HM Revenue
& Customs

Corporation Tax: accounting for credit losses

Who is likely to be affected?

This measure potentially affects any company that incurs credit losses (also known as bad debts). The impact is expected to principally fall on the banking sector.

General description of the measure

The accounting standard covering financial instruments is changing with the introduction of International Financial Reporting Standard 9 (IFRS 9). When IFRS 9 is first adopted companies will need to account for the transitional adjustment which may reduce their taxable profits. This measure amends existing Corporation Tax regulations to deal with transitional adjustments specifically arising on first adoption of IFRS 9 in respect of credit losses. The impact of the measure will be that all transitional adjustments relating to this accounting change will be spread over 10 years. This will be achieved by amending existing regulations.

Policy objective

The government will continue to provide tax relief for credit loss allowances recognised in companies' accounts upon the introduction of the new IFRS 9 accounting standard. This will support the objectives of the accounting change and help ensure that the tax and regulatory regime are aligned in this area.

This measure also removes potentially distorting effects of the introduction of IFRS 9 by ensuring the full impact on Corporation Tax receipts on transition will be spread over 10 years. This helps to protect the Exchequer from a sudden reduction in corporation tax receipts as a result of the change.

Background to the measure

A new accounting standard (IFRS9) for financial instruments was published in July 2014. The new standard will require companies which apply International Accounting Standards or Financial Reporting Standard 101 to make credit loss allowances on a more forward looking basis from 2018.

This will result in an increase of credit loss allowances in the companies affected. These higher allowances will effectively bring forward tax relief, therefore reducing Corporation Tax receipts following the adoption of the new accounting standard.

This measure was announced in Autumn Statement 2014.

Detailed proposal

Operative date

This measure will have effect for periods of account commencing on or after 1 January 2015.

Current law

Section 316 Corporation Tax Act 2009 requires prescribed debits or credits to be brought into account on the change of an accounting policy. Section 316 is subject to the Change of Accounting Practice (COAP) Regulations 2004 (SI 2004 / 3271) – the 'COAP Regulations'.

The COAP Regulations generally prescribes that amounts arising from loans and derivatives on transition to a new accounting policy are not brought into account immediately but rather are spread over a 10 year period. However, this requirement to spread any transitional adjustment over a period of 10 years does not apply where the debt falls to be repaid in the current accounting period (normally 12 months).

Proposed revisions

A statutory instrument will be introduced to amend the COAP Regulations. As a result, all transitional adjustments arising from the adoption of IFRS 9 in respect of credit losses will be spread over a 10 year period, regardless of when the debt falls to be repaid.

Summary of impacts

<table>
<tr><td rowspan="3">Exchequer impact (£m)</td><td>2015 to 2016</td><td>2016 to 2017</td><td>2017 to 2018</td><td>2018 to 2019</td><td>2019 to 2020</td></tr>
<tr><td>Nil</td><td>+5</td><td>+10</td><td>+240</td><td>+40</td></tr>
<tr><td colspan="5">These figures were set out in Table 2.1 of Autumn Statement 2014 and have been certified by the Office for Budget Responsibility. More details can be found in the policy costings document published alongside Autumn Statement 2014.</td></tr>
<tr><td>Economic impact</td><td colspan="5">This measure is not expected to have any significant economic impacts.</td></tr>
<tr><td>Impact on individuals, households and families</td><td colspan="5">No impact on individuals, households or families has been identified. This measure is concerned with corporate taxpayers only.</td></tr>
<tr><td>Equalities impacts</td><td colspan="5">There are no impacts on equalities because this measure only affects companies.</td></tr>
<tr><td>Impact on business including civil society organisations</td><td colspan="5">It is expected that up to 15,000 businesses could be affected by the accounting change. Affected business are expected to incur a negligible one-off familiarisation cost on the change in the tax rules.

This measure requires affected companies to spread the transitional amounts over 10 years for Corporation Tax purposes. This is a simple calculation and the change is estimated to have a negligible impact on administrative burdens. It will defer tax relief for transitional adjustments to the new accounting, potentially impacting on their cash-flows.

The impact on small and medium business is expected to be minimal given the accountancy change principally affects groups with listed debt or equity.

This measure is expected to have no impact on Civil Society Organisations.</td></tr>
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Operational impact (£m) (HMRC or other)	The additional costs for HM Revenue and Customs in implementing this measure are anticipated to be negligible.
Other impacts	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 Richard Daniel on Telephone: 03000 569408 (email: richard.daniel@hmrc.gsi.gov.uk).

Declaration

David Gauke MP, Financial 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.