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Briefing document

Cap on income tax reliefs

Introduction
The government introduced a cap from 6 April 2013 on the amount of sideways income tax loss relief (i.e. relief against general income) that can be claimed on certain reliefs, such as business losses and loan interest. The cap is the higher of £50,000 and 25% of total income (as adjusted for the purposes of the cap). Trading losses that exceed the cap are not lost altogether but are instead carried forward and relieved against future income from the same trade.

The cap does not affect reliefs that are already capped in some way, such as income tax relief available on acquisition of shares where investments are made under the Enterprise Investment Scheme (EIS), Seed Enterprise Investment Scheme (SEIS), Social Investment Tax Relief (SITR) or the Venture Capital Trust (VCT) scheme. Neither is relief for pension contributions and charitable donations affected.

The cap applies to the aggregate of the affected reliefs offset against income in a tax year, rather than applying to each relief separately.

Tax reliefs that are affected
The tax reliefs that are affected by the cap are those that are deducted from total income in determining the amounts liable to income tax, with a few exceptions. A number of reliefs are affected, the most common ones being:

- Relief for trading losses offset against general income, including relief for losses made in the first four years of trading;
- Relief for losses on disposal of unquoted shares (including losses on disposal of EIS, SEIS or SITR shares to which no income tax relief was attributable on subscription);
- Relief for excess capital allowances on property businesses; and
- Interest relief on qualifying loans (e.g. loans to invest in a partnership or to buy an interest in a close company).

Tax reliefs not affected by the cap
The cap on income tax relief is not applied to the following available reliefs:

- Deductions that are available when determining the amount of income from a particular source, such as capital allowance deductions from trading profits (although if capital allowances create or increase a trading loss, that loss would be affected by the cap).
- Trading losses carried back to an earlier tax year, or brought forward from an earlier tax year, and set against profits of the same trade to the extent that they are reducing those profits.
- Trade losses that arise as a result of overlap relief (which is a relief available in certain circumstances where profits are taxed twice at the commencement of trade or on change of accounting date).

- Losses on property businesses which are carried forward and offset against future profits from the same property business.

- Income tax relief on subscription for qualifying EIS, SITR or SEIS shares and on qualifying VCT investments.

- Relief for losses on disposal of EIS, SEIS or SITR shares on which income tax relief was available on subscription for those shares and which has not been completely clawed back. Loss relief on disposal of VCT shares is unavailable in any event.

Operation of the cap

The cap is the greater of £50,000 and 25% of the individual's "adjusted total income". Adjusted total income is, broadly, the total income in the tax computation plus charitable contributions relieved by way of payroll giving less pension contributions that have not already been relieved via payroll arrangements (e.g. contributions to personal pension schemes or retirement annuity premiums).

These adjustments are intended to ensure that there is a level playing field between individuals who have had the same level of pension contributions or charitable donations, but have had those amounts relieved in different ways. The effect of the calculation is to ensure that adjusted total income is measured after pension contributions (however made) but before charitable donations.

The cap applies to losses made from 2013/14 onwards, irrespective of the tax year in which they are set off. Where a relief is available for offset in more than one tax year (e.g. trading losses), the cap applies to the amount of loss which can be relieved in each tax year affected. For example, a trading loss in 2019/20 may be offset against income in 2018/19 and 2019/20. If the income for each of those years is less than £200,000, there would be caps for each year of £50,000, so losses of up to £100,000 could potentially be relieved across the two years.

Find out more…

This note reflects the law in force as at 6 April 2020. Please be aware that it does not cover all aspects of this subject. To find out more about any aspect of the above, please discuss with your usual Deloitte contact. If you do not have a usual contact, please contact Patricia Mock (pmock@deloitte.co.uk).

For further information visit our website at www.deloitte.co.uk.