

Part 4: Loss Relief

Overview

1. This Part contains rules relating to various reliefs available for losses. It is based on sections 118, 118ZB to 118ZD, 392A to 397, 399, 400 and 503 of ICTA.
2. The majority of the legislation is in Chapters II and III of Part X of ICTA. However, provisions that deal with specific areas of taxation are located elsewhere. For example, the sections that deal with loss relief available to corporate partners are located with the partnership legislation in Chapter VII of Part IV of ICTA. To make it easier for users to find the particular loss provisions in which they are interested the proposed approach is to bring together all of the clauses dealing with corporation tax losses in one Part.

Q1. We welcome comments on the approach of bringing the loss relief provisions together in one Part.

3. The reliefs are set out in separate Chapters.
4. The source legislation deals with the carry forward of trade losses (section 393 of ICTA) before set off against total profits of the same accounting period or carry back (section 393A of ICTA). In practice companies tend to prefer to set losses off against total profits or carry them back rather than carry them forward. The rewritten legislation reflects this practice by dealing first with the set-off against total profits and carry back, from clause 3 onwards, and then turning to the carry forward of losses in clause 15.

Q2. We welcome comments on the proposal to re-order the loss relief provisions so they appear in a more logical order.

5. The terms “total profits”, “net profits” and “profits” are currently being considered in the context of Bill 6 as a whole. Where these terms occur in the Loss Relief clauses they should be regarded as provisional for the time being.
6. “Profits” is currently defined in section 6(4) of ICTA as “income and chargeable gains”. In Bill 6 it is likely that “total profits” will describe all those items of income and chargeable gains added together. “Total profits” will thus include everything within the charge to corporation tax and is to be arrived at without any deductions, except those allowed in arriving at the constituent part of a company’s income, or in calculating its chargeable gains. Reliefs and deductions (trade losses claimed under clause 3, management expenses, group relief etc) will then be subtracted from “total profits” to arrive at “net profits”.
7. In some instances “profits” refers to commercial profits and is not intended to attract the “income and chargeable gains” definition in section 6(4) of ICTA. In ICTA such instances are either covered by the phrase in section 6(4) “except in so far as the

context otherwise requires” or by the relevant section not being one to which section 6 applies. The approach to “profits” of this nature in Bill 6 has not been finally decided. Where in this Part “profits” is intended to refer to commercial profits it will either be clear from the clause itself or will be referred to in the relevant note.

Chapter 1

Clause 1: Overview of Part

8. This clause provides an overview of the Part. It is new.

9. *Subsection (3)* refers to clause 1261[[j030302](#)] of Bill 5 which provides as follows:

(1) The same rules apply for corporation tax purposes in calculating losses of a trade as apply in calculating profits.

(2) This is subject to any express provision to the contrary.

Chapter 2: Trade Losses

Overview

10. This Chapter deals with relief for trading losses.

Clause 2: Overview of Chapter etc

11. This clause provides an overview of the Chapter. In addition it carries forward the effect of sections 6(4)(b) and 834(2) of ICTA in providing that a “trade” includes an office.

Clause 3: Relief for trade losses against total profits

12. This clause explains how a loss in a trade may be relieved against total profits of the same or earlier periods. It is based on section 393A(1), (2), (3), (9) & (10) of ICTA.

13. *Subsection (3)(b)* establishes that a loss in trade may be carried back to the twelve month period prior to the accounting period in which the loss arose. The exceptions to this rule, where the carry period is extended, are set out in clauses 5 to 7. These exceptions will either affect companies rarely or not at all. *Subsection (10)* provides signposts to clauses 5 to 7. These are intended to assist the reader by indicating where to find provisions which extend the scope for relief in certain circumstances.

14. *Subsection (4)* deals with the order of set off of losses claimed under subsection (3). Such losses must first be set against total profits of the loss making period before, if the claim so requires, being carried back to earlier periods. Where it is possible to carry a loss back for more than one period (see Clauses 4, 5 and 6) then the loss must be set against total profits of the most recent period before the balance of the loss can be carried back to the period preceding that period and so on.

15. *Subsection (4)* refers to “... the amount of the loss so far as it cannot be deducted ...”. The use of “cannot” accords with the current wording of the clause that sets out

the corporation tax calculation. Work on this clause is still in progress. If at any stage the wording of this clause changes then it will be necessary to consider the effect on this subsection.

16. *Subsection (7)* sets out the time limits for making a claim. The time limit may be extended by an officer of Revenue and Customs. See *Change 601* in Annex 1.

Q3. *Change 601* reproduces *Change 5* in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry *Change 5* across to corporation tax.

Clause 4: Limit on deduction if accounting period falls partly within 12 month period

17. Where a loss is being relieved against the profits of an earlier accounting period this clause limits the relief available if that period falls partly within the twelve month period prior to the loss-making period. It is based on section 393A(2) of ICTA.

18. The effect of this clause can be illustrated as follows:

Example

Accounting period 3	12m	01/01/11 to 31/12/11	Loss in trade	£24,000
Accounting period 2	8m	01/05/10 to 31/12/10	Total profits	£12,000
Accounting period 1	12m	01/05/09 to 30/04/10	Total profits	£15,000

The twelve month period prior to the loss making period is 01/01/10 – 31/12/10. Accounting period 2 falls wholly within this period and the loss in trade is sufficient to cover all of the total profits of this period. £12,000 of the loss in trade remains to be relieved. The proportion of Accounting period 1 that falls within the relevant twelve month period is 4/12. 4/12 of the total profits of Accounting period 1 is £5,000. Therefore the amount to be deducted under clause 3(3) cannot exceed £5,000. This means that £7,000 of the loss in trade arising in Accounting period 3 cannot be relieved under clause 3.

Clause 5: Terminal losses: extension of periods for which relief may be given

19. This clause extends the length of the period referred to in clause 3(3)(b) when a company ceases to trade and makes a terminal loss. It is based on section 393A(2B) of ICTA.

20. The entitlement to make a claim remains an entitlement under clause 3. If a loss has already been fully utilised under that clause there is no possibility of relieving that loss again by virtue of the fact that it is a terminal loss within clause 5.

Clause 6: Ring fence trades: extension of periods for which relief may be given

21. This clause extends the length of the period referred to in clause 3(3)(b) when a company makes a loss in a ring fence trade and certain conditions are met. It is based on section 393A(2C) of ICTA.

22. The definition of a “ring fence trade” is to be found in section 162 of CAA 2001. Broadly such a trade is one concerned with oil extraction activities.

23. *Subsection (1)(b)* provides that in the loss-making period the company must have received an allowance under section 164 of CAA 2001. Such an allowance is given in relation to expenditure incurred on abandonment, ie on the decommissioning of oil fields.

Clause 7: Ring fence trades: modification of time for making claim

24. This clause extends the time limit for making claims under clause 3 where the company has carried on a ring fence trade and certain conditions are met. It is based on section 393A(11) and (12) of ICTA.

Q4. In the source legislation the exceptions in clauses 5 to 7 are included as subsections of the main loss relief provision. The approach here is to leave the main clause uncluttered by legislation that is only of limited application. We welcome comments on this approach.

Clause 8: Trade must be commercial or carried on for statutory functions

25. This clause denies relief in relation to losses arising from trades which are not commercial. It is based on section 393A(3) and (4) of ICTA.

26. *Subsection (1)* refers to the making of a profit in the trade. “Profit” in this instance, as the context suggests, has its ordinary commercial meaning rather than “profit” as defined in clause x[j][the clause that rewrites section 6(4) of ICTA].

27. *Subsection (2)* provides for the case where the trade is carried on as part of a larger undertaking. In such a case the larger undertaking (that is, the undertaking as a whole) may be carried on with a view to the realisation of profits even if the trade itself is not.

28. In *subsection (4)* the reference to an Act includes Acts of the Scottish Parliament. See *Change 619* in Annex 1.

Q5. Change 619 reproduces Change 152 in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry Change 152 across to corporation tax.

Clause 9: Restriction on relief in case of farming or market gardening

29. This clause restricts, in certain cases, loss relief in respect of losses arising from a trade of farming or market gardening. It is based on section 397 of ICTA.

30. It is the first of a group of clauses (clauses 9 to 13) which deal with the potential restriction of losses where the losses arise in respect of a trade of farming or

market gardening. It establishes the basic rule. None of these clauses apply to trades other than farming or market gardening.

31. *Subsection (2)* sets out the circumstances in which loss relief is restricted. Broadly this happens once losses have arisen for six successive years.

32. *Subsection (3)* sets out the exceptions to the restriction. Subsection (3)(b) provides that if the trade meets the “reasonable expectation of profit” test then the loss restriction does not apply.

33. Definitions of the terms “farming” and “market gardening” will be included in Bill 6 and such definitions will apply for the purposes of clause 9. The definitions will be in line with those currently to be found in section 832(1) of ICTA but as if those definitions were not restricted to activities in the United Kingdom.

Clause 10: Reasonable expectation of profit

34. This clause sets out the “reasonable expectation of profit” test which, if met, enables relief to be given that would otherwise be restricted under clause 9. It is based on section 397 of ICTA.

35. “Profit” in clause 10 refers to profit in its ordinary commercial sense rather than “profit” as defined in clause x[j][the clause that rewrites section 6(4) of ICTA].

Clause 11: Cessation of trades

36. This clause sets out the circumstances under which a trade is treated as having ceased. This is necessary in order to determine the length of the period during which losses have arisen in that trade for the purposes of clause 9. It is based on section 397(8), (9), and (10) of ICTA.

Clause 12: Rules treating certain persons as the same person

37. This clause sets out the rules for determining whether certain individuals or companies are to be treated as the same person for the purposes of clause 11. It is based on section 397(10) of ICTA.

Clause 13: Companies treated as same person as individual

38. This clause explains how to calculate losses for the purposes of clause 9 where a trade has been transferred from an individual to a company but that individual and that company are treated as the same person by virtue of clause 12. It is based on section 397(10) of ICTA.

39. *Subsection (4)* adapts rules in section 70 of ITA 2007 and section 203 of ITTOIA to deal with cases where profits or losses have not actually been calculated by reference to tax years. In such cases, the calculation of profits or losses for tax years is an arithmetical exercise, involving apportioning (on a time basis) the profits or losses of periods falling partly within the tax year, and combining these with the profits or losses of any periods falling completely within the tax year.

Clause 14: Dealing in commodity futures

40. This clause denies relief where losses have been made in a trade of dealing in commodity futures and certain other conditions are met. It is an anti-avoidance provision. It is based on section 399(2), (3) and (5) of ICTA.

41. *Subsection (4)* defines “arrangements”. The source legislation does not provide a definition but instead denies relief where “a scheme has been effected or arrangements have been made (whether by the partnership agreement or otherwise)”, (see section 399(2)(b) of ICTA). The rewritten clause does not represent a change in substance but a change in presentation.

<p>Q6. We welcome comment on the inclusion of a definition of “arrangements” in this clause.</p>

42. It is intended that, in clauses such as this, the definition of “arrangements” will adopt this same form of words. We will in due course consider whether this definition of “arrangements” could be located at the end of the Bill so that it applies for the purposes of the Bill as a whole. If we adopt this course, then the specific definition of “arrangements” in this clause will be removed.

43. *Subsection (6)* refers to a “recognised futures exchange” as defined in section 288(6) of TCGA 92. The subsection is reproduced here to avoid the need to cross refer to that Act.

(6) In this Act “recognised futures exchange” means the London International Financial Futures Exchange and any other futures exchange which is for the time being designated for the purposes of this Act by order made by the Board.

Clause 15: Carry forward of trade loss against subsequent trade profits

44. This clause provides for trade losses which have not been relieved in accordance with clause 3 to be carried forward and relieved against future trade profits. It is based on section 393 ICTA.

45. The method of giving relief may be contrasted with that for trade losses claimed under clause 3. Losses claimed under clause 3 are deducted from total profits. Losses given under clause 15 are used to reduce profits of the trade prior to their inclusion within “total profits”.

Clause 16: Use of trade-related interest and dividends if insufficient trade profits

46. This clause provides that certain interest and dividends are treated as trade profits if the profits are otherwise insufficient to use some or all of a carry-forward trade loss. It is based on section 393(8) of ICTA.

47. It is only interest and dividends that would otherwise be treated as receipts of the trade that can attract this treatment.

Clause 17: Restriction on relief under sections 3 and 15

48. This clause restricts relief in respect of certain leasing arrangements. It is anti-avoidance legislation. It is based on section 395 of ICTA.

49. Arrangements are defined at *subsection (5)*. The definition is the same as that used in clause 14. In this instance the source legislation does define “arrangements” (see section 395(5) of ICTA). The definition in the clause differs from that in the source legislation but the change is one of presentation rather than of substance.

50. It is intended that, in clauses such as this, the definition of “arrangements” will adopt this same form of words. We will in due course consider whether this definition of “arrangements” could be located at the end of the Bill so that it applies for the purposes of the Bill as a whole. If we adopt this course, then the specific definition of “arrangements” in this clause will be removed.

Chapter 3: Limited Partners and Members of Limited Liability Partnerships

Clause 18: Overview of Chapter etc

51. This clause provides an overview of the Chapter. It is new.

52. The Chapter applies to companies that are either limited partners or member of limited liability partnerships. It limits the amount of relief that may be given under clause 3 (other than against profits of the trade) or in respect of group relief. Carry-forward losses under clause 15 are not affected.

53. Broadly, relief given must not exceed the amount that the company stands to lose commercially.

54. The source legislation expresses the amount that a partner stands to lose commercially by reference to the partner’s contribution to the trade that a partnership carries on (the “contribution to the trade”). But, in such cases, the amount that a partner stands to lose commercially is more likely to be reflected in the partner’s contribution to the partnership that carries on the trade.

55. So this Chapter makes a change by expressing the amount that a partner stands to lose commercially in terms of the partner’s contribution to the partnership (the “contribution to the firm”). The change to “contribution to the firm” requires that the possibility of there being partnerships with more than one trade is addressed. And for consistency with other partnerships, the possibility of a limited liability partnership carrying on more than one trade is also addressed.

56. This change also makes a number of clarifications as to what is included in a partner’s contribution. See *Change 620* in Annex 1.

Q7. *Change 620 reproduces Change 16 in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry Change 16 in ITA 2007 across to corporation tax.*

57. Subsection (2) refers to Part 19 of Bill 5 and provides that references to a firm are to be read in the same way as in that Part. The relevant clause is to be found in Clause [1237[j190301](1)] of that bill. It is reproduced here to avoid the need to cross refer:

In this Act persons carrying on a trade in partnership are referred to collectively as a “firm”.

Clause 19: Restrictions on reliefs for limited partners

58. This clause restricts certain reliefs available to a company that is a limited partner to the amount of the company’s contribution to the firm. It is based on section 118 of ICTA.

59. *Subsection (3)* refers to a “contribution to the firm” whereas the source legislation refers to a “contribution to the trade”. See *Change 620* in Annex 1.

Q8. *Change 620 reproduces Change 16 in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry Change 16 in ITA 2007 across to corporation tax.*

60. *Subsection (6)* sets out how to apply *subsection (4)* and so limit relief if the firm is carrying on more than one trade. See *Change 620* in Annex 1.

Q9. *Change 620 reproduces Change 16 in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry Change 16 in ITA 2007 across to corporation tax.*

Clause 20: Meaning of “contribution to the firm”

61. This clause defines “contribution to the firm” for the purposes of clause 19. It is based on section 118(3) of ICTA.

62. The subsections set out the steps necessary to calculate the “contribution to the firm”. The source legislation refers to a “contribution to the trade”. This change and some points of clarification are covered in the change note. See *Change 620* in Annex 1.

Q10. *Change 620 reproduces Change 16 in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry Change 16 in ITA 2007 across to corporation tax.*

63. *Subsection (5)* explains how amounts that have been drawn out or received back by the company but have been taxed as profits of a trade are to be excluded from the calculation. See *Change 618* in Annex 1.

Q11. *Change 618* reproduces *Change 17* in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry *Change 17* in ITA 2007 across to corporation tax.

Clause 21: Meaning of “limited partner”

64. This clause defines “limited partner” for the purposes of clauses 19 and 20. It is based on section 118(2) of ICTA.

65. A limited partner of a limited partnership registered under the Limited Partnership Act 1907 is someone who is not entitled to take part in the management of the firm’s business and is not liable for the debts or obligations of the firm beyond a certain limit. A limited partner of any other firm is someone who is similarly not entitled to take part in management and not liable for debts or obligations in accordance with the rules applying to the firm in question.

66. *Subsection (4)* is introduced as part of drafting in terms of a company’s “contribution to the firm” in place of “contribution to the trade”. See *Change 620* in Annex 1.

Q12. *Change 620* reproduces *Change 16* in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry *Change 16* in ITA 2007 across to corporation tax.

Clause 22: Restrictions on relief for members of LLPs

67. This clause restricts certain reliefs available to a company that is a member of an LLP to the amount of the company’s contribution to the LLP. It is based on sections 118 and 118ZB of ICTA.

68. *Subsection (6)* sets out how to apply *subsection (4)* and so limit relief if the firm is carrying on more than one trade. See *Change 620* in Annex 1.

Q13. *Change 620* reproduces *Change 16* in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry *Change 16* in ITA 2007 across to corporation tax.

Clause 23: Meaning of “contribution to the LLP”

69. This clause defines “contribution to the LLP” for the purposes of clause 22. It is based on sections 118ZB and 118ZC of ICTA.

70. An LLP formed under the Limited Liability Partnership Act 2000 is an entity with separate legal personality. That Act defines what is meant by contribution to a limited liability partnership.

71. *Subsection (3)* makes explicit the fact that capitalised undrawn profits are to be included in a company's contribution. See *Change 620* in Annex 1.

Q14. *Change 620* reproduces *Change 16* in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry *Change 16* in ITA 2007 across to corporation tax.

72. *Subsection (6)* explains how amounts that have been drawn out or received back by the company but have been taxed as profits of a trade are to be excluded from the calculation. See *Change 618* in Annex 1.

Q15. *Change 618* reproduces *Change 17* in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry *Change 17* in ITA 2007 across to corporation tax.

Clause 24: Unrelieved losses brought forward

73. This clause provides that relief may be given in a later accounting period for losses restricted in accordance with clause 22, if certain conditions are met. It is based on section 118ZD of ICTA.

Chapter 4: Property Business Losses

Overview

74. This Chapter deals with property business losses both from UK property businesses and from overseas property businesses.

Clause 25: Relief for losses made in UK property business

75. This clause provides relief for losses arising from a UK property business. It is based on section 392A of ICTA.

76. "UK property business" is defined in clause x[j] of this Bill. [The current definition is to be found in section 832(1) of ICTA which in turn relies on the definition at Chapter 2 of Part 3 of ITTOIA 2005.] This definition is reproduced here in order to avoid the need to cross refer:

A person's UK property business consists of—

(a) every business which the person carries on for generating income from land in the United Kingdom, and

(b) every transaction which the person enters into for that purpose otherwise than in the course of such a business.

77. *Subsection (3)* refers to the loss being deducted in calculating the company's net profits. In other words the loss will be one of those deducted from the company's "total profits".

78. *Subsections (4) and (5)* provide that any unused losses are to be carried forward and treated as UK property business losses of later periods. In other words such unused losses may be set against "total profits" of later periods.

79. *Subsection (4)* uses the word "can" and *subsection (5)* uses the word "cannot". The use of "can" and "cannot" accords with the current wording of the clause that sets out the corporation tax calculation. If at any stage the wording of this clause changes then it will be necessary to consider the effect on these subsections.

Clause 26: Company with investment business ceasing to carry on UK property business

80. This clause provides a relaxation of the loss carry-forward rules where a company ceases to carry on a UK property business but continues to carry on an investment business. It is based on section 392A(3) and (4) of ICTA.

81. A company with investment business is defined in clause x[j] of this Bill. [The current definition is to be found in section 130 of ICTA.] This definition is reproduced here to avoid the need to cross refer:

["company with investment business" means any company whose business consists wholly or partly in the making of investments;]

Clause 27: UK property business to be commercial or carried on for statutory functions

82. This clause provides that clauses 25 and 26 only apply when a UK property business is carried on on a commercial basis or in the exercise of functions conferred by an Act. It is based on section 392A(5), (6) and (7) of ICTA.

83. The reference to an Act in *subsection (1)* includes an Act of the Scottish Parliament. See *Change 619* in Annex 1.

Q16. *Change 619* reproduces *Change 152* in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry *Change 152* in ITA 2007 across to corporation tax.

84. The reference to "profit" in *subsection (2)* refers to profit in its ordinary commercial sense rather than "profit" as defined in clause x[j][the clause that rewrites section 6(4) of ICTA].

Clause 28: UK furnished holiday lettings business treated as trade

85. This clause provides that a UK furnished holiday lettings (UKFHL) business is treated as a trade for loss relief purposes. It is based on section 503 of ICTA.

86. *Subsection (6)* is intended to clarify that where a company carries on a number of different UKFHL businesses in different capacities each business is to be considered separately when applying the rules of the clauses. For example a company may carry on one UKFHL business on its own behalf and another UKFHL business as member of a partnership.

Clause 29: Relief for losses made in overseas property business

87. This clause sets out the rules for relieving losses made in an overseas property business. It is based on section 392B of ICTA.

88. “Overseas property business” is defined in clause x[j] of this Bill. [The current definition is to be found in section 832(1) of ICTA which in turn relies on the definition in section 70A(4) of ICTA.] This definition is reproduced in order to avoid the need to cross refer:

[(4) All businesses and transactions carried on or entered into by a particular company or partnership, so far as they are businesses or transactions the income from which is chargeable to tax under Case V of Schedule D in accordance with this section, are treated for the purposes of the charge to tax under Case V as, or as entered into in the course of carrying on, a single business (an “overseas property business”).]

89. *Subsection (3)* provides that a loss from an overseas property business may be carried forward and set against future profits of that business. Such profits do not include chargeable gains.

Clause 30: Overseas property business to be commercial or carried on for statutory functions

90. This clause provides that clause 29 only applies when an overseas property business is carried on on a commercial basis or in the exercise of functions conferred by an Act. It is based on section 392A(5), (6) and (7) of ICTA and section 392B(2) of ICTA.

91. The reference to an Act in *subsection (1)* includes an Act of the Scottish Parliament. See *Change 619* in Annex 1.

Q17. Change 619 reproduces Change 152 in ITA 2007 and so brings the income and corporation tax codes back into line. We welcome comments on the proposal to carry Change 152 in ITA 2007 across to corporation tax.

92. *Subsection (1)* also refers to functions conferred by the law of a territory outside the United Kingdom. See *Change 621* in Annex 1.

Q18. We propose to extend the scope of the section in the source legislation to include legislation of a territory outside the United Kingdom. We welcome comments on this proposed rewrite change.

93. The reference to “profit” in *subsection (2)* refers to profit in its ordinary commercial sense rather than “profit” as defined in clause x[j][the clause that rewrites section 6(4) of ICTA].

Chapter 5: Losses from Miscellaneous Transactions

Overview

94. This Chapter deals with loss relief in respect of miscellaneous transactions.

Clause 31: Relief for losses from miscellaneous transactions

95. This clause provides relief for losses arising from transactions that, had they resulted in gains, would have been treated as miscellaneous income. It is based on section 396 of ICTA.

96. *Subsections (4), (5) and (6)* ensure that such losses may only be relieved against miscellaneous income.

Chapter 6: Write-Off of Government Investment

Overview

97. This Chapter restricts losses where there has been a write-off of an amount of government investment in a company.

Clause 32: Loss relief to be reduced in case of write-off of government investment

98. This clause provides that if an amount of government investment in a company is written off that company’s carry-forward losses are restricted by the amount written off. It is based on section 400 of ICTA.

Clause 33: Groups of companies

99. This clause sets out the further rules that apply if clause 32 applies and the company is a member of a group of companies. It is based on section 400(5) and (10) of ICTA.

100. In these circumstances *subsection (2)* provides that the restriction may be to the carry forward losses of any of the group companies provided that the restriction is on a just and reasonable basis. For example, if the government investment had been in a holding company and that company had lent the money to a subsidiary then it would be appropriate to restrict the carry-forward losses of the subsidiary.

Clause 34: Cases in which government investment is written off

101. This clause sets out the three circumstances which constitute a write-off of government investment. It is based on section 400(7) to (10) of ICTA.

Clause 35: Meaning of “carry-forward losses”

102. This clause defines the five types of “carry-forward losses”. It is based on section 400(2) to (4) of ICTA.

103. *Subsection (2)* provides that certain amounts are not to be included in the calculation of “carry-forward losses”. The effect of this is to limit the reduction of loss relief provided for by clause 32.

104. *Subsection (4)* sets out the order in which losses are to be set off against the various “carry-forward losses” set out at subsection (1).

Clause 36: Interaction with other tax provisions

105. This clause ensures that a company is not prevented from deducting an amount in calculating its profits of a trade simply because an amount of government investment in the company has been written off. It is based on section 400(6) and (9A) of ICTA.

ANNEX 1: MINOR CHANGES IN THE LAW MADE BY THE BILL

Change 601: References to “officer of Revenue and Customs”: clause 3

This change replaces references to the “Board of Inland Revenue” in the source legislation with references to “an officer of Revenue and Customs”.

It brings the income and corporation tax codes into line.

References in the source legislation to the “Board of Inland Revenue” are treated by section 50(1) of the Commissioners for Revenue and Customs Act 2005 (CRCA) as references to “the Commissioners for Her Majesty’s Revenue and Customs”. The rest of this note accordingly refers to the Commissioners for Her Majesty’s Revenue and Customs (“the Commissioners”) rather than to the Board of Inland Revenue.

The provisions affected by this change will in future authorise or require things to be done by or in relation to an officer of Revenue and Customs rather than by or in relation to the Commissioners. This reflects the way in which Her Majesty’s Revenue and Customs is organised and operates in practice. Section 13 of CRCA allows nearly all functions conferred on the Commissioners to be exercised by any officer. All of the functions affected by this change, which are in the main concerned with administrative processes, are in fact exercised by officers of the Commissioners, and the Commissioners themselves are not personally involved in their exercise.

Each provision affected by the conversion of references to the Commissioners will be identified in the Table of Origins by a cross-reference to this change.

This change has no implications for the amount of tax due, who pays it or when. It affects (in principle and in practice) only administrative matters.

Change 619: Reference to an Act to include an Act of the Scottish Parliament: clauses 8, 27 and 30

This change expands the definition of Act to include an Act of the Scottish Parliament.

“Act” on its own does not include Acts of the Scottish Parliament (see the definition of “Act” in Schedule 1 to the Interpretation Act of 1978) and the definition of “Act” in clause x[j] [equivalent of section 990 of the Income Tax Act 07] does not extend its meaning to include Acts of the Scottish Parliament.

But it is appropriate that references to “Act” in clauses 8, 27 and 30 should include references to Acts of the Scottish Parliament. In each of these cases the extension of the meaning of “Act” can only be advantageous to taxpayers. A similar provision is contained in section 879 of ITTOIA.

This change is in taxpayers' favour in principle and may benefit some in practice. But the numbers affected and the amounts involved are likely to be small.

Change 620: Trading losses: restrictions: contribution to the firm in place of contribution to the trade: clauses 19, 20, 21, 22 and 23

This change provides for certain restrictions on the use of trade losses, incurred by companies acting as limited partners or as members of limited liability partnerships, to operate by reference to the company's contribution to the firm (rather than its contribution to the trade, as in the source legislation). It also deals with a number of consequential matters and clarifies a number of points about what is included in a company's contribution.

Contribution to the firm

For companies that are members of limited liability partnerships (LLPs), the source legislation restricts loss relief against total profits by reference to a company's *contribution to the limited liability partnership* (see section 118ZC(2) and (3) of ICTA).

By contrast, for companies that are limited partners (that are not also members of LLPs), the source legislation restricts loss relief against total profits by reference to the company's *contribution to the trade* (see section 118(2) and (3) of ICTA).

But partnership law is more likely to look at capital contributed to the partnership (referred to in the relevant clauses of the Bill as the firm), rather than to capital contributed to a trade that the partnership carries on. For instance, a company might become a limited partner in a partnership formed under the Limited Partnerships Act 1907 (LPA). Under section 4(2) of LPA the company, at the time of entering into the partnership, contributes a sum or sums as capital (or property valued at a stated amount). LPA does not prevent further amounts being contributed at a later date. But the intention of LPA is that the contribution is to the firm, not the trade. The firm uses the capital contributed to fund its various activities – its trade or trades and any investments etc that the firm might hold. And the company has limited liability for the debts and obligations of the firm, rather than just for the debts and obligations of any trade that the firm happens to carry on.

The Bill reflects this by providing that total profit or group relief restrictions on trade losses operate in relation to a company's "contribution to the firm" rather than "contribution to the trade". This is, in principle, taxpayer-favourable as it may allow total profit relief or group relief to be obtained by reference to a larger amount than would otherwise be the case.

Firm carries on more than one trade

Some consequential changes have been made to cater for the possibility that a firm might carry on more than one trade.

If a firm carries on only one trade, the restriction of total profit or group relief for trade losses by reference to the contribution to the firm means that the company can get such relief for losses up to the amount at risk, and no more. But if the firm carries on more than one trade, restricting total profit or group relief for trade losses in each trade by reference to the contribution to the firm might result in the company getting such relief for more than the amount at risk. Clearly the source legislation does not allow this in the case of limited partners (who are not also members of LLPs) as it restricts relief for trade losses against total profits by reference to the amount of capital contributed to each trade.

So in the case of limited partners (who are not also members of LLPs) the Bill restricts the total profit relief available in respect of losses from all trades carried on by the firm to the amount that the company has at risk.

As noted earlier, for LLPs a member's contribution is already in terms of the contribution to the LLP. But the source legislation does not explicitly deal with the possibility that an LLP might carry on more than one trade. Therefore to ensure that a consistent policy is applied throughout the clauses (i.e. the relief available is restricted to the amount at risk), the restriction mentioned in the preceding paragraph has been explicitly applied in relation to members of LLPs as well. This is in principle taxpayer-adverse in the case of members of LLPs.

Contribution to an LLP

The source legislation provides that the contribution to an LLP is the greater of the amount which the company has contributed to it as capital (so far as it is not recoverable) and the amount of the company's liability on a winding up (see section 118ZC(2) of ICTA).

But the total amount the company has at risk in an LLP is, in principle, the sum of what has been contributed as capital to the LLP and the additional amount that the company could be called on to meet in a winding up of the LLP.

The Bill provides that a company's contribution to an LLP takes account of the total amount at risk, namely any amounts contributed as capital to the LLP and any further amounts for which the company is liable on a winding up. See clause 23(7).

Profits or losses in accordance with generally accepted accounting practice

The Bill provides explicitly, where source legislation does not, instances where a reference to profits or losses means amounts calculated in accordance with generally accepted accounting practice. See clauses 20(9) and 23(4).

Capitalised profits

The Bill also explicitly provides that capitalised undrawn profits are included in an individual's contribution. See clauses 20(3), and 23(3).

Contributions to a firm — trading profits not drawn

The Bill also provides that a company's share of trading profits, taken into account in determining the company's contribution to the firm, is calculated by looking at periods where such profits were made, and ignoring trading losses in other periods. The source legislation does not contain an equivalent provision. The effect is broadly to determine a company's share of undrawn trading profits as the amount that the company would have received if such profits had been distributed fully on a period by period basis. See clause 20(8).

This change is adverse to some taxpayers and favourable to others in principle and in practice. But the numbers affected and the amounts involved are likely to be small.

Change 618: Trading losses: restrictions: withdrawal of capital ignored where amounts charged to tax as profits of a trade: clauses 20 and 23

This change amends the way in which the trading losses of limited partners or members of limited liability partnerships are restricted.

One of the elements in the restriction of such a trading loss is the net amount contributed (the full amount contributed less any capital withdrawn) by the limited partner or the member of the limited liability partnership to the firm. However, it is possible that amounts of capital withdrawn may be regarded for tax purposes as profits. In these circumstances it is inequitable to restrict loss relief by reference to those amounts. This change corrects this potential inequity.

This change is in taxpayers' favour in principle and may benefit some in practice. But the numbers affected and the amounts involved are likely to be small.

Change 621: Trading losses: restrictions: restrictions not to apply where an overseas property business carried on in the exercise of functions conferred by or under the law of a territory outside the UK: clause 30

This change brings the position of an overseas property business that is carried on in the exercise of functions conferred by or under the law of a territory outside the United Kingdom in line with the treatment of an overseas property business that is carried on in the exercise of functions conferred by or under an Act of Parliament (including an Act of the Scottish Parliament).

If an overseas property business is not carried on on a commercial basis then relief for losses can only be obtained if the business is carried on in the exercise of functions conferred by or under specific legislation. In these limited circumstances it is considered inequitable that relief may only be obtained if the legislation in question is UK legislation. The change extends the scope of the relief to functions conferred by or under the law of a territory outside the United Kingdom.

*Corporation tax: Bill 6
Loss Relief
November 2007: Committee paper CC/SC (07) 38*

***This change is in taxpayers' favour in principle and may benefit some in practice.
But the numbers affected and the amounts involved are likely to be small.***