

# don't get lost with losses

Lisa Gilmour looks at the extension of trading loss carry back in the Budget 2009.

■ **New measures introduced in the Pre-Budget Report (PBR) 2008 for extension of trading loss carry back were extended in Budget 2009. The extension to three years carry back now applies to losses made in a two year period, as opposed to the year initially proposed by the PBR.**

In addition, the HMRC Business Support Service, launched in the 2008 PBR, has been expanded to allow leeway to businesses expecting to make a loss, not just those that have already made a loss.

#### companies

Under existing rules, a company can relieve a trading loss in the following ways:

- by setting the loss against any profits of any type of the same accounting period
- by setting any unused balance of losses against all profits of the preceding twelve months (if the company was carrying on the trade in that period)
- by carrying the loss, or any unused balance, forward to set against profits of the same trade in subsequent periods.

If a company ceases to trade it may apply terminal loss relief, which allows the carry back of trading losses in the final period to be set against trading profits of the previous three years as long as the company was carrying on the same trade in that three years. Apportionment is applied if any of the preceding accounting periods was not a year, or if the year end has changed.

The new measure brings no change to the current one year carry back of trade losses, but extends it so that any unused trading losses, up to a maximum of £50,000, may be carried back a further two years. It applies only to trading losses, but they can be set against all profits of the earlier periods. It applies to losses made in accounting periods ending between 24 November 2008 and 23 November 2010.

All existing loss reliefs will still be available. Should a company have made losses in earlier years and so have no profits to set the trading losses against, the loss can still be carried forward for relief against future trading profits.

#### Example:

Where company A Ltd has a current year trading loss of £130,000 (year 4 for illustration purposes) and the following profits:

- Year 3 - £70,000
- Year 2 - £40,000
- Year 1 - £40,000

Current rules allow £70,000 of the current year (year 4) trading loss to be carried back one year, i.e. to year 3. The unrelieved amount of £60,000 would be carried forward under current rules. The proposed legislative changes would, however, additionally allow company A Ltd to carry back £40,000 of the current year trading loss to year 2 and £10,000 of the loss to year 1 (using the relief to the maximum £50,000). The remaining £10,000 of the current year trading loss will be carried forward under current rules for relief under section 393 ICTA 1988.

#### unincorporated businesses

Under existing rules an unincorporated business can relieve a trading loss in the following ways:

## 'Apportionment is applied if any of the preceding accounting periods was not a year, or if the year end has changed'

- by setting that loss against general income for the year of the loss and the previous year
- if a loss is made in one of the first four tax years of trading, that loss may be set against an individual's other income of the three tax years before the one in which the loss was made
- if the trade ceases, making a loss in the twelve months leading up to the cessation date, that loss may be relieved against profits of the same trade for the final year and each of the three previous years
- any unrelieved losses may be carried forward and set against future trading profits of the same trade.

The existing one year carry back of trade losses remains, but is extended to allow any unrelieved trading losses for 2008/09 up to a maximum of £50,000 to be carried back to 2006/07 and 2005/06.

Losses for 2009/10 can be carried back to 2008/09 as under the old rules but also to 2007/08 and 2006/07.

As with companies, all current loss reliefs will still be available, enabling the business to carry forward any unrelieved losses to set against future profits from the same trade.

### Example:

An individual trader's profits, losses and other income are:

- 2005/06 Trade Profit £80,000
- Employment Income £5,000
- 2006/07 Trade Profit £60,000
- Employment Income £5,000
- 2007/08 Trade Profit £30,000
- Employment Income £5,000
- 2008/09 Trade Loss £100,000
- Employment Income £5,000

The trader makes a claim under section 64 ITA 2007 to set the 2008/09 loss against general income of both the year of loss (£5,000) and the previous year 2007/08 (£35,000).

The remaining part of the 2008/09 loss, up to a maximum of £50,000, is available to carry back to set against trading profits of 2006/07 and 2005/06 in that order.

Loss set against:

- 1) £5,000 employment income of 2008/09
  - 2) £35,000 employment income + trade profit of 2007/08
  - 3) £50,000 trade profit of 2006/07 (cap applied)
- (Total £90,000)  
£10,000 available to carry forward to set against trade profits in future years.

### how to claim

A company can claim by making a return once the extent of the loss has been established. Claims must be made within two years of the end of the period in which the loss arises.

An individual can claim in their tax return, though if it will affect more than one year, a claim must be made separately specifying the amount of the loss, which period it was made in and how it is to be utilised. The claim can be made when the basis period of the loss has ended, and must be made by 31 January 2011 for 2008/09, and 31 January 2012 for 2009/10.

### interaction with tax credits

In assessing a person's entitlement to tax credits, it is necessary to look at the claimant's income. Self employed income for this purpose will be the taxable profit for the tax year. In this context, 'taxable profit' has the same meaning as it has in part two of ITTOIA 2005.

If a loss is carried back, the previous year's tax credit entitlement will not be amended for the resultant reduced income. However, a loss carried forward will reduce any taxable profit in the following year, producing a lower figure for tax credit purposes. This does not mean that losses carried back against the previous year's income for real tax purposes cannot be used for tax credits; they must be used against the

current year's income, then that of the following years. The amount carried forward for real tax purposes and tax credit purposes will often be different because:

- losses for tax credit purposes must be set against a partner's income, whereas this is not normally done for real tax purposes;
- losses can be carried back for real tax purposes but not for tax credit purposes.

### Example:

Robert makes a loss of £25,000, having made a profit of £10,000 in the previous year. He has no other income. His partner has income of £6,000.

For income tax purposes, he can carry back £10,000 against the previous year and carry forward £15,000 against the following year.

For tax credits, he must use £6,000 against his partner's income and carry forward £19,000 against the following year.

### current anticipated losses

HMRC Business Support Service was launched in the 2008 Pre-Budget Report as a measure to help businesses with temporary financial difficulties, by allowing them to spread tax payments over an affordable timescale.

From 22 April 2009, this service is expanded to allow businesses expecting to make a loss to offset it against tax bills due on profits from the previous year which they are unable to pay.

This new measure does not mean HMRC will agree not to collect the tax due on the previous year's profits, but that all the circumstances will be taken into account in deciding how much time the business will be given to pay.

If the business is:

- genuinely unable to pay immediately or enter into a reasonable time to pay arrangement; and
- the tax owed is corporation tax or income tax on the previous year's profit; and
- the business is likely to make a trading loss in the current year, then HMRC will allow an extended period to pay, taking this into account, provided that the business is viable. ■

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