

**Tax Law Rewrite**  
**Responses to Papers**  
**CC/SC(06)06 & CC/SC(06)07**

**ITTOIA-Related Clauses**

*Bill 5 response document  
Committee papers CC/SC(06)06 and 07  
Introduction*

**INTRODUCTION**

1. We published Committee Papers CC/SC(06)06 and CC/SC(06)07 in May and July 2006 respectively on the HMRC internet website [www.hmrc.gov.uk/rewrite](http://www.hmrc.gov.uk/rewrite). The closing date for responses in both cases was 30 November 2006. All the draft provisions rewrote, for corporation tax purposes, provisions that have already been rewritten for income tax purposes in the Income Tax (Trading and Other Income) Act 2005 (ITTOIA). The provisions were:

Paper CC/SC(06)06 - Bill 5: Corporation Tax – ITTOIA-related provisions

- Appendix A. Investment income – Gains from contracts for life insurance etc.
- Appendix B. Investment income – Sales of foreign dividend coupons
- Appendix C. Miscellaneous income – Annual payments not otherwise charged
- Appendix D. Miscellaneous income – Beneficiaries’ income from estates in administration
- Appendix E. Miscellaneous income – Income not otherwise charged
- Appendix F. Incentives to use electronic communications
- Appendix G. Unremittable income

Paper CC/SC(06)07 – Bill 5: Trading and Property Income and Partnerships

2. The purpose of this response document is to provide details of the substantive points made and to explain our analysis and proposals in respect of them. Minor points, such as suggestions to improve punctuation are not covered, but all comments received have been carefully considered. We also do not propose to make stylistic changes where these would require corresponding amendments to ITTOIA.

3. A significant number of questions and proposed changes in the current consultation reflected questions and changes that were the subject of extensive consultation for ITTOIA and therefore few substantive comments were received on them for the corresponding corporation tax clauses. In view of this, we are only including dissenting or other material responses to these issues in this document.

4. No dissenting or material responses were received for Appendix E or Appendix F to paper CC/SC(06)06 and there is therefore no discussion of these in this response document.

*Bill 5 response document  
Committee papers CC/SC(06)06 and 07  
Introduction*

5. We received written responses from the following:
- The Chartered Institute of Taxation
  - The Confederation of British Industry
  - The Institute of Chartered Accountants in England and Wales
  - KPMG
  - The Law Society
  - Three individuals
6. We are very grateful for all the comments made, many of which were detailed and we appreciate the time and effort that went into them. We have sent each respondent a copy of this response document.
7. The following abbreviations for tax legislation are used:
- CAA            Capital Allowances Act 2001
  - FA             Finance Act
  - ICTA          Income and Corporation Taxes Act 1988
  - ITA            Income Tax Act 2007
  - ITTOIA        Income Tax (Trading and Other Income) Act 2005
  - TCGA         Taxation of Chargeable Gains Act 1992
8. Following discussions with our Consultative and Steering Committees, the format of this response document has been amended from that adopted in the past so that the comments received and the project's proposals are more clearly presented.

**COMMITTEE PAPER CC/SC(06)(06): ITTOIA-RELATED PROVISIONS:  
APPENDIX A: INVESTMENT INCOME: GAINS FROM CONTRACTS FOR  
LIFE INSURANCE ETC**

**Clause 9: Trusts created by two or more persons**

*The use of the term “settlor” sits rather oddly with the concept of trusts being “created” by persons, and the user may worry that he needs to be concerned about the status of settlor. Would the term “creator” be more appropriate?*

*Bill 5 response document*  
*Committee paper CC/SC(06)06: ITTOIA-related provisions*  
*Appendix A: Investment income: gains from contracts for life insurance etc*

9. A settlor makes a settlement and thereby creates a trust. That is, there can't be a settlement without in some way creating a trust. If there is no trust, the transaction would be one of making a gift or some other form of outright disposal. So it is not inaccurate to refer to the creator of the trust as the settlor, as they are one and the same.

10. "Creator" is not a term in general use in this context, whereas "settlor" is a familiar term in connection with trusts. There is unlikely to be any confusion as to its use here or any real question on the "status of settlor".

11. *We do not propose to amend the clause to substitute "creator" for "settlor".*

**Clause 22: When chargeable events occur**

*Q2. We welcome comments on the proposal to omit the exception in section 545(1)(a) of ICTA and to omit section 486 of ITTOIA.*

*This proposal is described "as... in line with current practice". It would be more accurate to state that the exception is considered to have always been and to remain inoperable.*

12. The comment here is in line with our view of the exception. So the proposal to omit it (and the ITTOIA equivalent) has more in common with a decision not to rewrite but to repeal a redundant provision (see the table of such provisions commonly provided in a Change note at the end of Annex 1 to explanatory notes for a project Bill).

13. *We propose to omit the separate change and to include the otiose exception in section 545(1)(a) of ICTA (and section 468 of ITTOIA) in the Change note listing redundant provisions not rewritten and to be repealed.*

**Clause 31: The total allowable deductions for a policy or contract**

*In subsection (3), 'and in subsection (2)' should be inserted after 'in subsection (1)', as in section 494(3) of ITTOIA.*

14. We agree the words are needed for an accurate replication of the source legislation.

15. *We propose to insert the words "and in subsection (2)".*

**Clause 61: The total amount of part surrender gains**

*Step 1 in subsection (1) and subsections (4) and (5) are excessively complex.*

*Bill 5 response document*  
*Committee paper CC/SC(06)06: ITTOIA-related provisions*  
*Appendix A: Investment income: gains from contracts for life insurance etc*

16. This clause, particularly the Step 1 calculation, works by cross-reference to earlier computational rules. The subsections in question are concerned with excluding assignments of rights in life policies etc from the operation of those cross-referred provisions.

17. Cross-reference is arguably less clear than a full restatement of the rule in question. But full restatement may sometimes obscure the basic purpose of the provision. And in this particular case it was felt that cross-reference was preferable.

18. The provision is closely modelled on section 524 of ITTOIA. Any difference in drafting here of the equivalent corporation tax rule would cast doubt on the matching nature of the income tax and corporation tax rules for arriving at gains on personal portfolio bonds. The use of cross-reference in that ITTOIA section did not give rise to adverse comments from respondents to the draft clause on which it is based.

19. *We do not propose to amend the clause.*

**Schedule 1: Transitionals and savings etc.**

**Part 2: Investment income: insurance policies and contracts made before certain dates**

**Paragraph 7: Modifications relating to pre-14 March 1989 policies of life insurance treated as later ones under paragraph 6**

*How is paragraph 104 of Schedule 2 to ITTOIA (certain pre-23 February 1984 policies not foreign capital redemption policies) applied for the purposes of corporation tax by paragraph 7, Schedule 1 (transitionals and savings)?*

20. Paragraph 7 of the transitionals and savings Schedule makes modifications to the corporation tax application of the regime, if the policy of life insurance in question was issued before 14 March 1989 but has been varied thereafter, for rules applying only from particular dates before that date.

21. The corporation tax charge can only apply, as regard policies etc issued before 14 March 1989, to a policy of life insurance which has been varied thereafter. See section 539(9) of ICTA, which is rewritten in paragraph 6 of the transitionals and savings Schedule. A life annuity and a capital redemption policy are not affected by the rule in section 539(9) of ICTA, so paragraph 7 does not apply in respect of paragraph 104 of Schedule 2 to ITTOIA.

*Bill 5 response document*  
*Committee paper CC/SC(06)06: ITTOIA-related provisions*  
*Appendix A: Investment income: gains from contracts for life insurance etc*

22. (One respondent, while approving the approach taken by this paragraph, commented that *this is an instructive demonstration of the reduced clarity compared with rewriting the rules fully in Schedule 1.*)

23. *We do not propose to amend the paragraph to add paragraph 104 of Schedule 2 to ITTOIA.*

**COMMITTEE PAPER CC/SC(06)(06): ITTOIA-RELATED PROVISIONS:  
APPENDIX B: INVESTMENT INCOME: SALES OF FOREIGN DIVIDEND  
COUPONS**

**Chapter 1: Sales of foreign dividend coupons**

**Clause 1: Charge to tax under this Chapter**

*Is a reference to banks unnecessary in subsection (4)?*

24. Sales to banks fall within subsection (3).

25. *The explanatory notes will be amended to clarify this.*

**Clause 2: Meaning of “foreign holdings” etc**

*How can shares issued by non-residents not be shares “outside the United Kingdom”?*

26. This point was considered during drafting. The words “shares outside the United Kingdom” were included because of the wording of section 18(3B) of ICTA. That subsection states that the references in Schedule D Cases IV and V to income arising from securities or possessions out of the UK are to be taken *in the case of relevant foreign holdings* as including the various categories of proceeds detailed under heads (a) and (b). This can be construed as meaning that where the securities or possessions are out of the United Kingdom *and* are relevant foreign holdings references to income from them include the proceeds under these heads (but not in other cases). In other words there is no assumption that relevant foreign holdings are automatically possessions out of the United Kingdom and, given the absence of a comprehensive definition for the latter term, we consider it necessary to retain the current statutory position.

27. *The explanatory notes will be amended to explain why this wording was adopted.*

*Is the wording of this clause intended to cover bearer shares where certificates are held in the United Kingdom?*

*Bill 5 response document*  
*Committee paper CC/SC(06)06: ITTOIA-related provisions*  
*Appendix B: Investment income: sales of foreign dividend coupons*

28. It seems unlikely that the physical location of share certificates (or coupons) has a bearing on *whether* income from such shares is from a possession out of the United Kingdom. Income from bearer bonds or shares issued by overseas bodies would fall within the definition of “foreign holdings” in section 18(3C) of ICTA regardless of the location of the certificates if they are possessions or securities out of the United Kingdom which one would as a rule expect them to be. (See comments under previous response as to what constitutes a security or possession out of the United Kingdom.) The precursor of section 18(3B) to (3E) of ICTA (section 23 of FA 1938) was enacted as a response to the decision in Paget v CIR 21 TC 677 AC. In that case Miss Paget held 4½% bearer bonds in the City of Budapest and 7% bearer bonds in the Kingdom of Yugoslavia so it seems certain that the intention of the foreign coupons legislation has always been to catch such bearer bonds and shares.

29. *We do not consider that any action is required here as this is a wider matter regarding what constitutes a possession out of the United Kingdom.*

**COMMITTEE PAPER CC/SC(06)(06): ITTOIA-RELATED PROVISIONS:  
APPENDIX C: MISCELLANEOUS INCOME: ANNUAL PAYMENTS NOT  
OTHERWISE CHARGED**

**Clause 2: Income charged**

*Should section 684 of ITTOIA be amended to include the equivalent of the reference in clause 2(2) of ICTA s527?*

30. In ITTOIA, annual payments which constitute intellectual property have been carved out of the general annual payments charge in Chapter 7 of Part 5 of ITTOIA, and put into a separate charge in Chapter 2 of the same Part. Section 580(4) of ITTOIA refers to section 527 of ICTA.

31. The reason we have not followed a similar approach (that is, carving out of the general annual payments charge a separate charge for annual payments which constitute intellectual property) in Bill 5 is because intellectual property is now fully and comprehensively covered by the new “intangible fixed assets” regime in Schedule 29 to FA 2002.

32. We plan to rewrite Schedule 29 to FA 2002 will be rewritten in Part 8 of Bill 5. When clause 2 of this Part of Bill 5 is read with Part 8 of Bill 5, we do not think that there will be any confusion.

33. *We do not propose to amend ITTOIA section 684.*

**Clause 7: Discretionary payments by trustees**

*“(heritage bodies)” should be inserted after “ICTA” in clause 7(2)(b), as in ICTA section 687A(2)(b).*

34. ***We agree, and will amend the clause.***

**Clause 8: Payments by persons liable to pool betting duty**

*Q1. Change 1 reproduces Change 47 in ITTOIA and so brings income tax and corporation tax back into line.*

*Change 47 in ITTOIA has not been effectively carried across to Bill 5 by the wording of clause 8.*

35. The correspondent commented that the words of clause 8 do not appear to encompass the words ‘the support of athletic sports or athletic games but with power to support the arts’, which appear in section 121(1)(b) of FA 1991. It was suggested that the appropriate remedy was to insert the equivalent of Condition C in section 748 of ITTOIA.

36. Condition C rewrites section 121(1)(b) of FA 1991. Condition C is that the payment is to trustees established mainly for the support of athletic sports or athletic games but with power to support the arts.

37. Both section 748 of ITTOIA and Clause 8 of this Bill fall within a Part which creates an exemption from tax for the recipients of certain payments.

38. In our view, it would not be rational to insert Condition C into clause 8, because the recipient trustees contemplated in Condition C are in any event not liable to corporation tax, and therefore cannot benefit from a corporation tax only exemption.

39. Neither section 748 of ITTOIA nor Clause 8 of this Bill rewrite provisions that deal with the deductibility of the payments. The deductions which are made allowable by section 126 of FA 1990 and section 121 of FA 1991 are dealt with in section 162 of ITTOIA and clause 152 of Bill 5.

40. ***We do not propose to insert Condition C into clause 8.***

*The wording of clause 8(3) does not faithfully reflect the wording of the source legislation, because it omits the word “playing”.*

41. This query was directed at the words in clause 8(3) ‘at a ground to be used for the purposes of association football’.

*Bill 5 response document*  
*Committee paper CC/SC(06)06: ITTOIA-related provisions*  
*Appendix C: Miscellaneous income: annual payments not otherwise charged*

42. The source legislation is section 126(1) of FA 1990, the last portion of which reads ‘at a ground to be used for the purposes of *playing* association football’.

43. It was suggested that these words in clause 8(3) were broader than the similar wording in the source.

44. ***We agree, and will insert the word ‘playing’ into the phrase ‘at a ground to be used for the purposes of association football’.***

**COMMITTEE PAPER CC/SC(06)(06): ITTOIA-RELATED PROVISIONS:  
APPENDIX D: BENEFICIARIES’ INCOME FROM ESTATES IN  
ADMINISTRATION**

**General**

*Why was section 699 of ICTA not rewritten for corporation tax?*

45. Section 699 of ICTA existed to prevent a charge to inheritance tax and to income tax on the same income that arose before the deceased person’s death but credited after the death. This provision was rewritten for income tax purposes (section 669 of ITTOIA) and was repealed in ICTA. Section 699 of ICTA only applied to income tax and therefore cannot be rewritten for corporation tax purposes.

46. ***We do not agree that section 699 of ICTA applies to corporation tax.***

**Clause 5: Meaning of “the administration period”, “the final accounting period” and “the final year”**

*In subsection (4), and in the heading, should “the final year” be “the final tax year”?*

47. The equivalent section in ITTOIA (section 653(3)) uses the term “the final tax year”, and there was also inconsistency between the explanatory note referring to “the final tax year” and the clause using “the final year”. We agree that the correct term should be “the final tax year”. This ensures consistency with ITTOIA to describe the same situation.

48. ***We propose to amend clause 5 so that the term used is “the final tax year”.***

**Clause 9: Income charged: foreign estates**

*Subsection (1) – the tax charge is on “the amount” (of estate income) whereas in the equivalent section 657(1) of ITTOIA for income tax the charge is on “the full amount” of the income treated as arising.*

*Bill 5 response document*  
*Committee paper CC/SC(06)06: ITTOIA-related provisions*  
*Appendix D: Miscellaneous income: beneficiaries' income from estates in*  
*administration*

49. This subsection is based on sections 695(4)(b) and 696(6) of ICTA. ITTOIA 2005 amended these sections to remove reference to Schedule D Case IV. The amendment by ITTOIA represented a correction because the schedular charge should no longer have applied to income from foreign estates for corporation tax purposes. Schedule 14 to FA 1996 introduced a new Schedule D Case III for corporation tax purposes to replace the previous Cases III and IV (section 18(3A) of ICTA). This income does not fall within the ambit of the new Case III.

50. Since there are no schedular charges imposed on income from foreign estates for corporation tax purposes, the income is subject to a free-standing non-schedular charge in the same way as the income from United Kingdom estates (for both income tax and corporation tax).

51. In the source legislation for income from foreign estates for income tax purposes, the charge was schedular. Consequently section 65(1) of ICTA, which referred to “the full amount”, applied. This term was carried over to section 657(1) of ITTOIA. As income from foreign estates for corporation tax purposes is non-schedular, the term “the amount” has been used. “The amount” is also used for non-schedular charges on income from United Kingdom estates for both income tax (section 656(1) of ITTOIA) and corporation tax.

52. *We propose that clause 9 should remain as drafted.*

**Clause 12: Basic amount of estate income: discretionary interests**

*Should it be made clear that this clause refers to discretionary payments of income and not of capital?*

53. As payments relating to a company’s discretionary interest in the residue of an estate can only be income in nature, and not capital, it was not considered necessary to make this clarification.

54. *We propose that clause 12 should remain as drafted.*

**Clause 13: The applicable rate for grossing up basic amounts of estate income**

*It is not right that companies receiving dividends direct are not subject to tax, but if received through an estate then the income is subject to corporation tax.*

55. *We have passed the comment on to our policy colleagues. Any such change would be beyond the remit of the project.*

**Clause 16: The residuary income of the estate**

*Although it is implicit in clause 16 that the taxpayer may choose whichever allocation of allowable estate deductions against different categories of income that is most advantageous, should this be explicitly stated?*

56. The lack of an ordering rule for allocating these deductions is mentioned in paragraph 58 of the explanatory notes. We believe that including an ordering rule in the clause would be out of proportion to any benefit achieved, and would also require an amendment to the equivalent section in ITTOIA to maintain consistency.

57. ***We do not propose to make a change to clause 16 to explicitly state an ordering rule.***

*Subsection (2) – Can it be made clear that there is no relief by way of deduction for interest on unpaid inheritance tax?*

58. Subsection (2)(a) points the reader to “section 233 of IHTA 1984: Exclusion of interest on unpaid inheritance tax”. To further assist the reader, we will add subsection (3) to the above signpost. Section 233(3) says “*interest payable under this section shall not be allowed as a deduction in computing any income, profits or losses for any tax purposes*”. We believe that adding subsection (3) to the signpost will sufficiently highlight the restriction.

59. ***We propose to make a change to clause 16 by adding subsection (3) to the cross reference to section 233 of IHTA 1984 to add further clarification.***

*Subsection (5) - Is it possible for there to be a definition of when expenses are properly chargeable to income?*

60. We have concluded that to insert a definition of every instance where expenses are properly charged to income would be very cumbersome. It would also be very difficult to cover every possible scenario. We think that the length of such a definition would be out of proportion to any benefit achieved.

61. ***We do not propose to add a definition to clause 16.***

**Clause 27: Relief where UK income tax borne by foreign estate: absolute interests**

*Should references in clause 27(1)(b), (1)(c) and (2) to “the relevant tax year” instead be to “the accounting period”, on the basis that the relief given relates to income arising in the accounting period which has already borne UK income tax (and not only to income arising in the same tax year, as in the equivalent section 677 of ITTOIA)?*

*Bill 5 response document*  
*Committee paper CC/SC(06)06: ITTOIA-related provisions*  
*Appendix D: Miscellaneous income: beneficiaries' income from estates in*  
*administration*

62. We believe that the use of “the relevant tax year” (as defined in clause 13) in clauses 27 and 28 is correct because UK income tax is deducted by reference to tax years. Similarly, the aggregate income of the estate will be calculated (in the first instance) by reference to tax years.

63. *We propose that clauses 27 and 28 should remain as drafted.*

**Clause 31: Transfer of assets etc. treated as payments**

*Subsection (4) –What would happen if part of a debt is released?*

64. We think that the reference to “debt” would implicitly include part of a debt.

65. *We propose that clause 31 should remain as drafted.*

**Clause 32: Assessments, adjustments and claims after the administration period**

*Subsection (5) –Could the reference be to “the end of” the accounting period?*

66. We think that adding “the end of” would not be an improvement on the clause as currently drafted.

67. *We propose that clause 32 should remain as drafted.*

**COMMITTEE PAPER CC/SC(06)(06): ITTOIA-RELATED PROVISIONS:  
APPENDIX G: UNREMITTABLE INCOME**

*Q1 Change 1 (unremittable income: appeals to the Special Commissioners): We welcome comments on the proposal to carry Change 142 in ITTOIA across to corporation tax.*

*As a company would retain the right to have a matter heard by the Special Commissioners in any event, it is not necessary for there to be included a transitional rule limiting the effect of the change to post 31 March 2009 accounting periods. And the transitional provisions will be of no effect in respect of pre-1 April 2009 events that fall in accounting periods that end after 31 March 2009 – subject to any saving provision designed to deal with such straddling accounting periods.*

68. This change omits the rule in section 584(9) of ICTA that an appeal against an assessment which involves a question as to the operation of the unremittable income rules should be heard by the Special Commissioners. The same change was made in rewriting the income tax application of section 584 of ICTA in Chapter 4 of Part 8 of ITTOIA.

*Bill 5 response document*  
*Committee paper CC/SC(06)06: ITTOIA-related provisions*  
*Appendix G: Unremittable income*

69. Paragraph 153(4) of Schedule 2 to ITTOIA preserves the rule in section 584(9) of ICTA for income tax purposes if an appeal against an assessment for the tax year 2005-06 or later involves a question as to the operation of Chapter 4 of Part 8 of ITTOIA or section 584 of ICTA in respect of income that arose in a tax year before 2005-06.

70. We propose that the rule will be preserved similarly for corporation tax purposes if an appeal against an assessment for an accounting period ending after 31 March 2009 involves a question as to the operation of the rewritten section 584 of ICTA or the former section 584 of ICTA in respect of income that arose in an accounting period ending before 1 April 2009. Modifications will be proposed to paragraph 94 of Schedule 18 to FA 1998 so that the power of General Commissioners under paragraph 94(4) to disregard an election by the appellant for hearing before the Special Commissioners is omitted.

71. But for a transitional provision that omits that power, an appellant company would not in fact “retain the right to have a matter heard” by Special Commissioners.

72. If the first accounting period of the company to end after 31 March 2009 includes a period before 1 April 2009, that period will not fall in an accounting period ending before 1 April 2009, so the corporation tax transitional provision equivalent to paragraph 153(4) of Schedule 2 to ITTOIA will not apply. But we propose there will be a provision in the corporation tax Bill which includes the rewrite of section 584 of ICTA, equivalent to that in paragraph 11 of Schedule 2 to ITTOIA (election to disregard changes in the law), so that the right to elect for hearing by Special Commissioners is retained in relation to such a straddling period.

73. *We consider that a transitional provision equivalent to paragraph 153(4) of Schedule 2 to ITTOIA will be needed in respect of the change omitting section 584(9) of ICTA in the course of rewriting the rest of that section.*

**COMMITTEE PAPER CC/SC(06)(07): TRADING AND PROPERTY INCOME AND PARTNERSHIPS**

**Clause 1: Overview of Part 1**

*The explanatory notes should explain the difference between the income tax and corporation tax treatments of adjustment income.*

74. *We will change the notes.*

**Clause 3: Charge to tax on trade profits**

*Q1 Can we draft for corporation tax on the basis that a company does not carry on a profession or vocation?*

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

*Reference to profession is required because investment activity may not amount to a trade.*

75. A company need not be carrying on a trade to be within the charge to corporation tax. Indeed a Part of the Bill will be devoted to the expenses of companies with investment business. Those companies will usually not be carrying on a trade. And the omission of references to the carrying on of a profession cannot affect them.

*The HMRC “practice” of treating the provision of professional services as a trade should be enacted.*

76. We think that would be confusing. There is no question of treating such activities as a trade; they actually amount to a trade.

*To draft on the basis that a company does not carry on a profession is unwise in particular in the case of “mixed” partnerships, in which at least one individual and at least one company are partners.*

77. The arguments were set out in Committee Paper (06)03 which was considered by the committees at their meetings in February 2006. The majority view of the committees was that the project was right to proceed on the basis that, for corporation tax purposes, a company does not carry on a profession.

78. We still think that the correct view is that the essence of a profession is the provision of the personal services of the person carrying on a profession. Once a company is interposed between the person providing the services and the person carrying on the business, the business changes its nature and becomes, for instance, the trade of “providing legal or accountancy services” (see section 297(2)(f) of ICTA, rewritten for income tax as section 192(1)(f) of ITA).

79. The approach of the Bill as currently drafted avoids introducing any suggestion that some of the reliefs which are clearly intended to apply for all corporation tax purposes should be denied in the case of a company providing professional services. An example of such a relief is that for trading losses (section 393 of ICTA). And there should be no doubt that the cessation of such activities triggers the end of an accounting period (see section 12(3)(c) of ICTA).

80. In the case of a “mixed” partnership which was highlighted by the respondent we do not think it is helpful to ask whether “the partnership” carries on a trade or a profession. Strictly, the partnership does nothing; the partners carry on a trade or profession in partnership. For income tax purposes the position of each partner liable to that tax is arrived at by assuming (section 849(2) or (3) of ITTOIA) that the trade or profession is carried on by an individual. For corporation tax purposes the position of each partner liable to that tax is arrived at by assuming (section 114(1) of ICTA) that the trade or profession is carried on by a company. Those assumptions typically lead to different answers for the two taxes. So there is no special problem with calculating

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

separately the profits of a profession notionally carried on by an individual and the profits of a trade carried on by a company.

81. In the time since 1965 we are not aware that there has been any difficulty with the administration of corporation tax on the basis originally set out by the drafters of FA 1965: for corporation tax purposes a company does not carry on a profession. It seems unhelpful to introduce the possibility that a company may carry on a profession simply because the wording of some later legislation caters for it.

82. ***We will proceed with the proposal to omit references to a company carrying on a profession.***

83. There were no objections to the proposal to omit references to a company carrying on a vocation.

84. ***We will proceed with the proposal to omit references to a company carrying on a vocation.***

**Clause 8: Profits of mines, quarries and other concerns**

*Clause 8 alters the scope of “fishings” in section 55 of ICTA.*

85. ***We are considering this point.***

**Clause 10: Payments treated as made to visiting performers**

*Is the rule in clause 10(2) justified by the source legislation?*

86. Section 556(2)(a) of ICTA (before the ITTOIA amendment) provided for the entertainer or sportsman to be treated as the person to whom the payment is made.

87. It is correct to say that the original ICTA rule did not mention the actual recipient of the payment. But the fact that the rule applies “for the purposes of the Tax Acts” is an indication that the rule goes wider than the calculation of the performer’s own tax position.

88. We think that treating the payment as made to the performer carries the logical implication that the payment is treated as not made to the person to whom it is actually made. If that person is treated as not receiving the payment it must not be taken into account in calculating the person’s trading profits. That is a trading income rule and we think it is helpful to include it in the trading income Part of the Bill. The position of the performer (always liable to income tax) is set out in section 13 of ITTOIA. So this part of the rule applies only for the purposes of this Part of the Bill.

89. ***We are satisfied it is correct to provide that the company which receives a payment that ITTOIA taxes on the visiting performer is treated as not having received that payment.***

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

**Clause 12: Tied premises**

*There is no need for the label “the trader” because there is already a contrast between the company carrying on the trade and the other person who occupies the premises.*

90. We will consider this point. But we think that, even if a label is not strictly needed, it often makes a clause easier to read. Indeed, the respondent who made this suggestion thought that “the employer” is useful in clause 55 and did not suggest the removal of “the employer” from clause 59 or “the contributor” from clause 64.

91. *We will consider the suggestion that there is no need for the label “the trader”.*

**Clause 14: Surplus business accommodation**

*In subsection (1)(d), could we have a definition of “relatively small”?*

92. The same point was raised in relation to ITTOIA. The concept of a “relatively small” receipt is based on the reference to “comparatively small” receipts in IR Decision 9. We considered replacing the words with a cash limit or a definition by reference to profits or turnover but decided against this as it would be too inflexible and might discriminate against larger business or business in high rent areas.

93. *We do not intend to include a definition of “relatively small”.*

**Clause 15: Payments for wayleaves**

*Does the clause apply to rent received in respect of a mobile phone mast?*

94. *It does not and it would be beyond our remit to change this. We have passed this suggestion to policy colleagues.*

**Clause 16: Generally accepted accounting practice**

*The adoption of international financial reporting standards means that deviation from generally accepted accounting practice (GAAP) is allowed.*

95. *The definition of GAAP in section 50 of FA 2004 makes clear that international accounting standards may be appropriate for the purpose of this clause.*

**Clause 20: Animals kept for trade purposes**

*Does clause 20(1)(a) apply only to animals kept for the physical work they do, for example, dray horses?*

96. The clause is not restricted to animals kept for the purposes of doing work that would otherwise be carried out by a machine or vehicle. It is a question of fact

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

whether what the animal does is work “in connection with the carrying on of the trade”.

97. *We do not propose to restrict the scope of clause 20(1)(a).*

**Clause 22: Capital expenditure**

*Prohibiting a deduction for capital expenditure is too sweeping in view, for example, of the availability of capital allowances.*

98. We agree that a deduction is allowed for some expenditure of a capital nature. But that is preserved in the Bill.

99. The specific case of capital allowances is dealt with in clause 19. This provides that the rules for calculating trade profits are to be read with the provisions of the Capital Allowances Act 2001 which treat charges as trade receipts and allowances as trade expenses. Clause 22 is a rule for calculating the profits of a trade and is therefore subject to the provisions of the Capital Allowances Act 2001.

100. Rules in the trading income Part of the Bill that allow trade deductions for capital expenditure are dealt with by clause 21. That clause gives priority to the rule allowing the deduction.

101. *We are satisfied that clause 22 does not conflict with any provision that allows a deduction for capital expenditure.*

**Clause 24: Bad debts**

*This clause is unnecessary because clause 16 requires GAAP to be followed.*

102. *We think that it is necessary to have the rule set out, even if the result is usually the same as that presented in GAAP accounts. So we propose to retain the clause.*

*It should be made clear that the clause applies only to non-money debts.*

103. We agree that money debts are dealt with entirely within the loan relationship rules (see, in particular, section 100(1)(c)(iii) of FA 1996). So the debts with which this clause is concerned are non-money debts.

104. *We propose to make clear that the clause applies only to non-money debts..*

*There should be a definition of “impairment loss”.*

105. *The definition of “impairment loss”, currently in section 103(1) of FA 1996, does not expressly apply to section 88D of ICTA. We are not sure that it would be right to apply the definition to this clause but will consider the point.*

**Clause 27: Employee benefit contributions: restriction of deductions**

*Can the reference to “period” in clause 27 be changed to “period of account” as the calculation of profit is made by reference to periods of account?*

106. ***We agree this is clearer and will make the change.***

*Is the reference to “or profession” in subsection (4)(a) correct?*

107. The background to this suggestion is the proposal to omit references to companies carrying on a profession for corporation tax purposes. The reference to a person carrying on a profession is correct as it applies to the provider of the goods and services who may be an income tax payer.

108. ***The reference to professions in clause 27(4)(a) is correct.***

**Clause 38: Car or motor cycle hire: supplementary**

*The reference to a “qualifying hire car” in subsection (2)(c) should be expanded to include a motor cycle.*

109. Such an amendment is not technically necessary because the definition of “qualifying hire car” in section 82 of CAA is expanded by section 81 of CAA to include a motor cycle. A change to this clause would suggest a stylistic amendment to the corresponding clause in ITTOIA (see paragraph 2 in the introduction to this document).

110. ***We do not propose to adopt this suggestion.***

*An option to purchase is an essential part of a hire purchase contract.*

111. Not all hire purchase agreements require the hirer to exercise an option before ownership passes at the end of the hire period. Under some agreements ownership passes when some other event takes place, such as when the final payment is made.

112. ***We are satisfied it is correct for clause 38 to provide for the case in which there is no option to purchase.***

*The exclusion of a conditional sale agreement in subsection (3) is unnecessary, because under such an agreement there would be no hire charges.*

113. We are not sure that is the case. The definition of “hire purchase agreement” in subsections (3) and (4) of this clause is not new but is taken from section 29 of the Hire Purchase Act 1964. The drafter of that Act considered that a conditional sale agreement could be one under which goods are hired and we think it is prudent to retain the exclusion.

114. *We intend to retain the exclusion of conditional sale agreement from the definition of “hire-purchase agreement” in clause 38(3).*

**Clause 40: Patent royalties**

*There should be a signpost to the provision under which the payment of patent royalties may be allowed as a trade deduction.*

115. *We accept this would be helpful and will consider how best to deal with this suggestion when rewriting the rules for intangible fixed assets given by Schedule 29 to FA 2002.*

**Clause 42: Penalties, interest and VAT surcharges**

*There is an error in the explanatory notes. Section 86 of TMA applies only for accounting periods ending before 1 October 1993.*

116. *We will correct the explanatory notes.*

**Clause 43: Crime-related payments**

*Should there be a reference to the effective operative dates for these provisions?*

117. Section 141(4) of FA 1994 restricts the operation of part of section 577A of ICTA to expenditure incurred after 30 November 1993. It is hardly conceivable that crime-related expenditure incurred on or before that date is relevant to the calculation of profits for an accounting period ending after 31 March 2009 (when this Bill is planned to come into force). So the Bill does not cater for that possibility.

118. *We do not believe that there is any need to rewrite this transitional rule.*

**Clause 45: Tenants under taxed leases: introduction**

*The clause is not clear and the reference to “taxed leases” in the heading is unilluminating. Adding an explanation at the end of subsection (1), e.g. “that is, leases on the grant or assignment of which tax has been chargeable under Chapter 4 of Part 2” would be helpful.*

119. This clause corresponds to, and is based on, section 60 of ITTOIA. We do not think the suggested words are appropriate. That is because the meaning of “taxed lease” goes wider than suggested: it includes leases charged under Chapter 3 of Part 4 of ITTOIA (as well as those charged under Chapter 4 of Part 2 of the draft clauses in committee paper (06) 07) and also those which would have been so charged but for relief under section 288 of ITTOIA (or clause 189).

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

120. Subsection (4) has a signpost to the definitions of “taxed lease” and to other terms common to clauses 45 to 50 and to Chapter 4 of Part 2 of the draft clauses in committee paper (06) 07. We think that this is more helpful than repeating the definitions in this Chapter.

121. *We propose to follow section 60 of ITTOIA and not add an explanation of “taxed lease” in subsection (1).*

**Clause 51: Replacement and alteration of trade tools**

*The words “implement, utensil or article” imply a restriction to hand tools.*

122. The Shorter Oxford English Dictionary defines “implement” as “a tool, instrument or utensil, employed in a particular trade, activity etc”. There is no reason to believe that the meaning is confined in common usage to a hand tool. So the Bill follows ITTOIA and uses the words of section 74(1)(d) of ICTA.

123. *We do not intend to restrict the definition of “tool” to hand tools.*

**Clause 58: Retraining courses: recovery of tax**

*Clause 58(5) should refer to “an officer” rather than “the officer” because, if a notice has not been given, no specific officer is involved.*

124. *We agree and will substitute “an officer of Revenue and Customs” for “the officer”. This will bring the clause into line with section 75 of ITTOIA.*

**Clause 60: Payments in respect of employment wholly in employer’s trade**

*Subsection (1)(b) should refer to the “amount of the payment” rather than the “payment” to make clear that an accounting concept (the accrual) is involved.*

125. We do not think this would help. The consistent approach of the Bill (and ITTOIA) is to allow (or disallow) a deduction for something. It is clear that any deduction is for the amount of that thing and in most cases the amount will appear in accounts on which a tax calculation is based.

126. *We do not intend to introduce a reference to “the amount of the payment” in clause 60(1)(b).*

127. There were a number of comments on clause 60(5).

*It is not clear that the subsection applies to trades carried on in partnership.*

128. The same point arises in connection with clauses 256(1) and (2) and 258(3).

*Bill 5 response document*  
*Committee paper CC/SC(06)07*  
*Trading and Property Income and Partnerships*

129. It is true that subsection (5) applies only in the case of a trade carried on at some stage in partnership. But there is an important implication for the case where a company carrying on a trade on its own takes another company into partnership to carry on the trade. In that case, the original trader is treated as ceasing to carry on the trade and subsection (4) of the clause applies. We think that this implication is important and that subsection (5) should not be restricted in the way suggested.

130. ***We do not propose to amend the clause.***

*B The explicit reference to a company within the charge to corporation tax is a change in the law.*

131. The scheme of corporation tax is that the profits of a trade are calculated as if the trade ceases when its profits move into or out of the scope of the tax. The rules are in sections 114 and 337 of ICTA.

132. In the case of this clause the rule in subsection (4) gives the employer a deduction on the last day on which the trade is carried on. It would be illogical to deny a deduction if the expenditure appeared in accounts for a period when none of the partners was a company resident in the United Kingdom. So the departure of the last partner within the charge to corporation tax triggers a deemed cessation of the trade. We still think that the clause clarifies, and does not change, the law.

133. ***We do not intend to amend the reference to companies within the charge to corporation tax.***

*C The income tax and corporation tax rules are different.*

134. There has long been a difference of approach in the legislation. Following the introduction of Self Assessment for income tax, a partner's share of trade profits is (self-) assessed by the partner. Previously the whole of the trade profits were assessed in the partnership name.

135. The income tax basis period rules mean that it would be inconvenient to treat a continuing partner's notional trade as ceasing. So section 852(5) of ITTOIA (rewriting section 111(4)(e) of ICTA) treats it as continuing. In contrast, there are no basis period implications for corporation tax. So section 114 of ICTA produces a cessation when a company ceases to carry on in partnership a trade which it subsequently carries on alone.

136. ITTOIA and this Bill preserve the distinction between the income tax and corporation tax treatments. We see no reason to remove it.

137. ***We are satisfied it is correct to retain the differences between the income tax and corporation tax treatments.***

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

*D In subsection (5), “if” is more appropriate than “so long as”.*

138. *We are considering this drafting suggestion.*

**Clause 62: Additional payments**

139. The points made in relation to clause 60(5), apply equally to subsection (2) of this clause.

*Subsection (2) denies a deduction if there is a cessation of part of a trade and, at the same time, a change in the persons carrying on the whole trade.*

140. We agree that subsection (2), as currently drafted, denies a deduction if there is some “corporate continuity”. That is not the intention of Change 18.

141. *We will revise the clause to achieve the intended result.*

**Clause 64: Contributions to local enterprise organisations or urban regeneration companies**

*The restriction in subsection (3) (and the charge in subsection (6)) should be based on the cost of the benefit rather than its value.*

142. The point has not given rise to any problems in practice. It may be difficult to determine the cost of a benefit. Indeed, there may not be discernible cost because it is part of the original contribution. So we do not feel justified in proposing a change in the law to meet this point.

143. *We do not intend to alter the basis on which the value of any benefit received by the contributor is measured.*

**Clause 66: Approval of local enterprise agencies**

*The clause should specify that the body need not be a corporate body.*

144. Clause 66(2)(a) provides that a body may be approved “whatever its status or structure”. We think that covers the point clearly and that there is no need to depart from the words used in ITTOIA.

145. *We do not think it is necessary to provide that the company need not be a body corporate.*

**Clause 70: Payments to research associations, universities etc**

*What definition of research and development applies for the purposes of this clause?*

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

146. The clause anticipates the amendments to section 82B of ICTA that will be introduced when section 15 of F(No 2)A 2005 takes effect. Section 13 of that Act also amends section 508 of ICTA so that it applies to associations that carry out research and development as defined by section 837A of ICTA. So the definition of research and development in clause 70(1)(b) is that in section 837A of ICTA as applied through the cross-reference to the amended section 508 of ICTA.

147. ***The definition of research and development is in section 837A of ICTA.***

*Can the initial capital letter in “Association” be dropped and a comma be inserted between “college” and “research institute” in this clause and section 88 of ITTOIA?*

148. Although “Association” is not capitalised in section 88(1)(a) of ITTOIA as enacted that provision is prospectively amended by section 14 of F(No 2)A 2005. The amendment reinstates the capitalisation reflecting the capitalisation in section 508 of ICTA. Section 926(2)(f) of ITA also reflects that capitalisation. For the sake of consistency we will keep the initial capital letter in this clause.

149. We will insert the comma in this clause but will not amend ITTOIA to avoid making an amendment that does not modify the law.

150. ***We intend to keep the initial capital letter in “Association”. We will insert the comma in this clause but not in the equivalent clause in ITTOIA.***

**Clause 74: Capital receipts**

*The clause should be made expressly subject to rules elsewhere in the Corporation Tax Acts that require some capital amounts to be taken into account as trade receipts.*

151. The respondent who made this suggestion drew particular attention to those regimes which require items of a capital nature to be brought into account in calculating trade profits, for example, loan relationships, derivatives and intangibles.

152. ***We are considering this suggestion.***

**Clause 78: Excluded cases**

*Q29 We proposed reinstating the exclusion for principal private residences.*

153. Some concern was expressed about the delay in reinstating this exclusion: there is a four year gap between the repeal of the exclusion by ITTOIA and the proposed re-enactment by the corporation tax Bill.

154. *HMRC practice will be to apply the “continuity of the law” rule in paragraph 1 of Schedule 2 to ITTOIA so that the exclusion continues to apply for corporation tax.*

**Clause 80: Arrangements not at arm’s length**

*The timing rule in subsection (3) is of general application and should not be restricted to the anti-avoidance provision.*

155. If there is no element of artificiality, HMRC are content to follow the accountancy treatment of the reverse premium and there is no statutory timing rule.

156. *We are satisfied that the timing rule in clause 80(3) should be restricted to the anti-avoidance rule.*

**Clause 81: Connected persons and property arrangements**

*The “period” during which persons are connected should be an accounting period.*

157. We do not agree. The period in question is that during which the property transaction and connected arrangements are entered into. That period may be much longer than a single accounting period.

158. *We are satisfied that the reference to period in clause 81(a) should not be restricted to a single accounting period.*

**Clause 82: Distribution of assets of mutual concerns**

*Does the reference to “profits” in subsection (1)(d) include chargeable gains?*

159. “Profits” does not include chargeable gains. As explained in Change 25, chargeable gains may be part of the profits of the concern but they are not part of the profits of its mutual business. So the clause has no application to chargeable gains. But we will reconsider the point as part of our continuing work on the meaning of “profits”, “total profits” etc.

160. *“Profits” does not include chargeable gains but we will consider how we can make this clearer.*

**Clause 86: Meaning of “designated educational establishment”**

*Shouldn’t the designation of an educational establishment in Scotland be a function of Scottish Ministers?*

161. It is true that it was the overall policy intention that educational matters were to be within devolved competence. But the functions conferred by section 84 of

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

ICTA 1988 are conferred for the purposes of the Corporation Tax Acts, and thus relate to “taxes”, a reserved matter. So the position is not entirely clear. We are leaving the power in the hands of the Secretary of State.

162. *We propose to leave the power to designate educational establishments in Scotland in the hands of the Secretary of State.*

**Clause 87: Gifts of medical supplies and equipment**

*The relief should be given to all companies not just those liable to corporation tax.*

163. The respondent who made this suggestion accepted that a line has to be drawn somewhere between companies resident in the United Kingdom (which are certainly eligible for the relief) and individuals (who are certainly not eligible for the relief). The clause draws the line between companies liable to corporation tax and all other persons. The respondent suggests drawing it between all companies (including those not liable to corporation tax) and all other persons.

164. There is a good deal of statutory material (set out in Change 30) which suggests that the relief is not intended to apply to persons liable to income tax. The alternative view would involve inserting a new clause into ITTOIA. Such a clause is unlikely to have any practical effect. So we do not propose to make the ITTOIA amendment.

165. *We do not propose to extend the relief to companies liable to income tax.*

**Clause 91: Herd basis: other interpretative provisions**

*Q41 – Should the income and corporation tax codes be brought back into line so that “a substantial part of the herd” is clarified?*

*Can clause 91(6) provide that “20% or more of a herd is always a substantial part of the herd”?*

166. There is no suggestion in clause 91(6) that there are any circumstances in which 20% or more of a herd would not be a substantial part of the herd.

167. *We do not think that “always” would add anything to the meaning of the clause.*

**Clause 98: Herd basis: acquisition of new herd begun within 5 years of sale**

*Clause 98(2) does not have any method of identifying which animals are treated as sold.*

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

168. We agree it is necessary to identify which animals are not replaced if the new herd is smaller than the old herd and the difference between the two herds is not substantial. But there is no method of identification in paragraph 3 of Schedule 5 to ICTA. Imposing a method of identification, such as first-in first-out, could give an adverse result in some cases. Therefore we do not suggest introducing one.

169. ***We do not intend to impose a statutory method of identification.***

*Why does clause 98(5)(a) refer to clause 97?*

170. Clause 98 applies if the acquisition of the new herd begins within five years of the sale. The parenthetical description in subsection (5)(a) suggests the clause includes a rule that applies only if the replacement does not start within five years. We agree that is confusing and will re-consider the drafting of clause 98(5).

171. ***We will reconsider the drafting of clause 98(5).***

**Clause 105: Herd basis: preventing abuse of the herd basis rules**

*Does clause 105 apply to a sale by a farming company to the farmer who controls the company?*

172. The respondent who asked this question was concerned that clause 105 does not rewrite the condition in paragraph 5(1)(a) of Schedule 5 to ICTA that “the transferor is a body or persons over whom the transferee has control”. We believe that subsection (2)(a) repeats that rule. So the clause does apply to a sale from a company to an individual who controls it.

173. ***The clause would apply to the sale. We are satisfied that the clause accurately reproduces the source legislation.***

**Clause 108: Taxation of amounts taken to reserves**

*“Reserves” should not appear in the title of the clause.*

174. It is true that the word “reserves” does not appear in the clause. But we think the title sends the right signal about the effect of the clause.

175. ***We do not propose to change the title of the clause.***

*Why are “securities” defined differently in clauses 108 and 109?*

176. We have looked again at this. There is no problem with the securities within paragraphs (a), (c) and (d) of clause 109(8) (which are identical to those within clause 108(4)(a), (b) and (c)).

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

177. The securities in paragraph (b) of clause 109(8) are those defined by section 132(3)(b) of TCGA. Profits and losses on all such securities are dealt with comprehensively in the rules for loan relationships and need not be dealt with here.

178. The quoted options in paragraph (e) of clause 109(8) are those treated as shares by section 147 of TCGA. Profits and losses on all such options are dealt with comprehensively in the rules for derivatives and need not be dealt with here.

179. The earn-out rights in paragraph (f) of clause 109(8) are those within section 138A of TCGA. But a dealer in securities does not hold such rights.

180. ***We propose to remove paragraphs (b), (e) and (f) of clause 109(8) and will consider removing paragraph (f) of section 150(8) of ITTOIA.***

**Clause 109: Conversion etc of securities held as circulating capital**

*Why is there a reference to income tax in subsection (7)?*

181. This is not a mistake but we accept that it would be helpful to explain why. Both corporation tax and capital gains tax are explicitly dealt with in section 137(1) of TCGA. But avoidance of income tax may be the purpose of the conversion of securities by a company.

182. ***We are satisfied that the reference is needed and will expand the explanatory notes to explain why.***

**Clause 112: Purchase or sale of woodlands**

*Should clause 112(3) refer to “the proportion of the sale price ignored under subsection (2)” or “the amount ignored under subsection (2)”?*

183. ***It is the amount and we think that subsection (3) accurately reproduces the source legislation.***

*It is not clear whether the amount ignored under clause 112(3) is:*

- *the whole of the amount attributable to the trees and underwood acquired; or*
- *the part attributable to the trees and underwood still standing at the time of the sale.*

184. ***It is the latter. We will make this clear in clause 112 and section 156 of ITTOIA.***

**Clause 113: Relief in respect of mineral royalties**

*The opening words of clause 113 are hard to follow.*

185. We agree the drafting could be improved but any change to this clause should be reflected also in section 157 of ITTOIA otherwise there would appear to be a difference between the provisions. But any amendment to ITTOIA would be stylistic only and would not modify the law. For that reason we do not think that we can amend ITTOIA. This means we should not amend this clause.

186. ***We do not intend to amend this clause or section 157 of ITTOIA.***

*Can the signpost to section 201 of TCGA be added in sections 156, 319 and 340 of ITTOIA?*

187. The signpost is included in a corporation tax Bill because the charge to corporation tax includes a company's chargeable gains. The signpost draws attention to the fact that the charge in this Bill is not the only charge to corporation tax on the royalties. The same considerations do not apply for income tax payers for whom capital gains tax is a separate tax.

188. Also any amendment to ITTOIA would not amend the law but would be stylistic only.

189. ***We will not add the signpost to the ITTOIA provisions.***

**Clause 118: Special rules for partnerships**

*Q48 We proposed using the firm's period of account, instead of a tax year, as the basis for the restriction in subsection (2).*

*A similar change should be made for income tax.*

190. A firm (even one comprising only individuals liable to income tax) does not have "profits ... for the tax year" (section 164(2) of ITTOIA). HMRC guidance (see paragraph 3204 of the Employment Status Manual) suggests using the profits of the year ending in the tax year. But that is not the only possible interpretation. We decided that we could not resolve the doubt when ITTOIA was drafted. That remains the position.

191. ***We do not propose to make the same change in ITTOIA.***

**Clause 119: Deduction for site preparation expenditure**

*The treatment of expenditure by a predecessor in clause 119(3) is not consistent with the approach in clause 124.*

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

192. There is the same inconsistency between sections 165 and 170 of ITTOIA. So we have to consider whether consistency should be gained at the expense of a divergence between the income tax and corporation tax codes.

193. *We will consider whether there should be greater consistency between the clauses in this Bill.*

**Clause 120: Allocation of site preparation expenditure**

*Should ordinal numbers be used for dates?*

194. *It is our preferred style now to use cardinal numbers consistently for dates.*

**Clause 124: Deduction for capital expenditure**

195. The point raised in connection with clause 119 affects this clause. We will also consider whether this clause should have a rule like that in clause 119(4)(a) which explicitly treats the trader's and the predecessor's trades as the same trade.

**Clause 137: Unremittable amounts: application of Chapter**

*Can we improve on the phrase "just because of" in subsections (2) and (3)?*

196. *We propose to substitute "merely because" both in this clause and in similar contexts. It is the phrase used in section 188 of ITTOIA and it is the phrase used consistently in ITA.*

**Clause 138: Relief for unremittable amounts**

*The relief should operate by reference to periods of account not accounting periods.*

197. Chapter 11 of Part 1 (unremittable amounts) is based on ESC B38. This extra-statutory concession was renumbered ESC C34 after ITTOIA. The extra-statutory concession operates by reference to accounting periods. In practice the company's accounting period will usually coincide with its 12 month period of account. But if a period of account spans more than one accounting period further work will be required to identify in which accounting period relief should be given. We agree it would be easier to operate the relief by reference to periods of account and will adopt the change.

198. *We will amend the clause so it operates by reference to accounting periods.*

**Clause 140: Withdrawal of relief**

*Why is the relief not withdrawn if the recovery event occurs after the trade has ceased?*

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

199. ***There is no provision for this in the extra-statutory concession and it would be beyond our remit to introduce it.***

*Why is the relief not withdrawn if a provision is made against the debt?*

200. The extra-statutory concession assumes that bad debt relief will not be available under section 74(1)(j) of ICTA on the grounds of unremittability. That paragraph was repealed by FA 2005. Relief for bad debts is given now through the loan relationship rules by deducting a provision for an impairment loss. We will consider how to amend the clause to deal with impairment losses.

201. ***We will consider how to deal with impairment losses.***

**Clause 147: Calculation of the adjustment**

*Why is there no reference to work in progress in item 3 of each of Steps 1 and 2 of the method statement?*

202. The reason there is no reference to work in progress is that the Bill does not cater for companies carrying on a profession (see Change 1 in Annex 1 to the explanatory notes). And we intend that anything relating to “materials” or incomplete services should be treated as part of a company’s trading stock (see the definition in clause 128). But that definition does not explicitly apply to this clause. We will consider reinstating the references to work in progress, leaving the method statement to be interpreted by reference to accounting concepts.

203. ***We will consider what changes are needed to the definitions used in this clause.***

**Clause 158: Debts released after cessation**

*Why is there no reference to section 337(1) of ICTA, corresponding to section 249(3) of ITTOIA?*

204. ***We plan to rewrite section 337 of ICTA in terms of a company ceasing to carry on a trade, rather than the discontinuance of the trade.***

**Clauses 167 and 168: UK property business and overseas property business**

*What is the position with regard to a single business of letting land within and outside the UK and, particularly, when properties straddle the border?*

205. What is a single business in commercial terms is two businesses in tax terms if the business has income from UK land and non-UK land: the UK property business (clause 167) and the Overseas property business (clause 168). That distinction follows from the distinction in the source legislation between, respectively, a Schedule A source and a Schedule D, Case VI source.

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

206. If, exceptionally, the same property physically straddled a UK border (the respondent referred to an Irish property), an apportionment of income between the two businesses would, theoretically, be required.

207. *We believe these matters are covered by the current clauses.*

**Clause 171: Non-UK resident companies**

*This clause is less clear than the source legislation it rewrites.*

208. *We agree and are considering how it could be improved.*

*Section 15(1A) paragraphs (a) and (b) of ICTA currently both refer wrongly to income tax charges.*

209. The amendment to section 15 of ICTA provided for by paragraph 8(2) of Schedule 1 to ITTOIA has not been applied correctly. As the respondent recognised, that will be corrected in the course of the corporation tax rewrite but we are grateful to have been alerted to the position.

210. *The error is an unintended editing error and the law is as provided for by the ITTOIA amendment.*

**Clause 177: Introduction**

*Subsection (2)'s reference to "short-term leases" would be more helpful if an explanation was added such as "(that is, leases with an unexpired term of 50 years or less)" because most people would not think that it could mean a lease with 50 years to run.*

211. This clause corresponds to, and is based on, section 276 of ITTOIA. Subsection (6) defines "short-term lease" in terms of the effective duration of the lease (the rules for which are in clauses 201 and 202). The effective duration is calculated by reference to the terms of the original lease, or of a contract for the variation or waiver of those terms, and not on the "unexpired term". The additional words suggested might be misleading as, for the purposes of the Chapter, a lease with an unexpired term of more than 50 years could be a short-term lease and another lease with an unexpired term of less than 50 years might not be a short-term lease.

212. *We propose to follow section 276 of ITTOIA and not add the suggested explanation to subsection (2).*

**Clause 188: Circumstances in which additional calculation rule applies**

*A rewrite change should be made whereby subsection (3)(c) (assignment is of a taxed lease) applies where the assignment is of a lease granted at undervalue out of a taxed lease.*

*Bill 5 response document*  
*Committee paper CC/SC(06)07*  
*Trading and Property Income and Partnerships*

213. A respondent felt that, without such a change, the additional calculation rule does not work rationally where the receipt under calculation arises in respect of the assignment of a lease granted at undervalue. The respondent thought that the root of the problem was that the additional calculation rule is constructed on the assumption that the charges in sections 34 to 36 of ICTA work in the same way; whereas section 35 works differently from the others by generating a charge on the (assigning) lessee under the lease rather than on the landlord.

214. Section 35 of ICTA (assignment of a lease granted at an undervalue) does work differently from section 34 of ICTA (treatment of premium as rent). But they share the characteristic that, in respect of the lease (“Lease L”) in question, an amount (“X”) is charged on a person other than the lessee who may be entitled to deductions in respect of X; in a section 35 of ICTA case the charge is on the person who assigns lease L and it is the assignee who may be entitled to deductions in respect of X. So, regardless of whether it is section 34 of ICTA or section 35 of ICTA that has applied, it is the lessee, for the time being, under L who may be entitled to deductions by reference to X.

215. Giving deductions (by reference to X) to persons other than the lessee for the time being under lease L would complicate the current rules and raise policy issues on which there are likely to be differing views.

216. *We do not believe that the suggested rewrite change is appropriate for subsection (3)(c).*

**Clause 194: Restrictions on section 193 expenses: the additional calculation rule**

*Subsection (1) should make it clearer that “the taxed receipt” referred to at the end of paragraphs (a) and (b) is distinct from the “receipt” mentioned in the first line of those two paragraphs*

217. We agree.

218. *We will amend subsection (1).*

**Clause 195: Restrictions on section 193 expenses: lease of part of premises**

*Subsection (2) should make it clearer that “the taxed receipt” referred to at the end of paragraphs (a) and (b) is distinct from the “receipt” mentioned in the first line of those two paragraphs.*

219. We agree.

220. *We will amend subsection (2).*

**Clause 196: Limit on reductions and deductions**

*This clause may not be needed as clauses 188 to 195 appear designed to avoid giving too much relief without recourse to this clause.*

221. Clause 192(4) (deductions for expenses under clause 193) uses clause 196 to set a limit on deductions under clause 193 (tenants under taxed leases treated as incurring expenses). This clause corresponds to section 295 of ITTOIA and clause 192(4) corresponds to section 291(4) of ITTOIA.

222. ***We propose to follow ITTOIA and retain this clause.***

*The reliefs mentioned in subsection (3) apparently have priority regardless of when they arise. It would be more practical to allow the various reliefs to take priority simply in order of time, which is impliedly the approach taken in section 37(9) of ICTA.*

223. This clause essentially follows the approach in section 295 of ITTOIA. Section 295 of ITTOIA provides that, in relation to the unreduced amount of a taxed receipt, the total of deductions/reductions in computing property income must not be greater than that unreduced amount less the total of trading deductions allowed.

224. When considering whether, at any particular time, a deduction/reduction in computing property income is restricted by the limit in section 295 of ITTOIA, we do not think that section 295 gives priority to trading deductions that may, or may not, arise at some later time. In other words, we think that section 295 of ITTOIA already reflects the more practical approach of considering reliefs in order of time.

225. ***We do not think that this clause gives priority to the reliefs mentioned in subsection (3) without regard to when those reliefs arise.***

*Section 295 of ITTOIA, as amended by paragraph 125 of Schedule 1 to the draft, apparently provides for the opposite order of priorities as between income tax and corporation tax reliefs.*

226. This clause differs slightly from section 295 of ITTOIA in that it places a limit on the total of deductions/reductions in calculating property income for corporation tax purposes (with a corresponding amendment so that section 295 of ITTOIA places a limit on such deductions/reductions for income tax).

227. But we do not think this causes problems since we do not believe that subsection (3) (either of this clause or of section 295 (as proposed to be amended)) gives priority to the reliefs mentioned, without regard to when those reliefs arise.

228. ***We do not think that a conflict arises between section 295(3) of ITTOIA (as proposed to be amended) and subsection (3) of this clause.***

**Clause 201: Rules for determining effective duration of lease**

*O68 We proposed clarifying the application of section 38(1)(b) of ICTA. We proposed also to amend Rule 2 in section 303 of ITTOIA to bring the income tax and corporation tax codes into line.*

*The rewrite change proposed for Rule 2 should be expanded to include a test essentially defining circumstances in which it is economically probable that the lease will be extended. This involves policy which might be disadvantageous to some taxpayers but that is acceptable so long as any change reflects existing practice (whatever that might be).*

229. A respondent thought that the real problem with Rule 2 is that it does not address how likely the lease extension has to be before it can be taken into account, nor how one can quantify a probability of that sort. To some extent Rule 1 was thought to suffer from the same weakness but that was largely mitigated by the additional objective test based on the amount of the premium (“the premium test”).

230. While Rule 1 seems more objective than the other rules because of the premium test, section 81 of FA 1972 inserted that test into Rule 1 for a different reason. The premium test was inserted to prevent Rule 1 being exploited to claim tax deductions for all, or almost all, of substantial premiums which related to what were, in commercial terms, very long leases.

231. Section 81 of FA 1972 also inserted Rule 3 to supplement Rule 1; preventing similar avoidance through arrangements where a short lease (on the grant of which a disproportionately large premium is attributed) would be followed by another (much longer) lease to which no premium is attributed.

232. Section 81 of FA 1972 did not alter Rule 2 as it already prevented similar avoidance through arrangements for the term of a short lease to be subsequently extended. FA 1972 appears to have been successful in curbing the artificial arrangements that were entered into prior to its introduction and we are not aware of problems in practice with Rule 2.

233. ***We do not propose to define in more detail the circumstances in which Rule 2 will apply.***

*Rule 3 suffers from essentially the same problem as Rule 2 and since the matters dealt with in Rules 2 and 3 are economically equivalent the drafting of the two rules should be in substantially the same terms.*

234. As a result of this comment we have reconsidered the proposed change to Rule 2. The proposed change to Rule 2 might give rise to arrangements designed to avoid Rule 1. For instance, arrangements might be made whereby the term of a lease is likely to be extended but where the lease is unlikely to last for the term of the extension. The proposed change to Rule 2 would indicate that the effective duration of

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

the lease is longer than would be the case if the lease was originally expressed to run to the end of the extended term and Rule 1 applied.

235. Dropping the proposed change to Rule 2 keeps its drafting closer to Rule 3.

236. *We are no longer proposing to make the change to Rule 2 that was originally proposed.*

*Q69 We proposed treating all ICTA section 34 amounts as premiums for the purposes of the duration rules.*

*Clause 201(3)(b) to (d) go too far in including as premiums sums payable under the lease in lieu of rent or for the surrender of the lease or which are payable for the variation or waiver of the lease.*

237. A respondent accepted that in some cases such sums should be taken into account as premiums (for example, if a sum is payable to commute the rent immediately after the grant of the lease and is calculated on a basis that suggests it will be paid) but felt that the change was not appropriate as it went too wide.

238. We agree that Rule 1(b) should not require, at the time of the grant of the lease (or contract for variation or waiver), sums to be treated as premiums under clause 201(3)(b) to (d) where the existence of those sums is speculative at the time of grant (or contract).

239. We think that clause 202(1) ensures that such speculative sums are ignored because it requires the rules in clause 201 to be applied by reference to facts known or ascertainable at the time of the grant (or contract).

240. *We think that clause 202(1) deals with the possible problems that concerned the respondent.*

**Clause 203: Information about effective duration of lease**

*A minimum time should be specified in subsection (3), eg 28 days.*

241. There is nothing to suggest that the present rule is not working well.

242. *We do not propose to change the law in this respect.*

**Clause 206: Furnished lettings**

*The words "lease or other arrangement" in clause 206(3) widen the current scope of the Schedule A charge on incidental income from providing furniture in furnished lettings.*

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

243. We do not think they do. Clause 206 follows the approach we adopted in section 308 of ITTOIA in dropping the words “tenant or other person entitled to the use of the premises” in rewriting section 15(1) Schedule A paragraph 4(2)(b) of ICTA. Strictly, only persons entitled to occupy land under a lease are tenants so the reference to “other arrangement” is necessary in clause 206(3) to cover persons who are entitled to the use of premises but are not “tenants”.

244. But, more widely, clause 206 can apply only if there is a property business within clause 167 or 168. And, under clause 169, the profits of a property business can include only income from land. The purpose of clause 206 is limited to bringing within the charge on the property business any income from the incidental hiring of furniture that is inherent in the letting of furnished property.

245. *We do not propose a change in wording.*

**Clause 207: Acquisition of business: receipts from transferor’s UK property business**

*This rule should be with the other post-cessation receipt rules in Chapter 9 of this Part of the Bill.*

246. It is a rule about receipts which can stand on its own, with just a single cross-reference (in subsection (3)) to Chapter 9. So we think it belongs in Chapter 5. This approach follows sections 98 and 310 of ITTOIA and clause 76 of this Bill.

247. *We are satisfied the clause should stand on its own.*

*Subsection (2)(a) should be amended so that it is clearer that the sums are the result of the transfer of rights, not the transfer of the business.*

248. *We will consider this.*

*Subsection (2)(b) should be amended so that it refers to sums to the extent that they have not been taxed.*

249. *We do not think this is necessary. The clause deals with sums (rather than, for instance, profits): each sum has either been taxed or it has not.*

*What about the treatment of sums which have been the subject of an accrual in the accounts?*

250. If such a sum is not ultimately received, a deduction will be available in accordance with the usual rule in clause 24 or the loan relationship rules (as applied by section 100(1)(c)(iii) of FA 1996). Those same rules apply even if the debt is inherited by a successor to the business (see also Change 7 in Annex 1 to the

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

explanatory notes). So there is no need for this clause (or clause 241) to provide for a deduction.

**251. *There is no need to make specific provision for sums for which there has been an accrual in the accounts.***

**Clause 208: Reverse premiums**

*It is inconvenient to have to go back to clause 79(1) to find the rule that a reverse premium is to be treated as a receipt of a revenue nature.*

252. We think that the rule in subsection (3) of this clause is clear enough. The premium is treated as a receipt in calculating the profits of the property business. So it must be a revenue receipt for this purpose.

**253. *Clause 208(3) taxes the premium as a revenue receipt without the need to refer to clause 79(1).***

**Clause 209: Deduction for expenditure on seawalls**

*Subsection (5)(b) should make it clear that the “no apportionment” rule applies only to the last accounting period before the transfer.*

254. Section 30(4) of ICTA states explicitly that this rule applies to any (accounting) period before the transfer takes place.

**255. *We do not propose to amend clause 209 as suggested because we believe it reflects the current law. But we have amended subsection (5)(b) to make it clear that it applies only to the transferee and can affect only accounting periods ending in the tax year in which the transfer takes place.***

**Clause 210: Transfer of interest in premises**

*Subsection (5) does not address the possibility that the expenditure might be wholly referable to only one part of the premises transferred and therefore that only one of the parties is entitled to the deduction.*

256. Section 30 of ICTA proceeds on the assumption that at least some of the expenditure is attributable to each part of the premises. Section 30(1) says that the expenditure must be “necessary for the preservation or protection of the premises...” and picks those words up again when it says that the owner/tenant is “treated as making a payment in relation to *the premises preserved or protected by the embankment*” (emphasis added). The section then goes on to deal with a sale of part of the “premises preserved or protected by the embankment”, under that assumption.

**257. *We do not propose to amend clause 210 as suggested because we believe it reflects the current law.***

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

**Clause 211: Ending of lease in premises**

*There is a better reason for not rewriting the definition of “lease” in section 24(6)(a) of ICTA.*

258. Paragraphs 930 to 932 of the commentary explain why we are not rewriting the definition of “lease” in section 24(6)(a) of ICTA. One respondent commented that a better reason for not rewriting it is that a lease is not referred to in section 30(1) of ICTA. That suggests an unrestricted interpretation of “tenant” in section 30(1) and, by extension, of “lease” in section 30(3).

259. *The respondent agrees that section 24(6)(a) is redundant so no changes are required.*

**Clause 213: Relief in respect of mineral royalties**

*The restriction in clause 213(2)(b) is less clearly expressed than the wording in sections 121 and 122(2) of ICTA.*

260. Clause 213 applies only to mineral rents that are taxed under Schedule A. Section 121 of ICTA has no application to this income. This is not because no deductions are available but because deductions are given under the normal rules of Schedule A. Section 122(2) of ICTA distinguishes between royalties to which section 121 of ICTA applies and royalties taxed under Schedule A. Clause 213 preserves that distinction and repeats the language of section 122(2)(b) of ICTA.

261. *Section 121 of ICTA has no application to this income and clause 213(2)(b) repeats the language of section 122(2) of ICTA. We do not believe it is necessary to amend clause 213(2).*

*There should be an express provision to the effect that clause 213 has priority to Chapter 7 of the property income Part.*

262. There is no overlap between the two provisions. Clause 213 applies only to income taxed under Schedule A and Chapter 7 only to income taxed under Schedule D Case VI. Section 119 of ICTA gives priority to income taxed under Schedule D Case VI and this is preserved in clause 165. Clause 226 applies if the rent is received in respect of a UK section 8(4) concern.

263. *There is no overlap between clause 213 and Chapter 7 so no order of priority is required.*

**Clause 217: Giving effect to positive and negative adjustments**

*Clause 217(3) and 217(5) should refer to the relevant proportion of the receipt or expense.*

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

264. We do not agree. The clause refers to an amount in respect of depreciation. Each such amount (relating to a single asset) is considered separately. There may, of course, be several such amounts on a change of basis.

265. *We believe the clause is correct to refer to an amount in respect of depreciation and not a relevant proportion of the amount.*

**Clause 221: Meaning of “qualifying holiday accommodation”**

*The meaning of “circumstances that are not normal” in clause 221(6) should be clarified.*

266. Clause 221(6) rewrites section 504(3) of ICTA which includes a reference to accommodation “not normally in the same occupation for a continuous period exceeding 31 days”. Both the source and the rewritten legislation are intended to cope with circumstances of potentially infinite variety. What is “normal” in the context of a particular case will usually be clear. On the other hand, attempting to legislate what is “normal” in all circumstances would be a change in the law which would remove the present flexibility and could disadvantage taxpayers in particular cases.

267. *We will not try to define the term “circumstances that are not normal”.*

**Clause 225: Meaning of “rent receivable in connection with a UK section 8(4) concern”**

*As the definition of rent includes other receipts it would be helpful to say “rent or similar receipts”.*

268. *We have decided not to adopt this suggestion as it would add to the length of this clause and clause 224 each time the word “rent” was used.*

**Clauses 226 and 235: Rents in connection with UK concerns and wayleaves: income charged**

*It is inaccurate to use the word “profits” in the “income charged” clauses of Chapters 7 and 8 of the property income Part.*

269. Chapters 7 and 8 of the property income Part rewrite the charge under Schedule D Case VI given by sections 119 and 120 of ICTA in the case of certain rents that would be taxed under Schedule A. Apart from the deductions identified in clause 226(2) the charge is on the gross amount of the rent received.

270. We agree it would be clearer to say this and not to imply that there is some balance of profit or loss to be struck.

271. *We will consider how to amend the clauses to reflect this.*

**Clause 248: Calculation of firm's profits or losses**

*Subsection (1) should make it clearer that more than one calculation may be needed.*

272. *We will consider this.*

**Clause 249: Section 248: supplementary**

*Not rewriting section 114(1)(b) of ICTA is a change in the law, particularly in a case involving the re-allocation of partnership profits or losses under clause 251 or 252.*

273. We do not agree. Section 114(1)(b) of ICTA dates from the time when the profit shares of all partners were calculated in accordance with the corporation tax rules, even if some of the partners were liable to income tax. In those days for income tax purposes capital allowances were given "in taxing" the trade. So they had to be taken out of the partnership calculation.

274. Now the profit shares of the partners liable to income tax are calculated using the income tax rules (see section 849 of ITTOIA) and there is no need for a special rule for capital allowances. Similarly, the combined effect of section 114(1)(b) and (2) of ICTA on charges is always to restore the calculation to what it would have been without the exclusion under subsection (1)(b).

275. Clauses 251 or 252 merely enact an HMRC practice. Any interaction with section 114(1)(b) of ICTA is a matter of practice rather than a question of law. So this aspect of the repeal of section 114(1)(b) cannot be a change in the law.

276. *We do not agree that there is a change in the law.*

*The absence of an income tax equivalent of clause 249(1) of the clause may carry the incorrect implication that losses of another period are relevant to a calculation under section 849 of ITTOIA.*

277. *We will consider whether ITTOIA should be amended.*

*The words in brackets at the end of clause 249(2) are misleading.*

278. The words are merely a description of section 337A(1) of ICTA, which is disapplied by the clause; they do not reverse the effect of the subsection.

279. *We will consider changing the words in brackets.*

**Clause 250: Allocation of firm's profits or losses between partners**

*Q78 We proposed dropping paragraph 13(2) of Schedule 22 to FA 2002.*

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

*The income tax and corporation tax rules should be the same and the rule in paragraph 13(2) is more logical than the general rule in paragraph 4 of Schedule 22.*

280. The rules for income tax and corporation tax have been different since FA 2002 was enacted: the income tax charge was under Schedule D Case VI; the corporation tax charge is as a receipt of the trade. We would not be justified in changing this approach.

281. The general rule for corporation tax is that a positive adjustment is “treated as a receipt of the trade ... arising on the first day of the first period of account for which the new basis is adopted” (paragraph 4 of Schedule 22 to FA 2002). Both respondents argued that it would be more logical to treat the receipt as arising a day earlier, because it represents a “catching up” exercise. We do not propose to change the law on this point generally (see clause 146(2)).

282. But we have reconsidered the proposal to drop paragraph 13(2) of Schedule 22 to FA 2002 (Change 57 in Annex 1 to the explanatory notes). It is clear that the rule in paragraph 13(2) of Schedule 22 to FA 2002 is intended to have some effect; and that the effect is intended, in some cases, to be different from the effect of paragraph 4 of Schedule 22 to FA 2002. So, in the light of these respondents’ comments we will rewrite paragraph 13(2) and clarify its relationship with the general rule in this clause.

283. ***We will rewrite paragraph 13(2) of Schedule 22 to FA 2002.***

**Clause 251: Profit-making period in which some partners have losses**

*The words “in relation to a partner” give the impression that the clause is not dealing with the calculation of the profits of the whole trade carried on in partnership.*

284. The point of the words is to indicate that the profits of the firm have to be calculated on the appropriate basis, according to the residence of the partners.

285. It may be that the calculation required under clause 248(3) produces a result that requires an adjustment in accordance with this clause for a non-resident partner. But no such adjustment may be needed to the calculation under clause 248(2) for a resident partner. Similarly, there may be an adjustment for a resident partner but none for a non-resident partner.

286. ***We will consider whether the clause can be made clearer when we look at the suggestion made for clause 248.***

**Clause 257: Sale of patent rights: effect of partnership changes**

*There are no circumstances in which clause 257(3)(b) will ever apply.*

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

287. It is true that when a company takes another company into partnership the deemed company formed for the purpose of section 114(1) of ICTA starts to trade. So the original trader ceases to carry on the trade and this triggers the discontinuance of the trade in accordance with section 337(1) of ICTA.

288. But the position is different for income tax. When an individual takes another individual into partnership the trade is treated as continuing (originally section 113(2) of ICTA, rewritten in this context as section 861(4) of ITTOIA). The same rule applies even if the new partner is liable to corporation tax. The rule in section 337(1) of ICTA applies only for the purposes of corporation tax and the income tax trade is not treated as ceasing.

289. The result is that section 558(1)(c) of CAA is satisfied and the charge is made on the “present partners”. So we believe that subsection (3)(b) of the clause may apply.

290. ***We believe that clause 257(3)(b) can be relevant.***

*What is the reason for the difference in wording between clause 257(4) and clause 258(1)(d)?*

291. Clause 257 applies only if the company carrying on the trade before the change did so in partnership. This is because, as explained in paragraph 287, the trade is treated as discontinued when a company not in partnership takes another company into partnership.

292. Clause 258 applies if there is a later change. Like clause 257 it applies only if the company carrying on the trade before the later change did so in partnership. This is explicit in subsection (1)(b). So the reference to trading in partnership is not needed in subsection (1)(d).

293. ***We do not propose to bring the wording of clauses 257(4) and 258(1)(d) into line.***

*There may be a problem with the operation of the clause if there is a partnership change part way through an accounting period.*

294. The rule in subsection (6) applies only to the “remainder of the amount” and for the “remainder of the tax spreading period”. This seems to leave open the treatment of the amount that would have been chargeable for the accounting period in the period before the change. We will look at this again.

295. There are other, more fundamental, problems with the clause as currently drafted. We will think again about the uncertain length of the “tax spreading period” as currently defined in subsection (7) of this clause and the need to define more closely the firm’s profit sharing arrangements in clause 258(3).

*Bill 5 response document  
Committee paper CC/SC(06)07  
Trading and Property Income and Partnerships*

296. *We will re-work this clause.*

**Miscellaneous**

*Why has section 578 of ICTA (Housing grants) not been rewritten?*

297. Section 578 of ICTA gives a general exemption from corporation tax and is not restricted to Trading Income or Property Income.

298. *We intend to rewrite section 578 of ICTA as part of the exempt income Part in Bill 5 as we did in ITTOIA (in section 769 of that Act).*