Corporate Capital Loss Restriction – comments on draft legislation

To: reform.capitalloss@hmrc.gsi.gov.uk

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Introduction

1. The British Property Federation (BPF) represents the real estate sector – an industry which contributed more than £100bn to the economy in 2018 and supported more than 2 million jobs. We promote the interests of those with a stake in the UK built environment, and our membership comprises a broad range of owners, managers and developers of real estate as well as those who support them. Their investments help drive the UK's economic success; provide essential infrastructure and create great places where people can live, work and relax.

2. The sector is one of the most successful in the world at attracting domestic and overseas long-term investment capital into the renewal of the UK's towns and cities. Such large, long-term, patient investors are critical to the urban redevelopment and regeneration of our country's towns and cities.

3. We appreciate the opportunity to respond the draft legislation. Our primary concerns are summarised below:

   a. **Many businesses will not pay tax on their economic profit as a result of these rules -** these measures will create a cliff edge where gains and losses arise in different accounting periods.

   b. **The anti-forestalling rules are very broadly drafted** – this will create uncertainty, even for purely commercial arrangements. As such, we would recommend that a white list of acceptable scenarios is published to provide certainty for those looking to making a capital gain or loss.

4. While we appreciate that this is no longer a policy consultation, it is important to reiterate our concerns around combining the treatment of capital losses within the income loss restriction rules. The distinction between income and capital is a key feature of the UK tax system – it reflects the fact that the predictability and timing of gains and losses is fundamentally different to the basis on which income profits arise. To adopt one of the classic caselaw tests applied in determining whether an item is income or capital in nature, income is generally "recurrent", whereas capital is "one-off". Therefore, adopting a measure which, for income losses, is designed to affect the timing of relief only will in many cases result in an (effective) absolute restriction of capital losses and as a result risks undermining the principle that a "the tax paid by a company is reflective of its net capital gains over the long term".

5. The real estate sector will be one of the few industries bearing the brunt of these changes. Given the irregular and bulky nature of transactions in the sector, "one-off" gains and losses often accrue in different accounting periods. This means that a property business's "capital" returns can only really be measured over time, as gains and losses (and the tax thereon) net out. Any measures – such as these – that substantially divorce a business's tax profits from its economic profits make it increasingly challenging for investors to determine with any certainty the viability of particular investment propositions. Given how tight the viability of new development is – particularly in "left behind" parts of the UK – the proposed restriction on capital losses cannot but negatively impact the level of investment flowing into our towns and cities.

6. We cannot stress this concern strongly enough – not least because the issue was not adequately acknowledged in the government's summary of consultation responses. It is important to ensure that the tax paid by a company should adequately reflect their net capital gains over the long term, or at least the medium term. As such, we continue to recommend that the rules should allow for greater flexibility to carry back (and limited carry forward) of losses in full (as outlined in our original response on 25th January).

7. In addition to our overarching concern with the policy itself, we have provided some comments on the draft legislation within the appendices. Our appendices are structured as follows:

   Appendix I: One day accounting period concerns

   Appendix II: Proposed examples to be included in a white list of scenarios which would not be caught by the anti-forestalling rules

   Appendix III: Summary of other concerns with the draft corporate capital loss restriction legislation

8. If you would like to discuss any aspect of our response in more detail, please get in touch.

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Appendix I: One day accounting period concerns

One day accounting period

9. At section 11.16, the Summary of Responses references certain measures to address the position of companies that have one or more "one-day accounting periods" in a given financial year. We welcome the government's willingness to provide a policy solution to the issues that could otherwise arise for such companies, both in relation to the changes to carry forward relief for capital losses (paragraph 32) and also the availability (and quantum of) any deductions allowance (paragraph 8, inserting a new s269ZYA and s269ZYB in Part 7ZA Corporation Tax Act 2010 (**CTA2010**)).

10. The companies impacted by these provisions will be non-UK resident companies within the charge to corporation tax as a result of making an indirect disposal of UK land within Schedule 1A TCGA 1992 (companies that directly own UK land are likely to be carrying on a property rental business and so be within the charge to corporation tax on income). As a result their nexus with the UK may well be very limited (particularly if the investee company is a collective investment vehicle where any interest in the investee is a "substantial indirect interest in UK land"). Such companies are therefore likely to have little familiarity with corporation tax (or CGT) to date and so it is important that any rules that impact them are as straightforward and simple to understand as possible.

11. In that context, we consider that certain aspects of these provisions need clarification and possibly amendment. In addition, we ask that clear guidance be published, with examples, to ensure that taxpayers are alerted to what these rules mean in practice (particularly in relation to the deductions allowance). This is because the companies within the scope of these rules will, by definition, have limited or no knowledge of the UK tax rules in practice. Given that the changes will impact disposals made on or after 1 April 2020 (in relation to which negotiations may have commenced some months earlier), it would be helpful if such guidance could be issued in advance of commencement.

12. We set out our comments below:

General

Companies without a source of chargeable income - length of accounting period

13. The amendments made by paragraph 8 and 32 apply where a company has an accounting period only because it has a chargeable gain (so that an accounting period has commenced under s9(3) Corporation Tax Act 2009 (**CTA2009**)). That accounting period will end on "the company ceasing to be within the charge to corporation tax" (s10(I)(h) CTA 2009) which we understand is generally considered to be at the end of the day on which the gain was realised. Hence, a one-day accounting period.

14. We understand, based on discussions with HMRC relating to Schedule 5AAA TCGA, that in practice HMRC has been willing to accept that, if a non-resident makes regular disposals over its period of account, the one-day rule will be disregarded so that the (corporation tax) accounting period continues for the default 12 months. (This in effect assumes a continuing source of gains as a result of the regularity of disposals

15. We also understand that this practice is intended to be extended to apply to any company (or deemed company) that is a collective investment vehicle for the purposes of Schedule 5AAA, regardless of the regularity of disposals (although this will be only be relevant where there has been at least one disposal in a year). This practice has now been reflected in guidance on registering for corporation tax at

https://www.gov.uk/guidance/register-a-non-resident-company-for-corporation-tax. We note that this practice provides a sensible outcome in terms of administration.

16. However, where a company is, as a result of this HMRC practice, treated as having an accounting period of 12 months, it still (as a result of s10(1)(g)) arguably has a shorter one-day accounting period as far as legislation is concerned. Are such companies within the scope of paragraphs 8 and 32 (assuming any other conditions are met, if applicable)? For paragraph 8, the existence of a one-day accounting period determines if a claim can be made; we note that for paragraph 32 there could be a different outcome in practice only if the end date of the (in practice) 12 months accounting period is not 31 March (the end of a financial year).

17. Please can you clarify how these provisions will work in relation to HMRC's practice.

18. Finally, taking account of the various amendments now being proposed to address unintended consequences of the one-day accounting period (including these provisions as well as the changes to QIPs referenced in the Summary of Responses), we ask that the government considers amending s10 CTA 2009 to put the status of affected non-resident companies on a statutory footing so the position is clear. This could, depending on the approach made, allow significant simplification of the provisions in paragraph 8 – and minimise the need for specific amendments to other legislative provisions.

Paragraph 8

Section 269ZYA(1)(c)(ii)

Membership of a group

19. The "group" test is by reference to the company being a member of a group (within s269ZZB) "at all times" in the financial year. Please can further examples of the application of the broader CILR group test be included in guidance in relation to the extension of normal group relief rules in s269ZZB(7) to assist non-residents assess if the condition is met.

No source of chargeable income – group

20. Investment in UK real estate means that in many cases, a company (Holdco) will wholly own a UK property rich company (Propco). Propco will be within the charge to corporation tax on income as a result of Schedule 5 Finance Act 2019 from 6 April 2020.

21. We assume in such a case Holdco is intended to be excluded from the benefit of these provisions as a result of s269ZYA(1)(c)(ii). This means Holdco will only be entitled to a maximum 1/365th of the deductions allowance for its accounting period.

22. As a result, this provision will only be relevant to a fully non-resident group that has no subsidiaries that own UK property or otherwise have UK taxable activities at any time in the year. We ask that the guidance make clear the type of group/company it is directed at.

23. However, if Holdco say owns more than one Propco and makes "regular disposals", our understanding of HMRC's practice suggests that Holdco will be treated as a member of the same group for a full accounting period (and so could have access to the entirety of the £5m through the group deductions allowance process). Is this difference in treatment intended?

Company or group deductions allowance?

24. Assuming Holdco is grouped with a single Propco, so s269ZYA does not apply.

25. Unless and until Holdco makes a disposal, Propco will be entitled to a company deductions allowance under s269ZW. At the point Holdco makes a disposal it is a company within the charge to corporation tax and so, assuming that at any time in the relevant day, Holdco and Propco are grouped, s269ZR would apply to each of Holdco and Propco: in relation to Holdco for its one-day period and for Propco, its full accounting period.

26. If Propco is degrouped as a result of the sale, we assume that notwithstanding the "at any time" requirement, the sale is taken to have effect at midnight on the start of the day and so Propco is not a member of a group with Holdco: is this correct? This would seem the appropriate result and simplify any administrative requirements as Holdco would then be a stand-alone company on that one day -and Propco would not be treated as grouped simply because its parent sells it.

27. If Holdco disposes of part of its shareholding in Propco, Holdco and Propco may be grouped throughout the entire one-day. As a result of s269ZR, Holdco and Propco will need to comply with the group deductions allowance processes for either company being able to claim any part of the deductions allowance.

28. In practice, as Propco would continue to be entitled to a non-group deductions allowance for 364/365th of its accounting period, there may be limited benefit for Propco; but unless the nomination/return requirements are is complied with, then Holdco will have no entitlement to a deductions allowance: is this intended? (We note that the provisions do not deny deductions allowance to Holdco in such circumstances, but query whether the administrative requirements could be simplified where there is a single Holdco/Propco on the basis of proportionality.)

Section 269ZYA(2)

29. Please include clear and simple examples of how the alternatives work in the guidance.

30. If, by happenstance, two or more Holdcos are grouped, and make a disposal on the same day, we note s269ZR is disapplied and so there is no requirement for "group" information to be provided to HMRC. This should be made clear in the guidance - i.e. explaining the impact of the tailpiece to s269ZYA(2) on the administrative requirements.

Section 269ZYA(3)

31. We ask HMRC to reconsider the drafting of this provision, particularly subsection (b) and the tailpiece.

32. Our assumption is that, assuming Holdco is not part of a group for these purposes, if it makes more than one disposal in a financial year, then this allows Holdco to allocate the company £5m deductions allowance between the various disposals (ie so if it makes three disposals, it has three one-day accounting periods and can "specify" three separate deductions allowance (one per disposal/accounting period) in that year, subject to the total specified allowances not exceeding £5m. (In effect the £5m per accounting period deductions allowance becomes a £5m per financial year deductions allowance.)

33. This is of course subject to the "caps" in s269ZYA(2)(b) and (c) not being applicable.

34. This follows on from the Explanatory Notes: "[s269ZYA(3)] defines the available deductions allowance amount as £5 million less the amounts of deductions allowance already claimed or used (or which could have been claimed) by any company within the group during the financial year."

35. On this basis (again assuming neither s269ZYA(2)(b) or (c) apply at any time), the intention would appear to be that on any one given disposal, the available deductions allowance is the £5m less the amounts (up to £5m) "applicable" to the other disposals/accounting period.

36. The issue is then how you determine the amount applicable to the other disposals – both generally but also noting that if Holdco is filing a separate CT return for each disposal, it is possible a return may be required to be filed for the first disposal before the second is made: we are not clear as to how the legislation addresses this issue.

37. The tailpiece references the amount in (3)(b) - which is relevant to each of the three accounting periods - as the amount that the company "would have been entitled to claim in respect of each accounting period".

38. Unless s269ZYA(2)(b) or (c) apply to limit deductions allowance "available" on a particular disposal, the amount that Holdco "would be entitled" to claim in relation to each one-day period is dependent on what is available in each other one day period. The definition is therefore circular.

39. Further, it is unclear how this condition relates to the requirement in Part 7ZA to specify deductions allowance. The provision appears intended to set the maximum amount available - this follows on from the reference to "available" deductions allowance, the limits in s269ZYA(3)(b) and (c) and the disapplication of s269ZR to ZY) - and "would have been entitled to claim under this section" supports that.

40. However, a deductions allowance, albeit available, cannot be used in calculating any of the relevant maxima unless it is specified in a tax return - both generally (s269ZZ) and for Holdco specifically as a chargeable gains deductions allowance (s269ZBA).

41. The drafting suggests that no account is taken of the amount actually specified by Holdco in relation to a different accounting period in the financial year when quantifying amounts in s269ZYA(3)(b). However, the reference in the Explanatory Notes to "used" suggests that whether an allowance has been specified in a return is a relevant factor in working out the relevant amounts.

42. For a single Holdco, in practice, it could perhaps be assumed that it would look to maximise the deductions allowance on its first disposal (and so specify the full amount then) and so this may not be an issue in practice.

43. But there is a difference if Holdco is a member of a group, as then the deductions allowance may be "shared" among group members. This raises first the issue of how this circular test applies (what "would be able to be claimed" by other group members on their (future) disposals given the inter-dependence?) and secondly, what happens where a company specifies less than its otherwise maximum entitlement for commercial reasons.

44. Therefore, please clarify how the two requirements interact.

45. Given the limited UK tax experience of the companies that will be within the scope of this provision, we recommend that the drafting is revisited so that the application of these provisions is as clear as possible from the language used. Guidance can then supplement this with examples but should not be used a substitute for clear legislation.

Section 269YZA(4)

46. This requires a claim to be made per accounting period. We assume from this that, again assuming three disposals, Holdco could make a claim for one only - and so for each of the other two disposals, its maximum deductions allowance would be 1/365 x £5m (given the "would be entitled" in s269ZYA(3)(b)) - given the drafting of s269ZYA(3), how do the different periods interact in determining the available amount on the first disposal?

47. If however Holdco intended to make the same claim for each of its one-day accounting periods within a financial year, would it be possible for the legislation to allow that alternative single claim - ie so there is "one" claim only per financial year?

Section 269ZYB

48. Please can the guidance be clear as to the appropriate placement of such a declaration in a return (we note here there was a lack of clarity about where to specify deductions allowance under CILR, and hence the importance of certainty within the guidance).

49. We ask that the guidance include a specific (and easy to understand) example of a situation where a declaration has been included in a return, but then ceases to have effect under s269ZYB(4)(c).

50. In any event, given s269ZZA (excessive specification of deductions allowance), are ss269ZYB(6)(7) needed? This is because, if the declaration has been included, and the tax return assumes a particular level of allowance, at the point the declaration ceases to be of effect, that allowance could be "excessive" as compared to the 1/365 x £5m alternative.

Claims v declarations v specify

51. We ask that HMRC consider possible means of simplifying the compliance obligations placed on a non-resident company to obtain an appropriate amount of deductions allowance where it has a "one-off" disposal. Under Part 7ZA, the company may first have to "declare" under s269ZYB in its return. It then has to claim under s269ZYA.

52. The only deductions allowance that can be relevant to it is a chargeable gains deductions allowance - yet it will have to specify in its return both a deductions allowance and a chargeable gains deductions allowance (s269ZW and s269ZBA). Failure to specify means that its declaration and claim have no effect. (We note that this too should be spelled out in the guidance – particularly given the experience in relation to CILR: note that if it is sufficient to simply assume an element of allowance in the computations for these purposes, then this should be explained – i.e. what would be accepted as meeting the requirement.)

53. For such companies, could the process be streamlined - so there is a single claim/specifying: ie if Holdco makes the claim, could that be deemed to be specifying a relevant amount under both s269ZZ and s269ZBA?

54. In this context we ask the Government to reconsider its rejection of including a specific box in the tax return to deal with deductions allowance (see 11.18 of the Summary of Responses). We are aware from discussions with HMRC on the movement of non-resident landlords to corporation tax that consideration is being given to amending the CT600 in any event to assist such companies in relation to compliance, and would hope that a deductions allowance "box" could easily be included as part of any changes without adding material costs. We do not agree that the inclusion of a box would impose an additional burden: all companies with any carry forward losses have to specify the allowance in order to be able to use (some or all) without restriction given how the measure is structured, and a box would be of benefit to all those

companies. A simple note that it is only relevant if you have carry-forward losses of any type should suffice to ensure that it does not place an additional burden on other companies.

55. A "box" of this type would also be useful for those companies where the application of the restriction is only relevant because of a "one-off" disposal - i.e. the group has capital losses but not income losses - where (in compliance terms) there may be a risk of the company not being aware of CILR in practice.

Holdco/Propco not within s269ZYA

56. In the event that a Holdco has two or more UK Propcos, it would be a member of a group and its maximum entitlement determined by reference to s269ZV. On a disposal of a UK property-rich company, Holdco would be a member of a CGT group with the remaining Propco on that day. In such a case, we assume that HMRC would accept that it is reasonable for Holdco to make a s171A election (given s171A(1)(b)) and transfer any resulting gain to a Propco - the Propco would be able to use its carry forward losses (if any) with the benefit of its deduction allowance allocation. This is in accordance with the policy and principle that the group deductions allowance is a benefit to the group, for it to allocate as between "group" profits and gains as it chooses.

57. We ask that this be included this in the guidance as an example of something that would not trigger the TAAR (which is to be extended to capital losses within the context of the restriction by paragraph 20).

Definition of group

58. ‘‘Group" is defined in s269ZZ. The definition applies to "companies" where the relevant tests are met (75% ownership of ordinary share capital or equivalent for "companies" without share capital and unincorporated associations).

59. Under paragraph 4, Schedule 5AAA TCGA, certain entities are deemed to be a company for limited purposes (namely, Schedule 5AAA and the purposes of applying s1A(3)(b)(c) and s2B(4) TCGA "and the other provisions of this or any other Act so far as relevant to their application) in relation to the vehicle"). This would include for the purposes of determining and obtaining relief for capital losses. We assume that this would extend to the capital loss restriction within Part 7ZA (as it is an "other Act" relevant to the application of s2B(4)). Please confirm.

60. In that case, please confirm how a Jersey property unit trust (or equivalent) (**JPUT**) that is deemed to be a company under Schedule 5AAA would be regarded for these purposes - i.e. whether as a stand-alone company (and so entitled to an allowance within s269ZW) or as a potential group member.

61. The status of a such a JPUT is relevant to s269ZYA and paragraph 32 because if a JPUT is a group member, these provisions could never apply if the JPUT had a single member holding at least 75% - its transparency for income means that its corporate investors are within the charge to corporation tax on income.

62. "Company" within the CTA2010 references bodies corporate and so on that basis we would assume that a JPUT would not be regarded as a company within s269ZZ (i.e. this provision is directed at "real" companies, and not deemed ones).

63. Further, the definition of group was cast in the context of a measure originally designed for income losses only, and a JPUT would not be a "company" in relation to income - its treatment as a company is for limited purposes only.

64. This seems an appropriate result given that a JPUT cannot benefit from grouping as it does not have ordinary share capital (and, in discussions with HMRC on the 2019 changes to the CGT treatment of non-resident (and earlier discussions in 2016/2017 on SSE), we were told that there was no intention to treat deemed “shares” in a JPUT as ordinary share capital).

65. However, given the language of paragraph 4(3)(b), the position is not clear-cut. We also acknowledge that there may be policy reasons for taking a particular approach - if a JPUT is grouped, then a single £5m would apply as between its capital gain and the income arising from its asset on which its 75% investor is taxable; but if a JPUT is not grouped, then there are disadvantages as reliefs otherwise available as between “true” companies would not be available to either investor or JPUT (for example, the investor could not benefit from SSE and the JPUT could not be party to a s171A election): i.e. treating a JPUT as a “company” for some, but not all CILR/CCLR purposes would mean inequality of treatment with “real” companies. Similarly, we note that if a transparency election is made, the gain would be that of the investor (and so a single deductions allowance would apply to gain and income at investor level).

66. If HMRC’s view is that a deemed JPUT company is to be regarded as a “company” within s269ZZ, and so a potential group member, we ask the government reconsider allowing a deemed company to both be a member of a CGT group and to be eligible for SSE, such that the same options available to a real company (in terms of s171A elections etc) are available to a JPUT - i.e. creating a level playing field.

67. If a JPUT were to be a company within s269ZZ, we ask that this is referenced specifically in the legislation so it is clear on the face of the provisions (rather than be a matter of interpretation as to the extent of a deeming provision in another Act for a different purpose). We ask this given the number of investor JPUTs in the property sector owned by non-residents.

Paragraph 32

68. The change made by paragraph 32 comes into effect on 1 April 2020. A company that owns one or more UK (investment) properties will come into the charge to corporation tax on 6 April 2020 under Schedule 5 Finance Act 2019. If that company makes a disposal between 1 April 2020 and 5 April 2020, then it will have two or more accounting periods within the same financial year, but the second will not be only because of a chargeable gain.

69. Therefore, this provision appears to discriminate between non-resident companies by reference to the nature of the UK land related asset they own. A company that comes fully into corporation tax on 6 April 2020 has all capital losses before that date treated as “carry forward” capital losses, even if they arise in the same period of account or financial year.

70. Many non-resident landlords have accounting periods that end on 31 March or 31 December. Under this provision, they are restricted in their use of same period capital losses because of a policy decision to implement the move to corporation tax by reference to the income tax year and not the corporation tax financial year.

71. We assume this cannot be intended: a capital loss on a disposal made after 1 April 2020 but before 6 April 2020 should similarly be treated for such companies as a “same year” capital loss.

Appendix II: Proposed examples to be included in a white list of scenarios which would not be caught by the anti-forestalling rules

Example 1: Timing of transferring investment to trading stock

72. A trading group has certain land interests which are held on capital account and which it has identified as being surplus to the requirements of its operational business. It intends over time to appropriate those surplus assets to trading stock and to develop and sell them, either on its own or through a joint venture with other parties. The group has brought forward capital losses. The group is currently analysing the gain accrued to date on the surplus assets, considering when planning permission might be obtained and thinking about what further gain might accrue on the relevant assets after April 2020.

73. There is no doubt that there will at some point be an appropriation to trading stock in the future and this will probably involve a series of transfers of the surplus assets to a new group company set up to carry out the trade of development and sale. The group is naturally looking at appropriating certain assets before April 2020 in order to shelter the resultant chargeable gain with its brought forward losses rather than making any election under s. 161(3) TCGA.

74. While the timing of the project itself is utterly commercial, the timing of the various appropriations is naturally motivated by a desire to use the brought forward capital losses to shelter gains. We do not consider that this should be caught by anti-avoidance rules but would be grateful if HMRC can clarify their views in the white list.

Example 2: Winding up dormant subsidiaries

75. A holding company has among its subsidiaries several of which are either dormant or have limited activities which, at some point, in the normal course would be wound up. There is no business need or urgency to this: it is in many ways a matter of housekeeping. Winding up a company will result in a disposal which will give rise to a gain or a loss - the amount of which would be known now. In some cases, a loss could be triggered simply by making a negligible value claim.

76. The group decides to carry out this housekeeping exercise now and winds up some companies where a material gain may be realized to be able to offset carried forward losses without restriction.

77. Here the gain is commercial but the timing of realisation is influenced by these proposals. We do not consider that this should be caught by anti-avoidance rules but would be grateful if HMRC can clarify their views in any white list.

Example 3: Taxpayer availing themselves of a choice conferred by Parliament

78. Statute - or in some cases HMRC established practice – may confer on taxpayers the ability to alter the timing of any gain/loss. We assume that the exercise of such a choice would not be within the scope of the anti-forestalling TAAR. (We note that the Summary of Responses comments on the exercise of choice in relation to recognising a loss as a result of a negligible value claim at section 11.22, but not in the context of the anti-forestalling TAAR). The guidance should confirm that exercising such a choice would not be within this TAAR, notwithstanding the influence of CCLR on the timing of that exercise. Such choices could include any deferral

relief (for example rollover or holdover relief, the making of a s171A election to access losses elsewhere in the group, s187B elections (on migration) or negligible value claims).

79. It would be helpful if HMRC could clarify their views in the guidance on how the anti-forestalling provision could apply here: as an election by itself would not appear to be within "arrangement" but if in conjunction with a transaction then the transaction would be within paragraph 39(4)(a)/

Example 4: Commercial sale

80. A company proposes to sell a property to a third party: it is an arms-length arrangement. However, the parties agree to exchange unconditionally by a certain date (pre-1 April 2020) as the seller wishes to access its capital losses without restriction – the purchaser's ability to do so may be taken into account in the pricing. The sale is "commercial" but the timing is influenced by the restriction coming into effect. A tax advantage results – we assume that this will be accepted as "subsidiary" to the main purpose of a commercial disposal – i.e. the decision on timing, although tax-influenced, follows on from the decision to sell. We do not consider that this should be caught by anti-avoidance rules but would be grateful if HMRC can clarify their views in the white list.

81. This example is in some ways the counter to example 2 in the original Consultation - where HMRC suggested that if the reason for delay was not commercial then the relevant sale "would be expected to be caught". Here the sale date is accelerated, not delayed.) This type of fact-pattern was referenced at paragraph 131 of our response to the Consultation.

General

82. The original Consultation included examples relating to the anti-forestalling TAAR. We assume these will be repeated in any guidance. It would be helpful if these could be linked to the terms of the legislation itself – namely, demonstrating the basis on which HMRC considers these would not be caught by the "main purpose" test, particularly given recent judicial comment on HMRC "white lists".

Other comments

83. If the anti-forestalling measure applies. a tax payer could be in a worse position than it would have been in the event that a relevant disposal occurred after commencement. This is because losses are restricted to 50% of the gain under paragraph 36(2) – whereas for post-commencement disposal the £5 million deductions allowance may be available (noting here that given the lack of flexibility in the use of capital losses a group is likely to prioritise utilising the chargeable gains deductions allowance).

84. We acknowledge that allowing for the deductions allowance to apply pre-commencement could give rise to significant complexity. We also note that the provision is intended to deter certain behavior and hence we assume this too influences the difference between the position under paragraph 38 and the position if the perceived forestalling transaction had not happened (although in principle the same result should apply to both)

85. This differential in treatment however emphasises the importance of clarity as to the scope of the TAAR. Paragraph 38((1)(b) means that the provision can apply if a tax advantage is obtained – which would be met simply by being able to offset an allowable loss. Therefore, any disposal made after 29 October 2018 is potentially within scope where a company either realises a gain against which it offsets a carried forward loss or realises a loss that it can use on a current year basis - subject to the main purpose test being met.

86. We have in Appendix II included some examples we consider should be addressed in guidance. We ask that draft guidance be published as soon as practicable (and that it is not held back to coincide with a fiscal event). The provision was first proposed at Budget 2018 – and effectively takes effect from then (i.e. 10 months ago) – and hence the importance of providing some certainty to taxpayers now (if possible, by the addition of a statutory exclusion (as was done in relation to CIR and also Schedule 5 FA 2019 in addition to any "white list" in guidance.).

87. We also ask that the existing guidance on the TAAR in s19 FA 2019 is supplemented to indicate how it applies in the context of chargeable gains where a company generally has more of an ability to influence the timing of recognition (given the realisation basis) as compared to income profits. This is particularly relevant to condition B (whether it is reasonable to regard the arrangements as circumventing the intended limits of relief under the relevant provisions or otherwise exploiting shortcomings in the relevant provisions) – noting here D17 of the GAAR guidance which concerns planning around the "timing" of disposals.

Appendix III: Summary of other concerns with the draft corporate capital loss restriction legislation

Terminal Loss Relief

88. The Summary of Responses says that the government is still considering whether to make specific provision in relation to companies that become insolvent. In this context, in our submission in response to the original Consultation on the capital loss restriction, we asked that the government add:
    a. a terminal loss relief for CGT (see paragraphs 139 and 140 of our response to the Consultation); and
    b. a terminal loss relief for non-trading deficits (paragraph 141 to 148 of our response).

89. We note that terminal loss reliefs of this type would apply to any cessation of business, not just a cessation due to insolvency. However, given that terminal loss relief has been provided for trading losses because of the effect of CILR, we consider that an equivalent relief should be given to UK property businesses (noting that their losses/deficits are subject to the same restrictions as trading companies as a result of CILR and the proposed CCLR reforms.

REITs

90. We welcome the proposed changes set out in paragraphs 16 to 18 which are intended to ensure that REITs do not have to apply the restriction in relation to gains arising in their exempt property business. We have no comments on the changes to s535A CTA 2010: however, we are uncertain whether, as a technical matter, paragraph 17 achieves the stated policy intention (given the structure of the REIT rules as referable to CGT).

91. In our response to the original Consultation, we said:

> "A REIT is not required to distribute (exempt) chargeable gains. But, under s549A CTA 2010, if a distribution is made in respect of an exempt chargeable gain, it will be a PID. Determining whether a distribution is in respect of exempt capital gains is under s550 CTA 2010. The attribution under s550(2)(d) references "relevant non-chargeable gains" which is defined by reference to s535 CTA 2010. Although there is no express reference to losses, we understand that the PID is attributed to "net" relevant non-chargeable gains only - i.e. exempt gains less (non-allowable) losses. We assume that the capital loss restriction will not change the position. This is because the relevant losses are not allowable losses and so cannot be restricted. As a result, the notional CGT calculation to determine the amount to which a PID is attributed in relation to "relevant chargeable gains" will allow full offset of (exempt) losses. This seems to be the implication of the proposed guidance at GREIT 05507. It would be helpful if this could be clarified - and if necessary, amendments made to s550(3) CTA 2010 to put the position beyond question."

92. No change is proposed to s550(3). A change is however proposed to s535 which we assume is intended to address this concern (given the "blanket" exemption within s535 means that the restriction is irrelevant in that context).

93. In particular, the exemption conferred by s535(a) is in relation to a gain arising on **<u>the</u>** disposal of **<u>an</u>** asset: this must mean the "gross" gain on that disposal (i.e. on a single disposal of an asset, you are looking at the outcome of that disposal only – carry forward losses are irrelevant (they only come into play as a result of s2A TGCA when determining "net" chargeable gains (based on the totality of gains on **<u>all</u>** disposals in a given period)

for inclusion in total profits). Therefore, the proposed s535(10) has no application to the determination of that gain on a particular asset disposal. There is no netting required – or indeed provided for - in determining the amount of any exempt gain within the legislation.

94. Further, as the corollary of the exemption in s535(1), losses on disposals of assets within the exempt property business are not allowable losses. Therefore the restriction is irrelevant to them in any event (s2A – and therefore the restriction in s269ZBA(2) - only applies where a company has allowable losses).

95. As a result, the new s535(10) cannot be relevant in the context of s535 (for completeness, the position in relation to s535 is different to that which applies to s5353A – within s535A, an offset is permitted for residual business losses which will be allowable losses within s2A TCGA and thus within the scope of the restriction and hence the (similarly worded) new s5353B(4) is required).

96. As s535(10) is redundant in the context of s535, we assume therefore it is directed at the issue discussed in our earlier response concerning sS550(3) relating to distributions in respect of gains (and the concept of "relevant non-chargeable gains").

97. "Relevant non-chargeable gains" are defined as gains accruing to property rental business of a company/ of the group, which as a result of section 535 or 535A are not chargeable gains. As we set out in our earlier response, we understand that in practice this figure is taken to be net of losses (which makes sense as a matter of policy and in effect replicates the amount that would be brought into account as part of total profits were the REIT taxable – it also reflects what would be shown in the financial statements).

98. We assume that the new s535(10) is intended to provide a means by which the aggregate of gross gains within s535 become a net amount for the purposes of s550. We would suggest the drafting is revisited – and potentially the placement of this amending section. An alternative approach would be to amend s550 itself – and perhaps provide that relevant non-chargeable gains means the aggregate of gains exempt under the relevant section less any non-allowable losses (to be defined by reference to ss535/535A), and that when determining relevant non-chargeable gains on this basis, Part 7ZA does not apply.

99. We note that amending the definition in this way means that consideration would need to be given to the risk of unintended consequences (given that s550(3) has been its current form for some time). In this context it may be possible to make a simpler change by adding a new s550(4) to say that in determining the amount of relevant non-chargeable gains, s269ZBA is to be ignored – this then links netting to the s550 calculation specifically without itself rewriting s550(3) (and maintains the integrity of s535).

Paragraph 14: Clogged Losses

100. Paragraph 14 inserts a new section 18(11) that defines what "deductible clogged losses" as losses for which relief is not available as a result of the restriction in Part 7ZA.

101. If a company has "mixed" losses (i.e. some from connected party disposals, some not), how is it intended that this provision applies – or, to put another way, how would you work out which losses are "restricted"?

102. For example, assume a company has £10m of gains in 2020, of which £2m are connected party gains. It has carry forward capital losses of £6.5m, of which £1.5m are connected party loss. As a result of the restriction, only £5m of those losses can be used (assuming no deductions allowance for simplicity). This means that £1.5m

losses are restricted.

103. Is the company required to treat the losses “equally”, so the restriction applies separately to each type of gain (as happens under CILR in relation to pre-2017 and post-2017 losses): this would mean that the company would be assumed to use £1m of its connected company loss (i.e. 50% of the connected party gain) (if you have current year losses to swap it for). Or can it simply allocate the full restricted amount to the connected party losses, and so can (assuming sufficient current year losses to “exchange” for the clogged losses) treat the entirety of the connected party loss as restricted? We assume it is the latter – first, losses are (for the purposes of applying the restriction) fungible; secondly, there is no specific legislation requiring proportionate use of the restriction - or for potentially clogged losses to be restricted on a stand-alone basis and finally, (in any event) the limit imposed by s18(9)(b) TCGA in effect protects the Exchequer in terms of any potential loss of tax if the taxpayer has this choice. Please confirm the intended operation of s18(11) and, if required, clarify within the legislation.