

CPA Ireland Skillnet

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The CPA Ireland Skillnet provides excellent value CPE (continual Professional Education) in accountancy, law, tax and strategic personal development to accountants working both in practice and in industry. However our attendees are not limited to the accountancy field as we welcome all interested parties to our events.



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The Institute of Certified Public Accountants in Ireland www.skillnets.ie

Trainee Accountant Webinar

F2 –Taxation Presented By: Sandra Gleeson

Introduction

- The purpose of this webinar is to give an overview of the topic of trading losses as examinable in an F2 Taxation exam.
- This webinar will focus on how a Case I or Case II loss incurred by a company can be utilised in the period in which the loss arises, in the preceding period, and in future periods.

Note – for ease of reference we will refer to the loss incurred in a relevant trade as a ‘trading loss’.

A relevant trade is a trade other than an expected trade.

How to calculate trading losses?

Trading losses are calculated in the same way as trading profits:

| Case I Computation for year ended 31 December 2017 | € |
|--|--------------|
| Profit or loss per accounts | X/(X) |
| Add backs | X |
| Deductions | (X) |
| Capital Allowances | <u>(X)</u> |
| Case I Income or Loss | <u>X/(X)</u> |

How do trading losses arise?

Example:

| Case I Computation for year ended 31 December 2017 | Scenario 1 € | Scenario 2 € | Scenario 3 € |
|--|------------------------|------------------------|----------------------|
| Profit or (loss) per accounts | (30,000) | 40,000 | (50,000) |
| Add backs | 12,000 | 25,000 | 80,000 |
| Deductions | (10,000) | (50,000) | (2,000) |
| Capital Allowances | <u>(5,000)</u> | <u>(30,000)</u> | <u>(10,000)</u> |
| Case I Income or (Loss) | <u>(33,000)</u> | <u>(15,000)</u> | <u>18,000</u> |

| Corporation Tax Computation for year ended 31 December 2017 | Scenario 1 € | Scenario 2 € | Scenario 3 € |
|---|-----------------|-----------------|-----------------|
| Case I Income | Nil | Nil | 18,000 |

How are trading losses utilised?

There are three ways in which trading losses can be utilised for continuing trades:

1. Against other trading income in the same period (current period) and the immediately preceding period of the same length under [section 396A](#)
2. Against the corporation tax liability in the same period (current period) and the immediately preceding period of the same length under [section 396B](#)
3. Carried forward and ring-fenced against income of the same trade under [section 396\(1\)](#)

Section 396A

- The losses are offset against other trading income in the current period and the immediately preceding period of the same length.
- This relief is available on a **€ for € basis** against other relevant trading income (note - the trading income must be taxable at 12.5%)

Example 1

ABC Ltd incurred a Case I loss of €100,000 in the year ended 31 December 2017. The Case I income of ABC Ltd for the year ended 31 December 2016 was €100,000.

Section 396A Example 1

Example 1:

| CT Computation for year ended 31 December | 2016 € | 2017 € |
|---|-----------|-----------|
| Case I | 100,000 | Nil |
| | | |
| | | |

| Loss Memo | | 2017 |
|-------------|--|---------|
| Case I Loss | | 100,000 |
| | | |
| | | |

Section 396A Example 1

Example 1:

| CT Computation for year ended 31 December | 2016 € | 2017 € |
|---|------------------|-----------|
| Case I | 100,000 | Nil |
| S396A Loss relief | <u>(100,000)</u> | |
| Taxable income | <u>Nil</u> | |

Note CT for 2016 paid by 23/9/2017 was €100,000 x 12.5% = €12,500

| Loss Memo | | 2017 |
|---|--|------------------|
| Case I Loss | | 100,000 |
| S396A Against year ended 31 December 2016 | | <u>(100,000)</u> |
| Carried forward | | <u>Nil</u> |

Section 396A Example 2

S396A

*Against other trading income in the same period (current period) and the **immediately preceding period of the same length***

Example 2

ZYZ Ltd incurred a Case I loss of €120,000 in the **6 months** ended 30th June 2017.

The Case I income of ABC Ltd for the **year** ended 31 December 2016 was €90,000.

Section 396A Example 2

Example 2:

| CT Computation for period ended | 31 Dec 2016 € | 30 June 2017 € |
|---------------------------------|------------------|-------------------|
| Case I | 90,000 | Nil |
| | | |
| | | |

| Loss Memo | | 30 June 2017 |
|-------------|--|--------------|
| Case I Loss | | 120,000 |
| | | |
| | | |

Section 396A Example 2

Example 2:

| CT Computation for period ended | 31 Dec 2016 € | 30 June 2017 € |
|---------------------------------|------------------|-------------------|
| Case I | 90,000 | Nil |
| S396A | <u>(45,000)</u> | |
| Taxable Profits | <u>45,000</u> | |

Note CT for 2016 paid by 23/9/2017 was €90,000 x 12.5% = €11,250

| Loss Memo | | 30 June 2017 |
|--|--|-----------------|
| Case I Loss | | 120,000 |
| S396A Against 6/12 of year ended 31 December 2016 | | <u>(45,000)</u> |
| Carried forward (under S 396(1) ring-fenced to income of same trade) | | <u>55,000</u> |

Section 396B

- Relief under S396B is given on a “value basis” against the corporation tax liability for other non relevant trading income of the current period and the immediately preceding period of the same length.
- Value basis relief is calculated at the same rate as the trade in which the loss arose is taxed i.e. for relevant trades at 12.5%
- A company must use all available losses against other ring-fenced (trading) income in the current and preceding accounting period before utilising the excess on the value basis.

Section 396B Example 1

DC Ltd had a Case I loss of €100,000 in the year ended 31 December 2017 and a Case I profit of €20,000 in the year ended 31 December 2016.

DC Ltd also had Case V income of €12,000 in the year ended 31 December 2016 and €18,000 in the year ended 31 December 2017

Section 396A Example 1

Example 1:

| CT Computation for year ended 31 December | 2016 € | 2017 € |
|---|-----------|-----------|
| Case I | 20,000 | Nil |
| | | |
| Case V | 12,000 | 18,000 |

| Loss Memo | | 2017 |
|-------------|--|---------|
| Case I Loss | | 100,000 |
| | | |
| | | |

Section 396B Example 1

How will the loss be utilised?

- S396A** Against other trading income in the same period (current period) and the immediately preceding period of the same length

DC Ltd has no trading income in the current period but does have trading income in the preceding period of the same length.

The relief is available on a **€ for € basis** against other trading income of €20,000 in the year ended 31 December 2016.

Section 396B Example 1

Example 1:

| CT Computation for year ended 31 December | 2016 € | 2017 € |
|---|-----------|-----------|
| Case I | 20,000 | Nil |
| S396A | (20,000) | |
| Case V | 12,000 | 18,000 |

| Loss Memo | | 2017 |
|---|--|-----------------|
| Case I Loss | | 100,000 |
| S396A Against year ended 31 December 2016 | | <u>(20,000)</u> |
| Excess loss | | 80,000 |

Section 396B Example 1

How will the excess loss be utilised?

2. S396B On a “value basis” against the corporation tax liability on other non trading income of the current period and immediately preceding period of the same length.

But, we haven't yet calculated the CT liability for either period??

Section 396B Example 1

Example 1:

| CT Computation for year ended 31 December | 2016 € | 2017 € |
|---|---------------|---------------|
| Case I | 20,000 | Nil |
| S396A | (20,000) | |
| Case V | <u>12,000</u> | <u>18,000</u> |
| Taxable profits | <u>12,000</u> | <u>18,000</u> |
| Corporation Tax @ 25% | 3,000 | 4,500 |

Section 396B Example 1

There are tax liabilities of €3,000 and €4,500 in the year's ended 31 December 2016 and 2017 and there are excess losses available of €80,000.

We need to calculate how much losses must be used to generate the required value basis relief. Are there enough losses available?

| Tax liability | Divide by 12.5% tax rate = | Required losses |
|---------------|-------------------------------|-----------------|
| €4,500 | .125 | €36,000 |
| €3,000 | .125 | <u>€24,000</u> |
| | | <u>€60,000</u> |

Only €60,000 losses required, therefore we have enough losses.

Section 396B Example 1

Example 1:

| Loss Memo | 2017 |
|---|-----------------|
| Case I Loss | 100,000 |
| S396A Against year ended 31 December 2016 | <u>(20,000)</u> |
| Excess | 80,000 |
| S396B Value basis in year ended 31 December 2017 | (36,000) |
| S396B Value basis in year ended 31 December 2016 | <u>(24,000)</u> |
| Carried forward (S396(1) ring-fenced to income of same trade) | <u>20,000</u> |

Section 396B Example 1

Example 1:

| CT Computation for year ended 31 December | 2016 € | 2017 € |
|---|----------------|----------------|
| Case I | 20,000 | Nil |
| S396A | (20,000) | |
| Case V | <u>12,000</u> | <u>18,000</u> |
| Taxable profits | <u>12,000</u> | <u>18,000</u> |
| Corporation Tax @ 25% | 3,000 | 4,500 |
| S396B loss relief | <u>(3,000)</u> | <u>(4,500)</u> |
| | Nil | Nil |

Claims for Section 396A And 396B

Time limit for claims to be made under S396A and S396B = within 2 years of the end of accounting period in which the relevant trading loss arises.

Example

BF Ltd incurred a Case I loss in the year ended 30th June 2017.

A claim for loss relief under S396A and S396B must be made by 30th June 2019.

Note - A claim for relief under S396B can only be made in the amount of excess losses after deducting the losses which can be utilised under S396A regardless of whether the company actually makes such a claim.

Section 396B Example 1

Example 1 revisited:

| Loss Memo | 2017 |
|---|-----------------|
| Case I Loss | 100,000 |
| S396A Against year ended 31 December 2016 | <u>(20,000)</u> |
| Excess | 80,000 |
| S396B Value basis in year ended 31 December 2017 | (36,000) |
| S396B Value basis in year ended 31 December 2016 | <u>(24,000)</u> |
| Carried forward (S396(1) ring-fenced to income of same trade) | <u>20,000</u> |

Section 396(1)

Loss relief under S396(1) is taken in the next accounting period and is ring-fenced i.e. can only be used against income of the same trade.

The loss is automatically used in this way before any other type of loss relief.

Late Filing Restriction

- Corporation tax return filing deadline = within 9 months of the end of the accounting period, i.e. CT Return for year ended 31 December 2017 must be filed on or before 23 September 2018.
- Relief under S396A and S396B in the current period and preceding periods will be restricted by:
 - **25% where the return is filed late, but within 2 months of the deadline (subject to a maximum restriction of €31,740)**
 - **50% thereafter, (subject to a maximum restriction of €158,715)**

Step Plan for Loss Relief

1. Set out the corporation tax computations for each year/period and the loss memo on two separate pages (facing pages is easier in exams).
2. Insert the income given in the question into the relevant rows for each year.
3. Insert the loss amount in the loss memo
4. For trading losses, the order of utilisation will always be S396A before S396B (remember, you need to calculate corporation tax between utilisation of S396A and S396B)

Sample Loss Memo for Trading Losses

| Case I Loss Memo | Note | € |
|------------------|---|------------|
| Case I Loss | (Given in the question or negative answer calculated in the Case I comp) | X |
| S396A | Current period against trading income (only arises if the company has Case I income from another trade in the current period) | (X) |
| S396A | Prior period against trading income (make sure to apportion if the periods are not the same length) | <u>(X)</u> |
| Excess Loss | (Calculate the CT liabilities before moving to S396B) | X |
| S396B | Current period value basis (CT Liability / .125) | (X) |
| S396B | Prior period value basis (CT Liability / .125) (make sure to apportion if the periods are not the same length) | <u>(X)</u> |
| Carried Forward | (under S396(1) ring-fenced to income of same trade) | <u>X</u> |

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