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**Peer to Peer tax relief for irrecoverable loans  
Draft Guidance**

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To be included in the Savings and Investment Manual

Technical Guidance Note  
9 December 2015

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## Introduction

This guidance sets out the rules on how to apply the Tax Relief for irrecoverable loans that occur on Peer to Peer (P2P) Investments under [Section XX Income Tax Act 2007]. This tax relief was brought in at [Section XX Finance Act 2016].

This tax relief allows P2P loans that become irrecoverable to be relieved by the lender against interest that they receive from other P2P loans.

The purpose of this relief is to ensure that people who invest in P2P loans are subject to tax on the return that they make from their lending portfolio as a whole. This will create a level playing field for the taxation of income from P2P lending when compared to the taxation of traditional forms of retail investment and bring the tax position of the peer to peer sector in line with other forms of investment products available for individuals to purchase, such as collective investment schemes (more detail in [SAIM6000](#)).

P2P lending is an area of Financial Technology that enables individuals and businesses to lend to each other through the intermediary of an Internet platform. The sector seeks to avoid a traditional financial middleman such as a bank by having a platform act as a conduit to arrange and manage loans made directly between the lender and the borrower.

P2P lending is regulated by the Financial Conduct Authority and the platforms are regulated under Part 4A of the Financial Services and Markets Act 2000.

## When is P2P tax relief available?

To be able to claim relief on a P2P loan that becomes irrecoverable all of the following conditions must have been met:

- 1) Assuming interest were paid on the loan, the lender would be the person subject to any income tax on the interest.

This condition will still be met if the lender has no tax to actually pay.

The lender will include a person to whom a loan is assigned (more detail in [Who receives P2P tax relief](#))

- 2) The loan must be made through a regulated peer to peer platform.

The loan must be made through an operator who has permission under Part 4A of the Financial Services and Markets Act 2000 to operate an electronic system in relation to the lending of money.

- 3) Any outstanding amount of the principal (capital) of a loan made at any time has, on or after 6 April 2015, become irrecoverable (more detail in [When does a P2P loan become irrecoverable](#)).

- 4) The loan is a "peer to peer loan" as defined by the legislation (more detail in [What is a "peer to peer loan"](#))

If the lender is an Individual (who is subject to UK Income Tax on their income from the loan) then the loan should always meet this condition.

If the lender is not an individual, then they will have to consider whether the loan does fall within the definition in the legislation.

Persons subject to corporation tax will not be eligible for the new relief, but may be able to claim a deduction for any losses under the Loan relationships regime (more detail in the Corporate Finance Manual at [CFM30000](#)).

## What is a “peer to peer loan”?

The definition of a peer to peer loan for this tax relief is set out at [section XX, Finance Act 2016].

This definition is the same as the one used to define P2P lending as an activity that is regulated by the Financial Conduct Authority (FCA) ([link to FCA website](#)), but with the additional condition that the lender must be subject to UK Income Tax on their income from the loan.

If the lender is subject to UK Income Tax on their income from the loan then the loan will be a “peer to peer loan” if it also meets the following conditions;

EITHER

- a) The lender is
  - i. an individual, OR
  - ii. a partnership consisting of 2 or 3 persons, of which at least one must not be a company, OR
  - iii. an unincorporated body of persons which is not a partnership but contains at least one person who is not a company.

OR

- b) The borrower is of the same description as in a) AND
  - i. the loan is not used for the purpose of a business carried on by the borrower, OR
  - ii. the loan principal is less than £25,000.

These conditions are the same as those that define an “article 36H agreement” in FSMA 2000 (Regulated Activities) (Amendment) (No.2) Order 2013 ([here](#)).

## When does a P2P loan become irrecoverable?

A loan may be accepted as having become irrecoverable when there is no reasonable prospect of the recovery of the loan. When assessing recoverability, the funds available **and potentially available** to the borrower must be considered. A claim therefore cannot be established simply because the borrower has insufficient liquidity on the date the loan had been called in.

Whether a loan has become irrecoverable should be judged on a case by case basis, however the following common examples are relevant:

- When the borrower has entered formal recovery procedures such as liquidation, administration, receivership or bankruptcy the debt would normally be considered irrecoverable.
- If the debt is released by the lender it would normally be considered irrecoverable.

As the loan will be managed by a platform, the platform would usually be in a position to determine when a loan has become irrecoverable. The platform would then inform the lender that the loan had become irrecoverable.

### Loans with security

Where loans are made against security, the loan would be treated as becoming irrecoverable as if the security did not exist.

- If the lender or the platforms has entered into formal recovery procedures (collection, administration, receivership, seizure or liquidation of security, transfer to a recovery agent etc) the loan would normally be considered irrecoverable.

If the bad debt relief is given on an irrecoverable loan, and value is subsequently recovered from any loan security then this would be treated in the same way as any other subsequent recoveries of relieved irrecoverable loans (more detail in [Unexpected recoveries](#)).

## Who receives P2P tax relief?

The person who made the loan through the platform is entitled to the relief, unless they have assigned the right to recover the principal of the loan to another person

If the person who made the original loan through the platform has assigned the right to recover the principal of the loan to another person in exchange for a payment, the person to whom the right has been assigned would then be entitled to any relief.

However, in this case the amount that they can claim is limited to the amount that they paid for the right to recover to be assigned to them, less any amount of the principal already recovered (more detail in [Amount of P2P tax relief](#)).

## Amount of P2P tax relief

P2P tax relief for irrecoverable P2P loans can only be set against interest received by the lender on other P2P loans. It cannot be used against any other form of income.

### If the right to recover the loan still rests with the original lender

The amount of relief available is the amount originally lent, less any repayments of the principal of the loan already received.

### If the right to recover the loan has been assigned

The amount of relief available is the **lower** of

- 1) The amount paid for the right to receive the principal of the loan less subsequent repayments
- 2) The amount of the principal of the loan outstanding on assignment, less subsequent repayments.

#### Example 1

Terry lends £20 through a P2P platform. £5 is repaid, whilst £15 becomes irrecoverable. Terry can claim relief for the £15.

#### Example 2

Terry lends £20 through a P2P platform. He then assigns the right to recover the remaining principal to Brenda for £15. £5 of the loan is repaid to Brenda. The remaining principal of the loan becomes irrecoverable.

The amount of relief that Brenda can claim is the **lower** of:

- 1) amount paid for the loan to be reassigned less subsequent repayments (£15 - £5 = £10) and
- 2) the principal of the loan outstanding on assignment less subsequent repayments (£20 - £5 = £15)

So the amount of relief Brenda can claim therefore £10.

#### Example 3

Terry lends £20 through a P2P platform. He then assigns the right to recover the remaining principal to Barbara for £22. £5 of the loan is repaid to Barbara. The remaining principal of the loan is written off.

The amount of relief is the **lower** of:

- 1) amount paid for the loan to be reassigned less subsequent repayments (£22 - £5 = £17) and
- 2) the principal of the loan outstanding on assignment, less subsequent repayments (£20 - £5 = £15)

So the amount of relief that Barbara can claim is therefore £15.



## P2P tax relief against interest received through the same platform, in the same tax year

The person who made the loan or the person to whom the rights to recover the principal of the loan have been assigned are referred to here as simply as the Lender.

### From 6 April 16 onwards

Relief for irrecoverable P2P loans is given by deducting the amount of irrecoverable P2P loans from the P2P interest that the Lender receives from other P2P loans when calculating the lenders taxable income for the tax year in which the amount became irrecoverable.

From 6 April 2016 relief for irrecoverable P2P loans against income from P2P loans that are made through the same platform will be given automatically, that is without the need for the lender to make a claim.

The amount of P2P interest that the Lender will be subject to tax on is:

- the total amount of P2P interest that they receive through each platform, less
- the principal of P2P loans made through **the same platform** that have become irrecoverable in the same tax year.

### Example 1

Paul makes a series of interest bearing 5 year loans through Platform 'Zapo' in tax year 2015. In tax year 2017 one of the loans becomes irrecoverable. The amount of interest which Paul will be treated as receiving through 'Zapo' for tax purposes will be the amount of interest they received from other loans made through the 'Zapo' in the tax year 2017 less the irrecoverable amount of the loan.

### 6 April 15 to 5 April 16

The Lender can also claim relief on P2P loans that became irrecoverable on or after 6 April 2015 against other interest received in the same tax year from other P2P loans that were made through the same platform as the now irrecoverable loan.

This relief should be claimed in a tax return.

### Example 2

Niall makes a series of interest bearing 5 year loans through Platform 'Zapo' in tax year 2014. In November 2015 one of the loans becomes irrecoverable. Niall can set off the irrecoverable amount of the loan against any interest received from other loans made through 'Zapo' in his tax return in the tax year 2015.

## P2P tax relief against interest received through a different platform, in the same tax year.

The person who made the loan or the person to whom the rights to recover the principal of the loan have been assigned are referred to here as simply as the Lender.

The Lender can claim relief on an irrecoverable P2P loan that became irrecoverable on or after 6 April 2015, against interest received from loans made through a different P2P platform to that of the now irrecoverable loan.

This relief can only be claimed if the loss resulting from the irrecoverable loan cannot be used wholly or partly against interest received through the same P2P platform as the now irrecoverable loan. This is because the irrecoverable loan must be first set off against interest received through the same P2P platform.

The relief should be claimed in a tax return.

### Example

Geoffrey in tax year 2013 made 5 loans through platform 'Zapo' and 6 loans through platform 'SateRetter'.

When one loan made through Zapo became irrecoverable in tax year 2016, the irrecoverable amount was set against interest received from Zapo loans in the year. However, the irrecoverable amount exceeded the amount of interest received from the other Zapo loans in 2016.

Geoffrey then set off the remaining irrecoverable amount against interest received from SateRetter loans in tax year 2016.

## P2P tax relief against interest received in later tax years.

The person who made the loan or the person to whom the rights to recover the principal of the loan have been assigned are referred to here as simply as the Lender.

The Lender can claim relief on P2P loans that became irrecoverable on or after 6 April 2015, against interest received from loans made through P2P platforms in the 4 years following the year in which the debt became irrecoverable.

This relief can only be claimed if the loss resulting from the irrecoverable loan cannot be used wholly against interest received through P2P platforms in the same year as the loan becomes irrecoverable.

If carried forward, relief for the outstanding amount of the irrecoverable loan must be used against P2P interest received in the earliest year first, up to a maximum of 4 years.

The relief should be claimed in a tax return.

### **Example**

Harold in tax year 2013 made a series of 10 year loans through platform 'Wending Lorks'. When a loan made through Wending Lorks became irrecoverable in tax year 2019, Harold's loss is set against interest arising from Wending Lorks loans in tax year 2019.

However, the amount of the irrecoverable loss in tax year 2019 exceeded the amount of interest received from Wending Lorks loans in that year. Therefore, Harold can carry forward the outstanding amount of the irrecoverable loan to be set off against any P2P interest received in tax year 2020. If there is any amount of the irrecoverable loan outstanding after being set off against P2P interest received in tax year 2020, the outstanding amount can be carried forward against P2P interest received in tax year 2021, and so on, with the last year for set off being tax year 2023.

## Unexpected recoveries of P2P loans

If relief has been claimed because the principal of a loan has become irrecoverable, but subsequently the lender recovers any or all of the principal of the loan, they should treat this amount as P2P interest received at the time of the recovery.

In a case where the right to recover a loan has been assigned to another person, the person to whom the right to recover has been assigned is treated as recovering the loan and they must treat the amount as interest received at the time of the recovery.

The amount of the principal recovered that is deemed to be a payment of interest under the unexpected recovery provision is the lower of:

- 1) the amount that is recovered, and
- 2) the amount of relief that has been given for the irrecoverable loan.

### Example 1

Bridget makes 15 identical £10 loans. 2 of these loans become irrecoverable in tax year 17 and she receives relief of £20 to set against the other P2P interest that she receives in the tax year 17. In tax year 18, one of the irrecoverable loans is partly recovered to an amount of £5. In the tax year 18 this £5 recovery is taxable as P2P interest received by Bridget.

### Example 2

Terry lends £20 through a P2P platform. He then assigns the right to recover the remaining principal to Brenda for £15. £5 of the loan is repaid to Brenda. The remaining principal of the loan is written off.

The amount of Brenda's tax relief is the **lower** of

- 1) amount paid for the loan to be reassigned less subsequent repayments ( $£15 - £5 = £10$ ) and
- 2) the principal of the loan outstanding on assignment less subsequent repayments ( $£20 - £5 = £15$ )

So the amount of relief that Brenda receives is therefore £10.

A year later, the whole of the principal of the loan that was written off is recovered. Brenda therefore gets a recovery for the full amount (£15), but only the amount of relief she has claimed (£10) is treated as P2P interest received under the Unexpected recovery provision.

The additional £5 that Brenda receives above what she paid for the loan is taxed in the same way as it would have been had the loan been repaid in full and on time.

## P2P tax relief: Example

Paul makes 10 identical loans of £10 at 10% simple interest rates per year on 6 April 2013 through platform 'Zapo'. Paul also makes 2 loans of £30 at 10% simple interest rate per year on 6 April 2014 through platform 'SateRetter'. All these loans are interest only loans repayable in 5 years.

On 25<sup>th</sup> November 2015, Sateretter contact Paul to inform him that one of the loans has gone bad and is now irrecoverable.

On 31<sup>st</sup> July 2017 Sateretter informs Paul that £25 of the loan has been recovered.

### What is the tax effect?

**2013/14 year:** In this year Paul receives £10 in interest from his Zapo loans, which he suffers income tax on.

**2014/15 year:** in this year Paul receives £10 in interest from his Zapo loans and £6 in interest from his Sateretter loans, both of which he suffers income tax on

**2015/16 year:** In this year Paul's income is £10 in interest from Zapo loans, and £3 from the Sateretter loan which has not become irrecoverable. One loan of £30 has become irrecoverable as the creditor has entered into financial difficulties.

He can set this £30 off first against the interest received from the other Sateretter loan (£30-£3 = £27).

He can then set it off against other P2P interest received in the same year from loans made through Zapo (£27-£10 = £17).

The remaining £17 can be carried forward. Paul has no P2P income left and therefore does not suffer the related income tax charge.

He has used £13 of the available £30 relief.

**2016/17 year:** In this year Paul's income is £10 in interest from Zapo loans, and £3 from the remaining Pacesetter loan. He can use the carried forward relief against this income, taking his P2P income to 0.

The remaining relief is £17-£13 = £4.

**2017/2018 year:** In this year Paul's P2P income is again £13. He makes a recovery when he receives £25 as a result of the liquidation of the former creditor who was deemed to not be able to repay the loan in 15/16.

The full amount of the recovery is treated as interest received in 16/17. £25 is treated as income in the year 2016/17 taking Paul's P2P income to £13+£25 = £38. He can use the carried forward relief of £4 against this income, taking his P2P income to £34.

Paul also receives his principal back on the 5 Zapo loans on 5 April 2018. None of these loans have been treated as irrecoverable at any point so none of the repayment of principal is taxed as interest.

**2018/19 year:** In this year Paul's P2P income is the interest from the remaining Sateretter loan of £3, which he suffers income tax on.

## Interaction of P2P tax relief with Capital Gains Tax

A small proportion of Peer to peer loans have been historically eligible for relief as a capital loss under Taxation of Chargeable Gains Act (TCGA 1992).

This may be the case for peer to peer loans that have been assigned to another person (more details in the Capital gains manual at [CG53480](#)), or for 'loans to a trader' (more details at [CG65900](#)).

This has especially applied for lenders using P2P platforms which specialise in loans to small businesses.

### **Loans that become irrecoverable after on or after 6 April 2016**

An irrecoverable loan that would have been eligible for capital gains relief as a capital loss under TCGA 1992 will no longer be eligible for that relief.

This is because Section 2(3) of TCGA 1992 specifically gives priority to income tax reliefs.

### **Loans that become irrecoverable between 6 April 2015 and 5 April 2016**

An irrecoverable loan that would have been eligible for relief as a capital loss under TCGA 1992 may still be eligible for Capital Gains relief, but only if no claim is made for P2P income tax relief for the loss on the loan.