CHAPTER 17

THE PRINCIPLES OF GROUP RELIEF

17.1 Introduction

Group relief allows losses to be transferred to profit making companies in the same **75% group**.

Illustration 1

A Ltd £100,000

75%

B Ltd (£60,000)

Under the group relief provisions, we can surrender the loss of £60,000 from B to A reducing A's taxable profit and its corporation tax liability.

The maximum claim is the lower of the **available loss or the available profit**.

Illustration 2

A Ltd (£100,000)

75%

B Ltd £60,000

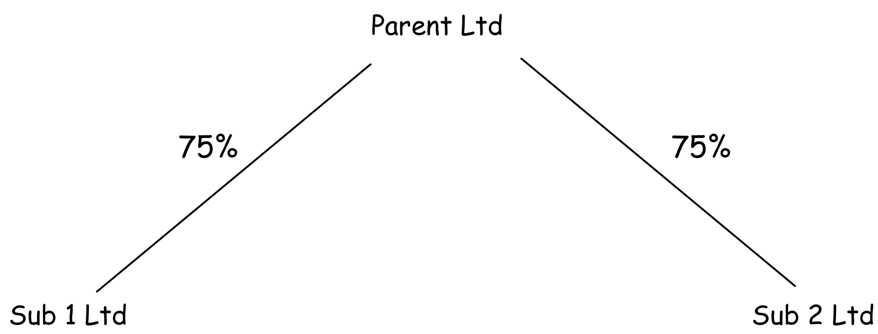
The group relief claim here will be a maximum of £60,000. A Ltd will have the remaining loss of £40,000 which it may be able to set off in the current year, carry back, or carry forward. Losses that are unutilised can only be carried forward in the company that originally sustained them.

17.2 The 75% definition CTA 2010, s.152

For **group relief** to apply, **one company must own at least 75% of the other.** For example if A Limited owns 75% of B Limited, that means that losses can flow from A to B or from B to A.

Note that the provisions **only apply to company ownership**, therefore, if Mr A owned 75% of B Limited, losses could not flow between Mr A and B Limited, as Mr A pays Income Tax and B Limited pays Corporation Tax.

Group relief **also applies between two companies** that are **each owned to** the extent of **75% by the same parent company**.



Losses can flow between the parent and the two subsidiaries **in either direction** and losses can also flow between the two subsidiaries.

If the two subsidiaries are owned by Mr P instead of Parent Ltd, losses could not flow either between Mr P and the two companies, or indeed between the two subsidiaries. Corporate ownership must apply for group relief of losses.

The **75% test** applies to **all three** of the following: CTA 2010, s.151

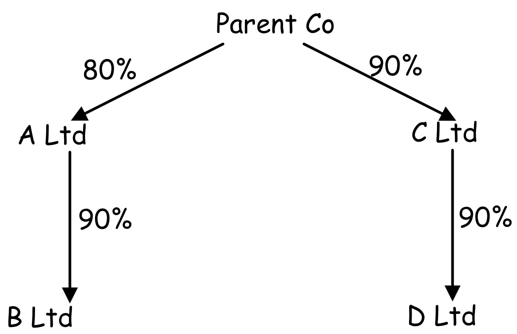
(i) There must be 75% **ownership of ordinary share capital** of the company; and

(ii) Those shares must entitle the shareholders to at least 75% of the **available distributable profits**; and

(iii) Those shares must entitle the shareholder to at least 75% of the company's **assets on a winding up.**

These three together form the definition of **"equitable ownership".**

Illustration 3



In the above scenario, Parent Co and A Ltd are in a 75% group.

However, to determine whether Parent Co and B Ltd are in the same group relief group, we multiply 80% and 90% to give 72%. This is less than 75% so a group is not formed. If B Ltd has a loss, it cannot surrender it to Parent Co or vice versa. B Ltd and A Ltd are in a 75% group so trading losses can be surrendered between them.

Contrast this with the relationship between Parent Co and C Ltd and D Ltd. In this instance the 3 companies are in a group relief group as Parent Co's effective interest in D Ltd is 81% (i.e. 90% x 90%).

The group relief groups are therefore:

Parent Co + A Ltd + C Ltd + D Ltd

and

A Ltd + B Ltd

It can be seen, therefore, **that a company can participate in more than one group relief group.**

Note that all 5 companies are associated with each other so the corporation tax limits for each of the companies are divided by 5.

17.3 Available amounts

The surrendering company (i.e. the loss making company) may surrender: CTA 2010, s.99

(i) trading losses

(ii) Non-trading deficits (LR)

The total amount of these losses may be surrendered before the surrendering company is required to consider any loss offset in its own computation.

Furthermore the surrendering company may also surrender CTA 2010, s.105

(iii) excess management expenses

(iv) excess UK property business losses

(v) excess losses on non-trade IFAs

(vi) excess qualifying charitable donations

The amount of "excess" available for group relief is found by comparing gross income **before any loss set offs** (including brought forward losses) to qualifying charitable donations, management expenses, UK property business losses and losses on IFAs as appropriate.

Only losses of the current chargeable accounting period may be surrendered. Brought forward losses are not available for surrender.

The surrendering company surrenders to the claimant company or companies (i.e. the profit making companies) who must **set the losses against taxable total profits (TTP)** of the same chargeable accounting period.

The claimant company **must use the losses in its current chargeable accounting period** – any losses claimed under group relief cannot be carried back, carried forward or given to another group member.

The offset against TTP will be made after qualifying charitable donations and any current year or brought forward losses. However, the offset is made before losses brought back from a future period i.e. losses carried back do not displace group relief already claimed. CTA 2010, s.137

Illustration 4

Two 75% group companies have the following results:

	Claimton Ltd	*Surrton Ltd*
	£	£
Trade profits/(losses)	(6,000)	(80,000)
Non-trading (LR) profits/(deficits)	20,000	(4,000)
UK property business income	-	10,000
Qualifying charitable donations	(1,000)	-

The available loss of Surrton Ltd is as follows:

	Surrton Ltd
	£
Trading loss	(80,000)
Non-trading deficits (LR)	(4,000)
Available loss	(84,000)

The available profit of Claimton Ltd is as follows:

	Claimton Ltd
	£
Trade profits	Nil
Non-trading profits (LR)	20,000
Less: Current Year Loss	(6,000)
	14,000
Less: Qualifying charitable donation	(1,000)
	13,000
Maximum group relief from Surrton Ltd lower of: (i) TTP £13,000; or (ii) Available loss £(84000)	(13,000)
Revised TTP	Nil

Remaining loss of Surrton Ltd is as follows:

	Surrton Ltd
	£
Available loss	(84,000)
Less: Group relief surrendered to Claimton Ltd	13,000
Less: Current year claim in Surrton (if made)	10,000
Remaining loss	£(61,000)

17.4 Effective use of losses

When using losses, it is important to obtain relief at the highest marginal rates of tax and secondly to use the losses up sooner rather than later.

From a timing perspective our preference would be for claims in the following order:

(i) **current year** and then **carry back**;

(ii) **group relief**;

(iii) **carry forward**.

However, the primary objective for the companies is to save the maximum tax possible on a group wide basis. To appreciate how this is done, we must consider the effective **marginal rates** of tax of all of the companies in the group.

17.5 Marginal rates of tax

We have various marginal rates of tax, depending on the level of the company's augmented profits.

By "marginal" rate we mean the rate of corporation tax effectively payable on the final £1 of a company's TTP.

Tax rates:	*FY 2009 & FY 2010*
£0 - £300,000	21%
£300,001 - £1,500,000	29.75%
> £1,500,000	28%

The **limits** would obviously be **divided amongst the number of associates in the group**.

The marginal rate for FY 2010 is 29.75% and is calculated as follows:

29.75% rate:

£			£
1,500,000	X 28%		420,000
(300,000)	X 21%		(63,000)
1,200,000			357,000
		$\frac{357000}{1200000}$	= 29.75%

Illustration 5

Hill Ltd owns 100% of the shares of Collis Ltd. As the companies are associated, the corporation tax limits (FY 2010) will be as follows:

	£
Lower limit	150,000
Upper limit	750,000

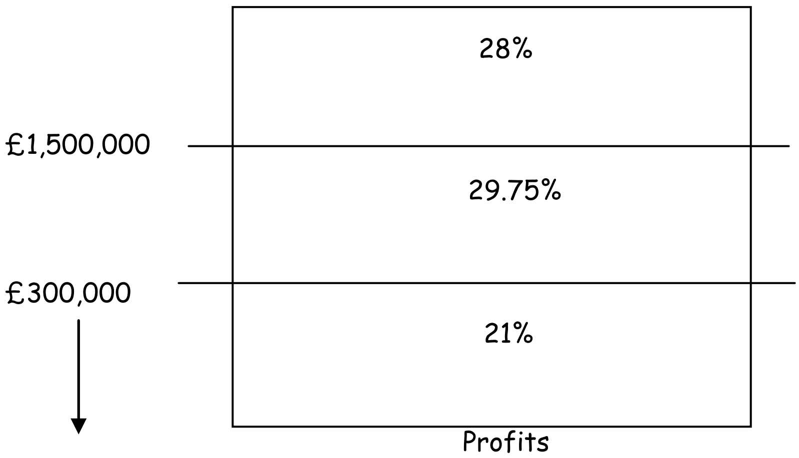
Assuming Hill Ltd has TTP of £1m it will be a "large" company and will pay corporation tax at the main rate of 28%, i.e.

£1,000,000 x 28% = £280,000

Another way to arrive at this CT liability is to consider the marginal tax rates which apply within each of the tax bands:

	£
First £150,000 @ 21%	31,500
Next £600,000 @ 29.75%	178,500
Remaining £250,000 @ 28%	70,000
Total tax on TTP of £1m	£280,000

Diagramatically these marginal rates can be illustrated as below:



Divided by number of associates as appropriate

This diagram illustrates that if a company had profits between the lower limit and the upper limits (i.e. between £300,000 and £1,500,000 in this example), and it were given an **extra £1** of income it would pay corporation tax at a rate of **29.75%** on that "marginal" £1.

This 29.75% rate is an effective **marginal** rate and should **not** be used when calculating CT liabilities.

Therefore when making group relief claims, we will try to eliminate profits taxed at the highest marginal rate, i.e. 29.75%.
To achieve this we need to **specify** the amount of group relief required in order to bring the profit down to the **exact level** of the lower limit. This ensures that **all** of the loss will be relieved at an effective rate of 29.75%. As group relief claims can be specified, this is very easy to do.

We would then start eroding profits taxed at 28%, then profits taxed at 21%.

Illustration 6

X Ltd is a parent company with two wholly-owned subsidiaries Y Ltd and Z Ltd.

The results in the year ending 31 March 2011 are as follows:

	X Ltd	*Y Ltd*	*Z Ltd*
	£	£	£
Trade profit/(loss)	600,000	(40,000)	(20,000)
Non-trading profit (LR)	50,000	121,000	10,000

In order to calculate the optimum loss relief we need to carry out the following steps.

First we build up the corporation tax computations so that we can work out what rates of tax the profits are being charged at.

	X Ltd	Y Ltd	Z Ltd
	£	£	£
Trade profit	600,000	Nil	Nil
Non-trading profit (LR)	50,000	121,000	10,000
Profit	650,000	121,000	10,000

Next we need to calculate the upper and lower limits:

Limits $\frac{£300000}{3} = £100,000$

$\frac{£1.5m}{3} = £500,000$

We can see that X is paying tax at 28%, Y is paying tax at 29.75% on the top part of its profits and Z is paying tax at 21%.

We want to save tax at the highest marginal rate.

Y has a loss of £40,000. The optimum claim will be to use £21,000 of loss to reduce Y's profits down to the lower limit and then to use the balance of the loss in X by way of group relief.

Z has a loss of £20,000 and the best place to use this loss will again be in X by way of group relief.
Therefore, in Y, as we cannot specify the amount to offset under a current year claim (it is an all or nothing claim), the group relief claim of £19,000 must be made first before submitting an all-or-nothing current year claim under s.37(3)(a) for the balance, being £21,000.

	X Ltd	Y Ltd	Z Ltd
	£	£	£
Trade profit	600,000	Nil	Nil
Non-trading profit (LR)	50,000	121,000	10,000
Profit	650,000	121,000	10,000
Less: Group relief: Y Ltd	(19,000)		
Z Ltd	(20,000)		
Less: Current year claim		(21,000)	
TTP	**£611,000**	**100,000**	**10,000**

Example 1

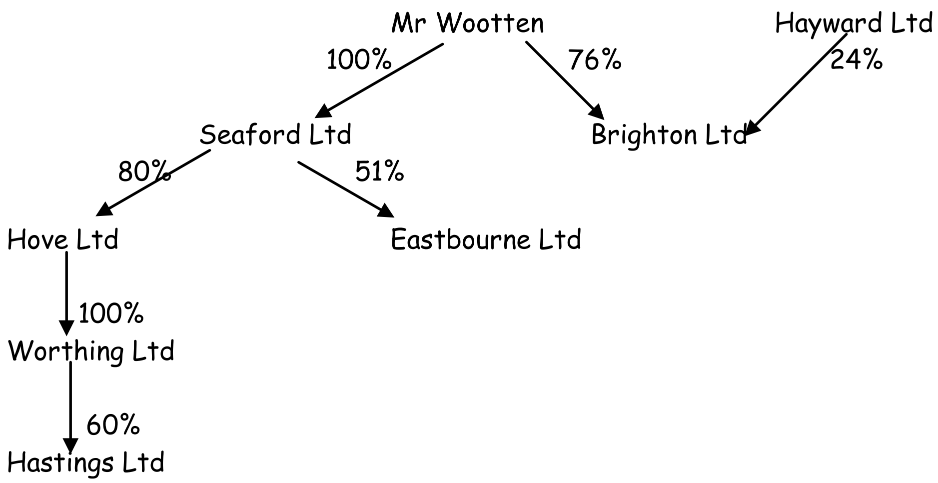
Consider the following:

	Fog Ltd	*Mist Ltd*
	£	£
Trade profit	120,000	10,000
UK property business loss	-	(100,000)
Qualifying charitable donations	(5,000)	-

What is the maximum loss that can be surrendered from Mist Ltd to Fog Ltd?

Example 2

Consider the group below:



You are required to:

(1) Identify the companies which are associated with Seaford Ltd for corporation tax purposes.

(2) Identify the groups which exist for group relief purposes.

Example 3

Houllier Ltd has two wholly owned subsidiaries Owen Ltd and Heskey Ltd, and 60% of the shares in Gerrard Ltd. The results for the year ended 31 March 2011 are as follows:

	Houllier Ltd £	*Owen Ltd £*	*Heskey Ltd £*	*Gerrard Ltd £*
Trade profits	100,000	40,000	nil	90,000
Trading loss			(60,000)	
Non trading profit (LR)	10,000	4,000	6,000	2,000
Chargeable gain	20,000	-	-	4,000

You are required to calculate the corporation tax liability for each company, assuming the loss relief is taken in the most efficient way.

Answer 1

	Fog Ltd	Mist Ltd
	£	£
Trade profit	120,000	10,000
UK property business loss		(10,000)
Qualifying charitable donations	(5,000)	___
Profit	115,000	Nil
Less: Group relief	**(90,000)**	
TTP	25,000	

The excess UK property business loss is £90,000 for group relief purposes. Remember only **excess** UK property business loss can be group relieved.

Answer 2

(1) Associated companies:

Seaford Ltd
Hove Ltd
Eastbourne Ltd
Worthing Ltd
Hastings Ltd
Brighton Ltd

Limits for corporation tax are therefore divided by 6

Seaford Ltd is associated with Brighton Ltd as they are controlled by the same person – i.e. Mr Wootten.

To determine whether Seaford Ltd and Hastings Ltd are associated, we do <u>not</u> multiply the effective interests – it is sufficient that each company in the chain is controlled by its parent.

(2) Group relief group:

There is only one group for group relief purposes, i.e.

Seaford Ltd + Hove Ltd + Worthing Ltd.

Seaford Ltd and Brighton Ltd are not in the same group as they are not under the 75% control of the same <u>company.</u>

Answer 3

4 associated companies:

£300,000 x $\frac{1}{4}$	£75,000
£1.5m x $\frac{1}{4}$	£375,000

Houllier Ltd, Owen Ltd and Heskey Ltd are in a group relief group.

	Houllier Ltd	Owen Ltd	Heskey Ltd	Gerrard Ltd
	£	£	£	£
Trade profit	100,000	40,000	-	90,000
Non-trading profit (LR)	10,000	4,000	6,000	2,000
Chargeable gain	20,000			4,000
TTP before loss relief	130,000	44,000	6,000	96,000
Tax rate prior to relief	*Marginal*	*21%*	*21%*	*Marginal*
Less: Group relief	(55,000)			n/a
Less: Current year claim			(5,000)	
TTP after group relief	75,000	44,000	1,000	96,000
CT @ 21%	15,750	9,240	210	
CT @ 28%				26,880
$\frac{7}{400}$ x (375,000 – 96,000)				(4,883)
CT liability	15,750	9,240	210	21,997

Notes:

1 Gerrard Ltd is not a 75 % subsidiary and so cannot participate in the group relief claim (however, it is an associate)

2 Houllier Ltd's profits are in the highest marginal band – i.e. 29.75%. Therefore, we first use sufficient losses to bring Houllier Ltd's profits down to the small profits limit of £75,000.

3 Heskey's Ltd's profits are within the small profits band – i.e. 21%.

4 It would have been equally correct to allocate the £5,000 balance of losses to Houllier Ltd or Owen Ltd instead of Heskey Ltd, as it saves 21% tax in all cases.

5 The order of claims will be as follows:

	£
Loss in Heskey Ltd	60,000
Less: Group relief in Houllier Ltd	(55,000)
Balance	5,000
Less: s.37(3)(a) current year Claim in Heskey Ltd	(5,000)
Loss remaining	Nil