

Capital Loss Reform
Room 3/64
CT Capital Losses
BAI
HMRC

reform.capitalloss@hmrc.gsi.gov.uk

25 January 2019

Dear Sirs

Corporate Capital Loss Restriction: Consultation on delivery

We welcome the opportunity to respond to HMRC's consultation on the delivery of the Corporate Capital Loss Restriction proposals. We have not responded to the specific questions raised in the consultation document as this is best left to individual companies who may have specific issues, however we have set out below some wider concerns that we have on the principles behind the proposals.

Policy

The consultation document states that there is a desire to align the Corporate Capital Loss regime with the Corporate Income Loss Restriction ('CILR'). However, reform of the Corporate Capital Loss regime was considered at the time of the CILR consultation in 2016. At that time a joint HM Treasury / HMRC paper established the policy objective of maintaining the distinctions for capital losses¹. Tax policy will and should develop over time but, bearing in mind the relatively recent statements during the CILR consultation, it is not clear why the policy has changed in this case.

Whilst in principle we would prefer the CILR to allow losses to be relieved without restriction, we consider that there are justifiable reasons to retain the current differences between the treatment of capital and income losses as follows:

- The consultation document states that, without this change, there is a risk that significant gains will be made without any tax being paid. Companies should be taxed on their net gains over the longer term. The existing system for capital loss relief allows this but the current proposals run the risk of creating an asymmetric system for capital gains and losses with gains always being taxed and losses not always being relieved.
- By their nature the events that trigger capital gains and losses are often one-off and are not 'business as usual' transactions. In contrast, trading profits are generally more predictable. This means that, even with the existing income loss restriction, the objective of 'net positions over time' being taxed can be achieved in relatively short order. This is much less likely to happen in the

¹ Objective 5 of 'Reforms to Corporation tax loss relief: consultation on delivery', HMT and HMRC, May 2016

context of capital gains transactions and therefore is more likely to result in tax relief for capital losses being permanently denied.

Competitiveness

We are also concerned at the potential impact these proposals could have on UK competitiveness. The 100 group represents the largest UK businesses and as such we believe that the domestic tax regime should enhance the UK as a place to do business.

The UK has made significant strides in being a location of choice for holding companies over the years. The introduction of the Substantial Shareholding Exemption (SSE) and the dividend exemption, for example, improved our competitiveness against some of the more traditional overseas holding locations. The flexibility of our capital loss regime is seen as an advantage, especially as the SSE rules can be more restrictive than some overseas participation exemption regimes in relation to capital gains (for example, by restricting it to holdings of more than 10% and to investments in trading groups).

We are concerned that restricting the use of capital losses as proposed will remove a valuable feature of the UK's tax system and that we will see multinational groups choosing to use overseas holding companies to acquire investments in order to protect future gains from taxation.

This potential consequence is exacerbated by the ongoing Brexit uncertainty which is likely to continue for some years as future trading arrangements are debated and agreed. We believe it is vitally important to maintain a positive investment environment as the country goes through the anticipated economic disruption.

We are already seeing some groups choosing to relocate activity outside of the UK as a result of Brexit and the likelihood of capital losses being restricted may make taxpayers accelerate those plans to ensure historic losses can be fully utilised.

The proposals also introduce yet more complexity into the UK tax code. The document anticipates calculations being linked to some extent to the CILR because the £5m allowance will be effectively shared across both regimes. This results in the complex multi-step calculation set out in the consultation. The UK has enacted a number of complex legislative reforms in recent years including the Diverted Profits Tax, the Corporate Interest Restriction and the CILR. A core component of a jurisdiction's tax competitiveness is the complexity of its tax code and we are concerned that the UK is gradually eroding its attractiveness internationally due to this increasing complexity. Again, this is of heightened concern when viewed alongside Brexit. In addition it is worth noting that increased complexity will increase the cost of administering the UK's tax system for both HM Government and our members and we question whether this is in the UK's best interests.

Specific Impacts

It is worth mentioning a few specific impacts that these proposals are likely to cause:

- Many companies will be recognising capital losses in their financial statements (either in the form of a deferred tax asset or a reduction in deferred tax liabilities on unrealised gains). These proposals will result in taxpayers having to reassess the ability to recognise such losses and in

many cases may lead to a write-off of some or all of these assets producing negative effects on balance sheets and distributable reserves.

- The consultation document states that the proposals will affect the largest 1% of businesses, particularly those that hold real property. In practice this is likely to mean that the tax burden will fall on the Financial Services and Retail sectors. The 100 group's recent Total Tax Contribution report² found that there is already a concentration of tax burdens on these two sectors with retail and FS accounting for 58.7% of taxes borne by 100 group members in 2018. This proposal seems to add to the pressure already faced by the High Street in particular, and has the capacity to drive commercial decisions on asset disposals with distorting effects on the sector.
- More generally, the proposal could lead to taxpayers delaying or advancing commercial capital transactions in order to try to net off current year gains and losses in legitimate ways. This measure could therefore distort commercial behaviour.

Concluding comments

The Assessment of Impacts in the document states that the consultation will be used to 'fully identify the impacts on business' but only invites comments on the delivery aspects. We are concerned that the full impacts will not be properly understood before proceeding to implementation.

We are very concerned that these changes will practically lead to permanent denial of relief for capital losses as well as negative impacts on the competitiveness of the UK, particularly as a holding location. For the reasons stated, we think that these proposals should be withdrawn.

Please feel free to contact me at chris.oshea@the100group.co.uk should you wish to discuss our comments further.

Yours faithfully



Chris O'Shea

Chairman

Taxation Committee

Who we are

The 100 Group of Finance Directors represents the view of the finance directors of FTSE100 and several large UK private companies. Our member companies represent almost 90% of the market capitalisation of the UK FTSE 100 Index. Our aim is to contribute positively to the development of UK and international policy and practice on matters that affect our business, including taxation, financial reporting, corporate governance and capital market regulation. Whilst this letter expresses the views of the 100 Group of Finance Directors as a whole, those views are not necessarily those of our individual members or the respective employers.

² Key findings, page 6, 2018 Total Tax Contribution Survey for the 100 group
<http://www.the100group.co.uk/~media/Files/T/The-Hundred-Group-V2/documents/tax-committee/other/2018%20TTC%20survey%20for%20the%20100%20Group.pdf>