



Headlines

- Are Redundancy Payments Tax Deductible?
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Are Redundancy Payments Tax Deductible?

One question many business owners ask during restructures or closures is whether redundancy payments qualify for corporation tax relief. The answer depends largely on the circumstances in which the redundancy arises.

The tax treatment differs depending on whether:

- The business is continuing to trade, or
- The business is ceasing entirely

Understanding the distinction is important because it can significantly affect the amount of tax relief available.

Redundancies in an ongoing business

Where a business continues trading but reduces staff numbers, redundancy payments will generally qualify for tax relief under the normal trading expense rules.

This often happens where:

- Part of the business closes
- Operations are scaled back
- Certain departments become unprofitable

For example, a manufacturer may decide to shut a loss-making retail outlet while continuing its wholesale operations. Staff made redundant as part of the closure would typically generate an allowable tax deduction for the business.

The key test is whether the expense is incurred **wholly and exclusively for the purposes of the trade**.

In practice, HMRC will usually accept redundancy payments made by an ongoing business as deductible, particularly where the payments are commercially reasonable.

Redundancies when a business closes

Different rules apply where the business is ceasing to trade completely.

Normally, once trading ends, expenses incurred afterwards may not qualify under the standard trading deduction rules. However, special tax provisions exist to allow relief for redundancy payments made on closure.

This is helpful for businesses winding down operations, but there is an important restriction.

Tax relief can be capped

For businesses that cease trading, the amount of tax relief available for redundancy payments may be limited.

The allowable deduction is capped at the greater of:

- The employee's statutory redundancy entitlement, or
- The amount payable under the employment contract

However, contractual redundancy payments only qualify up to three times the statutory redundancy amount.

Importantly, this does not restrict how much redundancy pay a business can offer. It only restricts how much can be claimed as a tax deduction.

Director-shareholder redundancies need care

Extra caution is needed where redundancy payments involve directors who are also shareholders, particularly if they are exiting the business as part of a sale or restructuring.

HMRC may scrutinise whether the payment is genuinely compensation for redundancy or whether it is linked to ownership or share disposal arrangements. In these situations, supporting documentation and commercial justification become especially important.

Final thoughts

The tax treatment of redundancy payments depends heavily on the wider commercial context.

- If the business continues trading, redundancy payments will generally qualify for full tax relief
- If the business is closing, relief is still available, but statutory limits may apply

Given the potential for HMRC scrutiny, particularly around director-shareholders or large payments, businesses should review redundancy arrangements carefully before making payments.

Investing in a Start-Up: Should You Use Shares or a Loan?

When investing in a start-up company, one of the first decisions is how to structure the investment. Should you subscribe for shares or lend the business money?

While both approaches can support a growing company, the tax treatment and commercial outcomes can differ significantly, particularly if the business struggles or fails.

Understanding the risk

Start-up investing always carries risk. Higher potential returns usually come with a greater chance of losing capital.

Because of this, investors should consider not only the possible upside, but also what tax relief may be available if the investment performs poorly.

Tax treatment if the investment fails

Whether you invest through shares or a loan, you may suffer a financial loss if the company fails. In many cases, this can create a capital loss for tax purposes.

However, there is an important difference between the two structures.

Why shares can offer a tax advantage

If you subscribe for shares and later sell them at a loss, or the shares become effectively worthless, you may be able to claim **share loss relief**.

This can be particularly valuable because, subject to conditions, the capital loss can potentially be converted into an income tax loss. Instead of only offsetting the loss against capital gains, you may be able to offset it against:

- Employment income
- Rental income
- Dividend income
- Other taxable income

For higher-rate taxpayers, this can substantially reduce the real financial loss.

Example

An investor subscribes £50,000 for shares in a start-up company. A few years later, the shares are sold for £25,000 after the business underperforms.

This creates a £25,000 loss.

If the investor qualifies for share loss relief and pays tax at 40%, the loss could generate an income tax saving of £10,000.

As a result:

- Economic loss: £25,000
- Tax saving: £10,000
- Net loss after tax relief: £15,000

When loans may be preferable

Although shares can provide stronger downside tax protection, loans offer different advantages.

With a loan:

- You can charge interest
- You may receive regular income even if the company is not profitable
- The loan may rank ahead of shareholders if the company becomes insolvent

This can appeal to investors who want ongoing returns rather than relying purely on future growth in company value.

Investors may also negotiate a higher interest rate to reflect the additional risk of lending to an early-stage business.

Shares are often better for growth

If your goal is long-term capital appreciation, shares are generally the more attractive option.

As the company grows:

- The value of the shares can increase significantly
- Any eventual gain may be taxed under capital gains tax rules rather than income tax rates

This can produce a more favourable tax outcome on a successful exit.

Can you combine both benefits?

In some situations, investors may try to combine the advantages of shares and loans.

One option can be **convertible shares**, which may later convert into a loan arrangement. This can provide:

- Access to share loss relief in the higher-risk early years
- The ability to receive interest income later if converted into debt

These arrangements require careful structuring and professional advice, but they can offer flexibility depending on the investor's objectives.

Final thoughts

There is no universal answer when choosing between shares and loans. The best option depends on:

- Your appetite for risk
- Whether you want income or capital growth
- Your personal tax position
- How important downside protection is to you

In general:

- **Shares** can provide stronger tax relief if the investment fails and better upside potential if the company succeeds
- **Loans** may suit investors looking for regular income and additional security

Before investing in a start-up, it is worth reviewing both the commercial and tax implications carefully to ensure the structure aligns with your long-term objectives.

Can HMRC Refuse Tax Relief for Travel Expenses?

Many business owners assume that if a journey is work-related, the travel costs will automatically qualify for tax relief. However, the rules can become far more restrictive when a sole trader incorporates and begins operating through a limited company.

In some cases, a journey that previously qualified for tax relief as a sole trader may no longer qualify once the business operates through a company.

Business travel versus ordinary commuting

The basic principle is straightforward:

- Business travel costs are generally tax deductible
- Ordinary commuting costs are not

The challenge lies in understanding the difference.

Ordinary commuting is travel between:

- Your home, and
- Your permanent workplace

Travel to a temporary workplace, however, can qualify for tax relief.

Position for sole traders

For self-employed individuals, the rules are often more flexible.

If you travel from home to different customer sites, suppliers or temporary work locations, these journeys are usually treated as business travel. This means the associated costs can normally be deducted for tax purposes.

However, problems can arise if you attend the same location regularly and frequently. HMRC may argue that the location has effectively become a permanent workplace, turning the journeys into ordinary commuting.

What changes after incorporation?

Once you operate through a limited company, you become an employee or director of that company. This means the employment travel rules apply instead of the self-employed rules.

Under these rules:

- Travel to temporary workplaces can still qualify for relief
- But there is a key restriction known as the 24-month rule

If you attend the same workplace for more than 24 months, or you expect the engagement to last longer than 24 months, the workplace becomes permanent for tax purposes. From that point onwards, travel costs are no longer deductible.

The IR35 trap

The position becomes even stricter where:

- You work through your own company or another intermediary, and
- The IR35 or off-payroll working rules apply

In these circumstances, journeys between your home and the place where you work are treated as ordinary commuting in almost all cases.

This means:

- No tax deduction is available for the travel costs
- The restriction can apply even where the workplace would otherwise have qualified as temporary

The same restriction may also apply where the worker operates under another person's supervision, direction or control, even if IR35 itself does not apply.

Example

A consultant previously operated as a sole trader and travelled from home to various client sites, claiming tax relief for mileage and travel expenses.

The consultant later incorporates and provides services through a limited company. The consultant then works at the same client site for an extended period under the client's supervision.

As a sole trader, the travel may have qualified for relief. After incorporation, however, the travel could be treated as ordinary commuting under the IR35 or employment travel rules, meaning no deduction is available.

Final thoughts

Changing from sole trader to limited company status can affect more than corporation tax and liability protection. It can also significantly alter the tax treatment of travel expenses.

In general:

- Sole traders can often claim relief for travel to temporary customer locations
- Company directors and employees face stricter rules
- IR35 and supervision or control arrangements can remove relief entirely for home-to-work journeys

Before incorporating or accepting long-term assignments through a company, it is worth reviewing the travel expense implications carefully. What qualified for tax relief previously may no longer do so under the employment and IR35 rules.

EIS Relief Denied Despite Advance Assurance

The Enterprise Investment Scheme (EIS) remains one of the UK's most valuable tax reliefs for investors backing higher-risk businesses. However, a recent tribunal case highlights just how strict the qualifying conditions can be, even where HMRC has already provided advance assurance.

The case involved two energy companies that believed they had satisfied the conditions for EIS relief, only for HMRC to later deny the relief because trading had not started within the required timeframe.

The background

Both companies issued shares on 4 April 2016 after receiving advance assurance from HMRC that the investments were expected to qualify for EIS relief.

Under the EIS rules, the companies then had to begin carrying on a qualifying trade within two years, meaning by 4 April 2018.

The businesses intended to operate power stations and had taken substantial preparatory steps:

- Suitable sites had been identified
- Contracts had been entered into
- Construction work had begun in one case

Despite this, neither company was actually generating electricity or earning income by the deadline.

HMRC's position

HMRC argued that neither company had commenced trading within the required period because:

- The power stations were not operational
- No electricity was being supplied
- No income was being generated

In HMRC's view, the businesses were still in a preparatory phase rather than actively trading.

Tribunal decision

The Upper Tribunal agreed with HMRC and dismissed both appeals.

The tribunal concluded that:

- Entering into contracts and preparing facilities was not enough

- Construction work alone did not amount to trading
- The businesses needed to be operational and capable of carrying out their intended commercial activity by the deadline

One company had not even secured a final site in time after its original plans fell through. The other had started building the power station, but it was still not operational when the deadline passed.

Why this matters

The decision highlights an important distinction between:

- Commencing a trade for corporation tax purposes, and
- Commencing a qualifying trade for EIS purposes

For normal corporation tax, activities such as:

- Opening a business bank account
- Advertising services
- Signing contracts

may sometimes indicate that trading has started.

For EIS, however, the threshold is much higher. The business generally needs to be actively operational and capable of generating revenue.

Advance assurance is not a guarantee

A key point from the case is that HMRC's advance assurance does not guarantee that relief will ultimately be available.

Advance assurance is based on the information provided at the time. If the business later fails to meet the qualifying conditions, relief can still be refused.

Investors and founders should therefore avoid treating advance assurance as final approval.

Final thoughts

EIS relief can provide significant tax advantages, but the rules are tightly drafted and strictly applied.

Businesses seeking EIS relief should ensure:

- Trading genuinely begins within the required timeframe
- The business is operational, not merely preparing to trade
- Evidence exists showing commercial activity and income generation where possible

For investors, this case is a reminder that even where HMRC has provided advance assurance, the qualifying conditions must still be fully met in practice.

Interesting Reads

UK Personal Tax: Complete Guide for Individuals

In this UK Personal Tax guide by Clear House, you'll explore Income Tax, NICs, Capital Gains Tax, dividends, pensions, Inheritance Tax, savings interest, student loans, HICBC, and personal tax allowances. The guide also covers tax rates, allowances, and filing rules.

How to Take Money Out of a Limited Company?

Most directors don't take money out in just one way. The typical structure is a small salary plus dividends, then layering pensions or expenses depending on goals.

A Beginner's Guide to Making Tax Digital

Making Tax Digital (MTD) is a digital system for reporting income and expenses and submitting tax returns. Announced in the 2015 budget, MTD aimed to modernise the UK's tax system.



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