Corporate Tax

A. INTRODUCTORY NOTE

1. This section presents analyses of the direct taxes paid by companies: mainly corporation tax and, for companies extracting oil or gas from the North Sea, petroleum revenue tax. This chapter excludes the windfall tax on the excess profits of privatised utilities which was introduced in the July 1997 Budget (see the Table T1.2).

B. CORPORATION TAX

An outline and major milestones

2. Corporation tax is charged on the profits made by companies, public corporations and unincorporated associations such as industrial and provident societies, clubs and trade associations. The tax is charged on the profits made in each accounting period, i.e. the period over which the company draws up its accounts. The rates of taxation are set for the financial year April to March; where an accounting period straddles 31 March the profits are apportioned between the two financial years on a time basis.

3. Companies have been charged to corporation tax since 1965. Before that they were liable to income tax on their total income and also to profits tax. The system introduced in 1965 charged a uniform rate on all profits and an additional charge to income tax was made when profits were distributed.

4. In 1973 a 'partial imputation system' was introduced to mitigate the double tax charge when profits are distributed. This was achieved by the twin mechanisms of advance corporation tax (ACT) and tax credits.

5. In July 1997, the new Government began a series of reforms of tax credits and corporation tax payments. Payments of tax credits to pension schemes and UK companies were abolished on dividends paid on or after 2 July 1997 and the remaining payments of tax credits were cut from 6 April 1999. ACT was abolished for dividends paid on or after 6 April 1999 as were Foreign Income Dividends which allowed companies to pay dividends without tax credits. A system of quarterly instalment payments of corporation tax was introduced for large companies for accounting periods ending on or after 1 July 1999.

The partial imputation system

6. Until April 1999 a company paid ACT when it paid a dividend. This tax could be set off, within a limit, against the corporation tax liability of the accounting period. The remaining tax liability was called "mainstream" corporation tax. One purpose of ACT was to finance the tax credit which the Exchequer made available to the shareholder receiving the dividend. The tax credit could be set against the shareholder's income tax liability on the dividend or, until the payment of tax credit was abolished for non-taxpayers and exempt institutions, the credit would be paid to the shareholder.

7. A company which could not set off the whole of the ACT paid against the tax charged on its profits had "surplus ACT". This could be carried back for up to 6 years (up to 2 years before 1984) to reduce tax liability in earlier accounting periods, or it could be carried forward without time limit. In any accounting period the amount of ACT set against tax on profits was limited to the amount which, with the distribution to which it related, absorbed the whole of the profits of the accounting period. For example, a company with profits of 100 would have had an ACT limit of 20 (assuming an ACT rate of a quarter), because a distribution of 80 and ACT of 20 would have absorbed all the profits of 100.

Tax rates

8. The rates of corporation tax from 1969 to those set in Finance Act 2005 are shown in the Table TA.6. Rates were substantially reduced from 1983 to 1986 as part of a range of measures which included the abolition of stock relief and major changes to capital allowances. The rate of ACT changed in line with the basic rate of income tax until 1992-93. From then until its abolition the rate was linked to the lower rate of income tax of 20 per cent with a transitional rate for ACT (equivalent to 22.5 per cent) in 1993-94.

9. Since 1973, there has been a lower rate of corporation tax for companies with small profits. The rate applies when the profits are below a lower limit of profits (as given in Table TA.6). Between that limit and an upper limit, a higher marginal rate is applied to produce a smooth progression in the average tax rate from the lower rate to the main rate which applies above the upper limit. The profit limits are restricted for companies associated with one or more other companies according to the number of associated companies to prevent abuse by a company fragmenting into smaller ones. In April 2000 a new starter rate of 10 per cent was introduced on profits up to £10,000 but the benefit is withdrawn for more profitable companies by a higher marginal rate on profits in the band £10,000 to £50,000. In his April 2002 Budget the Chancellor reduced the starting to zero and the small companies' rate of corporation tax to 19%. In April 2004, the Chancellor introduced a 19 per cent minimum rate of corporation tax on distributed profits, commonly referred to as the Non Corporate Distributed Rate (NCDR). In the 2005 Pre-Budget Report, the NCDR and zero per cent rates were replaced with a single banding set at the small companies' rate of 19 per cent. This rate was raised to 20 per cent from 1 April 2007 and 21 per cent from 1 April 2008. The main rate of CT was reduced from 30 per cent to 28 per cent from 1 April 2008.

Payment and assessment arrangements

10. ACT was payable on the 14th day of the month following the end of the quarter in which the distribution was made and mainstream corporation tax was payable 9 months after the end of the accounting period. Before 1990-91, payment rules allowed a longer period before mainstream tax was paid. Some companies paid mainstream tax up to 21 months after the end of their accounting periods.

11. A further change was made for all accounting periods ending on or after 1 October 1993 when Corporation Tax Pay and File was introduced. Under this administrative system, after nine months a company was required to pay its own estimate of its mainstream corporation tax liability, rather than an estimate produced by the tax inspector. After twelve months it submitted a standard return giving the basis of the liability. Further payments and repayments could be made when a final assessment of tax was agreed. This system also introduced some changes to accounting methods which increased the recorded levels of both payments and repayments, but had no effect on net receipts. For accounting periods ending on or after 1 July 1999 companies are required to assess their liabilities on broadly the same self assessment principles that underly the collection of income tax under self assessment.

12. With the abolition of ACT in 1999, a system of quarterly instalment payments was introduced for large companies starting with accounting periods ending on or after 1 July 1999. The first instalment became due in month 7 of the accounting period with further instalments due in months 10, 13, and 16 with any balance to be paid 9 months after the end of the period. Transitional arrangements phase in the change over four years. Quarterly payments were first made in January 1999 and the first large amounts were paid in July 1999.

13. For corporation tax purposes, a company's profits comprise its income and capital gains. Income - whether from trading or investments - is calculated in the same way as for income tax purposes including capital allowances where appropriate. Gains are calculated in the same way as for capital gains tax (see the capital gains tax chapter) except that companies have no exempt amount and company gains are not affected

by the reforms made in 1998 to capital gains tax. Before 1987, gains charged to corporation tax were reduced by a specified fraction to produce the equivalent of the tax rate on gains by individuals.

14. Capital allowances provide relief, for corporation tax purposes, for the consumption or depreciation of capital assets incurred for the purposes of carrying on a trade. Different types of assets qualify for different rates of allowances (see the Table TA.5). Capital allowances may be claimed in the year in which they accrue and any unused capital allowances may be carried forward to set against Capital Gains in later years. They may also be carried back in the same way as trading losses. Tax credits were introduced in the 1999 Budget, and extended later, to provide enhanced relief for research and development and some other types of expenditure. For some types of expenditure non taxpayers can receive a payable tax credit.

15. A company which makes a trading loss may carry that loss back for 1 year (3 years from 1991 to July 1997) to set against the profits of an earlier accounting period. An unrelieved trading loss can also be carried forward without time limit to set against income from the same trade in a future accounting period.

16. Deductions are allowed from a company's total profits for any charges (interest and other payments) it pays and, in the case of an investment company, its management expenses. From April 1996, new "loan relationship" rules have been in force for the treatment of interest and similar payments. A deduction against the tax liability is allowed for income tax deducted at source from interest received (to the extent that it is not used to cover income tax the company itself deducts on interest payments it makes). Double taxation relief for foreign tax is allowed as a deduction against the tax charged on profits.

Company groups

17. Certain special rules and reliefs apply to companies which operate as a group. A company which makes a trading loss can surrender that loss as group relief to set against the profits of an equivalent accounting period of another group member. Assets can be transferred between group members without giving rise to a chargeable gain at the time of transfer. Before the abolition of ACT a subsidiary could pay a dividend to its parent company without paying ACT and a parent could surrender ACT it had paid to a subsidiary company.

Inter-company dividends

18. A company is not taxable on a dividend received from another company resident in the United Kingdom (UK). Such dividend income if received with the tax credit is called "franked investment income". When the company itself pays a dividend it makes a "franked payment". A company only had to pay ACT on the excess of its franked payments over its franked investment income.

C. TAXATION OF OIL AND GAS PRODUCTION (INCLUDING PETROLEUM REVENUE TAX)

Petroleum revenue tax

19. Companies which earn profits from the extraction under licence of oil and gas from the UK and its waters are liable to petroleum revenue tax (PRT) as well as corporation tax and supplementary charge on their share of the production from fields approved for development before 16 March 1993. Revenues from fields approved on or after that date are only subject to corporation tax and supplementary charge on their profits.

20. Unlike corporation tax, PRT is not assessed on each company's profits for a 12 month accounting period. Instead, it is assessed every six months on each company's share of the cash flow from each separate oil field. Fields are determined on geological grounds by the Department of Energy and Climate Change. The

assessment includes tariff receipts from the hire of infrastructure, such as pipelines, and receipts from the sale of some assets. Sales of gas to British Gas (Centrica from early 1997) under contracts agreed before 30 June 1975 is generally exempt from PRT. From 1 January 2004 PRT was abolished on new tariffing business under contracts completed on or after 9 April 2003.

21. Broadly, oil and gas sales are brought into tax at their arm's length value (with special rules applying where the sale is not at arm's length). These are termed "gross profits". Costs of finding, appraising, extracting and transporting the oil and gas to a place of reasonable delivery are deducted. PRT gives immediate full relief for allowable expenditure rather than writing down allowances and revenue deductions. There are also deductions for royalties and other licence payments.

22. Various further deductions and reliefs are available against income assessed for PRT liability:
    - Losses when expenditure is greater than income: such losses can be carried forward or backward indefinitely;
    - Uplift: a supplement of 35 per cent is given on capital expenditure incurred during the Net Profit Period (NPP). The NPP covers the period where the cumulative field costs exceed the cumulative income
    - Oil Allowance: for fields approved for development up to 31 March 1982, an oil allowance equal to the profits of the field up to the value of 0.25 million tonnes of oil is given for each 6 month chargeable period, subject to a total of 5 million tonnes per field. For fields given development consent after 31 March 1982 and before 16 March 1993, a double allowance (0.5 million tonnes per chargeable period up to a total of 10 million tonnes per field) is given for offshore fields outside the Southern Basin of the North Sea; Southern Basin fields approved between those dates receive a smaller allowance of 0.125 million tonnes up to a total of 2.5 million tonnes;
    - Tariff Receipts Allowance: this excludes from charge tariff income from each 'satellite' field approved for development before 16 March 1993 up to a limit of the income from processing 0.25 million tonnes in a 6 month chargeable period;
    - Exploration and Appraisal Relief: offshore expenditure on exploration and appraisal, like other spending can, if necessary, be carried forward to be set against revenues in the same field. However expenditure occurring between 16 March 1983 and 15 March 1993 could obtain immediate PRT relief by being set against any profits in a developed field of the same company. This relief was phased out in the period to 15 March 1995;
    - Unrelievable Field Loss: when a field is abandoned with a net loss for PRT purposes, this can be transferred to another field and claimed by the same company (or an associated company);
    - Cross Field Allowance: this allows 10 per cent of development expenditure that would have qualified for uplift in offshore fields outside the Southern Basin of the North Sea and approved for development between 17 March 1987 and 15 March 1993 to be claimed and deducted from profits in other fields;
    - Research Relief: since 1987, certain research expenditure not related to specific fields has been deductible, but only after a three year delay. The first such relief appears in assessments for the first 6 months of 1990.

23. Tax is charged on profits arising in each chargeable period and the rates at which petroleum revenue tax has been charged are:

1975 to 1978	45 per cent
1979	60 per cent
1980 to 1982	70 per cent
1983 to June 1993	75 per cent
from July 1993	50 per cent

24. Safeguard relief is set against the tax charge. This is available in chargeable periods up to the NPP and for half as many periods again. When safeguard applies, profits in the period are compared with a threshold level which is 15% of the aggregate capital

expenditure qualifying for uplift. If the profits are below that threshold level, no PRT is payable. If they are above the threshold, PRT payable is limited to 80% of the excess, if that is less than the amount of PRT payable under normal rules.

25. PRT is paid in 6 equal monthly instalments of one eighth of the previous half yearly chargeable period's liability with the first payment due at the end of the second month of each new chargeable period. The sixth payment is followed a month later by a balancing payment of the outstanding liability for the half year based on a company's self assessment of its liability for the period. This payment coincides with the first instalment payment for the next chargeable period. Assessments are issued by HMRC three months after they have received companies' self assessments. Any repayments from the carry back of losses would be made subsequently.

Corporation tax

26. The corporation tax regime for oil and gas companies which operate in the UK allows any PRT liability as a deduction in computing chargeable profits. There are however special rules which prevent profits from oil and gas production being reduced by losses transferred from other activities; these profits are 'ring fenced' for corporation tax purposes. Similarly ACT accounted for on dividends paid by associated UK resident companies outside the ring fence could not be set off against the tax liability of companies within the ring fence. Companies have been able to claim a 100 per cent first year allowance for most capital expenditure incurred on or after 17 April 2002. Since Budget 2005 ring fence oil and gas companies have been required to make three instalment payments rather than the usual four, initially with the April 2006 instalment payment being brought forward to January 2006, but with the three payments being equalised in subsequent years. Ring fence oil and gas companies mostly have calendar year accounting periods.

27. The Exploration Expenditure Supplement (EES) was introduced for exploration and appraisal expenditure on or after 1 January 2004 to enable companies with no corporation tax liability to enhance the value of relief by 6 per cent a year for a maximum of 6 years. An extension of the EES to cover all ring fence expenditure (known as the RFES) was announced in the 2005 Pre-Budget Report. The rate of RFES was increased to 10% for accounting periods beginning on or after 1 January 2012.

28. From 17 April 2002, companies that operate in the UK or UKCS have been subject to a supplementary charge on their profits in respect of ring fence trades, initially at a rate of 10 per cent. The rate of supplementary charge was increased to 20% in the 2005 Pre-Budget Report and at Budget 2011 was then raised to 32% on profits earned on or after 24 March 2011. The supplementary charge is assessed on the basis of ring fence profits as computed for corporation tax, but without any deduction for financing costs. To accompany the first increase in the supplementary charge companies were allowed to defer their 100% first year capital allowance claims for 2005 into 2006. From 21 March 2012 tax relief for decommissioning expenditure for supplementary charge purposes is restricted to 20%.

29. In 2009 the field allowance was introduced to provide an incentive for the development of new economic but commercially marginal oil and gas fields. FA2012 amended the field allowance legislation so that, if Government wishes to introduce a field allowance targeted at commercially marginal projects in existing fields, it can do so by way of secondary legislation.

Other charges

30. In addition to PRT, corporation tax and supplementary charge, other charges on UK oil and gas production were as follows:
    - Royalties: these were administered by the former Department of Trade and Industry and, generally, levied at 12.5 per cent of the value of production, less the cost of initial transportation and processing, for fields approved before 1 April 1982.

Royalties were deductible in computing profits chargeable to PRT and corporation tax. Royalties were abolished from 1 January 2003;

- Gas Levy: was administered by the former Department of Trade and Industry and levied, from 1982-83, at 4p per therm on certain PRT exempt deliveries from fields under contracts dating before July 1975. It was paid principally by British Gas (now Centrica) as a purchaser of gas and was deductible in computing profits for corporation tax purposes. The gas levy was abolished from April 1998;
- Supplementary Petroleum Duty: was charged in 1981 and 1982 at 20 per cent on oil and gas revenues (less an allowance of the value of 0.5 million tonnes per field in each 6 month period). It was treated as an expense for the purpose of computing PRT;
- Advance Petroleum Revenue Tax: was charged from 1983 to 1986 on oil and gas revenues (less an allowance of the value of 0.5 million tonnes per field in each 6 month period). Rates of charge decreased from 20 per cent to 5 per cent over the 4 years. Credit for it was given against any liability for petroleum revenue tax. Any amount not credited was repaid after 5 years or earlier in some circumstances;

E. ENQUIRIES AND FURTHER INFORMATION

31. Enquiries about statistics on corporate taxes should be addressed to the appropriate analyst listed below at KAI (Direct Business Taxes), HM Revenue and Customs, 100 Parliament Street, London. SW1A 2BQ. Tel 020 7147 (Extension).

Corporation Tax receipts	Anna Stonell Ext. 3963
Assessments	Derek Hull Ext. 2940
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