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Section 25 and Schedule 4: corporate capital losses

Background

Section 25 of the Finance Act 2020 (FA 2020) incorporates Schedule 4 FA 2020 (Schedule 4) which introduces a number of changes to carry-forward capital loss relief. These include a new corporate capital loss restriction (CCLR) which is broadly based on the corporation tax income loss restriction (CILR) enacted in Finance (No.2) Act 2017 (F(No.2)A 2017).[1]

[1] A. Greenbank and J. Moncrieff, "Finance (No.2) Act 2017 Notes: Section 18 and Schedule 4: carried-forward losses; Section 19: losses: counteraction of avoidance arrangements" [2017] BTR 547.

The changes were announced at Budget 2018. A consultation on delivery followed (*Corporate Capital Loss Restriction: Consultation on delivery* (Consultation Document)),[2] with draft legislation published for comment as part of "L-day" in July 2019.[3]

During the Public Bill Committee's discussions on Finance Bill 2019–2021, the Financial Secretary to the Treasury was keen to emphasise how, in taking forward these changes, the Government had complied with its Tax Consultation Framework,[4] commenting that

> "…these measures have been regarded within the profession as the model of how to achieve effective tax legislation".[5]

What the Financial Secretary failed to mention was that, because the Consultation started at Stage 2, a key stage of that framework had been missed: that of stating objectives and setting out options. The lack of an opportunity to comment more broadly on possible ways of reforming capital loss relief was, for this member of the profession at least, disappointing: after all, just over two years before, capital losses were expressly excluded from the Government's 2017 reforms of corporate loss relief:

> "…[T]he distinct treatment of capital losses remains appropriate and [the Government] does not intend to change it as part of these reforms."[6]

Surely the appropriateness (or not) of such distinct treatment merited a Stage 1 consultation, particularly given the significant differences between how the UK taxes income and capital gains?[7]

The Government clearly thought not, even though it described the changes as a "major reform".[8] Focused on avoiding what it described as an "undesirable outcome" of businesses not paying tax when they made disposals (because their historic realised losses offset future gains)[9], the

[2] HM Treasury and HMRC, *Corporate Capital Loss Restriction: Consultation on delivery* (29 October 2018), available at: *https://www.gov.uk/government/consultations/corporate-capital-loss-restriction-consultation-on-delivery* [Accessed 9 September 2020].

[3] HMRC, *Corporate capital loss restriction for corporation tax: draft legislation* (issue date of consultation 11 July 2019), available at: *https://www.gov.uk/government/publications/corporate-capital-loss-restriction-for-corporation-tax* [Accessed 27 August 2020].

[4] HM Treasury and HMRC, *Tax Consultation Framework* (March 2011), available at: *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/89261/tax-consultation-framework.pdf* [Accessed 9 September 2020].

[5] The Rt Hon Jesse Norman MP, *Hansard*, Public Bill Committee (2019–2021), Third Sitting, col 81 (Tuesday 9 June (morning) 2020), available at: *https://hansard.parliament.uk/commons/2020-06-09/debates/5927b7da-9829-4504-b795-7657d95cdd1a/FinanceBill(ThirdSitting)* [Accessed 9 September 2020].

[6] HM Treasury and HMRC, *Reforms to corporation tax loss relief: consultation on delivery* (May 2016), available at: *https://www.gov.uk/government/consultations/reforms-to-corporation-tax-loss-relief-consultation-on-delivery* [Accessed 26 October 2020], para.2.19.

[7] It seems that the writer is not alone in this view: for example, see the response of the Chartered Institute of Taxation to the initial Consultation on delivery (see CIOT, Technical Team, *Corporate Capital Loss Restriction: Consultation on delivery: Response by the Chartered Institute of Taxation* (7 February 2019), available at: *https://www.tax.org.uk/policy-technical/submissions/corporate-capital-loss-restriction-ciot-comments* [Accessed 9 September 2020], para.1.4).

[8] Consultation Document, above fn.2, para.1.22.

[9] In the Consultation Document, the Government highlighted that in some cases the historic losses that offset (now taxable) gains arose on disposals of assets that would now be exempt from capital gains tax (CGT) (for example, under the substantial shareholding exemption (SSE) or the exemption for real estate investment trusts (REITs)). See Consultation Document, above fn.2, para.2.3.

main objective was to ensure large companies pay tax when they make substantial profits (whether income or capital gains).[10] Unsurprisingly, the Government borrowed from its corporate income loss playbook where a similar mantra had been invoked. As a result, the changes represent a further means of increasing the tax base of larger companies.[11]

The original plan was to create a separate calculation for CCLR.[12] But, as a result of the consultation process, the Government was "persuaded" that this would add even more complexity to the UK tax system. So, instead, CILR has been complicated: a large part of Schedule 4 FA 2020 amends Part 7ZA of the Corporation Tax Act 2010 (CTA 2010) to embed CCLR within the CILR framework.

The remainder of Schedule 4 mainly contains technical changes to the recently rewritten Taxation of Chargeable Gains Act 1992 (TCGA) (mainly, but not exclusively, to deal with transition). It also includes the anti-forestalling provision announced (and taking effect) at Budget 2018.[13]

This note cannot deal in detail with all the provisions in Schedule 4 and so what follows is a summary of the main changes. In particular, this note does not consider the provisions in Schedule 4 that relate to specific sectors such as insurance, oil and gas and banking groups.

CILR to CILR plus CCLR

The starting point for understanding CCLR is the existing CILR rules in Part 7ZA CTA 2010.

CILR imposes a restriction on the use of carry-forward income loss reliefs—or, to be precise, three restrictions on the use of carry-forward income loss relief. The three restrictions follow on from the three main categories of corporation tax income loss relief that result from the F(No.2)A 2017 loss reforms (streamed trading losses, streamed non-trading deficits (NTDs) and flexible losses[14]).

For each category of loss, in broad terms, the applicable CILR restriction limits carry-forward relief to 50 per cent of the relevant profits. However, there are two points to note.

First, the rules provide for a "deductions allowance"[15] of up to £5 million per accounting period[16] allowing unrestricted offset of carry-forward losses to the extent of that allowance provided the allowance is specified in the company's tax return.[17] The purpose of the deductions allowance is to ensure that small and (many) medium sized businesses do not suffer restriction (as CILR only applies to profits in excess of the deductions allowance, companies with profits of less than £5 million should be able to access carry-forward income relief in full).

[10] Here, see Consultation Document, above fn.2, para.1.8 which echoes comments made in the May 2016 *Reforms to corporation tax loss relief: consultation on delivery*, above fn.6, para.1.16.
[11] Other measures that have the same effect are obviously CILR and also the corporate interest restriction (given the £2 million de minimis).
[12] Consultation Document, above fn.2, para.3.3.
[13] FA 2020 Sch.4, para.46.
[14] More precisely, these are: 1. trading losses that offset trading profits of the same trade; 2. non-trading deficits (NTDs) that offset non-trading profits only; and 3. all other losses that offset total profits (which include (most) trading losses and non-trading deficits that arise on or after 1 April 2017).
[15] CTA 2010 s.269ZW (company that is not a member of a group) and s.269ZR (company that is a member of a group).
[16] If a company is a member of a group (defined in CTA 2010 s.269ZZB) the £5 million annual allowance is shared between all group members that are within the charge to corporation tax (CTA 2010 ss.269ZR and 269ZS).
[17] CTA 2010 s.269ZZ.

Because there are three restrictions, the deductions allowance can be shared between the different categories of loss; how it is allocated impacts available capacity for each category of loss.

Secondly, because total profits are made up of trading and non-trading profits, there is double-counting of profits between the different restrictions—which unless corrected could risk doubling up loss capacity. As a result, carry-forward capacity for flexible income losses (those that offset total profits) is worked out by calculating 50 per cent of total profits (subject to the deductions allowance) and then deducting the amount (if any) of any streamed trading losses/NTDs used to offset trading and non-trading profits as allowed under the other restrictions.

For example, assume a company has total profits of 100 of which 80 are trading profits. It has trading losses available for relief under section 45 CTA 2010 of 40, and excess management expenses of 30. Ignoring the deductions allowance, it can use all 40 of its trading losses against its trading profits. It can offset up to 50 of its total profits by carry-forward reliefs generally. However, because it is using 40 of its trading losses, it can only offset 10 of its management expenses that year.

The above may appear very much "old" Finance Act, but because of CCLR, becomes "new" Finance Act again as CILR has had to be tweaked so that, when taken together, the different restrictions ensure that overall the "right" amount of carry-forward losses are restricted. Although this necessitates some very technical amendments to the existing rules, the economy of the drafting used to do this is particularly impressive.[18]

CCLR is contained in one section: new section 269ZBA CTA 2010.[19] Drafting wise, it mirrors each of the income loss restrictions, determining a "relevant maximum" for the amount of carry-forward capital loss relief available for offset against a company's "relevant chargeable gains"[20] (basically current year gains less current year allowable losses). The relevant maximum is basically 50 per cent of those gains (but, as with the income loss restrictions, loss capacity can be increased by allocating (and specifying) an amount as a "chargeable gains deductions allowance").[21]

As CCLR shares in the same deductions allowance (of up to £5 million) available in relation to income losses, there are only limited changes to the deductions allowance rules. These are in the main designed to ensure that specifying an amount as chargeable gains deductions allowance reduces the amount available for allocation to trading and non-trading profits within CILR.[22] This brings with it changes in nomenclature within the existing rules around non-trading deductions allowance,[23] with new definitions adding new complexity to the rules in Part 7ZA CTA 2010.

[18] The extension of CILR to include CCLR takes up no more than five pages of the Schedule (see FA 2020 Sch.4, paras 2–7 and 25–35). If the sections dealing just with non-resident companies are disregarded, the changes to CTA 2010 Pt 7ZA are very limited.

[19] FA 2020 Sch.4 para.2.

[20] See definition of "relevant chargeable gains" in CTA 2010 s.269ZF(2A) (inserted by FA 2020 Sch.4 para.5).

[21] FA 2020 Sch.4 para.2, inserting CTA 2010 s.269ZBA.

[22] In particular, see changes to CTA 2010 ss.269ZB and 269ZF made by FA 2020 Sch.4 paras 25 and 29 respectively.

[23] The former "non-trading profits" becomes "total non-trading profits", which consists of "non-trading income profits" and "non-trading chargeable gains". This re-naming impacts the definitions of "qualifying [profits]", "relevant [profits]" and the different deduction allowance options: see FA 2020 Sch.4 para.29.

During the Consultation on the changes, a number of people asked that the maximum £5 million deductions allowance be increased given it now had to cover a further category of losses.[24] Although intuitively this seems the right answer, Government modelling suggested otherwise: apparently, the "99% of companies will not pay additional tax" line rolled out under CILR still holds true even with capital losses now in the mix.[25]

Finally, the CILR rules in section 269ZF CTA 2010 that deal with computing the profits to which each restriction applies are amended. Chargeable gains are now dealt with as a separate source of profit (rather than as a constituent part of each of non-trading profits and therefore total profits).[26] This ensures that in-year reliefs can be allocated specifically against chargeable gains (or not) when working out the amount of "relevant chargeable gains" used to work out the relevant maximum under CCLR.[27] Given that carry-forward capital losses continue to offset chargeable gains automatically, the allocation of 1. deductions allowance and 2. in-year reliefs are therefore the only means by which a company can influence the "relevant maximum" for these losses.[28]

The remainder of Schedule 4 mainly provides for consequential amendments (most of which are connected with the extension of capital gains tax (CGT) to non-resident owners of UK land in Finance Act 2019 (FA 2019)) and the commencement provisions.

Other changes to capital loss relief?

As well as CILR, F(No.2)A 2017 brought a much needed modernisation to carry-forward loss relief. From 1 April 2017, "new"[29] trading losses and non-trading deficits can offset total profits[30] and groups can benefit from a new carry-forward group relief (that applies to all post 1 April 2017 income losses).[31]

Sadly, no such sweetener was offered to help the medicine of the CCLR go down. Although the Consultation Document referenced a desire to "bring the treatment of capital losses closer to other corporate losses and thus create a more modern loss relief regime in the UK",[32] the Government was unwilling to make any substantive changes. This was not just because of possible Exchequer impact (offsetting capital losses against income profits would result in a

[24] For example, CIOT, Technical Team, *Corporate Capital Loss Restriction: Consultation on delivery: Response by the Chartered Institute of Taxation* (7 February 2019), above fn.7, para.3.1.
[25] Consultation Document, above fn.2, para.2.10. The Government has separately said that around 200 companies will have capital losses restricted under CCLR each year: see HMRC, Policy paper, *Corporate capital loss restriction for Corporation Tax* (11 July 2019), available at: *https://www.gov.uk/government/publications/corporate-capital-loss-restriction-for-corporation-tax/corporate-capital-loss-restriction-for-corporation-tax* [Accessed 9 September 2020].
[26] FA 2020 Sch.4 paras 5 and 6, amending CTA 2010 s.269ZF.
[27] HMRC, Internal Manual, *Capital Gains Manual* (published 12 March 2016; updated 20 August 2020), CG-APP17, "Appendix 17 - Draft guidance on the Corporate Capital Loss Restriction" (CG-APP17), available at: *https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg-app17* [Accessed 9 September 2020].
[28] Examples of applying CCLR in various scenarios are set out in CG-APP17, above fn.27.
[29] "New" means arising on or after 1 April 2017.
[30] CTA 2010 s.45A and CTA 2009 s.463G.
[31] CTA 2010 Pt 5A.
[32] Consultation Document, above fn.2, para.1.23.

"large cost"), but also to maintain symmetry with the position under CGT for individuals and trustees.[33]

The basic rules around capital loss relief are therefore unchanged. Relief is only available against chargeable gains, and then only on a current year and, subject to CCLR, carry-forward basis.[34] Relief remains automatic—there is no ability to claim (or indeed disclaim) capital loss relief.[35]

As a result, CCLR creates a cliff-edge for new capital losses. If a company realises a capital loss in an accounting period, the economic benefit of that loss is now significantly diminished unless a gain is also realised in that period. As it can only be used on a carry-forward basis (the Government specifically rejected introducing a carry-back relief, in part because "[it] would not ensure that large companies pay some tax when making substantial capital gains"[36]), offset against any future gains will be subject to CCLR. Further, for many companies, there is likely to be a significant gap between disposal and so the period over which full relief is obtained is likely to be significantly extended.

Obviously, for companies within a CGT group, there is a possibility of transferring a loss to another group company under section 171A TCGA. But unless the accounting period of gain and loss coincide, CCLR applies as any transferred gain/loss is treated as accruing to the transferee at the time it originally accrued to the transferor.

However, there are some changes to the rules that apply to capital losses that can only be used against particular types of gain: connected party losses under section 18 TCGA and pre-entry losses within Schedule 7A TCGA. These are in response to comments made during the Consultation on the consequences of restricting losses that were already restricted.

For these losses, the legislation offers what is in effect a "loss swap" arrangement.

The relevant provisions are contained in paragraph 17 of Schedule 4 (for connected party losses—newly defined as "clogged losses") and paragraph 18 (for pre-entry losses). Although paragraph 17 is relatively easy to follow, the nature of the pre-entry loss rules means that making sense of paragraph 18, on first read-through at least, is almost impossible.

Despite the drafting differences, both provisions take the same basic approach. If, in the accounting period in which the company makes a gain against which it can offset these streamed losses it also has current year capital losses,[37] it is able to "swap" its carry-forward streamed

[33] HM Treasury and HMRC, *Corporate Capital Loss Restriction: Summary of responses to consultation and the Government's response* (Summary of Responses) (11 July 2019), available at: *https://www.gov.uk/government/consultations/corporate-capital-loss-restriction-consultation-on-delivery* [Accessed 9 September 2020], para.1.23 (the Government response to Question 3). In contrast, the fact that asymmetry now exists because individuals are not subject to any capital loss restriction is clearly seen as acceptable. It is unclear if "symmetry" between the rules for individuals and companies will feature in the recently announced review of CGT by the Office of Tax Simplification: see Office of Tax Simplification, *Capital Gains Tax Simplification Review: Scoping Document* (July 2020), available at: *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/900225/CGT_Scoping_document_July_2020.pdf* [Accessed 9 September 2020].

[34] TCGA s.2A.

[35] This is a further differentiation from the 2017 changes to corporation tax income loss relief.

[36] Summary of Responses, above fn.33, 10. Although part of the policy justification for the changes was the use by large companies of historic losses to offset new gains, this comment highlights that, for the Exchequer, CCLR is directed at increasing the tax base (and effective tax rate) of larger companies whilst maintaining a low headline corporation tax rate: after all, a carry-back relief would only benefit capital losses arising after April 2020.

[37] TCGA s.18(1) (inserted by FA 2020 Sch.4 para.6(1A)–(1C)).

losses for an equivalent amount of current year losses. This means the company can use its carry-forward clogged/pre-entry losses to offset the relevant gain without restriction, but the quid pro quo is that an equivalent amount of current year losses become carry-forward capital losses (and so subject to restriction under CCLR).[38] For clogged losses, a claim is needed; for pre-entry losses, it seems that the company simply chooses which losses it wants to offset against its pre-entry gains without restriction.

Insolvent companies: special rules

As with CILR, CCLR should generally only impact the timing of relief. But if a company is wound up before it has used up all its carry-forward losses, the restriction could impose an absolute tax cost. For this reason, the 2017 changes included a new terminal loss relief for trading losses in section 45F CTA 2010 (effectively dis-applying CILR in the final three years of trading). Representations were made that there should be a similar relief for capital losses: the result is paragraph 8 of Schedule 4 FA 2020.[39]

This is explained in the *Finance Bill Explanatory Notes* as follows:

> "A provision was added for companies in insolvent liquation [sic] which can now offset carried-forward capital losses against gains without the restriction being applied."[40]

The result is that, where a company goes into insolvent liquidation in the UK (or the equivalent in another jurisdiction), CCLR is effectively dis-applied.

Whereas the terminal loss relief for trading losses looks backwards from the point at which a trade ends (for a maximum of three years[41]), the insolvent company capital loss rules look forward with a starting point of commencement of winding up (when a new accounting period begins under section 12 CTA 2009). That new period (and all subsequent periods in which the company is being wound up) are defined as "winding up accounting periods",[42] and, in broad terms, new section 269ZWA CTA 2010 means that carry-forward capital losses can be used by the relevant company without any restriction to offset gains arising in any of its winding up period.

It is not quite as simple as this suggests though. CCLR still applies to the insolvent company. Section 269ZWA CTA 2010 simply allows the company to increase its deductions allowance to an amount which means carry-forward capital losses can (in practice) be used without restriction (with any increase capped at the lower of the company's current year net chargeable gains and its carry-forward losses).[43] This means that an insolvent company in theory could end up with a

[38] Examples of how these "loss swaps" work are contained in CG-APP17, above fn.27, ss.2 and 3.
[39] In Summary of Responses, above fn.33, the Government said it was considering the possibility of some form of relief on insolvency. The detail of what was proposed was only made public when Finance Bill 2019–2021 was published in March 2020.
[40] HM Treasury, *Finance Bill Explanatory Notes* (19 March 2020), available at: *https://publications.parliament.uk/pa/bills/cbill/58-01/0114/en/20114en.pdf* [Accessed 9 September 2020], para.97.
[41] CTA 2010 s.45F(3).
[42] FA 2020 Sch.4 para.8 inserting CTA 2020 s.269ZW(5).
[43] The deductions allowance is increased by the lower of either the company's chargeable gains in the relevant winding up accounting period or its carry-forward losses.

deductions allowance significantly in excess of £5 million in a given winding up accounting period.[44]

Secondly, to ensure that other (solvent) group companies do not benefit from this relaxation of CCLR, subsection (3) to section 269ZWA CTA 2010 excludes certain imported gains when working out the company's increased deductions allowance. Imported gains are defined as gains realised by the company on disposing of an asset that was previously transferred to it intra-group (so section 171 TCGA applied) and gains transferred to it pursuant to a section 171A TCGA election—but only where the transfer or, as the case may be, election was made in a winding up period. If however the section 171 transfer or, as the case may be, section 171A election is made by a group company that is itself in insolvent liquidation, this disregard of imported gains does not apply (reflecting the purpose of the provision—mitigating the potential impact of CCLR during insolvency).

Relying on an increased deductions allowance to achieve this objective means that the ability to switch off CCLR in insolvency is subject to the company specifying deductions allowance in its tax return: here, paragraph 9 of Schedule 4 creates a double "specifying" obligation.

A new subsection (1)(aa) to section 269ZZ CTA 2010 is added as a result of which the insolvent company is required to specify both its actual (that is, increased) deductions allowance and the deductions allowance that it would have had absent section 269ZWA.[45] This creates additional compliance complexity and, as the Government rejected the inclusion of a "deductions allowance" box in the company tax return form (CT600), there is clearly potential for this particular requirement to be missed in practice.[46]

Non-resident companies: the problem with one day accounting periods

A number of the provisions of Schedule 4 are directed at companies which, following the extension of CGT to non-resident owners of land in FA 2019, have one day accounting periods for corporation tax purposes.

A non-resident company that disposes of an interest in UK land comes into the charge to corporation tax only because of that disposal. Where they have no other source of profit within the charge to corporation tax (as was the case for most direct disposals until 6 April 2020[47] and will continue to be the case for many indirect disposals), their accounting period ends on the same day.

[44] See CG-APP17, above fn.27, which includes at Example 32 a company that has its deduction allowance increased by £9 million.
[45] CTA 2010 s.269ZZ(1)(aa).
[46] Summary of Responses, above fn.33, para.11.18. See also letter of 5 October 2018 from the Chartered Institute of Taxation to HMRC, available at: *https://www.tax.org.uk/policy-technical/submissions/carried-forward-corporation-tax-losses-compliance-obligations-ciot* [Accessed 9 September 2020].
[47] This is because any profits of a UK property rental business are brought into account to income tax until 5 April 2020.

This gives rise to a number of issues, particularly for companies with multiple one day accounting periods within a short period.[48] CCLR adds further issues (described by HMRC as "unintended consequences") for this particular class of taxpayer.[49]

Not only do one day accounting periods make it very likely that capital losses are always carried forward (subject to CCLR), the rules around the deduction allowance make that restriction even harsher. The maximum deductions allowance of £5 million is based on a 12 month accounting period. Where an accounting period is less than 12 months, that £5 million must be proportionately reduced.[50] The maximum deductions allowance for a one day period would therefore be less than £13,700.[51]

Amending the legislation dealing with corporation tax accounting periods might have allowed all the various issues around one day periods to be resolved in one go. But the Government appears to be taking a piecemeal approach—dealing with specific issues as they are identified, whether by guidance, concession[52] or, in relation to CCLR, rather complex legislation (set out in paragraphs 10, 39 and 45 of Schedule 4).

Given that non-residents with one day accounting periods are unlikely to have much familiarity with the UK tax system, this is perhaps less than ideal.

Deductions allowance and non-residents

Paragraph 10 of Schedule 4, introducing new sections 269ZYA and 269ZYB CTA 2010, addresses the problem of the "one day" deductions allowance.

The aim of these provisions is straightforward enough: it is to "allow companies with one-day accounting periods to be able to access the full £5 million deductions allowance per financial year".[53] The legislation itself is not as straightforward: the first draft (the July 2019 clauses) was completely rewritten and although the rewrite adds clarity, it does not add simplicity.

The provisions work by (in effect) deeming the non-resident to have a 12 month accounting period for the purposes of working out the amount of available deduction allowance. That 12 month period, which runs from 1 April to 31 March (to coincide with the corporation tax financial year),[54] can benefit from the maximum £5 million deductions allowance—but only if this special treatment is claimed.

The provisions only apply to "a company without a source of chargeable income"[55] throughout the entirety of the relevant financial year (basically a company that is only within the charge to corporation tax because of a chargeable gain). So a non-resident that sells its only UK rental

[48] See, for example, the apparently concessionary accounting period practice for funds and companies making more than four disposals in a financial year set out in HMRC, Guidance, *Register a non-resident company for Corporation Tax* (published 8 April 2019; last updated 22 June 2020), available at: *https://www.gov.uk/guidance/register-a-non-resident-company-for-corporation-tax* [Accessed 9 September 2020].
[49] Summary of Responses, above fn.33, para.11.16.
[50] CTA 2002 s.269ZW(3).
[51] And the amount will vary depending on whether or not the accounting period is in a leap year.
[52] For example, in relation to quarterly instalment payments (though now legislated for in FA 2020 s.26).
[53] Summary of Responses, above fn.33, para.11.16 summary.
[54] See CTA 2010 s.1119 for definition of "financial year".
[55] See section heading. However the legislation itself rewrites this as a company that "has no source of chargeable income" (see CTA 2010 s.269ZYA(1) and (2)).

property on 2 April 2021 cannot benefit because the property provided a source of income for corporation tax on 1 April 2021.

If the non-resident is a member of a group, the provisions are only available if no member of the group has a source of chargeable income in the deemed 12 month period. Care is needed here as the condition is drafted by reference to "each other company that is, at any time during the relevant financial year, a member of the group".[56] However, it is not enough that the other group member had no source of chargeable income whilst it was a group member—it must have no such source at any time in the relevant financial year (whether or not it was then a member of the group).

As a result, if a group consists of 20 non-UK companies and just one UK trading company, section 269ZYA CTA 2010 cannot apply. In such a situation, if one of the non-resident companies makes an indirect disposal, its deductions allowance will be limited to just under £13,700. Plus, as it seems that the normal group deductions allowance provisions then apply (as on that one day there are two group members within the charge to corporation tax),[57] there will be a lot of compliance for (if the gain is material) relatively limited benefit.

If paragraph 10 of Schedule 4 applies, the position should be relatively straightforward where there is only one disposal in a financial year—provided the company remembers to make the relevant claim.[58]

Things are a little more complicated if a company makes more than one disposal in a given financial year (and so has two or more one day accounting periods) and wishes to benefit from the full £5 million allowance for at least one of them.[59]

This is because the £5 million annual deductions allowance has to be shared between the various disposals. This "sharing" is provided for in subsections (7) to (11) of section 269ZYA CTA 2010. In broad terms, assuming the non-resident makes a claim for section 269ZYA CTA 2010 to apply to a particular disposal in a financial year (the relevant one day period being defined as a "claim AP" in section 269ZYA(4) CTA 2010), the amount of deductions allowance available for a particular disposal is dependent on the amount of deductions allowance applicable to other disposals in that financial year (whether or not a claim was made for those other disposals). This sharing is not based on a simple time of disposal rule: instead, a table in section 269ZYA(11) CTA 2010 sets out an order of priority between disposals for working out available deductions allowance.[60]

If the non-resident company is a member of a group (as defined within section 269ZZB CTA 2010), the same principle applies, with the maximum £5 million allowance shared between those group companies that make a disposal within the same financial year.[61]

[56] FA 2020 Sch.4, para.10(9)(b)(ii).
[57] CTA 2010 s.269ZR(1).
[58] CTA 2010 s.269ZYA(4). It may also need to make a declaration under CTA 2010 s.269YB and of course will need to specify the deductions allowance in its tax return (as both deductions allowance and chargeable gains deductions allowance). See CG-APP17, above fn.27, Example 23.
[59] CG-APP17, above fn.27, Examples 24 and 25.
[60] CG-APP17, above fn.27, Example 21, shows how this provision works in practice.
[61] CTA 2010 s.269ZYA(9)(b)(ii). See also CG-APP17, above fn.27, Example 20. Note that this is not the same as having a group deductions allowance.

As a claim under section 269ZYA CTA 2010 cannot be made before the end of the relevant financial year, paragraph 10 of Schedule 4 also introduces a new section 269ZYB CTA 2010 to provide for provisional claims for the special deductions allowance. By way of example, a company making a disposal on say 5 April may end up filing its tax return (for its one day 5 April "real" accounting period) before the following 31 March and so it cannot then make a claim under section 269ZYA CTA 2010. This is where section 269ZYB CTA 2010 comes in: the company makes a declaration that it will be making a claim, and on that basis, assesses (and pays) corporation tax.

This does not obviate the need for an actual claim once the financial year has ended (if no claim is made, the declaration falls away and additional tax due). Similarly, if the company (or a group member) subsequently comes within the charge to corporation tax in the relevant financial year, the declaration ceases to have effect (as one of the pre-conditions to making a claim is no longer met)—again, meaning an amended tax return and further tax is payable.[62]

Merging one day accounting periods

Where a non-resident company makes multiple disposals in a financial year (and so has multiple one day accounting periods), paragraph 39 of Schedule 4 means that the company can offset "same" financial year gains and losses against each other without CCLR applying.[63]

Paragraph 39 of Schedule 4 enacts new section 2A(1)(aa) TCGA. This has the effect of allowing a loss accruing to a non-resident company to be both carried forward (without restriction) and carried back to offset gains in different one day accounting periods in the same financial year. Like paragraph 10 of Schedule 4, this only applies to a company that is not otherwise within the charge to corporation tax in that financial year.

Special treatment for non-resident landlords newly within the charge to corporation tax

On 6 April 2020, non-resident companies carrying on a UK property business become subject to corporation tax on income under Schedule 5 FA 2019 and so, within the 2020–2021 financial year, will have a source of chargeable income. Absent special provision, they cannot therefore benefit from paragraphs 10 or 39 of Schedule 4 if they made a disposal between 1 and 5 April 2020. As this seemed harsh, representations were made, and so paragraph 45 was added to the initial draft clauses.

The effect of paragraph 45 of Schedule 4 is to merge the one day accounting period of the disposal (made between 1 and 5 April 2020) with the landlord's first full corporation tax accounting period (starting 6 April 2020) both for the purposes of capital loss relief (so a loss realised in the one day accounting period can be offset against gains realised in the accounting period beginning on 6 April 2020[64] and vice versa[65]) and for determining the maximum available deductions allowance available on the one day disposal (see paragraph 45(4), adapting section 269ZYA CTA 2010).

[62] CG-APP17, above fn.27, Examples 27–29.
[63] TCGA s.2A(3), as inserted by FA 2020 Sch.4 para.39.
[64] FA 2019 Sch.5 para.36.
[65] FA 2020 Sch.4 para.40(3).

Offshore collective investment vehicles and CCLR

Schedule 4 has one further surprise for a particular type of non-resident impacted by the FA 2019 changes; one that is not as helpful as those summarised above.

Paragraph 4 of Schedule 5AAA TCGA deems certain offshore collective investment vehicles to be companies for specified CGT purposes ("relevant purposes" within the legislation—which includes the purpose of applying the provisions of any Act relevant to the application of section 2B(4) TCGA).[66]

It was unclear from the July draft legislation whether such a deemed company would be a "company" for the purposes of CCLR. Although the application of the capital loss provisions is relevant for the purposes of applying section 2B(4) TCGA, the definition of "group" in section 269ZZB CTA 2010 adopts the meaning of "company" that applies generally for corporation tax purposes[67]: a deemed company is not a body corporate.

Clarity was provided in March 2020 in paragraph 11 of Schedule 4. This states that "relevant purposes" within paragraph 4 of Schedule 5AAA TCGA includes the definition of "group" in section 269ZZB CTA 2010[68] (but note not for any other grouping purposes).

So, if a Jersey property unit trust (JPUT) makes a disposal of UK land, the group deductions allowance provisions will potentially apply if any corporate unitholder has the relevant 75 per cent interest in the JPUT (because paragraph 4 of Schedule 5AAA TCGA only applies where the vehicle is tax-transparent for income, the corporate unitholder should as a result have at least one source of chargeable income (the rent from the UK land)).[69]

The result is not only that there is potentially a very different outcome for a "grouped" JPUT to that which would apply if a transparency election was made (where any gain arises directly to unitholders), but also means that a deemed company is treated less favourably than a "real" company (given a real company can benefit from CGT grouping and section 171A TCGA elections).

REITs and CCLR

Specific provision is also made for real estate investment trusts (REITs). This may seem counter-intuitive given that a REIT is exempt from corporation tax on chargeable gains arising in its property rental business.[70] But, as was the case for CILR,[71] something was needed to deal with the calculation of property income dividends (PIDs).

This is because a distribution of gains arising on a disposal of an asset used in a REIT's property rental business is treated as a PID (with shareholders, and not the REIT, taxed on any gain).

[66] S. Squires, "Finance Act 2019 Notes: Section 13: disposals by non-UK residents etc; and Schedule 1, paragraph 21: Schedule 5AAA to the Taxation of Chargeable Gains Act 1992—UK property rich collective investment vehicles etc" [2019] BTR 278.
[67] CTA 2010 s.1121.
[68] TCGA Sch.5AAA para.4 has not been amended.
[69] As a result, the normal deduction allowance rules apply, and not the provisions enacted by FA 2020 Sch.4 para.10.
[70] CTA 2010 s.535.
[71] CTA 2010 s.599(9).

A specific provision—section 550 CTA 2010—identifies whether a dividend is attributable to an exempt chargeable gain (or, as per the legislation, "relevant non-chargeable gains").

The definition of "relevant non-chargeable gains" refers to the main CGT exemptions in sections 535 and 535A CTA 2010 and implies gross gains: losses are irrelevant when a gain is exempt.[72] However, in practice, "relevant non-chargeable gains" appears to be interpreted (purposively perhaps?) as meaning "net" non-chargeable gains (reflecting the fact that, economically speaking, shareholders' profits are based on the net position). HMRC's *Investment Funds Manual* at IFM28035 comments:

> "Note that the amount of gains in this category is the amount as calculated for TCGA purposes, so will be reduced by indexation relief net of losses realised while in the REIT regime."[73]

On this basis, to work out "relevant non-chargeable gains", a REIT presumably undertakes a "shadow" CGT computation—and, if so, does it need to apply CCLR (and on what technical basis[74])? The resultant drafting challenge—to deal with this issue without creating others—was singularly failed at first attempt.[75]

This is now dealt with by paragraph 21 of Schedule 4 which states that CCLR is to be ignored when working out relevant non-chargeable gains: this provides clarity whilst avoiding any need to rewrite the basic CGT exemptions available to REITs.

There is one further dis-application of CCLR for REITs in the context of the new exemption for gains on sales of UK property-rich companies (introduced in FA 2019). If a REIT chooses to offset a pre 6 April 2019 residual business capital loss against any such gain, CCLR does not apply (see paragraph 20 of Schedule 4).

And finally, commencement…

CCLR (and the other related changes) applies to all companies on 1 April 2020. Like CILR, if a company has a "real" accounting period that straddles that date, the commencement rules require that period to be split into two separate (deemed) accounting periods: one (AP1) ending on 31 March 2020; and the other (AP2) beginning 1 April 2020, with CCLR applying in AP2. As gains (and losses) are recognised on a realisation basis, apportionment of amounts between AP1 and AP2 is thankfully a lot more straightforward than it was for CILR.

Again, as was the case for CILR, the commencement rules are not intended to impact same "real" year capital loss relief. The Summary of Responses confirmed this:

[72] Plus, as a technical matter, losses accruing to the property rental business are not "allowable losses" in any event given TCGA s.16(2).

[73] HMRC, Internal Manual, *Investment Funds Manual* (published 5 July 2019; updated 13 October 2020), IFM28035, "Real Estate Investment Trust: Distributions: attribution rules: category (d) - gains of the property rental business: CTA2010/S550(2)(d)".

[74] The prescriptive nature of CTA 2010 Pt 7ZA means that a loss must be within TCGA s.2A to be subject to restriction and for REITs, as the loss is not an allowable loss (technically) it cannot be within TCGA s.2A.

[75] The July 2019 draft legislation, see above fn.3, included a new CTA 2010 s.535(10) which provided that CCLR was to be ignored when working out the amount of a gain arising on a property rental disposal (notwithstanding that under TCGA s.2A losses offset the total gains arising in an accounting period, not individual gains).

> "As previously set out there will be no restriction applied to capital losses arising in the transitional period where these can offset capital gains arising in either of the notional periods."[76]

To enable current "real" year capital losses to be accessed in each of AP1 and AP2 without restriction, paragraph 44 of Schedule 4 modifies both section 2A TCGA and Part 7ZA CTA 2010. It would have been a lot easier to have the rules apply from the start of an actual accounting period (noting that the timing of gains is, in any event, often within the control of the taxpayer), but the Government felt this created a risk of "one company having an unfair advantage over another purely because they have different accounting periods".[77]

Instead, a company that makes one or more disposals in a straddle period has to calculate its net chargeable gains position in relation to each of AP1 and AP2 separately, taking account of both current year and carry-forward capital losses (and, in AP2, CCLR).

If a net loss arises in either AP1 or AP2,[78] it can offset any net gain arising in the other deemed period.[79]

So, if the company has a net loss in AP1, but a gain in AP2, the AP1 loss offsets the AP2 gain under section 2A(1)(a) TCGA and CCLR is irrelevant. If, however, the company has a net loss in AP2, but a gain in AP1, that AP2 loss offsets the AP1 gain on a similar basis (a special "carry back"). The end result determines the amount of chargeable gains to be included in total profits for its "real" accounting period.

The modifications to Part 7ZA CTA 2010 are slightly more challenging to work through (linked to the complexity of CILR). Paragraphs 44(4)(a) and (b) of Schedule 4 ensure CCLR is only relevant to AP2 (and, because of paragraph 44(3)(b) of Schedule 4, only relevant to carried-forward losses from earlier "real" accounting periods). Paragraph 44(4)(c) of Schedule 4 deals with the calculation of modified total profits within CILR given that capital losses are excluded when working out modified total profits for AP2 (see section 269ZF(4) CTA 2010). The easiest way to understand this in practice is to work through the examples included in HMRC's draft guidance on CCLR.[80] No wonder the Government has been in discussion with software providers: after all, in the real world, companies will be heavily relying on their tax software to apply these rules.

The commencement provisions also include an anti-forestalling provision in paragraph 46 of Schedule 4. This is now effectively spent: the legislation can no longer be forestalled.[81] The provision was announced at Budget 2018 and HMRC's draft guidance simply lifts, word-for-word, the very limited examples included in the Consultation Document and so are not likely to be of

[76] Summary of Responses, above fn.33, para.6.2.
[77] Summary of Responses, above fn.33, para.6.1.
[78] FA 2020 Sch.4, para.44 applies only to "allowable losses accruing to the company in the [relevant deemed period] so far as they exceed the chargeable gains accruing to the company in the [relevant deemed period]".
[79] FA 2020 Sch.4, paras 44(3)(a) and (b).
[80] CG-APP17, above fn.27, Examples 7–10.
[81] Going forward, FA 2020 Sch.4 para.23 amends the broadly drafted CILR regime anti-avoidance provision (see F(No.2) A 2017 s.19) to cover capital losses. For commentary on this provision, see Greenbank and Moncrieff, above fn.1, 554–555.

any particular assistance to anyone who, in the last 18 months or so, had to think about these rules.

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Accounting periods; Capital losses; Carry-forward reliefs; Collective investment schemes; Corporation tax; Non-resident companies; Real estate investment trusts; Winding-up

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