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# Corporate loss restriction

## 1. Background

The original corporate loss restriction (CLR or CILR) was introduced as part of a package of corporate loss relief measures with effect from 1 April 2017. The other measures generally increased the flexibility with which carried-forward losses can be used. In contrast, the CILR may, in certain circumstances, reduce the amount of carried-forward losses that can be relieved in later periods.

Under the CLR, all stand-alone companies and groups can claim a deductions allowance of £5m, and all carried–forward losses are deductible in later periods up to the full value of that deductions allowance. For profits above the £5m allowance however, only 50% may be relieved by carried-forward losses. This, in a nutshell, is the essence of the CLR.

For a stand-alone company therefore, with current period trading profits of £20m and £20m of trading losses carried-forward from earlier periods, the maximum permissible deduction for the carried-forward losses is £12.5m, i.e. the company's deductions allowance of £5m plus 50% of the company's profits above the deductions allowance.

Capital losses were originally outside the scope of the CLR but it is now proposed (subject to enactment of Finance Bill 2019-20) that they will be brought within scope from 1 April 2020.The case study in the eCPD module illustrates how the CLR calculations will look once capital losses have been brought in-scope.

## 2. Case study assumptions

For simplicity, the case study considers a stand-alone company that has:

(1) a current period trading profit of £60m and brought forward trading losses of £60m;
(2) a current period loan relationship non-trading credit of £50m and a brought forward loan relationship non-trading deficit of £50m; and
(3) current period chargeable gains of £40m and brought forward capital losses of £40m.

It is assumed that the CLR has been extended to capital losses in line with the proposals in Finance Bill 2019-20.

The brought-forward trading losses are pre-1 April 2017 trading losses. This means they can only be relieved against **trading profits** of future periods. Likewise, the brought-forward loan relationship deficit is also pre-1 April 2017 so this can only be relieved against **non-trading profits** of future periods. Finally, the capital losses can only be relieved against chargeable gains of later periods regardless of when the losses arose.

We have also assumed that the company has current year losses of £50m capable of being relieved against total profits. In the circumstances of this case study, these losses could not be trading losses because the company has made a current period trading profit. They could however be an intangible fixed asset non-trading loss of the current period without being inconsistent with other assumptions.

Slide 6 illustrates how the computation of the company's total profits would look in the absence of the CLR. Total profits are exactly zero because:

- the trading profits of £60m would be relieved by the £60m brought-forward pre-1 April 2017 trading loss;
- the non-trading credit of £50m would be relieved by the brought-forward pre-1 April 2017 loan relationship non-trading deficit of £50m; and
- the chargeable gain of £40m would be relieved by the carried-forward capital loss of £40m.

This means all carried-forward losses would be fully used in the current period and the current period losses would be unrelieved in the current period and hence available to carry-forward in their entirety.

## 3. The CLR calculations

The starting point is the calculation of "modified total profits". This modification is required because we need a consistent and comprehensive measure of profits which takes account of all sources of profit for the year.

The total profits figure calculated on slide 6 has already been reduced by loss reliefs deductible **before** arriving at total profits. Consequently, the "total profit" measure understates the true amount of profits that should be subject to the CLR. We therefore need to add back to total profits the £60m of brought-forward trading losses already deducted in arriving at that amount. Likewise, we also need to add back the £50m of brought forward non-trading deficit and the £40m of capital losses because these too are deducted before arriving at total profits.

Slide 7 illustrates that modified total profits in the case study amount to £150m in total made up of trading, non-trading and chargeable gains amounts of £60m, £50m and £40m respectively.

## 4. Calculate qualifying profits

In the same way that "total profits" may understate the correct amount of profits subject to the CLR, the "modified total profits" measure outlined on the last slide can overstate the true amount. This is because most current year loss reliefs are deducted **after** "total profits" and not **before**. "Modified total profits" therefore need to be reduced for any current year losses deductible after total profits. In legislative terms this is achieved by deducting the "Step 2 amount" from modified total profits to arrive at the various "qualifying profits" (see slide 8).

The "Step 2 amount" includes a current year:

- trading loss deductible from total profits;
- intangible fixed asset non-trading loss;
- post-1 April 2017 loan relationship non-trading deficit;
- management expenses; and
- group relief claimed.

The Step 2 amount can be allocated to different income streams at the company's discretion. In the case study, it has been allocated entirely to trading income.

## 5. Calculate relevant profits

In slide 9, the deductions allowance is deducted from qualifying profits to arrive at total “relevant profits” of £95m. This too can be allocated at the company’s discretion to one or more of the different income streams making up qualifying profits. In slide 9, it has been allocated entirely to the chargeable gains income stream to give a “relevant chargeable gain” of £35m.

## 6. The separate CLR restrictions

There are four main CTA 2010 provisions which impose the CLR as follows:

(1) section 269ZB which applies to carried-forward losses that can only be relieved against trading profits of later periods, i.e. pre-1 April 2017 trading losses, or a post-1 April 2017 trading loss that fails the qualifying conditions for relief against total profits;
(2) section 269ZBA which, from 1 April 2020 subject to enactment, will impose the capital loss restriction proposed in Finance Bill 2019-20;
(3) section 269ZC which restricts relief for pre-1 April loan relationship non-trading deficits which can only be relieved against non-trading profits of later periods; and
(4) section 269ZD which applies to a number of different loss-types (“relevant deductions”), the key feature in common is that they are deductible against a company’s total profits.

## 7. Order of restrictions

To determine the order in which the four CLR restrictions must be calculated, we need to understand the order in which “unrestricted losses” must be deducted. “Unrestricted losses” in this context means losses potentially within the scope of any of the four CLR restrictions but which in practice fall to be included in the allowable amount.

For non-trading losses, i.e. those within section 269ZC, we need to consider both loan relationship non-trading deficits and capital losses. Of the two, the legislation requires that unrestricted capital losses must be deducted first and that any unrestricted loan relationship non-trading losses can only be deducted after the capital losses have been relieved. So, if capital losses account for the whole of a company’s allowable losses under the CILR, this means that no deduction will be permitted for any brought forward loan relationship non-trading deficit.

In a similar manner, losses allowable against total profits, i.e. those within the scope of section 269ZD, can only be deducted after first deducting any unrestricted losses allowable under any of the other three restrictions. In practice his means that the chargeable gains allowable amount must be calculated before the non-trading income allowable amount. Then, the allowable amount for trading losses relievable against trading income and the allowable amount for loan relationship non-trading deficits must also be calculated before the final allowable amount for relevant deductions can be determined. Slide 11 illustrates this inter-relationship.

## 8. Restriction for pre-1 April 2017 trading losses

To recap, these are pre-1 April 2017 trading losses, or post-1 April 2017 trading losses that do not meet the conditions for relief against total profits. Post-1 April 2017 trading losses that do satisfy the conditions for relief against "total profits" fall within the section 269ZD restriction for "relevant deductions".

The starting point is 50% of "relevant trading profits". To this we add the "trading profits deductions allowance" to arrive at the relevant maximum, i.e. the maximum amount of losses of this type that can be relieved against trading profits.

Remember that the overall deductions allowance of £5m can be allocated at the company's discretion to each of the individual income streams. In the case study, 50% of relevant trading profits is £5m. The trading profits deductions allowance has been set at zero, therefore the relevant maximum is also £5m.

In total, there are £60m of brought forward trading losses available for relief against trading profits. This means that the maximum permissible deduction is not restricted by the size of the available carried-forward losses and is therefore £5m.

## 9. Restriction for capital losses

The calculation of the capital loss restriction is similar. The starting point is 50% of "relevant chargeable gains" to which we add the "chargeable gains deductions allowance". The resulting amount (another "relevant maximum") is the maximum amount of capital losses that can be relieved against chargeable gains.

In the case study, 50% of relevant chargeable gains is £17.5m. The chargeable gains deductions allowance has already been set by the company at £5.0m, therefore the relevant maximum is £22.5m. Although there are £40m of capital losses brought forward for relief only against chargeable gains, the maximum permissible deduction can only be £22.5m.

## 10. Restriction for pre-1 April 2019 LRNTDs

The calculation of the maximum permissible deduction for loan relationship non-trading debits deductible only against non-trading income proceeds in a similar manner but first it is necessary to aggregate chargeable gains and non-trading income profits. Likewise, it is necessary to aggregate the chargeable gains deductions allowance and the non-trading income profits deductions allowance. This aggregation process allows loan relationship deficits to be relieved against chargeable gains and capital losses to be relieved against non-trading loan relationship deficits where circumstances allow.

Slide 14 illustrates the calculations. The total non-trading profits deductions allowance of £5m is deducted from qualifying non-trading profits (both income and gains) to give total relevant non-trading profits of £85m. The relevant maximum here is £47.5m being 50% of that amount plus the non-trading profits deductions allowance of £5m.

For this restriction, actual relief given for capital losses within, but not actually restricted by, the capital loss restriction - £22.5m in this example - must first be deducted from the relevant maximum to determine the maximum permissible relief for non-trading income profits of £25m. This is not limited by the size of the £50m available brought forward losses, so the actual relief claimed for pre-1 April 2017 LRNTDs brought forward is £25.0m.

## 11. Restriction for relevant deductions

The final stage of the CLR calculations is to work out the maximum permissible relief for "relevant deductions" i.e. relief for brought forward losses deductible from a company's total profits.

Total relevant profits across all types of income and gains are £95m. 50% of this is £47.5m to which we add the total deductions allowance of £5m giving a relevant maximum of £52.5m. From this we must deduct actual reliefs claimed in relation to unrestricted losses falling within the scope of all the previous CILR restrictions.

So, as slide 15 illustrates, we need to deduct:

- the actual £5m relief claimed for pre-1 April 2017 trading losses within the scope of the section 269ZB restriction;
- the actual £22.5m relief claimed for capital losses within the scope of the section 269ZBA restriction; and
- the actual £25.0m relief claimed for loan relationship non-trading deficits within the section 269ZC restriction.

This amount is zero, so no relief could have been claimed for any relevant deductions had there been any. Slide 16 summarises the final taxable profits position across all income streams. By way of comparison, and in the absence of the CLR, all £150m of carried-forward losses would have been fully relieved in the current period and all of the £50m current period losses would have been carried-forward to later periods.

## 12. Basic tax planning

The key to any tax planning associated with the CLR is three-fold:

First, to identify any loss-types the company would like to use in priority to other losses e.g. our company may not expect to generate any future chargeable gains so its priority may be to relieve brought forward capital losses in priority to other losses.

Second, to understand the elements of discretion permitted under the CLR calculations. These are:

(1) the allocation and deduction of the Step 2 amount to "modified total profits" in slide 8;
(2) the allocation of the company's deductions allowance between the trading, non-trading income; and chargeable gains deductions allowances; and
(3) the sharing of the deductions allowance with other group members.

Finally, consider the requirement to claim or the ability to disclaim loss reliefs as appropriate. The available combinations of claims and disclaimers may, depending on the circumstances, allow companies further scope to alter the manner in which the CLR will apply to its own unique set of facts.

## 13. Further reading

Detailed guidance

https://library.croneri.co.uk/cch_uk/btr/730-850

Legislation

https://library.croneri.co.uk/cch_uk/btl/cta2010-it-pt-7za

HMRC guidance

https://library.croneri.co.uk/cch_uk/irm/ctm-ctm05000