

Corporation tax loss relief –from 1 April 2017

(Lecture B1079 – 20.27 minutes)

More flexible use of brought forward losses

Certain corporation tax loss amounts incurred from 1 April 2017 can be carried forward against all income and gains and those of 75% group companies in future. Group relief of brought forward losses is only after the company that incurred the loss has reduced its relevant profits by the maximum amount in that period.

A company that does not have a period to 31 March 2018 will need to apportion any profit or loss on a just and reasonable basis, though there are special rules in some situations.

This flexible use of brought forward losses covers:

- trading losses;
- non-trading loan relationship deficits;
- management expenses of investment companies;
- UK property losses; and
- non-trading losses on intangible fixed assets

If the trade falls to a negligible level after 1 April 2017, trade losses from then can only be carried forward against future profit of same trade.

Separate records of Pre-1 April and post 1- April 2017 will need to be kept as will post-1 April 2017 losses that can only be used against profits of the same trade to ensure the correct set-off is made.

Restriction on the amount of losses brought forward that can be set off in a period

The set off of losses brought forward in a particular period is limited to £5m plus 50% of profits above £5m. This is a group wide limit and for a period of 12 months – in a short accounting period the £5m will need to be time-apportioned. A group can choose how to allocate the £5m allowance to each company. This restriction does not just apply to losses from 1 April 2017, but older losses brought forward as well.

Capital losses can still only be offset against gains, but without any £5m restriction.

Loss pro-forma approach

Calculate the company's taxable profits after all reliefs (including in-year losses and group relief), but exclude:

- carried forward losses;
- carried back reliefs; and
- post-31 March 2017 carried forward losses to be claimed from other group companies;

- Allow up to £5,000,000 of these profits to be relieved in full by carried forward losses;
- Allow up to 50% of the remaining profits to be relieved by the remaining carried forward losses (with pre-1 April 2017 losses to be used in priority to later ones); and
- If there are still profits which can be relieved within the 50% limit, allow them to be relieved by post-31 March 2017 carried forward losses which have been claimed from other group companies.

Other points

Losses carried back from a later year are not deducted in arriving at the 50% of profit above £5m figure for current year loss set-off.

If the profit for the current period is both trading and non-trading, allocate in-year losses and group relief pro-rata. This may then affect the ability to utilise pre-1 April 2017 brought forward losses.

Groups can allocate their £5m allowance to group companies in any proportion they choose.

Pre 1 April 2017 losses can only be carried forward against profits of the same trade. They are however subject to the 50% restriction and £5m allowance.

Principles not affected by the new rules

Loss carry back – still attractive as there is no £5m cap on the amount of losses carried back, so they are fully deductible.

Cessation rules for trading and property businesses will not change. E.g. terminal loss relief of losses made in final accounting period – still carry back against trading profits of the previous 3 years (LIFO basis)

Any losses brought forward for periods before the period when the trade ceases can be carried back three years against all income and gains without the £5m restriction applying

The set off of capital losses is unaffected as seen earlier.

Anti-avoidance rules

There have been some changes to the loss anti-avoidance rules to cater for the possible abuse of the flexible set off of post 1-April 2017 loss amounts. If a company with post 1-April 2017 losses brought forward is acquired, the new group it has joined cannot use those losses for a period of 5 years by means of group relief. There are also rules to prevent the use of the acquired company's brought forward losses by allocating gains to it from other group companies.

Major change in nature of conduct of trade ("MCINOCOT")

If there is a MCINOCOT and within 3 years the ownership of the company changes, any remaining trade losses are forfeited (as before).

If there is change in ownership of the company, followed by a MCINICOT in the following 5 years, any remaining losses are forfeited (an increase from 3 years).

Winners

- Small groups unlikely to have more than £5m of losses or for which this is a high proportion of the total - £5m exclusion from the 50% rule will then benefit them (but unless the £5m is index-linked, its value will erode over time).
- Groups with post-2017 losses which would have become trapped losses (more flexible offset will outweigh impact of the 50% restriction).

Losers

- Large groups with bad trading year post April 2017 (in past relief in full against the next available trading profits but where relief now spread forward).
- Capital intensive businesses or high risk start-up businesses with deep initial losses
- Groups with unpredictable income patterns e.g. split between trading and non-trading income may be difficult to judge most efficient use of tax losses within election time limits
- Groups and entities where there is a variable split between trading and non-trading income (can lead to distortion).

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