

CORPORATION TAX ACT 2009

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 3: Trading income

Overview

147. This Part contains the rules relating to trading income. The Part charges:
- the profits of a trade (charged in the source legislation under Schedule D Case I or V); and
 - post-cessation receipts (charged in the source legislation under Schedule D Case VI).
148. The structure of the Part is to:
- identify the income taxed as profits of a trade (Chapter 2);
 - calculate the profits of the trade (Chapters 3 to 7);
 - apply the rules for particular trades (Chapters 8 and 9);
 - apply other rules affecting the calculation of profits of the trade (Chapters 10 to 14); and
 - identify the other component of trading income – post-cessation receipts – (Chapter 15).
149. This Part is not an exhaustive statement of the rules for the calculation of trading income. Other regimes may affect that calculation. In particular, Parts 5 to 8 and 11 to 15 of this Act contain rules that may affect trade profits.
150. References to “profits or gains” in the source legislation which relate only to income are rewritten in this Part omitting the reference to “gains”. This continues the tidying up of such references started in section 46(3) of, and Schedule 7 to, FA 1998.

Chapter 1: Introduction

Section 34: Overview of Part

151. This section provides an overview of this Part. It is new. The corresponding income tax rule is in section 3 of ITTOIA.
152. In contrast to section 3 of ITTOIA, this section makes no reference to adjustment income. This is because for corporation tax purposes adjustments on a change of basis of accounting are brought into account in computing trading profits rather than being treated as a distinct category of income.

Chapter 2: Income taxed as trade profits

Overview

153. This Chapter explains what is taxed as profits of a trade. It identifies a number of activities and receipts and sets out how they are treated.

Section 35: Charge to tax on trade profits

154. This section applies the corporation tax charge on income to the profits of a trade. It is based on section 18 of ICTA. The corresponding rule for income tax is in section 5 of ITTOIA.
155. The section does not rewrite the reference to “profession or vocation” in Schedule D Case II. See *Change 2* in Annex 1.
156. Section 832(1) of ICTA provides that “trade” includes “every trade, manufacture, adventure or concern in the nature of trade”. This brings within the meaning of trade an isolated transaction (or a small number of transactions) which, while in the nature of trade, is not sufficiently extensive to amount to a trade.

Section 36: Farming and market gardening

157. This section has two functions. First, it treats all farming or market gardening carried on in the United Kingdom as a trade. Second, it treats all farming carried on in the United Kingdom by a particular person as a single trade. It is based on section 53 of ICTA. The rules for income tax are rewritten in section 9 of ITTOIA.
158. *Subsection (1)* deals with the first function. In most cases there will be no doubt that farming is a trade on first principles. Like section 38 of this Act this section can trace its origins back to the time when there was a charge to income tax under Schedule B on the occupation of land. Farming was originally charged under Schedule B. The purpose of section 53 of ICTA and its predecessor provisions was to take the charge on farming out of Schedule B and into Schedule D. With the abolition of Schedule B that function is now spent.
159. But section 53 of ICTA does make clear that even uncommercial farming is treated as a trade. This section preserves that effect.
160. *Subsection (2)* deals with the second function of the section. It provides that all farming carried on by a company in the United Kingdom is treated as a single trade. It makes clear that farming carried on as part of another trade is not included in the single trade of farming.
161. The restriction of subsection (2) to farming in the United Kingdom is derived from the definition of “farming” in section 832(1) of ICTA.
162. Section 53(2) of ICTA uses the expression “particular company or partnership” to make clear that the single trade rule applies also to a firm. It follows that farming carried on by a company as a member of a firm is separate from any farming carried on by that company alone. This rule is dealt with in section 1270 in Part 17 (Partnerships). The corresponding provision for income tax is section 859 of ITTOIA.
163. The definition of “farming” and “market gardening” is given in section 1317 in Part 21 (Other general provisions). The corresponding provision for income tax is section 996 of ITA.

Section 37: Commercial occupation of woodlands

164. This section provides that the commercial occupation of woodlands is not treated as a trade for any corporation tax purpose. It is based on section 53 of ICTA and paragraph

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3 of Schedule 6 to FA 1988. The corresponding rule for income tax is in section 11 of ITTOIA.

165. *Subsection (3)* makes clear that when this section is read together with related sections any profits and losses arising from the commercial occupation of woodlands are wholly outside the corporation tax code.
166. This section prevents any charge to tax as trading income and denies any claim for relief for a trade loss. Section 208(b) of this Act performs a similar function in relation to property income. Section 980 prevents there being any charge to tax under Chapter 8 of Part 10 (income not otherwise charged). The corresponding rule for income tax is in section 768 of ITTOIA.

Section 38: Commercial occupation of land other than woodlands

167. This section deals with the commercial occupation of land for purposes other than farming or woodlands. It is based on section 53 of ICTA. The corresponding rule for income tax is in section 10 of ITTOIA.
168. The section treats the commercial occupation of land in the United Kingdom as the carrying on of a trade. It provides certainty of treatment if land is occupied on a commercial basis in circumstances that do not amount to the carrying on of a trade on first principles.
169. The origins of section 53 of ICTA go back to the time when there was a charge to income tax under Schedule B on the occupation of land. The purpose of the Schedule B charge was to tax the profit that an occupier of the land could earn from the land itself, for example, by farming it. The tax was charged whether or not the occupier actually exploited the land.
170. The Schedule B charge was calculated by reference to the annual value of the land. This amount could be considerably less than the amount of profit an occupier could in fact derive from the land. For this reason the basis of charge was switched from Schedule B to Schedule D Case I if the land was farmed or otherwise managed on a commercial basis.
171. The last remnant of Schedule B was repealed by FA 1988. Schedule 6 to FA 1988 exempted any profits and losses from the occupation of commercial woodlands from corporation tax.
172. The provisions of section 53 of ICTA relating to farming are rewritten as section 36 of this Act. The provisions relating to the occupation of commercial woodlands are rewritten as section 37 of this Act.

Section 39: Profits of mines, quarries and other concerns

173. This section treats the profits and losses of certain concerns as if they were the profits and losses of a trade. It is based on section 55 of ICTA. The corresponding rule for income tax is in section 12 of ITTOIA.
174. The feature that most of these concerns have in common is that they exploit land for its natural resources. The section applies only if the activity carried on by the concern does not amount to a trade on first principles. If the activity is a trade on first principles the profits and losses will be taxed in accordance with section 35 of this Act.
175. The section does not deem the concern to be carrying on a trade. The company will not qualify for roll-over relief under section 152 of TCGA on any chargeable gain. That section requires the taxpayer to be carrying on a trade as defined in section 158(2) of TCGA. If the concern is operated by a company not resident in the United Kingdom that company does not become liable to corporation tax through the application of section 5(2). Section 5(2) requires a trade to be carried on in the United Kingdom.

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176. *Subsections (1) and (2)* provide that the profits and losses of the concern are calculated and charged to tax as if the concern were a trade. The source legislation was not explicit in this regard. See Part A of *Change 3* in Annex 1. This change reproduces Change 2 in ITTOIA and so brings the income tax and corporation tax codes back into line.
177. *Subsection (3)* provides that the normal loss rules apply. See Part B of *Change 3* in Annex 1.
178. *Subsection (4)* lists the concerns to which the section applies. It updates the reference to “fishings” to “rights of fishing”.
179. *Subsection (5)* makes clear that section 38 of this Act has priority over section 39. This is because section 38 treats the activity as if it were a trade. This contrasts with the approach of this section, which is to treat the profits and losses as trade profits and losses. Section 38 may be more beneficial for the company. For example, the activity would qualify as a trade for chargeable gains purposes. See section 158(2) of TCGA.

Section 40: Credit unions

180. This section ensures that most credit unions are not treated as carrying on a trade for tax purposes. It is based on section 487 of ICTA.
181. Credit unions are profit-sharing financial co-operatives, owned and managed by their own members, which offer a convenient way of saving and loans to their members.
182. The members make regular savings, as little or as much as they wish. These savings then form a common pool of money from which loans are made to members. When members have been saving for a certain period of time (usually about 12 weeks) they can apply for a loan from the pool. Interest on the loan is charged at about 1% per month on the monthly reducing balance.
183. There are other rules about credit unions:
- in Part 5 (loan relationships);
 - in section 133; and
 - in section 1218.
184. *Subsection (1)* is the rule that the usual activities of a credit union are not to be treated as a trade. The rule applies only in the calculation of the credit union’s income. So, if the carrying on of a trade is relevant for some other purpose (for instance, the taxation of chargeable gains), and the credit union is in fact carrying on a trade, the position is not disturbed by this rule.

Section 41: Effect of company starting or ceasing to be within charge to corporation tax

185. This section treats a company as starting or ceasing to carry on a trade in particular circumstances. It is based on section 337 of ICTA. The corresponding rule for income tax is in section 18 of ITTOIA.
186. Section 337 of ICTA requires the company’s trade or property business income to be calculated as though it had started or ceased to carry on a trade or a property business in two cases. Section 41 deals with trades and section 289 with property businesses.
187. The first trade case is when the company begins or ceases to carry on the trade (section 337(1)(a) of ICTA). Then its profits from that trade are calculated as though the trade had, at that time, begun or ceased. It is not necessary to rewrite this case. It is dealt with automatically in the rewritten rules because they are “person-based” and do not assume that a particular trade can continue independently of the person actually carrying it on.

188. The second case involves movement by the company into or out of the corporation tax regime (section 337(1)(b) of ICTA). Non-UK resident companies are within the charge to corporation tax only if they are trading, are trading in the United Kingdom, and through a permanent establishment in the United Kingdom. Then they are chargeable to corporation tax on all the profits attributable to that permanent establishment. First meeting or ceasing to meet those conditions can result in a change of taxing regime from income tax to corporation tax or vice versa.
189. **Section 41** says what happens when a company enters or leaves the corporation tax regime in respect of the trade: then its trade profits are calculated as though it had started or ceased to carry on the trade. The corresponding income tax rule in section 18 of ITTOIA is a complementary, mirror-image rule which applies when the company enters or leaves the income tax regime in respect of the trade.

Section 42: Tied premises

190. This section treats rent received by a company carrying on a trade, for premises let to persons to whom the company supplies goods sold or used on those premises, as a receipt of the trade rather than a receipt of a property business. It is based on section 98 of ICTA. The corresponding rule for income tax is in section 19 of ITTOIA.
191. Section 98 of ICTA is expressed in general terms. But it most commonly applies to rent received by a brewing company which lets premises to tied tenants.

Section 43: Caravan sites where trade carried on

192. This section allows a company which carries on a trade associated with the operation of a caravan site to include in the receipts of that trade income from letting pitches or caravans where the letting does not itself constitute a trade. It is based on ESC C36. The corresponding rule for income tax is in section 20 of ITTOIA. See *Change 4* in Annex 1.
193. See section 1314 and *Change 96* in Annex 1 for the definition of “caravan”.

Section 44: Surplus business accommodation

194. This section allows income from letting surplus business accommodation to be treated as a trade receipt instead of as rent. It is based on the practice known as “Revenue Decision 9” set out in the HMRC publication *Tax Bulletin* of 15 February 1994. The corresponding rule for income tax is in section 21 of ITTOIA. See *Change 5* in Annex 1.

Section 45: Payments for wayleaves

195. This section applies if a trader receives rent from a wayleave granted in respect of land on which a trade is carried on. It is based on section 120 of ICTA. The corresponding rule for income tax is in section 22 of ITTOIA.
196. Rent received in respect of a wayleave is normally taxed as property income either by Chapter 2 of Part 4 of this Act (property businesses) or by section 277 (charge to tax on rent receivable for a UK electric-line wayleave). But if the rent is received in respect of land on which a trader carries on a trade and the trader receives no other rent in respect of the same land the rent, and any associated expenses, can be included in the calculation of the trade profits. See *Change 6* in Annex 1. This change enacts a non-statutory practice, and also makes changes to both practice and the law. It reproduces *Change 5* in ITTOIA and so brings the income and corporation tax codes back into line.
197. *Subsection (4)* defines “rent”. Section 120 of ICTA uses the definition of “rent” in section 119(3) of ICTA (rent etc. payable in connection with mines, quarries and similar concerns). Section 119 of ICTA is rewritten in Chapter 7 of Part 4 of this Act. The definition of rent in that Chapter and in this section must be the same. See the commentary on section 271 of this Act for a fuller description of the rewrite of the word “rent” in Chapter 7 of Part 4 of this Act.

198. *Subsection (5)* defines “wayleave”. Section 120 of ICTA uses the word “easement” as defined in section 119(3) of ICTA to describe the nature of the right for which the rent is paid. This section uses “wayleave” as that is how most of the payments covered by this section are usually described in practice. The definition of “easement” in section 119(3) of ICTA gives that word a meaning that is much wider than its usual legal meaning. See the comments of Uthwatt J at pages 329 and 330 of *Mosley v George Wimpey & Co Ltd* (1945), 27 TC 314 CA.
199. The definition of “wayleave” preserves the generality of the words in section 119(3) of ICTA and includes a reference to the Scottish equivalent, “servitude”.
200. The definition has no territorial limitation. So the section covers services other than UK electric-line wayleaves.
201. The section does not rewrite the reference to “profession or vocation” in Schedule D Case II. See *Change 2* in Annex 1.

Chapter 3: Trade profits: basic rules

Section 46: Generally accepted accounting practice

202. This section sets out the starting point for the calculation of trade profits. It is based on section 42 of FA 1998. The corresponding rule for income tax is in section 25 of ITTOIA.
203. *Subsection (1)* is the general rule that requires profits to be calculated “in accordance with generally accepted accounting practice”, an expression defined in section 50 of FA 2004. In particular, such practice generally requires account to be taken of debtors and creditors and of the value of stock. The general rule is subject to any special rule of law whether expressed in statute or explained by the courts.
204. The relevant statutory laws are mainly those that are rewritten in this Part. But there are also provisions not included in Part 3 of this Act which may affect the calculation of profits: for example, the pension contributions deductions provisions in FA 2004 and some anti-avoidance provisions in ICTA that apply to all income types.
205. *Subsection (2)* makes clear that subsection (1) does not bring with it any of the other accounting requirements, such as a formal audit.
206. *Subsection (3)* sets out exceptions to the general rule in subsection (1). Lloyd’s underwriters have their own special rules (mostly in Chapter 3 of Part 2 of FA 1993); there are special rules for insurance companies (mostly in Chapter 1 of Part 12 of ICTA and Chapter 1 of Part 2 of FA 1989); and tonnage tax companies (see Schedule 22 to FA 2000) are subject to “special rules” for the calculation of profits.

Section 47: Losses calculated on same basis as profits

207. This section ensures that profits and losses are calculated on a consistent basis. It is based on section 46 of FA 1998. The corresponding rule for income tax is in section 26 of ITTOIA.

Section 48: Receipts and expenses

208. This section is based on section 46 of FA 1998. The corresponding rule for income tax is in section 27 of ITTOIA.

Section 49: Items treated as receipts and expenses

209. This section signposts rules affecting trade profits that are elsewhere in the Corporation Tax Acts. It is new. The corresponding rule for income tax is in section 28 of ITTOIA.

210. In particular the CAA rules override the rules against the inclusion of capital items in sections 53 and 93 of this Act.

Section 50: Animals kept for trade purposes

211. This section contains the basic rule for the corporation tax treatment of animals. It is based on paragraphs 1, 7 and 9 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 30 of ITTOIA. The animals are treated as trading stock unless a herd basis election is made under Chapter 8 of this Part.

Section 51: Relationship between rules prohibiting and allowing deductions

212. This section makes clear the interaction between those provisions that allow a deduction and those provisions that prohibit a deduction. It is new. See *Change 7* in Annex 1. The corresponding rule for income tax is in section 31 of ICTA.
213. The general principle is that a rule allowing a deduction takes priority over a rule prohibiting a deduction. But this is subject to a number of exceptions.

Section 52: Apportionment etc of profits and losses to accounting period

214. This section provides for apportionment of profits and losses when a company's period of account does not coincide with an accounting period. It is based on section 72 of ICTA. That section is rewritten for income tax purposes in sections 203 and 871 of ITTOIA.
215. This section does not carry over the rewrite change in sections 203(4) and 871(5) of ITTOIA whereby apportionment is permitted by a measure of time other than the days permitted by section 72(2) of ICTA. HMRC has a long-established view that days cannot be split into accounting periods. That helps prevent exploitation of the wider range of reliefs available in the rather different context of corporation tax.

Chapter 4: Trade profits: rules restricting deductions

Overview

216. This Chapter contains provisions prohibiting various deductions in calculating the profits of a trade or restricting the extent to which such deductions can be made.

Section 53: Capital expenditure

217. This section prohibits deductions for capital expenditure and is based on section 74(1) (f) of ICTA. The corresponding rule for income tax is in section 33 of ITTOIA.
218. It is a long-established and generally accepted principle that capital items are ignored in calculating the profits of a trade and the question whether a sum is income or capital is ultimately a question of law, not accountancy. For judicial authority for this proposition, see, for example the words of Brightman J on page 173 of *ECC Quarries Ltd v Watkis* (1975), 51 TC 153 ChD¹:

...unchallenged evidence, or a finding, that a sum falls to be treated as capital or income on principles of correct accountancy practice is not decisive of the question whether in law the expenditure is of a capital or an income nature.

219. A sum which is of a capital nature may however be allowed as a deduction in calculating the profits of a trade because of a statutory exception to the general rule on the deduction of such items in this section. See, for example, section 89 (expenses connected with patents).

¹ STC [1975] 578

220. In the absence of general agreement on what constitutes capital expenditure “items of a capital nature” is not defined.
221. Section 74(1)(g) of ICTA is redundant as the deduction of capital employed in the improvement of premises is covered by the general prohibition on the deduction of “items of a capital nature”. So this Act repeals section 74(1)(g) of ICTA without rewriting it.

Section 54: Expenses not wholly and exclusively for trade and unconnected losses

222. This section contains rules for the deduction of expenses and losses in calculating the profits of a trade. It is based on section 74(1)(a) (expenses) and (e) (losses) of ICTA. The corresponding rules for income tax are in section 34 of ITTOIA.
223. Section 74(1)(a) of ICTA provides that in calculating the profits of a trade no deduction is allowed for expenditure which is not incurred “wholly and exclusively” for the purposes of that trade. This could be construed to mean that if expenditure is incurred partly for trade purposes and partly for some other purposes, no part of that expenditure can be deducted in arriving at the trade profits.
224. But section 74(1)(c) of ICTA, which prohibits any deduction in respect of the rent of premises used for residential or “domestic” purposes, provides for the *apportionment* of rent paid for premises used partly as residential accommodation and partly for the purposes of a trade. And in practice a deduction is allowed for any expenditure which can be apportioned between trade and non-trade expenditure – for example, expenditure on a car used partly for trade and partly for private purposes.
225. There is judicial support for allowing a deduction where expenditure incurred for more than one purpose can reasonably be apportioned between expenditure incurred for the purpose of the trade and non-trade expenditure. See, for example, *Lochgelly Iron and Coal Company Ltd v Crawford* (1913), 6 TC 267 CS, in which a deduction was allowed for part of a subscription to a trade association and *Copeman v William Flood & Sons Ltd* (1941), 24 TC 53 KB, in which the High Court remitted the case to the Commissioners to find as a fact whether the remuneration paid to certain directors who were also shareholders in the family company was wholly and exclusively expended for the purpose of the Company’s trade, and if not, how much of the remuneration was so expended.
226. Conversely, the courts have held that if it is not possible to identify any part of the expenditure that is incurred wholly and exclusively for the purposes of the trade, no apportionment is possible. See, for example, *Mallalieu v Drummond* (1983), 57 TC 330 HL² in which no deduction was allowable for clothing worn for warmth and decency as well as being required by the taxpayer’s profession.
227. So *subsection (2)* of this section provides for the deduction of any part or proportion of expenses incurred partly for the purposes of the trade and partly for some other purpose that can be identified as incurred wholly and exclusively for the purposes of the trade. Rent on dual purpose accommodation can be apportioned under *subsection (2)* of this section. So this Act repeals section 74(1)(c) of ICTA without rewriting it.

Section 55: Bad debts

228. This section is based on the rule restricting relief for some debts in section 88D of ICTA. It also rewrites the relief in section 89 of ICTA for debts proved irrecoverable after a trade is treated as having ceased. See *Change 8* in Annex 1. The corresponding rule for income tax is in section 35 of ITTOIA.
229. *Subsection (2)(a)* refers to a deduction “by way of impairment loss”. That expression is not defined for the purpose of this section. But section 476(1) defines “impairment

loss” for the purposes of the loan relationships legislation as “a debit in respect of the impairment of a financial asset”. “Impairment” includes “uncollectability”.

230. *Subsection (2)(b)* deals with debts released as part of a “statutory insolvency arrangement”, which is defined in section 834(1) of ICTA.
231. *Subsection (3)* provides a definition that clarifies the scope of the section. All money debts (see section 303) arising in a trade that produce an impairment loss are within the loan relationships rules (see section 479). Even if a money trade debt is released as part of a statutory insolvency arrangement any loss on the debt is within the extended meaning of “impairment” in section 476(1).
232. There is a corresponding rule for income from holding an office in section 970.

Section 56: Car or motor cycle hire

233. 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 restriction increases in line with the retail price. The section is based on sections 578A and 578B of ICTA. The corresponding rule for income tax is in section 48 of ITTOIA.
234. Section 578B(1) of ICTA says that for the purposes of section 578A of ICTA “car” includes a motor cycle. So this section and section 57 refer to a “car or motor cycle” throughout.
235. Section 578A(4) of ICTA provides for amounts in respect of hire charges brought into account as a receipt of the trade under section 94 of ICTA (see section 94 of this Act) to be reduced in the same proportion as the deduction in respect of those charges is reduced under section 578A(3) of ICTA. *Subsection (4)* of this section extends the same treatment to amounts in respect of hire charges taxed as a post-cessation receipt under section 193 (debts released after cessation). See *Change 9* in Annex 1.

Section 57: Car or motor cycle hire: supplementary

236. This section defines various terms and is based on section 578B of ICTA. The corresponding rule for income tax is in section 49 of ITTOIA.
237. Section 578B(2) of ICTA defines “qualifying hire car” for the purposes of section 578A of ICTA as a car hired under a hire-purchase agreement subject to an option to purchase which is exercisable for a nominal amount.
238. Not all hire-purchase agreements require the hirer to exercise an option at the end of the hire period. Under some types of agreement, ownership of the vehicle passes automatically to the hirer at the end of the hire period. So *subsection (2)(a)* of this section extends the definition of “qualifying hire car or motor cycle” to include a car or motor cycle where ownership passes without the exercise of an option to purchase. See *Change 10* in Annex 1.

Section 58: Hiring cars (but not motor cycles) with low CO2 emissions before 1 April 2013

239. This section excludes certain cars hired before 1 April 2013 under a contract entered into before that date from the restriction in section 56. It is based on section 578A(2A) and (2B) of ICTA and section 60 of FA 2002. The corresponding rule for income tax is in section 50 of ITTOIA.
240. *Subsection (2)* defines low emissions by reference to section 45D of CAA. A transitional rule in Schedule 1 to this Act provides that, for a car hired on or before 31 March 2008, the carbon emissions limit in section 45D(4) of CAA remains 120 grams instead of the new limit of 110 grams.

Section 59: Patent royalties

241. This section prohibits a deduction for patent royalties. It is based on section 74(1)(p) of ICTA.
242. For most patent royalties this rule is overridden by the rules of the intangible fixed assets regime (rewritten in Part 8 of this Act) which provide relief for trades as well as other commercial activities (see, in particular, section 728(5) and Chapter 6 of Part 8 of this Act). But for a minority of cases, this section will remain relevant and will continue to prevent a deduction. That includes, for example, cases where the royalty is in respect of an intangible asset that is not a fixed asset of the payer's trade.

Section 60: Expenditure on integral features

243. This section draws attention to the rule in section 33A(3) of CAA. There is a signpost to that rule in section 74(1)(da) of ICTA. That subsection is repealed. The signpost is not formally rewritten but it is replaced in this section (and in the property income section 263).

Chapter 5: Trade profits: rules allowing deductions

Overview

244. This Chapter contains provisions allowing various deductions in calculating the profits of a trade.

Section 61: Pre-trading expenses

245. This section gives relief for expenses incurred before a trade starts. It is based on section 401 of ICTA. The corresponding rule for income tax is in section 57 of ITTOIA.
246. *Subsection (1)* sets the scene. Consistent with other rules in this Part, it refers to the "date" on which (instead of the "time" when) a company starts to trade.

Section 62: Tenants under taxed leases: introduction

247. This section provides for the following five sections to apply where a tenant, under a taxed lease, uses land for the purposes of a trade. It is based on section 87(1), (2), (8) and (9A) of ICTA. The corresponding provision for income tax is in section 60 of ITTOIA.
248. Chapter 4 of Part 4 (profits of property businesses: lease premiums etc) contains provisions (in sections 217 to 222) treating certain premiums, and other amounts, relating to a lease ("the taxed lease") as giving rise to receipts of a property business (of amount X). Chapter 4 of Part 4 also provides that in certain cases a tenant under the taxed lease obtains relief in respect of all, or part, of X:
- by reducing the amount of another property business receipt (sections 227 to 230), or
 - by being treated as an expense of a property business (sections 231 to 234).
249. **Sections 62 to 67** provide for certain cases in which a tenant under the taxed lease obtains relief as a trading expense in respect of all, or part, of X.
250. *Subsection (1)* extends relief to cases in which X arose in relation to a lease of land outside the United Kingdom. See *Change 11* in Annex 1. This is in accordance with the policy of treating UK and overseas property businesses in the same way as far as possible.
251. The amount which a tenant can deduct in respect of rent which it is treated as paying under section 87(2) of ICTA is qualified by:

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- the general rules as to deductions not allowable in computing the profits of a trade in section 74(1) of ICTA; and
 - rules prohibiting or restricting the deduction of specific expenditure elsewhere in ICTA.
252. In this Act, the rules restricting deductions are in Chapter 4 of this Part and section 74(1) (a) of ICTA is rewritten in that Chapter in section 54. *Subsection (3)* preserves the interaction of section 87(2) of ICTA and the general and specific rules restricting deductions in ICTA by providing that a deduction for an expense which a tenant is treated as incurring under section 63 is subject to the application of any provision of Chapter 4 of this Part.

Section 63: Tenants occupying land for purposes of trade treated as incurring expenses

253. This section treats a tenant under a lease, in respect of which an amount is brought into account by the landlord, (a “taxed lease”) as incurring an expense for each day on which the property held under the lease is occupied for the purposes of the tenant’s trade. It is based on section 87(2), (3) and (9) of ICTA. The corresponding rule for income tax is in section 61 of ITTOIA.
254. [Sections 217 to 222](#) provide for a company to bring an amount into account as a receipt of a property business in cases where the company has granted a short-term lease at a premium (or in certain other cases).
255. Sections 277 to 282 of ITTOIA make corresponding provision for a person to bring an amount into account as a receipt of a property business for income tax.
256. *Subsection (1)* treats a tenant which, for a qualifying day, occupies land for the purposes of a trade as incurring an expense. This corresponds to the treatment of the landlord who has been, or would have been (see section 227(4)), treated as receiving a receipt (“taxed receipt”) of the landlord’s property business.
257. The formula in *subsection (4)* calculates the expense for each qualifying day by spreading an amount in respect of the taxed receipt evenly over the receipt period of that receipt. Defining “A” in that formula as “the unreduced amount of the taxed receipt” makes clear that the amount of the expense which the tenant is treated as incurring for each qualifying day is calculated by reference to the amount of the taxed receipt *before* any reductions or deductions.
258. *Subsection (5)* modifies that formula for a qualifying day on which the tenant occupies only part of the land subject to the taxed lease for the purposes of a trade. The subsection requires the fraction of the land which is occupied by the tenant for the purposes of the trade to be calculated “on a just and reasonable basis”, where section 87(3) of ICTA requires a “just apportionment”. See *Change 12* in Annex 1.

Section 64: Limit on deductions if tenant entitled to mineral extraction allowance

259. This section prevents a double deduction where a tenant is entitled under section 403 of CAA to an allowance in respect of qualifying expenditure on acquiring a mineral asset. It is based on section 87(7) of ICTA. The corresponding rule for income tax is in section 62 of ITTOIA.

Section 65: Tenants dealing with land as property employed for purposes of trade

260. This section applies to a tenant which, while not occupying a property, uses the property for the purposes of a trade – for example a company which lets premises held under a taxed lease to a person who sells only goods supplied by that company. It is based on

section 87(4) and (6) of ICTA. The corresponding rule for income tax is in section 63 of ITTOIA.

261. *Subsection (2)* treats the tenant as if it occupied the property, or part of it, for the purposes of relief under section 63.
262. *Subsection (3)* prevents the tenant obtaining relief under section 63 to the extent that relief for the same day is allowed in calculating the profits of the tenant's property business under section 232.

Section 66: Restrictions on section 63 expenses: lease premium receipts

263. This section restricts the expenses that section 65 treats a tenant as incurring, under section 63, by reference to the unreduced amount of a taxed receipt under a taxed lease if:

- a sublease has been granted out of the taxed lease; and
- in respect of the sublease, the unreduced amount of the taxed receipt reduces an amount which is brought into account as a receipt under Chapter 4 of Part 4 of this Act or the corresponding provisions in ITTOIA (the "lease premium receipt").

This section is based on sections 87(5) and 87A of ICTA. The corresponding rule for income tax is in section 64 of ITTOIA.

264. The restriction in this section extends to cases where the unreduced amount of the taxed receipt reduces a lease premium receipt of an overseas property business. See *Change 11* in Annex 1.

265. **Section 63** treats the tenant as incurring an expense for each qualifying day in the receipt period of the taxed receipt relating to the taxed lease. The expense is calculated by reference to the unreduced amount of the taxed receipt.

266. If, in respect of the sublease, the unreduced amount of the taxed receipt is used to reduce:

- under section 228, the amount brought into account as a lease premium receipt under Chapter 4 of Part 4 of this Act; or
- under section 288 of ITTOIA, the amount brought into account as a lease premium receipt under Chapter 4 of Part 3 of ITTOIA,

this section makes a corresponding reduction to the amount of the expense which section 63 treats as incurred by the tenant for a qualifying day in the receipt period of the lease premium receipt.

267. *Subsections (3) to (5)* treat the tenant as incurring an expense for a qualifying day of the amount, if any, by which the "daily amount" of the taxed receipt exceeds:

- the "daily reduction" of the lease premium receipt; or
- if the qualifying day falls within the receipt period of more than one lease premium receipt, the "total of the daily reductions" of those lease premium receipts.

268. This corresponds to the treatment in section 233 of cases where lease premium receipts, with overlapping receipt periods, are reduced by reference to the unreduced amount of a single taxed receipt. See *Change 13* in Annex 1.

269. *Subsection (6)* contains formulas for calculating the "daily amount" of a taxed receipt and the "daily reduction" of a lease premium receipt. The subsection provides that the "daily reduction" only takes account of the taxed receipt in question. This corresponds to the treatment in section 233 of cases where more than one taxed receipt reduces a single lease premium receipt. See *Change 13* in Annex 1.

Section 67: Restrictions on section 63 expenses: lease of part of premises

270. This section adapts section 63 if section 66 applies but the sublease does not extend to the whole of the premises subject to the taxed lease. It is based on sections 87(5) and 87A of ICTA. The corresponding rule for income tax is in section 65 of ITTOIA.
271. *Subsection (4)* deals with the case where, for a qualifying day, there is more than one lease premium receipt, relating to subleases that do not extend to the whole of the premises, that has been reduced by the taxed receipt. This corresponds to the treatment in section 234(5) of expenses under sections 232 and 233 where more than one lease premium receipt falls to be reduced by reference to the same taxed receipt. See *Change 13* in Annex 1.
272. *Subsection (5)* adapts the formulas in sections 63(4) and 66(6) by multiplying the unreduced amount of the taxed receipt in those formulas (“A”) by the fraction of the premises to which the sublease relates.
273. *Subsection (6)* requires the fraction in subsection (5) to be calculated “on a just and reasonable basis”, where section 87(5) of ICTA, which applies section 37(6) of ICTA, is not explicit about the necessary basis of apportionment. See *Change 12* in Annex 1.

Section 68: Replacement and alteration of trade tools

274. This section allows a deduction for the cost of replacing or altering trade tools if the *only* reason a deduction would not be allowed is that the expenditure is of a capital nature. It is based on that part of section 74(1)(d) of ICTA which relates to deductions in respect of the replacement (“supply”) or alteration of implements, utensils or other articles employed for the purposes of the trade. The corresponding rule for income tax is in section 68 of ITTOIA.
275. Expenditure on repairing trade premises or tools is revenue under the normal rules. And following the Special Commissioners decision in *Jenners Princes Street Edinburgh Ltd v CIR* (1998), SpC000166³, it is generally accepted that the reference in section 74(1)(d) of ICTA to expenditure “beyond the sum actually expended” does not prohibit the deduction of a provision for repairs if the cost of the repairs would be allowable. So that part of section 74(1)(d) of ICTA which deals with repairs is redundant and is not rewritten.

Section 69: Payments for restrictive undertakings

276. This section allows a company to deduct certain amounts paid to employees for restrictive undertakings. Such amounts might not otherwise be deductible to the extent that they are capital in nature or fall foul of the “wholly and exclusively” rule. The section is based on section 73(2) of FA 1988. The corresponding rule for income tax is in section 69 of ITTOIA.
277. Section 73(2) of FA 1988 applies only to amounts brought into charge on the employee as earnings under section 225 of ITEPA. The former cross-refers to the latter where the definition of the amounts concerned is set out:
- In this section “restrictive undertaking” means an undertaking which restricts the individual’s conduct or activities.
- For this purpose it does not matter whether or not the undertaking is legally enforceable or is qualified.
278. *Subsection (1)* provides for the deduction. In so doing it focuses on the key element for the rule to apply: the fact of payment.

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279. *Subsection (2)* provides a timing rule. The deduction allowed by section 73 of FA 1988 is taken in the accounting period in which the payment is made and no deduction is allowed in any other period. Similar words are used in sections 77 and 88. This ensures that the timing rules for deductions in this Chapter which depend on payment are explicit and consistent.

Section 70: Employees seconded to charities and educational establishments

280. This section allows a company carrying on a trade to deduct the cost of an employee seconded to a charity or educational establishment in calculating the trade profits. It is based on section 86 of ICTA. The corresponding rule for income tax is in section 70 of ITTOIA.
281. Section 86 of ICTA allows a company which second an employee to a charity or educational establishment to deduct the cost of employing the seconded person *to the extent that* those costs would have been deductible if the employee continued to be employed for the purposes of the employer's trade. 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 71: Educational establishments

282. This section defines "educational establishment" for the purposes of section 70. It is based on section 86 of ICTA. The corresponding rule for income tax is in section 71 of ITTOIA.
283. Section 86(4)(c) of ICTA refers to an independent school registered under section 465 of the Education Act 1996. Section 465 of the Education Act 1996 was repealed by the Education Act 2002. So *subsection (1)(c)* of this section refers instead to an independent school registered under section 161 of the 2002 Act.
284. **Schedule 1** to this Act makes corresponding amendments to section 71 of ITTOIA.

Section 72: Payroll deduction schemes: contributions to agents' expenses

285. This section allows an employer a deduction for expenses incurred in operating a payroll deduction scheme. It is based on section 86A of ICTA. The corresponding rule for income tax is in section 72 of ITTOIA.
286. The main rules for payroll deduction schemes are found in Part 12 of ITEPA. Under such a scheme an employer deducts charitable donations from employees' salaries and pays them to an agent, who distributes them to the employees' chosen charities.
287. The agent's administrative costs may be deducted from the donations. But many employers voluntarily pay the costs themselves so that the employees' full donations can go to the chosen charities.
288. Normally, payments made voluntarily to meet someone else's expenses are not made wholly and exclusively for the purposes of a trade and therefore would not be deductible. Employers might get relief for donations to charitable agencies under the Gift Aid scheme. But there are restrictions on the operation of that scheme and relief would not be available if the agent was not itself a charity.
289. This section gives relief for the expenses as a trading deduction.
290. The section does not rewrite the reference to "profession or vocation" in Schedule D Case II. See *Change 2* in Annex 1.

Section 73: Counselling and other outplacement services

291. This section allows a deduction for certain expenses of counselling provided for employees. It is based on sections 589A and 589B of ICTA. The corresponding rule for income tax is in section 73 of ITTOIA.
292. *Subsection (3)* cross-refers to ITEPA for the conditions that need to be met for the deduction to be allowed (section 310 of ITEPA exempts the employee from tax in respect of counselling received).

Section 74: Retraining courses

293. This section allows a deduction for certain expenses of retraining provided for employees. It is based on section 588 of ICTA. The corresponding rule for income tax is in section 74 of ITTOIA.
294. *Subsection (2)* cross-refers to ITEPA for the conditions that need to be met for the deduction to be allowed (section 311 of ITEPA exempts the employee from tax in respect of qualifying retraining courses).
295. The section does not rewrite section 588(3)(b) of ICTA. That provision makes a deduction in calculating the employer's trade profits 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 rewritten in section 73 and does not serve any material purpose. See *Change 16* in Annex 1.

Section 75: Retraining courses: recovery of tax

296. This section allows the recovery of tax when a deduction under section 74 proves to have been wrongly allowed. It is based on section 588 of ICTA. The corresponding rule for income tax is in section 75 of ITTOIA.
297. *Subsection (2)*, like section 74(2) of this Act, cross-refers to the relevant provisions in ITEPA to refer to the conditions that have not been met.

Sections 76 to 81: Redundancy payments etc

Overview

298. These six sections are based on the trading income rules relating to redundancy payments in sections 90, 579 and 580 of ICTA. The rules that deal with the employee's liability are in section 309 of ITEPA. The corresponding rules for income tax are in sections 76 to 80 of ITTOIA.
299. The trading income rules were introduced to reverse the decisions in *CIR v Anglo Brewing Co Ltd* (1925), 12 TC 803 and *Godden v A Wilson's Stores (Holdings) Ltd* (1962), 40 TC 161. In those cases the courts held that certain payments to employees on the closing down of a trade were not deductible in arriving at trading profits. In neither case was the payment made in accordance with a pre-existing obligation.
300. In 1999 HMRC announced (Tax Bulletin 39G, February 1999) that they would be guided by the decision in *Commissioner of Inland Revenue v Cosmotron Manufacturing Co Ltd* (1997), 70 TC 292⁴.
301. In that Hong Kong case the Privy Council decided that redundancy payments made under a pre-existing obligation are deductible. Although that decision is merely persuasive in the United Kingdom, HMRC do not argue that payments made under a pre-existing obligation (including a statutory obligation) are covered by the *Anglo Brewing* and *Wilson's Stores* decisions. The announcement in Tax Bulletin means

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that it may not be necessary to give the employer a statutory right to a deduction in calculating trading profits. But these sections put the matter beyond doubt.

Section 76: Redundancy payments and approved contractual payments

302. This section sets out the circumstances in which the following three sections apply and explains the terms used in the main provisions. It is based on section 579 of ICTA. The corresponding rule for income tax is in section 76 of ITTOIA.
303. The sections retain the label “redundancy payment” (from section 579 of ICTA) and the expression “additional payment” (from section 90 of ICTA). This section also introduces the label “approved contractual payment” to describe the payments that may replace redundancy payments in some cases.

Section 77: Payments in respect of employment wholly in employer’s trade

304. This section sets out the main rule governing redundancy payments made by an employer. It is based on section 579 of ICTA. The corresponding rule for income tax is in section 77 of ITTOIA.
305. If a payment is otherwise allowable (possibly as a result of the Cosmotron decision – see the overview for this group of sections), this section does not interfere with the accountancy treatment of the payment. In that case, the normal accounting basis applies.
306. The deduction allowed by section 579 of ICTA is for “a redundancy payment ... made”. It is clear that a deduction is allowed only if a payment has been made. It follows that the deduction is to be taken in the accounting period in which the payment is made and that no deduction is allowed in any other period.
307. Section 579(2)(b) of ICTA sets out the rule that applies if a redundancy payment is made after the discontinuance of the employer’s trade. The rule applies if the company ceases to carry on a trade or to be within the charge to corporation tax (see section 41 of this Act).
308. In the case of a trade carried on by a company in partnership, section 114(1)(c) of ICTA deals with a change of membership of a partnership. The profits of the trade are calculated as if there is a transfer of the trade from one deemed company to another, unless a particular company carries on the trade before and after the change. Such a transfer means that the first deemed company ceases to carry on the trade. This brings it within the rule in section 579(2)(b) of ICTA.
309. *Subsection (5)* of the section sets out the partnership rule.
310. *Subsection (6)* has a timing rule expressed in words similar to those used in sections 69 and 88 of this Act. This ensures that the timing rules for deductions in Chapter 5 of Part 3 of this Act which depend on payment are explicit and consistent. This special timing rule applies if the payment is allowable only as a result of this section.

Section 78: Payments in respect of employment in more than one capacity

311. This section deals with the case where the employee is employed in more than one capacity. It is based on section 579 of ICTA. The corresponding rule for income tax is in section 78 of ITTOIA. The section covers the case where there is a non-trade element in the employment and makes clear what part of the payment is allowed as a deduction in calculating trade profits.
312. Section 579(5) of ICTA does not specify the basis on which to apportion the payment. This section adopts the “just and reasonable” apportionment that is used consistently in this Act. See *Change 12* in Annex 1.

Section 79: Additional payments

- 313. This section deals with any voluntary payments that an employer makes in addition to the statutory (or approved) payments dealt with in section 77. It is based on section 90 of ICTA. The corresponding rule for income tax is in section 79 of ITTOIA.
- 314. Unlike the payments in section 77, these additional payments are allowable only if the sole reason for their disallowance is the cessation of the trade.
- 315. The section applies to payments in connection with the cessation of *part* of a trade in the same way as it applies to payments in connection with the cessation of a whole trade. See *Change 17* in Annex 1.

Section 80: Application of section 79 in cases involving partnerships

- 316. This section clarifies what happens on a change of partnership. It is based on sections 90 and 114 of ICTA. The corresponding rule for income tax is in section 79A of ITTOIA (inserted by Schedule 1 to this Act).
- 317. Section 90(3) of ICTA refers to the “discontinuance” of a trade. That word has to be interpreted in the light of sections 114 and 337 of ICTA: the trade is not treated as discontinued unless there is a complete change in the companies carrying it on.
- 318. A redundancy payment is not disallowable solely on account of a partial change of companies carrying on a trade. This section puts it beyond doubt that a partial change of companies carrying on a trade does not count as a cessation.

Section 81: Payments made by the Government

- 319. This section sets out what happens if it is not the employer who makes the redundancy payment to the employee. It is based on section 579 of ICTA. The corresponding rule for income tax is in section 80 of ITTOIA.
- 320. In some cases the Government makes the payment and is reimbursed by the employer. This section ensures that the employer is allowed a trading deduction.
- 321. The references in ICTA to section 166 of the Employment Rights Act 1996 and Article 201 of the [Employment Rights \(Northern Ireland\) Order 1996 \(SI 1996/1919 \(NI 16\)\)](#) are corrected to section 167 and Article 202.
- 322. *Subsection (1)(b)* reflects the effect of the devolution settlements. See *Change 15* in Annex 1.

Section 82: Contributions to local enterprise organisations or urban regeneration companies

- 323. This is the first of five sections that allow deductions for contributions to local enterprise agencies, training and enterprise councils, local enterprise companies in Scotland, business links and urban regeneration companies. The sections are based on sections 79, 79A and 79B of ICTA. The corresponding rules for income tax are in sections 82 to 86 of ITTOIA.
- 324. Contributions to these bodies are generally donations and are likely to be made for benevolent reasons, rather than wholly and exclusively for the purposes of the trade (see section 54 of this Act).
- 325. *Subsection (3)* is an anti-avoidance rule. It prevents a company using the section to obtain a deduction for non-trade 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.

326. Subsections (5) and (6) set out what happens if the company (or a connected person) receives a benefit in connection with the contribution. The charge on the benefit applies if the benefit is received by a person “connected with” the company. That expression is explained in section 1316.
327. Subsection (6)(b) deals with the case where the recipient’s trade has ceased before the benefit is received. It treats the benefit explicitly as a post-cessation receipt. See *Change 19* in Annex 1.
328. Subsection (7) makes clear the extent of the disallowance under subsection (3) or charge under subsection (6).
329. The subsection limits the “disqualifying benefit” in accordance with HMRC practice. See *Change 18* in Annex 1.

Section 83: Meaning of “local enterprise organisation”

330. This section lists some of the organisations that qualify for deductions to be allowed under section 82. It is based on the definitions in sections 79(4) and 79A(5) of ICTA. The corresponding rule for income tax is in section 83 of ITTOIA.
331. Subsection (2) deals with local enterprise agencies. These agencies may take a number of forms and do not have an approval procedure for any other purpose. So the tax legislation specifies that they must be approved for this purpose.
332. The subsection introduces the expression “relevant national authority”. The expression is used also in sections 84 and 85.
333. The subsection reflects the effect of the devolution settlements. See *Change 15* in Annex 1. [The National Assembly for Wales \(Transfer of Functions\) Order 1999 \(SI 1999/672\)](#) devolves the functions of the Secretary of State under section 79 of ICTA to the National Assembly for Wales. So the “relevant national authority” may be the Assembly. But the Order does not refer to section 79A of ICTA. So the equivalent functions in subsections (3) and (5) of this section are still exercised only by the Secretary of State.
334. Subsections (3) to (5) deal with other bodies to which section 82 applies. These other bodies have to be set up in a particular way for other reasons and the tax legislation merely follows the existing procedures.

Section 84: Approval of local enterprise agencies

335. This section and section 85 set out the detailed rules that apply for the approval of local enterprise agencies and the withdrawal of such approval. They are based on section 79 of ICTA. The corresponding rule for income tax is in section 84 of ITTOIA.
336. The section sets out the basic procedure for approving a local enterprise agency. The references to “relevant national authority” are explained in section 83(2).

Section 85: Supplementary provisions with respect to approvals

337. This section and section 84 set out the detailed rules that apply for the approval of local enterprise agencies and the withdrawal of such approval. They are based on section 79 of ICTA. The corresponding rule for income tax is in section 85 of ITTOIA.
338. The references to “relevant national authority” in this section are explained in section 83(2).

Section 86: Meaning of “urban regeneration company”

339. This section sets out the detailed rules that apply for the designation of urban regeneration companies. It is based on section 79B of ICTA. The corresponding rule for income tax is in section 86 of ITTOIA.

Section 87: Expenses of research and development

340. This section gives relief for the cost of research and development undertaken by or on behalf of a company carrying on a trade. It is based on section 82A of ICTA. The corresponding rule for income tax is in section 87 of ITTOIA.

Section 88: Payments to research associations, universities etc

341. This section gives relief for payments by a company carrying on a trade to various bodies engaged in scientific research. It is based on section 82B of ICTA. The corresponding rule for income tax is in section 88 of ITTOIA.
342. The amendments to section 82B of ICTA in section 15 of F(No 2)A 2005 have effect in relation to sums paid to an association within *subsection (1)(a)* of this section during any accounting period of the association beginning on or after a day to be appointed by the Treasury under section 13(6) of F(No 2)A 2005.
343. Section 82B(1) of ICTA allows a deduction for “the sum paid”. So *subsection (2)* allows a deduction for the accounting period in which the payment is made. The wording is similar to that used in sections 69 and 77. This ensures that the timing rules for deductions in Chapter 5 of this Part of this Act which depend on payment are explicit and consistent.
344. Section 82B(4) of ICTA provides that “the Board” shall refer any question as to whether, or to what extent, activities constitute scientific research for the purposes of section 82B to the Secretary of State. Section 832(1) of ICTA defines “the Board” as “the Commissioners of Inland Revenue”.
345. In practice, the function in section 82B of ICTA is exercised by an officer of Revenue and Customs. So *subsection (6)* of this section provides that any question as to what constitutes scientific research must be referred to the Secretary of State by “an officer of Revenue and Customs”. This Change corresponds to Part B of Change 149 in ITTOIA (as amended by CRCA) and so brings the income tax and corporation tax codes back into line. See *Change 1* in Annex 1.

Section 89: Expenses connected with patents

346. This section allows a deduction for expenses connected with patents. It is based on section 83 of ICTA. The corresponding rule for income tax is in section 89 of ITTOIA.
347. The section sets out the expenses that are allowable. The deduction is on the basis of expenses incurred. This relaxes any requirement in the source legislation that fees have to be paid before a deduction can be made. See *Change 20* in Annex 1.
348. For most expenses connected with patents this rule is overridden by the rules of the intangible fixed assets regime (rewritten in Part 8 of this Act) which provide relief for trades as well as other commercial activities (see Chapter 6 of that Part). But, for a minority of cases, this section remains relevant and allows a deduction.

Section 90: Expenses connected with designs or trade marks

349. This section allows a deduction for expenses connected with designs or trade marks. It is based on section 83 of ICTA. The corresponding rule for income tax is in section 90 of ITTOIA.
350. The section sets out the expenses that are allowable. The deduction is on the basis of expenses incurred. This relaxes any requirement in the source legislation that fees have to be paid before a deduction can be made. See *Change 20* in Annex 1.
351. For most expenses connected with designs or trade marks this rule is overridden by the rules of the intangible fixed assets regime (rewritten in Part 8 of this Act) which provide

relief for trades as well as other commercial activities (see Chapter 6 of that Part). But, for a minority of cases, this section remains relevant and allows a deduction.

Section 91: Payments to Export Credits Guarantee Department

352. This section allows a company carrying on a trade to deduct the cost of certain payments to the Export Credits Guarantee Department (“ECGD”). It is based on section 88 of ICTA. The corresponding rule for income tax is in section 91 of ITTOIA.
353. Section 88 of ICTA refers to payments made under arrangements made by the Secretary of State in pursuance of section 11 of the Export Guarantees and Overseas Investment Act 1978. This section refers instead to arrangements made under section 2 of the Export and Investment Guarantees Act 1991 which replaced the 1978 Act.
354. Section 13(1) of the Export and Investment Guarantees Act 1991 delegates the functions of the Secretary of State under section 2 of the 1991 Act to the ECGD. So the reference to the Secretary of State in section 88 of ICTA is not rewritten in this section.
355. Section 88 of ICTA allows a trader to deduct “sums paid” to the ECGD. This section instead allows a deduction for any “sum payable” by the trader. See *Change 21* in Annex 1.

Section 92: Levies etc under FISMA 2000

356. This section provides for the inclusion, in a calculation of trading profits, of certain payments arising from FISMA. It is based on section 76A of ICTA. The corresponding rule for income tax is in section 155 of ITTOIA.
357. *Subsection (1)* applies the section to any company that pays a “levy” and removes three minor restrictions.
- Section 76A of ICTA applies only to an “authorised person”. This section removes that restriction.
 - The section does not reproduce the restriction in section 76A(2)(e) of ICTA for some “costs”.
 - A trading company that also has investment business may qualify for a deduction under this section which is denied by section 76A(1)(b) of ICTA.

See *Change 22* in Annex 1.

358. *Subsection (1)* provides for a deduction. Most FISMA levies would be allowable expenses under the basic trade profit calculation rules. The purpose of this provision is to deal with the exceptional case where deduction of a levy would otherwise be prevented by a prohibitive rule.
359. The expenses allowable are determined by reference to FISMA. *Subsections (2) and (3)* provide the links with FISMA.
360. There is a similar rule about FISMA repayments in section 104.

Chapter 6: Trade profits: receipts

Overview

361. This Chapter contains provisions on how various receipts are to be treated in calculating the profits of a trade.

Section 93: Capital receipts

362. This section is the mirror image of section 53 (capital expenditure). It is new. The corresponding rule for income tax is in section 96 of ITTOIA.

363. *Subsection (1)* sets out the general rule that items of a capital nature are not to be treated as receipts of a trade.
364. It is a long-established principle that capital receipts are ignored in calculating tax on income.
365. *Subsection (2)* disapplies the general rule in subsection (1) where there is statutory provision for a capital sum to be taken into account as a receipt in calculating the profits of a trade. See, for example, section 103 (sums recovered under insurance policies etc) and the rules in Part 5 (loan relationships), Part 7 (derivative contracts) and Part 8 (intangible fixed assets).

Section 94: Debts incurred and later released

366. If an amount owed by a company is released, this section treats the amount released as a trading receipt. The section is based on section 94 of ICTA. The corresponding rule for income tax is in section 97 of ITTOIA.
367. *Subsection (1)(c)* sets out the exception that applies if the debt is released as part of a “statutory insolvency arrangement”, which is defined in section 834(1) of ICTA.
368. The source legislation treats the sum as a receipt “in the period in which the release is effected”. The section makes it clear that the period in question is an accounting period. If the company is no longer carrying on the trade when the debt is released, the amount released is charged to tax as a post-cessation receipt (see section 193 of this Act).

Section 95: Acquisition of trade: receipts from transferor’s trade

369. This section sets out what happens if a successor to a trade receives a sum that arose from the trade when it was carried on by the predecessor. It is based on section 106 of ICTA. The corresponding rule for income tax is in section 98 of ITTOIA.
370. If a sum arises from a trade that has ceased, the usual rule is that the sum is a post-cessation receipt (see Chapter 15 of this Part). But, if the right to receive the sum is transferred with the trade to a company which takes over the trade, this section applies instead.
371. *Subsection (1)* refers to a “person” ceasing to carry on a trade. That person may be one of the partners in a firm. If a firm ceases to carry on a trade, all its partners must also cease. So the section applies in either case.
372. *Subsection (2)* treats the sum as a receipt of the successor’s trade. It is not charged on the predecessor. The source legislation treats the sum as a receipt “in the period in which it is received”. The section makes it clear that the period in question is an accounting period.
373. Different rules apply if the right to receive sums is transferred to a person who does not take over the trade (see section 194 of this Act).

Section 96: Reverse premiums

374. This is the first of a group of five sections based on section 54 of, and Schedule 6 to, FA 1999. This legislation was introduced following the decision of the Privy Council in *Commissioner of Inland Revenue v Wattie and another* (1998), 72 TC 639⁵. An inducement (a “reverse premium”) paid to a tenant to take a lease of land is taxed as income in the hands of the tenant. The corresponding rules for income tax are in sections 99 to 103 of ITTOIA.
375. *Subsection (2)* introduces the term “the recipient”, which is used throughout this group of sections.

376. *Subsection (3)* identifies the transaction which gives rise to a reverse premium.
377. *Subsection (4)* refers to an interest in land being “granted”. This distinguishes such a transaction from one in which an interest is assigned. The general rule is that a charge to tax on a reverse premium arises on the grant of an interest in land but not on its assignment. But assignment can give rise to a charge if the assignor is connected with the grantor.
378. The meaning of “reverse premium” in this section is applied for the purpose of section 250 by subsection (6) of that section.
379. [Schedule 2](#) to this Act rewrites the transitional provision in section 54(2) of FA 1999. These sections do not apply to pre-1999 reverse premiums.

Section 97: Excluded cases

380. This section brings together the various exclusions from the charge on reverse premiums. It is based on paragraphs 5 and 7 of Schedule 6 to FA 1999. The corresponding rule for income tax is in section 100 of ITTOIA.
381. *Subsection (2)* rewrites the rule in paragraph 6 of Schedule 6 to FA 1999 as it was before it was repealed by ITTOIA. It is possible for a company to receive a reverse premium in connection with a property transaction entered into by an individual involving the individual’s only or main residence. The income tax relief is rewritten in section 100(2) of ITTOIA. It was not intended that ITTOIA should withdraw this relief from a company. So this subsection restores the position as it was before ITTOIA. See *Change 23* in Annex 1.

Section 98: Tax treatment of reverse premiums

382. This section treats a reverse premium as a revenue receipt, rather than a capital item. It is based on paragraph 2 of Schedule 6 to FA 1999. The corresponding rule for income tax is in section 101 of ITTOIA.
383. If the transaction giving rise to the reverse premium is at arm’s length there is no statutory timing rule; the normal accountancy treatment applies. If the transaction is not at arm’s length, there is a timing rule in section 99.

Section 99: Arrangements not at arm’s length

384. If a property transaction is not at arm’s length there is a special timing rule. This section provides that the whole of the reverse premium is taxed when the property transaction is entered into. It is based on paragraph 3 of Schedule 6 to FA 1999. The corresponding rule for income tax is in section 102 of ITTOIA.
385. *Subsection (1)* refers to “connected persons”. That expression is defined for the purpose of this section in section 100.
386. *Subsection (5)* deals with the case where the recipient enters into a property transaction for the purposes of a trade but the trade has not yet started. In that case, the reverse premium is brought into account when the trade starts.

Section 100: Connected persons and property arrangements

387. This section sets out the special meaning of “connected persons” that applies for the group of sections on reverse premiums. The basic definition is in section 1316, which imports the definition of “connected persons” in section 839 of ICTA. The section is based on paragraph 8 of Schedule 6 to FA 1999. The corresponding rule for income tax is in section 103 of ITTOIA.

Section 101: Distribution of assets of mutual concerns

388. This section deals with the consequences for a trader of receiving a distribution from a mutual concern that is a corporate body. It is based on section 491 of ICTA. The corresponding rule for income tax is in section 104 of ITTOIA.
389. *Subsection (1)* sets out the circumstances in which a distribution may give rise to a tax charge. It refers to a distribution out of assets that “represent profits” of the concern. This is not quite the same as “assets of a body corporate, other than assets representing capital”, as identified in section 491(1) of ICTA. The difference is that the section excludes assets that represent capital gains of the concern. See *Change 24* in Annex 1.
390. *Subsection (2)* is the general rule: the distribution is treated as a receipt of the trade.
391. *Subsection (3)* deals with the case where the distribution is received after the trade has ceased. The section treats the distribution explicitly as a post-cessation receipt. See *Change 19* in Annex 1.
392. In this Part the rules apply to the company carrying on a trade rather than to the trade itself. So section 337(1)(a) of ICTA is not needed to treat a trade as ceasing when there is a change of company carrying it on. Subsection (3) of this section reproduces the combined effect of section 491(3)(b) and (4) of ICTA.
393. *Subsection (5)* is a special rule that applies if the right to receive a distribution is transferred other than at arm’s length. Market value is substituted for the actual amount received.
394. The section omits the references to mutual insurance and industrial and provident societies in section 491(9) and (11) of ICTA. Those examples were intended to help readers but there is no comprehensive definition of “mutual business”. The subsections were intended to deal with particular doubts which were common when the provision was enacted in 1964. Those doubts do not exist today.

Section 102: Industrial development grants

395. 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 income tax is in section 105 of ITTOIA.
396. This section does not rewrite the references in section 93(2)(a) of ICTA to section 7 or 8 of the Industry Act 1972 or in section 93(2)(b) to section 1 of the Industries Development Act (Northern Ireland) 1966 and section 4 of the Industries Development Act (Northern Ireland) 1971. These enactments were repealed or replaced in 1982 and there are no outstanding instalments under the old enactments.
397. Section 93(3) of ICTA disapplies section 93(1) of ICTA in the case of grants towards the payment of all or part of a corporation tax liability made under Article 7 of the Industrial Development (Northern Ireland) Order 1982. Grants in respect of corporation tax liabilities cannot be made under any of the enactments listed in *subsection (1)* of this section other than Article 7 of the Industrial Development (Northern Ireland) Order 1982. So *subsection (2)* excludes *all* grants in respect of corporation tax liabilities.

Section 103: Sums recovered under insurance policies etc

398. This section concerns insurance recoveries. It is based on section 74(1)(l) of ICTA. The corresponding rule for income tax is in section 106 of ITTOIA.
399. Section 74(1)(l) of ICTA prohibits the deduction in computing a trader’s profits of “any sum recoverable under an insurance or contract of indemnity”. This is regardless of whether the sum is revenue or capital in nature.

*These notes refer to the Corporation Tax Act 2009
(c.4) which received Royal Assent on 26 March 2009*

400. When a sum is recovered under an insurance policy or contract of indemnity in an accounting period *other than* the accounting period in which the event in respect of which it is received occurs, section 74(1)(l) of ICTA requires any deduction made in respect of that event to be adjusted to reflect the recovery.
401. This section provides instead that a capital sum recovered by a trader under an insurance policy or a contract of indemnity is brought into account as a receipt in calculating the profits of the trade to the extent that the loss or expense has been deducted in calculating those profits. This means that the timing of the receipt will follow the accountancy treatment. See *Change 25* in Annex 1.
402. No special provision is needed for sums of a revenue nature.

Section 104: Repayments under FISMA 2000

403. This section provides for the inclusion in a calculation of trading profits of certain receipts arising from FISMA. It is based on section 76A of ICTA. The corresponding rule for income tax is in section 155 of ITTOIA.
404. *Subsection (2)* provides for a repayment under FISMA to be treated as a trade receipt. Most FISMA repayments would be charged to tax under the basic trade profit calculation rules. The purpose of this provision is to deal with the exceptional case where the FISMA repayment would not otherwise be a trade receipt.
405. The receipts chargeable are determined by reference to FISMA. *Subsections (3) and (4)* provide the links with FISMA.
406. There is a similar rule about FISMA levies etc in section 92.

Chapter 7: Trade profits: gifts to charities etc

Section 105: Gifts of trading stock to charities etc

407. This section sets out the main rule for gifts of trading stock. It is based on sections 83A and 84 of ICTA, which give relief for gifts to charities and educational establishments respectively. The corresponding rule for income tax is in section 108 of ITTOIA.
408. When a company disposes of trading stock other than in the course of a trade the general rule is that the market value of the stock is taken into account in calculating the profits of the trade (see Chapter 10 of this Part of this Act). This section sets out an exception to this general rule and applies if the company disposes of trading stock by way of gift to a charity etc.
409. There is a test for gifts to educational establishments in section 84(1)(a) of ICTA concerning the use to which the gift is put in the business of the educational establishment. There is no equivalent test in the rules for the relief for gifts to charities, in section 83A of ICTA. This section does not reproduce the condition in section 84(1)(a) of ICTA. See *Change 26* in Annex 1.
410. *Subsection (1)* combines the ICTA reliefs for gifts to charities and gifts to educational establishments. It includes the extension of the relief to registered clubs in Part 3 of Schedule 18 to FA 2002. The relief covers gifts “for the purposes of” charities etc. See *Change 27* in Annex 1.
411. The section does not require a claim by the company. In this respect, the section is different from section 84(3) of ICTA (but not from section 83A). See *Change 28* in Annex 1.
412. *Subsection (4)* does not reproduce the references to the British Museum and the Natural History Museum. These bodies are charities within subsection (1)(a) of the section.

Section 106: Meaning of “designated educational establishment”

413. This section defines “designated educational establishment” for the purpose of section 105. It is based on section 84 of ICTA. The corresponding rule for income tax is in section 110 of ITTOIA.
414. Section 84(6) of ICTA provides that “the Board” shall refer any question as to whether a particular establishment is a designated educational establishment for the purposes of the section to the Secretary of State or the Department of Education for Northern Ireland. Section 832(1) of ICTA defines “the Board” as “the Commissioners of Inland Revenue” (to be taken as a reference to the Commissioners for Her Majesty’s Revenue and Customs, in accordance with section 50(1) of CRCA).
415. In practice, the function in section 84 of ICTA is exercised by an officer of Revenue and Customs. So *subsection (3)* of this section provides that any question as to whether a particular establishment is a designated educational establishment must be referred to the Secretary of State by “an officer of Revenue and Customs”. See *Change 1* in Annex 1.
416. [The National Assembly for Wales \(Transfer of Functions\) Order 1999 \(SI 1999/672\)](#) devolves the functions of the Secretary of State under section 84 of ICTA to the Welsh Ministers. So this section refers to the Welsh Ministers (and the Assembly).

Section 107: Gifts of medical supplies and equipment

417. This section sets out the main rule for gifts of medical supplies and equipment. It is based on section 55 of FA 2002. It also gives a trading deduction for expenses connected with such gifts.
418. As in section 105, this section overrides the rule in Chapter 10 of this Part of this Act that the market value of a gift should be treated as a trade receipt.
419. *Subsection (3)* is the special rule that the costs of getting the medical supplies and equipment to the recipient are allowed as a deduction.
420. *Subsection (5)* is based on section 55(6) of FA 2002. The power of the Treasury to exclude certain medical supplies and equipment has not been used.
421. There is no corresponding rule for income tax. So section 55 of FA 2002 is repealed by Schedule 1 to this Act. See *Change 29* in Annex 1.

Section 108: Receipt of benefits by donor or connected person

422. This section sets out what happens if a company receives a benefit in connection with a gift of trading stock or plant and machinery. It is based on sections 83A and 84 of ICTA and section 55 of FA 2002. The corresponding rule for income tax is in section 109 of ITTOIA.
423. *Subsection (1)* applies the section if a benefit is received by the company or a connected person. Section 82 of this Act (contributions to local enterprise organisations or urban regeneration companies) uses the same approach. The benefit must be in connection with a gift for which relief has been given under section 105, section 107 or the corresponding capital allowances rule.
424. *Subsection (2)* extends the recovery charge to a benefit attributable to the costs associated with making a gift of medical supplies and equipment.
425. If the donor is still carrying on the trade when the benefit is received the value of the benefit is treated as a trading receipt.

426. If the donor has ceased to carry on the trade when the benefit is received the value of the benefit is treated as a post-cessation receipt. This treatment replaces the general charge under Schedule D Case VI. See *Change 19* in Annex 1.

Chapter 8: Trade profits: herd basis rules

Overview

427. This Chapter gives the rules for what is commonly known as the “herd basis”. It is based on Schedule 5 to ICTA. The corresponding rules for income tax are in Chapter 8 of Part 2 of ITTOIA.
428. The object of the herd basis is to treat a herd of animals in a similar fashion to a capital asset. Without the election the individual animals in the herd would be treated as separate items of trading stock. With the election:
- there is no tax allowance for the initial cost of, or any subsequent increase in the size of, the herd;
 - the net cost of replacing animals in the herd is allowable;
 - any profit or loss on the sale of a single animal or a small number of animals from the herd without replacement is included in the profits of the trade; and
 - if the whole, or a substantial part, of the herd is sold and not replaced the resulting profit or loss is not included in the profits of the trade.
429. An election can be made only in respect of animals kept for their produce.

Section 109: Election for application of herd basis rules

430. This section allows a taxpayer to elect for the “herd basis rules” to apply and introduces some basic concepts. It is based on paragraphs 1, 2, 3 and 9 of Schedule 5 to ICTA. The corresponding rules for income tax are in section 111 of ITTOIA.
431. *Subsection (1)* allows a company or firm of which a company is a member to make a “herd basis election” if it keeps, or has kept, a “production herd”. “Production herd” is defined in section 110(1)(c). The effect of a “herd basis election” is that the “herd basis rules” apply. These rules are set out in sections 112 to 121. The time limits for making the election are set out in sections 122 to 124.

Section 110: Meaning of “animal”, “herd”, “production herd” etc

432. This section provides various definitions used in the Chapter. It is based on paragraphs 8 and 9 of Schedule 5 to ICTA. The corresponding rules for income tax are in section 112 of ITTOIA.
433. This section would be the natural home for the rule in paragraphs 7 and 9(5) of Schedule 5 to ICTA that prevents the herd basis rules applying to working animals. Paragraphs 7 and 9(5) of Schedule 5 to ICTA exclude certain animals from being part of a production herd. These are animals kept for the work they do in connection with the trade or those kept for public exhibition, or racing or other competitive purposes. This rule is unnecessary because animals in a production herd must be kept wholly or mainly for the sake of their produce. So the exclusions are not rewritten.
434. *Subsection (1)(a)* rewrites the definition of “animal” in paragraph 9 of Schedule 5 to ICTA. Most of the definitions in paragraph 9 of Schedule 5 to ICTA refer to “animals and other living creatures”. The main reason for the reference to “other living creatures” is to make clear that the Schedule applies to birds.
435. *Subsection (1)(c)* rewrites the definition of “production herd” in paragraph 8(5) of Schedule 5 to ICTA. Herd basis elections are made by reference to classes of production

herd. See section 122. Section 111(2) identifies when different production herds are treated as being of the same class.

436. *Subsection (6)* makes clear that an immature animal can be treated as added to the herd when it becomes mature. There is a definition of maturity for female animals in section 111(5).

Section 111: Other interpretative provisions

437. This section provides further definitions. It is based on paragraphs 3, 8 and 9 of Schedule 5 to ICTA. The corresponding rules for income tax are section 113 of ITTOIA.
438. *Subsection (2)(a)* applies if production herds of animals of different species are kept for the same product; for example, a herd of cows and a herd of goats both kept for milk production. Each herd satisfies the definition of production herd. Subsection (2) (a) prevents them being treated as of the same class.
439. Subsection (2)(b) prevents animals of the same species being treated as of the same class if they are kept for different products; for example, one herd of cows kept for milk production and another herd of cows kept for its calves.
440. *Subsection (6)* clarifies what is meant by “a substantial part of the herd”. This is a question of fact depending on the circumstances. But 20% of the herd is always regarded as substantial. This change clarifies this practice. This change reproduces Change 32 in ITTOIA. See *Change 30* in Annex 1.
441. The following sections refer to “a substantial part of the herd”.
- Section 116(1) (sale of animals from the herd);
 - Section 117(1) (sale of whole or substantial part of herd);
 - Section 118(4) and (5) (acquisition of new herd begun within five years of sale);
 - Section 120(1) (replacement of part sold within five years of sale); and
 - Section 124(1) (slaughter under disease control order).

Section 112: Initial cost of herd and value of herd

442. This section sets out the treatment of the initial cost, and value, of the herd. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 114 of ITTOIA.

Section 113: Addition of animals to herd

443. This section sets out the treatment of additions to the herd. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 115 of ITTOIA.
444. *Subsection (1)* makes clear that there is a difference between additions, to which this section applies, and replacements dealt with in section 114.
445. *Subsection (2)* prevents a deduction for the cost of the additional animal. It is a similar rule to section 112(1).

Section 114: Replacement of animals in herd

446. This section sets out the treatment if an animal in the herd is replaced. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 116 of ITTOIA.

447. *Subsection (1)* introduces the terms “old animal” to describe an animal leaving the herd and “new animal” to describe the animal that replaces it. The circumstances in which an animal is treated as sold and the meaning of “sale proceeds” are extended by the definitions in section 111(3) and (4).
448. *Subsection (4)* deals with the deduction due for the replacement animal. The basic principle in paragraph 3(4)(b) of Schedule 5 to ICTA is that the cost of the second animal is deducted as a trading expense. But paragraph 3(4)(b) of Schedule 5 to ICTA provides for an exception - “in so far as that cost consists of such costs as are allowable apart from the provisions of this Schedule as deductions in computing profits of farming under Case I of Schedule D”.
449. It is not clear from ICTA what these costs are. In fact the exception is aimed at the case where the replacement animal comes from trading stock. Here the costs of breeding or acquiring it and, if relevant, rearing it to maturity have already been allowed. The farmer is not allowed a double deduction for costs that have already been allowed.
450. This section does not reproduce that part of paragraph 3(4)(b) of Schedule 5 to ICTA which refers to the cost of the new animal being subject to paragraph 3(6) of Schedule 5 to ICTA. This reference appears to be an error made in the 1988 consolidation of ICTA. It is generally accepted that it is the rule in paragraph 3(4)(a), and not paragraph 3(4)(b), of Schedule 5 to ICTA which should be qualified by paragraph 3(6) of Schedule 5 to ICTA.

Section 115: Amount of receipt if old animal slaughtered under disease control order

451. This section limits the amount of the receipt taxed under section 114 if the old animal is slaughtered under a disease control order. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 117 of ITTOIA.
452. Paragraph 3(6) of Schedule 5 to ICTA restricts the amount of the receipt to “the amount allowable as a deduction”. It is not immediately clear what this amount is. This section makes clear that it is the amount allowable as a deduction in respect of the new animal. This is called “the equivalent amount for the new animal”.
453. *Subsections (4)* and *(5)* define “the equivalent amount for the new animal”. *Subsection (4)* deals with the case in which the replacement animal comes from the farmer’s trading stock. *Subsection (5)* deals with all other cases.

Section 116: Sale of animals from herd

454. This section sets out the rules that apply if an animal is sold from the herd and not replaced. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 118 of ITTOIA.

Section 117: Sale of whole or substantial part of herd

455. This is the first of three sections that set out the rules relating to the sale of all or a substantial part of the herd within 12 months. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 119 of ITTOIA.
456. The section merges the rules in paragraph 3(7) to (9) of Schedule 5 to ICTA. This Change reproduces Change 33 in ITTOIA. See *Change 31* in Annex 1.

Section 118: Acquisition of new herd begun within 5 years of sale

457. This section sets out the rules that apply if, following the sale of the herd (either all at once or within 12 months), the farmer begins to acquire a new herd within five years. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 120 of ITTOIA.

458. *Subsection (4)* applies if the number of animals in the new herd is smaller than the number of animals in the old herd but the difference is not substantial. See *Change 31* in Annex 1.
459. *Subsection (7)* clarifies what is meant by a “substantial difference”. See *Change 30* in Annex 1.

Section 119: Section 118: sale for reasons outside farmer’s control

460. This section limits the amount taxed as a trade receipt under section 118 if the sale is for reasons outside the farmer’s control and the replacement animal is of a worse quality. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 121 of ITTOIA.
461. The section is similar to section 115 although it is not limited, as that section is, to disposals under a disease control order. The source legislation for both sections refers to the amount of the trading receipt being restricted to “the amount allowable as a deduction”. It is not immediately clear what this amount is.
462. *Subsection (2)* makes clear that it is the amount allowable as a deduction in respect of the new animal. The section calls this “the equivalent amount for the new animal”.
463. *Subsections (3) and (4)* define “the equivalent amount for the new animal”. Subsection (3) deals with the case in which the replacement animal comes from the farmer’s trading stock. Subsection (4) deals with all other cases.

Section 120: Replacement of part sold begun within 5 years of sale

464. This section sets out the rules that apply if, following the sale of a substantial part of a herd (either all at once or within a year), the farmer begins to replace it within five years. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 122 of ITTOIA.

Section 121: Section 120: sale for reasons outside farmer’s control

465. This section limits the amount taxed as a trade receipt under section 120 if the sale is for reasons outside the farmer’s control and the new animal is of a worse quality. It is based on paragraph 3 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 123 of ITTOIA.
466. The section is similar to section 115 although it is not limited, as that section is, to disposals under a disease control order. The source legislation for both sections refers to the amount of the trading receipt being restricted to “the amount allowable as a deduction”. It is not immediately clear what this amount is.
467. *Subsection (2)* makes clear that it is the amount allowable as a deduction in respect of the new animal. The section calls this “the equivalent amount for the new animal”.
468. *Subsections (3) and (4)* define “the equivalent amount for the new animal”. Subsection (3) deals with the case in which the replacement animal comes from the farmer’s trading stock. Subsection (4) deals with all other cases.

Section 122: Herd basis elections

469. This section sets out the rules for the making of herd basis elections. It is based on paragraph 2 of Schedule 5 to ICTA. The corresponding rules for income tax are in section 124 of ITTOIA.
470. Paragraph 2 of Schedule 5 to ICTA requires that the election must be made “in writing” and to an officer of Revenue and Customs. The general rules in Part 7 of Schedule 18 to FA 1998 that apply to claims and elections mean it is not necessary to repeat these requirements.

471. *Subsection (2)* sets out the time limits for making the election. The election is made by the farmer. The farmer can be a company or a firm in which one of the partners is a company. The time limits are different depending on whether the farmer is a company or a firm.
472. If the farmer is a firm the same time limit applies whether the partners are all income tax payers, all corporation tax payers or a combination of the two. Because of the possible involvement of income tax payers the time limit is set by reference to income tax years. The time limit in section 122(2)(b) is the same as that in section 124(2)(a) of ITTOIA.
473. The different time limits for a company or a firm are reflected in the other two sections that deal with herd basis elections, sections 123 and 124. Those sections identify the difference by referring to the “accounting period” (company) or the “period of account” (firm).
474. *Subsection (4)* expands on *subsection (1)*, which provides that an election must specify the class of production herd to which it relates. This means separate elections must be made for each class of production herd and that an election may not relate to more than one class of production herd. Separate elections may be made for different classes.
475. *Subsection (7)* identifies the period for which the herd basis election has effect. This depends on whether the farmer is a company (accounting period) or firm (period of account).
476. *Subsection (8)* deals with the case in which the farmer is a firm and there is a change in the partners in the firm. Paragraph 2 of Schedule 5 to ICTA refers to “the farmer making the election”. If the farming trade is carried on in partnership, the “farmer” means the firm. If there is a change in the members of a firm, the question arises whether there is a new “farmer”. Subsection (8) makes clear that there is.

Section 123: Five year gap in which no production herd kept

477. This section deals with the case where there is a period of at least five years when the farmer does not keep a production herd of the particular class for which a herd basis election has been made. It is based on paragraph 4 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 125 of ITTOIA.
478. *Subsection (2)* explains the consequences for the herd basis rules if the farmer starts to keep another production herd of the same class after the end of the five year period. Subsection (2) enacts an extra-statutory practice. See *Change 32* in Annex 1. This Change reproduces Change 36 in ITTOIA.

Section 124: Slaughter under disease control order

479. This section sets out the rules for making an election outside the normal time limits following slaughter under a disease control order. It is based on paragraph 6 of Schedule 5 to ICTA. The corresponding rules for income tax are in section 126 of ITTOIA.

Section 125: Preventing abuse of the herd basis rules

480. This section provides anti-avoidance rules that may apply if a farmer transfers the whole or part of a production herd in a transaction that is not an open market sale. It is based on paragraph 5 of Schedule 5 to ICTA. The corresponding rules for income tax are in section 127 of ITTOIA.
481. **Section 164(3)** in Chapter 11 of this Part (trade profits: valuation of stock) makes clear that this section takes priority over the provisions of that Chapter.

Section 126: Information if election made

482. This section allows an officer of Revenue and Customs to obtain information about the animals kept for the purposes of the trade. It is based on paragraph 10 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 128 of ITTOIA.

Section 127: Further assessment etc if herd basis rules apply

483. This section enables effect to be given to a herd basis election made after an assessment has become final, either by amendment or by repayment of tax. It is based on paragraph 11 of Schedule 5 to ICTA. The corresponding rule for income tax is in section 129 of ITTOIA.

Chapter 9: Trade profits: other specific trades

Overview

484. This Chapter contains special rules for the taxation of particular trades.

Section 128: Taxation of amounts taken to reserves

485. This section contains a special rule for the treatment of securities held by a company carrying on a banking or insurance business, or a business of dealing in securities, and on which profits and losses are calculated by reference to the “fair value” of the securities rather than on a realisation basis. It is based on section 472A of ICTA. The corresponding rule for income tax is in section 149 of ITTOIA.
486. Financial assets can be dealt with in a number of ways for accounting purposes.
487. Where a company dealing in securities uses United Kingdom generally accepted accountancy practice (“UK GAAP”), profits and losses calculated by reference to the fair value of securities treated as trading assets are taken to profit and loss account. “Fair value” is an accounting term, the meaning of which is broadly equivalent to market value. UK GAAP is defined in section 50(4) of FA 2004.
488. Where a company dealing in securities prepares accounts in accordance with international accounting standards, the securities would usually fall to be accounted for as at fair value, in accordance with paragraph 9 of International Accounting Standard 39 (“IAS 39”), and any profits and losses calculated by reference to the fair value of securities taken to the profit and loss account. But the company may instead account for certain securities as “available for sale” if they do not meet the conditions for being treated as at fair value through profit or loss. In such a case profits and losses calculated by reference to the fair value of securities are taken initially to a statement of changes in equity.
489. Since 2005, UK GAAP in this area follows IAS 39. Under UK GAAP the profits and losses on “available for sale” assets are taken to the statement of total recognised gains and losses.
490. **Section 46** of this Act provides that the calculation of profits or losses from a trade must be based on accounts drawn up in accordance with generally accepted accountancy practice, subject to any adjustment authorised by law. Implicit in this rule is that the profits must appear in the profit and loss account. There is no tax law (apart from this section) which allows profits on equity securities taken to any form of reserve to be treated for corporation tax purposes as if they were taken to profit and loss account.
491. *Subsection (3)(b)* provides that subsection (2) does not apply to “an amount recognised for accounting purposes by way of correction of a fundamental error”. This refers to the requirement in International Accounting Standard 8 (Accounting Policies, Changes in Accounting Estimates and Errors) that the correction of a fundamental error should be treated as a prior period adjustment. “For accounting purposes” is defined in

section 832(1) of ICTA as “for the purposes of accounts drawn up in accordance with generally accepted accounting practice”.

492. Section 472A(4)(a) of ICTA defines “securities” to include rights, interests or options treated as shares for the purposes of sections 126 to 136 of TCGA by virtue of sections 135(5) or 136(5) of TCGA. Sections 135(5) and 136(5) of TCGA define “shares” in the case of a company with no share capital as “any interests in the company possessed by members of the company.” So *subsection (4)(c)* of this section defines “securities” to include such interests.

Section 129: Conversion etc of securities held as circulating capital

493. This section provides for relief on the conversion or exchange of securities held as part of the circulating capital of a company dealing in securities. It is based on section 473 of ICTA. The corresponding rule for income tax is in section 150 of ITTOIA.
494. Section 473(1) of ICTA applies to securities to which a company carrying on a banking or insurance business, or a business of dealing in securities, is beneficially entitled, the profits from the sale of which would “form part of the trading profits of that business”. This section does not stipulate that the company must be beneficially entitled to the securities in question. See *Change 33* in Annex 1.
495. *Subsection (3)* excludes securities brought into account at “fair value” in calculating the profits for the period in which the relevant transaction takes place. These are instead dealt with in section 128.
496. Section 137(1) of TCGA provides that sections 135 and 136 of TCGA do not apply to an exchange of shares unless the exchange is:
- effected for bona fide commercial reasons and does not form part of a scheme or arrangements of which the main purpose, or one of the main purposes, is avoidance of liability to capital gains tax or corporation tax.
497. *Subsection (7)* of this section adapts the rule in section 137(1) of TCGA to include the avoidance of income tax. This covers, for example, a scheme or arrangement the purpose of which is the avoidance of income tax by a director of, or participator in, the company rather than the avoidance of corporation tax by the company itself.

Section 130: Traders receiving distributions etc

498. This section provides that distributions of a UK resident company, and payments “representative of” such distributions, are brought into account in calculating the profits of a trade if those distributions and payments are receipts or expenses of the trade on first principles. It is based on section 95 of ICTA. The corresponding rule for income tax is in section 366(1) of ITTOIA.
499. A payment “representative of” a distribution may arise, for example, if shares are on loan at the dividend date. The dividend is received by the person to whom the shares are lent. A payment made by that person to compensate the lender for the dividend which would have been received if the shares had not been lent “represents” that dividend.
500. Section 95 of ICTA operates by bringing the distribution or representative payment into account in calculating the profits of a company which is a dealer in relation to that distribution or payment. That company holds the shares in respect of which the distribution is received (or the payment made) as assets on current account rather than as investments.
501. *Subsections (1)* and *(2)* focus on the nature of the receipt rather than on the recipient. Similarly, *subsections (3)* and *(4)* focus on the nature of the payment. See *Change 34* in Annex 1.

502. **Section 1285** of this Act is the general rule that no liability to corporation tax arises on dividends or other distributions of a UK resident company. Subsection (2) of this section disapplies section 1285 in the case of a UK distribution or a payment representing such a distribution.
503. **Section 1305** of this Act is the general rule that no deduction is allowed in respect of a dividend or other distribution. Schedule 23A to ICTA contains special rules for the treatment of amounts representative of dividends on UK shares. In accordance with paragraph 2(2)(b) of Schedule 23A, a payment representative of a UK dividend is treated, in relation to the company by which it is paid, as if it were a dividend on its own shares.
504. Subsections (3) and (4) override section 1305. So a payment representative of a UK distribution is to be taken into account in calculating the corporation tax profits of the company making the payment.
505. Subsection (3) applies to a payment which would be allowed but for section 1305. A payment in respect of which a deduction is disallowed under paragraph 7A of Schedule 23A of ICTA is not within subsection (3). So it is not necessary to rewrite section 95(1C) ICTA in this section.

Section 131: Incidental costs of issuing qualifying shares

506. This section allows a deduction to building societies for the incidental costs of issuing shares. It is based on section 477B of ICTA.
507. Most shares issued by building societies fall with the loan relationship rules in Parts 6 and 7 of this Act. This is because they are excluded from the definition of “share” in section 476(1) of this Act. The result is that most of the incidental costs associated with the issue of the shares are relieved under section 307 of this Act.
508. But it is possible for some building society shares not to qualify as loan relationships. And, even if they do, some incidental costs may not fall within section 307. So this section deals with the costs that are not relieved under the loan relationship rules.

Section 132: Dividends etc granted by industrial and provident societies

509. This section ensures that a “divi” paid by an industrial and provident society is allowed as a trading deduction. It is based on section 486 of ICTA.
510. The main rules about industrial and provident societies are in Chapter 5 of Part 6 of this Act (loan relationships).
511. A definition of “registered industrial and provident society” is inserted into section 834(1) of ICTA (see Schedule 1).
512. *Subsection (1)* sets out the sort of society to which the section applies. An example is an agricultural co-operative that sells (or buys) on behalf its farming members.
513. *Subsection (2)* is the trading income rule. In practice it is likely that the payments with which the section is concerned would be allowable under the normal trading income rule. But this section puts the matter beyond doubt.
514. The source legislation refers to the calculation of any profits “for the purpose of any provision of the Tax Acts relating to profits chargeable under Case I of Schedule D”. It is probable that the quoted words, read with sections 21A and 21C of ICTA, apply the rule for the purpose of a calculation of Schedule A profits. But, in the context of a property business, a “divi” is not paid “on account of the recipient’s transactions with the society”. So in practice the rule does not apply to a property business and the section refers simply to calculating the profits of the trade.

515. *Subsection (5)* is a signpost to the rule (inserted into ICTA by Schedule 1) that the “divi” is not a distribution.

Section 133: Annual payments paid by a credit union

516. This section denies a trading deduction for an annual payment made by a credit union. It is based on section 487 of ICTA.
517. Most credit unions do not carry on a trade for tax purposes. This is the consequence of section 40. But it is possible that some of the activities of a credit union fall outside the scope of the rule in that section. In that case, a calculation of the profits of the trade is required.
518. It is also possible that a credit union carries on a property business. So section 210(2) applies the trading income rule to property businesses.

Section 134: Purchase or sale of woodlands

519. This section applies to a person carrying on a trade of dealing in land who buys and sells land on which trees are growing. It is based on section 99 of ICTA. The corresponding rule for income tax is in section 156 of ITTOIA.
520. Any profit on the sale of the trees and underwood is tax-free because of the exemption for the occupation of commercial woodlands. See section 37 of this Act. *Subsection (2)* prevents the dealer in land obtaining a trade deduction for that part of the cost of the land that is attributable to the cost of the trees.
521. The legislation rewritten by subsection (2) only applies to woodlands purchased under a contract entered into on or after 1 May 1963. This limitation is preserved in Schedule 2 (transitions and savings). The corresponding provision for income tax is paragraph 42 of Schedule 2 to ITTOIA.

Section 135: Relief in respect of mineral royalties

522. This section gives relief if trade receipts include mineral royalties. It is based on section 122 of ICTA. The corresponding rule for income tax is in section 157 of ITTOIA.
523. Most mineral royalties are taxed under Chapter 7 of Part 4 of this Act. That Chapter rewrites the charge under Schedule D Case VI if rents are received from a concern listed in section 55 of ICTA. That list includes mines and quarries. In nearly all cases the rents are taxed under Chapter 7 of Part 4 of this Act as they are not received in respect of a trade. But it is possible that the receipt of the rent will be incidental to a trade. In that case section 287 of this Act provides that the rent is taxed under Part 3 of this Act. This is only likely to happen if the rent is received by a property developer in respect of land held as trading stock.
524. The mineral royalties are halved. The relief is rewritten under the italicised heading “dealers in land” because they are the traders who are most likely to benefit from the relief. But the relief is not confined to dealers in land.

Section 136: Lease premiums etc: reduction of receipts

525. This section prevents a person, carrying on a trade of dealing in land, from being taxed on all or part of a lease premium, or of certain other amounts received in respect of a lease, both as a receipt of the trade under this Part and as a receipt of a property business under Part 4 of this Act. It is based on section 99(2) and (3) of ICTA. The corresponding rule for income tax is in section 158 of ITTOIA.

Section 137: Mineral exploration and access

526. This section deals with intangible drilling costs of production wells in the oil and gas industry. It is based on section 91C of ICTA. The corresponding rule for income tax is in section 161 of ITTOIA.
527. Intangible costs are those which do not result in the acquisition or creation of machinery or plant. An example would be the cost of hiring a drilling rig. Production wells are wells that are drilled after the presence of oil in an area has been established and which are used to extract the oil.
528. Before the enactment of section 91C of ICTA, a deduction was allowed for the intangible drilling costs of the second and subsequent production wells in any area. This reflected a Special Commissioners decision in 1920 that this expenditure is of a revenue nature. This section disallows a deduction for such costs. It does this by denying a deduction for expenditure which, if it had been carried out while exploring for oil, would not have been allowed as a deduction.
529. These costs are capital expenditure and qualify for mineral extraction capital allowances (see Part 5 of CAA).

Section 138: Payments by companies liable to pool betting duty

530. This section gives a special deduction to companies which pay pool betting duty. It is based on those parts of section 126 of FA 1990 and section 121 of FA 1991 which relate to the calculation of the profits of traders. The corresponding rule for income tax is in section 162 of ITTOIA.
531. In 1990, following the Hillsborough disaster, pool betting duty was reduced on condition that the money saved be paid to the Football Trust 1990 to implement Lord Justice Taylor's recommendations on safety and comfort at football grounds. In 1991 the duty was reduced again, this time on condition that the money be paid to the Foundation for Sport and the Arts, a charitable trust which supports athletic sports and games and promotes the arts. The reductions were initially for a limited period, but have so far been maintained.
532. *Subsection (1)* sets out the circumstances in which the section applies. It introduces the expression "qualifying payment".
533. *Subsection (2)* defines a "qualifying payment" to which the section applies. It does not specify that payments in consequence of the 1990 reduction in pool betting duty must be paid for football safety and comfort, and that payments in consequence of the 1991 reduction must be paid to the Foundation for Sport and the Arts. Instead the section applies to a payment for either purpose in consequence of any reduction in pool betting duty. See *Change 35* in Annex 1.
534. The section retains a general description of the payments, without identifying the bodies which were the targets of the original legislation. It is clear that payments made as a consequence of a reduction in pool betting duty to either body would qualify for relief under the section.
535. The source legislation is restricted to the 1990 and 1991 reductions in pool betting duty. This section applies to payments made in consequence of any reduction in the duty. See *Change 36* in Annex 1.
536. *Subsection (3)* is the rule that allows the payments as a trading deduction. Without this rule the payments might be disallowed because they are not made wholly and exclusively for the purposes of the company's trade.

Section 139: Deduction for deemed employment payment

537. This section sets out the trading income rules that were originally part of the “IR35” scheme for the taxation of workers supplied by an intermediary. It is based on paragraph 17 of Schedule 12 to FA 2000. The corresponding rule for income tax is in section 163 of ITTOIA.
538. The worker is treated as receiving a “deemed employment payment” and is taxed accordingly (see Chapter 8 of Part 2 of ITEPA). This section ensures that an equivalent amount is allowed as a trading deduction in calculating the profits of the intermediary.
539. *Subsection (3)* is a timing rule. Generally, the deemed employment payment is treated as made at the end of the tax year (see section 50(3) of ITEPA). In some circumstances the payment is treated as made earlier (see section 57 of ITEPA). In either case, the trading deduction is given for the period of account in which the payment is treated as made.
540. *Subsection (4)* is the rule that prevents any double deduction. It caters for the possibility that the payment may qualify as a trading deduction on first principles and also qualify as a trading deduction in a period of account different from that specified in subsection (3).

Section 140: Special rules for partnerships

541. This section sets out two additional rules that apply if a deduction under section 139 is to be given in calculating the trading profits of a firm. It is based on paragraph 18 of Schedule 12 to FA 2000. The corresponding rule for income tax is in section 164 of ITTOIA.
542. [Section 1257](#) of this Act explains that “firm” is used in this Act to refer to persons carrying on a trade in partnership. It includes a limited liability partnership (see section 1273).
543. *Subsection (2)* is the rule that a deduction under section 139 of this Act cannot be used to create a loss in a firm. It operates by reference to the firm’s period of account. See *Change 37* in Annex 1.
544. *Subsection (3)* is the rule that limits the trading deduction to the amount that would have been deductible if the worker had been an employee of the intermediary, plus a margin to cover the expenses of the firm.
545. In accordance with paragraph 244 of Schedule 6 to ITEPA, “deemed Schedule E payment” in paragraph 18 of Schedule 12 to FA 2000 is replaced by “deemed employment payment”. Similarly, in the same paragraph, “Schedule E” is replaced by “the employment income Parts of the Income Tax (Earnings and Pensions) Act 2003”.
546. But the specific statutory references, such as those to “paragraph 7” (of Schedule 12 to FA 2000), are covered by the general rule in paragraph 5 of Schedule 7 to ITEPA. That general rule is that any reference to a repealed provision is to be read as a reference to the rewritten provision.
547. Paragraph 7 of Schedule 12 to FA 2000 has been repealed and rewritten as section 54(1) of ITEPA. So the reference to that paragraph in paragraph 18 of Schedule 12 is to be read as a reference to section 54(1) of ITEPA. This section updates the references to paragraph 7.

Section 141: Deduction for deemed employment payments

548. This section gives a trading deduction if a managed service company (“MSC”) makes a “deemed employment payment” to a worker under section 61D of ITEPA. It is based on paragraph 10 of Schedule 3 to FA 2007. The corresponding rule for income tax is in section 164A of ITTOIA.

549. The worker is treated as receiving a “deemed employment payment” and is taxed accordingly (see Chapter 9 of Part 2 of ITEPA). This section ensures that an equivalent amount (and no more) is allowed as a trading deduction in calculating the profits of the MSC.
550. *Subsection (5)* prevents any double deduction. It caters for the possibility that the payment may qualify as a trading deduction on first principles and also qualify as a trading deduction in a period of account different from that specified in subsection (3).

Section 142: Deduction for site preparation expenditure

551. This section sets out the rules for expenditure on preparing a site so that it can be used for waste disposal. It is the first of four sections that deal with waste disposal. They are based on sections 91B and 91BA of ICTA. The corresponding rules for income tax are in sections 165 to 168 of ITTOIA.
552. This section covers expenditure which is not deductible because it is capital and which is not eligible for capital allowances; in other words, expenditure that would otherwise go unrelieved for corporation tax purposes.
553. *Subsection (1)* introduces the concept of waste materials being deposited on a “waste disposal site”, an expression defined in section 144.
554. *Subsection (2)* is the link to section 143, which calculates the amount of expenditure that is allowed as deduction.
555. A deduction under section 91B of ICTA is allowed only if the company makes a claim (in such form as the Commissioners for HMRC may direct) and submits such plans and other documents (if any) as the Commissioners may require. This section drops the requirement for a claim. See *Change 38* in Annex 1.
556. [Schedule 2](#) to this Act rewrites the transitional provision in section 91BA(1) of ICTA. Expenditure cannot be “inherited” if the site changed hands before March 2000.
557. *Subsection (4)* treats the company’s trade as the same as that of its predecessor. This is necessary because the activities taken over may amount to less than the whole of the predecessor’s trade (see subsection (3)(a)).

Section 143: Allocation of site preparation expenditure

558. This section spreads site preparation expenditure over the useful life of the site. It is based on section 91B of ICTA. The corresponding rule for income tax is in section 166 of ITTOIA.
559. Some waste disposal sites, notably in the nuclear waste industry, have preparation expenditure dating from before 6 April 1989. So this section preserves the rules for the pre-1989 expenditure.

Section 144: Site preparation expenditure: supplementary

560. This section contains the definitions of the expressions used in the waste disposal sections and sets out the rules for pre-trading expenditure. It is based on sections 91A, 91B and 91BA of ICTA. The corresponding rule for income tax is in section 167 of ITTOIA.
561. Although the definitions are expressed to apply “for the purposes of sections 142 and 143”, the definition of “waste disposal licence” is also used to define a “site restoration payment” in section 145(5).
562. In *subsection (1)(b)* the corresponding Northern Ireland provision is Part 2 of the [Waste and Contaminated Land \(Northern Ireland\) Order 1997 \(SI 1997/2778 \(N.I.19\)\)](#).

563. *Subsection (1)(c)* identifies more specifically the provisions described in section 167(1)(c) of ITTOIA. It reflects the amendments to section 91A(6) of ICTA made by:
- the [Pollution Prevention and Control \(England and Wales\) Regulations \(SI 2000/1973\)](#);
 - the [Pollution Prevention and Control \(Scotland\) Regulations \(SI 2000/323\)](#); and
 - paragraph 3 of Schedule 11 to the [Pollution Prevention and Control Regulations \(Northern Ireland\) 2003 \(SR 2003/46\)](#).

Section 145: Site restoration payments

564. This section deals with payments for the restoration of a site after it has been used for waste disposal. It is based on section 91A of ICTA. The corresponding rule for income tax is in section 168 of ITTOIA.
565. In *subsection (6)(a), (c) and (d)* the corresponding Northern Ireland provision is Article 40 of the [Planning \(Northern Ireland\) Order 1991 \(SI 1991/1220 \(N.I. 11\)\)](#).

Section 146: Cemeteries and crematoria: introduction

566. This section, and the following three sections, contain special rules for companies carrying on a trade of operating a cemetery or crematorium. They are based on section 91 of ICTA. The corresponding rules for income tax are in sections 169 to 172 of ITTOIA.
567. Without special provisions, no allowance would be due for the cost of land sold for interments, memorial gardens attached to crematoria or the surrounding land and buildings because expenditure on such land and buildings is in the nature of capital. The provisions in sections 146 to 149 recognise that most land and buildings in a cemetery or memorial garden are of little value when the cemetery or memorial garden is full.
568. This section introduces the provisions in sections 147 to 149 and defines some of the terms used in those sections.
569. Section 91(7)(a) of ICTA adapts the rules for cemeteries in section 91 of ICTA to crematoria and treats “land which is devoted wholly to memorial garden plots” as a cemetery, or as land in a cemetery. *Subsection (1)* of this section instead includes the carrying on of a crematorium, and the maintenance of “memorial gardens plots” in the trades to which sections 146 to 149 apply.
570. Section 91(5) of ICTA provides that a change of ownership is ignored in calculating the relief due to the person then carrying on the trade. So *subsection (4)* of this section includes expenditure incurred by “a predecessor” of the company carrying on the trade in the definition of ancillary capital expenditure.

Section 147: Deduction for capital expenditure

571. This section provides for a deduction for certain capital expenditure incurred by the trader or a predecessor. It is based on section 91 of ICTA. The corresponding rule for income tax is in section 170 of ITTOIA.
572. Section 91 of ICTA refers to “land” in a cemetery or crematorium. *Subsection (1)* refers instead to “an interest in” such land. This accommodates better the possibility that operators of cemeteries and crematoria might sometimes hold land in leasehold rather than in freehold form.

Section 148: Allocation of ancillary capital expenditure

573. This section contains special rules for allocating ancillary capital expenditure to a period of account. It is based on section 91 of ICTA. The corresponding rule for income tax is in section 171 of ITTOIA.
574. See section 146(4) for the definition of “ancillary capital expenditure”.

Section 149: Exclusion of expenditure met by subsidies

575. This section excludes certain expenditure for the purposes of section 147. It is based on section 91 of ICTA which applies the provisions of section 532 of CAA for the purposes of section 91 of ICTA. The corresponding rule for income tax is in section 172 of ITTOIA.
576. *Subsection (3)* refers to a grant made under Northern Ireland legislation and declared by the Treasury to correspond to a grant under Part 2 of the Industrial Development Act 1982. The term “Northern Ireland legislation” is defined by Schedule 1 to, and section 24(5) of, the Interpretation Act 1978.
577. The [Capital Allowances \(Corresponding Northern Ireland Grants\) Order 2001 \(SI 2001/810\)](#) lists various grants made in Northern Ireland and declared by the Treasury to correspond to a grant under Part 2 of the Industrial Development Act 1982 in so far as they are made towards capital expenditure. The Industrial Development Act 1982 has been repealed. But a deduction under section 147 of this Act continues to be allowed for expenditure met by a grant corresponding to a grant under Part 2 of the 1982 Act incurred by the trader, or by a predecessor.

Section 150: Revenue nature of expenditure

578. This section provides for the trader’s expenditure, on producing or acquiring the original master version of a sound recording, to be treated as expenditure of a revenue nature. It is based on section 48 of FA 2006.
579. Where this section applies to a sound recording any of the trader’s receipts from it are treated as having a revenue nature.

Section 151: Allocation of expenditure

580. This section provides for the allocation of a trader’s expenditure on producing or acquiring the original master version of a sound recording except where that master version is trading stock. It is based on section 49 of FA 2006.
581. *Subsection (3)* sets out the basis for the allocation and *subsection (4)* provides for an enhanced allocation in certain cases.

Section 152: Interpretation of sections 150 and 151

582. This section provides definitions of terms used in the previous two sections. It is based on sections 31 and 50 of FA 2006.

Section 153: Reserves of marketing authorities and certain other statutory bodies

583. This section, and the following two sections, contain special rules for the treatment of the statutory reserve funds which must in certain circumstances be maintained by certain statutory authorities. It is based on section 509 of ICTA.
584. This section allows a qualifying statutory body a deduction in calculating its trade profits for any amount of its trade surplus that it is required to pay into a reserve fund. Any amount withdrawn from the fund is taxed as a trade receipt unless it is a repayment of the levy or paid to the producers or a Government Department.

585. *Subsections (1) and (2)* identify the statutory bodies to which this section applies.
586. *Subsection (5)* provides definitions for the purposes of this section.
587. The roll of statutes which confer functions that are relevant to these sections and the population of statutory authorities to which these sections might apply has declined in recent years. The Cereals Marketing Act 1965 and the Agriculture Act 1967 still confer functions that are relevant for the purposes of these sections. See, in particular, the powers to make schemes under section 16 of the 1965 Act and section 13 of the 1967 Act.

Section 154: Conditions to be met by reserve fund

588. This section contains conditions which must be met by the reserve fund if the relief under section 153 is to be available. It is based on section 509 of ICTA.

Section 155: Interpretation of sections 153 and 154

589. This section provides definitions of constitutional authorities for the purposes of the two previous sections. It is based on section 509 of ICTA, paragraph 11 of Schedule 12 to the Northern Ireland Act 1998 and section 85 of the Government of Wales Act 2006.
590. *Subsections (1) and (2)* rewrite the source legislation to reflect the effect of devolution settlements. See *Change 15* in Annex 1.
591. The Government of Wales Act 2006 created a new devolution settlement for Wales. It replaced the National Assembly for Wales constituted under the Government of Wales Act 1998 (“the old Assembly”) with a new National Assembly for Wales. Schedule 11 to the 2006 Act provides for functions conferred on the old Assembly (with certain exceptions that are not relevant here) to be transferred to the Welsh Ministers. It is in theory possible that schemes such as are mentioned in section 509(1) of ICTA could have been approved by the old Assembly before its functions were transferred to the Welsh Ministers. A paragraph in Schedule 2, the Schedule of transitionals and savings (reserves of marketing authorities etc), affecting section 153(5), covers this possibility.
592. Subsection (1) refers to “a Minister within the meaning of the Northern Ireland Act 1988”. This rewrites the reference in section 509(3) of ICTA to a “head of department” read with paragraph 11(1) of Schedule 12 to the Northern Ireland Act 1998.

Chapter 10: Trade profits: changes in trading stock

Overview

593. This Chapter rewrites the rules in Part 2 of Schedule 15 to FA 2008. The rules relate to the corporation tax consequences of taking stock from, or introducing stock to, a trade.

Section 156: Meaning of “trading stock”

594. This section provides a definition for the purposes of this Chapter. It is based on paragraph 5 of Schedule 15 to FA 2008. The corresponding income tax rule is in section 172A of ITTOIA (inserted by Part 1 of Schedule 15 to FA 2008).
595. *Subsection (2)* sets out the main difference between this definition and the one used in Chapter 11 of this Part.

Section 157: Trading stock appropriated by trader

596. This section sets out the rule for trading stock taken by a trader. It is based on paragraph 6 of Schedule 15 to FA 2008. The corresponding income tax rule is in section 172B of ITTOIA (inserted by Part 1 of Schedule 15 to FA 2008).

Section 158: Trading stock supplied by trader

597. This section sets out the rule for something that is supplied by a trader for use as trading stock. It is based on paragraph 7 of Schedule 15 to FA 2008. The corresponding income tax rule is in section 172C of ITTOIA (inserted by Part 1 of Schedule 15 to FA 2008).

Section 159: Disposals not made in the course of trade

598. This section sets out the rule for trading stock disposed of by a trader. It is based on paragraph 8 of Schedule 15 to FA 2008. The corresponding income tax rule is in section 172D of ITTOIA (inserted by Part 1 of Schedule 15 to FA 2008).
599. The rule in this section applies to non-trading disposals to a person other than the trader. If the stock is taken by the trader section 157 applies instead.

Section 160: Acquisitions not made in the course of trade

600. This section sets out the rule for trading stock acquired by a trader. It is based on paragraph 9 of Schedule 15 to FA 2008. The corresponding income tax rule is in section 172E of ITTOIA (inserted by Part 1 of Schedule 15 to FA 2008).
601. The rule in this section applies to non-trading acquisitions from a person other than the trader. If the stock is acquired from the trader section 158 applies instead.

Section 161: Transfer pricing rules to take precedence

602. This section gives priority to the transfer-pricing rules in Schedule 28AA to ICTA. It is based on paragraph 10 of Schedule 15 to FA 2008. The corresponding income tax rule is in section 172F of ITTOIA (inserted by Part 1 of Schedule 15 to FA 2008).
603. The rule in this section ensures that none of the exemptions in Schedule 28AA to ICTA can be overridden by an adjustment imposed by this Chapter of the Act.

Chapter 11: Trade profits: valuation of stock on cessation of trade

Overview

604. This Chapter sets out the rules for valuing stock when a company ceases to carry on a trade. The rules for valuing work in progress are not rewritten because, for tax purposes, a company cannot carry on a profession (see *Change 2* in Annex 1). If a company has incomplete services when it ceases to carry on a trade they are included in its trading stock (see section 163(2) of this Act) and valued in accordance with the rules in this Chapter.

Section 162: Valuation of trading stock on cessation

605. This section sets out two general propositions. It is based on section 100 of ICTA. The corresponding rule for income tax is in section 173 of ITTOIA. The first proposition is that a valuation has to be made. The second is that the valuation has to be made in accordance with the rules in this Chapter.
606. *Subsection (3)* is the rule for trades carried on in partnership. The general rule in ICTA is that a change in the companies carrying on a trade is treated as the cessation of the trade. But, in the case of a trade carried on in partnership, section 114(1) of ICTA provides that there is a cessation for the purpose of calculating the profits of the firm's trade only if there is a complete change in the companies carrying on the trade.

Section 163: Meaning of "trading stock"

607. This section defines trading stock. It is based on sections 100 and 101 of ICTA. The corresponding rule for income tax is in section 174 of ITTOIA.

608. The definition of trading stock applies:
- in section 151 (sound recordings);
 - in this Chapter;
 - in section 185 (adjustment on change of basis); and
 - in section 195 (post-cessation receipts).
609. Section 101(3) of ICTA is invoked by section 100(2) of that Act and is concerned with valuation of incomplete services “at the discontinuance”. So the definition in this section refers to incomplete services “at the time of the cessation”.

Section 164: Basis of valuation of trading stock

610. This section introduces the five sections that follow. It is based on section 100 of ICTA. The corresponding rule for income tax is in section 175 of ITTOIA.
611. The five sections (including section 168 which defines “connected persons”) deal with the valuation of stock that is transferred to another trader. In each case, the requirement in section 100 of ICTA that the transferee carries on a trade is relaxed to include transfers to a person carrying on a profession or vocation. The income tax rules are amended to bring the income tax and corporation tax codes into line. See *Change 39* in Annex 1.
612. *Subsection (4)* of this section deals with the case where the stock is not transferred to a person carrying on a trade, profession or vocation.

Section 165: Sale basis of valuation: sale to unconnected person

613. This section sets out the rule for the common case where the trading stock is transferred to an unconnected trader. It is based on section 100 of ICTA. The corresponding rule for income tax is in section 176 of ITTOIA.
614. The section leads directly to the use of the sale price of the stock as the basis of valuation. If the transfer is other than by sale, section 170 explains how the expressions used in this section are to be interpreted.

Section 166: Sale basis of valuation: sale to connected person

615. This section sets out the rule for the case where the stock is transferred to a connected person. It is based on section 100 of ICTA. The corresponding rule for income tax is in section 177 of ITTOIA.
616. The section preserves the concept of an arm’s length price. This will usually be the same as the open market value (see section 164(4)) but sometimes there will be a difference.
617. For example, in a capital transfer tax case, *IRC v Spencer-Nairn* [1991] STC 60, the Court of Session considered the meaning of an arm’s length price and distinguished it from open market value. This was on the basis that the seller in that case had imperfect information. A sale at arm’s length by that seller would not assume that the seller had better information; a sale in the open market would assume perfect information on both sides of the bargain.
618. Furthermore, in the case of an actual sale to a connected trader, there is no need to *assume* there is a sale. It is enough to treat the sale as made at arm’s length. This leaves open the possibility that the stock is worth something different from open market value to a person who intends to use the stock in the trade.

Section 167: Sale basis of valuation: election by connected persons

619. This section allows the seller and purchaser of stock that would otherwise be valued at arm's length under section 166 to elect to use instead the price paid for the stock. It is based on section 100 of ICTA. The corresponding rule for income tax is in section 178 of ITTOIA.
620. The election cannot be made unless the arm's length value of the stock is greater than its "acquisition value" in the hands of the seller.
621. The "acquisition value" of the stock for the company which ceases to trade is effectively book value, but the definition in *subsection (5)* is more complicated than this. In the case where the net realisable value of stock has fallen below cost in the period leading up to cessation, a new period is deemed to start just before the deemed sale. That allows the new, lower, net realisable value to be used. It may be possible to manipulate net realisable value by selling the stock at an undervalue after the accounting date. So paragraph (a) of the definition assumes that the sale is at an arm's length value.
622. The election substitutes the price paid for the arm's length value of the stock. But the price paid must be higher than the acquisition value. Otherwise, the election substitutes the acquisition value for the arm's length value.
623. This section does not specify that the election is to be made to "the inspector". But the general rules about claims and elections in Schedule 18 to FA 1998 require elections to be made in a return or, if that is not possible, to "an officer of Revenue and Customs" in accordance with Schedule 1A to TMA.

Section 168: Connected persons

624. This section provides a definition of connected persons for the stock valuation sections. It is based on section 100 of ICTA. The corresponding rule for income tax is in section 179 of ITTOIA.
625. This section is one of the exceptions to the general rule in section 1258 that a firm is not to be regarded for tax purposes as a separate entity. If a firm is connected with the seller or purchaser of its stock, section 166 (rather than section 165) applies but the firm may make an election under section 167.

Section 169: Cost to buyer of stock valued on sale basis of valuation

626. This section sets out the rule for the buyer of the stock. It is based on section 100 of ICTA. The corresponding rule for income tax is in section 180 of ITTOIA.
627. In a "sale basis" case, the value given to the trading stock of the company whose trade has ceased is also used to calculate the profits of the buyer of the stock.
628. The reference to ITTOIA caters for the case where the stock is acquired from a person liable to income tax. The valuation under that Act for income tax purposes is used as the cost to the buyer who is liable to corporation tax.

Section 170: Meaning of "sale" and related expressions

629. The stock valuation sections refer to a sale of stock. This section explains how the sections are to be interpreted if the stock is transferred other than by way of sale. It is based on section 100 of ICTA. The corresponding rule for income tax is in section 181 of ITTOIA.

Section 171: Determination of questions

630. This section treats any "question" arising under sections 164 to 167 as an appeal (to be determined by the tribunal). It is based on section 102 of ICTA. The corresponding rule for income tax is in section 186 of ITTOIA.

Chapter 12: Deductions from profits: unremittable amounts

Overview

- 631. This Chapter gives statutory effect to ESC C34. The corresponding rules for income tax are in Chapter 13 of Part 2 of ITTOIA. See part (A) of *Change 40* in Annex 1. This change reproduces Change 50 in ITTOIA and so brings the income tax and corporation tax codes back into line.
- 632. The extra-statutory concession provides relief for trade debts that cannot be remitted to the United Kingdom. It is similar in scope to section 584 of ICTA (relief for unremittable overseas income), which is rewritten as Part 18 of this Act (unremittable income). The corresponding provision for income tax is Chapter 4 of Part 8 of ITTOIA.
- 633. Section 584 of ICTA provides relief for unremittable income arising outside the United Kingdom, including unremittable trade profits. But relief under section 584 of ICTA does not extend to trade debts owed to, or paid to, the company outside the United Kingdom if the profits of the trade arise in the United Kingdom. This Chapter provides relief for such debts and payments.
- 634. ESC C34 requires the relief to be claimed. Under this Chapter the relief is allowed as a deduction without the need for a formal claim. See part (B) of *Change 40* in Annex 1.
- 635. The deduction is not mandatory if the qualifying conditions are met. A company can choose whether or not to include the deduction in its tax return. If a deduction is taken the recovery provisions in section 175 follow automatically.

Section 172: Application of Chapter

- 636. This section defines the basic concepts. It is based on ESC C34. The corresponding rule for income tax is in section 188 of ITTOIA.
- 637. The relief applies both to amounts owed to the company and to amounts that have been paid to the company. Relief is allowed if some, or all, of those amounts cannot be remitted to the United Kingdom because of foreign exchange restrictions. The different definitions of “unremittable” in *subsections (2) and (3)* reflect the differences between an amount that has been paid and an amount owed.
- 638. The relief is available to any company, including a company carrying on a financial trade.
- 639. *Subsection (4)* provides a definition of “foreign exchange restrictions”. Local foreign exchange restrictions are not defined in the extra-statutory concession but are clearly a key concept in the operation of the concession. This subsection introduces a definition based on section 584(1)(a) of ICTA. That subsection is rewritten as section 1274 (unremittable income: introduction) in Part 18. The corresponding provision for income tax is section 841(3) of ITTOIA. By basing the definition on section 584 of ICTA this Act brings the two reliefs into line.
- 640. This section and the rewrite of section 584 of ICTA in Part 18 of this Act clarify the scope of section 584 of ICTA and the extra-statutory concession in two ways.
- 641. First, sections 584(1)(a) of ICTA refers to “the impossibility of obtaining foreign currency in that territory”. It could be argued that this condition is not met if it is possible to obtain foreign currency in the overseas territory regardless of whether that currency may be transferred to the United Kingdom. Section 1274 of Part 18 of this Act makes clear that it must not be possible to obtain foreign currency that could be transferred to the United Kingdom.
- 642. Second, section 1274 of Part 18 of this Act makes clear that the reference to foreign currency in section 584(1)(a) of ICTA does not include currency of the overseas country

or territory. In relation to sterling the currency of the overseas country or territory clearly is foreign but in this context “foreign” means foreign to the local territory.

643. *Subsection (5)* deals with the interaction with the loan relationship rules. Most of the amounts in this Chapter will be within the scope of Chapter 2 of Part 4 of FA 1996 because they are loan relationships (rewritten in Parts 5 and 6 of this Act). In particular section 100 of FA 1996 treats trade debts as loan relationships (see Chapter 2 of Part 6).
644. Section 80(5) of FA 1996 is a wide-ranging rule which provides that only Chapter 2 of Part 4 of FA 1996 applies to any loan relationship unless there is an express provision to the contrary. Section 80(5) of FA 1996 has been rewritten as section 464(1). This rule would prevent relief being given under section 173 or recovered under section 175. *Subsection (5)* overrides section 464(1).

Section 173: Relief for unremittable amounts

645. This section sets out how the relief is given. It is based on ESC C34. The corresponding rule for income tax is in section 189 of ITTOIA.
646. The section has more detail than the extra-statutory concession about the mechanics of the relief. This is necessary to give the certainty required for corporation tax self assessment. Relief can be given only against the profits of the trade that include the unremittable amount. It cannot be used to create or increase a loss. But any excess relief is not lost. It is carried forward and set against future profits of the trade.

Section 174: Restrictions on relief

647. This section describes the various circumstances in which relief is not allowed. It is based on ESC C34. The corresponding rule for income tax is in section 190 of ITTOIA.
648. *Subsection (1)* denies a deduction if the funds are applied outside the United Kingdom.
649. *Subsection (2)* denies a deduction if the company has received an insurance recovery in respect of the debt. This differs from the approach in the extra-statutory concession. Paragraph 4 of the concession denies relief if any part of the debt is insured. This Act denies, or recovers, relief only if an insurance recovery is received. See part (C) of *Change 40* in Annex 1.
650. *Subsection (3)* denies a deduction if the company can make a claim under section 1275 (claim for relief for unremittable income) in Part 18 that the income is unremittable. The corresponding provision for income tax is section 842 of ITTOIA.
651. This restriction will apply only if the profits of the trade that include the unremittable amounts arise outside the United Kingdom, for example, because the profits arise in an overseas branch.

Section 175: Withdrawal of relief

652. This section sets out the circumstances in which relief is withdrawn and the machinery by which it is withdrawn. It is based on ESC C34. The corresponding rule for income tax is in section 191 of ITTOIA.
653. *Subsection (2)* lists the events that trigger a withdrawal of the relief. Paragraphs (a) and (e) deal with the straightforward cases in which the amount, or part of it, ceases to be unremittable or is exchanged for an amount that can be remitted. Paragraphs (c), (d), and (f) deal with the events listed in section 174 that would have prevented relief being given if they had occurred before the deduction was allowed.
654. Paragraph (f) deals with the case of insurance recoveries. It differs from the approach in the extra-statutory concession, which denies any relief if the debt is insured. This Chapter denies or recovers relief only if an insurance recovery is received (see the commentary on section 174). See part (C) of *Change 40* in Annex 1.

655. This follows the approach in section 584 of ICTA when a payment is received from the Exports Credit Guarantee Department. The withdrawal of relief under section 584 of ICTA is rewritten as section 1276 (unremittable income: withdrawal of relief) in Part 18. The corresponding provision for income tax is section 843 of ITTOIA.
656. *Subsection (3)* sets out the way the relief is recovered. The amount identified in subsection (2) is treated as a trade receipt for the accounting period in which the event occurs. It is possible that more than one event will apply to the same amount. Subsection (3)(b) ensures the relief is withdrawn only once.
657. *Subsection (4)* applies if the amount of the insurance recovery is less than the amount that is unremittable. In that case the amount of the recovery is limited to the amount of the insurance recovery.

Chapter 13: Disposal and acquisition of know-how

Overview

658. This Chapter sets out the rules for calculating trade profits if a trading company receives a payment for know-how. Payments to non-traders are dealt with by the rules in Chapter 2 of Part 9 of this Act.
659. [Part 8](#) of this Act sets out rules for the taxation of gains and losses on companies' intangible fixed assets. Those rules take priority over any other tax rules (see section 906). So the Part 8 rules generally apply instead of the rules in this Chapter. But Chapter 16 of Part 8 ensures that the new rules apply only to assets created or acquired on or after 1 April 2002.
660. The Chapter refers to the “disposal” of know-how. As Walton J pointed out in *John and E Sturges Ltd v Hessel* (1975), 51 TC 183 ChD⁶ (on page 206):
- the mere imparting of “know-how” cannot be equated with the disposal of a capital asset. Just like the schoolmaster’s knowledge, it remains the property of the person imparting it as well after as before another is told.
661. This Act retains “disposal” because “disclosure” gives rise to difficulties in identifying the person to whom the disclosure is made (who may not be the person who buys the know-how).

Section 176: Meaning of “know-how” etc

662. This section sets out the meaning of know-how and explains other concepts used in the Chapter. It is based on sections 531 and 533 of ICTA and section 572 of CAA. The corresponding rule for income tax is in section 192 of ITTOIA.
663. The definition of “mineral deposits” in *subsection (2)* is restored to what it was before the enactment of CAA. See *Change 41* in Annex 1.
664. *Subsections (5)* and *(6)* extend the meaning of “sale” to include an exchange. This rule is based on section 572 of CAA, which applies to section 531 of ICTA in accordance with section 532 of ICTA.

Section 177: Disposal of know-how if trade continues to be carried on

665. This section sets out a general rule for the treatment of payments received for the disposal of know-how. It is based on section 531 of ICTA. The corresponding rule for income tax is in section 193 of ITTOIA.

6 [1975] STC 127

666. *Subsections (3) to (6)* deal with the case where know-how is disposed of with other assets. The rules are based on sections 562 and 563 of CAA, which apply to section 531 of ICTA in accordance with section 532 of ICTA.

Section 178: Disposal of know-how as part of disposal of all or part of a trade

667. This section sets out the main exception to the general rule in section 177. It is based on section 531 of ICTA. The corresponding rule for income tax is in section 194 of ITTOIA.
668. *Subsection (2)* provides that a payment for know-how as part of the disposal of a trade is generally treated as a capital receipt for goodwill. This rule applies only if the person making the disposal is liable to corporation tax. If that person is liable to income tax the rule in section 194 of ITTOIA applies, with the same result.
669. *Subsection (5)* allows the parties to the transaction to elect for the payment not to be treated as one for goodwill. The effect of an election for the purchaser is that the payment may qualify for capital allowances under Part 7 of CAA. Or, exceptionally, the purchaser may be able to treat the payment as a trading expense. As such an election may affect both parties to the transaction the election has to be made by both.
670. The question whether the election is made under this section or under section 194(5) of ITTOIA is decided by reference to the position of the person disposing of the know-how. If that person is liable to corporation tax this section applies; if the person is liable to income tax, ITTOIA applies.
671. This section does not specify that the election is to be made to “the inspector”. But the general rules about claims and elections in Schedule 18 to FA 1998 require elections to be made in a return or, if that is not possible, to “an officer of Revenue and Customs” in accordance with Schedule 1A to TMA.
672. *Subsection (6)* gives the time limit for the election. Most elections in this Act have to be made “not later than two years after the end of the accounting period ...”. But in this case one of the persons making the election may be chargeable to income tax. So the time limit for an election is based on the date of the disposal.
673. *Subsection (7)* deals with a disposal by an income tax payer to a corporation tax payer. An election under section 194(5) of ITTOIA is treated as an election under this section. The corresponding rule for a disposal by a corporation payer to an income tax payer is in section 194(7) of ITTOIA.

Section 179: Seller controlled by buyer etc

674. This section ensures that if the seller and buyer are under common control:
- the general rule in section 177 does not apply; and
 - the parties to the transaction may not elect for the payment for know-how not to be treated as a capital payment for goodwill.
675. The section is based on section 531 of ICTA. The corresponding rule for income tax is in section 195 of ITTOIA.
676. For the purposes of this section, “control” is defined in section 840 of ICTA (as applied by section 1316 of this Act). The ICTA definition of “control” is identical in effect to that in section 574 of CAA. But, as the relevance of “control” in this Act goes wider than this Chapter, the ICTA definition is used here.
677. This section is one of the exceptions to the general rule in section 1258 of this Act that a firm is not to be regarded for tax purposes as a separate entity. If a firm is connected with the seller or purchaser of its know-how the payment for know-how is treated as one for goodwill.

Chapter 14: Adjustment on change of basis

Overview

678. This Chapter sets out the rules for dealing with two sorts of changes in the way profits of a trade are calculated.
679. The first sort of change is in the way the accounts are drawn up. The rule is that profits must be calculated on the basis of accounts drawn up in accordance with generally accepted accounting practice (see section 50 of FA 2004 and section 46 of this Act).
680. If there is a change in the basis on which accounts are drawn up, some receipts and expenses may fall out of account for tax purposes. This sort of change was dealt with originally in the rules that became section 104(4) to (7) of ICTA. Those rules were replaced by the rules in section 44 of, and Schedule 6 to, FA 1998. The 1998 rules were replaced by section 64 of, and Schedule 22 to, FA 2002.
681. The second sort of change is in the way tax adjustments are made. These are the adjustments “required or authorised by law in calculating profits for tax purposes” (section 46). This sort of change was dealt with for the first time by the 2002 legislation.
682. [Section 1267](#) of this Act applies the rules to trades carried on in partnership.
683. The corresponding rules for income tax are in Chapter 17 of Part 2 of ITTOIA. The title of that Chapter is “adjustment income” because there is a charge on such income in section 228(2) of ITTOIA. For corporation tax a positive adjustment is treated as a trade receipt. So the title of this Chapter is more general.

Section 180: Application of Chapter

684. This section sets out the circumstances in which an adjustment may arise. It is based on section 64 of FA 2002. The corresponding rule for income tax is in section 227 of ITTOIA.
685. Section 64 of FA 2002 refers to a change of the basis on which profits are calculated. This might mean *any* change of basis. But paragraph 3(2) of Schedule 22 to FA 2002 makes clear that it does not include a change which occurs on a change of ownership of a trade.
686. The trading income rules in this Part are generally “company-based”. So this section applies when *a company* changes the basis. That company must be the same before and after the change of basis. So this section reproduces the effect of paragraph 3(2) of Schedule 22 to FA 2002.
687. An adjustment has to be made if:
- the “old basis” accorded with the law *or* practice at the time; and
 - the “new basis” accords with the current law *and* practice.
688. The difference in wording is to cater for a case in which a decision of the Courts makes it clear that a previously accepted view of the law was wrong. In that case, the old basis accorded with the practice but not the law. The 1998 rules did not cater for this. But the 2002 rules (and the rules in this Chapter) do.
689. The section refers to “a trade”. So the rules apply to trades carried on wholly outside the United Kingdom as they apply to trades carried on at least partly in the United Kingdom.

Section 181: Giving effect to positive and negative adjustments

690. This section sets out the treatment of the adjustment. It is based on paragraphs 4 and 5 of Schedule 22 to FA 2002. The corresponding rule for income tax is in section 228 of ITTOIA.
691. If the adjustment is positive it is treated as a trade receipt; if the adjustment is negative it is treated as a trade expense.
692. In both cases the treatment is the same whether the trade is taxable under Case I or Case V of Schedule D in the source legislation. The adjustment is treated as arising on the first day of the first period of account for which the new basis is adopted. This contrasts with the income tax treatment which is that the adjustment arises on the last day of the period (see sections 232 and 233 of ITTOIA).

Section 182: Calculation of the adjustment

693. This section contains the main rules for calculating the adjustment. It is based on paragraph 2 of Schedule 22 to FA 2002. The corresponding rule for income tax is in section 231 of ITTOIA. The section presents the rules as a method statement.
694. In item 3 of each of Step 1 and Step 2 there is a reference to work in progress as an alternative to trading stock. This follows the source legislation and is needed because the extended meaning of “trading stock” in section 163 of this Act does not apply outside Chapter 11.

Section 183: No adjustment for certain expenses previously brought into account

695. This section deals with the case where the old basis of calculation allowed a tax deduction but the new basis requires the deduction to be spread over several periods. It is based on paragraph 6 of Schedule 22 to FA 2002. The corresponding rule for income tax is in section 234 of ITTOIA.
696. In the absence of this section there would be a positive adjustment within item 2 of Step 1 of the calculation of the adjustment in section 182. That would produce the right result overall but the rule would take effect too early. Instead, no adjustment is calculated but no deduction is allowed in future for expenses that have already been taken into account.

Section 184: Cases where adjustment not required until assets realised or written off

697. This section is a timing rule for an adjustment which results from any of the amounts in subsection (2). It is based on paragraph 7 of Schedule 22 to FA 2002. The corresponding rule for income tax is in section 235 of ITTOIA.
698. The amounts in subsection (2) are:
- closing trading stock;
 - opening trading stock; and
 - depreciation.
699. The general timing rule is that any adjustment is made at the start of the first period of account on the new basis (see section 181(2) and (3)). But any adjustment for stock or depreciation is made when the asset is realised or written off.

Section 185: Change from realisation basis to mark to market

700. This section is concerned with a change from the realisation basis to “mark to market” accounting. It is based on paragraph 8 of Schedule 22 to FA 2002. The corresponding rule for income tax is in section 236 of ITTOIA.

701. “Mark to market” is a basis of accounting used by traders in financial assets. Instead of carrying the assets in the books at cost, financial traders draw up accounts to show the assets at fair value at the accounting date. But for tax purposes the realisation basis may have been used.
702. In the first period in which mark to market is adopted for tax purposes, the opening stock may be valued at a higher (market) value than the closing stock of the previous period. Or a financial asset may have been carried in the accounts at cost but appear as a deduction in a later period at fair value. In either case, there is an adjustment within section 182.
703. As in section 184, the adjustment is postponed until the asset is realised.

Section 186: Election for spreading if section 185 applies

704. This section provides for an election to be made if there is a receipt (following a change to mark to market) under section 185. It is based on paragraph 9 of Schedule 22 to FA 2002. The corresponding rule for income tax is in section 237 of ITTOIA.
705. The election is to spread the adjustment receipt over six periods of account beginning with the first one in which the new basis is adopted. As the receipt is postponed under section 185 until the asset is realised, this first period is not necessarily the one in which the charge would be made without the election.
706. “Period of account” is defined in section 832(1) of ICTA.

Section 187: Transfer of insurance business

707. This section further postpones the charge on an adjustment in the case of assets to which section 185 or 186 applies. It is based on paragraph 10 of Schedule 22 to FA 2002. It is the only section in this Chapter that has no corresponding section in Chapter 17 of Part 2 of ITTOIA.
708. The section applies only to insurance companies. If the asset of an insurance company is transferred to another insurance company in accordance with a relevant transfer scheme, it is not treated as “realised” for the purpose of sections 185 and 186 until it is realised by the transferee company.

Chapter 15: Post-cessation receipts

Overview

709. This Chapter charges receipts which are derived from a trade but are not received until after the trade has ceased and have not been brought into the calculation of profits.
710. The Chapter rewrites sections 103 and 104 of ICTA without distinguishing between trade profits calculated on an earnings basis and trade profits calculated on a “conventional basis” (see section 110(4) of ICTA). One consequence of this approach is that there is no need to rewrite section 104(3) or section 110(3) to (5) of ICTA.

Section 188: Charge to tax on post-cessation receipts

711. This section applies the corporation tax charge on income to post-cessation receipts. It is based on sections 103 and 104 of ICTA. This application of the charge is separate from that on the profits of a trade (see section 35 of this Act). The corresponding rule for income tax is in section 242 of ITTOIA.

Section 189: Extent of charge to tax

712. This section sets out the charge to tax. It is based on sections 103 and 104 of ICTA, which create a charge under Schedule D Case VI on post-cessation receipts. This Act

deals with the income where it logically belongs. In this case the income is trading income. The corresponding rule for income tax is in section 243 of ITTOIA.

713. The charge in the source legislation under Schedule D Case VI has consequences for loss relief. This Act preserves the position for loss relief by amending section 396 of ICTA and listing this Chapter in section 834A of ICTA (see Schedule 1 to this Act).
714. *Subsection (3)* deals with a company which has become non-UK resident after the trade has ceased. A trade carried on at least partly in the United Kingdom may include income that arises abroad. When the company was resident in the United Kingdom all the profits of the trade would have been within the charge under Part 2 of this Act (see section 5). This subsection removes the charge on a non-UK resident company if the receipt arises abroad.

Section 190: Basic meaning of “post-cessation receipt”

715. This section sets out the basic meaning of “post-cessation receipt”. It is based on sections 103, 104 and 110 of ICTA. The corresponding rule for income tax is in section 246 of ITTOIA.
716. *Subsection (2)* deals with the unusual case of a company receiving a “sum” which arises from the carrying on of a trade by a person liable to income tax.
717. Paragraph (a) deals with a non-UK resident company liable to income tax. If a company becomes liable to corporation tax it is treated as ceasing to carry on the income tax trade. A post-cessation receipt from that trade may be charged to corporation tax.
718. Paragraph (b) applies where the trade was carried on in partnership. If a partner leaves a firm and a company receives a sum arising from the carrying on of the trade by that partner, the sum may be a post-cessation receipt.

Section 191: Other rules about what counts as post-cessation receipts

719. This section is new. It contains signposts to:
- the seven sections in this Act that treat other sums as post-cessation receipts; and
 - the two sections in this Act that exclude certain sums from the charge on post-cessation receipts.
720. The corresponding rule for income tax is in section 247 of ITTOIA.

Section 192: Debts paid after cessation

721. This section sets out what happens when a trader is allowed a deduction for a bad or doubtful debt owed to the trade but then recovers the debt after the trade has ceased. It is based on section 103 of ICTA. The corresponding rule for income tax is in section 248 of ITTOIA.
722. If a deduction for the debt has been given during the course of the trade section 103(5) of ICTA makes it clear that the recovery has not been “brought into account” in calculating the trade profits. The result is that the recovery is within the charge in section 103 of ICTA.
723. *Subsections (1)* and *(2)* treat the recovery of the debt as a post-cessation receipt. The references to section 35 of ITTOIA and income tax cater for the possibility that a deduction for a bad debt is allowed to a person liable to income tax but the debt is paid to a person liable to corporation tax.

Section 193: Debts released after cessation

724. This section sets out the rules that apply when a debt owed by the trader is released after the trade has ceased. It is based on section 103 of ICTA. The corresponding rule for income tax is in section 249 of ITTOIA.
725. *Subsection (1)* sets out the four conditions to be met if the section is to apply. It is the equivalent of section 94 of this Act which applies in the case of a continuing trade. The reference to income tax caters for the possibility that a deduction for an expense is allowed to a person liable to income tax but a person liable to corporation tax takes over the related trade debt and is released from it.

Section 194: Transfer of rights if transferee does not carry on trade

726. This section deals with the position of the transferor if the right to a post-cessation receipt is transferred for value to a non-trading transferee. It is based on section 106 of ICTA. The corresponding rule for income tax is in section 251 of ITTOIA.
727. The transferor is charged to tax on the amount received for the transfer if the transfer is at arm's length. Otherwise the transferor is charged to tax on the arm's length value of the transfer. There is no later charge to tax on the transferee when the post-cessation receipt is received.
728. **Section 95** of this Act sets out the position if the transfer is to a trading transferee.

Section 195: Transfer of trading stock

729. This section excludes from the charge on post-cessation receipts sums arising from the transfer of stock. It is based on sections 103, 104 and 110 of ICTA. The corresponding rule for income tax is in section 252 of ITTOIA.
730. *Subsection (1)* makes explicit the general rule that there is no tax charge on a post-cessation receipt arising from trading stock.
731. The policy is that stock should be valued at cessation in accordance with the rules in Chapter 11 of this Part. Once that has been done there is no need to charge tax on any sums arising from the disposal or realisation of stock.

Section 196: Allowable deductions

732. This section is the first of two that set out the rules for allowing deductions from sums charged as post-cessation receipts. It is based on section 105 of ICTA. The corresponding rule for income tax is in section 254 of ITTOIA.
733. *Subsection (3)* ensures that a deduction is not allowed for any expenses for which relief has already been allowed (for income tax) under section 96 of ITA or under any other provision.

Section 197: Further rules about allowable deductions

734. This section is the second of two that set out the rules for allowing deductions from sums charged as post-cessation receipts. It is based on section 105 of ICTA. The corresponding rule for income tax is in section 255 of ITTOIA.
735. *Subsection (2)* ensures that any loss unused at the date of cessation is set off against post-cessation receipts in the same order as it would have been set off against profits under section 393 of ICTA, that is, against an earlier accounting period before a later accounting period.
736. The references to capital allowances in section 105(1)(b) and (3) of ICTA are no longer needed because any capital allowance is allowed as a trading expense.

Section 198: Election to carry back

737. This section allows a company to elect to have a post-cessation receipt taxed as though it had been received in the accounting period in which the company ceased to carry on the trade. It is based on section 108 of ICTA, although that section was repealed by ITTOIA. The corresponding rule for income tax is in section 257 of ITTOIA.
738. See *Change 42* in Annex 1.
739. *Subsection (1)* requires that the post-cessation receipt is received (broadly) within six years after the company ceases to carry on the trade. This corresponds to the limit in section 108 of ICTA (which was expressed in terms of years of assessment).
740. *Subsection (3)* gives a two year time limit for the election. This was the original time limit in section 108 of ICTA before it was amended for (income tax) Self Assessment.

Section 199: Deductions already made are not displaced

741. This section is a rule about losses allowed against a post-cessation receipts carried back to the period of cessation under section 198. It is new.
742. The rule in this section is broadly the same as the income tax rule in paragraph 5(5) of Schedule 1B to TMA. If relief has already been given under section 196, for a period later than the period of cessation, this section makes clear that the relief is not to be re-calculated as a result of the election under section 198.
743. The section refers only to a “loss” for which a deduction has already been made. Any “expense or debit” already allowed under section 196 would in any event not be available for the accounting period in which the cessation occurred.
744. *Subsection (3)* makes clear that the rule about “displacing” a deduction for a loss does not apply to a deduction that has been made from the post-cessation receipt that is to be carried back.
745. See *Change 42* in Annex 1.

Section 200: Election given effect in accounting period in which receipt is received

746. This section sets out the procedure for dealing with an election under section 198. It is new.
747. The procedure for giving the relief is broadly the same as that for income tax. This is an election to which paragraph 58 of Schedule 18 to FA 1998 applies. This section makes clear that the relief is in terms of tax and corresponds to the income tax rule in paragraph 5 of Schedule 1B to TMA.
748. See *Change 42* in Annex 1.

Chapter 16: Priority rules

Section 201: Provisions which must be given priority over this Part

749. This section sets out the priority rules that apply when a receipt or other credit item might otherwise fall within more than one head of charge. It is based on section 18 of ICTA. The corresponding rules for income tax are in section 4 of ITTOIA.
750. *Subsection (2)* deals with potential overlap with ITEPA. It is based on section 18 of ICTA. In the source legislation Schedule D is the residual Schedule. So the charge in ITEPA on employment income, and other income formerly within Schedule E, has priority over the charge on profits of a trade (Schedule D in the source legislation).