

Driving Facts

TAX NEWS

Utilisation Of Losses

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It is always intended that a business will be consistently profitable, but it is not unusual for a company to experience at least one loss making year in its lifetime. The key from a corporation tax perspective is to ensure that the loss is utilised in the most efficient way to maximise cashflow and minimise the company's overall tax liability. This article examines some of the different types of losses that can arise and the options for their utilisation.

In certain circumstances by changing the company's financial year end the gain can be "forced" into the desired corporation tax period. This strategy can be difficult to implement successfully and early action and planning is required to increase the chance of success.

The final issue we will consider regarding trading losses is the way in which they follow the trade which created them. When the trade ceases any unused losses are effectively stranded and any potential relief wasted.

The first important point to make is that when we are talking about losses in this article, we are referring to losses calculated for tax purposes and there can often be a significant difference between this and the loss shown in the accounts. There are broadly four types of tax loss – trading, capital, non-trading loan relationship and schedule A. As non-trading loan relationship losses rarely arise in practice we have ignored them for the purpose of this article

Capital Losses

Capital losses can arise on the sale of land and buildings and in certain circumstances the sale of goodwill. If the goodwill is purchased after 1 April 2002 however, it does not fall within the capital gains regime and is instead governed by the new intangible fixed assets rules which are outside the scope of this article. Capital losses are automatically offset against capital gains of the same corporation tax period and then carried forward against the next future gains.

Trading Losses

Current year trading losses of a stand alone company can be offset against other taxable profits of the same accounting period, carried back against total taxable profits of the previous 12 months or carried forward against future profits of the same trade.

Schedule A Losses

Losses on property rentals undertaken by the company can be offset against total profits of the same accounting period and then indefinitely against any future period in which the rental business still continues.

Normally these rules cause few problems and the recommended strategy would be to set off current year trading losses against other current year profits, carry back the balance of such an amount to absorb the profits of the previous 12 months, then carry forward any residue. This gives the best cash flow advantage but may not always give the best solution. What if the current year loss arises from an isolated poor trading year and it is expected that significant trading profits will be made in the following year? If these profits are likely to bring the company into the marginal rates of Corporation Tax of 32.75% consideration can usually be given to carrying forward the loss and obtaining corporation tax relief at this marginal relief. However even if the overall tax saving is greater; it is often the case that the immediate cash flow advantages of a repayment outweigh the long term benefits.

Group relief

So far this article has considered the case of a stand alone company, but if the loss making company is part of a group, further options can be opened up for the use of the losses. Depending on the type of loss, all or some of it can be surrendered to another group company in the year the loss arises. This can sometimes provide the most tax efficient route for the group as a whole if the group members are paying corporation tax at different rates. The rules concerning group relief are complex and we will explore them in greater detail in a later edition of Tax News.

In conclusion, although the loss relief rules can appear relatively simple, careful planning must be undertaken to ensure any loss is utilised in the optimum manner.

Where a company is likely to realise a capital gain on the sale of an asset around the time a trading loss arises, it is important to note that the gain has to occur in the same corporation tax accounting period as the loss or the previous 12 months for relief to be obtained. The way in which corporation tax return periods operate means that a corporation tax period may not be the same as the company's financial reporting period.

Redundancy Pay

With effect from 1 February 2007 a weeks' pay for redundancy purposes will increase to £310 (from £290). This figure is also used to calculate the basic unfair dismissal award. The maximum compensatory award for unfair dismissal has also increased to £60,000 (from £58,400)

Age Discrimination

The new age discrimination law came into effect on 1 October 2006, and its impact on businesses is enormous. As with all other types of discrimination, compensation is uncapped, consequently the risk needs to be carefully assessed. Whilst in certain circumstances employers will be able to discriminate if it can be objectively justified, they should however tread carefully and must have evidence in support of their claims. Commercial justification could for example be used as a reason for setting a maximum recruitment age, due to the training requirements of the post. As both young and old are now protected, the legislation and potential pitfalls are extremely complex.

All employers should review and update their policies, practices and procedures, and train managers on the new laws so here are a few pointers to get you started

Recruitment

The recruitment process should not involve any consideration of age, therefore applications should not ask for date of birth. Advertisements must be carefully worded and should not specify any upper or lower age limit. Wording such as "young", "old" "energetic", "mature" or even "graduate" should be avoided, similarly care should be taken in asking for a number of years experience, as this could be seen to discriminate against young people.

Training

Training and promotions must be open to all regardless of age. As there is now scope for employees to work beyond the default retirement age of 65, this is particularly important.

Service Related Benefits

Differences in pay and benefits based on experience or length of service, such as holidays and long service awards are likely to lead to claims of indirect discrimination, because older workers are more likely to have completed the required service or experience. The regulations do however allow employers to continue to use service related pay and benefits provided that the period of service does not exceed five years.

Retirement

There will be a default retirement age of 65 and employers must notify their employees of the intended retirement date at least six months and not more than twelve months before that date, and that the employee has the right to request working beyond retirement.

If the employee makes a request to work beyond retirement age, in the period of three to six months before the retirement date, then the employer must consider the request.

If the employer does not wish to allow the request then a meeting must be held to discuss the position and the employee must be notified of the decision. The normal appeals procedure applies.

If the correct procedure is not followed then the employee may be awarded eight weeks pay and the dismissal may be deemed to be automatically unfair

Redundancy

The upper age limit for redundancy has now been removed for all redundancies after 1 October 2006.

Company Cars

We are aware that there are several schemes being marketed to get employees out of the benefit for the private use of company cars. Many involve the sale of a car by giving an interest free loan to the employee. The car is then repurchased, at its market value, thus repaying part of the loan, relying on the HM Revenue & Customs approved mileage rates for business use, to make up the deficit.

In our opinion the schemes are unlikely to work unless there is significant business mileage, and in most cases salesmen do not do a great deal of business mileage. There is also the question of how the vehicle is insured as the car is no longer a company car and would probably not then be available to customers, cutting down on the business mileage. You would also need to carefully consider how the loan would be repaid, or the car be repossessed, should the employee leave.

National Minimum Wage

The National Minimum Wage increased with effect from 1 October 2006. The rates are now as follows:

Age of worker	Current rate	New rate
22+	£5.05	£5.35
18-21	£4.25	£4.45
16-17	£3.00	£3.30

16 and 17 year old apprentices are exempt from the young workers rate. More information can be obtained from a detailed guide available at www.dti.gov.uk/er/nmw or from the helpline on 0845 6000 678

Email Scams

HMRC website has reported a scam involving an e-mail supposedly sent by them and asking for bank details. Visit www.hmrc.gov.uk/news/scams.htm for further information.

If you have any queries on any of the subjects covered in this newsletter or on any other tax or company secretarial matter please e-mail us at taxteam@trevorjones.uk.com or call helpline on 0161 475 4700.

These articles are of a general nature and specific advice should be obtained before they are acted upon.