

## **Part 1: Special rules about charitable companies etc**

### **Overview**

1. This Part contains rules specific to charitable companies. It follows closely the structure of Part 10 of ITA 2007, and as with those provisions it is based mainly on sections 505 to 506C of, and Schedule 20 to, ICTA, section 25 of FA 1990 and section 46 of FA 2000.

2. The draft legislation contains a number of references to provisions in ICTA 1988 or subsequent finance acts that we propose to rewrite in the corporation tax bills. The ICTA references have been retained for this draft for ease of construction except where there is reasonable certainty about the location of new legislation in the first corporation tax bill, in which case the expected reference is used.

### **Clause 1: Overview of Part**

3. This clause sets out the scope of the Part and provides signposts to rules about:

- the tax treatment of gifts made to charitable companies;
- exemptions from charges to corporation tax; and
- the restrictions on when exemptions can apply.

It is new.

4. The exemptions are given effect by saying that an amount “is not taken into account in calculating total profits”. This follows the approach taken for income tax in Part 10 of ITA 2007.

### **Clause 2: Meaning of “charitable company”**

5. This clause defines “charitable company” for the purposes of this Part. It is based on section 506(1) of ICTA.

6. The effect of splitting the source legislation between income tax and corporation tax is that the income tax rules apply to charities constituted in the form of charitable trusts while the corporation tax rules apply to charitable companies.

7. The definition of charitable company therefore includes charities constituted as unincorporated associations and charities incorporated by Royal Charter in line with the definition of “company” in section 832 of ICTA.

8. A definition of a “charity” will be included in the general definitions section in this Bill. The definition for income tax is in section 989 of ITA 2007.

### **Clause 3: Gifts entitling donor to gift aid relief: income tax treated as paid**

9. This clause deals with the income tax treated as paid when a charitable company receives gift aid donations from individuals. It is based on section 25(10) and (12) of FA 1990.

10. The company is treated as receiving a grossed up amount, and the tax treated as deducted from the gift is treated as paid by the charitable company.

**Clause 4: Gifts entitling donor to gift aid relief: corporation tax liability and exemption**

11. This clause sets out the charge to tax that can arise on gift aid payments received by a charitable company. It is based on section 505(1) of ICTA and section 25(10) and (12) of FA 1990.

12. The clause imposes a freestanding charge to corporation tax on gift aid payments, unlike the source legislation which operates by treating the gifts as annual payments. It also sets out the exemption which will normally apply if the charitable company uses the gifts for charitable purposes.

**Clause 5: Gifts of money from companies: corporation tax liability and exemption**

13. This clause sets out the charge to tax that can arise on gifts received by a charitable company from other companies. It is based on section 339(4) of ICTA.

14. As with clause 4, this clause imposes a freestanding charge to corporation tax on gifts.

**Clause 6: Payments from other charities: corporation tax liability and exemption**

15. This clause prevents charities avoiding the operation of the restrictions on exemptions by routeing non-charitable expenditure through other charities. It is based on section 505(1) and (2) of ICTA.

16. The clause operates by imposing a charge to tax on certain payments made by a charity to a charitable company. It also sets out the exemption that will normally apply if the charitable company uses the payments for charitable purposes.

17. *Subsection (6)* makes it clear that section 494 ITA 2007, which deals with the grossing up of discretionary payments from trusts, takes precedence over this clause where applicable.

**Clause 7: Exemption for profits etc of charitable trades**

18. This clause sets out the exemption for trading profits of charitable companies. It is based on section 505(1) of ICTA.

19. The exemption applies only if the trade is a charitable trade. This is defined in clause 8.

20. There is a difference between this clause and the corresponding provision in ITA 2007. Adjustment income (arising, for example, on a change of accounting basis) is an integral part of the trading profits of a company. This follows from section 64 of and Schedule 22 to FA 2002, to be rewritten in Bill 5. As a result charitable companies have been entitled to the exemption on adjustment income on the same basis as their trading profits. The consequence is that, in contrast to ITA 2007, there is

no proposed change to the legislation to establish an exemption for adjustment income.

21. This clause does make it clear that, in the same way as the income tax legislation, post-cessation receipts (arising from what was a charitable trade) are exempt, in line with practice. Post-cessation receipt is defined by reference to Chapter 14 of Part 3 in Bill 5. See *Change 627* in Annex 1. This change also affects clauses 8, 14, 20, 21 and 24.

**Q1. We welcome comments on whether the legislation should treat post-cessation receipts arising from a primary purpose trade as exempt**

22. Exemptions for small-scale trades are dealt with separately in clause 9.

**Clause 8: Meaning of “charitable trade”**

23. This clause defines “charitable trade” for the purposes of clause 7. It is based on section 505(1) and (1B) of ICTA.

24. The source legislation in section 505(1)(e) of ICTA refers to the trade being carried on “in the United Kingdom or elsewhere”, and section 505(1)(e)(i) refers to it being exercised in the “actual” carrying out of a primary purpose. The words in inverted commas have been omitted as they add nothing.

25. The clause differs slightly from its income tax counterpart in section 525 of ITA 2007. For income tax the conditions must be met throughout the *basis period* for the relevant tax year to reflect the fact that the two time periods are not usually the same, and it clearly makes sense to test the condition by reference to the time period in which the activity was being carried on. This is not necessary for corporation tax as the accounting period is both the basis period and the chargeable period.

26. *Subsection (4)*, about making apportionments where different parts of a trade are treated as separate trades, makes specific mention of post-cessation receipts. See *Change 627* in Annex 1 and the commentary on clause 7.

27. Any apportionments must be “just” as well as “reasonable”. Only the latter term appeared in the source legislation. See *Change 604* in Annex 1.

**Q2. We welcome comments on the proposal to make it explicit that apportionments should be “just” as well as “reasonable”**

**Clause 9: Exemption for profits of small-scale trades**

28. This clause provides an exemption for trading income, related adjustment income and post-cessation receipts in circumstances where the amount of income to be exempted under this clause and the next is small, and provided the income is applied to the purposes of the charitable company. It is based on section 46 of FA 2000.

29. The exemption provided by this clause applies only if the income is not otherwise exempt. So profits from primary purpose trading (including related adjustment income and post-cessation receipts) are exempt under clause 7, whereas profits from a non-primary purpose trading activity (including related adjustment income and post-cessation receipts) may be exempt under this clause.

30. *Change 627* is not necessary here as post-cessation receipts from a “small trade” were already exempt because of the existing exemption in section 46 FA 2000 for income chargeable under Case VI of Schedule D.

31. The condition about the limit on the level of income for this exemption to apply is in clause 11.

**Clause 10: Exemption from charges under [Case VI of Schedule D]**

32. This clause provides an exemption for certain miscellaneous income and gains arising to a charitable company and applied to the purposes of the charitable company. It is based on section 46 of FA 2000.

33. The income tax legislation has replaced the charge to tax under Case VI Schedule D with freestanding charges to tax. These are brought together in section 1016 of ITA 2007. It is likely that the same approach will be followed for corporation tax, but as this is some way in the future the reference to Case VI of Schedule D has been retained in this draft for ease of interpretation and reference.

34. *Subsection (2)* specifies particular types of income and gains which cannot benefit from the exemption.

35. The exemption provided by this clause applies only if the income or gains are not otherwise exempt. So, for example, post-cessation primary purpose trading receipts are exempt under clause 7 and post-cessation trading receipts from a non-primary purpose trading activity are exempt under clause 9.

36. The scope of this provision has therefore narrowed slightly in that post-cessation receipts from a primary purpose trade can now be exempt under clause 7 whereas previously they could only be statutorily exempt under section 46 FA 2000 - see *Change 627* in Annex 1 and the commentary on clause 7.

37. The condition about the level of the income and gains is in clause 11.

**Clause 11: Condition as to trading and miscellaneous incoming resources**

38. This clause sets out the condition about the limit on the level of trading and miscellaneous incoming resources that has to be met if the exemptions in clauses 8 and 9 are to apply. It is based on section 46 of FA 2000.

39. The condition operates by reference to the incoming resources associated with the trading activity and miscellaneous transactions whose profits are not exempt under the other exemptions in this Part. The expression “incoming resources” is used instead of “gross income” because this accounting term is a more direct and accessible way of

capturing the meaning of the income labelled “gross income” in the source legislation. There are also related points of clarification. See *Change 628* in Annex 1.

**Q3. We welcome comments on whether the legislation should reflect accounting terms**

40. Trading incoming resources and miscellaneous incoming resources are defined in *subsections (2) and (4)* respectively. The requisite limit is given in *subsection (6)*.

41. *Subsection (7)* provides a rule to deal with situations where an accounting period is shorter than twelve months. The formula adopted has been used widely in the rewritten legislation. In this case it makes a small change in favour of the taxpayer – see *Change 652* in Annex 1.

**Q4. We welcome comments on the use of an apportionment formula that is always based on 365 days, irrespective of the length of the calendar year.**

**Clause 12: Exemption for profits from fund-raising events**

42. This clause gives statutory effect to ESC C4 as it applies to charitable companies provided the profits in question are applied to the purposes of the charitable company. It is new.

43. The fund-raising event has to fall within the exemption from VAT under Group 12 of Schedule 9 to the Value Added Tax Act 1994. That Schedule provides an exemption from VAT for the supply by a charity of goods and services in connection with an event that is organised primarily to raise money for itself or other charities. The Schedule defines “event” and places certain limits on the number of events that a charity can hold in the same location in any given year.

44. See *Change 629* in Annex 1. This change also affects clauses 20, 21 and 24.

**Q5. We welcome comments on whether ESC C4 should be reflected in the legislation**

**Clause 13: Exemption for profits from lotteries**

45. This clause provides an exemption for lottery income provided the income is applied to the purposes of the charitable company. It is based on section 505(1) of ICTA.

**Clause 14: Exemption for property income etc**

46. This clause sets out the exemption from corporation tax for property income and certain trading income arising from land, provided the income is applied to charitable purposes. It is based on section 505(1) of ICTA.

47. The exemption applies where the income is chargeable to tax under either Part 3 or Part 4 of Bill 5. *Subsection (1)* deals with income chargeable under Part 3 of Bill 5, rather than Part 4.

48. Income chargeable to tax under Part 3 of Bill 5 means profits of a trade (including adjustment income) and post-cessation receipts. This means that the section encompasses an exemption for post-cessation receipts, in line with practice, without need for explicit reference. See *Change 627* in Annex 1 and the commentary on clause 7.

**Q6. We welcome comments on whether the legislation should treat as exempt post-cessation receipts that arise from trading income derived from land.**

49. There is no requirement for the trade to be exercised in the course of carrying on a primary purpose of the charitable company. Instead, the exemption applies where the income derives from land vested for charitable purposes. But if some of the land is vested for charitable purposes and some vested or held for other purposes (for example, as an investment to generate income for non-charitable purposes) it is necessary to allocate the profits of the single property business between the two parts. This reflects the approach of the exemption in the source legislation that looks to particular interests in land, rather than to one overall property business.

50. This makes the effect of the source legislation in section 505(1)(a) of ICTA explicit. There is no other income arising from land and chargeable to tax under Part 3 of Bill 5 which is exempt under that provision.

51. The exemption in *subsection (2)* encompasses the whole of Part 4 of Bill 5, which means that the clause also provides an exemption from corporation tax for post-cessation receipts of UK property businesses, provided the income is applied to charitable purposes, but without the need for explicit reference. See *Change 627* in Annex 1 and the commentary on clause 7.

**Q7. We welcome comments on whether the legislation should treat as exempt post-cessation receipts that arise from a property business.**

52. As with trading profits charged under Part 3 of Bill 5, adjustment income already forms part of the computation of profits – section 21B ICTA includes the relevant source legislation (section 62 of and Schedule 22 to FA 2002) among the legislation relevant to the computation of profits of a business chargeable under Schedule A.

53. *Subsection (3)* provides an exemption from corporation tax for distributions from a Real Estate Investment Trust (REIT). The source legislation in section 505(1aa) of ICTA refers to charging provisions in ITTOIA 2005. These are not necessary for corporation tax and will not be included in the rewritten legislation. The equivalent income tax exemption is in section 531(2A) of ITA 2007.

**Clause 15: Exemption for investment income and non-trading profits from loan relationships**

54. This clause sets out the various categories of savings and investment income that qualify for exemption from corporation tax, provided the income is applied to charitable purposes. It is based on section 505(1) of ICTA.

55. There are some differences from the equivalent income tax provision in section 532 of ITA 2007. Dividends and distributions from UK companies are exempt from corporation tax by section 208 of ICTA so there is no need for further exemption. Interest and related amounts are exempted by reference to the loan relationships regime, and the reference to a non-trading profit on a loan relationship also encompasses income from derivative contracts.

56. In *subsection (1)*, the reference to Act includes references to Acts of the Scottish Parliament and Northern Ireland legislation. See *Change 619* in Annex 1. This mirrors the approach taken in ITA 2007.

**Q8. *Change 619 reproduces Change 152 in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.***

**Clause 16: Exemption for public revenue dividends**

57. This clause provides an exemption for public revenue dividends used for the repair of certain places of worship. It is based on section 505(1) and (1A) of ICTA.

**Clause 17: Exemption for offshore income gains**

58. This clause provides an exemption for a gain on the disposal of a material interest in a non-qualifying offshore fund, provided the gain is applied to charitable purposes. It is based on section 761(6) of ICTA.

59. Details of the offshore funds legislation can be found in Chapter 5 of Part 17 of ICTA. A signpost to the new location of the exemption and a definition of “charity” will be added to section 761 of ICTA by Schedule 1.

**Clause 18: Exemption for certain miscellaneous income**

60. This clause provides an exemption for certain categories of miscellaneous income from corporation tax, provided the income is applied to charitable purposes. It is based on section 505(1) and (1AA) of ICTA.

61. In *subsection (1)(b)*, the reference to Act includes references to Acts of the Scottish Parliament and Northern Ireland legislation. See *Change 619* in Annex 1.

**Q9. *Change 619 reproduces Change 152 in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.***

62. *Subsection (3)(c)* deals with income from intangible fixed assets that does not fall within Part 9 of Bill 5 (which rewrites Schedule 29 to FA 2002) because the assets involved are “pre-FA 2002 assets”. Previously the only exemption that covered this type of income was the exemption for annual payments chargeable under Case III of Schedule D. This clause broadens the exemption to encompass income that is not covered by another exemption (for example, as a trading receipt) and is not exempted by this clause as an annual payment, in the same way as for income tax in section 536 ITA 2007. *Change 651* in Annex 1 gives more detail. This change also affects clauses 20 and 21.

**Q10. We welcome comments on the proposal to reflect in the legislation exemption for income from intangible fixed assets that is not covered by other exemptions.**

63. The term “relevant foreign distribution” covers distributions, as defined in Part VI of ICTA, made by non-UK resident companies – other than dividends. The references to ITTOIA are necessary because there is no charge to corporation tax for distributions of a UK resident company and therefore no equivalent point of reference in the corporation tax legislation.

**Clause 19: Exemption for income from estates in administration**

64. This clause provides an exemption for estate income received by a charitable company provided the income is applied to the purposes of the charitable company. It is new.

65. Estate income is income from property held by the personal representatives of the estate of a deceased person on behalf of the beneficiaries of the estate. The personal representatives are liable to income tax on the income. The exemption provided by this clause allows a charitable company to recover any income tax suffered by the personal representatives. See *Change 630* in Annex 1. This change also affects clauses 20, 21 and 24.

**Q11. We welcome comments on the proposal to reflect in legislation the practice of treating United Kingdom estate income received by charities as exempt**

**Clause 20: National Heritage Memorial Fund, Historic Buildings and Monuments Commission for England etc**

66. This clause extends certain of the exemptions to five specified bodies. It is based on section 507 of ICTA.

67. Section 507 of ICTA grants to these bodies the exemptions under section 505 that would fall to be allowed to a charitable company where the whole of the charitable company’s income is applied to charitable purposes.

68. The exemptions are listed in *subsection (3)*. The list includes exemption under clause 12 and clause 19. These were not part of the source legislation which referred only to the exemptions under section 505 ICTA, but they have been brought into the purview of the exemptions for these bodies – see *Changes 629* and *630* in Annex 1. The broadening of the exemptions under clauses 7 and 14 in respect of post-cessation receipts, and under clause 18 in respect of intangible fixed assets also has an effect – see *Change 627* and *Change 651* in Annex 1.

**Q12. We welcome comments on the proposal to extend to these named bodies the exemptions for post-cessation receipts, profits from certain fundraising events, estate income, and certain income from intangible fixed assets.**

69. The list does not include the exemption under section 16 as the conditions for this exemption are structured in a different way.

70. The National Endowment for Science, Technology and the Arts is included in the list. Exemption under section 507 ICTA was granted to this body by section 24 of the National Lottery Act 1998.

**Clause 21: Scientific research associations**

71. This clause brings scientific research associations (SRAs) within most of the exemptions in this Part. It is based on section 508 ICTA.

72. Like the bodies named in clause 20 SRAs are assumed to have met the test regarding the purpose of their expenditure. The relevant exemptions are listed in *subsection (2)*.

73. The list includes exemption under clause 12 and clause 19. These were not part of the source legislation which referred only to the exemptions under section 505 ICTA, but they have been brought into the purview of the exemptions for these bodies – see *Changes 629 and 630* in Annex 1. The broadening of the exemptions under clauses 7 and 14 in respect of post-cessation receipts, and under clause 18 in respect of intangible fixed assets also has an effect – see *Change 627 and Change 651* in Annex 1.

**Q13. We welcome comments on the proposal to extend to scientific research associations the exemptions for post-cessation receipts, profits from certain fundraising events, estate income, and certain income from intangible fixed assets.**

**Clause 22: Meaning of “scientific research association”**

74. This clause defines a scientific research association (SRA) for the purposes of this Part (and specifically clauses 5 and 21). It is based on section 508 ICTA, as amended by section 13 of the Finance (No 2) Act 2005. Those amendments are expected to be expected to be brought into force in 2008.

**Clause 23: Requirement to make claim**

75. This clause provides that in general a claim is necessary for an exemption. It is based on sections 505(1) and 761(6) of ICTA, section 46(1) of FA 2000 and section 83(4) of FA 2004.

76. Claims are made either as required during the accounting period, for example to secure repayments of income tax treated as paid in relation to gift aid payments, or in a corporation tax self-assessment return. The need to make a claim ensures that there is a mechanism for appeals in the event of any dispute about the availability or amount of any exemption.

77. The corporation tax self-assessment procedure means that a charitable company only needs to complete a tax return, and make the associated claims, if the charitable company is chargeable to tax or is required to do so by HMRC.

78. The reference in section 505(1) of ICTA to claims being to the Board of Inland Revenue has been changed. Claims will simply be to an officer of Revenue and Customs. See *Change 601* in Annex 1, which also affects clauses 27, 36, 39, 42, 43 and 46. One effect of a claim being made to the Board is that appeals are to the Special Commissioners. This is maintained by means of an amendment to section 46C of TMA – see paragraph 13 of Schedule 1.

**Q14. *Change 601* reproduces *Change 5* in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.**

79. *Subsection (3)* provides that where an individual makes a direction in a self-assessment return for a tax repayment to be paid as a gift to a charitable company, the company is treated as having made a claim.

**Clause 24: Restrictions on exemptions**

80. This clause restricts exemptions where income of a charitable company is attributed to non-charitable expenditure. It is based on section 505(4) of ICTA.

81. Certain exemptions have been extended or put onto a statutory footing:

- post-cessation receipts - see *Change 627* in Annex 1 and the commentary on clauses 7 and 14;
- profits of fund-raising events - see *Change 629* in Annex 1 and the commentary on clause 12; and
- income from estates in administration - see *Change 630* in Annex 1 and the commentary on clause 19.

The restrictions apply to these extended exemptions.

**Q15. We welcome comments on the proposal to extend the restrictions to these additional exemptions.**

**Clause 25: The non-exempt amount**

82. This clause specifies how the non-exempt amount is calculated. It is based on section 505(3) and (4) of ICTA.

83. The term “attributable income and gains” is defined in *subsection (3)*. This label replaces “relievable income and gains” as defined in section 505(3) of ICTA.

84. *Subsection (5)* specifies that section 256(4) of TCGA is to be ignored in applying subsection (3)(b). Section 256 of TCGA provides the exemption from capital gains tax for certain gains accruing to a charity. Schedule 1 amends section 256 TCGA, adding subsections (3A), (6) and (7), and amending subsection (4). Schedule 1 also inserts sections 256C and 256D TCGA, to deal with the interaction of this Bill and the chargeable gains legislation as regards attributing income and gains

to the non-exempt amount. It complements clause 26. The headings to section 256A and 256B TCGA are amended to make it clear that they apply to charitable trusts only.

**Clause 26: Attributing income to the non-exempt amount**

85. This clause sets out how income is attributed to the non-exempt amount. It is based on section 505(4) and (7) of ICTA.

86. It specifies that the non-exempt amount is to have attributed to it amounts of attributable income or amounts of attributable gains or a combination of both, until it is used up. The commentary on clause 25 contains further detail about the amendments to TCGA 1992.

**Clause 27: How income is attributed to the non-exempt amount**

87. This clause specifies that the charitable company can decide which items of what would otherwise be exempt income or chargeable gains should be treated as taxable. It is based on section 505(7) of ICTA.

88. Where the restrictions apply, an amount of income (or chargeable gains) equal to the non-exempt amount (of expenditure) must be identified (as calculated in accordance with clause 25) in order to enable the charitable company to complete its tax return and self-assess its tax liability. This clause provides the mechanism for the charitable company to specify the items or elements of income (such as trading income or investment income) which lose the benefit of exemption.

89. If the charitable company has not provided the attribution within a period of 30 days from the day of a request for a specification of the attribution, an officer of Revenue and Customs can decide the attribution. References to “the Board” have been replaced with “an officer of Revenue and Customs”. See *Change 601* in Annex 1 and the commentary on clause 23.

**Q16. *Change 601* reproduces *Change 5* in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.**

**Clause 28: Meaning of “non-charitable expenditure”**

90. This clause defines “non-charitable expenditure”. It is based on sections 506 and 506A of ICTA.

91. Section 506(1) of ICTA contains a definition of “charitable expenditure”, but neither expenditure itself nor “non-charitable expenditure” is defined explicitly. This clause sets out the definition in some detail, to reflect practice and HMRC guidance. See *Change 631* in Annex 1, which also affects clauses 29 and 30.

**Q17. We welcome comments on the proposal to set out the definition of “non-charitable expenditure” in the legislation, to reflect practice and HMRC guidance.**

92. Paragraph 2 of Schedule 2 contains a transitional provision to ensure that the pre-22 March 2006 rules continue to operate where appropriate.

**Clause 29: Clause 28: supplementary**

93. This clause applies relevant material located elsewhere to the definition of “non-charitable expenditure” (eg rules for computing trading losses) and provides interpretative material. It is new.

94. It is expected that the reference to Case VI of Schedule D will be replaced by a reference to a specified clause in this Bill, on the same lines as section 1016 of ITA 2007. For current purposes the reference to Case VI of Schedule D has been retained for ease of construction.

95. *Change 631* in Annex 1 affects this clause.

**Q18. We welcome comments on the proposal to set out the definition of “non-charitable expenditure” in the legislation, to reflect practice and HMRC guidance.**

**Clause 30: Clause 28(1)(d): meaning of expenditure**

96. This clause provides interpretative material about the meaning of “expenditure”. It is new.

97. *Change 631* in Annex 1 affects this clause.

**Q19. We welcome comments on the proposal to set out the definition of “non-charitable expenditure” in the legislation, to reflect practice and HMRC guidance.**

98. *Subsection (1)* makes it clear that “expenditure” includes expenditure on the acquisition of capital assets. But expenditure on assets qualifying for capital allowances is taken account of in determining, for example, a trading loss and so is not included in expenditure within clause 28(1)(d).

**Clause 31: Clause 28(1)(d): accounting period in which certain expenditure treated as incurred**

99. This clause specifies the accounting period to which expenditure relating to commitments (whether or not contractual in nature) that have been entered into is to be allocated for the purpose of operating the restrictions. It is based on section 506(2) of ICTA.

100. This rule has been rewritten in terms which make explicit reference to United Kingdom generally accepted accounting practice. See *Change 632* in Annex 1.

**Q20. We welcome comments on the proposal to make it explicit in the legislation that the time when expenditure is treated as incurred depends on UK generally accepted accounting practice (UK GAAP).**

**Clause 32: Clause 28(1)(d): payment to body outside the UK**

101. This clause provides interpretative material about payments to a body situated outside the United Kingdom. It is based on section 506(3) of ICTA.

102. The clause makes it clear that the onus is on the charitable company to ensure that any payments to a body outside the United Kingdom are applied for charitable purposes. Otherwise the charitable company must classify the payments as “non-charitable expenditure”.

**Clause 33: Clause 28(1)(g) and (h): investments and loans**

103. This clause provides interpretative material about the making of investments or loans. It is based on section 506(5) of ICTA.

104. The clause makes it clear that it is only the expenditure in the accounting period on making new investments and loans, or expenditure to fund net increases in such investments or loans, that is included in the calculation of non-charitable expenditure.

**Clause 34: Transactions with substantial donors**

105. This clause defines “substantial donor transaction” and explains when a person is a substantial donor to a charitable company. It is based on sections 506A(1) and (2) and 506C(3) of ICTA.

106. References to a charitable company include connected charities (see clause 41) and references to a substantial donor include persons connected with the donor (see clause 42(1)(a)).

**Clause 35: Meaning of “relievable gift”**

107. This clause includes details of the sources of gifts that are “relievable gifts” for the purposes of the preceding clause. It is based on section 506C(1) of ICTA.

**Clause 36: Non-charitable expenditure in substantial donor transactions**

108. This clause specifies that certain amounts relating to substantial donor transactions are to be treated as non-charitable expenditure. It is based on sections 506A(3) to (5) and 506C(2) and (6) of ICTA.

109. The source legislation specifies that certain matters are to be determined by the Commissioners for Her Majesty’s Revenue and Customs. References to “the Commissioners for Her Majesty’s Revenue and Customs” have been replaced with references to “an officer of Revenue and Customs”. See *Change 601* in Annex 1, which also affects clauses 39 and 42. The source legislation specifies that, on an appeal against an assessment, the Special Commissioners may review a decision of the Commissioners, so clause 42 specifies that the Special Commissioners may affirm or replace a decision of an officer.

<p><b>Q21. <i>Change 601</i> reproduces <i>Change 5</i> in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.</b></p>
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**Clause 37: Adjustment if clause 36(1) and (2) applied to single transaction**

110. This clause makes it clear that if both subsections (1) and (2) of clause 36 apply to an amount, the effect is not duplicated to create more “non-charitable expenditure” than the total amount in question. It is based on section 506C(4) of ICTA.

**Clause 38: Clause 36: certain payments and benefits to be ignored**

111. This clause provides that, in determining the amount of non-charitable expenditure payments or benefits arising from transactions relating to gift aid donations made by individuals or qualifying donations by companies, are to be ignored in certain circumstances. It is based on section 506B(7) of ICTA.

112. The payments or benefits are ignored if they would not prevent the donation being a “qualifying donation” by virtue of the rules concerning associated benefits provided to donors in section 416 of ITA and section 339(3)(b) of ICTA.

**Clause 39: Transactions: exceptions**

113. This clause specifies exceptions to the transactions caught by clause 34. It is based on section 506B of ICTA.

114. In particular, the clause carves out of the substantial donor provisions transactions of an ordinary commercial nature between the parties.

115. References to “the Commissioners for Her Majesty’s Revenue and Customs” and “the Commissioners” have been replaced with references to “an officer of Revenue and Customs”. See *Change 601* in Annex 1 and the commentary on clause 36.

**Q22. *Change 601* reproduces *Change 5* in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.**

**Clause 40: Donors: exceptions**

116. This clause specifies exceptions to the donors caught by section 34. It is based on section 506B(8) and (9) of ICTA.

117. *Subsection (1)* concerns companies set up by charitable companies, for example to carry on trading activities as a means of generating funds.

118. *Subsection (2)* concerns registered social landlords and housing associations, which often share services and accommodation with charities as a means of meeting charitable and non-charitable objectives.

**Clause 41: Connected charities**

119. This clause extends, for the purposes of clauses 34 to 40, the meaning of “charitable company” to include charities connected with the charitable company. It is based on section 506C(5) of ICTA.

**Clause 42: Substantial donor transactions: supplementary**

120. This clause provides interpretative material for clauses 34 to 40. It is based on section 506C(7) to (9) of ICTA.

121. References to “the Commissioners” have been replaced with references to “an officer of Revenue and Customs”. See *Change 601* in Annex 1 and the commentary on clause 36.

**Q23. *Change 601* reproduces *Change 5* in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.**

**Clause 43: Approved charitable investments**

122. This clause sets out which investments, including loans made by way of investment, count as approved charitable investments for the purposes of the rules restricting exemptions. It is based on Schedule 20 to ICTA.

123. The label “approved charitable investments” replaces the label “qualifying investments” in section 506(4) of ICTA.

124. Paragraph 2 of Schedule 20 to ICTA specifies investments falling within Schedule 1 to the Trustee Investment Act 1961 (TIA 1961) as approved, with a small exception. For trust law purposes TIA 1961 has been largely superseded by the Trustee Act 2000 (TA 2000). So the detail of investments covered by Schedule 1 to TIA 1961 has been incorporated into the clauses in an updated form, removing the need to refer to a Schedule to an Act (TIA 1961) that trustees no longer need to refer to for investment purposes. See *Change 633* in Annex 1, which also affects clause 44 and clause 45.

**Q24. We welcome comments on the proposal to provide an updated and simplified reference list of investments in the legislation.**

125. The reference to securities traded on the Unlisted Securities Market has been deleted as obsolete. The Unlisted Securities Market ceased trading in December 1996.

126. Investments can qualify as approved charitable investments if, despite not falling into any of the specified types not requiring a claim, a claim is made and it is accepted by HMRC. In order to be accepted, the claimant must show that the investment has been made for the benefit of the charitable company and has not been made for the avoidance of tax.

127. Investments include loans made by way of investment. Although not explicitly stated, such a loan would include a loan secured by a mortgage over land.

128. The source legislation includes a reference in paragraph 7(2) of Schedule 20 to ICTA to an “authorised institution” – which in the context of that paragraph clearly means a “bank”. “Authorised institution” was amended to read “bank” in

paragraph 7(1) by Schedule 37 to FA 1996, but was not amended in paragraph 7(2). This was an oversight and is corrected here.

129. In *Type 4*, the reference to Act includes references to Acts of the Scottish Parliament and Northern Ireland legislation. See *Change 619* in Annex 1.

**Q25. *Change 619* reproduces *Change 152* in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.**

130. References to “the Board” have been replaced with “an officer of Revenue and Customs”. See *Change 601* in Annex 1.

**Q26. *Change 601* reproduces *Change 5* in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.**

**Clause 44: Securities which are approved charitable investments**

131. This clause sets out details of which investments in securities count as approved charitable investments for the purposes of the rules restricting exemptions. It is based on Schedule 20 to ICTA and Schedule 1 to TIA 1961.

132. The detail of investments covered by Schedule 1 to TIA 1961 have been incorporated into these clauses in an updated form. See *Change 633* in Annex 1 and the commentary on clause 43.

**Q27. We welcome comments on the proposal to provide an updated and simplified reference list of investments in the legislation.**

**Clause 45: Conditions to be met for some securities**

133. This clause sets out details of certain conditions which some of the securities specified in the previous clause have to meet to count as approved charitable investments for the purposes of the rules restricting exemptions. It is based on Schedule 1 to TIA 1961.

134. The detail of the investments covered by Schedule 1 to TIA 1961 is incorporated into these clauses in an updated form. See *Change 633* in Annex 1 and the commentary on clause 43.

135. *Subsection (8)* specifies (among other things) that a company acquiring control of another company or other companies is treated as having paid a dividend or dividends paid by the other company or companies. The effect of including this provision (rather than cross-referring to a provision in TIA 1961) is that “control” needs to be defined. Consequently the definition of “control” in section 840 of ICTA applies for the purposes of this subsection. See *Change 633* in Annex 1.

**Q28. We welcome comments on the proposal to provide an updated and simplified reference list of investments in the legislation.**

**Clause 46: Approved charitable loans**

136. This clause sets out which loans (not being made by way of investment) count as approved charitable loans for the purposes of the rules restricting exemptions. It is based on Schedule 20 to ICTA.

137. The label “approved charitable loans” replaces the label “qualifying loans” in section 506(4) of ICTA.

138. References to “the Board” have been replaced with references to “an officer of Revenue and Customs”. See *Change 601* in Annex 1.

**Q29. *Change 601* reproduces *Change 5* in ITA 2007 and so brings the income tax and corporation tax codes back into line. We welcome comments on the proposal to carry this change into corporation tax.**

**Clause 47: Excess expenditure treated as non-charitable expenditure of earlier periods**

139. This clause treats “excess expenditure” in an accounting period as non-charitable expenditure for earlier accounting periods. It is based on section 505(3) and (5) of ICTA.

140. The “excess expenditure” is the amount of the non-charitable expenditure of the year in excess of the available income and gains of the accounting period.

141. The term “available income and gains” is defined in *subsection (4)*. This label replaces “total income and gains” as defined in section 505(3) of ICTA.

**Clause 48: Rules for attributing excess expenditure to earlier periods**

142. This clause specifies the earlier accounting periods to which the excess expenditure is to be attributed, later periods taking priority over earlier ones. It is based on section 505(5) and (6) of ICTA.

143. The amount of excess expenditure that can be attributed to an accounting period commencing before 22 March 2006 or earlier periods cannot exceed the amount that would have been attributed if the change in the method of calculating excess expenditure resulting from section 55 of FA 2006 had not been introduced. See the transitional provision in Part 1 of Schedule 2.

**Clause 49: Adjustments in consequence of section 47**

This clause specifies that any necessary adjustments (eg to tax, interest etc) for earlier years may be made. It is based on section 505(5) of ICTA.

**Schedules**

**Schedule 1: Minor and consequential amendments**

144. This Schedule contains consequential repeals and amendments. In particular it amends section 46C TMA 1970 to preserve the right of appeal to the Special Commissioners (see the note on clause 23) and it makes a number of amendments and insertions to TCGA 1992 (see the note on clause 25). Further consequential amendments will be identified as the work progresses.

**Schedule 2: Transitionals and Savings etc**

145. This Schedule contains transitional and saving provisions.

146. The exemption under section 56(3)(c) of ICTA in relation to transactions in deposits is preserved to take account of any relevant matters still in existence that pre-date the loan relationships legislation of FA 1996.

147. The treatment of non-charitable expenditure was amended and the rules in relation to substantial donors were introduced in FA 2006. The Schedule preserves the previous treatment where relevant (see in particular the commentary on clauses 28, 34 to 42, 47 and 49).

**ANNEX 1: MINOR CHANGES IN THE LAW MADE BY THE BILL**

**Change 601: References to “officer of Revenue and Customs”:  
clauses 23, 27, 36, 39, 42, 43, and 46**

This change replaces references to the “Board of Inland Revenue” in the source legislation with references to “an officer of Revenue and Customs”.

It brings the income and corporation tax codes back into line.

References in the source legislation to the “Board of Inland Revenue” are treated by section 50(1) of the Commissioners for Revenue and Customs Act 2005 (CRCA) as references to “the Commissioners for Her Majesty’s Revenue and Customs”. The rest of this note accordingly refers to the Commissioners for Her Majesty’s Revenue and Customs (“the Commissioners”) rather than to the Board of Inland Revenue.

The provisions affected by this change will in future authorise or require things to be done by or in relation to an officer of Revenue and Customs rather than by or in relation to the Commissioners. This reflects the way in which Her Majesty’s Revenue and Customs is organised and operates in practice. Section 13 of CRCA allows nearly all functions conferred on the Commissioners to be exercised by any officer. All of the functions affected by this change, which are in the main concerned with administrative processes, are in fact exercised by officers of the Commissioners, and the Commissioners themselves are not personally involved in their exercise.

Where the source legislation provides for a claim or election to be made to the Commissioners, this Bill does not expressly state to whom such a claim or election is to be made. Where a notice to deliver a corporation tax return has been issued paragraphs 57 and 58 of Schedule 18 to FA 1998 require the claim to be made in the return or by amendment of the return if possible. A return must be made to the officer who issued it. A notice amending a return must be made to an officer. Similarly, where the claim is made outside a return or amendment, paragraph 2(1) of Schedule 1A to TMA requires the claim to be made to an officer.

Each provision affected by the conversion of references to the Commissioners will be identified in the Table of Origins by a cross-reference to this change.

***This change has no implications for the amount of tax due, who pays it or when. It affects (in principle and in practice) only administrative matters.***

**Change 604: Requiring an apportionment to be just and reasonable: clause 8**

This change requires any apportionment that is not required by the source legislation to be made on a just and reasonable basis to be made on such a basis.

In some cases where there is an apportionment under legislation rewritten in this Act, the apportionment is required by the source legislation to be made on a just and reasonable basis. In other cases, it is required to be made only on a just basis or only on a reasonable basis, or there are no requirements. In new tax legislation it is now the practice to require an apportionment to be just and reasonable. For example, before it was replaced by ITEPA, section 140B(4) of ICTA required a just and reasonable apportionment to be made of any consideration given partly in respect of one thing and partly in respect of another.

There is no reason why an apportionment should not be on a just and reasonable basis. And it is desirable that all apportionments should be made on the same basis. Accordingly, where an apportionment under legislation rewritten in this Act is not required to be made on a just and reasonable basis, the rewritten provision requires the apportionment to be made on a just and reasonable basis.

The same change was made in ITTOIA to provide a uniform expression of the basis on which apportionments are to be made.

*This change makes minor amendments to a number of existing rules, but is expected to have no practical effect as it is in line with generally accepted practice.*

**Change 619: Interpretation: references to Scottish and Northern Ireland legislation: clauses 15, 18, 43**

This change is about the extent to which references to “Act” are to be interpreted as including references to Scottish and Northern Irish primary legislation.

Section 1018 of ITA 2007 sets out a list of sections of ITA where “Act” includes an Act of the Scottish Parliament and/or Northern Ireland legislation. We expect to adopt the same approach in this Bill.

Clauses 15 and 18 provide exemption for income of a charitable company or for income that “is required under an Act....to be applied to charitable purposes only”. Clause 43 contains the words “by or under a provision relating to any particular charities or class of charities contained in an Act”.

In each of these instances the reference to “an Act” is to the general law and not specifically to tax law.

“Northern Ireland legislation” is defined in section 24(5) of the Interpretation Act 1978 (the 1978 Act) and applies by virtue of Schedule 1 to the 1978 Act. It is the term commonly used in legislation when referring to Northern Irish primary legislation. The definition of “Northern Ireland legislation” has seven limbs, (a) to (g).

Section 832(1) of ICTA defines “Act” to include Acts of the Parliament of Northern Ireland and a Measure of the Northern Ireland Assembly. So it expressly covers limbs

(b) and (d) of the definition of “Northern Ireland legislation” in the 1978 Act. As a consequence of various deeming provisions contained in Schedule 12 to the Northern Ireland Act 1998, it also covers limbs (c), (e) and (f) of the definition of “Northern Ireland legislation”. Only limbs (a) and (g) of the definition of “Northern Ireland legislation” are not covered.

To simplify the definition of “Act” the current wording in section 832(1) of ICTA is to be replaced in the new clause with a simple reference to “Northern Ireland legislation”. The change in law is that limbs (a) and (g) of the definition of “Northern Ireland legislation” will now be covered.

The clause corresponding to section 1018 of ITA will also provide that in certain sections of this Act “Act” is to include Acts of the Scottish Parliament.

“Act” on its own does not include Acts of the Scottish Parliament (see the definition of “Act” in Schedule 1 to the 1978 Act). But it is appropriate that references to “Act” in clauses 15, 18 and 43 should include references to Acts of the Scottish Parliament. In each of these cases the extension of the meaning of “Act” can only be advantageous to taxpayers.

***This change is in taxpayers’ favour in principle and may benefit some in practice. But the numbers affected and the amounts involved are likely to be small.***

**Change 627: Charitable companies: exemption for post-cessation receipts of certain trades and property businesses: clauses 7, 8, 14, 20, 21 and 24; and Schedule 1 paragraph 22.**

This change introduces an exemption from corporation tax, in the case of charitable companies, for the post-cessation receipts of trades whose profits are exempt, or would be exempt if the trade had not ceased. It also introduces an exemption for the post-cessation receipts of property businesses, and of trades in cases where such income or receipts arise from land.

In contrast with the equivalent income tax rules in ITA 2007, adjustment income is subsumed within trading profits and, therefore, unlike the position for income tax, is already covered by the charitable exemptions.

Post-cessation receipts are taxed under Chapter 14 of Part 3 of Bill 5. There is no exemption for post-cessation receipts in the source legislation for charitable companies, other than the exemption in section 46 of FA 2000 (rewritten in clauses 9 to 11) which applies only if the receipts are below a certain level. But HMRC practice is to treat post-cessation receipts as exempt from corporation tax if they arise from a trade that benefited from the exemption in section 505(1)(e) of ICTA (rewritten as clause 7).

If a trade is treated as two separate trades in accordance with clause 8(2) and (3) any post-cessation receipts will be apportioned to the two parts (and this could mean completely apportioned to just one part if relating only to that part) and an exemption will then be available for the receipts apportioned to the charitable part.

The source legislation (section 505(1)(a) of ICTA, rewritten in clause 14) provides an exemption from tax under Parts 3 and 4 of Bill 5 in respect of any profits or gains arising in respect of rents or other receipts from an estate, interest or right in or over any land. The exemption is available only to the extent that the profits or gains arise from land vested for charitable purposes and the profits or gains are applied for charitable purposes. HMRC practice is to treat associated post-cessation receipts as eligible for exemption. This change provides such an exemption.

*This change is in taxpayers' favour in principle. But it is expected to have no practical effect as it is in line with generally accepted practice.*

**Change 628: Charitable companies: limit on exemption for profits etc of small-scale trades and certain miscellaneous income: clauses 9, 10 and 11**

This change rewrites the limit on the level of a charitable company's income for the purposes of the exemption for profits etc of small-scale trades in clause 9 and certain miscellaneous income in clause 10 by reference to the charitable company's incoming resources rather than in terms of its gross income. It also removes the requirement that the exemption for profits etc of a small-scale trade can apply only if the trade is carried on wholly or partly in the United Kingdom.

Section 46 of FA 2000 provides for an exemption from corporation tax for certain profits or other income or gains of a charitable company which are chargeable to corporation tax. The exemption applies in respect of a trade or to miscellaneous income chargeable under Case VI of Schedule D (subject to listed exceptions).

ITA 2007 collected together a list of miscellaneous income charges in section 1016. It is envisaged that the same approach will be taken for corporation tax, but for the present the reference to Case VI of Schedule D has been retained for ease of construction.

Section 46(3) of FA 2000 provides that one of the requirements for the exemption to apply is that the charitable company's "gross income" must not exceed the "requisite limit". The "requisite limit" is defined in section 46(4) of that Act and depends on the charitable company's incoming resources for the chargeable period.

Clause 11 sets out the condition about the level of the trading and miscellaneous income that has to be met if the exemptions in clauses 9 and 10 are to apply.

The condition operates by reference to the incoming resources associated with the trading activity and miscellaneous transactions whose profits are not exempt under other provisions. Tax law brings into account receipts that would not normally feature as incoming resources for accounting purposes – for example balancing charges under the capital allowances rules. The new definition ensures that all potentially taxable receipts are brought within its compass.

The source legislation aimed to bring in turnover for trading activity and gross receipts for Schedule D Case VI transactions. But these terms are not used in charity accounting. "Incoming resources" is familiar to those involved in preparing or working with charity accounts. And since charity accounting does not allow offset

between income and expenditure in determining disclosure (in contrast with the disclosure in the accounts of commercial organisations), it is relatively easy to check the limits.

It is not clear in section 46 of FA 2000 whether “gross income” includes incoming resources from an activity which gives rise to a loss, in cases where a profit would be taxable. But incoming resources from an activity are included irrespective of whether there is a profit or a loss.

This change aligns the rewritten legislation with the way it is considered section 46 of FA 2000 is operated in practice.

***This change is in taxpayers’ favour in principle. But it is expected to have no practical effect as it is in line with generally accepted practice.***

**Change 629: Charitable companies: exemption for profits from fund-raising events: clauses 12, 20, 21 and 24; and Schedule 1 paragraph 22**

This change gives statutory effect to Extra Statutory Concession C4 (trading activities for charitable purposes).

The concession provides an exemption for the profits of various fund-raising activities which amount to a trade, but which are only undertaken to raise money for charity. The concession does not apply in circumstances where an attempt is made to use it for tax avoidance. To reflect this, the new statutory exemption is subject to the restrictions in clause 24.

The fund-raising event has to be of a kind that falls within the exemption from VAT under Group 12 of Schedule 9 to the Value Added Tax Act 1994. This Schedule provides an exemption from VAT for the supply by a charity of goods and services in connection with an event that is organised primarily to raise money for itself or other charities. The Schedule defines “event” and places certain limits on the number of events that a charity can hold in the same location in any given year.

Clause 12, in line with the extra-statutory concession, is linked to the VAT legislation to provide consistency in tax treatment.

This exemption is also extended to the bodies listed in clause 20 and to scientific research associations (see clause 21).

***This change is in taxpayers’ favour in principle. But it is expected to have no practical effect as it is in line with generally accepted practice.***

**Change 630: Charitable companies: exemption for income from estates in administration: clauses 19, 20, 21 and 24; and Schedule 1 paragraph 22.**

This change provides an exemption to charitable companies who are liable to corporation tax on estate income charged under Chapter 1 of Part 10 of Bill 5, to the extent that the income is applied to the purposes of the charitable company.

Estate income is income from property held by the personal representatives or administrators of the estate of a deceased person on behalf of the beneficiaries of the estate.

There is a long-standing HMRC practice of treating United Kingdom estate income received by charities as exempt, and of allowing repayment claims in such cases. This change puts this on an explicit statutory basis.

This exemption is also extended to the bodies listed in clause 20 and to scientific research associations (see clause 21).

***This change is in taxpayers' favour in principle. But it is expected to have no practical effect as it is in line with generally accepted practice.***

**Change 631: Charitable companies: meaning of non-charitable expenditure: clauses 28, 29 and 30**

This change clarifies the meaning of “non-charitable expenditure”.

Section 506(1) of ICTA defines “charitable expenditure” as:

(subject to subsections (3) to (5) below) expenditure which is exclusively for charitable purposes.

Section 506(3) to (5) treats certain payments, investments or loans as amounts of non-charitable expenditure.

Section 505(4) of ICTA restricts a charitable company’s tax exemption by reference to non-charitable expenditure. “Non-charitable expenditure” is not defined but, by implication, it is expenditure which is not charitable expenditure.

Clauses 28, 29 and 30 set out the definition of “non-charitable expenditure” in some detail, to reflect practice and HMRC guidance.

Clause 28(1)(a) to (d), supported by clause 29, provide in relation to trades, property businesses and miscellaneous transactions, that it is *losses* which may count as non-charitable expenditure, rather than those expenses which are required to be taken into account in calculating the profits or losses concerned.

Clause 28(1)(a) to (d) also ensure that such losses do not count as non-charitable expenditure if corresponding profits would have been exempt under the provisions about small-scale trades, fund-raising events, lotteries or property income in clauses 9, 12, 13 and 14. And clause 28(1)(a)(i) makes it clear that losses made in a charitable trade do not count as non-charitable expenditure.

Clause 30 supports clause 28(1)(d), making it clear that expenditure (which is not itself defined in the source legislation) includes capital expenditure, but not the making of investments or loans or the repayment of loans made to the charitable company. Clause 28(1)(g) and (h) then make specific provision about investments or loans that are not approved charitable investments or loans, reflecting section 506(4) of ICTA.

*This change is adverse to some taxpayers and favourable to others in principle. But it is expected to have no practical effect as it is line with generally accepted practice.*

**Change 632: Charitable companies: accounting period in which certain expenditure treated as incurred: clause 31**

This change makes it explicit that the time when expenditure is treated as incurred depends on UK generally accepted accounting practice (UK GAAP).

Section 506(2) of ICTA provides that, for the purposes of section 505 of ICTA:

where expenditure which is not actually incurred in a particular chargeable period properly falls to be charged against the income of that chargeable period as being referable to commitments (whether or not of a contractual nature) which the charity has entered into before or during that period, it shall be treated as incurred in that period.

Section 506(2) was first enacted in FA 1986 and advanced the time that certain expenditure is recognised, on the basis that charitable companies may have some flexibility in this regard. As a result of subsequent developments in accounting practice, the legislation now implicitly mirrors UK GAAP.

Clause 31 is based on section 506(2) of ICTA, and makes the reference to UK GAAP explicit.

Clause 31 is drafted in terms of the position if UK GAAP had applied, because there is no legal or other obligation requiring all charitable companies to prepare their accounts in accordance with UK GAAP. In particular “Accounting and Reporting for Charities: Statement of Recommended Practice (revised 2005)”, which imposes a requirement to account in accordance with UK GAAP on charitable companies (with certain exceptions), is not mandatory in Scotland and Northern Ireland. Neither does it apply to charitable companies which are able to prepare accounts on a “receipts and payments” basis rather than an “accruals” basis. This could, for example, apply to unincorporated associations whose turnover and assets do not exceed the statutory limits.

This approach ensures parity of treatment as between charitable companies operating in different parts of the United Kingdom or adopting different bases of accounting.

*This change is adverse to some taxpayers and favourable to others in principle. But it is expected to have no practical effect as it is in line with generally accepted practice.*

**Change 633: Charitable companies: approved charitable investments: clauses 43, 44, and 45**

This change modernises the list of investments qualifying as approved charitable investments for the purposes of the rules restricting exemptions.

Although the list is based on Part I of Schedule 20 to ICTA (qualifying investments), it does not replicate the approach taken in that Part.

Part I of Schedule 20 defines qualifying investments by specifying certain investments itself, and also by referring to investments falling within Part I, Part II (apart from paragraph 13) or Part III of Schedule 1 to the Trustee Investment Act 1961 (TIA 1961).

For trust law purposes TIA 1961 has been largely superseded by the Trustee Act 2000 (TA 2000). TA 2000 increased significantly the range of investments trustees can invest in, and it would be a significant change in the law to allow any investment in accordance with TA 2000 to be treated as an approved charitable investment. But it would be unhelpful to continue to refer for tax purposes to a Schedule to an Act (TIA 1961) that trustees no longer need to refer to for investment purposes.

So the detail of investments covered by Schedule 1 to TIA 1961 is incorporated in clauses 43 and 44 in an updated form.

This has been done by referring to the types of investment that a charitable company can hold on “an approved basis”. So investment in, for example, fixed or variable interest securities issued by any of Her Majesty’s Government, the government of any overseas territory within the Commonwealth and the government of any state within (broadly) the European Union (EU) is reduced to securities issued by the government of any state in the EU and of any other state. This is wider, and so (strictly) is a taxpayer-favourable change. And rather than list the large number of individual entities in whose securities a charitable company can hold an approved investment, reference is made to the international entities listed in the directive on the taxation of interest payments. Again, this is a taxpayer-favourable change.

This approach tends to broaden the scope of possible investments, but in a way that is in keeping with HMRC practice in relation to claims that an individual investment should be regarded as qualifying, as set out in paragraph 9(1) of Schedule 20.

When it comes to the ability to hold an approved investment in the securities of (broadly) a non-listed company, the anti-avoidance provisions in Part IV of Schedule 1 to TIA 1961 have been largely repeated.

A more detailed analysis of where the approved investments in the source legislation appear in the rewritten clauses 43 and 44 is as follows:

<b>Schedule 20 to ICTA</b>	<b>Clause 43</b>	<b>Clause 44</b>
Paragraph 2	See details below relating to investments listed in TIA 1961	
Paragraph 3	Types 2 and 4	
Paragraph 3A	Types 3 and 4	
Paragraph 4	Type 5	
Paragraph 5 (note: the Unlisted Securities Market no longer exists)	Type 1	Subsection (1)(h)
Paragraph 6	Type 8	
Paragraph 6A	Type 1	Subsection (1)(g)
Paragraph 7	Type 9	
Paragraph 7A	Type 11	

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<b>Schedule 20 to ICTA</b>	<b>Clause 43</b>	<b>Clause 44</b>
Paragraph 8	Type 11	
Paragraph 9	Type 12	

<b>Part 1 of Schedule 1 to TIA 1961:</b>	<b>Clause 43</b>	<b>Clause 44</b>
Paragraph 1: Savings Certificates	Type 6	
Paragraph 1: Other	Type 1	Subsection (1)(a)
Paragraph 2 (note: only deposits in the National Savings Bank are still relevant)	Type 10(a)	

<b>Part 2 of Schedule 1 to TIA 1961</b>	<b>Clause 43</b>	<b>Clause 44</b>
Paragraph 1: Treasury Bills and Tax Reserve Certificates	Type 6	
Paragraph 1: Northern Ireland Treasury Bills	Type 7	
Paragraph 1: Other	Type 1	Subsection (1)(a)
Paragraph 2 (but principal must be guaranteed as well as interest)	Type 1	Subsection (1)(a)
Paragraph 3 (but assumes nationalised industries are not an issue in the United Kingdom and are not likely to be an issue elsewhere)	Type 1	Subsection (1)(b)
Paragraph 4 (and extended to securities issued outside the United Kingdom)	Type 1	Subsection (1)(b)
Paragraph 4A (and extended to securities issued outside the United Kingdom and drops requirement about parameters for setting the interest rate)	Type 1	Subsection (1)(b)
Paragraph 5 (and extended to securities issued outside the United Kingdom)	Type 1	Subsection (1)(c) and (d)
Paragraph 5A (and extended to securities issued outside the United Kingdom and drops requirement about parameters for setting the interest rate)	Type 1	Subsection (1)(c) and (d)
Paragraph 5B	Type 1	Subsection (1)(b) and (c)
Paragraph 6	Type 1	Subsection (1)(h)
Paragraph 7	Type 1	Subsection (1)(h)
Paragraph 9 (but some loans and deposits are not covered as this is considered unnecessary)	Type 1	Subsection (1)(b)
Paragraph 9A (but drops requirement about parameters for setting the interest rate)	Type 1	Subsection (1)(b)
Paragraph 10A	Type 8	
Paragraph 12	Type 10(b)	

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<b>Part 2 of Schedule 1 to TIA 1961</b>	<b>Clause 43</b>	<b>Clause 44</b>
Paragraph 13	Formerly excluded by paragraph 2 of Schedule 20 to ICTA – now excluded by reference under Type 5	
Paragraph 14	Type 5	
Paragraph 15	Type 6	
Paragraph 16	Type 1	Subsection (1)(b)
Paragraph 17 (but principal must be guaranteed as well as interest)	Type 1	Subsection (1)(b)
Paragraph 18 (but assumes nationalised industries are not an issue in the United Kingdom and are not likely to be an issue elsewhere)	Type 1	Subsection (1)(b)
Paragraph 19	Type 1	Subsection (1)(b)
Paragraph 20	Type 1	Subsection (1)(c) and (d)
Paragraph 21	Type 1	Subsection (1)(i)
Paragraph 22 (but some loans and deposits are not covered as this is considered unnecessary)	Type 1	Subsection (1)(b)
Paragraph 23 (and extended to similar societies outside the EU)	Type 10(c)	
Paragraph 24	Formerly excluded by paragraph 2 of Schedule 20 to ICTA – now excluded by reference under Type 5	

<b>Part 3 of Schedule 1 to TIA 1961</b>	<b>Clause 43</b>	<b>Clause 44</b>
Paragraph 1 (and extended to securities issued outside the United Kingdom)	Type 1	Subsection (1)(i)
Paragraph 2	Type 1	Subsection (1)(e)
Paragraph 2A	Type 1	Subsection (1)(g)
Paragraph 3	Type 8	
Paragraph 4 (and extended to securities issued outside the EU and to securities of non-EU incorporated companies)	Type 1	Subsection (1)(i)
Paragraph 5 (and extended to similar societies outside the EU)	Type 1	Subsection (1)(f)
Paragraph 6	Type 8	

<b>Part 4 of Schedule 1 to TIA 1961</b>	<b>Clause 45</b>
Paragraph 1	Not covered – this is taxpayer-favourable
Paragraph 2	Covered by Conditions A and B
Paragraph 2A	Covered by Conditions A and B
Paragraph 3	Covered by Condition C

*This change is adverse to some taxpayers and favourable to others in principle. But it is expected to have no practical effect as it is in line with generally accepted practice.*

**Change 651: Charitable companies: exemption for income from intellectual property etc: clauses 18, 20 and 21**

This change provides an exemption from corporation tax for certain income from intangible assets, whether or not the income is annual in nature.

Schedule 29 to FA 2002 introduced a comprehensive regime for corporation tax for income and gains arising from intangible fixed assets, rewritten as Part 9 of Bill 5. Those rules apply in general only to certain assets (principally, but not exclusively, those created or acquired on or after 1 April 2002). However, all income from royalties and certain telecommunication rights falls within the regime – see paragraphs 119 and 128 of Schedule 29 to FA 2002. These are all covered by the existing exemption in section 505(1)(c)(iic) of ICTA, rewritten as clause 18(3)(a).

Assets that do not fall within the rules of Part 9 of Bill 5 are referred to in Bill 5 as “pre FA 2002 assets”. Any chargeable gains arising from those assets will be exempt in the hands of a charitable company under section 256 of TCGA, provided the necessary conditions are met. However, any income from those assets that does not fall within Part 9 of Bill 5 is only exempt if it falls to be treated as an annual payment under Case III of Schedule D and is thus exempt under section 505(1)(c)(ii) of ICTA.

In practice HMRC allow an exemption for income from pre-FA 2002 intangible assets, whether or not it is annual in nature. This change is in line with that practice, and mirrors the change made for income tax in section 536 of ITA 2007. The rewritten legislation adopts the concept of a non-trading gain on an intangible fixed asset, and is written in terms that assume that the income in question would be such a gain, even though the assets fall outside the 2002 IFA regime.

This change also affects the exemptions available to the bodies listed in clause 20 and to scientific research associations under clause 21.

*This change is in taxpayers’ favour in principle. But it is expected to have no practical effect as it is in line with current practice.*

**Change 652: Charitable companies: condition as to trading and miscellaneous incoming resources: clause 11**

This change makes a small adjustment in the calculation of the limit in incoming resources where a charitable company has an accounting period that is shorter than twelve months.

Section 46 of FA 2000 provides an exemption for trading and miscellaneous income of a charity where the charity's income does not exceed a set limit. The limit cannot be less than £5,000 nor greater than £50,000. These two figures are both reduced in the case of an accounting period of less than twelve months.

The source legislation in section 46 FA 2000 states that the two amounts shall be "proportionally reduced". It has been common practice in the rewritten legislation to use a formula, and this practice has been followed here. The number of days in the accounting period is divided by 365 days to obtain the relevant proportion. Where the year has 366 days the formula will produce a slightly higher limit because of the smaller divisor. Where this occurs it will be beneficial to the taxpayer, although the amounts involved are expected to be very small.

*This change is in taxpayers' favour in principle and will benefit some in practice, but the numbers affected and the amounts involved are likely to be small.*