

# Stewart & Co.

Chartered Accountants

## TRANSACTIONS WITH DIRECTORS

The implementation of the Companies Act 2006 has resulted in significant change relating to the legality of directors' transactions and their disclosure in the Company accounts.

Legality is a major concern, but so is the risk of conducting transactions in a particular way which leads to a potentially incorrect tax treatment.

*'This can be expensive to the Company not only in terms of tax underpaid but also HMRC penalties and interest charged thereon.'*

On the basis that the final phase of the new Companies Act has come into force from October 2009, now is a good time to review directors' transactions in more detail.

### **Legal implications**

In broad terms, although there are some exceptions, member approval is required for loans, related guarantees and security made by a Company to or for a director of the Company or its holding company.

The main exceptions here are

- Small loans and quasi loans (as defined by s199 of CA2006) in respect of a director and any connected persons, total value of not exceeding £10,000
- Small credit transactions in respect of a director and any connected persons, total value of not exceeding £15,000
- Transactions in the normal course of business, ceiling of £50,000
- Group transactions

Legislation is still in place under the Act regarding Substantial Property Transactions. Defined as any arrangement by which a director (or connected person) of the Company acquires from, or disposes to the Company non cash assets (including property), the legislation applies only to transactions which are greater than:-

- £5,000; and
- The lower of £100,000 and 10% of Company net assets.

These transactions require approval by the members, with any contract entered into by the Company, being conditional upon this approval. The Company will not be liable under any contract if member approval is not forthcoming. There are some exceptions, principally group transactions.

### **Disclosure requirements**

Disclosure requirements in Company accounts have changed significantly under the new Act. For all accounting periods commencing after 6 April 2008, statutory disclosure requirements have been relaxed which is good news. This said, disclosure is still required in respect of:-

- Advances
- Credit facilities
- Guarantees provided

These items will continue to appear in both the full shareholder accounts and the abbreviated accounts (if produced for filing at Companies House, albeit directors transactions on a 'no names' basis).

Accounting legislation is more onerous, Financial Reporting Standard 8 "Related Party Transactions" asks for all material transactions with related parties (being close family of the director and any party that is controlled by or significantly influenced by a director and any other related parties).

Disclosure is based on materiality. Transactions are material when their disclosure might reasonably be expected to influence decisions made by the users of accounts, so very judgemental.

## **What taxation implications arise out of directors' transactions?**

1. Beneficial loans made to any employee (or relative of) by reason of employment. Where the aggregate of all loans in any tax year exceeds £5,000, there is a taxable benefit in kind if interest charged is less than that that would have been charged at the HMRC Official Rate of Interest. There are exceptions for employee expense advances upto £1,000.
2. Loans to participators or their associates in a "close company". On any outstanding loan balance, a tax liability will arise equal to 25% of the loan. This is payable with the normal corporation tax and repayable on repayment of the loan itself.
3. Any loan to a participator written off, the borrower will be assessed as if the loan was a dividend. The write off of a loan to an employee or director who is not a participator, the written off amount will be deemed emoluments, although there are some exceptions.
4. There are significant issues with salary payments in advance of remuneration. These should be subject to PAYE and NIC as they are drawn, or if earlier when the person has entitlement to or in respect of directors specifically when amounts are credited to their current accounts. Some may argue these are loans, although HMRC will be keen to argue remuneration, which is likely to be more expensive from a tax view point.
5. Directors' current accounts are always a target for Tax Inspectors, so please note:-
  - Net remuneration/bonuses can only be credited when paid
  - Overdrawn director accounts must always be disclosed to HMRC
  - Any evidence of "window dressing" is likely to be unwound should there be any Tax Enquiry, which could cause significant tax problems.
  - Husband and wife balances cannot be offset – this is the agreed position, so an overdrawn loan account cannot be offset or reduced by a spouse's credit balance.
  - Any dividends voted and credited must be supported by the necessary minutes and resolutions at the time and not backdated.
6. Standard benefit in kind rules apply, as they always have, for transfers of company assets at undervalue plus use of company assets (living accommodation, company cars etc).

## **Conclusion**

The above is a summary only but emphasises the need for directors to be very careful regarding transactions they may have with the Company.

In a climate where HMRC are actively seeking to collect more tax and national insurance, it is important that directors take notice of the legislation; if they do not then it could prove to be very expensive.

If you would like more advice in this area then please feel free to contact a partner of **Stewart & Co.**