

What is HMRC's Targeted Anti-Avoidance Rule (TAAR)?

Glossary

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If you're thinking about closing your limited company and taking the remaining profits as a capital distribution, you should be aware of HMRC's **2-year rule** or the **Targeted Anti-Avoidance Rule (TAAR)**, as it's technically called.

It's HMRC's way of stopping "phoenixing" which is when someone shuts down one company, pockets the profits at a lower capital gains tax rate, and then starts up a very similar business shortly after.

Here's what you need to know.

First up: how capital distributions are normally taxed

When you close a company and take out any remaining profits, it's often possible to treat that money as a **capital gain**, rather than income.

That's great news if you're eligible for **Business Asset Disposal Relief (BADR)**, as you'd usually pay **just 18%** tax on those profits, instead of higher dividend rates (up to 39.35%).

But, and it's a big but, HMRC can reclassify that capital gain as **income** (e.g. dividends) if they think you're trying to get around the rules.

The TAAR: what it is and why it matters

TAAR stands for **Targeted Anti-Avoidance Rule**, and it kicks in when all **four** of the following apply:

1. You **close your company** and receive a capital distribution (typically via Members Voluntary Liquidation or informal strike-off).
2. Within **2 years**, you're involved in a **similar trade or activity** whether as a sole trader, a partner, or even through a new limited company.
3. The main purpose (or one of the main purposes) of closing the old company was to **get a tax advantage** i.e. paying lower Capital Gains Tax rather than dividend tax.
4. HMRC believes your **intention** was to avoid higher income tax on those profits.

If all of that sounds a bit subjective, it is. HMRC looks at your **actions, timing, and intentions**.

So... can I start another business after closing my company?

Yes — but with caution. Here's the key question: **how similar is the new business?**

- If you close a software consultancy and start another software consultancy within 2 years - red flag.
- If you shut down a design agency and open a bakery - probably fine.
- If your spouse or a business partner sets up a "new" company doing the same work for the same clients - also a red flag.

The more it looks like the new business is just a continuation of the old one, the more likely HMRC is to apply TAAR.

What happens if HMRC applies the rule?

They'll reclassify your capital distribution as **income**, which means you'll pay **dividend tax rates** on that money instead of Capital Gains Tax.

So, if you've already claimed BADR and paid 18% tax, you may end up with a **retrospective tax bill** and possibly interest and penalties.

Avoiding trouble: best practices

Here's how to stay on the right side of the rules:

- **Don't plan to close and restart the same trade within 2 years.** Wait it out if needed. If a contract has come to an end and you're moving into permanent employment, we also advise that you give it a month or two in this permanent employment to make sure you're happy and don't have the urge to return to contracting/freelancing in the near future.
- **Keep things clearly separate.** A new company doing totally different work is much less risky.
- **Document your intentions.** If you're retiring, leaving freelancing permanently, or genuinely changing career - make a note of that in your records.
- **Get professional advice.** Before looking to close, always speak to your Mighty accountant - we're happy to advise you!

Final word

TAAR isn't about stopping you from moving on, it's about stopping tax avoidance.

If you can't see yourself starting a new business in the next couple of years, and your next steps are genuine and not just a way to access your company profits at a lower tax rate, you're probably fine. But if there's even a small chance that HMRC might see your new business as a continuation of the old one, it's worth treading carefully.

In short: don't risk it. Play it smart, and stay *TAARtally* informed (apologies, we couldn't resist). Got questions? Just email your dedicated Mighty accountant or support@mightyaccounting.com and we'll be happy to help.

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