Summary: Intervention & Options

Department /Agency: HM Treasury	Title: Temporarily enhancing loss carry back for business	
Stage: Implementation	**Version:** 1	**Date:** 20 April 2009
Related Publications:		

Available to view or download at:

http://www.hmrc.gov.uk/better-regulation/ia.htm

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What is the problem under consideration? Why is government intervention necessary?

As the downturn progresses some businesses will make tax losses, not due to the viability of their business, but because of wider economic conditions. Loss-making businesses are particularly affected by cash flow and credit problems as they have more limited means to respond to these pressures. All companies and unincorporated businesses making losses from trades, professions or vocations can currently carry losses back against profits of the preceding year to get a repayment of tax. Although this already provides considerable support for businesses the Government believes that businesses should be further helped by temporarily extending the trading loss carry back rules, to support otherwise viable businesses now making losses, so they can continue to trade.

What are the policy objectives and the intended effects?

The Government's objective is to provide further help for loss-making businesses who are experiencing worsening cash flow positions in the current challenging economic climate. Enhanced loss carry back provides additional, temporary cash flow benefits to these businesses as they will get a repayment of tax. Such changes could keep loss-making, but viable, businesses trading until the economy improves.

What policy options have been considered? Please justify any preferred option.

Option 1: Do nothing. Failure to support loss-making businesses would risk some viable businesses ceasing trading.

Option 2: Provide support to loss-making businesses by temporarily extending the carry-back of losses from one year to three years, for losses up to £50,000 per year.

The preferred option is to provide temporary support for businesses that are experiencing worsening cash flow positions for a period of two years, targeting support on smaller businesses.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

The policy will be reviewed around two years after implementation to assess the actual impacts. This would follow the receipt of data from tax returns for 2009-10 during 2011.

Ministerial Sign-off For final proposal/implementation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.

Signed by the responsible Minister:

Stephen Timms

Date: 20 April 2009

Summary: Analysis & Evidence

Policy Option: 2

Description: Temporarily enhance loss carry back for business

COSTS

ANNUAL COSTS		Description and scale of **key monetised costs** by 'main affected groups'
One-off (Transition)	**Yrs**	Increased compliance costs of £1.7 million per year of enhanced loss carry back. In order to calculate the repayment of tax to which they are entitled some loss-making businesses will have a more complex tax calculation.
£ 1.7m per year	2	
Average Annual Cost (excluding one-off)		
£ 0		**Total Cost** (PV) **£ £3.4 m**

Other **key non-monetised costs** by 'main affected groups'

Estimated Exchequer loss of £10 million in 2008-09, £230 million in 2009-10, £215 million in 2010-11 and £30 million in 2011-12.

BENEFITS

ANNUAL BENEFITS		Description and scale of **key monetised benefits** by 'main affected groups'
One-off	**Yrs**	The benefits from providing temporary financial support to prevent viable businesses from ceasing to trade are unquantifiable.
£ unquantifiable		
Average Annual Benefit (excluding one-off)		
£ unquantifiable		**Total Benefit** (PV) **£ unquantifiable**

Other **key non-monetised benefits** by 'main affected groups'

Long term economic benefits associated with businesses that are saved as a direct result.

Key Assumptions/Sensitivities/Risks

The taxpayer population benefiting from the temporary enhancement is assumed to be unchanged since 2006-07, the latest year for which complete information is available.

Price Base Year 2009	Time Period Years N/A	**Net Benefit Range** (NPV) **£ unquantifiable**	**NET BENEFIT** (NPV Best estimate) **£ unquantifiable**

What is the geographic coverage of the policy/option?	UK
On what date will the policy be implemented?	24 November 2008
Which organisation(s) will enforce the policy?	HMRC
What is the total annual cost of enforcement for these organisations?	£ No change
Does enforcement comply with Hampton principles?	N/A
Will implementation go beyond minimum EU requirements?	N/A
What is the value of the proposed offsetting measure per year?	£ 0
What is the value of changes in greenhouse gas emissions?	£ 0
Will the proposal have a significant impact on competition?	No

	Micro	Small	Medium	Large
Annual cost (£-£) per organisation (excluding one-off)	0	0	0	0
Are any of these organisations exempt?	No	No	No	No

Impact on Admin Burdens Baseline (2005 Prices) (Increase - Decrease)

Increase of £ 0 | Decrease of £ 0 | **Net Impact** **£ 0**

Key: **Annual costs and benefits:** **(Net) Present**

Evidence Base (for summary sheets)

The Issue

As the downturn progresses many businesses will make losses, not due to the viability of their business, but because of wider economic conditions. Loss-making businesses are particularly affected by cash flow and credit problems as they have more limited means to respond to these pressures.

Current loss relief rules already provide considerable support for businesses. Under current rules businesses already have a number of mechanisms to ensure tax from profitable years is repaid through off-set against losses that arise in subsequent periods when times are harder:

- firstly, businesses can offset unlimited trading losses against profits in the preceding year and thereby reclaim tax previously paid;
- secondly, businesses can offset unlimited trading losses against profits in any subsequent year;
- thirdly, start-up unincorporated businesses in the early years of operation can carry trading losses back for three years; and
- finally, any business ceasing to trade can also carry trading losses back for three years.

The Government remains committed to helping businesses affected by the downturn however it can, and believes that temporarily making these rules more generous will help achieve this objective.

Policy Objectives and Intended Effects

The policy objective is to temporarily help businesses with worsening cash flow positions. Providing such support could keep loss-making but viable businesses in operation until the economy improves. Businesses benefiting from the policy would get a larger repayment of corporation tax or income tax (depending on their legal status) immediately improving their cash flow. The policy would apply to all businesses, irrespective of size. Limiting the amount of losses eligible for enhanced carry back to £50,000 per year ensures resources are targeted on smaller businesses.

The Options

Option 1: Do nothing

Failing to provide support to loss-making businesses risks some otherwise viable businesses ceasing to trade.

Option 2: Temporarily enhance loss carry back relief for businesses

The preferred option would apply for two years and extend the period that trading losses from businesses could be carried back against previous profits, from the current one year entitlement to a period of three years, with losses being carried back against later years first.

The amount of losses that could be carried back to the preceding year would remain unlimited. After carry back to the preceding year, a maximum of £50,000 of the balance of unused losses would then be available for carry back to the two earlier years. This £50,000 limit would apply separately to unused losses of each 12 month period or tax year within the duration of the extension. For companies this means a cap of £50,000 on the extended carry-back of losses arising in accounting periods ending in the 12 months to 23 November 2009 and a separate £50,000 cap on the extended carry-back of losses arising in accounting periods ending in the 12 months to 23 November 2010. For unincorporated businesses, this means a cap in each of the tax years 2008-09 and 2009-10.

A company could make a loss relief claim when it makes its return for accounting periods ending in the period 24 November 2008 to 23 November 2010. Unincorporated businesses could make a loss relief claim as soon as they have calculated their losses for their basis period for the tax years 2008-09 and 2009-10. HM Revenue and Customs (HMRC) could make repayments arising from such loss relief claims on or after Budget Day 2009. The implementation date of 24 November 2008 is the date of the 2008 Pre-Budget Report when an extension of trading loss carry back was first announced.

This option is considered a proportionate response as it targets available resources at viable businesses. Businesses ceasing to trade are already eligible to carry back all their trading losses for three years and so are unaffected by this option.

Taxpayer Populations

HM Revenue and Customs receive annual tax returns from businesses. The latest year for which complete information is available is 2006-07. Longitudinal analysis of historical tax returns for the years 2002-03 to 2006-07 enables us to model the numbers of taxpayers who would benefit from enhanced loss carry back. Estimates of the business population affected by a temporary enhanced loss carry back are shown below.

Table 1: Estimated business population

Type of taxpayer	Estimated number of taxpayers benefiting per year from a temporary enhancement increasing loss carry back to three years*
Self-employed: sole traders	25,000
Self-employed: partners	15,000
Small and Medium companies	30,000
Large companies	5,500
Total	75,500

*Detailed forecasts of how individual businesses' profits and/or losses have changed since 2006-07 are not available. HMRC do not forecast the future profits and losses of individual businesses so all modelling has been based on 2006-07 and earlier data.

Not all taxpayers making losses would benefit from the preferred option. Only those ongoing viable businesses with a balance of unused losses after one year carry back and with profits in the earlier two years would benefit from the option. Longitudinal analysis of tax returns suggests that around 75,500 taxpayers per year would benefit from enhanced loss carry back relief – around 40,000 self-employed taxpayers and 35,500 companies. This is around one per cent of the total number of unincorporated taxpayers, and around two per cent of all companies.

Administrative Burden

HMRC is subject to quantified targets to reduce one aspect of compliance costs in particular; the administrative burden of disclosing information to HMRC or to third parties. This burden is assessed through the 'Standard Cost Model' (SCM), an activity based costing model that identifies what activities a business has to do to comply with HMRC's obligations, and which estimates the cost of these activities, including agent fees and software costs.

Costs and Benefits / Impacts

Option 1: Do nothing

There are no changes in compliance costs. Not supporting businesses making losses could result in some viable businesses ceasing to trade.

Option 2: Temporarily enhance loss carry back relief for businesses

Table 1 shows that around 40,000 self-employed taxpayers and 35,500 companies could benefit per year from enhanced loss carry back. However these businesses would have increased compliance costs arising from a more complex tax calculation.

The SCM already has information on the administrative burden associated with i) businesses carrying losses back against any profits of the preceding year; and ii) where a business ceases to carry on a trade, carrying losses back three years.

Data from the SCM suggests it is fair to assume that all unincorporated taxpayers and almost three-quarters of companies carrying back losses for three years are represented by an agent. The SCM suggests an increased compliance cost of £25 each for represented businesses and around £6 for unrepresented businesses. There is an increased compliance cost of around £1.7 million for each year the temporary extension applies. The total increased compliance cost, assuming the same eligible population as observed in 2006-07 is **around £3.4 million**, although the eligible population may have increased. A 2005 wage rate of £11.70 is assumed for in-house tasks.

There is no ongoing increase in the administrative burden on taxpayers as this is a temporary measure.

Consultation

It was not possible to consult publicly on the effects of these changes prior to their announcement. As a result, there was no consultation stage Impact Assessment to inform this final Impact Assessment.

HMRC costs

HMRC would incur additional administrative costs from extending loss carry back. Unincorporated businesses could make a standalone repayment claim outside of the tax return resulting in increased HMRC costs. HMRC would need to develop guidance for taxpayers and staff. However, these costs are not monetised.

Competition assessment

Applying the Office of Fair Trading competition filter to the affected sectors to assess the impact of the proposed measure, it was found that an in depth competition assessment is not warranted because the estimated impacts on competition are not significant.

Small Firms Impact Test

Analysis of tax returns suggests that over 90 per cent of businesses who would benefit from enhanced loss carry back are small or medium sized businesses. Small businesses are more likely to utilise all their losses against previous profits than larger businesses. This is a measure that will help small businesses.

Other Impact Tests

Other Impact Assessments were undertaken and found that the changes should have no significant impact on legal aid or sustainable development. Assessments for carbon or environmental impacts or health impacts concluded that these issues are not applicable.

The Equality Impact Assessment Screening procedure has been undertaken for the measure. Some race, disability, gender and rural specific impacts are probable, but only insofar as these characteristics are correlated with the incidence of individuals running businesses.

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

Type of testing undertaken	***Results in Evidence Base?***	***Results annexed?***
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	Yes	No
Sustainable Development	Yes	No
Carbon Assessment	Yes	No
Other Environment	Yes	No
Health Impact Assessment	Yes	No
Race Equality	Yes	No
Disability Equality	Yes	No
Gender Equality	Yes	No
Human Rights	Yes	No
Rural Proofing	Yes	No

Annexes