# Cheatography

### UK Tax System Cheat Sheet

by mgxx2004 (mgrawahi) via cheatography.com/197440/cs/45419/

#### Tax Classification

Tax is classified into two categories:

- 1. Direct Tax
- 2. Indirect Tax

#### **Direct Tax**

Tax on individual's wealth/income.

Examples: 1. Income Tax

Capital GainsTax

#### Indirect Tax

Tax on an individual's transactions

Example: 1. VAT

2. Insurance Tax

## What profits are subject to income tax?

Trading profits of UK residents are subject/chargeable to income tax

## Determination of trading vs. capital transactions

By applying the '6 Badges of Trade'.

If one or more apply, then the transaction is considered a trade, though final decision is made by the courts.

## Sole Trader (self-employed) vs. Company

**Tax:** Self-employed face lighter taxes (20% income tax vs 25% corporation tax).

Liability:

Companies limited liability **vs.** sole traders risk losing everything.

Setup and Mainte-

nance:

Sole trader simpler set-ups vs.
Companies require legal administration paperwork and costs to maintain.

Ownership & Flexibility: Companies owned via shares, thus, are offer more flexibility for raising capital, investment, or selling, unlike sole traders.

#### The Six Badges of Trade

- 1. Subject of Matter of Transaction
- Length of Period of Ownership
- 3. Frequency of Transactions
- 4. Supplementary Work
- 5. Reason for Sale
- 6. Motive of Transaction

#### Tax Evasion

Illegal actions like hiding income or falsifying tax return, is punishable by fines or imprisonment.

## Activities Classified as Trading for Tax Purposes

Activities that involve repeated buying and selling, particularly to make profit.

#### Tax Avoidance

Legal but crafty use of loopholes to reduce tax, often through artificial schemes, although legal, the HMRC see it as exploitation of rules against their intended purposes.

#### **HMRC**

Her Majesty's Revenue and Customs

Responsible for collecting taxes, administering benefits, and enforcement of tax and customs law

### Tax Year for Individuals - UK

Individuals (e.g. Assessment Fiscal Year).

### Addressing/reducing tax evasion/avoidance

 Targeted Anti-avoi-TAAR dance Rule
 General Anti-abuse GAAR Rule
 Disposal of Tax DOTAS Avoidance Schemes

## Impact of measures to reduce tax evasion/avoidance

Decline of creative tax planning by making avoidance schemes increasingly difficult and risky.

## HMRC Criteria for Self-employment

Control

Holidays and Sickness

Equipment

**W**ork Performance and Correction

Exclusivity

Remuneration and Financial Risk

## Tax Application to Limited Companies

Limited companies pays:

- 1. Salary to employees (20% income tax & 8% national insurance).
- 2. **Dividends** (taxed at 8.5% basic rate).
- 3. **Corporation tax** (25%) on profits before dividends.

### Tax Year for Corporations - UK

Corpor- 1st April to 31st ation March inclusive (e.g. Tax Financial Year).

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Year

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By mgxx2004 (mgrawahi)

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### Self-employment vs. Employment

Self Employment

- Higher risk and reward.
- More expenses allowed (lower tax).
- Taxes paid later.
- No compulsory national insurance.
- More control over Activities.

### Employment

- Fewer expenses allowed.
- Taxes paid via PAYE.
- Compulsory national insurance (8%).
- Holiday and sick pay.
- Social security benefits.

### Tax Application to Sole Traders

Sole traders are **taxed** on business profits under income tax rules, with no corporation tax or dividends.

- Income tax is 20% on profits.



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