



Income Tax (Trading and Other Income) Act 2005

2005 CHAPTER 5

PART 2

TRADING INCOME

CHAPTER 4

TRADE PROFITS: RULES RESTRICTING DEDUCTIONS

Employee benefit contributions

38 Restriction of deductions

[^{F1}(1) This section applies if, in calculating for income tax purposes the profits of a trade of a person (“the employer”) for a period, a deduction would otherwise be allowable for the period in respect of employee benefit contributions made or to be made (but see subsection (4)).]

[^{F2}(1A) No deduction is allowed under this section in respect of employee benefit contributions for a period of account which starts more than 5 years after the end of the period of account in which the contributions are made.]

- (2) No deduction is allowed for the contributions for the period except so far as—
- qualifying benefits are provided, or qualifying expenses are paid, out of the contributions during the period or within 9 months from the end of it, or
 - if the making of the contributions is itself the provision of qualifying benefits, the contributions are made during the period or within 9 months from the end of it.

[^{F3}(2AA) Subsection (2) is subject to subsections (1A) and (2AB).

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- (2AB) Where subsection (3C) applies, no deduction is allowed for an amount in respect of the contributions for the period except so far as the amount is a qualifying amount (see subsection (3D)).]
- [^{F4}(2A) In calculating for income tax purposes the profits of a trade on the cash basis, this section has effect as if—
- (a) in subsection (1), the words “or to be made” were omitted, and
 - (b) in subsection (2), the words “or within 9 months from the end of it” were omitted (in both places).]
- (3) An amount disallowed under subsection (2) is allowed as a deduction for a subsequent period so far as—
- (a) qualifying benefits are provided out of the contributions before the end of the subsequent period, or
 - (b) if the making of the contributions is itself the provision of qualifying benefits, the contributions are made before the end of the subsequent period.
- [^{F5}(3A) Subsection (3) is subject to subsections (1A) and (3B).
- (3B) Where subsection (3C) applies, an amount disallowed under subsection (2) is allowed as a deduction for a subsequent period only so far as it is a qualifying amount.
- (3C) This subsection applies where the provision of qualifying benefits out of, or by way of, the contributions gives rise both to an employment income tax charge and to an NIC charge.
- (3D) An amount in respect of employee benefit contributions is a “qualifying amount” if the relevant tax charges are paid before the end of the relevant period (and are not repaid).
- (3E) For the purposes of subsection (3D)—
- (a) the “relevant tax charges”, in relation to an amount, are the employment income tax charge and the NIC charge arising in respect of benefits which are provided out of, or by way of, that amount, and
 - (b) the “relevant period” is the period of 12 months immediately following the end of the period of account for which the deduction for the employee benefit contributions would (apart from this section) be allowable.
- (3F) For the purposes of subsections (3C) and (3E), “employment income tax charge” and “NIC charge” have the meaning given by section 40(7).]
- [^{F6}(3G) Subsection (3H) applies where—
- (a) a deduction would, apart from this section, be allowable for an amount (the “remuneration amount”) in respect of employees' remuneration, and
 - (b) in consequence of the payment of the employees' remuneration, employee benefit contributions are made, or are to be made, in respect of the remuneration amount.
- (3H) In calculating for income tax purposes the profits of a trade, the deduction referred to in subsection (3G)(a) is to be treated as a deduction in respect of employee benefit contributions made or to be made (and is to be treated as not being a deduction in respect of employees' remuneration).]
- (4) This section does not apply to any deduction that is allowable for—

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- (a) anything given as consideration for goods or services provided in the course of a trade or profession,
- (b) contributions under a registered pension scheme or under a superannuation fund to which section 615(3) of ICTA applies,
- (c) contributions under a qualifying overseas pension scheme in respect of an individual who is a relevant migrant member of the pension scheme in relation to the contributions, or
- (d) contributions under an accident benefit scheme.

For the purposes of paragraph (c) “qualifying overseas pension scheme” and “relevant migrant member” have the same meaning as in Schedule 33 to FA 2004 (see paragraphs 4 to 6 of that Schedule).

(5) See also—

- section 39 (making of “employee benefit contributions”),
- section 40 (provision of qualifying benefits),
- section 41 (timing and amount of certain qualifying benefits),
- section 42 (provision or payment out of employee benefit contributions),
- section 43 (profits calculated before end of 9 month period), and
- section 44 (interpretation of sections 38 to 44).

Textual Amendments

- F1** S. 38(1) substituted (with effect as stated in s. 34(13) of the amending Act) by [Finance Act 2007 \(c. 11\), s. 34\(8\)](#)
- F2** S. 38(1A) inserted (16.11.2017) (with effect in accordance with s. 36(11) of the amending Act) by [Finance \(No. 2\) Act 2017 \(c. 32\), s. 36\(2\)](#)
- F3** S. 38(2AA)(2AB) inserted (16.11.2017) (with effect in accordance with s. 36(11) of the amending Act) by [Finance \(No. 2\) Act 2017 \(c. 32\), s. 36\(3\)](#)
- F4** S. 38(2A) inserted (with effect in accordance with Sch. 4 paras. 56, 57 of the amending Act) by [Finance Act 2013 \(c. 29\), Sch. 4 para. 9](#)
- F5** S. 38(3A)-(3F) inserted (16.11.2017) (with effect in accordance with s. 36(11) of the amending Act) by [Finance \(No. 2\) Act 2017 \(c. 32\), s. 36\(4\)](#)
- F6** S. 38(3G)(3H) inserted (16.11.2017) (with effect in accordance with s. 36(12) of the amending Act) by [Finance \(No. 2\) Act 2017 \(c. 32\), s. 36\(5\)](#)

39 Making of “employee benefit contributions”

[^{F7}(1) For the purposes of section 38, an “employee benefit contribution” is made if, as a result of any act or omission—

- (a) property is held, or may be used, under an employee benefit scheme, or
- (b) there is an increase in the total value of property that is so held or may be so used (or a reduction in any liabilities under an employee benefit scheme).]

(2) For this purpose “employee benefit scheme” means a trust, scheme or other arrangement for the benefit of persons who are, or include, present or former employees of the employer [^{F8} or persons linked with present or former employees of the employer] .

[^{F9}(3) Section 554Z1 of ITEPA 2003 applies for the purposes of subsection (2) but as if references to A were to a present or former employee of the employer.

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- (4) So far as it is not covered by subsection (2), “employee benefit scheme” also means—
- [^{F10}(a) an arrangement (the “relevant arrangement”) which is—
- (i) an arrangement within subsection (1)(b) of section 554A of ITEPA 2003 to which subsection (1)(c) of that section applies, or
- (ii) an arrangement within subsection (1)(b) of section 554AA of ITEPA 2003 to which subsection (1)(c) of that section applies,] or
- (b) any other arrangement connected (directly or indirectly) with the relevant arrangement.]

Textual Amendments

- F7** S. 39(1) substituted (19.7.2007 with effect as stated in s. 34(13) of the amending Act) by [Finance Act 2007 \(c. 11\)](#), [s. 34\(9\)](#)
- F8** Words in s. 39(2) inserted (with effect in accordance with Sch. 2 para. 52-59 61 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 36\(2\)](#)
- F9** S. 39(3)(4) inserted (with effect in accordance with Sch. 2 para. 52-59 61 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 36\(3\)](#)
- F10** S. 39(4)(a) substituted (with effect in accordance with Sch. 1 para. 15 of the amending Act) by [Finance Act 2018 \(c. 3\)](#), [Sch. 1 para. 6](#)

40 Provision of qualifying benefits

- (1) For the purposes of section 38 qualifying benefits are provided if there is—
- (a) a payment of money, or
- (b) a transfer of assets,
- which meets condition A, B, C or D.
- (2) Condition A is that the payment or transfer gives rise both to an employment income tax charge and to an NIC charge.
- (3) Condition B is that the payment or transfer would give rise to both charges if—
- (a) the duties of the employment in respect of which the payment or transfer was made were performed in the United Kingdom, and
- (b) the person in respect of whose employment the payment or transfer was made met at all relevant times the conditions as to residence or presence in Great Britain or Northern Ireland prescribed under section 1(6) of the Contributions and Benefits Act.
- (4) Condition C is that the payment or transfer is made in connection with the termination of the recipient's employment with the employer.
- (5) Condition D is that the payment or transfer is made under an employer-financed retirement benefits scheme^{F11} and the payment or transfer—
- (a) gives rise to an employment income tax charge under Chapter 2 of Part 6 of ITEPA 2003 or under Part 9 of that Act, or
- (b) is an excluded benefit as defined in section 393B(3) of that Act.]
- (6) None of the conditions is met if the payment or transfer is by way of loan.
- [^{F12}(6A) For the purposes of section 38 qualifying benefits are also provided if—
- (a) a relevant step within the meaning of Part 7A of ITEPA 2003 is taken, and

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(b) Chapter 2 of that Part applies by reason of the step.]

(7) In this section—

“the Contributions and Benefits Act” means—

- (a) the Social Security Contributions and Benefits Act 1992 (c. 4), or
- (b) the Social Security Contributions and Benefits (Northern Ireland) Act 1992 (c. 7),

“employment income tax charge” means a charge to tax under ITEPA 2003 (whether on the recipient or on someone else), and

“NIC charge” means a liability to pay national insurance contributions under section 6 (Class 1 contributions), section 10 (Class 1A contributions) or section 10A (Class 1B contributions) of the Contributions and Benefits Act.

Textual Amendments

F11 Words in s. 40(5) inserted (with effect in accordance with Sch . 2 para. 52-59 62 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 37\(2\)](#)

F12 S. 40(6A) inserted (with effect in accordance with Sch . 2 para. 52-59 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 37\(3\)](#)

41 Timing and amount of certain qualifying benefits

[^{F13}(1) If the provision of a qualifying benefit takes the form of a payment of money, the benefit, so far as Chapter 4 of Part 2 of ITEPA 2003 applies to the money, is provided for the purposes of section 38 when the money is treated as received for the purposes of that Chapter (applying the rules in section 18 of that Act (receipt of money earnings)).]

[^{F14}(1A) Except so far as subsection (1) applies to the provision of the qualifying benefit, if the provision of a qualifying benefit is a chargeable relevant step, for the purposes of section 38—

- (a) the benefit is provided when A's employment with B starts if the chargeable relevant step is taken before then, or
- (b) otherwise, the benefit is provided when the chargeable relevant step is taken.]

(2) If the provision of a qualifying benefit takes the form of a transfer of an asset [^{F15} which meets condition A, B, C or D in section 40], the amount provided for the purposes of section 38 is the total of—

- (a) the amount (if any) spent on the asset by [^{F16}a scheme manager] , ^{F17}...
- (b) in a case where the asset was transferred to [^{F16}a scheme manager] by the employer, the amount of the deduction that would be allowable as mentioned in subsection (1) of that section in respect of the transfer^{F18}, and
- (c) if the transfer is a chargeable relevant step, the cost of the relevant step so far as not covered by paragraph (a) or (b).]

(3) But if the amount given by subsection (2) is more than the amount that—

- (a) is charged to tax under ITEPA 2003 in respect of the transfer, or
- (b) would be so charged if condition B in section 40 were met,

the deduction allowable under section 38(2) or (3) is limited to that lower amount.

[^{F19}(4) If the provision of a qualifying benefit is a chargeable relevant step which does not involve a sum of money (see section 554Z(10) of ITEPA 2003) and is not covered by

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subsection (2), the amount provided for the purposes of section 38 is the cost of the relevant step (subject to subsection (5)).

- (5) If the provision of a qualifying benefit is a chargeable relevant step which is not covered by subsection (2) (whether or not it involves a sum of money), the amount provided for the purposes of section 38 is not to exceed the amount that—
- (a) is charged to tax under ITEPA 2003 in relation to the relevant step (whether under Part 7A of that Act or otherwise), or
 - (b) would be charged had not A been non-UK resident in any tax year.
- (6) In this section—
- (a) “chargeable relevant step” means a relevant step within the meaning of Part 7A of ITEPA 2003 by reason of which Chapter 2 of that Part applies (and references to A and B are to be read accordingly), and
 - (b) references to the cost of a chargeable relevant step are to be read in accordance with section 554Z3(6) of that Act.]

Textual Amendments

- F13** S. 41(1) substituted (with effect in accordance with Sch. 2 paras. 52-59, 63 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 38\(2\)](#)
- F14** S. 41(1A) inserted (with effect in accordance with Sch. 2 paras. 52-59 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 38\(3\)](#)
- F15** Words in s. 41(2) inserted (with effect in accordance with Sch. 2 paras. 52-59 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 38\(4\)\(a\)](#)
- F16** Words in s. 41 substituted (19.7.2007 with effect as stated in [s. 34\(13\)](#) of the amending Act) by [Finance Act 2007 \(c. 11\)](#), [s. 34\(10\)](#)
- F17** Word in s. 41(2) omitted (with effect in accordance with Sch. 2 paras. 52-59 of the amending Act) by virtue of [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 38\(4\)\(b\)](#)
- F18** S. 41(2)(c) and word inserted (with effect in accordance with Sch. 2 paras. 52-59 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 38\(4\)\(c\)](#)
- F19** S. 41(4)-(6) inserted (with effect in accordance with Sch. 2 paras. 52-59 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 38\(5\)](#)

42 Provision or payment out of employee benefit contributions

- (1) For the purposes of section 38(2)(a)—
- (a) any qualifying benefits provided, or
 - (b) any qualifying expenses paid,
- by [^{F20}a scheme manager] after the receipt by [^{F21}the scheme manager] of employee benefit contributions are treated as being provided or paid out of the contributions.
- (2) This operates up to the total amount of the contributions reduced by the amount of any benefits or expenses previously provided or paid as mentioned in section 38(2)(a).
- (3) For the purposes of section 38(3)(a) any qualifying benefits provided by [^{F22}a scheme manager] after the receipt by [^{F23}the scheme manager] of employee benefit contributions are treated as being provided out of the contributions.
- (4) This operates up to the total amount of the contributions reduced by the amount of any benefits or expenses previously provided or paid as mentioned in section 38(2)(a) or (3)(a).

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- (5) For the purposes of this section no account is taken of any other amount received or paid by the [F24 scheme manager] .

Textual Amendments

- F20** Words in s. 42(1) substituted (19.7.2007 with effect as stated in s. 34(13) of the amending Act) by Finance Act 2007 (c. 11), s. 34(11)(a)
- F21** Words in s. 42(1) substituted (19.7.2007 with effect as stated in s. 34(13) of the amending Act) by Finance Act 2007 (c. 11), s. 34(11)(a)
- F22** Words in s. 42(3) substituted (19.7.2007 with effect as stated in s. 34(13) of the amending Act) by Finance Act 2007 (c. 11), s. 34(11)(b)
- F23** Words in s. 42(3) substituted (19.7.2007 with effect as stated in s. 34(13) of the amending Act) by Finance Act 2007 (c. 11), s. 34(11)(b)
- F24** Words in s. 42(5) substituted (19.7.2007 with effect as stated in s. 34(13) of the amending Act) by Finance Act 2007 (c. 11), s. 34(11)(c)

43 Profits calculated before end of 9 month period

- (1) This section applies if the profits of the trade are calculated before the end of the 9 month period mentioned in section 38(2).
- (2) It must be assumed, in making the calculation, that any benefits, expenses or contributions which are not provided, paid or made when the calculation is made will not be provided, paid or made before the end of that period.
- (3) But if the benefits, expenses or contributions are subsequently provided, paid or made before the end of that period, nothing in this section prevents the calculation being revised and any tax return being amended accordingly.

44 Interpretation of sections 38 to 44

- (1) In this section and sections 38 to 43—
- “accident benefit scheme” means an employee benefit scheme under which benefits may be provided only by reason of a person's disablement, or death, caused by an accident occurring during the person's service as an employee of the employer,
- “employee benefit contribution” is to be read in accordance with section 39(1),
- “employee benefit scheme” has the meaning given by section [F25 39(2) to (4)] ,
- “the employer” is to be read in accordance with section 38(1),
- “employer-financed retirement benefits scheme” has the same meaning as in Chapter 2 of Part 6 of ITEPA 2003 (see section 393A of that Act), [F26 but ignoring section 393B(2)(a) and (c) of that Act]
- “qualifying benefits” is to be read in accordance with section 40,
- “qualifying expenses” includes any expenses of the third party (other than the provision of benefits to employees of the employer)—
- (a) which are incurred in operating the employee benefit scheme, and
- (b) which, if incurred by the employer, would be deductible in calculating for income tax purposes the employer's profits for any period, and

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[^{F27}“scheme manager” means a person who administers an employee benefit scheme (acting in that capacity).]

(2) A reference in this section and sections 38 to 43 to a person's employee includes the holder of an office under that person, and “employment” is to be read accordingly.

Textual Amendments

- F25** Words in s. 44(1) substituted (with effect in accordance with Sch. 2 paras. 52-59 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 39\(a\)](#)
- F26** Words in s. 44(1) inserted (with effect in accordance with Sch. 2 paras. 52-59, 62 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 39\(b\)](#)
- F27** S. 44(1): definition of "third party" substituted (19.7.2007 with effect as stated in [s. 34\(13\)](#) of the amending Act) by [Finance Act 2007 \(c. 11\)](#), [s. 34\(12\)](#)

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Changes and effects yet to be applied to the whole Act associated Parts and Chapters:

Whole provisions yet to be inserted into this Act (including any effects on those provisions):

- s. 7A-7D inserted by [2022 c. 3 Sch. 1 para. 3](#)
- s. 31E(4) inserted by [2022 c. 3 Sch. 1 para. 7\(3\)](#)
- s. 649(1A)(1B) inserted by [2023 c. 30 Sch. 2 para. 11\(2\)](#)
- s. 679(3A) inserted by [2023 c. 30 Sch. 2 para. 11\(5\)\(b\)](#)
- s. 679A(3A) inserted by [2023 c. 30 Sch. 2 para. 11\(6\)\(b\)](#)
- s. 680(1A) inserted by [2023 c. 30 Sch. 2 para. 11\(7\)\(a\)](#)