HM TREASURY

HM Revenue & Customs

Delivering a cap on income tax reliefs: a technical consultation

summary of responses

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1 Introduction

Background

1.1 The Government announced at Budget 2012 the introduction of a limit on currently uncapped income tax reliefs from April 2013. The limit will cap relief at the greater of £50,000 or 25 per cent of the individual's annual income.

Consultation

1.2 On 13 July 2012 HM Treasury published a consultation document "*Delivering a cap on income tax relief: a technical consultation*" seeking views on the operation of the relief cap. The consultation ran for a period of 12 weeks, closing on 5 October 2012.

1.3 Fifty-eight responses to this consultation were received. Most respondents were tax consultants and agents. Entrepreneurs, investors, representative bodies and other individuals also replied with their views on the proposed changes. In addition to reviewing written consultation responses, HM Treasury and HM Revenue & Customs (HMRC) met with businesses, representative groups and professional groups to hear their views. A full list of respondents to the consultation is contained at Annex A.

1.4 The Government is grateful to all those who responded to the consultation. Respondents engaged constructively with the process and the feedback has been valuable in identifying areas of broad consensus, or where there are concerns.

Aim of consultation

1.5 The aim of the technical consultation was to:

- seek views on the proposed approach in order to feed into draft legislation, which will have effect from April 2013;
- explain which reliefs will be affected by the cap;
- propose how income will be defined for the purpose of calculating the cap; and
- explain how the cap will operate in practice.

1.6 The consultation asked respondents:

- whether the right definition of income has been proposed;
- whether the proposed adjusted total income achieves the required parity between different pension saving arrangements and charitable donations;
- to identify opportunities for errors or misunderstanding;
- to give their views on the calculation and application of the cap; and
- to give their views on the impacts identified in the tax impact assessment.

2 Responses

2.1 This chapter summarises the responses to the questions asked, taking each question in turn.

2.2 Fifty-eight responses to the consultation were received. These can be broken down as follows:

- 45 from tax consultants, agents and representative bodies;
- seven from representatives of entrepreneurs / investors; and
- six from individuals.

2.3 In addition to reviewing written consultation responses, HM Treasury and HMRC also met with businesses, representative groups and professional groups to hear their views.

Questions 1, 2 and 3:

Do you agree that a new definition of adjusted total income for the purposes of the cap is required?

Do you consider that the definition of adjusted total income for the purposes of the cap achieves the required parity between different pension arrangements? Please explain your answer.

Do you consider the proposed mechanism for allowing relief obtained via Payroll Giving to be included in the definition of income satisfactory? Please explain your answer.

2.4 Twenty-four respondents commented on whether a new definition of income was needed to calculate the cap above the £50,000 lower limit and whether that definition dealt satisfactorily with adjustments for pension savings and charitable giving. The vast majority of respondents agreed that a new definition was required to achieve parity, and agreed that income for the purpose of calculating the 25 per cent cap should include charitable giving. A majority also agreed to the proposed exclusion of pension savings, but a small number of respondents suggested that that the cap should be calculated in a way most beneficial to the taxpayer. Some respondents noted that excluding pension savings could discourage the making of future contributions.

Question 4:

Do you see any opportunity for errors or misunderstanding in the application of the cap? If yes, please suggest how you believe HMRC guidance or processes could help manage this?

2.5 There were 21 responses to this question and a significant proportion of these felt that it could be difficult to convey to ordinary taxpayers the difference between adding back donations and deducting pension contributions from income in order to calculate the cap. Respondents felt that a degree of tax knowledge would be required to know which reliefs were set against total income and which were not. This left scope for errors.

2.6 Respondents suggested that;

- HMRC should produce clear guidance (including extensive examples) not only for the completion of the SA return, but also so that individuals could make informed decisions about their investment choices at the time of making them; and
- statements of pension contributions and Payroll Giving should be provided by employers alongside the P60 form.

Question 5:

Do you have any further comments on the practicalities of calculating or applying the cap?

2.7 Comments on the practicality of applying the cap included the following points:

- the Enterprise Investment Scheme and Seed Enterprise Investment Scheme already have their own limits and to apply the cap to share loss relief on such shares would either not be understood or would act as a disincentive to individuals participating in these schemes for whom the financial risks of investment would be complex to assess; and
- where trade losses or early trade losses arise wholly or partly from the deduction of overlap profits, overlap relief might be denied where the cap applies. Eight respondents questioned whether this was the intended technical outcome and expressed concern that applying the cap in these circumstances would add further complexity to the Self Assessment process and would require clear guidance to help taxpayers get it right.

Question 6:

Are there any other impacts not set out in the Impact Assessment?

2.8 Twenty-eight respondents expressed a view on the impact assessment, including that:

- the impact on investments in start-ups could have more significant consequences for economic growth than identified (i.e. where cash flow is maximised from the use of sideways and carried back relief);
- businesses would incur costs in restructuring – e.g. for incorporation and re-financing of loans to circumvent the cap;
- employment in local communities could be impacted where businesses are less able to invest in growth; and
- more individuals on lower incomes may be unintentionally caught, such as those with significant losses or loans.

Government Response

2.9 It is clear that the majority of respondents felt that the proposed definition of income, including how pension savings and charity donations are dealt with is acceptable.

2.10 The Government is grateful for the suggestions from respondents to help smooth the introduction of the cap. HMRC will look to work with interested parties to ensure effective guidance is made available. However, the Government does not want to impose additional administrative burdens on employers in relation to P60 forms. The Government considers that taxpayers and their advisors, who need to consider the adjusted income calculation, can be effectively supported with guidance.

2.11 In the light of the arguments made, the Government has decided that share loss relief for shares qualifying for EIS/SEIS should be excluded from the cap. Share loss relief on shares not within EIS/SEIS will remain within the cap.

2.12 The Government is grateful to respondents, of which a significant number were tax agents, for highlighting the issue of 'overlap relief'. This is provided to prevent the double taxation of profits over the lifetime of a business. The Government agrees with respondents that applying the cap in these circumstances may cause the unintended consequence of denying overlap relief. Therefore, the Government will make a technical adjustment and remove trade loss relief and early trade losses relief attributable to overlap relief from the scope of the cap. Overlap relief will now align with the other computational reliefs originally excluded from the cap.

2.13 The Government remains confident in the Impact Assessment which set out that this change will affect only around 8,000 people with the highest incomes, with a median loss of around £20,000. Over 90 per cent of the revenue from the measure will come from those with income over £150,000.

2.14 The Government believes the Economic Assessment is correct in identifying no significant impacts. Of the number of respondents who expressed concern about the impact on smaller businesses, some examples given did not take account of the ability individuals will still have to set trading losses against earlier or later profits from the same trade. We think it may help to clarify this aspect of the policy.

2.15 The Government's intention is to apply the cap to reliefs that an individual is able to claim against their general income. It is not intended to cap reliefs used against profits in another year from the same business. Box 2.A illustrates this:

Box 2.A: Worked example

Henry has trade losses in 2014-15 of £200,000 and 2013-14 profits from the same trade of £70,000. He has other income in each year of £120,000.

His relief against general income is capped at £50,000 for both 2013-14 and 2014-15.

Henry makes a claim to set £50,000 trade loss relief against his 2014-15 general income and to carry back £70,000 against 2013-14 profits from the same trade. He also claims £50,000 carried back against his general income in 2013-14.

Henry's income chargeable to tax is:

2014-15

Income	£120,000
Less sideways trade loss relief (capped)	£ 50,000
Income chargeable to tax	**£ 70,000**

2013-14

Income (£70,000 + £120,000)	£190,000
Less 2014-15 trade loss relief against same trade (uncapped)	£ 70,000
Less 2014-15 trade loss relief (capped)	£ 50,000
Income chargeable to tax	**£ 70,000**

3 Next steps

3.1 The Government will introduce legislation in the Finance Bill 2013 to apply a cap on income tax reliefs claimed by individuals from 6 April 2013. The cap will apply to reliefs set out at annex B and will be set at the greater of £50,000 or 25 per cent of income. Draft legislation was published on 11 December for a further eight week consultation.

3.2 HMRC will publish guidance on the changes, including worked examples, in advance of the effective date.

A List of respondents

A.1 In addition to the list below we were pleased to receive representations from six Individuals.

Alan Pink (Accountants)

Angel Capital Group

Angel News

Archangel Informal Investment Ltd

Association of Accounting Technicians (AAT)

Association of Chartered Certified Accountants (ACCA)

Association of International Accountants (AIA)

Association of Partnership Practitioners

Association of Tax Technicians (ATT)

Baker Tilly

Barnes Roffe LLP (Chartered Accountant)

BDO LLP

Boodle Hatfield (Law Firm)

CA-4 Partnership Ltd

Capitus

Chartered Institute of Taxation (CIOT)

Country Land and Business Association

Creaseys

Deloitte

DFJ Esprit LLP

Elacotts Chartered Accountants

Ernst & Young

Estates Business Group

Grant Thornton

Handley Roberts

Harcourt Capital LLP

Historic Houses Association

Icebreaker Management Services Ltd

Immunocore Ltd

Institute of Chartered Accountants in England and Wales (ICAEW)

Killik & Co

KPMG

Lewis Silkin LLP

Lloyd’s

London Society of Chartered Accountants Taxation Committee

Moore Stephens LLP

National Farmers Union

Octopus Ventures

Patricia J Arnold & Co (tax agent)

PFP Wealth Planning

PKF (UK)

Punter Southall

PWC

Reeves & Co LLP (Accountants)

Saffrey Champness (Chartered Accountant)

Scottish Land & Estates

Society of Trust and Estate Practitioners (STEP)

The Law Society

Trades Union Congress

Traylor Wessing

Try Lunn Accountants

UK Business Angels Association

B Reliefs subject to the cap

B.1 The following income tax reliefs will be capped to the extent that they can be relieved by individuals against general income:

- Trade Loss Relief against general income – available for losses made by an individual carrying on a trade, profession or vocation. This will exclude relief for losses attributable to overlap relief and Business Premises Renovation Allowances (BPRA);
- Early Trade Losses Relief – available to an individual in the first four years of the trade, profession or vocation. This will exclude relief for losses attributable to overlap relief and BPRA;
- Post-cessation Trade Relief – available for qualifying payments or qualifying events within seven years of the permanent cessation of the trade;
- Property Loss Relief against general income – available for property business losses arising from capital allowances or agricultural expenses. This will exclude relief for losses attributable to BPRA;
- Post-cessation Property Relief – available for qualifying payments or qualifying events within seven years of the permanent cessation of the UK property business;
- Employment Loss Relief – available in certain circumstances where losses or liabilities arise from employment;
- Former Employees Deduction for Liabilities – available for payments made by former employees for which they are entitled to claim a deduction from their general income in the year in which the payment is made;
- Share Loss Relief on non-EIS/SEIS shares – available for capital losses on the disposal (or deemed disposal) of certain qualifying shares;
- Losses on Deeply Discounted Securities – available only for losses on gilt strips and on listed securities held since at least 26 March 2003; and
- Qualifying Loan Interest – available for interest paid on certain loans. These include loans to buy an interest in certain types of company, or to invest in a partnership.

HM Treasury contacts

This document can be found in full on our website: http://www.hm-treasury.gov.uk

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