Increased flexibility

Large Corporate OMB

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Joe Brough provides a back to basics guide to corporation tax loss relief

Key Points

What is the issue?

Following the changes enacted by Finance Act (No 2) 2017 governing the restrictions on corporation tax trading losses carried forward, what are the options for relieving corporation tax trading losses?

What does this mean to me in practice?

For an accounting period beginning on or after the 1 April 2017, where trading losses are carried forward, they can now be used to offset a company, or unincorporated association that pays corporation taxes, total taxable profits or surrendered via group relief of a later period rather than be restricted to automatic use against trading profits of the same trade within the company that incurred the loss.

What can I take away?

Where corporation tax trading losses are incurred on or after 1 April 2017, the options to relieve the losses carried forward are now more flexible than they have been in the past.

Finance Act (No 2) 2017 introduced changes to the ways in which corporation tax trading losses carried forward can be relieved against future period total taxable profits for accounting periods beginning on or after 1 April 2017. Prior to the changes, any trading loss that had not been relieved by either a current year and carry back claim against total taxable profits, or surrendered via group relief, was only available to be carried forward and be automatically relieved against the first available trading profits of the same trade arising in the same company.

The changes introduced now alters the way and against what types of income a company can utilise its carried forward trading losses, so that trading losses incurred in accounting periods beginning on or after 1 April 2017 can now be used against a company’s total taxable profits, subject to certain restrictions, of a subsequent period, or surrendered via group relief to other group companies.

Changes have also been enacted so that more flexibility has also been given as to the relief that may be obtained for pre 1 April 2017 trading losses brought forward. The requirement for these losses to be automatically relieved against the first available trading profits from the same trade available has been lifted, which will allow companies to disclaim pre 1 April 2017 brought forward losses if they wish to do so in favour of post 1 April 2017 trading losses. However, when utilised, the losses are still subject to the streaming rules, which are more restrictive than for ‘new’ trading losses brought forward.

What are the options available for relieving a trading loss?

The change in legislation only affects losses carried forward for losses incurred during accounting periods beginning on or after 1 April 2017. Claims which affect current or prior periods are unaltered.

The options available to relieve a trading loss can be summarised as follows:

- Current year claim against total income
- Carry back claim against total income of the previous 12 months
- Group relief against total income
- Carry forward losses against future taxable profits

When making claims against total income in the current and previous periods the loss must be offset in its entirety and cannot be restricted to preserve the availability of relief for qualifying charitable donations. This is also true for losses surrendered via group relief, except that loss relief is claimed after the deduction of qualifying charitable donations.

Current year claim

A current year claim can be made to offset the trading loss against total income before qualifying charitable donations of the period. A current year claim does not have to be made, in which case the loss is automatically carried forward and a carry back claim cannot be made. If there are no other profits available to be offset by a current year claim then this does not prevent a carry back claim being made.

Carry back claim

The amount of loss that can be relieved under a carry back claim is the lower of the loss remaining after a current year claim has been made, and the total taxable profit before qualifying charitable donations in the previous 12 months.

A carry back claim can be used to relieve the remaining trading loss against the total profits of the company, for 12 months prior to the start of the loss making period. This is an important distinction as it means that where the accounting period immediately preceding the loss making period is less than 12 months, the loss can be carried back over more than one accounting period. To calculate the available profits that can be relieved, the profits of the period preceding the short period would have to be time apportioned.

Group relief

Where a trading loss is incurred, the loss making company may make an election to surrender the loss to a profit making company in the same 75% group. In determining whether the two companies are part of the same 75% group, one company must be a 75% subsidiary of the other, or they must both be 75% subsidiaries of a third company. Where there are sub-subsidiaries there must be an effective 75% shareholding when the holdings are multiplied down.

A claim for group relief can be made before the surrendering company considers any loss relief against its own profits.

The maximum amount of loss that can be surrendered is the lower of:

- The available profit in the claimant company
- The available loss in the surrendering company

When considering what loss can be claimed, the claimant company must first calculate the amount of available profit that can be offset by the surrendered loss. The available profit is the sum of its profits after deducting any of its own current losses, brought forward losses and qualifying charitable donations.

Where the accounting periods of the claimant and surrendering company are non-coterminous, the available profits and losses must be apportioned to reflect the common periods of the two companies. Time apportionment must also be made where there is a short accounting period, or one of the companies joins or leaves the group, as only losses incurred whilst a group member are available for offset against common period profits.

Where a loss is surrendered to a group company, it must be utilised within that chargeable period and cannot be further surrendered to another group company, carried back against prior period profits or withheld and carried forward for use against future losses.

Losses carried forward

Losses that remain after considering the above options are carried forward to be used against subsequent period’s profits.
Where brought forward losses have arisen in accounting periods prior to 1 April 2017 then these losses can still only be utilised against profits of the same trade in the same company. However, where the losses have been incurred post 1 April 2017 then these losses can now be utilised against the total profits of the company.

In a further change, brought forward losses can now also be group relieved against another group company’s profits.

Are there restrictions to relief?

The amount of total profits (after the deduction of in year reliefs, but excluding carried forward and carried back reliefs) that can be offset by brought forward losses is restricted to the first £5 million of profits, and an additional 50% of profits that exceed £5 million. This relief is subject to the following conditions (CTA 2010 s 45A):

- The company must continue to trade in the following accounting period
- The trade must not be an oil and gas ring fenced trade
- The trade must not have become small or negligible in the loss-making period*
- The trade must be commercial or be carried on for statutory functions in both the loss making period and the period for relief
- Losses must not be from a trade carried on wholly outside the United Kingdom for the loss making period

*Whether a trade has become small or negligible would have to be judged against the facts of each case.

Where relief against total profits is denied under CTA10/S45A, relief may still be available against profits of the same trade only under CTA10/S45B.

When relieving carried forward losses via group relief, a company can only surrender carried forward losses that it is unable to deduct from its own profits within that accounting period. Conversely, before claiming carried forward loss via group relief, the claimant company must have used any of its own carried forward profits to the fullest extent.

It should also be noted that the deductions allowance of £5 million and 50% of additional profits exceeding £5 million is shared amongst group companies and legislation is in place to prevent groups obtaining further relief than the restricted maximum.

Periods straddling 1 April 2017

When a company has an accounting period that straddles 1 April 2017, HMRC guidance states that the profits or losses must be apportioned on a time basis in order to calculate pre and post 1 April 2017 split, however, where this produces an unjust or unreasonable result, an alternative basis may be used.

What order should the reliefs be claimed in?

When considering how trading losses should be utilised, from a practical perspective, there are tangible cash flow advantages from making a claim as soon as possible and utilising the loss. The rate at which tax is saved is also important, as it should be the aim to save tax at the highest rate possible, which in a time where corporation tax rates are due to fall to 17% for accounting periods beginning on or after 1 April 2020, the tax saved by carrying forward trading losses is being eroded each year.

Where losses have been carried forward, HMRC’s draft guidance states that after the deduction of in year reliefs, pre 1 April 2017 losses should be relieved first followed by post 1 April 2017 losses.