.

According to the Government, this means 70% of actively trading companies – 1.4 million businesses – will be completely unaffected.

For profits between £50,000 and £250,000, the Government will introduce a taper to limit the increased tax burden on medium-sized companies.

If you have a profit of £300,000, all of it will be taxed at 25%, not just the amount above £250,000 – unlike income tax, where portions of your income are taxed at gradually increasing rates after a tax-free allowance.

---

## HOW THE TAPER WILL WORK

Companies and organisations may be able to claim marginal relief if their profits from 1 April 2023 are between £50,000 (lower limit) and £250,000 (upper limit).

However, these limits are proportionately reduced if your accounting period is shorter than 12 months. The lower and upper limits are also proportionally reduced by the number of associated companies your company has; this is referred to as the 'adjusted limits'.

So, if your company has three other associated companies, the limits are divided by four, reducing the lower limit to £12,500 and the upper limit to £62,500.

You cannot claim marginal relief if you are a non-UK resident company or a close investment holding company.

Organisations will be able to work out the amount of tax they pay with the following formula:

$$\frac{(\text{Adjusted upper limit} - \text{Augmented profits}^*) \times (\text{taxable total profit} \div \text{augmented profits}) \times (\text{standard marginal relief fraction})}{1}$$

The Government has developed a digital calculator on the gov.uk website to automatically calculate your corporation tax bill after marginal relief.

All you need to know is your information relating to the equation above and your company's accounting period start and end dates.

\*Augmented profits are 'taxable total profits' and any exempt distributions received from companies that are not 51% subsidiaries or held through a consortium.

---

## WHAT IS THE MARGINAL RELIEF FRACTION?

In the equation the Government has provided taxpayers, the marginal relief fraction is 3/200ths, which is the difference between the main rate and the marginal rate expressed as a fraction.

To explain where this fraction comes from, the Government says:

- Corporation tax payable on the upper limit = £62,500 (because £250,000 x 25% = £62,500).
- Corporation tax payable on the lower limit = £9,500 (because £50,000 x 19% = £9,500).
- The tax payable difference between the limits is, therefore, £53,000.
- Dividing £53,000 by £200,000 (the difference between the upper and lower limit) provides the marginal rate of 26.5%.
- The difference between the marginal rate of 26.5% and the main rate of 25% is 1.5%, which can also be expressed as 3/200.

---

## MITIGATING CORPORATION TAX

Although corporation tax is rising for a lot of companies, they can still benefit from tax planning.

For instance, the annual investment allowance will remain at its highest ever permanent level of £1 million from 1 April 2023.

Meanwhile, the R&D expenditure credit (RDEC) for larger companies will increase from 13% to 20% to give more tax money back for innovative projects.

However, the SME additional deduction will be cut from 130% to 86% from 1 April, and the SME credit will decrease from 14.5% to 10%, to "improve the competitiveness of the RDEC scheme".

There are also several tax reliefs available for creative industries, including video games tax relief, film tax relief and various television reliefs.

The Government also promised in the Autumn 2022 Statement to "build upon the success of the audio-visual subset of the creative industry tax reliefs" to "further incentivise the production of culturally British content".

**[Contact us to discuss your tax plan and other ways to reduce your corporation tax liability.](#)**