

# CORPORATION TAX ACT 2009

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## EXPLANATORY NOTES

### COMMENTARY ON SECTIONS

#### **Part 16: Companies with investment business**

##### **Overview**

3077. Expenses of management (generally known as “management expenses”) are designed to give relief for the cost of managing an investment business on broadly the same basis as relief for trading expenses or expenses of a property business.
3078. Originally relief was given for expenses “disbursed” but changes in 2004 brought the relief (and the recovery of relief) more closely into line with the treatment of the corresponding items in a company’s accounts. So, for instance, sections 1225 and 1231 rely on the concept of “generally accepted accounting practice”.

##### **Chapter 1: Introduction**

##### **Section 1217: Overview of Part**

3079. This section introduces the Part. It is new.
3080. This Act does not rewrite section 76 of ICTA (expenses of insurance companies). Instead, it inserts sections 76ZA to 76ZO into ICTA, to provide a version of the trading income rules adapted to insurance companies to which section 76 of ICTA applies. For companies carrying on life assurance business, but not charged in accordance with the trading income rules, this Part does not apply. Instead, the rules in section 76 apply.

##### **Section 1218: “Company with investment business” and “investment business”**

3081. This section sets out which companies are within the rules in this Part of the Act. It is based on sections 75 and 130 of ICTA.
3082. *Subsection (2)* is the rule that a credit union is not a company with investment business.
3083. The rule applies for the purposes of this Part of the Act. So there is no possibility of a charge on a credit union under section 1254 on a FISMA repayment. See *Change 80* in Annex 1.
3084. *Subsection (3)* is a signpost to section 1219(2) which restricts the application of this Part of the Act to the part of the company’s business which is an investment business. But that restriction does not affect the basic definition of a “company with investment business”.
3085. *Schedule 1* to this Act amends section 18 of CAA so that “managing the investments of a company with investment business” in section 15(1)(g) of CAA is defined by reference to sections 1218 and 1219 of this Act. So there is no need for a separate rule to the effect that a credit union is not a company with investment business for the purposes of CAA.

## **Chapter 2: Management expenses**

### **Section 1219: Expenses of management of a company's investment business**

3086. This section sets out what are “expenses of management”. It is based on section 75 of ICTA.
3087. There is no explicit definition of “expenses of management” either in the source legislation or in this Act. Instead, the limits of the expression are set by:
- case law, in which the expression (retained in this Act) has been considered;
  - general exclusions set out in this section;
  - specific reliefs set out in Chapter 3 of this Part; and
  - specific restrictions set out in Chapter 4 of this Part.
3088. *Subsection (1)* ties the expenses to the management of the company's investment business (defined in section 1218), and to the accounting period to which the expenses are “referable” (see section 1224).
3089. The section provides that the expenses are allowed as a deduction, echoing the words of Part 3 (trading income). HMRC guidance (see paragraph 8580 of the Company Taxation Manual) suggests that the deduction of management expenses is mandatory. But this amounts to the same thing.
3090. Both restrictions in *subsection (2)* apply for the purposes of this Part (see section 1218).
3091. *Subsection (3)* excludes capital expenditure, in terms that follow closely the trading income rule. It also prevents a deduction as management expenses for anything that is otherwise allowable for tax purposes.

### **Section 1220: Meaning of “unallowable purpose”**

3092. This section explains “unallowable purpose”, an expression used in section 1219(2)(b). It is based on section 75 of ICTA.
3093. *Subsection (1)* is the basic rule that explains the ordinary meaning of “unallowable purpose”.
3094. *Subsection (2)* extends “unallowable purpose” to include investments held in connection with arrangements to secure a tax advantage.

### **Section 1221: Amounts treated as expenses of management**

3095. This section makes clear the relationship between two of the rules in section 1219 and rules elsewhere in this Part. It is based on section 75 of ICTA.
3096. The rule in section 1219(3)(a) which excludes capital expenditure is not applied to a rule that treats an amount as an expense of management.
3097. Similarly, the rule in section 1219(2) that expenses must be “in respect of” the company's investment business is not applied to a rule that makes an amount deductible as an expense of management. See *Change 81* in Annex 1.

### **Section 1222: Income from a source not charged to tax**

3098. This section requires non-taxable income to be set off against management expenses. It is based on section 75 of ICTA.

***Section 1223: Carrying forward expenses of management and other amounts***

3099. This section allows excess management expenses to be carried forward. It is based on section 75 of ICTA.

***Section 1224: Accounting period to which expenses are referable***

3100. This section introduces the timing rules for management expenses. It is based on section 75A of ICTA.

3101. *Subsection (2)* makes clear that the general rules in this Chapter may be overridden by a specific timing rule elsewhere.

***Section 1225: Accounts conforming with GAAP***

3102. This section gives the timing rule in the two most common cases. It is based on section 75A of ICTA.

3103. *Subsection (1)* deals with the first most common case. The management expenses are “referable to” the accounting period for which accounts are drawn up in accordance with generally accepted accounting practice (“GAAP”). GAAP is defined in section 50(1) of FA 2004.

3104. UK generally accepted accounting practice is defined in section 50(4) of FA 2004.

3105. *Subsection (2)* deals with the second most common case. GAAP accounts are drawn up. But the period of the accounts does not coincide with the company’s accounting period. The expenses are apportioned.

3106. *Subsection (3)* sets out the basis of apportionment. It retains the words “it appears that” because they may make the test easier to meet than an apparently objective test (“if the method would work unreasonably ...”). But the second “appears” in section 75A(5) of ICTA (“such other method ... as appears just and reasonable”) is dropped as it adds nothing. So the wording here is consistent with other “just and reasonable” apportionments in the Act. The same point arises in connection with section 1229(6).

***Section 1226: Accounts not conforming with GAAP***

3107. This section gives the timing rule if accounts are not GAAP compliant. It is based on section 75A of ICTA.

***Section 1227: Accounts not drawn up***

3108. This section gives the timing rule if there are no accounts. It is based on section 75A(7) and (8) of ICTA.

3109. The rule is that the management expenses are “referable to” the accounting period into which they would have fallen if GAAP accounts had been drawn up.

3110. There are alternative definitions of GAAP in section 50 of FA 2004. International standards apply if the company “prepares accounts in accordance with international accounting standards”. In any other case (including the case where no accounts are prepared), the United Kingdom standard (UK GAAP) applies.

3111. The combined effect of section 50(1) and (4) of FA 2004 is that in section 75A(8) GAAP means UK GAAP. A similar point arises in section 1231. In each case the section specifies UK GAAP.

***Section 1228: Credits that reverse debits***

3112. This section explains that the credits in accounts with which sections 1229 and 1230 are concerned include repayments and amounts never paid. It is based on section 75B of ICTA.

***Section 1229: Claw back of relief***

3113. This section applies the corporation tax charge to credits in accounts that reverse management expenses. It is based on section 75B of ICTA.

3114. *Subsection (5)* provides for any necessary apportionment of the company's accounts to accounting periods.

3115. *Subsection (6)* sets out the basis of apportionment. It retains the words "it appears that" because they may make the test easier to meet than an apparently objective test ("if the method would work unreasonably ..."). But the second "appears" in section 75B(6) of ICTA ("such other method ... as appears just and reasonable") is dropped as it adds nothing. So the wording here is consistent with other "just and reasonable" apportionments in the Act. The same point arises in connection with section 1225(3).

***Section 1230: Meaning of "reversal amount"***

3116. This section calculates the reversal amount. It is based on section 75B of ICTA.

3117. The calculation is set out in a method statement that excludes from the credit in the accounts:

- anything that does not relate to management expenses previously allowed; and
- anything that has already been taxed.

***Section 1231: Absence of accounts***

3118. This section sets out what happens if there are no accounts. It is based on sections 75B and 578A of ICTA.

3119. The reversal amount is the amount that would have been credited to GAAP accounts for the company's accounting period.

3120. There are alternative definitions of GAAP in section 50 of FA 2004. International standards apply if the company "prepares accounts in accordance with international accounting standards". In any other case (including the case where no accounts are prepared), UK GAAP applies.

3121. The combined effect of section 50(1) and (4) of FA 2004 is that in section 75B(10) GAAP means UK GAAP. A similar point arises in section 1227. In each case the section specifies UK GAAP.

***Chapter 3: Amounts treated as expenses of management***

***Section 1232: Chapter applies to amounts not otherwise relieved***

3122. This section is a priority rule. It is based on section 75 of ICTA.

3123. If an expense falls within the general rule for management expenses in section 1219(1) that section takes priority over the rules in this Chapter. And if an expense is otherwise deductible for tax purposes the rules in this Chapter do not apply to it.

***Section 1233: Excess capital allowances***

3124. This section gives a deduction for some capital allowances. It is based on section 75 of ICTA.

3125. A company with an investment business carries on a “qualifying activity” (see section 15(1)(g) of CAA). The rule in section 253 of CAA is that capital allowances are to be deducted in calculating the profits of the business. But, if there is an excess of allowances, the excess is treated as management expenses and can be set against profits generally.

### ***Sections 1234 to 1246***

#### **Overview**

3126. The following 13 sections are equivalent to trading income sections.
3127. Generally there are no timing rules in the sections. So a deduction is made in the accounting period to which it is “referable” in accordance with section 1224. There are two exceptions: sections 1240(4) and 1242(4) require the deduction for a redundancy payment to be made in the final accounting period of the business if the payment is made after the business has ceased.

#### ***Section 1234: Payments for restrictive undertakings***

3128. This section allows a company to deduct certain amounts paid to employees for restrictive undertakings. It is based on section 73 of FA 1988. The corresponding rule for trading income is in section 69.

#### ***Section 1235: Employees seconded to charities and educational establishments***

3129. This section allows a company carrying on investment business to deduct the cost of an employee seconded to a charity or educational establishment. It is based on section 86 of ICTA. The corresponding rule for trading income is in section 70.
3130. The rule in section 86 of ICTA is that the cost of the employee “shall continue to be deductible in the manner and to the like extent” as if the employee continued to work in the employer’s business. This section allows the employer to deduct *all* costs attributable to the seconded employee during the period of the secondment, regardless of whether those costs would have been allowed if the employee had not been seconded. See *Change 14* in Annex 1.

#### ***Section 1236: Payroll deduction schemes***

3131. This section allows an employer a deduction for expenses incurred in operating the payroll deduction scheme. It is based on section 86A of ICTA. The corresponding rule for trading income is in section 72.

#### ***Section 1237: Counselling and other outplacement services***

3132. This section gives a deduction for certain expenses of counselling provided for employees. It is based on section 589A of ICTA. The corresponding rule for trading income is in section 73.

#### ***Section 1238: Retraining courses***

3133. This section gives a deduction for certain expenses of retraining provided for employees. It is based on section 588 of ICTA. The corresponding rule for trading income is in section 74.
3134. The section does not rewrite section 588(3)(b) of ICTA. That provision makes a deduction as a management expense conditional on the employee’s exemption under section 311 of ITEPA in respect of the expenditure in question. This condition is not consistent with the similar provision in section 1237 and does not serve any material purpose. See *Change 16* in Annex 1.

### ***Sections 1239 to 1243: Redundancy payments etc***

3135. These five sections are based on sections 90, 579 and 580 of ICTA. The parts of the rules that deal with the employee's liability are in section 309 of ITEPA. The corresponding rules for trading income are in sections 76 to 81.

#### **Timing**

3136. In sections 1240(4) and 1242(4) there is a special timing rule for management expenses. For trading income the Act adopts a "person-based" approach. So the corresponding trading income rules refer to a "payment ... made after the employer has permanently ceased to carry on the trade [or part of the trade]".
3137. In these sections the rules refer to a payment "referable to ... an accounting period beginning after the business [or the part of the business] has [permanently] ceased to be carried on". This produces the same result as the trading income sections, without the need to explain the rule for businesses carried on in partnership.
3138. If an investment business ceases, the closing words of the second sentence of section 90(1) and section 579(3A) of ICTA make the payments referable to the "accounting period ending on the last day on which the ... business was carried on". These sections specify instead "the last accounting period in which the business was carried on". See *Change 82* in Annex 1.

#### **Just and reasonable apportionment**

3139. [Section 1241\(2\)](#) requires a "just and reasonable" apportionment. Section 579(5) of ICTA does not specify the basis of apportionment. See *Change 12* in Annex 1.

#### **Part of a business**

3140. [Section 1242](#) applies to payments in connection with the cessation of *part* of a business in the same way as it applies to payments in connection with the cessation of a whole business. See *Change 17* in Annex 1.

#### **Devolution**

3141. [Section 1243\(2\)\(b\)](#) reflects the effect of the devolution settlements. See *Change 15* in Annex 1.

### ***Section 1244: Contributions to local enterprise organisations or urban regeneration companies***

3142. This section allows deductions for contributions to local enterprise agencies, training and enterprise councils, local enterprise companies in Scotland, business links and urban regeneration companies. It is based on sections 79, 79A and 79B of ICTA. The corresponding rule for trading income is in section 82.
3143. *Subsection (3)* is an anti-avoidance rule. It prevents a company using the section to obtain a deduction for non-commercial expenditure, such as funding the training of a member of a shareholder's family, by passing funds through one of these bodies. The source legislation disallows any deduction if there is a benefit to the company (or a connected person). This section merely restricts the deduction by the value of the benefit. See *Change 18* in Annex 1.
3144. *Subsection (6)* of this section invokes the supporting sections 83 and 86.
3145. If a disqualifying benefit is later received it is charged to tax by section 1253.



### ***Section 1245: Payments to Export Credits Guarantee Department***

3146. This section allows a company to deduct the cost of certain payments to the Export Credits Guarantee Department. It is based on section 88 of ICTA. The corresponding rule for trading income is in section 91.

### ***Section 1246: Levies under FISMA 2000***

3147. This section allows a deduction for certain payments arising from FISMA. It is based on section 76B of ICTA. The corresponding rule for trading income is in section 92.

3148. A company carrying on investment business may be called upon to make payments in connection with FISMA. The payments are of two sorts:

- a “levy” to meet the running costs of the schemes set up by FISMA; and
- “costs” which may be awarded at the conclusion of a hearing of a complaint.

3149. Section 76B of ICTA allows as a management expense both sorts of payment. But there is a difficulty with one sort of levy. So some changes are made in this section and in the trading income section to ensure that all the payments under FISMA qualify for a deduction. Schedule 1 to this Act makes a corresponding relaxation in section 155 of ITTOIA. See *Change 22* in Annex 1.

## ***Chapter 4: Rules restricting deductions***

### ***Section 1247: Introduction***

3150. This section introduces the Chapter. It is new.

3151. *Subsection (2)* lists rules outside this Part that affect the calculation of management expenses. All these rules in the source legislation are drafted in wide terms (for instance, “for the purpose of calculating profits or other income charged to corporation tax”). The rules apply to the calculation of management expenses because that is part of the calculation of profits charged to corporation tax.

3152. In some cases the application of the rewritten rules is restricted so that they do not apply in calculating the profits of a trade or property business. That is because there is an equivalent rule in Part 3 (trading income) which is also applied to property income by section 210.

3153. The permissive rules for management expenses in Chapter 3 of this Part say that expenses are “treated for the purposes of Chapter 2 as expenses of management”. The restrictive rules in this Chapter “restrict the deduction of expenses of management under section 1219” (which is in Chapter 2). So it is clear that the restrictive rules have priority.

3154. This is the reverse of the position for trading income, where the general rule in section 51 is that the permissive rules have priority. But, in the unusual cases where it is possible for the rules to overlap, the result is the same.

3155. *Subsection (3)* draws attention to section 196A of FA 2004. This rule about pension scheme contributions does not itself restrict management expenses. But it gives HMRC power to make regulations that may make such a restriction.

### ***Section 1248: Expenses in connection with arrangements for securing a tax advantage***

3156. This section disallows expenses incurred in connection with arrangements to secure a tax advantage. It is based on section 75 of ICTA.

3157. *Subsections (1)* and *(2)* are the basic rule that the expenses are not allowed as management expenses. The wording of the subsections echoes that of section 1220,

which treats investments held in connection with arrangements to secure a tax advantage as held for a disallowable purpose.

3158. *Subsection (3)* establishes an order of priority for “disallowable purposes” rules.
- If the investments concerned are held for an unallowable purpose, the expenses are not expenses of management of the company’s investment business (section 1219(2)(b)).
  - Otherwise, if a manufactured payment is made in pursuance of arrangements that have an unallowable purpose, relief may be denied for the payment by paragraph 7A of Schedule 23A to ICTA.
  - If neither of these applies, this section may apply.

### ***Section 1249: Unpaid remuneration***

3159. This section delays a deduction for employees’ (or an office-holder’s) pay if it is paid late. The section is based on section 44 of FA 1989. The corresponding rule for other businesses (based on section 43 of FA 1989) is in section 1288.

### ***Section 1250: Unpaid remuneration: supplementary***

3160. This section provides definitions and further explanation of the main rule in section 1249. It is based on section 44 of FA 1989. The corresponding rule for other businesses (based on section 43 of FA 1989) is in section 1289.
3161. *Subsection (1)* applies section 1249 to provisions made in the accounts for amounts that may become employees’ remuneration.
3162. *Subsection (3)* deals with the case in which the company submits its tax return before the end of the nine month limit in section 1249(2) and all or any of the remuneration is unpaid. The company must assume the remuneration will remain unpaid. If, subsequently, the remuneration is paid within the time limit the calculation can be adjusted and the return amended. See *Change 68* in Annex 1.

### ***Section 1251: Car or motor cycle hire***

3163. This section restricts the amount that a company can deduct in respect of the cost of hiring certain cars or motor cycles with a retail price (when new) of more than £12,000. The section is based on sections 578A and 578B of ICTA. The corresponding rule for trading income is in section 56.
3164. Under section 75B(3) of ICTA any recovery of the hire charge is restricted to the reversal of “so much of the debit as represents the expenses of management.” *Subsection (4)* makes this restriction explicit and mirrors the trading income rule in section 56(4). See *Change 83* in Annex 1.
3165. *Subsection (7)* of the section invokes the supporting sections 57 and 58. So the definition of “qualifying hire car or motor cycle” includes a car or motor cycle where ownership passes without the exercise of an option to purchase. See the commentary on section 57 and *Change 10* in Annex 1.

## ***Chapter 5: Companies with investment business: receipts***

### ***Section 1252: Industrial development grants***

3166. This section deals with the treatment of certain grants under the Industrial Development Act 1982 or the corresponding provision in Northern Ireland. It is based on section 93 of ICTA. The corresponding rule for trading income is in section 102.



3167. Under section 93(1) of ICTA the payment of a grant is “taken into account as a receipt in computing [the company’s] profits under Case VI of Schedule D”. Under section 70(1) of ICTA the basis of assessment for Schedule D is the “profits gains or income arising” in an accounting period. But there is no explicit rule to say into which accounting period the grant falls.

***Section 1253: Contributions to local enterprise organisations or urban regeneration companies: disqualifying benefits***

3168. This section sets out what happens if a company (or a connected person) receives a benefit in connection with a contribution to a local enterprise organisation or urban regeneration company (see section 1244). It is based on sections 79, 79A and 79B of ICTA. The corresponding rule for trading income is in section 82.
3169. Section 79(9) of ICTA refers to relief having been given “under subsection (1) above”. Strictly, relief for management expenses is given under subsection (2) by reference to a “deduction under subsection (1)”. But it is clear in the context of the section that the recovery under subsection (9) is intended to apply to management expenses as it applies to a trading deduction. The same analysis applies to the corresponding provisions in sections 79A and 79B of ICTA. This section clarifies the position.
3170. The charge is restricted to the amount of the “disqualifying benefit”. That expression is explained in section 1244(5). See the commentary on that section and *Change 18* in Annex 1.

***Section 1254: Repayments under FISMA 2000***

3171. This section charges tax on a repayment made to a company under FISMA. It is based on section 76B of ICTA. The corresponding rule for trading income is in section 92.
3172. Under section 76B(2) of ICTA the repayment is “charged to tax under Case VI of Schedule D”. Under section 70(1) of ICTA the basis of assessment for Schedule D is the “profits gains or income arising” in an accounting period. But there is no explicit rule to say in which accounting period the repayment falls.

***Chapter 6: Supplementary***

***Section 1255: Meaning of some accounting terms***

3173. This section provides definitions of some accounting terms used in this Part. It is based on sections 75A and 75B of ICTA.
3174. *Subsection (1)* deals with the concept of management expenses being “debited in accounts”. This expression is used in the rules that determine to which accounting period expenses are referable.
3175. *Subsection (2)* deals with the concept of an amount being “brought into account”. This expression is used in the rule that deals with the claw back of relief. There is no reason why the expression should be defined differently in sections 75A(10) and 75B(8) of ICTA. So this section adopts the fuller words of section 75A(10).
3176. *Subsection (3)* removes a small inconsistency between sections 75A(10) and 75B(12) of ICTA by referring to a debit that increases *or creates* a loss.