These notes refer to the Capital Allowances Act 2001 (c.2) which received Royal Assent on 22nd March 2001

CAPITAL ALLOWANCES ACT 2001

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Glossary

Part 2: Plant and machinery allowances

Chapter 2: Qualifying activities

Overview

127. This Chapter determines whether or not a person is carrying on a qualifying activity. This is a necessary condition of entitlement to plant and machinery allowances (see Chapter 1 of Part 2).

128. Section 15 lists the qualifying activities. It also points to provisions in Chapters 3 and 8 of Part 2 which affect particular qualifying activities.

129. The rest of this Chapter contains definitions of, and further provisions about, particular qualifying activities.

Section 15: Qualifying activities

130. This section is based on various sections of CAA 1990 which deem the activities listed to be trades. It also makes a minor change.

131. *Subsection (1)(f)* makes concerns listed in section 55 of ICTA a type of qualifying activity. The profits of these concerns are charged to tax under Case I of Schedule D by section 55(1) of ICTA but are not trades. As they are taxed under Schedule D they cannot be Schedule A businesses. That means Part II of CAA 1990 does not cater for them. This Act does so by making them qualifying activities. See *Change 1* in Annex 1.

132. *Subsection (1)(g)* provides for the management of an investment company to be a qualifying activity. It derives from section 28(1) of CAA 1990 which refers to "the management of the business of an investment company". This is new wording but is not a change. See *Note 8* in Annex 2.

133. The final words provide that an activity is only a qualifying activity to the extent that the profits or gains from it are chargeable to tax. They are based on section 83(2A) of CAA 1990. Exceptions to this rule can be found in Chapters 16, 17 and 20 of Part 2.

Section 16: Ordinary Schedule A businesses

134. This section defines "ordinary Schedule A business" for the purposes of this Part. This term is not used in CAA 1990. It is used in this Act to distinguish Schedule A businesses which are not furnished holiday lettings businesses from those which are.

Section 17: Furnished holiday lettings businesses

135. This section is based on section 29 of CAA 1990. It defines furnished holiday lettings businesses.

136. *Subsection (3)* applies the definition in section 504 of ICTA. This approach is taken here (and in some other places in the Act) in order to:

- make clear that precisely the same definition is used; and
- avoid duplication of legislation (with the risk that the definitions may diverge if one is amended but not the other by accident rather than design).

137. The vast majority of readers have access to that legislation. Increasingly they have electronic access (with hyperlinks to such cross-references). But for ease of reference in these notes:

Section 504 of ICTA (Supplementary provisions)

"(2) A letting—

(a) is a commercial letting if it is let on a commercial basis and with a view to the realisation of profits; and

(b) is of furnished accommodation if the tenant is entitled to the use of furniture.

(3) Accommodation shall not be treated as holiday accommodation for the purposes of this section unless—

(a) it is available for commercial letting to the public generally as holiday accommodation for periods which amount, in the aggregate, to not less than 140 days;

(b) the periods for which it is so let amount in the aggregate to at least 70 days; and

(c) for a period comprising at least seven months (which need not be continuous but includes any months in which it is let as mentioned in paragraph (b) above) it is not normally in the same occupation for a continuous period exceeding 31 days.

(4) Any question whether accommodation let by any person other than a company is, at any time in a year of assessment, holiday accommodation shall be determined—

(a) if the accommodation was not let by him as furnished accommodation in the preceding year of assessment but is so let in the following year of assessment, by reference to the 12 months beginning with the date on which he first so let it in the year of assessment;

(b) if the accommodation was let by him as furnished accommodation in the preceding year of assessment but is not so let in the following year of assessment, by reference to the 12 months ending with the date on which he ceased so to let it in the year of assessment; and

(c) in any other case, by reference to the year of assessment.

(5) Any question whether accommodation let by a company is at any time in an accounting period holiday accommodation shall be determined—

(a) if the accommodation was not let by it as furnished accommodation in the period of 12 months immediately preceding the accounting period but is so let in the period of 12 months immediately following the accounting period, by reference to the 12 months beginning with the date in the accounting period on which it first so let it;

(b) if the accommodation was let by it as furnished accommodation in the period of 12 months immediately preceding the accounting period but is not so let by it in the period of 12 months immediately following the accounting period, by reference to the 12 months ending with the date in the accounting period on which it ceased so to let it;

(c) in any other case, by reference to the period of 12 months ending with the last day of the accounting period.

(6) Where, in any year of assessment or accounting period, a person lets furnished accommodation which is treated as holiday accommodation for the purposes of this section in that year or period ("the qualifying accommodation"), he may make a claim under this subsection, within the time specified in subsection (6A) below, for averaging treatment to apply for that year or period to that and any other accommodation specified in the claim which was let by him as furnished accommodation during that year or period and would fall to be treated as holiday accommodation in that year or period if subsection (3)(b) above were satisfied in relation to it.

(6A) The time mentioned in subsection (6) above is—

(a) in the case of a claim for the purposes of income tax, the period ending with the first anniversary of the 31st January next following the year of assessment in which the accommodation was let;

(b) in the case of a claim for the purposes of corporation tax, the period of two years beginning at the end of the accounting period in which the accommodation was let.

(7) Where a claim is made under subsection (6) above in respect of any year of assessment or accounting period, any such other accommodation shall be treated as being holiday accommodation in that year or period if the number of days for which the qualifying accommodation and any other such accommodation was let by the claimant as mentioned in subsection (3)(a) above during the year or period amounts on average to at least 70.

(8) Qualifying accommodation may not be specified in more than one claim in respect of any one year of assessment or accounting period.

(9) For the purposes of this section a person lets accommodation if he permits another person to occupy it, whether or not in pursuance of a lease; and "letting" and "tenant" shall be construed accordingly.

138. *Subsection (4)* provides for all necessary apportionments under this Part if only part of accommodation is holiday accommodation.

Section 18: Management of investment companies

139. This section is based on section 28 of CAA 1990. It defines the qualifying activity of "management of an investment company".

140. Subsection (1) applies the definition of an investment company in ICTA. An investment company may carry on a trade or other qualifying activity. But subsection (2) provides that it is only a limited range of activities which are the "management of an investment company". These are activities expenditure on which would fall within "expenses of management" in section 75 of ICTA. This defines the qualifying activity for capital allowances in line with the treatment of expenses.

141. Section 28(1) of CAA 1990 refers to "the management of the business of an investment company". This has been shortened in this section and section 15(1)(g) to "management of an investment company". This does not change the effect of the legislation. See *Note 8* in Annex 2.

Section 19: Special leasing of plant or machinery

142. This section is based on section 61(1) of CAA 1990 and section 434E(2) of ICTA. It defines the qualifying activity of "special leasing" for plant or machinery which is hired out otherwise than in the course of any other qualifying activity.

143. *Subsection (1)* introduces and defines the term “special leasing”. This term is not used in CAA 1990. That provides for such an activity to be treated as a trade separate from any other trade the person carries on. Other provisions then have to refer to such activities in terms of the legislation which define them. For example in section 31(1)(c) of CAA 1990:

“the actual trade is not a separate trade which the shipowner is treated as carrying on by virtue of section 61(1).

144. The term “special leasing” allows more direct references – see for example section 128(2).

145. The section refers to “hiring out” plant or machinery. CAA 1990 refers to plant or machinery “let”. The use of the more colloquial phrase makes no practical difference. The section also omits the words in section 61(1) of CAA 1990 which provide that it does not matter whether the lessee does or does not carry on a qualifying activity. These are no longer needed. See *Note 9* in Annex 2.

146. *Subsection (3)* is based on section 61(1)(b) of CAA 1990. It states when the separate qualifying activity is permanently discontinued. This is not clear in CAA 1990. Section 61(1)(b) of CAA 1990 provides for the plant or machinery to be treated as being used wholly for purposes other than those of the deemed trade when the lessor permanently ceases to let the plant or machinery otherwise than in the course of a trade. This requires the lessor to bring a disposal event into account. But it does not explicitly provide for the deemed trade to be permanently discontinued. However, any other interpretation would leave the lessor with:

- no entitlement to a balancing allowance;
- entitlement only to writing-down allowances for an indefinite period, in ever decreasing amounts; and
- possibly allowances which are stranded because the lessor could only use them against income from letting the plant or machinery in question.

147. Subsection (3) accordingly reflects the alternative view that section 61(1) of CAA 1990 also provides for the deemed trade to end. See *Change 15* in Annex 1.

148. *Subsection (5)* is based on section 434E(2) ICTA. That (and section 434D ICTA) were introduced by section 51 of, and Schedule 8 to, FA 1995. As the legislation relates directly to capital allowances it is incorporated in this Act.

149. Section 61(8) of CAA 1990 is omitted from this section. It provides for a “lease” to mean also an agreement for a lease. It is now unnecessary except in relation to section 61(4) of CAA 1990 (see section 70 and paragraph 353 below).

Section 20: Employments and offices

150. This section is based on sections 198(2) and 314 of ICTA. It provides that some employments and offices are not qualifying activities as such.

151. *Subsection (1)* is based on section 314 of ICTA (divers and diving supervisors). Divers and diving supervisors operating in the North Sea normally have contracts of employment as a matter of general law. They would then be employees for tax purposes. But section 314 of ICTA provides that “the Income Tax Acts shall have effect as if” they were carrying on a trade. CAA 1990 is part of the “the Income Tax Acts” as defined in section 831(1)(b) of ICTA. So for the purposes of the capital allowances legislation North Sea divers have trades rather than employments. Subsection (1) puts this explicitly in terms of qualifying activities.

152. *Subsections (2)* and *(3)* are based on section 198(2) of ICTA. They exclude from plant and machinery allowances employments and offices which are taxed on the “remittance

basis" – that is, where only income remitted to the United Kingdom is taxed. Such remittances will already be net of any capital expenditure incurred out of that income.