# Flowchart - Associated companies

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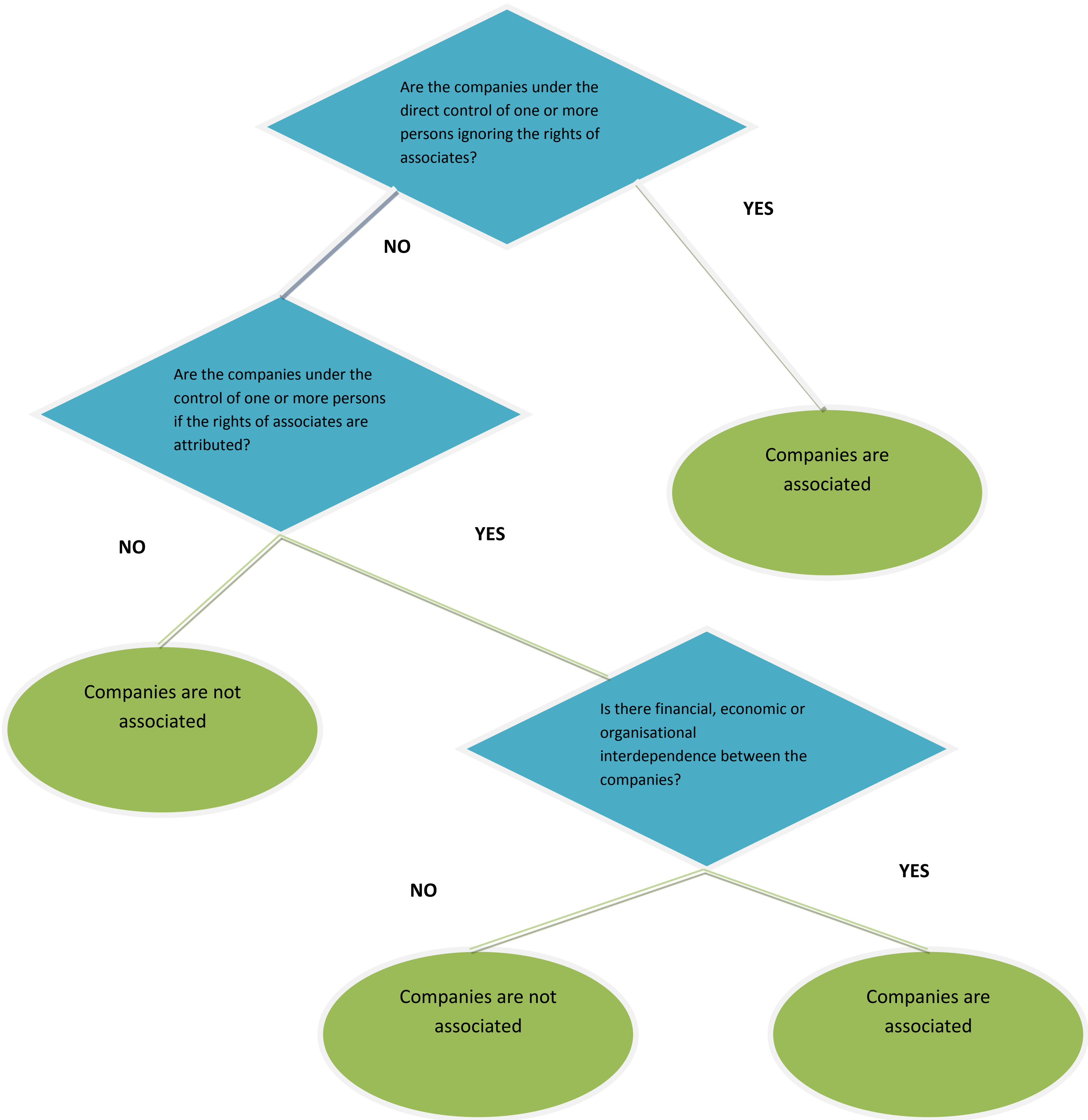
Are the companies under the direct control of one or more persons ignoring the rights of associates?
YES
NO
Are the companies under the control of one or more persons if the rights of associates are attributed?
Companies are associated
NO
YES
Companies are not associated
Is there financial, economic or organisational interdependence between the companies?
YES
NO
Companies are not associated
Companies are associated

## STEP 1 – Control

Control is defined in CTA 2010, s450:

A person (“P”) is treated as having control of a company (“C”) if P–

(a) exercises,

(b) is able to exercise or

(c) is entitled to acquire,

direct or indirect control over C's affairs.

A person (“P”), and in particular, is treated as having control of C if P possesses or is entitled to acquire:

(a) the greater part of the share capital or issued share capital of C,

(b) the greater part of the voting power in C; or

(c) so much of the issued share capital of C as would on the assumption that, the whole of the income of C were distributed among the participators, entitle P to receive the greater part of the amount so distributed; or

(d) such rights as would, entitle P, in the event of the winding-up of C or in any other circumstances, to receive the greater part of the assets of C which would then be available for distribution among the participators.

**If with this test the companies are under common control they are associated companies.**

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## STEP 2 – Rights of associates

The next step is to attribute the rights of associates.

Associate, in relation to a participator, includes:

- any relative — where relative means husband, wife or civil partner, parent or remoter forebear, child or remoter issue or brother or sister. Separated spouses are associated until they divorce. Half-brothers and sisters are associated, but step-brothers and sisters are not;
- business partner — where this means partners in a partnership or members in an LLP;
- the trustees of any settlement in relation to which the participator (or any relative living or dead) is or was a settlor;

- the trustees of a settlement or the personal representatives if the participator has an interest in any shares or obligations of the company which are the subject of a trust or are part of the estate of a deceased person; and
- if the participator is a company, any other company interested in those shares or obligations.

(CTA 2010, s448)

**If with this test the companies are under common control you need to see if the FA 2011 changes help.**

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## Step 3 –FA 2011 changes

CTA 2010, s27 has provisions to exclude business partners and some associates in determining control for the purposes of the small profits rate. Under the new provisions, in considering whether companies are associated s 27 CTA 2010 applies where there is no substantial commercial interdependence (SCI) between the companies. The impact is that the attribution of rights will only include associates under s451 CTA 2010 where there is SCI between the companies.

There is no statutory definition of SCI but HMRC have produced new guidance. SCI is determined by looking at the degree of financial, economic or organisational interdependence between the companies. It is not necessary for all three links to exist.

### Financial interdependence

Two companies are financially interdependent if one gives financial support to another or each has a financial interest in the affairs of the same business. HMRC's guidance has a number of examples including:

*"R is the major shareholder and director of Company D which provides IT services. His son, S, is the major shareholder and director of Company E which provides business management services. R provided, as a family, rather than business matter, a personal guarantee in respect of a bank loan made to Company E when S set up the business. The companies are controlled by associated individuals but there is no financial (or other) link between the two companies because the guarantee has been given by R in a personal capacity and this financial support has no link to Company D – the companies are therefore not*

*associated. If, however, the loan to Company E was made direct from Company D or R had given additional security over the assets of Company D in support of his loan, there would be a financial link between the two businesses, either directly or indirectly, which would cause the companies to be "associated"."*

*"Mr J owned a newsagents Company T and a joinery business, Company U. On retirement Mr J's son bought all J's shares in Company T and Mr J's daughter bought all J's shares in Company U. Neither J's son nor daughter has any involvement in the other's company and the companies themselves have no economic, financial or organisational links. Notwithstanding Mr J's previous ownership of both, company T and company U are not associated."*

## Economic interdependence

Two companies will be economically interdependent where:

- they seek to realise the same economic objective; or
- the activities of one benefit the other; or
- the companies have common customers.

HMRC's guidance has some examples, two of which are reproduced below.

*"Mr Q is the major shareholder in Company C which runs a large Chinese restaurant. It also operates a Chinese supermarket backed by its reputation as a restaurant. Mrs Q, who is a chef trained in France, is the sole shareholder in Company D which runs a gastronomically starred restaurant she has built up from scratch. Company D also imports delicacies from all over the world for sale on the internet, again backed by its reputation as a restaurant. Although Mr Q and Mrs Q are husband and wife and in the same trade, there is no link between their companies, which have been trading since well before they knew each other. They are not associated."*

*"M is the major shareholder in Company R, a dry cleaning business. Mrs M has opened a second dry cleaning business in the same town. This is run by Company S, of which she is the sole shareholder. Company S offers specialist services in relation to wedding and evening dresses in addition to the normal range of dry cleaning facilities. Company R acts as agent for these specialist services which it does not have the ability to supply itself. Company S and Company R share the same basic economic objective and their activities are of mutual benefit. The companies are therefore associated."*

## Organisational interdependence

Two companies are organisationally interdependent where they have:

- common management; or
- common employees; or
- common premises; or
- common equipment.

HMRC examples include:

*“Y is the director and sole shareholder of Company A and Mrs Y is the major shareholder in Company B. The two companies operate a chain of hairdressing salons. Company A provides hairdressing services and Company B provides hairdressing products. Company A rents the premises, employs the stylists and receptionists and pays all the bills. There is no cross charge for the use of facilities. Credit card payments are accepted by the salons, the electronic swipe machines being in the name of Company A. There is a single bank account to which the swipe machines are attached. At the end of each day the bankings are split between the two companies and transferred to their main bank current accounts. The accounts of the two companies do not truly reflect the situation of the businesses but are just an artificial division. In reality the two companies are part of a single organisation – there is just the one business.”*

*“Mr and Mrs B each run their separate companies from their family home which is owned by Mrs B. Mr B’s company could not afford to buy or rent other accommodation to trade from. Apart from sharing the family home and the family’s domestic ‘phone line for occasional business calls and internet access there are no other financial, economic or organisational links between the two companies. Although Mr B’s company could not survive organisationally or financially without use of the family home, there is no direct or indirect financial support from either his wife or his wife’s company to either him or his company, and no organisational links which amount to substantial interdependence.”*