Corporation Tax – "Targeted Loss Buying" - Rules, Draft Legislation, Explanatory Notes and Tax Information and Impact Note (TIIN)

Technical Notes
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Foreword

On 20 March 2013 the Chancellor of the Exchequer announced that the Government proposed to introduce legislation in the Finance Bill 2013, having effect from that date, to prevent companies entering arrangements to access, as part of a business transfer, various forms of unrealised corporation tax losses from unconnected third parties.

This document provides technical detail on the circumstances and manner in which the proposed legislation will operate. It was initially released on Budget Day 20 March 2013 , but has now been reissued to include the draft legislation, explanatory notes and the Tax Information and Impact Note (TIIN).

The draft legislation is now published for a short period of technical consultation which will close on 2 May 2013. Please direct any comment to the contact names below.

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Chapter 1: Introduction

1. The UK's loss relief system provides a measure of parity between taxing profits and relieving losses over the life cycle of a business, ensuring that businesses with different patterns of profit and loss pay a broadly similar amount of tax. Relief is based on the following underlying principles:

- Brought forward trade losses should only be relievable against future profits from the same trade, carried on by the same legal entity;
- Tax losses should not be transferable against profits of unconnected parties;
- The movement of losses between companies should only be allowed where they are under common economic ownership for the accounting period when the losses arise.

2. Within those principles companies can gain relief for losses through set off against profits in a number of ways but loss relief and business re-organisation rules are designed to prevent companies passing the benefit of a loss to a third party. These tax rules are designed to prevent companies 'selling' losses to some unconnected company that has taxable profits. HMRC has seen a marked increase in companies entering into arrangements to circumvent these rules.

3. A particular pressure point arises where it is possible to dictate or predict the amount and timing of reliefs, allowances and deductions. Where these are sizeable, they can encourage tax motivated reorganisations through which unconnected entities may get access to what are, in effect, unrealised losses.

4. Where amount and timing can be dictated or predicted, ownership or part ownership changes can take place in advance of the crystallisation of the amount enabling the current "loss buying" rules in Part 14 of Corporation Tax Act 2010 (CTA 2010) to be by-passed.

5. Such arrangements may take the form of selling all or some of the shares in a company or the assets of a company, where either there are allowances that could have been claimed but weren't by the previous owner or where it is known that a debit will be created in a future accounting period. Arrangements can, however, be more complex and contrived and may also involve moving profits into a company to use up relevant deductions.

6. The Government therefore proposes to bring the tax treatment of unrealised amounts, involved in a transfer between unconnected parties, more closely into line with the longstanding treatment of realised losses.

7. The proposed changes will introduce three separate rules to combat 'loss buying'.

8. The first rule expands the application of Chapter 16A of Part 2 of the Capital Allowances Act 2001 (CAA 2001). The other two rules are targeted anti-avoidance rules (TAARs) to be included in a new Part in CTA 2010: one to counter tax motivated reorganisations between unconnected parties involving other forms of relevant deductions; the other to counter arrangements that aim to transfer profits to companies so that the relevant deductions can be used. .

9. The legislation will be effective as from 20th March 2013 and published for technical consultation on 28th March. Legislation will then subsequently be included in Finance Bill 2013.

Chapter 2: Capital Allowances

Application of Chapter 16A of Part 2 CAA2001

10. Chapter 16A of Part 2 CAA 2001 was introduced in Finance Act 2010 in order to prevent tax-motivated capital allowance buying.

11. Chapter 16A applies where there is a company C and:
- the tax written down value (TWDV) of the company's plant or machinery assets exceeds the balance sheet value (BSV) of those assets (this excess being relevant excess of allowances);
- there is a "qualifying change of ownership" in relation to C; and
- the qualifying change has an "unallowable purpose".

12. Where these conditions apply the Chapter restricts the ways in which a plant and machinery allowance may be given effect. This is done by:
- bringing the accounting period of C to a close at the end of that day;
- reducing the capital allowances pool(s) at the start of the new accounting period (that begins on the following day) to the amount of the BSV; and
- treating the relevant excess of allowances as expenditure on plant or machinery. This expenditure is allocated to a new capital allowances pool. The capital allowances generated by this new pool may only be used to reduce the same profits that they could have reduced had the qualifying change not taken place.

13. Chapter 16A is aimed at cases where a company in a group makes losses, such that it decides not to claim all the allowances to which it was entitled. Arrangements are much later entered into for a main purpose of allowing another person to access those allowances. Typically this is done as part of transaction under which:
- the company is sold by the group;
- the later sale means that it forms part of a new group; and
- the company, as member of the new group, then claims the allowances in order to create or increase a loss which is then available for surrender by way of group relief.

Extension of Chapter 16A CAA 2001

14. In certain cases, companies may be sold in circumstances where although accessing excess capital allowances was not a main purpose of the arrangements (i.e. the "unallowable purpose" provision does not apply), the entitlement to claim such allowances was clearly a significant benefit. Such arrangements have the effect of converting deferred tax assets into a valuable asset in the new group. Permitting the new group to access the allowances in these circumstances is inconsistent with other tax rules that are designed to prevent companies 'selling' losses to an

unconnected company that has taxable profits.[1] In addition, Chapter 16A currently applies only to trades and so does not cover the full range of circumstances in which capital allowance buying may occur.

15. Accordingly, Chapter 16A will be extended so that it applies:
    - to allowances taken into account in calculating profits of any of the qualifying activities listed in section 15 CAA 2001 (and not just those taken into account in calculating trading profits, as is currently the case); and

    where:
    - the amount of the relevant excess of allowances is £50 million or more (whether or not the qualifying change has an unallowable purpose); or
    - the amount of the relevant excess of allowance is £2 million or more but less than £50 million and is not an insignificant benefit (whether or not the qualifying change has an unallowable purpose); or
    - the amount is less than £2 million and the qualifying change has an unallowable purpose.

16. The insignificant benefit condition ensures that Chapter 16A will not apply where the amount of the relevant excess allowances is insignificant in the context of the total amount or value of the benefits derived by a party (either the acquiring company or acquiring group) to the change arrangements or any other arrangements of which they form part.

17. The meaning of "insignificant" will be covered in more detail within the Technical Consultation Document to be published on 28th March. In a normal case HMRC would consider that 5% would be insignificant but there may be special considerations where a different figure would be appropriate.

18. For clarity, where the amount of the relevant excess of allowances is £50million or above it is never insignificant – and so the "insignificant benefit" condition does not apply to such excesses.

19. There will be an "anti-fragmentation" rule applied to the thresholds which apply at the £2million and £50million level (in respect of the relevant excess of allowances). The rule will disapply arrangements designed to ensure that the either of the two threshold tests are passed. This will counter attempts to structure transactions with the purpose of passing the threshold tests (and move out of the scope of the expanded Chapter 16A.

Consequences of Chapter applying

20. Where new expanded Chapter 16A applies the consequences will be exactly the same as currently (amended to reflect the expanded scope of Chapter 16A to cover all qualifying activities in section 15 of CAA 2001). Essentially the excess of

[1] For example, the rules in section 45 CTA 2010 that allow the carry forward of trade losses while carried on by the same company, subject to the rules in Part 22 CTA 2010 (transfers of trade without a change of ownership).

allowances is treated as qualifying expenditure in a new pool. The way in which relief for allowances in respect of expenditure in new pools, or losses attributable to such allowances, can be claimed is then restricted.

Chapter 3: "Deduction Transfer TAAR"

"Deduction Transfer TAAR"

21. A new Part will be added to CTA 2010 to introduce a "Deduction Transfer TAAR" that operates by way of a purposive test.

22. This TAAR will apply where there has been a "qualifying change" in relation to a company C. It seeks to deny claims for group relief and relief for trade losses against total profits in accounting periods ending on or after the date of the qualifying change in respect of certain types of deductible amounts. Those amounts are ones which, at the date of the qualifying change, can be regarded as highly likely to arise as deductions for an accounting period ending on or after that date.

23. This TAAR only applies where the purpose or one of the main purposes of arrangements connected to the qualifying change is to claim relief for such deductions.

Qualifying change

24. A "qualifying change" for the purposes of the Deduction Transfer TAAR has the same meaning as the definition of "qualifying change" in Chapter 16A of Part 2 of CAA 2001.

Deductible amounts

25. The relevant deductible amounts which are disallowed where the Deduction Transfer TAAR applies are:

- an expense of a trade
- an expense of a property business
- an expense of management of a company's investment business within the meaning of section 1219 of CTA 2009
- a non-trading debit within the meaning of Parts 5 and 6 of CTA 2009 (loan relationships and derivative contracts); and
- a non-trading debit within the meaning of Part 8 of CTA 2009 (intangible fixed assets).

26. Amounts that have been taken into account in determining "relevant tax written down value" under Chapter 16A of Part 2 of CAA 2001 are not within the scope of this TAAR.

Circumstances in which "deductible amounts" will be disallowed

27. If two conditions apply, a "deductible amount" is disallowed from certain claims for an accounting period ending on or after the date of the qualifying change. The

relevant claims are claims by C, or a company connected to C, for group relief (under Chapter 4 of Part 5 CTA 2010) or relief for trade losses against total profits (under section 37 CTA 2010).

28. The first condition is that at the date of the qualifying change it is highly likely that the deductible amount would be capable of being the subject of, or a deduction in a relevant group relief claim or claim under section 37. Factors to take into account in determining the "highly likely" test include arrangements made on or before the day of the qualifying change, any events on or before that day and the certainty with which the size of the amount can be predicted on that day.

29. The second condition is that the main purpose or one of the main purposes, of arrangements connected with the qualifying change is to bring the deductible amount into account in such a relevant claim or to be the subject of such a relevant claim.

30. The Deduction Transfer TAAR would not affect any claims, for example, for relief for carried forward of a trading loss against subsequent trade profits (under section 45 CTA 2010). It means that the benefit of the deductible amount may still be realised in a manner consistent with the purpose of the losses rules.

Chapter 4: “Profit Transfer TAAR”

“Profit Transfer” TAAR

31. The new Part to be added to CTA 2010, referred to in the previous Chapter, also introduces a Profit Transfer TAAR.

32. This TAAR will apply where there has been a “qualifying change” in relation to a company C. It tackles the transfer of profits to C (or a company connected to C) where the purpose, or one of the main purposes, of the transfer is to utilise deductible amounts.

33. The TAAR denies relief for deductible amounts claimed in any accounting period ending on or after the qualifying change. In this respect the “Profit Transfer TAAR” differs from the “Deduction Transfer TAAR” which merely restricts relief.

34. The TAAR applies where the purpose or one of the main purposes of the profit transfer arrangements (i.e. arrangements which result in profits being transferred to C or a company connected with C) is to bring the deductible amounts into account to claim relief against the transferred profit.

Qualifying change and deductible amounts

35. The Profit Transfer TAAR uses the same concepts of “qualifying change” and “deductible amounts” as are used for the Deduction Transfer TAAR described in the previous Chapter of this Note.

Circumstances in which “deductible amounts” will be disallowed

36. If two conditions apply, under the Profit Transfer TAAR, a “deductible amount” is not brought into account by C or a company connected with C as a deduction in an accounting period ending at or after the qualifying change.

37. The first condition is that at the date of the qualifying change it is highly likely that the deductible amount would be brought into account as a deduction in an accounting period ending at or after the qualifying change. The “highly likely” test is determined on the same basis as the equivalent test in the Deduction Transfer TAAR.

38. The second condition is that the purpose or one of the main purposes, of the “profit transfer arrangements” is to deduct the amounts for corporation tax purposes in any accounting period ending on or after the day of the qualifying change.

Chapter 5: Commencement

39. The new rules have effect if a “qualifying change” occurs on or after 20 March 2013, unless that change occurs as a result of an unconditional obligation (which may not be varied or extinguished by the exercise of a right) entered into before 20 March 2013.

Chapter 6: Interpretation of "Purpose"

40. HMRC expect that, as with similar anti-avoidance rules triggered by reference to purpose, it will be necessary to take all relevant factors into account in seeking to establish the purpose of the arrangements, but it is likely that HMRC will focus on the following factors when considering whether a tax avoidance purpose is present.

- The amount paid for the acquired company relative to the tax value of any relevant deductions (after taking into account other assets and liabilities of the acquired company).

- Changes made to the business carried on by the acquired company prior to its acquisition – in particular, attempts to isolate the value of the relevant deductions from other aspects of the business (e.g. through the use of special purpose vehicles and/or the hiving off of parts of the business) such that the acquired company in effect becomes little more than a shell for the latent deductions.

- The nature of the business carried on by the transferred company relative to the business carried on by the new group.

- The planned conduct of the transferred business following its transfer. For example, whether plans were in place to carry it on commercially and with a view to profit once it became part of the new group and whether arrangements are in place to transfer the trade back to the selling group.

Chapter 7: Draft Legislation -

Corporation Tax Targeted Loss Buying Rules -

Transfer of deductions –Part 14A Corporation Tax Act 2010

The Legislation appears on pages 15 to 19 inclusive.

1 Transfer of deductions

Schedule 1—

(a) inserts into CTA 2010 a new Part 14A (transfer of deductions), and
(b) makes consequential provision.

SCHEDULES

SCHEDULE 1

Section 1

TRANSFER OF DEDUCTIONS

New Part 14A of CTA 2010

1 After Part 14 of CTA 2010 insert—

"PART 14A

TRANSFER OF DEDUCTIONS

730A Overview

(1) This Part makes provision restricting the circumstances in which deductible amounts may be brought into account where there has been a qualifying change in relation to a company.

(2) For the meaning of "deductible amount" and "qualifying change" see section 730B.

(3) In this Part—
(a) "C" means the company mentioned in subsection (1),
(b) "the relevant day" means the day on which the qualifying change in relation to C occurred, and
(c) "arrangements" includes any agreement, understanding, scheme, transaction or series of transactions (whether or not legally enforceable).

730B Meaning of "deductible amount" and "qualifying change"

(1) In this Part "deductible amount" means—
(a) an expense of a trade,
(b) an expense of a UK property business or an overseas property business,
(c) an expense of management of a company's investment business within the meaning of section 1219 of CTA 2009,
(d) a non-trading debit within the meaning of Parts 5 and 6 of CTA 2009 (loan relationships and derivative contracts) (see section 301(2) of that Act), or
(e) a non-trading debit within the meaning of Part 8 of CTA 2009 (intangible fixed assets) (see section 746 of that Act).

(2) But "deductible amount" does not include any amount that has been taken into account in determining RTWDV within the meaning of Chapter 16A of Part 2 of CAA 2001 (see section 212K of that Act).

(3) "Qualifying change", in relation to a company, has the same meaning in this Part as in Chapter 16A of Part 2 of CAA 2001 (restrictions on allowance buying).

730C Disallowance of deductible amounts: relevant claims

(1) This section applies where a relevant claim is made for an accounting period ending on or after the relevant day.

(2) "Relevant claim" means a claim by C, or a company connected with C, under—
  (a) section 37 (relief for trade losses against total profits), or
  (b) Chapter 4 of Part 5 (group relief).

(3) A deductible amount that meets the following two conditions may not be the subject of, or brought into account as a deduction in, the claim.

(4) The first condition is that, on the relevant day, it is highly likely that the amount, or any part of it, would (disregarding this Part) be the subject of, or brought into account as a deduction in, a relevant claim for an accounting period ending on or after the relevant day.

(5) Any question as to what is "highly likely" on the relevant day for the purposes of subsection (4) is to be determined having regard to—
  (a) any arrangements made on or before that day, and
  (b) any events that take place on or before that day.

(6) The second condition is that the purpose, or one of the main purposes, of change arrangements is for the amount (whether or not together with other deductible amounts) to be the subject of, or brought into account as a deduction in, a relevant claim for an accounting period ending on or after the relevant day.

(7) "Change arrangements" means any arrangements made to bring about, or otherwise connected with, the qualifying change.

730D Disallowance of deductible amounts: profit transfers

(1) This section applies where arrangements ("the profit transfer arrangements") are made which result in an increase in the total profits of C, or of a company connected with C, in any accounting period ending on or after the relevant day.

(2) A deductible amount that meets the following two conditions may not be brought into account by C, nor any company connected with C, as a deduction in any accounting period ending on or after the relevant day.

(3) The first condition is that, on the relevant day, it is highly likely that the amount, or any part of it, would (disregarding this Part) be brought into account by C, or any company connected with C, as a deduction in any accounting period ending on or after the relevant day.

(4) Any question as to what is "highly likely" on the relevant day for the purposes of subsection (3) is to be determined having regard to—
  (a) any arrangements made on or before that day, and

(b) any events that take place on or before that day.

(5) The second condition is that the purpose, or one of the main purposes, of the profit transfer arrangements is to bring the amount (whether or not together with other deductible amounts) into account as a deduction in any accounting period ending on or after the relevant day.

(6) References in this section to bringing an amount into account "as a deduction" in any period are to bringing it into account as a deduction in that period—

(a) in calculating, or from, any profits or other amounts charged to corporation tax, or

(b) in calculating any losses or other amounts for which relief from corporation tax is given."

Consequential amendments

2 (1) In section 1(4) of CTA 2010 (overview of Act) after paragraph (a) insert—

"(aa) transfer of deductions,".

(2) In Schedule 4 to that Act (index of defined expressions) insert at the appropriate places—

"arrangements (in Part 14A)	section 730A(3)"
"C (in Part 14A)	section 730A(3)"
"deductible amount (in Part 14A)	section 730B"
"qualifying change (in Part 14A)	section 730B"
"the relevant day (in Part 14A)	section 730A(3)"

Commencement and transitional provision

3 (1) The amendments made by this Schedule have effect in relation to a qualifying change if the relevant day is on or after 20 March 2013.

(2) But those amendments do not have effect if the qualifying change happens pursuant to an unconditional obligation in a contract made before that date.

(3) "An unconditional obligation" means an obligation which may not be varied or extinguished by the exercise of a right (whether under the contract or otherwise).

Chapter 8: Draft Explanatory Note –

Corporation Tax Targeted Loss Buying Rules -

Transfer of deductions –Part 14A Corporation Tax Act 2010

SUMMARY

1. Clause x introduces a new Part 14A in Corporation Tax Act 2010 (CTA 2010) which includes two new substantive restrictions on the circumstances in which deductible amounts may be brought into account where there has been a qualifying in relation to a company (C). The deductible amounts are ones which, at the date of the qualifying change (the "relevant day"), can be regarded as highly likely to arise as deductions for an accounting period ending on or after that day.

2. The first restriction is on claims for group relief and relief for trade losses against total profits for deductible amounts in accounting periods ending on or after the relevant day where the purpose, or one of the main purposes, of arrangements connected to the qualifying change is for the deductible amounts to be the subject of, or brought into account as a deduction in, such a claim.

3. The second restriction is in respect of deductible amounts where there are 'profit transfer arrangements' (i.e. arrangements which result in an increase in the total profits of C, or a company connected to C) where the purpose, or one of the main purposes, of those arrangements is to bring the deductible amount into account as a deduction in any accounting period ending on or after the relevant day.

DETAILS OF THE SCHEDULE

4. Schedule 1 amends CTA 2010 by introducing a new Part 14A with the heading "Transfer of Deductions."

5. New Section 730A provides an overview of the Part.

6. New Section 730B explains the meaning of "deductible amount" and "qualifying change". A "deductible amount" is any expense of a trade or property business, an expense of management of an investment business, non-trading debits within the meaning of Parts 5 and 6 of the Corporation Tax Act 2009 (CTA 2009) (loan relationships, derivative contracts) or a non-trading debit within the meaning of Part 8 CTA 2009 (intangible fixed assets). "Deducible amount" does not include any amount that has been taken into account in determining RTWDV within the meaning of Chapter 16A of Part 2 of Capital Allowances Act 2001 (CAA 2001). A "qualifying change" has the same meaning in Part 14A as in Chapter 16A of Part 2 CAA 2001.

7. New Section 730C provides for the restriction which applies to disallow deductible amounts for relevant claims.

8. Subsection 1 applies the section where a relevant claim is made for an accounting period on or after the qualifying change.

9. Subsection 2 defines a relevant claim as a claim for relief for trade losses against total profits (under section 37 of CTA 2010) or group relief (under Chapter 4 of Part 5 of CTA 2010) by C or a company connected with C.

10. Subsection 3 provides that if two conditions are met the deductible amount may not be the subject of, or brought into account as a deduction in, a relevant claim.

11. Subsection 4 explains the first condition: on the relevant day it is highly likely that the deductible amount would be the subject of, or brought into account as a deduction in a relevant claim for an accounting period ending on or after the relevant day.

12. Subsection 5 explains that what is “highly likely” is determined having regard to any arrangements or events that take place on or before the qualifying change.

13. Subsection 6 explains the second condition: where the purpose, or one of the main purposes, of any “change arrangements” is for the deductible amount to be the subject of, or brought into account as a deduction in a relevant claim.

14. Subsection 7 defines change arrangements as arrangements made to bring about or other connected to the qualifying change.

15. New Section 730D provides the restriction which disallows deductible amounts where there is a profit transfer.

16. Subsection 1 provides that section 703D applies where profits transfer arrangements are made which results in an increase in the total profits of C, or any connected company, in any accounting period ending on or after the relevant day.

17. Subsection 2 provides that if two conditions are met a deductible amount may not be brought into account by C, or any connected company, as a deduction in any accounting period ending on or after the relevant day.

18. Subsection 3 explains the first condition: on the relevant day it is highly likely that the deductible amount would be brought into account by C or a connected company as a deduction in an accounting period ending on or after the relevant day.

19. Subsection 4 explains arrangements and events to have regard to when considering what is “highly likely”.

20. Subsection 5 explains the second condition: where the purpose or one of the main purposes, of the profit transfer arrangements is to bring the deductible amount into

account as a deduction in any accounting period ending on or after the relevant day.

21. Subsection 6 explains the references to bringing into account "as a deduction".

22. Schedule 1 Paragraph 2 makes consequential amendments to CTA 2010.

23. Schedule 1 Paragraph 3 provides the commencement provisions. The amendments apply to a qualifying change on or after 20 March 2013, unless that change was subject to an unconditional obligation before that day.

BACKGROUND

24. This clause is one of two preventing loss buying introduced by M5149.

25. The clause uses the term "qualifying change" as defined in Section 212C of Chapter 16A of Part 2 CAA 2001

26. Section 212C CAA2001 defines a qualifying change in relation to a company as -

- A change in ownership of a company,
- When a company becomes a member of a group
- When a company moves from a group into a consortium.
- When a consortium member increases it ownership of a consortium company.
- Where C ceases to carry on the whole or part of an activity and the activity (or part of it) begins to be carried on in partnership by two or more companies.
- When a partner increases its share in a partnership that is carrying out an activity

Current corporate tax loss buying rules

27. The general concept is that losses brought forward or after a change in ownership should be allowable only to the company and trade in which they occurred.

28. Section 39 of CTA 2010 provides that if a company sells its trade to a company that is not within the same 75% ownership then the cessation rules apply and the losses do not transfer.

Part 14 of CTA 2010 deals with realised losses where there is a change in ownership of a company (and where other circumstances apply). If the Part applies losses arising prior to the change are no longer available for periods after the change in ownership.

Chapter 9: Draft Legislation –

Corporation Tax Targeted Loss Buying Rules - Restrictions on buying capital allowances –Chapter 16A Part 2 Capital Allowances Act 2001

The Legislation appears on pages 24 to 27 inclusive.

1 Restrictions on buying capital allowances

Schedule 1 contains provision amending Chapter 16A of Part 2 of CAA 2001 (restrictions on allowance buying).

SCHEDULE

Section 1

RESTRICTIONS ON BUYING CAPITAL ALLOWANCES

PART 1

RESTRICTION WHERE CERTAIN CONDITIONS MET

1 Chapter 16A of Part 2 of CAA 2001 (avoidance involving allowance buying) is amended as follows.

2 (1) Section 212B (circumstances where Chapter 16A applies) is amended as follows.

(2) For subsection (1)(d) substitute—

"(d) the qualifying change meets one of the limiting conditions."

(3) For subsection (4) substitute—

"(4) Sections 212LA and 212M set out the limiting conditions and specify when those conditions are met."

3 After section 212L insert—

"Limiting conditions

212LA Limiting conditions

(1) The qualifying change meets one of the limiting conditions if condition A, B, C or D is met.

(2) Condition A is that the amount of the relevant excess of allowances is £50 million or more.

(3) Condition B is that the amount of the relevant excess of allowances—

(a) is £2 million or more but less than £50 million, and

(b) is not insignificant as a proportion of the total amount or value of the benefits derived by any relevant person by virtue of the qualifying change or change arrangements.

(4) "Relevant person" means a person who, at the end of the relevant day, is—

(a) a principal company of C,

(b) a person carrying on the relevant activity in partnership, or

(c) a person who is connected to a person within paragraph (a) or (b) (within the meaning of section 1122 of CTA 2010).

(5) Condition C is that—

(a) the amount of the relevant excess of allowances is less than £2 million, and

(b) the qualifying change has an unallowable purpose.

See section 212M for the meaning of “unallowable purpose”.

(6) Condition D is that the main purpose, or one of the main purposes, of any arrangements is to procure that condition A or B or paragraph (a) of condition C is not met.

(7) In this section—

the amount of the relevant excess of allowances is the difference between RTWDV and BSV (see sections 212K and 212L);

“change arrangements” and “arrangements” have the same meaning as in section 212M.”

4 In consequence of the amendments made by this Part, the heading to that Chapter becomes “RESTRICTIONS ON ALLOWANCE BUYING”.

PART 2

EXTENSION OF RESTRICTIONS TO OTHER QUALIFYING ACTIVITIES

5 (1) Section 212B (circumstances where Chapter 16A applies) is amended as follows.

(2) In subsection (1)—

(a) in paragraph (a), for “a trade (“the relevant trade”)” substitute “a qualifying activity (“the relevant activity”)”, and

(b) in paragraph (c), for “trade” (in both places) substitute “activity”.

(3) In subsection (3), for “trade” substitute “activity”.

6 (1) Section 212C (when there is a a qualifying change in relation to C) is amended as follows.

(2) In subsection (4)—

(a) after “Condition C is that” insert “the relevant activity is a trade (within the meaning of this Part) and”, and

(b) for “trade”, where it appears after “the relevant” (in both places), substitute “activity”.

(3) In subsection (5), for “trade” (in both places) substitute “activity”.

7 (1) Section 212I (relevant percentage share) is amended as follows.

(2) In subsections (1) and (3), for “trade” substitute “activity”.

(3) In subsection (2), for “a trade” substitute “an activity”.

8 In section 212J(1) (relevant excess of allowances), for “trade” substitute “activity”.

9 In section 212K(2), (3), (4) and (5) (relevant tax written-down value), for “trade” substitute “activity”.

10 In section 212N(2), (3) and (4) (old and new accounting periods), for “trade” substitute “activity”.

11 (1) Section 212P (effect of excess on pools) is amended as follows.

(2) In subsection (3)—

(a) for “a trade (or part of a trade)” substitute “a qualifying activity (or part of a qualifying activity)”,

(b) for “the activities of that trade (or part of a trade)” substitute “that activity (or that part of an activity)”,

(c) after “its trade” insert “or business”,

(d) for “those activities” substitute “that activity (or that part)”, and

(e) after “separate trade” insert “or business”.

(3) In subsection (4)—

(a) after “section 37” insert “, 62 or 66”,

(b) omit “trade”,

(c) for “earlier” substitute “other”, and

(d) after “period)” insert “or section 259 or 260(3) of this Act (special leasing)”.

12 (1) Section 212Q (when there are postponed capital allowances) is amended as follows.

(2) In subsection (3)—

(a) for “a trade (or part of a trade)” substitute “a qualifying activity (or part of a qualifying activity)”,

(b) for “the activities of that trade (or part of a trade)” substitute “that activity (or that part of an activity)”,

(c) after “its trade” insert “or business”,

(d) for “those activities” substitute “that activity (or that part)”, and

(e) after “separate trade” insert “or business”.

(3) In subsection (4)—

(a) after “section 37” insert “, 62 or 66”, and

(b) after “CTA 2010” insert “or section 259 or 260(3) of this Act”.

PART 3

COMMENCEMENT

13 (1) The amendments made by this Schedule have effect in relation to a qualifying change if the relevant day (within the meaning of Chapter 16A) is on or after 20 March 2013.

(2) But those amendments do not have effect if the qualifying change happens pursuant to an unconditional obligation in a contract made before that date.

(3) “An unconditional obligation” means an obligation which may not be varied or extinguished by the exercise of a right (whether under the contract or otherwise).

Chapter 10: Draft Explanatory Note –

Corporation Tax –Targeted Loss Buying Rules -Restrictions on buying capital allowances –Chapter 16A Part 2 Capital Allowances Act 2001

SUMMARY

29. This clause expands the application of Chapter 16A of Part 2 of the Capital Allowances Act 2001 (CAA 2001) which restricts the relevant excess of allowances after a qualifying change in relation to a company (C). It expands Chapter 16A to apply to all "qualifying activities" (under section 15 of CAA 2001) and not just trades, as currently. It also applies Chapter 16A where that relevant excess of allowances is £50 million or more (in any circumstances); or where the relevant excess is £2 million or more and less than £50 million (where the amount is not insignificant); or where the relevant excess is less than £2 million (and the qualifying change has an unallowable purpose).

DETAILS OF THE SCHEDULE

30. Paragraph 2 makes consequential amendments and introduces the requirement for a qualifying change to meet the "limiting conditions" set out in 212LA.

31. Paragraph 3 inserts new section 212LA into Chapter 16A of Part 2 of CAA 2001 which sets out the four "limiting conditions".

32. New subsection 212LA(2) provides that Condition A is met where the relevant excess of allowances is £50 million or more.

33. New subsection 212LA(3) explains Condition B. Where the relevant excess of allowances is £2 million or more but less than £50 million and the amount is not insignificant in the context of the value of the benefits obtained by a "relevant person" through the qualifying change or "change arrangements" then Condition B is met.

34. New subsection 212LA(4) defines "relevant person" as the company acquiring the company or the activity in partnership or any person connected with the company acquiring the company or trade.

35. New subsection 212LA(5) explains Condition C. This is met if the amount of the relevant excess of allowances is less than £2 million and the qualifying change has an unallowable purpose. The subsection refers to section 212M which provides the definition of unallowable purpose.

36. Subsections (6) explains Condition D. This is met if there are arrangements the purpose of which is to procure that the relevant excess allowance is below the £50 million or £2 million tests or to procure that the relevant excess of allowances is a smaller proportion of the total amount or value of the benefits referred to in Condition B.

37. Subsection (7) defines the amount of the relevant excess and arrangements.

38. Part 2 extends the restrictions on allowance buying to all other qualifying activities (under section 15 of CAA 2001) and provides the consequential amendments arising from this extension.

39. Part 3 provides the commencement provisions. The amendments apply to a qualifying change on or after 20 March 2013, unless that change was subject to an unconditional obligation before that day.

BACKGROUND

40. This clause is one of two preventing loss buying.

41. Chapter 16A of Part 2 CAA 2001 was introduced in Finance Act 2010 in order to prevent tax-motivated capital allowance buying. Chapter 16A applies to situations where a company in a group decided not to claim all the allowances to which it was entitled and that company is then subject to a qualifying change.

42. Chapter 16A applies where there is a company C and:

- the tax written down value (TWDV) of the company's plant or machinery assets exceeds the balance sheet value (BSV) of those assets. This excess is the relevant excess of allowances.
- there is a "qualifying change of ownership" in relation to C; and in certain circumstances where the qualifying change has an "unallowable purpose".

Prior to this amendment Chapter 16A applied to restrict claims to trading losses either by set off in year by carry back or by group relief where there is a qualifying change with an unallowable purpose as one where the main purpose or one of the main purposes of the change arrangements is to obtain a tax advantage for any person.

Chapter 11: Tax Information and Impact Note (TIIN) – Corporation Tax loss relief - targeted loss buying rules

Corporation Tax loss relief - targeted loss buying rules

Who is likely to be affected?

Companies that take over another unconnected company or activity or increase their ownership proportion of another company or partnership activity with a view to accessing unclaimed losses for offset against their own profits.

General description of the measure

This measure amends and supplements existing corporation tax provisions to address the issue of companies entering into arrangements, as part of a business transfer, to gain relief for corporation tax losses of unconnected third parties where it is possible to dictate or predict the timing of when those losses can be claimed.

Policy objective

This measure clarifies and reasserts the underlying principles on which UK loss relief rules are based. These include: i) brought forward losses should only be relievable against future profits from the same trade, carried on by the same legal entity; and ii) that tax losses should not be transferable between unconnected parties. In doing so it protects the Exchequer and provides a level tax playing field for companies to operate within.

Background to the measure

This measure was announced at Budget 2013.
Draft legislation was published for consultation on 28 March 2013.

Detailed proposal

Operative date

The measure has effect for any qualifying change on or after 20 March 2013, unless that change was subject to an unconditional obligation entered into before that day.

Current law

Chapter 16A of Part 2 of Capital Allowances Act 2001 (CAA 2001):

Chapter 16A applies when there is a qualifying change in relation to a company which carries on a trade. A qualifying change is either the sale or partial sale (to create a consortium) of a company, a change in the ownership proportions of a consortium company, a change in the profit sharing ratio of a partnership or a transfer of the trade. The rules apply if at least one of the main purposes of the qualifying change was to secure a tax advantage - i.e. reduction in profits / increased losses from a capital allowance claim. The legislation operates by allocating an amount of expenditure equal to the excess of allowances in each pool to a new separate pool of the same type. The relevant excess of allowances is the excess of the tax written down value of the plant and machinery over the balance sheet value. This relevant excess of allowances may only be used to reduce the profits (or increase the losses) from the trade as it was carried on, and to the extent that it was carried on, before the qualifying change. Any trading activities transferred in to the company or the partnership will be treated as a separate trade for these purposes.

Relief for the capital allowances are, still given after the change in ownership transaction but only to reduce the same profits and to the same extent that they could have reduced before the change.

Part 14 of Corporation Tax Act 2010 (CTA 2010):

Part 14 applies if a company carrying on a trade, investment business or property business is sold to another company not within the same 50%+ ownership. Relief for losses is restricted in any accounting period ending on or after a change in ownership if there is (i) a major change in the nature or conduct of the trade or business within three years of a change in ownership; or (ii) after a change in ownership, a significant revival of a trade or business that has become small or negligible or (iii) after a change in ownership, a significant increase in the capital of an investment business.

Proposed revisions

(A) Restrictions on allowance buying:

Legislation will be introduced to Finance Bill 2013 at committee stage to extend Chapter 16A of Part 2 of CAA2001. Chapter 16A will apply in respect of all qualifying activities (under section 15 of CAA 2001) and not just trades, as currently. Chapter 16A will apply where
(i) the relevant excess of allowances is £50 million or more (in any circumstances); or

(ii) the relevant excess of allowances is £2 million or more but less than £50 million but this is dependant on the amount not being insignificant having regard to the total amount or value of the benefits derived by any relevant person by virtue of the qualifying change or (arrangements connected to the change); or
(iii) the relevant excess of allowances less than £2 million and the qualifying change has an unallowable purpose.
There are rules to prevent attempts to get below the limits or to inflate the value of the transaction so that the excess appears as a smaller proportion. The same consequences of Chapter 16A applying will continue for the extended Chapter.

(B) Transfer of deductible amounts and profit transfer arrangements:

Legislation will be introduced to Finance Bill 2013 at committee stage introducing a new Part to Corporation Tax Act 2010. The new Part (14A) will apply where there has been a "qualifying change" in relation to a company. It prevents the company in relation to which there has been a qualifying change (or any connected company) surrendering group relief or claiming relief for trade losses aganst total profits so far as attributable to certain types of deductable amounts. Those amounts are ones which, at the date of the qualifying change, can be regarded as highly likely to arise as deductions for an accounting period ending on or after that date. The Part will only apply where the purpose or one of the main purposes of arrangements connected to the qualifying change is to claim relief for such a deduction. The consequence of the restriction will be that the deductions may not be the subject of, or brought into account as a deduction, in a relevant claim.

The new Part 14A also introduces provision to deal with profit transfer arrangements. This will apply where there has been a "qualifying change" in relation to a company. It tackles the transfer of profits to the company (or another company connected to that company) where the purpose, or one of the main purposes, of the transfer is to utilise deductible amounts. The rule denies relief for deductible amounts claimed in any accounting period ending on or after the qualifying change.

Summary of impacts

Exchequer impact (£m)	2013-14	2014-15	2015-16	2016-17	2017-18
	+225	+265	+235	+180	+165
	These figures are set out in Table 2.1 of Budget 2013 and have been certified by the Office for Budget Responsibility. More details can be found in the policy costings document published alongside the Budget.				
Economic impact	The measure is not expected to have any significant economic impacts.				
Impact on individuals and households	There is no impact on individuals because this measure only affects companies.				

Equalities impacts	No equalities impacts have been identified because this measure only affects companies.
Impact on business including civil society organisations	This measure is expected to have a negligible impact on businesses and civil society organisations. The number of companies affected by this measure is small; and those that are will be those undertaking transactions which access relief for losses either quicker than the legislation allows for or in ways contrary to the underlying principles upon which loss relief rules are based. There will be some admin burden for those companies acquiring other businesses, to establish whether the rules apply to those acquisitions and to apply the new rules if they do.
Operational impact (£m) (HMRC or other)	The additional costs for HMRC in implementing this measure are anticipated to be negligible
Other impacts	Small firms impact test: Some small businesses may be affected by this measure but only those that are engaged in arrangements where a significant tax relief is expected or where at least one of the purposes of the transaction is to access relief for tax losses. Other impacts have been considered and none have been identified.

Monitoring and evaluation

This measure will be kept under review through communication with affected taxpayer groups.

Further advice

If you have any questions about this change, please contact Simon Moulden on 020 7147 2629 (email: simon.moulden@hmrc.gsi.gov.uk) or Paula Jarnecki on 020 7147 2067 (email: paula.jarnecki@hmrc.gsi.gov.uk)

Declaration

David Gauke MP, Exchequer Secretary to the Treasury, has read this Tax Information and Impact Note and is satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impacts of the measure.