ANNEX 2

NOTES ON TECHNICAL POINTS

Note 1 The rule that capital allowances have to be claimed: section 3(1)

Section 3(1) provides that no allowance is to be made unless a claim for it is made. This codifies the effect of *Elliss* v *BP Oil Northern Ireland Refinery Ltd.* (59 TC 474; (1987) STC 52 (CA)).

The *Elliss* case concerned assessments made for periods between 1967 and 1976. By the time the case came to be decided, the crucial provision, section 56(2) of FA 1965, had been consolidated as section 73(2) of CAA 1968. The court treated the consolidation as having reproduced the earlier legislation without making any changes. After *Elliss* was decided, section 73(2) was in turn consolidated, as section 144(2) of CAA 1990. *Elliss* is an authority on section 144(2) of CAA 1990 in the same way that it was an authority on section 73(2) of CAA 1968.

Section 144(2) of CAA 1990 provides—

> "Allowances and charges which fall to be made for any accounting period in taxing a trade under the provisions of Parts I to VI and this Part as they apply for the purposes of corporation tax shall be given effect by treating the amount of any allowance as a trading expense of the trade in that period, and by treating the amount on which any such charge is to be made as a trading receipt of the trade in that period."

It was argued by the Inland Revenue that, because trading expenses are automatically deductible in computing trading profits, the effect of making a capital allowance a trading expense was to obviate the need for the allowance to be claimed and to make it automatically deductible.

This argument was rejected by the Court of Appeal: a claim was still needed.

The reasoning was as follows. It was common ground that from 1945 to 1965 a taxpayer had the right to choose whether to take capital allowances, and it would have been surprising if this rule had been changed in 1965 by legislation which appeared merely to be making technical changes consequential on the introduction of corporation tax. There were numerous references in tax legislation to claims for allowances which implied that capital allowances had to be claimed; it was impossible to describe the retention of all these references as "slips" on the part of those involved in the drafting of the legislation. An allowance is "a thing allowed" which had the connotation that a claim was required. The legislation did not say that capital allowances should be deducted as trading expenses, but that they should be given effect by treating the amount of any allowance as a trading expense. This language was entirely consistent with the contention that allowances had to be claimed for the purposes of corporation tax and, if claimed, had to be given effect in a particular manner. The argument that the introduction in 1971 of a two year period for disclaiming a first-year allowance for plant or machinery was inconsistent with the need to claim a first-year allowance was rejected on the grounds that the disclaimer provision gave a two year period in which to disclaim a first-year allowance that had already been claimed.

At the time when *Elliss* was decided, the provisions for income tax were worded differently from those for corporation tax (and, as mentioned above, were assumed to require allowances to be claimed).

In 1994 the income tax provisions were amended and section 140(2) of CAA 1990 is now expressed in essentially the same terms as section 144(2). There is no doubt that the rule is the same for income tax purposes as it is for corporation tax purposes.

Note 2 Claims made outside company tax returns: section 3(5)

Section 3(5) applies paragraphs 54 to 60 of Schedule 18 to FA 1998 to certain claims. This spells out a point that may have become less apparent following amendments consequential on the introduction of self-assessment for companies.

Sections 17(3) and 145(3) of CAA 1990 used to provide for section 42 of TMA 1970 to apply to certain claims.

Paragraphs 4 and 7 of Schedule 11 to FA 1999 (which made amendments consequential on Schedule 18 to FA 1998) restricted section 17(3) of CAA 1990 to claims "made for the purposes of income tax" and repealed words in section 145(3) of CAA 1990 applying section 42 of TMA 1970.

The explanatory notes published by the Treasury in March 1999 described paragraph 4 of Schedule 11 as dealing with a reference to section 42 which was "unnecessary" for corporation tax purposes, and paragraph 7 of Schedule 11 as merely removing a reference to section 42 "which is now redundant".

But the effect of getting rid of the reference to section 42 without substituting an alternative reference to the relevant provisions of Schedule 18 to FA 1998 was that paragraph 79(1) of that Schedule might in theory appear to apply. Paragraph 79(1) requires a claim for capital allowances to be made by being included in the claimant company's tax return for the accounting period for which the claim is made.

However, the claims dealt with in sections 17 and 145(3) of CAA 1990 are about giving effect to allowances in earlier chargeable periods. In these circumstances, time may have run out for including the claim in the return.

It is clear from the explanatory notes just referred to that the amendments in 1999 were not intended to restrict the rights to make claims under sections 17 and 145(3) of CAA 1990. It would be perverse to read the 1999 amendments as having had this effect. So section 3(5) makes clear that a claim under the rewritten version of section 17 or 145(3) of CAA 1990 can still be made, even though it cannot be included in the return.

Note 3 Determining when capital expenditure is incurred by reference to an unconditional obligation to pay: section 5

Section 5(1) provides that an amount of capital expenditure is to be treated as incurred as soon as there *is* an unconditional obligation to pay it. The wording here is different from section 159(3) of CAA 1990, which refers to the date on which the obligation to pay the amount *becomes* unconditional.

The phrase "becomes unconditional", read literally, implies that there must have been a time at which the obligation to pay was conditional. Often this will be so. If a person agrees to buy machinery which has to be delivered, he is likely to be under a conditional obligation to pay for the machinery when the agreement is entered into, which becomes unconditional when he has had a chance to inspect the machinery to make sure that the seller has fulfilled his side of the bargain.

But it is not impossible to envisage circumstances where there is no room for the obligation to be conditional before becoming unconditional. If a person has a chance to make a thorough examination of machinery displayed for sale at a fixed price and then offers to buy the machinery on the spot, the obligation to pay under English law will normally be unconditional as soon as it comes into being (when the offer is accepted).

Section 159(3) of CAA 1990 derives from section 56(2) of FA 1985. *Ensign Tankers (Leasing) Ltd.* v *Stokes (Inspector of Taxes)* is authority for the proposition that "to incur" means "to render oneself liable to" (see [1989] 1 WLR 122 at 1240, (1989) STC 705 at 769 per Millet J). If, on a literal reading of section 159(3), the rule does not apply if the obligation is never conditional, the expenditure would be treated as incurred when the person rendered himself or herself liable to make the payment. So section 5(1) does not change the law.

Section 159 of CAA 1990 is applied by section 48 of F(No.2)A 1997; the latter is amended by paragraph 99 of Schedule 2. The point discussed in this note is relevant to section 48 as amended.

Note 4 Meaning of period of account: section 6(2)(b)

Section 6(2)(b) provides that "period of account" means, in the case of a person other than one entitled to an allowance in calculating the profits of his trade, profession or vocation, any tax year. This comes from section 160(5) of CAA 1990. (Section 160(5) refers to a "year of assessment" but "tax year" is meant to be merely a modernisation of "year of assessment".)

Section 160(5) of CAA 1990 in terms applies only to those entitled to allowances under Parts I to VI or Part VIII of CAA 1990. On the other hand, section 6(2) applies (for simplicity of drafting) for the purposes of the Act as a whole. It might be thought that this is a change in the law because section 160(5) seems not to apply in relation to research and development, know-how and patent allowances, whereas section 6 seems to do so.

But there is no change in the law for the reasons set out below. In short, this is because section 160(5) of CAA 1990 (and the definition in section 6(2)(b) of the Act) are not relevant to research and development and know-how allowances, whilst section 160(5) *does* apply in relation to patent allowances.

Entitlement to research and development allowances arises under Part VII of CAA 1990 whilst entitlement to know-how allowances arises under Chapter I of Part XIII of ICTA. But a person is only entitled to research and development or know-how allowances in calculating the profits of his trade and so section 160(5) of CAA 1990 and section 6(2)(b) are not relevant to those allowances.

Entitlement to patent allowances also arises under Chapter I of Part XIII of ICTA. Under section 532(1) of ICTA, the Tax Acts have effect as if sections 520 to 533 "were contained in the 1990 Act" (i.e., CAA 1990). The failure to say where in CAA 1990 they are to be treated as inserted means that it is not entirely clear, at the purely verbal level, whether section 160(5) is meant to apply to patent allowances. But it seems clear that it does.

Patent allowances fall to be made in respect of "chargeable periods" (see section 520(4) of ICTA). Section 161(2) of CAA 1990 defines "chargeable period" for the purpose of CAA 1990 as meaning an accounting period of a company or a period of account. Although "chargeable period" is also defined in section 832(1) of ICTA (to mean an accounting period of a company or a year of assessment), section 532(1) of ICTA displaces this definition and gives the term its CAA 1990 meaning in relation to patent allowances.

Subsection (1) of section 160 of CAA 1990 provides that in CAA 1990 "period of account" has (in relation to income tax) the meaning given by the other provisions of that section. Subsections (2) to (4) give the meaning in relation to allowances falling to be made in taxing a trade. Subsection (5), as mentioned above, gives the meaning for other cases, but is expressed only to apply to Parts I to VI and VIII of CAA 1990 (i.e., the whole Act other than Part VII).

It would be bizarre to conclude that chargeable period has the CAA 1990 meaning in relation to patent allowances (because defined for the purposes of CAA 1990) and that period of account—a component of the definition of chargeable period—has the CAA 1990 meaning in relation to taxing a trade (because defined for the purposes of CAA 1990), but that period of account does not have the CAA 1990 meaning in relation to other cases (because defined for the purposes of CAA 1990 except Part VII). This is particularly so given that section 160(5) is not relevant to Part VII for the reasons mentioned above.

In any event, section 528(2) of ICTA confirms that chargeable period in the case of non-trade patent allowances means year of assessment. That provision concerns the manner in which such allowances are given effect and refers expressly to allowances falling to be made "for any year of assessment".

The potential for confusion about the meaning of period of account in relation to patent allowances has arisen only as a result of the CAA 1990 consolidation. The reference in section 532(1) to the 1990 Act at large was substituted by paragraph 8(28)(a) of Schedule 1 to CAA 1990 for a reference to Part I of CAA 1968. The replaced reference was more precise. Treating the ICTA sections as included in Part I of CAA 1968 ensured that the precursor of section 160(5) of CAA 1990, section 72(4) of CAA 1968, applied for the purposes of patent allowances.

Given the legislative context, the legislative history and the presumption of interpretation that a consolidation has not changed the law, the only tenable interpretation of the legislation is that references to "chargeable period" in sections 520 to 533 of ICTA in relation to patent allowances include a period of account as defined by section 160(5) of CAA 1990.

Note 5 Coinciding periods of account: section 6(4)

Section 160(6) of CAA 1990 provides—

> "Any reference in this section to the overlapping of two periods shall be construed as including a reference to *the coincidence of two periods or to* the inclusion of one period in another, and references to the period common to both of two periods shall be construed accordingly."

But section 6(4) does not contain any words to reflect the reference in section 160(6) of CAA 1990 to the coincidence of two periods.

Section 160 of CAA 1990 was substituted by section 212(1) of FA 1994. Subsection (6) is the same in both versions of section 160. The italicised words were needed under the old version of section 160 but are redundant in the substituted version.

The main difference between the two versions of section 160 is that the old version identified the "basis period" whereas the new version identified the "period of account". Before the 1994 changes, allowances and charges were, for income tax purposes, made for a year of assessment but calculated by reference to expenditure or disposal events occurring in the basis period. After the 1994 changes, they are not only calculated by reference to, but also made for, a period of account. (See the different definitions of "chargeable period" in section 161(2) of CAA 1990 before and after the amendment made by section 212(2) of FA 1994.)

Under the old version of section 160, subsection (6) was glossing a reference in subsection (3)(a) to *overlapping basis periods*. Under the new version of section 160, subsection (6) was glossing a reference in subsection (3)(a) to *overlapping periods of account*.

Under the old version of section 160, subsection (2) provided that the basis period was the period on the profits of which income tax fell to be finally computed under Case I of Schedule D. Subsection (3)(a) provided that, for the purposes of subsection (2), where two basis periods overlapped, the period common to both was to be deemed to fall in the first basis period only. The coincidence of two basis periods—the words in issue in subsection (6)—could occur as a result of section 61 of ICTA (as it stood before the 1994 changes). This dealt with the opening years of trades, professions and vocations. Under section 61(1), where the trade had been set up and commenced within the year of assessment, the computation of profits could be made on the profits of that year. Under section 61(3), where the trade had been set up and commenced in the year preceding the year of assessment, income tax could be charged on the profits for one year from its first being set up. If the trade were commenced on 6th April, the reference to coinciding periods in section 160(6) of CAA 1990 would have ensured that for capital allowances purposes there was only one basis period.

Under the new version of section 160, subsection (2) provided that the period of account is any period for which accounts are made up. Subsection (3)(a) provided that, for the purposes of subsection (2), where two periods of account overlap, the period common to both was to be deemed to fall in the first period of account only.

The effect of the new subsection (2) was that it ceased to be possible for two periods of account to coincide. Even if two sets of accounts were to be made up for coinciding periods (which is most unlikely in practice) they would produce a single "period of account" for the purposes of section 160(2) without the need for section 160(6). So the omission of the reference to the coincidence of two periods cannot be regarded as changing the effect of the provision.

Note 6 Exclusion of double relief (patent and know-how allowances): sections 7(2) and 8(5)

Sections 7(2) and 8(5) provide that the rules designed to prevent a person obtaining double relief do not apply to patent and know-how allowances. They come from parts of section 147 of CAA 1990.

Section 147(1) prevents a person to whom an allowance has been made under Part I, III, IV, VI or VII of CAA 1990 from obtaining an allowance under any other of those Parts and from allocating any expenditure to a pool under Part II of CAA 1990. Section 147(2) prevents a person who has made use of Part II expenditure from obtaining an allowance under any other Part of CAA 1990.

Section 147 does not refer to allowances made under Chapter I of Part XIII of ICTA (patents and know-how). So they do not appear to be subject to section 147.

In Note 4 some reliance was placed on the correct construction of section 532(1) of ICTA in the light of its amendment by CAA 1990 and the presumption that a consolidation has not changed the law. CAA 1990 amended section 532(1) of ICTA so that the Tax Acts have effect as if sections 520 to 533 "were contained in the 1990 Act" (i.e., CAA 1990). Previously, section 523(1) had treated the same sections as if contained in Part I of CAA 1968 (a slightly different entity).

But the point made in Note 4 does not in any way help to establish that section 147 is meant to apply to patent and know-how allowances. Section 147(1) of CAA 1990 consolidated paragraph 28(1) of Schedule 13 to FA 1989. That referred to selected Chapters of Part I of CAA 1968 and certain other enactments, but not to sections 520 to 533 of ICTA, thus making it clear that paragraph 28(1) was not meant to apply in relation to patent and know-how allowances.

The nature of patents and know-how is such that it seems unlikely that the subject matter of patent and know-how allowances could in practice lead to claims for double relief.

Note 7 Ownership and belonging: section 11(4)(b) etc.

Section 11(4)(b) requires that a person "owns" plant or machinery as a result of the incurring of expenditure. The wording here is different from the corresponding wording in sections 22(1)(b) and 24(1)(b) of CAA 1990, which requires that machinery or plant "belongs" to a person in consequence of incurring expenditure. The change is intended to reflect the judicial view that in this context "owns" means the same as "belongs" and is clearer. Two cases can be adduced in support of this.

The first is *Stokes (HM Inspector of Taxes)* v *Costain Property Investments Ltd* ((CA) [1984] 1 WLR 763; [1984] STC 204); (1984) 57 TC 688)). The case concerned the interpretation of section 41(1)(b) of FA 1971, which was subsequently consolidated as section 22(1)(b) of CAA 1990. The case decided that plant or machinery consisting of fixtures did not "belong" to a lessee for the purposes of section 41(1)(b) of FA 1971, mainly because of section 46(2) of FA 1971 (subsequently section 61(4) of CAA 1990), which treated machinery or plant as "belonging" to a person, but only in limited circumstances not applicable in the case in question. In passing Goff LJ remarked—

> "I refer in particular to s 12 of the Customs and Inland Revenue Act 1878, which is the legislative ancestor of s 46(2), and which is the section in which, for the first time, the word "belongs" appears to have been used in the legislation . . . Why it was thought right by the legislature to use in that section (or indeed thereafter) the expression "belonging to" rather than "owned by" nobody could explain; but it is plain that that is what is meant . . . "

The second is *Melluish (HM Inspector of Taxes)* v *BMI (No. 3) Ltd and Others* (HL) [1994] 3 WLR 630; [1995] STC 964; (1995) 68 TC 1. The case concerned the interpretation of section 44(1)(b) of FA 1971, which was subsequently consolidated as section 24(1)(b) of CAA 1990. The House of Lords decided (among other things) that plant or machinery which had become a fixture "belonged" to the person who was absolute owner of the land to which the plant or machinery was fixed. The fact that a person who had paid for the fixture might have some equitable right in relation to it did not mean that it "belonged" to him. In passing Lord Browne-Wilkinson (with whom the rest of their Lordships concurred) remarked—

> "I, therefore, reach the conclusion that for the purposes of s 44 property belongs to a person if he is, in law or in equity, the absolute owner of it. Such a construction reflects the obvious, *prima facie*, meaning of the word: what belongs to me is what I own."

This remark supports the view that "own" and "belong" are, in the context of capital allowances, synonymous.

This change in terminology is adopted throughout the Act.

Note 8 Management of an investment company: sections 15(1)(g) and 18(1)

Sections 15(1)(g) and 18(1) refer to the "management of an investment company". In contrast, section 28(1) and (4) of CAA 1990 refers to the "management of <u>the business of</u> an investment company". But the words "the business of" in section 28(1) and (4) do not now achieve anything and to retain them would merely be confusing.

"The business of" used to be needed in section 28 of CAA 1990, before its substitution by paragraph 24 of Schedule 8 to FA 1995. Section 28 in its earlier incarnation provided for Part II of CAA 1990 to apply to a company carrying on the business of life assurance (as well as to an investment company). Insurance companies are subject to rules segregating different classes of business.

The substituted version of section 28 has many verbal similarities to the replaced version, except that it does not mention a company carrying on the business of life assurance. It seems likely that "the business of" was repeated from the previous version of section 28 without it being noticed that the reason for its inclusion had disappeared.

To retain "the business of" would be confusing because these words do not fit with section 75 of ICTA (which section 28(4) of CAA 1990 and section 18 plead into). Section 75 of ICTA refers to "the management of a company".

Note 9 Special leasing of plant or machinery: section 19

Section 19 may at first sight appear to differ in certain respects from section 61 of CAA 1990 but it is thought that there is no real difference in its legal effect.

Section 19 does not reproduce the words "whether or not it is used for the purposes of a trade carried on by the lessee" that are used in section 61(1) of CAA 1990.

These words come from section 46(1) of FA 1971. Section 46(1) of FA 1971 replaced, with modifications, section 42 of CAA 1968, which consolidated section 298 of ITA 1952. The words appeared in section 46(1) of FA 1971 as a result of the decision in *Macsaga Investment Co. Ltd.* v *Lupton* (1967) 44 TC 659 that there was an implication from the sections surrounding section 298 that section 298 applied only where the lessee was carrying on a trade. Words to the effect that special leasing applies whether or not the lessee is carrying on a qualifying activity are needed only if there is some contrary implication to be ousted. The legislative context has changed. There is now no contrary implication to be ousted. So leaving out the words does not change the effect of the provision.

Section 19 describes a "special leasing" of plant or machinery as "hiring out" plant or machinery otherwise than in the course of any other qualifying activity. In contrast, section 61(1) of CAA 1990 refers to the situation where plant or machinery is "let" to another.

However, since the reforms relating to property businesses made by FA 1997 and FA 1998, which led to the insertion of sections 28A and 161(2A) of CAA 1990 and the repeal of section 61(6) of CAA 1990, it has become apparent that for practical purposes the application of section 61(1) is confined to hiring out of plant or machinery otherwise than in the context of a lease of land. The consultation process that preceded the Act established that the references in section 61(1) to letting of plant or machinery are now regarded as misleading.

In their comments, consultees did not specifically consider whether the reference to letting in section 61(1) was intended to include letting of a ship or aircraft on charter and whether changing the terminology would change the effect of the provision in relation to charterparties.

A charterparty of a vessel "by demise" is regarded as a contract for the hire of the vessel as a chattel (which is subject to statutory implied terms which apply to the hire of goods): see, for ships, Halsbury's *Laws of England* Volume 43(2) (14th ed, 1997 reissue), paragraph 1414 and endnote 4. A similar point can be inferred in the case of aircraft from Halsbury's *Laws of England* Volume 2 (14th ed, 1991 reissue) paragraph 1337, endnote 2. So it would appear that "hiring out" can be read as embracing this kind of charterparty. But it seems unlikely, in the nature of things, that a charter by demise will be entered into otherwise than in the course of a qualifying activity, or, in the case of a life assurance company, otherwise than in the course of a Schedule A business or overseas property business.

Under a charterparty of a vessel otherwise than "by demise", the shipowner retains possession of the vessel through the master and crew, who continue to be his employees (see Halsbury's *Laws of England* Volume 43(2), paragraph 1415). Similarly, under a charterparty of an aircraft otherwise than by demise the crew of the aircraft remain the owner's servants (see Halsbury's *Laws of England* Volume 2, paragraph 1336). The phrase "hiring out" is perhaps somewhat less appropriate for a charterparty of this sort.

But whether "hiring out" is apt to include a charterparty otherwise than by demise is even more academic than whether it is apt to include a charterparty by demise. It is very difficult, given the fact that a charterparty is a mercantile document, to envisage circumstances in which a person could enter into a charterparty otherwise than by demise, and not be carrying on a qualifying activity (or, in the case of subsection (5) of section 19, still be a company carrying on a life assurance business).

The conclusion is, therefore, that it is safe to change the terminology as recommended by the consultees.

Note 10 Wording referring to section 10 of the Fire Precautions Act 1971: section 29(4)

Section 29(4) refers to a "prohibition notice" under section 10 of the Fire Precautions Act 1971 and to steps "to remedy the matters specified in the notice".

In contrast, section 69(2)(b) of CAA 1990 refers to an "order" under section 10 of the 1971 Act prohibiting or restricting the use of premises, and to steps "to enable the premises to be used without contravention of the order".

Section 69(2)(b) reproduces the wording of the provision from which it derives, section 15 of FA 1975, which in turn was appropriate for section 10 of the Fire Precautions Act 1971 as enacted. But before the capital allowances legislation was consolidated as CAA 1990, a new version of section 10 of the 1971 Act had been substituted by section 9(1) of the Fire Safety and Places of Sport Act 1987.

In an ideal world, the 1987 Act would have made a consequential amendment of section 15 of FA 1975. When the consolidation which became CAA 1990 was being prepared, it would have been open to the consolidator to propose a change in the wording to reflect the wording in the new version of section 10 of the 1971 Act, because this is the sort of point that is often dealt with under the consolidation process.

Under section 17(2) of the Interpretation Act 1978—

> "Where an Act repeals and re-enacts, with or without modification, a previous enactment, then, unless the contrary intention appears—
>
> (a) any reference in any other enactment to the enactment so repealed shall be construed as a reference to the provision re-enacted; . . ."

So there is no real doubt about the legal effect of section 69(2)(b) of CAA 1990. The change in wording in section 29(4) is merely a matter of bringing the wording of the legislation into line with its actual legal effect.

Note 11 Personal security and "relevant qualifying activity": section 33(1)(b), (2)(a) and (8)

Section 33(1)(b) and (2)(a) refers to a "relevant qualifying activity". Section 33(8) defines "relevant qualifying activity" as a trade, an ordinary Schedule A business, a furnished holiday lettings business, an overseas property business or a profession or vocation.

This is based on section 71(1)(a) of CAA 1990, which refers to a "trade, profession or vocation". The following paragraphs explain why the list in section 33(8) can be regarded as reproducing the effect of the reference in section 71(1)(a) of CAA 1990 to a "trade, profession or vocation".

Section 27(1) of CAA 1990 applies the provisions of Part II to "professions, employments, vocations and offices" as they apply to trades "except as otherwise provided". The necessary implication of section 71(1)(a) of CAA 1990 in referring to a trade, profession or vocation, is that employees and office holders are excluded: section 71(1)(a) is providing otherwise. This justifies the exclusion of employments and offices from the list of "relevant qualifying activities".

Section 28 of CAA 1990 applies the provisions of Part II to investment companies. But section 71 of CAA 1990 applies to individuals and partnerships only. This justifies the exclusion of the management of an investment company from the list of "relevant qualifying activities".

Sections 28A, 29 and 161(2A) of CAA 1990 between them apply Part II to Schedule A businesses, furnished holiday lettings businesses and overseas property businesses. These have been included in the list of "relevant qualifying activities". This is thought to preserve the effect of the law.

Sections 28A, 29 and 161(2A) of CAA 1990 are not qualified by the words "except as otherwise provided" (or anything similar). The references to a "profession or vocation" do not create a necessary implication that these various property businesses are excluded.

But there is a strong reason for concluding that they are included.

Section 71 of CAA 1990 derives from section 117 of FA 1989. Sections 112 and 113 of FA 1989 provide for deductions of expenditure on security assets as a revenue expense. The effect of sections 21A(2) and 65A(5) of ICTA is that sections 112 and 113 apply to Schedule A businesses and overseas property businesses, and, because furnished holiday businesses are a sub-category of Schedule A business, to them as well.

The natural inference is that the scope of sections 112 and 113 of FA 1989 (revenue deductions for security expenses) and section 71 of CAA 1990 (capital allowances for security expenses) is meant to be the same.

Note 12 Expenditure on plant or machinery for use in dwelling-houses: section 35(3)

Section 35 excludes certain expenditure from being "qualifying expenditure" if it is incurred on the provision of plant or machinery for use in a dwelling-house. It is based on sections 28A(3) and 61(2) of CAA 1990 (read with section 161(2A) in so far as the exclusion relates to an overseas property business).

Section 35(3) provides for apportionment of expenditure which is incurred on plant or machinery partly for use in a dwelling-house and partly for other purposes. This reflects section 28A(4) of CAA 1990 but section 61 of CAA 1990 contains no provision equivalent to section 28A(4).

However, the same effect is achieved, for all practical purposes, by section 79 of CAA 1990, which enables allowances to be apportioned where expenditure is incurred partly for the purposes of trade (in the Act's terminology, a qualifying activity) and partly for other purposes. So the fact that section 35(3) extends to situations formerly dealt with by section 61 of CAA 1990 does not change the effect of the legislation.

Note 13 "Wear and tear" and "depreciation": section 37 and Chapter 16 of Part 2

Section 37 and Chapter 16 of Part 2 refer to "depreciation" instead of "wear and tear", the phrase used in section 80 of CAA 1990. The word "depreciation" is regarded as more modern and is preferred by users of the legislation.

"Depreciation", on its own, seems to go wider than "wear and tear". "Depreciation" is apt to include the kind of loss of value that an asset can suffer even though it has not suffered any physical deterioration. (For instance, a person who buys a new car may find that the value of the car has gone down overnight simply because the car is no longer brand new.)

So at first sight, the change in wording might appear to change the effect of the provisions. However, the word "depreciation" in section 37 and in Chapter 16 of Part 2 is qualified by the words "resulting from its use". This is a modernisation of the words "occasioned by its use" in section 80 of CAA 1990.

The additional words (whether they are "resulting from its use", or "occasioned by its use") make clear that the loss of value must be caused by "use" of the plant or machinery. "Use" is unlikely to cause a lowering of value without the plant or machinery suffering some "wear and tear". It is thought, therefore, that the change in wording has not brought about a real change in the effect of the provisions.

Note 14 Change in the nature of a trade or business: section 46(2), general exclusion 7

Section 46(2), general exclusion 7, is based on section 22(6C) of CAA 1990 (which provides for an exclusion from entitlement to first-year allowances). It, like section 22(6C), refers to the situation where the provision of the plant or machinery is "connected with a change in the nature or conduct of a trade or business".

As a result of section 83(2A) of CAA 1990 the reference in section 22(6C) to a trade is to be construed as if activities were capable of being comprised in a trade, or of being treated as a trade, to the extent only that they are activities the profits or gains of which are, or (if there were any) would be, chargeable to income tax or corporation tax.

Elsewhere this limitation is reflected in the rewritten legislation by converting references to a trade to references to a qualifying activity: section 15(1) restricts the meaning of "qualifying activity" in the same way as section 83(2A) of CAA 1990 restricts the meaning of "trade". By not referring in section 46(2) to a qualifying activity, and retaining the reference to a trade, the section might appear to go wider than section 22(6C) of CAA 1990, since there is nothing in the Act to limit the meaning of "trade" to trades with profits chargeable to tax.

However, this does not in fact change the real effect of the provision, and the advantage of not, in this instance, translating the reference to a trade into a reference to a qualifying activity is that it preserves some other effects of section 22(6C) of CAA 1990 without unduly complicating the drafting.

The word "business" is recognised as having a wider meaning than the word "trade" (see *American Leaf Blending Co Sdn Bhd* v *Director General of Inland Revenue* [1979] AC 676 at 684, per Lord Diplock) and as covering "almost anything which is an occupation as distinct from a pleasure" (*Rolls* v *Miller* [1884] 27 Ch D 71) or "an active occupation . . . continuously carried on" (*IRC* v *Marine Steam Turbine Co* [1920] 1 KB 193 at 202 to 203). The result is that it is extremely difficult to think of a trade that is not also a business. So, under section 22(6C) of CAA 1990, a change in the nature or conduct of a trade without profits chargeable to tax would be caught by the word "business" even though (since FA 2000) it is not caught by the word "trade".

It is fairly clear that the phrase "trade or business" in section 22(6C) of CAA 1990 is not apt to include an employment or office. Section 27(1) of CAA 1990 provides that Part II of CAA 1990 applies to professions, employments, vocations and offices as it applies to trades "except as otherwise provided". The implication of the express reference in section 22(6C) to a "business" is that the word "trade" in this specific context does not include an occupation which cannot be described as a business. Despite the width of the word "business", it does not seem apt to include an employment or office. But it would complicate general exclusion 7 unduly to refer to a qualifying activity other than an employment or office.

Another reason for retaining the reference to a "trade or business" is that it preserves the read-across to other statutory provisions which refer to a "major change in the nature or conduct of a trade or business" (see for example sections 767A, 768 and 768A of ICTA). This read-across cannot be preserved except by retaining "trade or business".

Note 15 Claim for first-year allowance in respect of part of expenditure: section 52(4)

Section 52(4) permits a person who is entitled to a first-year allowance to claim the allowance in respect of part of the expenditure qualifying for the first-year allowance as well as in respect of all of it. There is no provision in precisely these terms in CAA 1990. But section 52(4) reflects the effect of sections 22(7), 25(4) and 30(1)(b) of CAA 1990.

Section 22(7) of CAA 1990 enables a person claiming one or more first-year allowances to require the amount of the allowance, or the aggregate of the allowances, to be reduced to a specified amount. Section 30(1)(b) of CAA 1990 makes corresponding provision for first-year allowances in respect of expenditure on ships, which are excluded from section 22(7) by section 22(8). There is nothing in the Act directly corresponding to sections 22(7) and 30(1)(b) of CAA 1990.

Looked at in isolation, sections 22(7) and 30(1)(b) of CAA 1990 appear to mean that, if a first-year allowance is claimed, it must be claimed in respect of all the expenditure that qualifies for it, but that the amount of the allowance in respect of that expenditure can be reduced. If that was right, it would mean that all the expenditure qualifying for first-year allowances would be prevented from forming part of the expenditure qualifying for writing-down allowances by section 25(1)(a)(ii) of CAA 1990.

In contrast, if, under section 52(4), a first-year allowance is claimed in respect of only part of the expenditure qualifying for it, there is now nothing to prevent the rest of the expenditure from being allocated to a pool for the purpose of forming part of the expenditure qualifying for a writing-down allowance.

But a similar result is already achieved in CAA 1990 by section 25(4). That provides that, where the amount of a first-year allowance is reduced under section 22(7) or 30(1)(b), the part of the expenditure proportionate to the reduction in the allowance "shall be treated" as not being expenditure in respect of which a first-year allowance is or could be made. The effect of this is that the part of the expenditure is not prevented by section 25(1)(a)(ii) from being qualifying expenditure for writing-down allowance purposes. So the effect is the same as if the first-year allowance had been claimed in respect of only the other part of the expenditure.

Note 16 No unrelieved qualifying expenditure to be carried forward from final chargeable period: section 59(3)

There is nothing in CAA 1990 that corresponds precisely to section 59(3). But section 59(3) achieves results that are achieved under CAA 1990 by a different route.

Section 24(1) of CAA 1990 limits the making of allowances and charges to cases where the person concerned is carrying on a trade. The trade referred to could be either a real trade (or business) or one of the notional trades used to segregate special categories of expenditure (i.e., to create what practitioners and the Act call pools).

The final chargeable period under Part 2 corresponds to the notion in Part II of CAA 1990 of the chargeable period in which the trade is permanently discontinued. (The provisions which determine when the notional trade is to be treated as permanently discontinued are discussed in Change 15.)

If under Part II of CAA 1990 a person's actual or notional trade has been permanently discontinued, there is no further entitlement to allowances in respect of that trade. Any outstanding expenditure will have been returned to the person by way of a balancing allowance. There is no expenditure to carry forward and the actual or notional trade which brought the person within section 24(1) has vanished.

Section 59(3) produces the same effect but in a more direct way.

Note 17 Disposal value in the case of certain sales: sections 61, Table, item 2 and 423, Table, item 2

Item 2 in the Table in section 61 provides for the disposal value, in the case of certain sales, to be the market value of the plant or machinery at the time of the (actual) sale.

In contrast, section 26(1)(b) of CAA 1990 does not explicitly give the time at which the market value has to be ascertained as the time of the sale. But there can be no real doubt that this is how section 26(1)(b) is meant to apply.

When the disposal values in section 26(1) are put in tabular form, the contrast between the rule provided in section 26(1)(b) (which does not expressly refer to the time at which the market value is to be ascertained) and section 26(1)(f) (which does) becomes much more noticeable. There is a much greater risk that a difference in wording in the similar items in the table would be regarded as intentional.

So it is thought the true effect of CAA 1990 is better reflected by including the words "at the time of the sale" in item 2, rather than by slavishly following the absence of any such words in section 26(1)(b).

The same point arises in relation to item 2 in the Table in section 423. This is based on section 99(3) of CAA 1990 which borrows section 26 for the purposes of dealing with disposal values in connection with Part IV.

Note 18 Meaning of "relevant qualifying activity" in connection with gifts to charities, etc.: section 63(3)

Section 63(3) identifies the qualifying activities that enable a person to take advantage of the nil disposal value rule applicable to gifts to charities and similar bodies (discussed in Change 12). It comes from sections 83A and 84 of ICTA, which confer the relief on a "trade, profession or vocation". This note explains the reasons for the inclusions and exclusions in the list in section 63(3).

Section 27(1) of CAA 1990 provides for Part II of CAA 1990 to apply to professions, employments, offices and vocations as it applies to trades "except as otherwise provided". The necessary implication of the reference to a "profession or vocation" in sections 83A and 84 of ICTA is that employments and offices are excluded. (The same point is discussed in Note 11.) Furthermore, section 27(1) applies only the provisions of Part II of CAA 1990. It does not apply any provisions of ICTA. So employments and offices are not included in the list of relevant qualifying activities in section 63(3).

Section 61(1) of CAA 1990 treats the activity in question (in the Act called "special leasing") as a trade for the purposes of Part II. It does not treat the activity as a trade for the purposes of sections 83A and 84 of ICTA. So the qualifying activity of special leasing is not included in the list of relevant qualifying activities in section 63(3).

Sections 28(1), 28A(1) and 29(1) of CAA 1990 are a little more difficult, because they provide for the activities in question (managing an investment company, a Schedule A business or a furnished holiday lettings business) to be treated as a trade for the purposes of Part II of CAA 1990 and other provisions of the Tax Acts so far as relating to allowances and charges under Part II. Section 63(3) includes the various property businesses as relevant qualifying activities, but does not include investment companies.

This is because "trade" in sections 83A and 84 of ICTA must have the same meaning throughout; the meaning cannot be intended to chop and change as the reader moves through the subsections. The following paragraphs explain this point in more detail.

The relief in sections 83A(3)(b) and 84(3)(b) of ICTA for capital allowances purposes is accompanied by parallel provisions in sections 83A(3)(a) and 84(3)(a) relieving the donor from having to bring into account a trading receipt as a result of the disposal of the article. The consequential amendments made by the Act leave this latter relief where it is in ICTA (since it has nothing to do with capital allowances).

It would be very odd if the relief for trading stock were meant to apply to a narrower class of businesses than the relief for the purposes of plant and machinery allowances. To put it another way, "trade" must have the same meaning for the purposes of sections 83A(3)(b) and 84(3)(b) as it has for the purposes of sections 83A(3)(a) and 84(3)(a).

There is nothing in ICTA to extend the application of sections 83A(3)(a) and 84(3)(a) to managing an investment company.

But section 21A of ICTA (which applies to overseas property businesses under sections 65A(5) and 70A(5) of ICTA) extends sections 83A and 84 to a Schedule A business (including a furnished holiday lettings business) and an overseas property business. This is clear from the express reference in section 21A(2) of ICTA to Chapter V of Part IV (sections 83A and 84 are in that Chapter).

Note 19 Contribution to car above the cost threshold: section 76(3) and (4)

Subsections (3) and (4) of section 76 are based on section 35(1) of CAA 1990. Section 35(1) effectively creates a special pool for a contribution to a car costing more than £12,000 (it provides for a separate trade, the device used in CAA 1990 to produce a pool). But section 76 does not create a special pool for this kind of contribution.

However, there is in fact no longer any need for this special pool as a result of a change later on in the Act. Part 11 now makes clear (in contrast with section 155(6) of CAA 1990) that a contributor's pool is a "single asset pool". This point is discussed in Change 60. Once it is clear that a contributor has a "single asset pool" there is no need for a further special pool for a contribution to a car costing more than £12,000.

Note 20 Final chargeable period and the single asset pool for a car above the cost threshold: section 77(1)

Section 77(1) provides that in the case of a single asset pool for a car above the cost threshold, there is no final chargeable period merely because the car begins to be used for purposes other than those of the qualifying activity.

In contrast, section 34(2)(b) of CAA 1990 uses words typically used to create what the Act calls a "final chargeable period". That is—

> ". . . without prejudice to section 24(6)(c)(i) to (iii), the separate trade is permanently discontinued when the motor car begins to be used wholly <u>or partly</u> for purposes other than those of the actual trade . . ."

The function of these words in CAA 1990 is discussed in Change 15. The significance of the trade being "permanently discontinued" is that there is an entitlement to a balancing allowance under section 24(2)(b) of CAA 1990. The significance of "the final chargeable period" is the same. It is the chargeable period in which a person may be entitled to a balancing allowance.

Section 77(1) therefore might appear to change the law, since it prevents a balancing allowance arising where the car begins to be used <u>partly</u> for the purposes other than those of the qualifying activity, whereas section 34(2)(b) of CAA 1990 appears to enable a balancing allowance to be obtained.

But when section 34 of CAA 1990 is read as a whole, the irresistible conclusion is that a balancing allowance is not meant to be available in such circumstances. This is because section 34(5) provides for allowances to continue to be made for the chargeable period when the change of use occurs and for subsequent chargeable periods, subject to a just and reasonable reduction to take account of the mixed use. So the only possible inference is that the words “or partly” in section 34(2)(b) were included by mistake.

Note 21 Calculation of unrelieved qualifying expenditure for single asset pool for car above cost threshold: sections 77(4) and 78(3)

Sections 77(4) and 78(3) deal with a situation where a car above the cost threshold is used partly for purposes other than those of the qualifying activity or the person carrying on the qualifying activity receives a partial depreciation subsidy. In both these situations, writing-down allowances are subject to a just and reasonable reduction.

Sections 77(4) and 78(3) provide that in calculating the amount of unrelieved qualifying expenditure carried forward, any reduction in the writing-down allowance is to be disregarded.

This is based on section 34(5) of CAA 1990. Section 34(5) does not contain such an explicit statement of its inter-relationship with section 25(1)(b) of CAA 1990. (Section 25(1)(b) is the equivalent of what is dealt with in the Act as the carrying forward of unrelieved qualifying expenditure.)

Section 25(1)(b) carries forward the balance of the excess expenditure from the preceding period “after deducting any writing-down allowances made”. Section 34(5) provides that in the situations referred to above (mixed use and so on) “instead of there being made . . . the allowance or charge . . . which would fall to be made . . . there shall be made so much of that allowance or charge as . . . would be just and reasonable . . .”.

In terms this seems to produce the result that the allowance is reduced, and the expenditure to be carried forward is the balance after deducting the reduced allowance. So sections 77(4) and 78(3) seem to change the law. But the real effect is no different. If more expenditure is carried forward, the just and reasonable reduction for the next chargeable period under section 79 of CAA 1990 would have to have been greater.

Note 22 Long-life asset pool, overseas leasing pool and special leasing: sections 101(2), 102(2), 107(2) and 109(3)

Sections 101(2), 102(2), 107(2) and 109(3) are drafted on the basis that a qualifying activity of special leasing can have a long-life asset pool or an overseas leasing pool. The result is that the qualifying expenditure incurred in the qualifying activity will be subject to the reduced rates (of 6% and 10%) applicable to the long-life asset and overseas leasing pools. (See sections 102 and 109.)

This takes a different approach from CAA 1990, which in effect excludes the special leasing case from the provisions which effectively produce long-life asset and overseas leasing pools, but then nevertheless applies the reduced rates (of 6% and 10%) applicable to the long-life asset and overseas leasing pools to the special leasing case.

Although the conceptual approach is different, the effect is the same.

The following paragraphs give details of how CAA 1990 achieves the results mentioned in the last paragraph but one.

For long-life assets, the exclusion of special leasing expenditure from long-life asset pools is achieved by section 38E(6) of CAA 1990 and the application of the 6% rate to special leasing expenditure is achieved by section 38F(1)(b) of CAA 1990. (The provisions do not talk about pools, as such: they talk about separate trades.)

For overseas leasing, the application of the 10% rate to special leasing expenditure is achieved by section 42(2)(e) of CAA 1990 (which refers to section 61 of CAA 1990); and the fact that special leasing expenditure is not meant to be sucked into an overseas leasing pool follows from the fact that section 42(2) refers to section 61 (where special leasing comes from) as well as to section 41 of CAA 1990 (the basis for the overseas leasing pool).

Note 23 Application of 6% and 10% rates to contributor's single asset pool: sections 102(2) and 109(3)

Sections 102(2) and 109(3) provide that the 6% and 10% rates of writing-down allowances apply to long-life asset expenditure and certain expenditure on overseas leasing even if the expenditure is in a single asset pool.

In contrast, sections 38F(2) and 42(2) of CAA 1990, which deal with the application of the 6% and 10% rates, do not mention the provisions relating to contributions (sections 154 and 155 of CAA 1990).

The contributor's pool is the subject of discussion in Change 60 about whether the effect of section 155(6) is to create what is commonly known as, and is referred to in the Act as, a single asset pool. But that debate is, in fact, irrelevant to the interaction under CAA 1990 of sections 38F(2) and 42(2) with section 155(6).

Section 155(6) treats the contributor, for the purposes of sections 24, 25 and 26 of CAA 1990, as if the contribution was made for the purposes of a separate trade. It is thought that this notional separate trade can be the trade for the purposes of sections 38E(1) and (2) and 41 of CAA 1990, so as to create a pool (or, as CAA 1990 has it, another separate trade) for long-life asset expenditure and certain overseas leasing expenditure.

The compelling evidence in favour of this view, in relation to long-life assets, is section 38E(6) of CAA 1990. Section 38E(6) ensures that the notional trades created by sections 31, 61, 79 and 80 of CAA 1990 cannot be used to create a pool (or another separate trade) for long-life asset expenditure under section 38E. The implication is that the separate trade created by section 155(6) can generate a section 38E pool.

Similarly, section 41(6) of CAA 1990 lists the circumstances in which section 41 does not apply. Sections 154(2) and 155(6) do not figure in the list. The implication is that section 41 can apply in such circumstances, if the expenditure is expenditure on the provision of plant or machinery for the relevant kind of overseas leasing.

Note 24 The notional written-down value: sections 104(3), 197(3) and 222(3)

Sections 104(3), 197(3) and 222(3) define what is meant by the "notional written-down value" of plant or machinery or expenditure on plant or machinery. They come from sections 38G(2) and (3), 59A(2) and (3) and 76A(9) and (10) of CAA 1990.

The CAA 1990 sections define the notional written-down value as the amount which, if it were a disposal value and certain assumptions were made, would give rise to neither a balancing allowance nor a balancing charge.

The rewritten provisions define the notional written-down value in terms of the formula QE - A. "QE" stands for the expenditure on the plant or machinery in question and "A" stands for the total of all the allowances that could have been made in respect of that expenditure, on certain assumptions.

Under both the old and the new provisions, the assumptions to be made in determining the notional written-down value are, broadly, that the expenditure on the plant or machinery is the only expenditure to be taken into account for capital allowances purposes and that all the allowances that would have been available on that basis have been made.

On those assumptions, a disposal value would give rise to neither a balancing allowance nor a balancing charge if it were equal in amount to the expenditure left in the "pool". This is the expenditure on the plant or machinery (to the extent that it qualifies for capital allowances) less the allowances that could have been made in respect of it

So, in defining the notional written-down value as expenditure less allowances that could have been made, the Act reflects the effect of CAA 1990.

Note 25 Letting an aircraft on charter: section 105(1)(a)

Section 105(1)(a) glosses the meaning of "leasing" so that it includes "letting a ship *or aircraft* on charter . . ." In contrast, section 50(2) of CAA 1990, on which section 105(1)(a) is based, refers only to letting a ship on charter.

The purpose of the reference in section 50(2) of CAA 1990 to letting a ship on charter seems to have been to make clear that "leasing" includes letting of a ship on charter even if the charterparty is not "by demise". The usual characteristic of a "lease" is that the lessor parts with possession. So there is room for doubt about whether "lease" is appropriate to include a charterparty otherwise than by demise (cf. Note 9).

If this is so, the omission of a reference to "aircraft" would appear to suggest that letting an aircraft on charter otherwise than by demise is not subject to the regime in Chapter V of Part II of CAA 1990.

But this cannot be the intention of the legislation. Section 39 of CAA 1990 identifies what are "qualifying purposes" for the purposes of Chapter V of Part II. One of the qualifying purposes is letting a ship or aircraft on charter in specified circumstances. (See section 39(7) of CAA 1990, or, in the Act, section 123(2).) The circumstances specified are essentially those in which a shipowner or aircraft owner resident in the United Kingdom enters into a voyage or time charter (or a "wet lease")—i.e., charterparties which are not by demise. There would be no need to identify a subset of chartering aircraft otherwise than by demise as a qualifying purpose if chartering otherwise than by demise were not included in the first place.

The historical explanation for the absence of the words "or aircraft" in section 50(2) of CAA 1990 appears to be that the provisions (which come originally from sections 67 to 73 of FA 1980) were applied to aircraft at a very late stage in the preparation of the legislation and the desirability of revising the precursor of section 50(2) (section 73(3) of FA 1980) by adding a reference to "aircraft" was probably overlooked.

Note 26 "Profits chargeable to tax": section 105(3)

Subsections (3) and (4) of section 105 are based on the words in parentheses in section 42(1)(b) of CAA 1990 and on section 50(3A) of CAA 1990.

Section 42(1)(b) of CAA 1990 refers to "profits chargeable to tax (whether as profits arising from a trade carried on in the United Kingdom or by virtue of section 830(4) of the principal Act)".

Section 105(3) treats part of the words in parentheses in section 42(1)(b) of CAA 1990 as equally applicable to the references to profits chargeable to tax in sections 43(2) and 44(2)(a) of CAA 1990. It does not reflect some of those words. It replaces "whether as profits arising from a trade carried on in the United Kingdom or by virtue of" by "includes profits chargeable under". The basis on which this is done is that, as in the case of other "whether or not" phrases, there is very little weight on these words. They are marginally helpful for the avoidance of doubt. But to the extent that they are helpful, they need to be made applicable to "profits chargeable to tax" where it appears elsewhere.

Section 50(3A) of CAA 1990 provides that references in the Chapter to profits <u>or gains</u> chargeable to tax shall not include any of those arising to a person who, under arrangements specified in an Order in Council making any such provisions as are referred to in section 788 of the principal Act (double taxation arrangements), is afforded, or is entitled to claim, any relief from the tax chargeable thereon.

None of the provisions of CAA 1990 rewritten in the Act refer to "profits <u>or gains</u> chargeable to tax". The provisions rewritten in the Act that require the gloss in section 50(3A) are those referring to "profits chargeable to tax". (See sections 42(1)(b), 43(2) and 44(2)(a).) So the word "gains" in section 50(3A) has become redundant and can safely be omitted.

Note 27 Recovery mechanism where allowances prohibited: section 114(2)(b)

Section 114 provides recovery provisions for the situation where a person has obtained an allowance in respect of expenditure on plant or machinery and then, during the designated period, the plant or machinery is used for the kind of leasing where allowances are prohibited under section 110.

Section 114(2)(a) makes the person concerned liable to a balancing charge equal to any allowances that have been previously given and not recovered. This reflects section 42(4) of CAA 1990. Section 114(2)(b) also requires the person concerned to bring a disposal value into account.

This does not effect a real change. One might at first think that, in the absence of section 114(2)(b), a person could be left with expenditure on which he could claim allowances. But this would not be so. Section 110 would apply to ensure that allowances on that expenditure were prohibited. All that section 114(2)(b) does is take the expenditure out of the pool, rather than leave it in there as "dead" expenditure. This seems simpler and clearer. But there is no difference of substance.

Note 28 Joint lessees and overseas leasing: omission of section 43(5) of CAA 1990 from section 116

Section 116 does not reproduce section 43(5) of CAA 1990.

Section 43(5) of CAA 1990 provides—

> "(5) Any first-year allowance made in respect of expenditure to which section 22 applies by virtue only of subsection (3C), (3CA), (3D) or (3E) of that section shall be made on the same assumptions and subject to the same apportionments (if any) as it appears would, by virtue of subsection (3) above, be applicable in the case of a writing-down allowance."

Section 22(6B)(d) of CAA 1990 prevents first-year allowances being given in respect of expenditure incurred on providing plant or machinery for any kind of leasing. There is nothing in section 43(5) to override the restriction in section 22(6B). So there appear to be no circumstances in which section 43(5) can operate. It is unnecessary and to include anything in the Act to reflect it would be misleading.

Note 29 Recovery of allowances in case of joint lessees—addition of words in section 117(1)

Section 117(1) provides for recovery of allowances where (broadly speaking)—

a lessor to joint lessees has obtained normal writing-down allowances reflecting the extent to which the joint lessees are expected to use plant or machinery for the purpose of earning profits chargeable to tax, but

in the event, none of the joint lessees use the plant or machinery for that purpose.

The end of section 117(1) provides—

> "sections 111 and 112 (recovery of excess allowances) apply as if the plant or machinery or (as the case may be) the separate item of plant or machinery referred to in section 116(5)(a) had at that time begun to be used for overseas leasing which is not protected leasing."

In contrast, the relevant part of section 44(2) of CAA 1990, on which section 117(1) is based, provides—

> "sections 46 . . . shall have effect as if the separate item of machinery or plant referred to in section 43(3)(a) had at that time begun to be used for the purpose of being leased to a non-resident, otherwise than by permitted leasing."

The purpose of this note is to explain why the words "the plant or machinery or (as the case may be)" have been added in section 117(1).

Section 44(2) of CAA 1990 applies in a case where—

> "by virtue of section 43(2), the whole or part of the . . . expenditure has qualified for a normal writing-down allowance. . ."

But a separate item of plant or machinery is brought into being under section 43(3)(a) of CAA 1990 (in order to produce an apportionment) only for the case where—

> ". . . part only of the expenditure . . . is treated as not falling within section 42(1) . . ."

It is clear that either the reference in the opening words of section 44(2) of CAA 1990 to "the whole or" is wrong or the bare reference in the concluding words of section 44(2) to the separate item of machinery or plant (without any reference to the actual plant or machinery) is wrong.

So there is a choice as to whether the words "the whole or" at the beginning should be regarded as surplus or whether "the plant or machinery or (as the case may be)" should be added at the end. It would not make any sense to rewrite section 44(2) of CAA 1990 as it stands.

There are other references in sections 43 and 44 of CAA 1990 to cases where the whole of the expenditure has qualified for a normal writing-down allowance under section 43(2). See sections 43(4)(b) and 44(3) and (4). (Section 43(4) is now needed only for first-year allowances arising because of an additional VAT liability, and so is dealt with in paragraph 47(7) of Schedule 3.)

If the opening words of section 44(2) of CAA 1990 are wrong, the other references to the whole of the expenditure in sections 43(4)(b) and 44(3) and (4) must also be wrong. It seems implausible that all these references to the whole of the expenditure are wrong.

It may not be immediately apparent in what circumstances a lessor could lease to joint lessees as described in section 43(1) of CAA 1990 and end up being entitled to normal writing-down allowances on <u>the whole</u> of the expenditure under section 43(2).

But it could happen if, for example—

> one of the joint lessees is not resident in the United Kingdom and uses machinery partly for the purpose of earning profits which are chargeable to tax and partly for non-profit earning purposes, and
>
> all the other joint lessees use the machinery for the purpose of earning profits which are chargeable to tax.

So the conclusion is that section 44(2) of CAA 1990 should be read as if it referred to the plant or machinery as well as to "the separate item of plant or machinery". Section 117(1) reflects this interpretation.

Note 30 The appropriate non-ship pool: section 127(3)

Under section 127(1), qualifying expenditure on the provision of a ship is generally required to be allocated to a single asset pool. But there are circumstances in which Chapter 12 of Part 2 provides for expenditure to be allocated (or re-allocated) to the "appropriate non-ship pool", or for other amounts to be brought into account in that pool. Section 127(3) defines the appropriate non-ship pool as the one to which the expenditure incurred on the provision of the ship would be, or would have been, allocated in the absence of the ships rules.

CAA 1990 does not use the concept of pools. Section 31(2) of CAA 1990 requires expenditure incurred on the provision of a ship for the purposes of a trade to be treated as incurred for the purposes of a separate notional trade. Allowances and charges are calculated on that basis. The circumstances in which, under the Act, amounts are to be brought into account in the appropriate non-ship pool, are dealt with in CAA 1990 by requiring the amounts to be brought into account in relation to the shipowner's "actual trade".

This change in concepts might be thought to amount to a change in the law. But the effect of bringing amounts into account in the appropriate non-ship pool appears to be the same as bringing them into account in relation to the actual trade.

Section 31(1) of CAA 1990 uses "actual trade" as a label to describe the trade for the purposes of which expenditure on the provision of the ship was incurred. Where "actual trade" appears in sections 31, 32 and 33 of CAA 1990, it has that meaning.

Section 33A of CAA 1990 uses "actual trade" to refer to the trade carried on by the shipowner and in respect of which a balancing charge would be made but for a deferment claim. So, in the context of deferment claims, the "actual trade" is the one being carried on in the chargeable period in which the charge arises.

Section 127(3) defines the appropriate non-ship pool in terms which involve determining the pool to which expenditure would be, or would have been, allocated at the time the expenditure is or was incurred. So where sections 31 to 33F of CAA 1990 involve identifying the actual trade at that time, it is clear that using "appropriate non-ship pool" instead does not change the law.

This is the case if notice under section 31(1) of CAA 1990 is given in respect of the chargeable period in which expenditure on a ship is incurred. Section 31(2) provides for section 31 to be deemed never to have applied to the expenditure. The result is that there is no notional single asset trade and so the expenditure is brought into account in calculating allowances and charges for the actual trade.

But other provisions of Chapter II of Part II of CAA 1990 operate in relation to the actual trade at times that are later than that at which the expenditure is incurred. For section 31(7), the time is when a disposal value is required to be brought into account for the single ship trade. For section 32(1), it is when the ship ceases to belong to the shipowner without having been brought into use for the purposes of the actual trade. For section 33, it is when a notice under subsection (1) or (4) of that section is to be given effect. For sections 33A(2), (3) and (6) and 33B(1) to (3), it is the chargeable period in which a balancing charge that is to be deferred arises.

So it might be thought that, in these cases, using "appropriate non-ship pool" instead amounts to a change in the law, as the appropriate non-ship pool is determined at the time the expenditure is incurred. But it appears that the actual trade at the time of a disposal event (sections 31(7) and 32(1)), at the time at which a notice disapplying the ships rules has effect (section 33) or in the chargeable period in which a balancing charge arises (sections 33A and 33B) will always be the same as the actual trade for the purposes of which the expenditure was incurred.

The identity of the trade for the purposes of which expenditure is incurred is a question of fact. It will remain the same throughout the lifetime of the single ship trade.

So, if a disposal event occurs in relation to the single ship trade, the "actual trade" in relation to which an amount is to be brought into account under section 31(7) of CAA 1990 is the trade for the purposes of which the expenditure on the ship was initially incurred. The single ship trade will come to an end at that time.

It is not possible for a disposal event to occur in relation to the single ship trade after the actual trade has been permanently discontinued. There will be a disposal event in relation to the single ship trade at the point at which the actual trade is permanently discontinued, either because the ship is sold as part of the discontinuance or because it begins to be used for purposes other than those of the actual trade.

Notice under section 33(1) or (4) of CAA 1990 can be given only in relation to a chargeable period when the single ship trade is in existence. That will only be the case if the shipowner has not permanently ceased to carry on the trade for the purposes of which the expenditure on the ship was incurred.

It is possible to argue that there are circumstances in which a new “actual trade” comes into existence after the expenditure has been incurred. If this argument were correct, defining the appropriate non-ship pool by reference to the time when the expenditure is incurred would be a change in the law.

For example, if the ship starts to be used partly for non-trade purposes or a “partial depreciation subsidy” is paid, there will be a disposal event (by virtue of section 80(4) of CAA 1990 in the subsidy case). So a disposal value will be brought into account and the single ship trade will end. Sections 79(3) and 80(5)(a) of CAA 1990 deem expenditure equal in amount to the disposal value to have been incurred on the provision of the ship for the purposes of a new “notional” trade carried on by the shipowner.

In theory, that means the test in section 31(1)(a) of CAA 1990 is met and the section 79 or 80 notional trade becomes the “actual trade” for the purposes of sections 31 to 33. If that is right, section 31(2) then requires the creation of a new single ship trade. Allowances and charges that would be made in the single ship trade are instead made in the section 79/80 trade.

Sections 79(5) and 80(5)(b) of CAA 1990 would normally apply to reduce allowances or charges to be made in a section 79/80 trade to such extent as is just and reasonable and require the reduced allowance or charge to be made in respect of the “actual trade” identified in sections 79(3) and 80(3). It is not easy to tell whether sections 79(5) and 80(5)(b) apply to allowances and charges made in the notional trade as a result of section 31(2).

If sections 79(5) and 80(5)(b) of CAA 1990 do apply, there seems little point in having to go though the single ship pool to get them back into section 79 and from there back into the “real” actual trade for the purposes of which the expenditure on the ship was in fact incurred.

If they do not apply, then going through the section 31 pool looks like a way of taxpayers getting allowances that do not reflect the fact that the ship is e.g. now used only partly for trade purposes.

Section 31(3) of CAA 1990 enables all or part of a writing-down allowance to be postponed. It is not clear whether this is supposed to operate on the section 31 allowance that goes back into the section 79/80 trade or (if section 79(5) and 80(5)(b) apply) only to the reduced amount of allowance that is made in the case of the "real" actual trade.

The difficulty of resolving points like this with any degree of certainty lends weight to the view that, once circumstances arise that bring a single ship trade to an end and give rise to a section 79/80 trade, allowances and charges should be determined using the rules in sections 79 and 80. This would include the "just and reasonable" rules in those sections. This is a far more straightforward interpretation of CAA 1990 than treating the notional section 79/80 trade as a new "actual trade" for section 31(1) purposes. On this interpretation, the Act does not change the law.

Note 31 Election to use appropriate non-ship pool—effect of election: section 129(1)

Section 129 comes from section 33 of CAA 1990.

Section 33(1) enables a shipowner by notice to require that section 31 of CAA 1990 shall not or shall no longer apply. Section 31 provides for expenditure on the provision of a ship for the purposes of a trade to be treated as incurred for the purposes of a notional separate trade (the "single ship trade").

Section 129 enables the taxpayer to elect to allocate to the appropriate non-ship pool expenditure which would normally be allocated to the single ship pool or which is already in the single ship pool.

This Note and Notes 32 and 33 explain three differences between section 129 and section 33 of CAA 1990 in relation to the election to take expenditure out of the single ship pool (or, in section 33, the notice requiring that section 31 shall no longer apply). These are differences in approach rather than differences of substance.

Section 129 does not, on the face of it, reflect section 33(3)(a) of CAA 1990.

Section 33(3)(a) provides that, where notice disapplying section 31 has been given in relation to all the expenditure on a ship after a writing-down allowance has been made, the notional "single ship trade" is treated as permanently discontinued in the chargeable period to which the notice relates.

Section 24(6)(c) of CAA 1990 includes the permanent discontinuance of a trade in the list of events that require a disposal value to be brought into account. So the deemed discontinuance of the single ship trade under section 33(3)(a) will result in a requirement to bring the disposal value of the ship into account in the "pool" for the single ship trade.

But section 33(3)(a) also says that no balancing allowance or charge is to be made as a result of the deemed discontinuance. And the amount added to the shipowner's qualifying expenditure for his actual trade as a result of section 33(3)(b) is the amount that would be the shipowner's qualifying expenditure for the single ship trade, ignoring section 33. So it makes no difference whether a disposal value is brought into account under section 33(3)(a).

Note 32 Election to use appropriate non-ship pool—time at which election has effect: section 129(1)

This is the second point (alluded to in Note 31) relating to section 129 and section 33 of CAA 1990.

Notice given under section 33(1) of CAA 1990 has effect "from the beginning of a chargeable period of a single ship trade". In contrast, section 129(1) provides simply for an election to have effect "for" a chargeable period. But this does not change the effect of the provision.

Now that section 132(2)(b) provides for a disposal value to be brought into account in the appropriate non-ship pool (in contrast to section 31(7) of CAA 1990 which in effect works on the basis that it is brought into account in the single ship pool) it makes no difference whether the expenditure is taken out of the single ship pool at the beginning or end of a chargeable period.

Note 33 Election to use appropriate non-ship pool—chargeable period for which election has effect: section 129(1)

This is the third point (alluded to in Note 31) relating to section 129 and section 33 of CAA 1990.

Section 33(1) of CAA 1990 provides that the notice disapplying section 31 of CAA 1990 cannot be given for the chargeable period in which the single ship trade established by section 31 is permanently discontinued. In contrast, there is nothing to prevent an election under section 129(1) being made for the chargeable period in which the single ship pool ends (broadly, the equivalent of the permanent discontinuance of the single ship trade under CAA 1990).

This does not change the real effect of the provisions. There is nothing in the Act corresponding to section 33(3)(a) of CAA 1990, which treats the single ship trade as permanently discontinued if notice under section 33(1) is given after a writing-down allowance has been made. If there is a disposal event in relation to the single ship pool, section 132(2) now requires all the available qualifying expenditure left in the pool to be allocated to the appropriate non-ship pool. If that happens, there will be no expenditure left in the pool in relation to which an election under section 129 can apply.

Note 34 Effect of postponement of allowances in respect of ships: section 131(1)(b)

Section 131(1)(b) applies if a person gives notice under section 130 postponing all or part of a first-year allowance or writing-down allowance in respect of expenditure on the provision of a ship. It provides for the rules about allocating expenditure to pools to apply as if the allowance had been made without any postponement.

In the case of a postponement of a first-year allowance, the effect of section 131(1)(b) is that section 58(5) applies. The result is that the expenditure cannot be pooled for the chargeable period in which it is incurred and the amount that may be pooled for a later chargeable period is limited to the balance after deducting the first-year allowance.

As far as first-year allowances are concerned, section 131(1)(b) comes from section 30(2)(b) of CAA 1990. But, whereas section 131(1)(b) provides for the rules about allocation of expenditure to pools to apply as if the first-year allowance had been made without any postponement, section 30(2)(b) of CAA 1990 provides that for the purposes of those rules "so much of the expenditure as is equal to the whole allowance shall be disregarded".

The different wording in section 131(1)(b) is thought to bring out the intention behind section 30(2)(b) of CAA 1990 more clearly.

The approach taken in section 30(2)(b) of CAA 1990 originated in paragraph 8(2)(b) of Schedule 8 to FA 1971. At the time, first-year allowances were available at 100%. Paragraph 8(2)(b) provided that "the expenditure to which the allowance relates shall be disregarded for the purposes of [the pooling rules]". This ensured that, if a first-year allowance was postponed, none of the expenditure could be pooled.

In 1984, first-year allowances were reduced. Paragraph 8(2)(b) of Schedule 8 to FA 1971 was therefore amended by section 58(3) of FA 1984 so as to substitute the words quoted above—i.e., "so much of the expenditure as is equal to the whole allowance shall be disregarded". The purpose of the amendment was to ensure that the cost of the ship less the first-year allowance could qualify for a writing-down allowance.

However, the technique of "disregarding" part of the expenditure does not address clearly two specific points about how section 25(1) of CAA 1990 is supposed to apply in cases where first-year allowances in respect of ships are postponed.

Section 25(1)(a)(ii) ensures that expenditure in respect of which a first-year allowance is or could be made cannot be pooled for the chargeable period in which the expenditure is incurred. For this to apply in the normal way where the whole or a part of a first-year allowance is postponed, it has to be taken to be implicit that, despite the fact some of the expenditure is being "disregarded", the expenditure is still expenditure "in respect of which a first-year allowance is or could . . . be made". This is what the legislation is generally assumed to mean.

The opening words of section 25(1)(a) ensure that only “the balance remaining after deducting any first-year allowances in respect thereof of capital expenditure” is qualifying expenditure. But there is an awkwardness where a part of the first-year allowance is postponed and a part is taken straightaway. It would be absurd if the whole of the allowance had to be disregarded (because of section 30(2)(b)) and then the part of the first-year allowance actually made had to be deducted as well (because of the words at the start of section 25(1)(a)). The legislation is generally assumed not to have this effect.

Section 131(1)(b), by requiring the rules about pooling to be applied as if the whole of the first-year allowance had been made, is meant to bring out these two points more clearly.

Note 35 Effect of disposal events in relation to single ship pool: section 132(2)

Section 132(2) deals with what happens when a disposal event occurs in relation to a ship where expenditure on the provision of the ship has been allocated to a single ship pool under section 127.

Section 132(2) comes from section 31(7) of CAA 1990. Section 31(7) is in terms of the effect of the disposal event on the notional “single ship trade” created by section 31(2)(a).

The opening words of section 31(7) of CAA 1990 provide that no balancing allowance or balancing charge is to be made on the shipowner in respect of the notional trade.

The Act uses the concept of “pools” for expenditure rather than that of separate notional trades. So section 132(2) deals with what happens when there is a disposal event in relation to the “single ship pool” to which expenditure has been allocated under section 127(1). Normally, a disposal event occurring in a chargeable period in relation to a single asset pool would mean that chargeable period was the “final chargeable period” (section 65(2)). That would mean that entitlement to an allowance in that period was to a balancing allowance (section 55(4)). But section 132(2)(c) provides for the single ship pool to end without a “final chargeable period” and without any liability to a balancing charge. The effect of this is the same as that of the opening words of section 31(7) of CAA 1990.

But paragraphs (a) and (b) of section 31(7) of CAA 1990 then deal with the amount of the balancing allowance or balancing charge that would have been made were it not for the opening words. If a balancing allowance would have been made, the amount of the allowance is required to be added to the shipowner’s qualifying expenditure for his actual trade for the chargeable period in which the disposal event occurs. If a balancing charge would have been made, the amount on which the charge would have been made is required to be brought into account as a disposal value for the actual trade for that period.

To calculate the amount of the balancing allowance or balancing charge that would otherwise have been made, it is necessary to bring the ship's disposal value into account against the qualifying expenditure left in the "pool" for the notional trade (section 24(2) and (5) of CAA 1990). The "net" figure is then brought into account in the "main" pool, either as additional expenditure or as an additional disposal value.

In contrast, section 132(2) provides for the available qualifying expenditure in the pool to be allocated to the "appropriate non-ship pool" (as defined in section 127(3)) for the chargeable period in which the disposal event occurs and for the disposal value of the ship to be brought into account as a disposal value in the appropriate non-ship pool for that period. So the disposal value is set against expenditure in the non-ship pool (which includes the remaining qualifying expenditure on the ship), rather than against that expenditure in the ship pool. But the overall effect of section 132(2)(a) and (b) is the same as that of section 31(7)(a) and (b) of CAA 1990.

Note 36 Expenditure incurred by successors to shipowner's qualifying activity: section 155(2)(a)

Section 155(2)(a) comes from section 33D(7) of CAA 1990. Section 155(2) is expressed to apply for the purposes of "the deferment rules", that is, the rules about deferring a balancing charge. The deferment rules come from sections 33A to 33F of CAA 1990 and are rewritten in sections 135 to 156. But section 33D(7) of CAA 1990 applies for the purposes of the whole of Chapter II of Part II of CAA 1990, not just sections 33A to 33F. So section 155(2)(a) appears to be more restrictive than section 33D(7) of CAA 1990. But there is not in fact a change in the legal effect of the provisions.

Section 33D(7) of CAA 1990 provides for expenditure to be treated as incurred by the shipowner if it is incurred by a person carrying on the trade previously carried on by the shipowner and the trade has not been treated as discontinued since the shipowner carried it on. So any provision in Chapter II of Part II of CAA 1990 (sections 30 to 33F) that applies where expenditure is incurred by the shipowner also applies where expenditure is incurred by the successor.

To the extent that provisions of this kind appear in sections 33A to 33F of CAA 1990, section 155(2)(a) expressly reflects section 33D(7). The only other provision of Chapter II of Part II of CAA 1990 that applies where expenditure is incurred by the shipowner is section 31(1). Section 31(2) provides for the expenditure to be treated as incurred for the purposes of a separate notional trade. Allowances and charges are required to be calculated on that basis.

On the face of it, if expenditure on the provision of a ship is incurred by a successor to the shipowner's trade, section 33D(7) applies to treat the expenditure as incurred by the shipowner. It might then be argued that section 31(2) requires the shipowner to be treated as having incurred the expenditure for the purposes of a trade carried on by him separately from his actual trade.

But that is not a tenable interpretation. Section 31(1) applies only if the shipowner has incurred expenditure on the provision of a ship *for the purposes of a trade carried on by him*. If the expenditure is in fact incurred by the successor for the purposes of the trade which, at that point, is carried on by the successor, this condition will not be met. So confining the application of section 155(2)(a) to the deferment rules does not represent a change in the law.

Note 37 Effect of section 53(1A) of CAA 1990: section 177(3)

Section 177(3) is based on section 53(1A) of CAA 1990.

Section 177(3) deals with the case where (broadly speaking) plant or machinery is leased for the purposes of a qualifying activity to be carried on by the lessee (the case dealt with in section 53(1) of CAA 1990). It postpones the time from which an equipment lessor is to be treated as owning the fixture to the time when the lessee begins to carry on the qualifying activity.

Section 177(3) does not provide for such a postponement for the two other cases where an equipment lessor is treated as owning a fixture. The two other cases are, first, where the equipment lessor has the right to sever a fixture that is not part of a building (a provision originally aimed at "street furniture") and, secondly, where the subject matter of the lease is covered by the affordable warmth programme. These two cases are dealt with in section 53(1) as modified by section 53(1B) and (1D).

Whether section 177 is correct in limiting the postponement of the equipment lessor's ownership to the case where the plant or machinery is leased for the purposes of a qualifying activity to be carried on by the lessee turns on the meaning of "satisfied . . . by reference to . . ." in section 53(1A) of CAA 1990.

Section 53(1A) of CAA 1990 provides—

> "(1A) Where the condition specified in paragraph (b) of subsection (1) above is *satisfied* in any case *by reference to* an agreement entered into for the purposes of a trade which the equipment lessee has not begun to carry on at the time of the agreement, that subsection shall have effect in that case as if the reference in the words after paragraph (e) to the time at which the expenditure is incurred were a reference to whichever is the later of that time and the time when the equipment lessee begins to carry on that trade."

It is thought that the effect of "satisfied . . . by reference to . . ." is that the condition in subsection (1)(b) has to be satisfied because of an agreement entered into for the purposes of the trade. The words are not apt for the situation where the equipment lessee does not need to have "a trade" (in the CAA 1990 sense) in order to get allowances but merely happens to have one. In other words, section 53(1A) does not apply in relation to section 53(1) as modified by section 53(1B) and (1D).

Note 38 Reduction of allowances and pooling rules: sections 205(3), 207(4), 210(2) and 212(3)

Sections 205(3), 207(4), 210(2) and 212(3) deal with situations where a first-year allowance or a writing-down allowance has been reduced to take account of the fact that the plant or machinery is used partly for purposes other than those of the qualifying activity or the fact that a partial depreciation subsidy is paid in respect of the plant or machinery.

Sections 205(3) and 210(2) provide that a reduction in a first-year allowance is to be disregarded in calculating (for the purposes of initial allocation of expenditure to a pool) the balance left after deducting the first-year allowance.

Sections 207(4) and 212(3) provide that a reduction in a writing-down allowance is to be disregarded in calculating the unrelieved qualifying expenditure carried forward in the pool.

In relation to calculating the balance left after deducting a first-year allowance, the point dealt with in sections 205(3) and 210(2) used to be addressed explicitly by paragraphs 5(4)(d) and 6(5)(d) of Schedule 8 to FA 1971. But amendments made by paragraphs 6 and 7 of Schedule 14 to FA 1985 removed these explicit provisions. The 1985 amendments were largely consequential on removing the "brought into use" requirement for writing-down allowances. But in the process they also took account of the phasing out of first-year allowances by section 58 of, and Schedule 12 to, FA 1984. (FA 1984 abolished first-year allowances for expenditure incurred after 31st April 1986, except in the case of 100% allowances in respect of existing commitments under regional projects).

Since 1985, first-year allowances have been reintroduced. It is generally assumed that any reduction in a first-year allowance under section 79(1) or 80(2) of CAA 1990 has to be disregarded in calculating the balance for the purposes of section 25 of CAA 1990. It is perhaps arguable that, on a literal reading of sections 79 and 80 of CAA 1990, the taxpayer need only deduct the reduced first-year allowance when calculating the balance for pooling purposes. But even if that argument were right, the just and reasonable reduction of any subsequent writing-down allowances could be increased. So the practical effect would be very similar. The point here is similar to that discussed in Note 21 in relation to sections 77(3) and 78(3) and section 34(5) of CAA 1990.

In the case of the calculation of unrelieved qualifying expenditure carried forward—the point dealt with in sections 207(4) and 212(3)—it is clear that under CAA 1990 the reduction of the writing-down allowance is meant to be disregarded.

This is because sections 79(6) and 80(6) of CAA 1990 deal expressly with the situation where an allowance is not claimed or reduced under section 24(3) of CAA 1990. Sections 79(6) and 80(6) provide that for the purpose of determining allowances and charges for subsequent chargeable periods the allowance is to be treated as not claimed or as proportionately reduced. This is equivalent to saying that the unrelieved qualifying expenditure carried forward need not be reduced. (Sections 79(6) and 80(6) are reflected in sections 207(5) and 212(4)).

The plain implication of sections 79(6) and 80(6) of CAA 1990 is that in other cases the unrelieved qualifying expenditure is supposed to be reduced.

Note 39 Meaning of "finance lease": section 219(1) and (2)

Section 219 comes from section 82A of CAA 1990, which defines "finance lease" for the purposes of Part II of CAA 1990. A finance lease is defined as any arrangements providing for machinery or plant to be leased or made available, as long as the arrangements are of a kind that are treated, in accordance with normal accountancy practice, as a finance lease or as a loan. The latter aspect of the definition is expressed to apply "in cases where the lessor and persons connected with the lessor are all UK companies". Section 82A(2) defines "UK company" as a company incorporated in a part of the United Kingdom.

Section 219(1)(b) refers to normal accountancy practice without saying that it applies only in a UK company case. But section 219(2) provides that, for the purpose of applying the test concerning normal accountancy practice, the lessor and any person connected with the lessor are to be treated as being UK companies.

Section 219(1) and (2) reflects the intended effect of section 82A(1)(b) of CAA 1990. The normal accountancy practice test in section 82A(1)(b) could in theory be read as applying only where the lessor and connected persons are UK companies. This interpretation would mean that, if the lessor or a connected person were not a UK company, arrangements could be a finance lease simply by satisfying the requirements of section 82A(1)(a) of CAA 1990. That would mean any arrangements for leasing machinery or plant could constitute a finance lease in those cases.

But it is fairly clear that this is not what was intended. Rather, the aim was to ensure that the "normal accountancy practice" that applied for determining whether the arrangements were a finance lease or a loan was that applicable to companies incorporated in a part of the United Kingdom. So section 82A(1)(b) looks at how the arrangements in question would be treated in cases where the lessor and connected persons were UK companies, irrespective of whether, under the arrangements, the actual lessor and connected persons were all UK companies.

Section 219(2) achieves the same result by providing for the lessor and connected persons to be treated as companies incorporated in the United Kingdom for the purpose of applying section 219(1)(b). The effect is that the normal accountancy practice mentioned in subsection (1)(b) is that applicable to UK companies.

Note 40 Giving effect to allowances and charges for income tax purposes—special leasing: section 258

There are two points to mention in connection with section 258.

First, section 258(6) incorporates the extended meaning of "income" given in section 83(1) of CAA 1990. It is not needed for any other provision in Part II of CAA 1990 and to retain it in a general form would be misleading.

Secondly, the words in section 141(2)(b) of CAA 1990 "and tax shall be discharged or repaid accordingly" are not reproduced because they are unnecessary and misleading.

This paragraph is about the first point. The purpose of the extended meaning of income is to enable allowances to be set against balancing charges. An extended meaning of "income" very similar to that given in section 83(1) of CAA 1990 is also to be found in section 161(2) of CAA 1990. So at first sight it looks as if one possibility would have been to preserve the effect of section 83(1) in section 577 (which contains definitions of general application). But there are no provisions outside Part II of CAA 1990 that could benefit from the retention of the extended meaning in section 161(2). Hence section 258(6).

The following paragraphs are about the second point.

Where a claim is made otherwise than by being included in a tax return, the claim needs to be given effect by way of discharge or repayment of tax. Claims under section 258 can be made outside a tax return. See section 3(4)(a) (which is based on section 141(5) of CAA 1990).

But the words are unnecessary because paragraph 4(1) of Schedule 1A to TMA 1970 already provides for a claim made otherwise than by being included in a return to be given effect by discharge or repayment of tax.

The words are misleading because the fact that they appear only in section 141(2)(b) of CAA 1990 might be taken to suggest, wrongly, that a late claim for an allowance for the tax year for which the allowance falls to be made cannot be given effect by discharge or repayment of tax.

The words "and tax shall be discharged or repaid accordingly" can be traced back to section 56(1) of ITA 1945. They were repeated in section 324(1) of ITA 1952 (a consolidation) where they related both to the claim for an allowance for the year in which the allowance fell to be made and to claims to carry forward the excess. They were again repeated in section 71(1) of CAA 1968 (another consolidation). But section 71(1) of CAA 1968, in paragraphing section 324(1) of the 1952 Act, mistakenly tacked the words on to the end of paragraph (b) (instead of leaving the words to apply to both paragraph (a) and paragraph (b)).

When the words were included in section 56(1) of ITA 1945, they were a convenient summary for what could be done under some complicated, and rather different, provisions in sections 27 to 30 of ITA 1918 (which section 56(2) of ITA 1945 invoked by way of section 41 of FA 1927). The process by which sections 27 to 30 of ITA 1918 and section 56(1) of ITA 1945 were gradually transmogrified into section 141(2) of CAA 1990 and section 42 of, and Schedule 1A to, TMA 1970 has been a complicated one and it is perhaps not altogether surprising that in this process the possibility of dropping the words as redundant has not been considered.

Note 41 Giving effect to allowances and charges for employees and office holders: section 262

Section 262 provides for allowances and charges to be given effect, in the case of employees and office holders, by treating the allowance as an amount to be deducted from the emoluments of the employment or office and the charge as an emolument. It is based on parts of section 140 of CAA 1990.

A mechanical approach to rewriting the relevant parts of section 140 would appear to require an allowance to be treated as an expense of the employment and a charge to be treated as a receipt of the employment. But the wording actually used in section 262 fits better with the language of Schedule E and is not thought to change the legal effect.

This note considers two ways in which the change in language might be thought to change the legal effect, and explains why it does not in fact do so.

The first concerns losses.

Section 380 of ICTA enables a person who sustains a loss in a trade, profession, vocation or employment (but not one who sustains a loss in an office) to claim a relief from income tax equal to the amount of the loss for the current or the preceding year. There is very little scope for a loss in an employment apart from one arising because of an excess of capital allowances.

The main provision authorising the deduction of expenses in the case of employees and office holders, section 198 of ICTA, is interpreted as not enabling expenses to generate a loss for the purposes of Schedule E.

The fact that section 198 of ICTA cannot be used to generate a loss might lead one to suppose that a capital allowance cannot generate a loss. But this does not follow. Section 140(4) of CAA 1990 does not require a capital allowance to be treated as a section 198 expense.

So it is thought that the new form of wording, far from changing the law in relation to giving effect to capital allowances, actually makes its effect clearer, because it prevents readers from assuming that the allowance, like a section 198 expense, cannot generate a loss, whereas section 380 of ICTA is based on the contrary assumption.

The second way in which the change in language might be thought to change the legal effect concerns provisions which turn on the level of emoluments a person has. An example is Chapter II of Part V of ICTA, which brings into charge various benefits in kind.

Under section 167(1)(b) of ICTA, Chapter II of Part V applies to employment (which includes offices) with "emoluments" at the rate of £8,500 a year or more.

Before FA 1994, the provisions for giving effect to capital allowances were different. Capital allowances were given effect in charging profits or gains to tax. So capital allowances were irrelevant to working out whether an employee or office holder had emoluments at this level.

It would be very surprising if the amendments made by FA 1994 had changed this by a sidewind, and in fact they do not appear to have done so.

It seems unlikely that a notional "receipt" under section 140 of CAA 1990 comes within the definition of "emoluments" under section 131(1) of ICTA. Section 131(1) of ICTA provides that emoluments "includes all salaries, fees, wages, perquisites and profits whatsoever". It is not a "salary", a "fee" or a "wage". The normal meaning of the word "perquisite" is said to denote something that benefits a man by going "into his own pocket", or as having a known normal meaning, namely a personal advantage (*Owen* v *Pook (Inspector of Taxes)* [1970] AC 244 at 259, per Lord Pearce). But this notional receipt is not to the taxpayer's personal advantage. It exists to extract extra tax, or to prevent the employee or office holder from profiting from allowances on his capital expenditure.

So at first sight, the change in wording in section 262 might appear to change the effect of the provision. It no longer refers to a "receipt", but instead treats the charge as an emolument. Treating a charge as an emolument could, apparently, inflate the level of emoluments for the purposes of Chapter II of Part V of ICTA.

However, it would be wrong to regard the change in wording as having this effect. This is because section 140(2) of CAA 1990 contains other words limiting its effect and these are retained in section 262.

The limiting words are that the charge is to be given effect by treating an amount as a receipt, or, in section 262, as an emolument. The reasoning adopted by the Court of Appeal in the *Elliss* case (described above in Note 1) is applicable here. I.e., that the charge is not treated as an emolument for all the purposes of the Tax Acts, but only for the limited purpose of giving effect to the charge.

On this basis, the change in wording does not have any impact on Chapter II of Part V of ICTA (or on other provisions which turn on the level of emoluments).

Note 42 "Within the charge to tax" and "within the charge to tax in the United Kingdom": sections 266(1)(b), 339(1)(b) and (2) and 382(5)

Sections 266(1)(b), 339(1)(b) and (2) and 382(5) refer to a person being "within the charge to tax" even though the provisions from which they derive, sections 77(3)(b), 8(14) and 129(5) of CAA 1990 respectively, refer to a person being "within the charge to tax <u>in the United Kingdom</u>".

Section 161(2) of CAA 1990 and section 832(3) of ICTA define "tax" as either income tax or corporation tax, where neither is specified. (The definition in section 161(2) has not been reproduced in the Act since it merely duplicates section 832(3).) So if a person is within the charge to income or corporation tax, he has to be regarded as being within the charge to tax in the United Kingdom even if he is not resident in the United Kingdom.

The inclusion of the words "in the United Kingdom" in sections 77(3)(b), 8(14) and 129(5) of CAA 1990 may have been intended to be helpful in clarifying that United Kingdom tax, as opposed to, say, French tax is referred to.

But they are unhelpful in so far as they set up an unfortunate contrast with other provisions in CAA 1990 or ICTA which merely refer to a person being "within the charge to tax". The provisions relevant to capital allowances are sections 55(2), 76A(10)(b), 145(2) and (3) and 153(3) of CAA 1990 and sections 524(5) and 528(3) of ICTA. References to "within the charge to tax" in these provisions are not meant to refer to tax outside the United Kingdom.

Leaving out the words "in the United Kingdom" also has the advantage of making it clearer that the phrase is subject to the statutory gloss on "within the charge to tax". Under the legislation as it stood before the Act, there were two such glosses: one in section 832(1) of ICTA; the other in section 161(4) of CAA 1990. Section 161(4) has not been reproduced in the Act because it merely duplicates the more general provision in ICTA.

Note 43 Election for continuity on succession to qualifying activity: section 266(2) and (4)

Section 266 comes from section 77 of CAA 1990. The closing words of section 77(3) provide that the predecessor and successor may "by notice . . . elect". Section 266(2) provides that they may "jointly" elect. Section 77(3) already requires both parties to elect, and refers to only one election, so it is implicit that the election is to be made jointly.

Note 44 Preparation of sites for plant or machinery: section 273(2)(a)

Section 273 is based on section 13 of CAA 1990; but section 13 contains nothing corresponding to section 273(2)(a). Subsection (2)(a) has been added to make it clearer what the purpose of the provision is.

Section 13 of CAA 1990 applies where expenditure is or has been incurred on preparing, cutting, tunnelling or levelling land for the purposes of preparing the land as a site for the installation of machinery or plant, and, apart from the section, no allowance could be made in respect of the expenditure under Part I or II of CAA 1990. Where the section applies, then, in relation to the expenditure on preparing the land (etc.), the machinery or plant "shall be treated for the purposes of [Part I of CAA 1990] as a building or structure".

This is, at first sight, a rather baffling proposition. Section 13 of CAA 1990 derives from a Report Stage amendment which became section 16(3) of FA 1956. It emerged that certain plant or machinery forming part of an oil refinery might not be regarded as a building or structure. The purpose of the provision was in fact to ensure that industrial buildings allowances were available in respect of expenditure on installing this type of plant or machinery.

Section 273 makes provision corresponding to section 13 of CAA 1990 except that subsection (2)(a) explicitly provides for Part 3 to have effect as if the purpose of incurring the expenditure were to prepare the site for the construction of a building. (In Part 3, "building" is used as shorthand for "building or structure".) This addition is meant to make a little clearer that the purpose of the provision is, in these exceptional cases, to lift the expenditure over the main industrial buildings allowances hurdles.

Note 45 Omission of reference to a trade carried on in a mill, factory or other similar premises: section 274, Table A

Table A in section 274 does not include "a trade carried on in a mill, factory or other similar premises" even though such a trade is dealt with in section 18(1)(a) of CAA 1990. Given the way that section 18(1)(a) has been interpreted by the courts, it now seems to add nothing to section 18(1)(e) (which refers to "a trade which consists in the manufacture of goods or materials or the subjection of goods or materials to a process"). So to retain it would be misleading.

The authority on the relationship between section 18(1)(a) and (e) of CAA 1990 is *Vibroplant Ltd* v *Holland* ([1981] 1 All ER 792; (1981) 54 TC 658; [1982] STC 164).

Vibroplant Ltd carried on the trade of plant hire operators and it was argued that buildings used by the company for cleaning, servicing and repairing tractors, fork lift trucks, concrete mixers and other plant were within what is now (as a result of consolidation) section 18(1)(a) of CAA 1990.

Templeman LJ rejected this argument on the ground that "a building used for the purpose of cleaning, servicing and repairing vehicles and other articles belonging to a taxpayer whose trade consists of hiring out those articles for reward is not similar to a mill or factory because nothing similar to manufacturing or processing is involved at any stage".

This was on the basis that premises would only come within what is now section 18(1)(a) if the premises were "similar" to factories and mills and that "a factory makes an article and a mill processes an article".

It was argued that what is now section 18(1)(a) could not be confined to premises used for manufacturing or processing because what is now section 18(1)(e) dealt expressly with manufacturing and processing. But this was rejected.

Since then there has been no authority establishing that a trade which falls outside section 18(1)(e) can come within section 18(1)(a).

In *Girobank plc* v *Clarke (Inspector of Taxes)* ([1996] STC 540 (Ch.D); [1998] 1 WLR 942 (CA)) Girobank, who had based their case before the deputy Special Commissioner on the argument that their document and data processing centre at Wigan came within section 18(1)(e), tried to raise in the High Court the argument that the centre came within section 18(1)(a).

Nourse J refused to allow this new argument, but nevertheless said that if Girobank had been permitted to raise the argument he would have rejected it. There were two grounds on which he would have done so.

The first was that this would have followed from his ruling on section 18(1)(e), which was that the Wigan centre was excluded because it was an "office" for the purposes of section 18(4). This no longer holds good, because the Court of Appeal did not rely on the Wigan centre being an "office" to reject Girobank's claim under section 18(1)(e).

The second was that he would have concluded that the Wigan centre was not "similar" to a mill, which he characterised as being premises at which, chiefly by way of the use of machinery, one or more processes which require the use of that machinery are applied substantially to alter the physical nature of the materials to which they are applied and with a view to that alteration making that material more suitable for, or to add to its value for, commercial use or disposition as merchandise or wares. The defining characteristics of mills given by Nourse J are somewhat more elaborate than those given in *Vibroplant*, but the core point is the same: that for a building to be similar to a mill it must be a place where materials are processed.

The curious reader may wonder why it was thought appropriate to include what is now section 18(1)(a) as well as what is now section 18(1)(e) if the latter merely subsumes the former.

The answer lies in ITA 1945. It phased out allowances for mills, factories and other similar premises under section 37 of FA 1937 and laid the foundations for the modern system of industrial buildings allowances. At the time it was regarded as important to give those obtaining allowances under FA 1937 the option of either obtaining allowances under the new system or continuing under the old system for a period of 5 years.

An easy way of making crystal clear that premises which qualified under FA 1937 would also qualify under the 1945 Act was to preserve the 1937 wording in section 8(1)(a), the precursor of section 18(1)(a) of CAA 1990. This smoothed the transition and would have given comfort to anyone who might have had lingering doubts about their position if section 8(1)(a) had not been included. This transitional need has now passed. Section 18(1)(a) has become redundant and can only mislead those who are not aware of the modern case law and the legislative history.

Note 46 Omission of reference to aquifers and hot dry rocks: sections 274, Table A, item 7, 394(3) and 452(3)(a) ("mineral deposits")

Section 161(2) of CAA 1990 contains the following definition of "mineral deposits"—

> ""mineral deposits" includes any natural deposits capable of being lifted or extracted from the earth and, for this purpose, geothermal energy, whether in the form of aquifers, hot dry rocks or otherwise, shall be treated as a natural deposit".

This definition is given in section 161(2) for CAA 1990 as a whole. It is needed for provisions in Parts I and IV of CAA 1990 (industrial buildings and mineral extraction allowances) and for section 533(7) of ICTA (know-how allowances).

The corresponding Parts of the Act are Parts 3, 5 and 7. In those Parts, sections 274(1), 394(3) and 452(3) incorporate the definition of "mineral deposits" in section 161(2) of CAA 1990 except that the phrase "whether in the form of aquifers, hot dry rocks or otherwise" has been omitted.

In the definition, the words from "and for this purpose" to the end derive from an amendment to section 87(1) of CAA 1968 made by paragraph 2(3) of Schedule 13 to FA 1986.

"Geothermal energy" is energy from the internal heat of the earth. Geothermal aquifers are strata of porous rock permeated with water and deep enough to be a significant reservoir of heat. The heat can be extracted by pumping out the water. Heat can be extracted from hot dry rocks by drilling boreholes to a sufficient depth (5 to 8 km) and pumping water down to the rocks and extracting it.

The legal effect of the words added in 1986 is to treat geothermal energy in any form as a "natural deposit". The words "whether in the form of aquifers, hot dry rocks or otherwise" are intended to be merely illustrative. Those who know what "geothermal energy" means are also likely to know where it is to be found. Those who do not know what geothermal energy is are unlikely to be greatly assisted by the references to aquifers and hot dry rocks, which are no more part of everyday speech than geothermal energy is. Although illustrative, the words used may not be ideal. They might be taken to imply that the hot dry rocks themselves are capable of being lifted or extracted from the earth (the words "in the form of" may not have been the perfect choice) or that there are various other sources of geothermal energy apart from aquifers and hot dry rocks (see the words "or otherwise"). To this extent the illustrative words may be more of a hindrance than a help. Omitting the words does not change the legal effect.

Note 47 Giving effect to industrial buildings allowances: section 353(2) to (4)

Section 353 deals with giving effect to industrial buildings allowances where a person's interest in an industrial building is an asset of an overseas property business or it is not an asset of any property business.

Section 9 of CAA 1990 deals with two situations: where the person is carrying on a Schedule A business and where the person is not carrying on such a business.

Section 161(2A) of CAA 1990 applies CAA 1990 to overseas property businesses as it applies to Schedule A businesses.

Section 9 of CAA 1990 does not deal expressly with the situation where the person is carrying on an overseas property business as well as a Schedule A business. Section 353(2) to (4) resolves what is supposed to happen in this situation by requiring the allowance to be given effect in connection with the business of which the lease is an asset.

It is thought that this merely brings out what is implicit in CAA 1990.

Note 48 Land in the UK occupied for the purposes of husbandry: section 361(1)(b)

Section 361(1)(b) provides for one of the conditions for availability of agricultural buildings allowances to be that the expenditure in question was incurred by a person with a freehold or leasehold interest in <u>land in the United Kingdom</u> occupied wholly or mainly for the purposes of husbandry.

Section 123 of CAA 1990, from which section 361(1)(b) derives, refers instead to "agricultural land". Section 133(1) of CAA 1990 defines agricultural land as <u>land, houses or other buildings in the United Kingdom</u> occupied wholly or mainly for husbandry purposes.

So section 361(1)(b) looks as if it is narrower than section 133(1) of CAA 1990. But its effect, if anything, is wider, because it allows the Interpretation Act definition of "land" to operate and in doing so brings out a point that must be implicit in CAA 1990.

Under Schedule 1 to the Interpretation Act 1978—

> ""land" includes buildings and other structures, land covered with water, and any estate, interest, easement, servitude or right in or over land."

The definition of land in the 1978 Act is different from the definition of land in the previous (1889) Interpretation Act. The 1978 definition was the result of Recommendation 12 of the Report of the English and Scottish Law Commissions on the Interpretation Bill.

The point of Recommendation 12 was to produce a definition which would remove the need for constantly repeated ad hoc definitions which had the effect of including in the meaning of "land", among other things, (1) buildings and structures and (2) lakes, rivers and foreshore (land covered with water).

The effect of the rewritten version of the legislation is to make somewhat clearer that agricultural land includes structures and land covered with water, as well as buildings.

But there could hardly be any serious doubt on either of these points, given that allowances under Part V of CAA 1990 can be made in respect of "works", which includes structures, and in connection with the intensive rearing of fish, which may well occur on "land covered by water".

Note 49 Apportionment between different parts of related agricultural land: section 371

Section 371 applies where a person is entitled to different relevant interests in different parts of the "related agricultural land". It provides for expenditure for which allowances are available under Part 4 to be apportioned between the different parts of the land and for the Part to apply as if the expenditure apportioned to each part had been incurred separately.

There is no equivalent provision in CAA 1990. But it is thought that the approach taken in CAA 1990 produces the same result.

The provisions of CAA 1990 work on the basis that there is one "relevant interest" in the agricultural land concerned. Section 125(2) of CAA 1990 defines the "relevant interest" as "the" [freehold or leasehold] interest held by the person who incurred the expenditure at the time he incurred it. Sections 125(4) and 126(5) of CAA 1990 apply "where the relevant interest is a lease". And section 125(3) of CAA 1990 provides a means for creating a single relevant interest where a person is entitled to two or more interests in the same land.

Section 123 of CAA 1990 provides for allowances to be available in respect of expenditure on the construction of agricultural buildings if the person incurring the expenditure has a freehold or leasehold interest in some agricultural land. For example, a person might own the freehold of farm A and incur expenditure on building a farmhouse. Section 124(1) of CAA 1990 provides for expenditure not to be taken into account for allowances unless it is incurred for the purposes of husbandry on "the agricultural land in question". The only agricultural land to which this can refer is that in which the person has the freehold or leasehold interest: i.e., in the example, farm A.

But if the expenditure on the farmhouse can also be said to be for the purposes of husbandry on other land ("farm B") and the person has a leasehold interest in farm B, section 123 of CAA 1990 appears to be capable of applying again to give entitlement to another allowance in respect of the expenditure on the farmhouse. But it cannot be intended to give allowances twice in respect of the same expenditure.

It is thought that it is implicit in section 123 of CAA 1990 that, in cases like this, the expenditure would be apportioned between farms A and B. In the absence of express provision, the most likely basis for the apportionment would be "just and reasonable".

Section 361 deals rather differently with availability of allowances. It provides for them to be available if expenditure on the construction of an agricultural building is incurred for the purposes of husbandry on land in which the person incurring the expenditure has a freehold or leasehold interest. This land is referred to in the rest of Part 4 as the "related agricultural land". In the example given above, the person incurring the expenditure on the farmhouse has a freehold interest in farm A and a leasehold interest in farm B. The expenditure is incurred for the purposes of husbandry on both farms. So the "related agricultural land" consists of both farms.

So the effect of the change of approach is that there may be more than one "relevant interest" in the related agricultural land. But sections 367 and 368 (which derive from sections 125(4) and 126 (5) of CAA 1990) continue to be expressed in terms that assume there is only one relevant interest in the related agricultural land. Section 371 is needed to make these provisions work as intended.

Note 50 Expenditure which is treated as qualifying expenditure on mineral exploration and access: section 395(1)(c)

Section 395(1)(c) includes within the definition of "qualifying expenditure" expenditure which is treated as qualifying expenditure under section 407(5) or 408(2).

Sections 407 and 408 come from sections 115 and 118(2) of CAA 1990 which treat part of expenditure on a mineral asset as being expenditure on mineral exploration and access.

The approach taken in CAA 1990 leaves it to the reader to work out for himself or herself what further requirements have to be met before allowances can be obtained in respect of the part of the expenditure on the mineral asset that is being treated as expenditure on mineral exploration and access.

There are two requirements that need to be satisfied. First, the expenditure on the mineral asset must have been incurred by a person carrying on a mineral extraction trade for the purposes of the trade. (But expenditure incurred on a mineral asset by a person about to carry on the trade is treated as incurred on the first day of trading.) Secondly, the expenditure must be capital expenditure. (These requirements are contained in section 98(1) and section 105(1) of CAA 1990. The rule about pre-trading mineral asset expenditure is in section 120(1) of CAA 1990.)

The approach taken in the Act is to build these requirements into the sections based on sections 115 and 118(2) of CAA 1990, i.e. sections 407 and 408. This is meant to save the taxpayer the trouble of having to work out what other tests have to be met in order to obtain allowances on the part of the expenditure on the mineral asset that is treated as expenditure on mineral exploration and access. But if the extra tests are built into sections 407 and 408, it is then safe for section 395(1)(c) to describe the expenditure that passes the tests as "qualifying expenditure".

Note 51 Pre-trading expenditure: sections 400(4) and 434(2)

Sections 400(4) and 434(2) avoid the duplication that appears in sections 106(2), 107(3) and 120(2) of CAA 1990 and in doing so are thought to bring out the real effect of the legislation more clearly.

The duplication relates to propositions about the time when expenditure which is qualifying expenditure under section 106(2) or 107(2) or (3) is treated as incurred. Sections 106(2) and 107(3) contain ad hoc provision treating the expenditure as incurred on the first day of trading; section 107(2) does not contain such a provision, but section 120(2) contains a general provision for Chapter I of Part IV of CAA 1990 (the Chapter that contains sections 106(2) and 107(2) and (3)) which treats the expenditure as incurred on the first day of trading.

Section 120(2) of CAA 1990 derives from a paragraph of Schedule 13 to FA 1986 (paragraph 13(2)) that was inserted at a fairly late stage in the drafting of the Schedule; the element of duplication was almost certainly overlooked. But, however the provisions are read, there is only one possible conclusion, and that is that pre-trading expenditure on plant or machinery, and pre-trading exploration expenditure, are treated as incurred on the first day of trading. So removing the duplication does not change the effect of the legislation.

Note 52 Acquisition of mineral asset owned by previous trader and omission of section 115(2)(b) of CAA 1990: section 407

Section 407 is based mainly on section 115 of CAA 1990. But it contains nothing to reflect paragraph (b) of section 115(2), because paragraph (b) is thought to be redundant.

Section 115(2)(b) of CAA 1990 provides that if allowances under Part VII (research and development) were made to the previous trader, the existence of those allowances does not affect the question whether any of his expenditure was qualifying expenditure.

But there is nothing in section 115 of CAA 1990 which requires the previous trader to have had "qualifying expenditure". Section 115(2)(b) was clearly intended to ensure that section 115 would apply if the previous trader had obtained Part VII allowances, rather than Part IV allowances. But there is no reason to suppose that section 115 would not apply if the previous trader had obtained Part VII allowances. So section 115(2)(b) does not appear to serve any useful purpose.

Note 53 Expenditure on research and development: treatment of dwellings: section 438

Section 438(3) to (6) rewrites section 137(3) of CAA 1990. Subsection (4)(a) of section 438 resolves a possible ambiguity in that provision in favour of its more natural meaning. But this is not thought to change the law because the alternative reading of section 137(3) gives rise to absurd results.

Section 137(3) of CAA 1990 provides that expenditure on the provision of a dwelling is not research and development expenditure. But it goes on to say that where part of a building is used for research and development and part consists of a dwelling, the whole building is treated as used for research and development if no more than 25% of the capital expenditure on the construction or acquisition of the building is referable to the construction or acquisition of the dwelling.

The more natural way of reading the words "where part of a building is used for research and development and part consists of a dwelling" in section 137(3) would be that the provision applies where part of the building is a dwelling and the rest of it is used for research and development.

If it were to be read as applying where part of the building is a dwelling, part is used for research and development and part for any other purpose, that would give rise to absurd results. For example, if 24% of the capital expenditure on the construction or acquisition of a building were referable to a dwelling, 1% to research and development and 75% to some other purpose, such a reading would require the whole of the building to be treated as used for research and development. That clearly cannot have been the intention.

Section 438(4)(a) resolves the possible ambiguity in favour of the more natural meaning. It provides that the 25% test only applies where part of a building consists of a dwelling and the rest of the building is used for research and development.

Note 54 Research and development allowances: treatment of land: section 440

The approach to the treatment of land in the context of research and development allowances is different from that in section 137 of CAA 1990. But the effect is intended to be the same.

Section 137(2) of CAA 1990 provides that research and development allowances under section 137(1) are not available for expenditure on the acquisition of land or rights in or over land except so far as referable to the acquisition of an existing building or structure, rights in or over such a building or structure or plant or machinery forming part of such a building or structure. Section 440(1) on the other hand provides that expenditure on acquiring land or rights in or over land is not qualifying expenditure. But subsection (2) of section 440 provides that subsection (1) does not prevent such expenditure from being qualifying expenditure so far as referable to the acquisition of existing buildings or structures etc.

These subsections therefore have the same effect as section 137(2) of CAA 1990. As long as the requirements of section 439 (which defines qualifying expenditure) are met, expenditure on acquiring existing buildings etc. can give rise to allowances, but expenditure on acquiring land alone cannot.

Note 55 Research and development allowances: allowances and charges instead of deductions and trading receipts: sections 441, 442 and 450

In the case of research and development allowances, section 441 talks in terms of entitlement to an allowance and section 442 refers to liability to a balancing charge. But sections 137(1) and 138(5)(b) of CAA 1990 on which section 441 is based talk in terms of a deduction being allowed in taxing the trade. And section 138(2) and (3A) of CAA 1990 on which section 442 is based refers to a trading receipt being treated as accruing. But this does not change the law.

Deductions allowable in taxing a trade under Part VII of CAA 1990 are given effect for income tax purposes under section 140(1) and (2) of CAA 1990 as if they were allowances arising under the other Parts of CAA 1990 (see section 140(5)). The position is the same for corporation tax (see section 144(1) to (3) of CAA 1990). Sections 140(2) and 144(2) provide that an allowance falling to be made in taxing a trade is given effect by treating the amount of the allowance as a trading expense of the trade. The Act achieves the same result. Entitlement to an allowance arises under section 441. And under section 450(a) the allowance is given effect as an expense of the trade.

The charging provisions of Part VII of CAA 1990 operate directly by giving rise to a deemed trading receipt. The Act takes a more indirect approach to achieve the same result. Section 442 gives rise to a liability to a balancing charge. And under section 450(b) the charge is given effect as a receipt of the trade.

So the Act achieves the same effect as Part VII of CAA 1990 by a slightly different route.

Note 56 Chargeable period for which research and development allowances on pre-trading expenditure are available: sections 441(2) and 447(3)

Under section 137(5) of CAA 1990, research and development allowances are available for the chargeable period in which the expenditure is incurred or, if incurred before the setting up and commencement of the trade, for the chargeable period beginning with setting up and commencement. Under section 441(2), the allowances are available for the chargeable period in which the expenditure is incurred or, if incurred before the chargeable period in which the trade is set up and commenced, that chargeable period. (See also section 447(3) for allowances arising as a result of incurring additional VAT liabilities.) This involves two changes of approach but the better view is that neither changes the law.

The first change in approach concerns the chargeable period for which pre-trading allowances are available and the words "the chargeable period beginning with that setting up and commencement" in section 137(5) of CAA 1990. On a literal reading, section 137(5) appears to give absurd results.

Take a case where a company within the charge to tax sets up and commences a trade mid way through its chargeable period. Before setting up the trade it had incurred allowable research and development expenditure. The first limb of section 137(5) of CAA 1990 is not relevant because the expenditure is incurred before setting up and commencement of the trade. And the second limb does not seem to apply because the company's chargeable period does not begin with that setting up and commencement.

But the intention must have been that the company should be entitled to an allowance for the chargeable period in which it set up and commenced the trade. And it is thought that this is how a court would interpret section 137(5) of CAA 1990. This is the approach taken in sections 441(2)(b) and 447(3)(b).

The second change in approach concerns a case in which a person incurs allowable expenditure before setting up and commencing the trade but in the same chargeable period as that setting up and commencement. In such a case, the second limb of section 137(5) applies because the expenditure is incurred before setting up and commencement. But the first limb would also have given the right answer because the chargeable period in which the expenditure is incurred is the same chargeable period as that in which the trade is commenced.

So there is an element of overlap (albeit that the overlap is resolved in favour of the second limb in such a case by the words "if it was incurred before the setting up and commencement of the trade").

The Act avoids such an overlap because the equivalent to the second limb of section 137(5) of CAA 1990 applies only where the expenditure is incurred before the <u>chargeable period in which</u> the trade is set up, rather than before the <u>time</u> the trade is set up (sections 441(2)(b) and 447(3)(b)). So the case mentioned in the previous paragraph would fall within the Act's equivalent of the first limb of section 137(5) (sections 441(2)(a) and 447(3)(a)).

Note 57 Research and development disposal value arising for chargeable period rather than at particular time: section 444

Section 138(2) of CAA 1990 imposes a charge where an asset representing allowable research and development expenditure incurred by a person ceases to belong to him. The charge is treated as a trading receipt accruing at the time the asset ceases to belong to him (or, if that is on or after the permanent discontinuance of his trade, accruing immediately before discontinuance). But under Part 6, disposal values are brought into account (and balancing charges are imposed) for a chargeable period rather than at a particular time. This is a change in approach—made for consistency with the approach in the rest of the Act—but not a change in the law.

Under section 443(1), a person must bring a disposal value into account when he ceases to own an asset representing qualifying expenditure incurred by him (or when such an asset is demolished or destroyed while owned by him). Section 444 gives the chargeable period for which the disposal value is to be brought into account. The disposal value may reduce the allowance which would otherwise have been made in respect of the expenditure for the chargeable period (section 441(1)(b)) or give rise to a balancing charge for the chargeable period (section 442(2)). A balancing charge is given effect as a trading receipt for the chargeable period under section 450(b).

Subsections (2) and (3) of section 444 are based on section 138(2) of CAA 1990. (Subsection (4) reflects a change in the law discussed in Change 51.) Under subsections (2) and (3), the disposal value is brought into account for the chargeable period in which the person ceases to own the asset or it is demolished or destroyed (or, if that is after the chargeable period in which the trade is permanently discontinued, that chargeable period).

But a trade is taxed on the profits of the chargeable period, and the profits are calculated by reference to the expenses and receipts of the trade arising in that chargeable period. Nothing turns on what point in time during the period the receipt arises. So there is no difference whether one says that the receipt accrues at a particular point in time in the period or that it accrues for the period.

So this change in approach does not change the law.

Note 58 Accrual of post-trading additional VAT rebates for allowable research and development expenditure: sections 448(4) and (5) and 549

Section 138(3A) of CAA 1990 provides that in certain circumstances additional VAT rebates in respect of allowable research and development expenditure incurred by a person carrying on a trade are treated as trading receipts of the trade. They are treated as accruing for the chargeable period related to the making of the rebate or—

> "if the rebate is made on or after the date on which the trade is permanently discontinued, accruing immediately before the discontinuance."

Section 448 requires disposal values (or additions to disposal values) to be brought into account for additional VAT rebates in respect of allowable research and development expenditure. The section does not write out expressly the quoted words dealing with discontinuance. But this is not thought to change the law because those words are unnecessary.

The normal rule in section 138(3A) of CAA 1990 is that the trading receipt accrues for the chargeable period related to the making of the rebate. Under section 161(2) of CAA 1990 the "chargeable period related to" the making of the rebate means the chargeable period in which the rebate is made.

Section 159A(3) and (4) of CAA 1990 gives the time at which the rebate is made for this purpose. Section 159A(4)(c) applies if the rebate has not been accounted for on a VAT return to the Customs and Excise Commissioners or assessed by them for VAT purposes before the trade has been permanently discontinued. It provides that the rebate is regarded as made on the last day of the chargeable period related to the discontinuance—in other words the last day of the chargeable period in which the trade is permanently discontinued.

But if the rebate is treated as made on the last day of the chargeable period in which the trade is permanently discontinued, this means that the normal rule in section 138(3A) of CAA 1990 results in the trading receipt accruing for the chargeable period in which the trade is permanently discontinued. The effect of that is the same as providing that the trading receipt is treated as accruing (at a time rather than for a period) immediately before discontinuance. So the words in section 138(3A) concerning discontinuance are unnecessary.

Section 448(4) and (5)(a) provides that the disposal value (or the addition to the disposal value) is to be brought into account for the chargeable period in which the rebate accrues (unless the rebate accrued before the chargeable period in which the trade was set up and commenced—section 448(5)(b)). Under section 549(1) this means—where the trade is discontinued before the rebate is accounted for in a VAT return or assessed by the Commissioners—the chargeable period in which the trade is permanently discontinued. This is the same result as in section 138(3A) of CAA 1990.

Note 59 Same expenditure not to qualify in relation to more than one trade: sections 454(2) and 468(2)

Section 454(2) provides, in relation to know-how allowances, that the same expenditure may not be taken into account as qualifying expenditure in relation to more than one trade. Section 468(2) makes similar provision in relation to patent allowances. These provisions do not appear in ICTA. But they merely make explicit what is implicit and therefore do not change the law.

Section 530(1) of ICTA provides that where a person acquires know-how for use in a trade carried on by him, or acquires know-how and thereafter sets up and commences a trade in which it is used, allowances are to be made to him <u>in respect of his expenditure on the acquisition</u>.

It is clearly implicit in this provision that even if the person acquires the know-how for use in more than one trade carried on by him, the amount of the allowances which may be made to him cannot exceed the amount of his expenditure on the acquisition. It cannot have been intended that a person who spends £1000 on acquiring know-how for use in three trades carried on by him should be entitled to allowances on £3000.

Section 520(1) of ICTA gives rise to the same implication for patent allowances.

So sections 454(2) and 468(2) merely make explicit what is implicit in ICTA and do not change the law.

Note 60 No unrelieved qualifying expenditure to be carried forward from final chargeable period: sections 461(3) and 475(3)

There is nothing in ICTA that corresponds precisely to section 461(3) or 475(3). But these provisions achieve results that are achieved under ICTA by a different route. See also Note 16.

Section 530(1) of ICTA limits the making of know-how allowances and charges to cases where the person concerned is carrying on a trade. The final chargeable period under Part 7 corresponds to the notion in section 530(2)(b) of ICTA of the chargeable period in which the trade is permanently discontinued.

If under section 530(2)(b) a person’s trade has been permanently discontinued, there is no further entitlement to allowances in respect of that trade. Any outstanding expenditure will have been returned to the person by way of a balancing allowance. There is no expenditure to carry forward and the trade which brought the person within section 530(1) has vanished.

Section 461(3) produces the same effect but in a more direct way.

The same reasoning applies in relation to patent allowances in respect of a trade. See sections 520(1), (2)(a) and (4)(b) and 528(1) of ICTA.

A broadly similar analysis applies to patent allowances not made in taxing a trade. Section 520(2)(b) of ICTA provides that patent allowances are not to be made to a person unless any income receivable by him in respect of the rights would be liable to tax. Under section 471(6) the final chargeable period is the chargeable period in which the last of the patent rights in question comes to an end (without any of those rights being revived) or is wholly disposed of. This is based on section 520(4)(c) and (5) of ICTA, but altered as discussed in Change 56.

If in a chargeable period all the patent rights in question have come to an end (without any of those rights being revived) or have been wholly disposed of, there is no further entitlement to allowances in respect of those rights. Any outstanding expenditure will have been returned to the person by way of a balancing allowance. There is no expenditure to carry forward and the patent rights which brought the person within section 520(2)(b) of ICTA have gone.

So section 475(3) does not effect any real change.

Note 61 Giving effect to know-how allowances and patent allowances in respect of a trade: sections 463 and 478

Section 478 provides for the way in which patent allowances in respect of a trade are to be given effect. Section 463 makes similar provision for know-how allowances (which arise only in respect of a trade). Provisions to this effect are not to be found on the face of sections 520 to 533 of ICTA (which provide for patent and know-how allowances). This note explains how sections 478 and 463 are derived.

Section 528(1) of ICTA indicates that patent allowances in respect of a person's trade are to be made "in taxing his trade". Section 532(1) of ICTA requires sections 520 to 533 of ICTA to be read as if they were contained in CAA 1990. Under section 161(5) of CAA 1990, references to allowances or charges being made in taxing a trade are references to their being made in computing the trading income for income tax or corporation tax.

Section 140(1) of CAA 1990 provides that in computing for income tax purposes a person's income, there are to be made all deductions and additions as are required to give effect to the provisions of Parts I to VI and VIII of CAA 1990 relating to capital allowances/charges. And section 140(2) requires allowances to be given effect as trading expenses and charges as trading receipts. Section 144(1) and (2) of CAA 1990 makes similar provision for corporation tax. This is the basis for the rewritten section 478.

Section 532(1) of ICTA requires the patent allowances provisions to have effect as if “contained in the 1990 Act”. Although sections 140(2) and 144(2) of CAA 1990 apply only in relation to Parts I to VI and VIII of CAA 1990, it seems clear that they apply to patent allowances.

First, section 140(5) of CAA 1990 provides that deductions allowable in taxing a trade under Part VII are to be given effect in accordance with section 140(1) and (2). Section 144(3) of CAA 1990 does the same for corporation tax purposes. So sections 140(2) and 144(2) in effect apply to allowances under all Parts of CAA 1990. (Sections 140(5) and 144(3) do not apply to charges under Part VII because section 138(2) and (3A) gives effect to such charges directly as trading receipts.)

Secondly, in relation to corporation tax, the matter was clearer prior to the CAA 1990 consolidation. As mentioned at Note 4, section 532(1) of ICTA had originally treated the ICTA sections as included in Part I of CAA 1968. This ensured that the precursor of section 144(2) (section 73(2) of CAA 1968) applied to patent allowances. As to income tax, the matter was clearer in section 140 of CAA 1990 as enacted. A new section 140 was substituted by section 211 of FA 1994.

The same analysis applies to know-how allowances. Section 530(1) of ICTA does not provide that those allowances are to be made to a person “in taxing his trade”. But it seems clear that this is how they are to be given effect. They only arise in respect of a trade and ICTA makes no other provision for giving effect to them.

Indeed, section 530(6) of ICTA (which gives know-how allowances in respect of know-how acquired after 19th March 1968 and before 1st April 1986) provides expressly that those allowances are to be made “in taxing the trade”. Section 530(6) derives from section 386(1) of ICTA 1970 which was amended in relation to expenditure incurred on or after 1st April 1986 by section 65 of FA 1985. This became section 530(1) of ICTA. The failure to mention “taxing the trade” in section 530(1) may have been simply a drafting slip.

Note 62 Second half of section 532(1) of ICTA and giving effect to non-trade patent allowances: sections 479 and 480 and Schedule 2, paragraphs 49 and 62

The second half of section 532(1) of ICTA provides that any reference in the Tax Acts to a capital allowance to be given “by way of discharge or repayment of tax and to be available or available primarily against a specified class of income” is to include a reference to a capital allowance given in accordance with section 528(2) or (3) of ICTA. Section 528(2) and (3) concerns the way in which patent allowances not made in taxing a trade are given effect for income and corporation tax purposes.

A number of provisions are expressed to apply to allowances given by way of discharge or repayment of tax and available primarily against (rather than available only against) a specified class of income. But it is clear from the legislative history that the second half of section 532(1) of ICTA is not intended to apply those provisions to non-trade patent allowances.

For example, sections 141 and 145 of CAA 1990 apply to capital allowances to be given by way of discharge or repayment of tax and to be "available primarily against" a specified class of income. Section 145(3) to (5) allows the allowance to be used for corporation tax purposes to a limited extent otherwise than against income of the specified class. (Section 141(3) and (4) originally contained similar rules for income tax but these were repealed by FA 1997.)

Section 528(2) and (3) of ICTA appears to set out comprehensive rules for giving effect to non-trade patent allowances. The allowances are permitted to be used only against the person's patent income (i.e. income of the specified class). It would seem bizarre if sections 141 and 145 of CAA 1990 were also intended to apply to such allowances thereby giving a different treatment for corporation tax purposes under section 145(3) to (5). The legislative history confirms that this was not intended.

The origins of section 528(2) and (3) of ICTA can be traced back to section 42(2) of ITA 1945. This was consolidated as section 321(2) of ITA 1952 which provided that non-trade patent allowances were to be made by way of discharge or repayment of tax and "available against" (i.e. only against) income from patents. Certain other allowances under ITA 1952 were to be made by way of discharge or repayment of tax and "available primarily against" income of the specified class.

Section 324(1) of ITA 1952 provided that where an allowance was to be made by way of discharge or repayment of tax and "available, or available primarily, against" a specified class of income, then rules equivalent to section 528(2) of ICTA and section 141(1) and (2) of CAA 1990 applied. But section 324(1) contained a proviso which applied only to allowances "available primarily against" income of a specified class— and therefore not to non-trade patent allowances. This was the forerunner of section 141(3) and (4) of CAA 1990.

When corporation tax was introduced in 1965, provisions equivalent to section 324(1) of ITA 1952 were included. See section 56(3) and (5) to (7) of FA 1965 (the forerunner of section 145 of CAA 1990).

The patent allowances provisions of ITA 1952 were consolidated in ICTA 1970. The rules for giving effect to allowances available only against a specified class of income were written out in full as sections 385(2) and (3) of ICTA 1970, which became section 528(2) and (3) of ICTA.

So it is clear from the legislative history that sections 528(2) and (3) of ICTA are intended to be comprehensive and that sections 141 and 145 of CAA 1990 are not meant to apply to non-trade patent allowances. Those allowances were originally given by way of discharge or repayment of tax and available only against income of the specified class (i.e. income from patents) and the position has not been changed by consolidation.

The second part of section 532(1) of ICTA (which derives from section 387(1) of ICTA 1970) cannot have been intended to apply to patent allowances rules which formerly applied only to allowances available primarily (not available only) against a specified class of income, because such rules had not formerly applied to patent allowances. It was presumably intended to ensure that any remaining rule in the Tax Acts which applied to non-trade patent allowances would continue to apply to them. Without it, any such rule would have ceased to apply when the words from section 321(2) of ITA 1952 that such allowances were to be "available against income from patents" were dropped on writing out the giving effect provisions in full in sections 385(2) and (3) of ICTA 1970.

Why did section 387(1) of ICTA 1970 include the words "or available primarily against a specified class of income"? The answer seems to be that there was only one additional rule which applied to non-trade patent allowances—namely section 528(5)(c) of ICTA 1970—and it applied to both kinds of allowance. The quotation marks used in section 387(1) and the fact that section 528(5)(c) refers expressly to section 387(1) suggests that section 387(1) was aimed specifically at that provision.

One might also wonder why section 387(1) of ICTA 1970 referred to both subsections (2) and (3) of section 385 when section 528(5)(c) concerns only income tax. This may have been as a matter of caution in case any other references had not been identified.

Section 528(5)(c) of ICTA 1970 was consolidated as section 835(8)(c) of ICTA. That is the only provision which applies to allowances to be given by way of discharge or repayment of tax and available only against a specified class of income. So the Act simply amends it to refer directly to allowances under section 479—see paragraph 62 of Schedule 2—and the second half of section 532(1) of ICTA has not been rewritten—see paragraph 49 of Schedule 2.

Note 63 Giving effect to non-trade patent allowances: section 479

In addition to the comments at Note 62, there are two further points to make about section 479. First, the words "and tax shall be discharged or repaid accordingly" in section 528(2)(b) of ICTA have been dropped for the reasons given in Note 40.

Secondly, the words "Relief shall be given under this subsection on the making of a claim" have not been rewritten. One might think that they require two claims to be made—one for the allowance and one for relief to be given. But that does not seem right because the relief given under section 528(2) of ICTA is an allowance (or a carried-forward part of an allowance). The words seem intended merely to require the claim for the allowance to be made under section 42 of TMA 1970. But section 3(4)(c) does that.

Note 64 Writing-down and balancing allowances for dredging: sections 487(7) and 488

Section 487(7) provides that a person is not entitled to a writing-down allowance for a chargeable period in which a balancing allowance is made. In contrast, section 134(2) of CAA 1990 enables a person to have a balancing allowance in addition to a writing-down allowance.

But there is no difference in the effect, because under section 134(2) of CAA 1990, the amount of the balancing allowance is the amount of the original expenditure less any writing-down allowances made, including the writing-down allowance for the period in which the balancing allowance is made.

Section 488 enables a balancing allowance to be made if the qualifying trade is either permanently discontinued or sold.

This approach is different from that taken in section 134(2) and (4) of CAA 1990. Subsection (2) of section 134 provides for a balancing allowance if the trade is permanently discontinued. But subsection (4) then extends the notion of permanent discontinuance to include most sales. It then has to include a caveat to ensure that a company reconstruction of a kind dealt with in section 343(2) of ICTA is not swept in. (Section 343(2) provides for this kind of company reconstruction not to be treated as a permanent discontinuance.)

The more direct approach taken in section 488 (which avoids deeming a sale to be a permanent discontinuance of a trade) does not change the effect and has the advantage that it obviates the need to refer to section 343(2) of ICTA.

Note 65 Reference to sections 85 to 90 in section 91(1)(a) of CAA 1990: sections 502 and 503

Sections 502 and 503 clear up a possible source of confusion arising as a result of a slip made in the consolidation that produced CAA 1990. But it is not thought that they change the effect of the law.

Sections 502 and 503 deal with a situation where a person buys a building before the first use of any dwelling-house in the building. They treat the person as having incurred qualifying expenditure.

In contrast, section 91(1) of CAA 1990 treats the person as having incurred expenditure for the purposes of sections 85 to 90 of CAA 1990. This reference to sections 85 to 90 does not include section 96 of CAA 1990. Section 96 identifies what is the expenditure "appropriate" to a dwelling-house. (This idea is re-labelled expenditure "attributable" to a dwelling-house in section 511.) The significance of expenditure being appropriate (or attributable) to a dwelling-house is that a person's entitlement to writing-down allowances turns on this expenditure.

The fact that section 91(1) of CAA 1990 does not refer to section 96 is the result of a slip made when the provisions relating to assured tenancy allowances were consolidated in 1990. Section 91(1) derives from paragraph 8(1) of Schedule 12 to FA 1982. Paragraph 8(1) treated the person as having incurred expenditure for the purposes of "the preceding provisions of this Schedule". The preceding provisions of the Schedule included paragraph 1(4), the forerunner of section 96 of CAA 1990.

Despite the slip just described, it is extremely difficult to imagine anyone reading section 96 of CAA 1990 as if it did not apply in relation to the purchase expenditure dealt with in section 91. Quite apart from the common sense of the matter, section 96(3) provides that expenditure is appropriate to a dwelling-house only if it was incurred after 9th March 1982 and before 1st April 1992 "or is deemed to have been so incurred by virtue of section 91". This shows that the limited reference in section 91(1) to sections 85 to 90 should not be taken at its face value.

Note 66 Calculation of allowance after sale of relevant interest: section 509(2) (definition of "B")

Section 509(2) provides a formula for calculating the amount of the writing-down allowance where there is a sale of the relevant interest and a balancing adjustment falls to be made as a result of the sale. In the formula "B" is defined as the length of the period from the date of the sale to the end of the period of 25 years beginning with the day on which the <u>dwelling-house</u> was first used.

In contrast, section 85(3) of CAA 1990 refers to the period of 25 years beginning with time when the <u>building</u> was first used.

The reference in section 85(3) to the building is a mistake probably arising because many of the provisions in the code for assured tenancy allowances were copied from the industrial buildings allowances code (where "building" is correct).

Section 85(3) has been treated as if it referred to the time when the "dwelling-house" was first used, because anything else would produce absurd results. Assured tenancy allowances are based on use of the building as a dwelling-house (or as dwelling-houses). So the legislation has been rewritten to reflect the way it has been, and needs to be, operated in practice.

Note 67 Giving effect to assured tenancy allowances: section 529

Section 529 is based on section 92 of CAA 1990, but does not contain anything to reflect section 92(1). This is because section 92(1) is not needed.

Section 92(1) of CAA 1990 provides for assured tenancy allowances (and charges) to be given effect in taxing the profits of the trade.

Many capital allowances are given in effect "in taxing the trade". But those who can claim assured tenancy allowances will be carrying on Schedule A businesses. They do not need a provision enabling allowances and charges to be given effect in taxing the trade.

Section 161(5) of CAA 1990 provides that any reference to allowances or charges being made in taxing a trade (i.e., the words used in section 92(1)) is a reference to their being made in computing the trading income for tax purposes. But section 161(5) does not apply for the purposes of assured tenancy allowances (see section 161(10)). This is evidence that section 92(1) is the result of an error.

Section 92 of CAA 1990 was substituted by paragraph 58 of Schedule 5 to FA 1998. Before 1998, assured tenancy allowances were given effect against Schedule A income (and primarily against income coming from letting qualifying dwelling-houses) and there was no provision for giving effect to allowances in taxing the trade. It seems fairly clear that it was assumed that assured tenancy allowances needed the standard form "in taxing the trade" provision and that the peculiar characteristics of assured tenancy allowances were overlooked.

Note 68 Contributions for purposes of tenant's trade: sections 538(1) and 541(1)

Sections 538(1) and 541(1), which deal with the entitlement of a person to contribution allowances under Parts 2 and 5, are based on section 154(1) of CAA 1990 as applied, in the case of plant and machinery, by section 154(2).

Section 154(1) of CAA 1990 is a general provision dealing with entitlement to contribution allowances under Parts I, IV and V of CAA 1990. It deals with the case where—

> "a person, for the purposes of a trade carried on by him <u>or by a tenant of land in which he has an interest</u> contributes a capital sum . . ."

In contrast, sections 538(1) and 541(1) do not mention the situation where the person contributes a capital sum for the purposes of a tenant's trade. At first sight, this might appear to change the effect of the legislation. But this is not in fact the case.

The way in which section 154(1) of CAA 1990 enables the contributor to obtain allowances is by creating a fiction that the contributor has incurred expenditure on the provision of an asset for the purposes of the contributor's or the tenant's trade. Section 154(2) modifies section 154(1) to address the complications of pooling under Part II of CAA 1990 but the fiction is essentially the same.

In the case of contribution allowances under Parts I and V of CAA 1990 (Parts 3 and 4 of the Act), a tenant's trade is relevant to entitlement to allowances. But a tenant's trade is irrelevant to entitlement to allowances under Parts II and IV of CAA 1990 (Parts 2 and 5 of the Act). In order for the case where the contributor makes the contribution for the purposes of a tenant's trade to work for plant and machinery allowances and mineral extraction allowances, section 154(1) of CAA 1990 would have needed to extend the fiction it creates so as to deem the contributor to be carrying on the tenant's trade.

The change discussed in Change 59 extends entitlement to contribution allowances so that persons making contributions for the purposes of property businesses can obtain contribution allowances. So, for the purposes of Part 2, the limited nature of the fiction in section 154(1) and (2) of CAA 1990 has been overcome and landlords will be able to obtain contribution allowances under Part 2.

Note 69 Management of life assurance business: section 544(4)

Section 544(4) qualifies the meaning given to a reference to the management of a life assurance business. The basic meaning is that the management of a life assurance business consists of pursuing those purposes expenditure on which would be treated as expenses of management under section 75 of ICTA as applied by section 76 of ICTA (see section 544(3)). The qualification in section 544(4) is that, when applying this definition, section 76(1)(d) of ICTA is to be disregarded.

Section 544(3) is based on section 434D(7) of ICTA; but there is nothing in section 434D corresponding to section 544(4). The qualification in section 544(4) is, however, merely meant to bring out what it is implicit in ICTA.

Section 434D of ICTA is meant to govern when and how capital allowances are available in respect of assets provided for use, or used, for the management of a company's life assurance business.

Section 434D(7) of ICTA provides—

> "For the purposes of this section the purposes of the management of a business shall be taken to be those purposes expenditure on which would be treated as expenses of management within section 76."

Section 76(1)(d) of ICTA says that—

> "the amount treated as expenses of management shall not include any amount in respect of expenses referable to pension business, life reinsurance business or overseas life assurance business".

(This is modified by statutory instrument to include individual savings account business.) But taking section 76(1)(d) into account in applying section 434D(7) would make a nonsense of section 434D. Assets held for the purposes of pension business, ISA business, life reinsurance business or overseas life assurance business would appear not to be management assets. So the special rules in section 434D(3) to (5) for giving effect to plant and machinery allowances in the case of these categories of life assurance business would be completely pointless. This suggests that it cannot be the intention that section 76(1)(d) of ICTA is meant to be taken into account in applying section 434D(7) of ICTA.

Note 70 Time when additional VAT rebates "accrue": section 549, Table, column 3, item 1

Section 549, Table, column 3, item 1, gives a time when an additional VAT liability or rebate "accrues". This reflects the only intelligible way of reading section 159A(4)(a) of CAA 1990.

Section 159A of CAA 1990 gives two meanings to the idea of when an additional VAT liability is incurred or an additional VAT rebate is made. The first is to be found in section 159A(1). The second is to be found in section 159A(3) and (4). This Act uses different words to describe the two different meanings: it uses "accrue" to describe the second meaning.

Under section 159A(3) of CAA 1990—

> "An additional VAT liability or rebate shall, for the purpose only of determining the chargeable period—
>
> (a) for which an allowance or charge under this Act may be made . . . , or
>
> (b) in which the amount of the liability or rebate is to be brought into account in connection with the making of such allowances or charges,
>
> be regarded as incurred or made at a time determined in accordance with subsection (4) . . ."

It is clear from the concluding words of section 159A(3) of CAA 1990 that each of the paragraphs in section 159A(4) is meant to produce a "time" at which the liability is incurred or the rebate is made. Paragraphs (b) and (c) do so. But the wording in paragraph (a) is garbled.

Section 159A(4) of CAA 1990 provides—

> "(4) For the purpose of determining the chargeable period referred to in subsection (3) above—
>
> (a) where a return for the purposes of value added tax is made to the Commissioners of Customs and Excise in which the liability or rebate is accounted for, the liability or rebate shall be regarded as incurred or made <u>in the chargeable period which includes</u> the last day of the period to which that return relates; but
>
> (b) if, before any such return is made, those Commissioners assess the liability or rebate as due or repayable, then, notwithstanding paragraph (a) above, the liability or rebate shall be regarded as incurred or made <u>on</u> the day on which that assessment is made; and

(c) if the additional VAT liability or rebate has not been accounted for on a return for the purposes of value added tax to those Commissioners, or assessed by them for those purposes, before the trade in question has been permanently discontinued or treated by any provision of the Tax Acts as permanently discontinued, then, notwithstanding paragraphs (a) and (b) above, the liability or rebate shall be regarded as incurred or made <u>on</u> the last day of the chargeable period related to the discontinuance."

Various provisions of CAA 1990 refer, in connection with making allowances and charges for a chargeable period, to the time when the liability is incurred or made. (See, for example, section 3(2A), (2B) and (2C).) For these provisions to work, it is necessary to infer what time is meant to be supplied by section 159A(4)(a). It seems clear that the time that is meant to emerge from section 159A(4)(a) is the last day of the period to which the VAT return relates. (I.e., paragraph (a) should have said, instead of "in the chargeable period which includes", "on".) Item 1 of the Table in section 549 reflects this interpretation.

Note 71 Disposal of oil licences relating to undeveloped areas: meaning of "material disposal": section 553(3)

Section 118A of CAA 1990 derives from section 62 of FA 1988. When the TCGA 1992 consolidation was prepared, the capital allowances aspects of section 62 of FA 1988 were put into CAA 1990 by way of amendment. Section 118A(4) imported the lengthy definitions needed for section 62 (many of which were contained in section 64 of FA 1988) by providing that "expressions used in this section and in section 194 of the Taxation of Chargeable Gains Act 1992 have the same meaning in this section as in that Act".

The approach taken in the Act is, on this occasion, to incorporate the definitions. (The meaning of "undeveloped area", for example, is crucial to the effect of the main proposition.) But to incorporate the definitions correctly it is necessary to know what section 118A(4) of CAA 1990 was meant to import.

The only question of any difficulty is whether section 118A(4) of CAA 1990 is meant to import the definition of "material disposal" in section 194(1) of TCGA. At first blush, one might conclude that it should be imported. It is a phrase which appears to add a further qualification to "material disposal", over and above what is said in section 118A(2). But it is clear from section 62(2)(a) of FA 1988 that section 194(1) should not be imported. Section 62(2)(a) expressed the exclusion of disposals made otherwise than by way of bargains at arm's length to be "so far as concerns the 1979 Act". There is a presumption that a consolidation does not change the law. The Act takes the opportunity to make clear that section 118A(4) did not inadvertently change the law.

Section 118A(2) of CAA 1990 comes from section 62(2)(b) of FA 1988 which refers to "a disposal in relation to which Schedule 7 to the Capital Allowances Act 1968 has effect".

This was translated by the consolidator as “a disposal in relation to which sections 157 and 158 have effect” but the word “and” was plainly a mistake; the consolidated provision should have said “or”. Section 553(3) reflects this construction by referring to “section 562 or 563”.

Note 72 Omission of section 150(5)(a) of CAA 1990: section 562(5)

Section 562(5) is based on section 150(5) of CAA 1990 but contains nothing to reflect section 150(5)(a).

Section 150(5) of CAA 1990 provides—

> “The reference in subsection (1) above to expenditure incurred on the provision or the purchase of property shall in relation to sections 98 to 118 be deemed to include—
>
> (a) a reference to expenditure on the acquisition of, or rights in or over, mineral deposits;
>
> (b) a reference to expenditure on the acquisition of land; and
>
> (c) a reference to expenditure on the acquisition of a mineral asset.”

Section 150(5)(a) of CAA 1990 is redundant because of the definition of “mineral asset” in section 121(1) of CAA 1990. That definition is—

> ““mineral asset” means any mineral deposits or land comprising mineral deposits, or any interest in or right over such deposits or land”.

The precursor of section 150(5) of CAA 1990, section 77(4) of CAA 1968, needed all three paragraphs because each paragraph operated for different sections of the previous code for mines and oil wells (sections 53, 54 and 60 of CAA 1968 respectively).

Paragraph 2(1) of Schedule 13 to FA 1986 treated what was then a new code for minerals extraction allowances as if it were contained in Chapter III of Part I of CAA 1968 so that the supplementary provisions in Chapter VI of that Part could apply. Paragraph 2(2) of Schedule 13 to FA 1986 then provided that in section 77(4) of CAA 1968 any reference to a specific provision of the 1968 Act included a reference to the new code for mineral extraction allowances.

Paragraph (a) of section 77(4) of CAA 1968 could have been dropped when section 77(4) was consolidated as section 150(5) of CAA 1990. It has been dropped now because it serves no purpose.

Note 73 Omission of section 157(3) of CAA 1990: sections 567 to 570

Sections 567 to 570 come from sections 157 and 158 of CAA 1990. They provide for a sale of property to be treated as being at market value if it is between connected persons or involves a control relationship or is to obtain a tax advantage. They enable an election to be made (except in a tax advantage case) for the sale to be treated as being at a smaller amount.

Sections 567 to 570 do not contain anything to reflect section 157(3) of CAA 1990. Section 157(3) provides—

> "This section and section 158 shall have effect in relation to a sale notwithstanding that they are not fully applicable by reason of the non-residence of a party to the sale or otherwise, but subject to subsection (3) of that section."

The effect is that sections 157 and 158 apply even if a party to the sale is not resident in the UK. But this would be the position even in the absence of section 157(3). There is nothing to prevent the provisions applying to non-residents. So the omission of section 157(3) does not change the law.

The provision that became section 157(3) was originally enacted in section 23(a) of FA 1954.

Section 23(a) of FA 1954 prohibited an election from being made under paragraph 4 of Schedule 14 to ITA 1952 (the precursor of section 158) if (i) any of the parties to the sale was not resident at the time of the sale, and (ii) the circumstances at the time of the sale were not such that an allowance or charge might be made to or on the non-resident as a result of the sale. But section 23(a) provided that, with that exception, Schedule 14 to the 1952 Act (the precursor of sections 157 and 158) applied even if one of the parties to the sale was non-resident.

As the rule in section 23(a) prohibiting an election applied only if one of the parties to the sale was non-resident, it might have been considered helpful (though even at that time not strictly necessary) to tell taxpayers that non-residence did not prevent the rest of the rules in Schedule 14 to the 1952 Act from applying.

Section 23(a) was consolidated as paragraphs 1(2) and 4(3) of Schedule 7 to CAA 1968. Those paragraphs became sections 157(3) and 158(3)(a) of CAA 1990. As enacted, section 158(3)(a) was in very similar terms to section 23(a)(i) and (ii) of FA 1954.

But section 117(4) of FA 1993 replaced section 158(3)(a) with a new paragraph that prohibited an election from being made, irrespective of whether or not a party to the sale was non-resident, if the circumstances of the sale were such that an allowance or charge that might otherwise have been made would not be capable of being made.

So, since 1993, there has been nothing in sections 157 and 158 to suggest that residence or non-residence is relevant in determining whether, or the extent to which, the provisions apply. So it is no longer necessary to retain section 157(3).

Note 74 Section 161(3) of CAA 1990: section 577 (and sections 27(1) and 468(1) and paragraph 94(2) of Schedule 3)

Section 161(3) of CAA 1990 comes from paragraph 1 of Schedule 29 to ICTA, which in turn came from section 23(2)(b) of FA 1974.

Section 23(2)(b) was needed because in 1974 capital allowances were treated as not being available for trades, professions and vocations whose income was chargeable under Case V (or possibly Case IV) of Schedule D. That treatment was based on provisions that have not survived the self-assessment reforms made in 1994.

The only possible need for section 161(3) now is in relation to provisions which still contain an explicit reference to Case I or II of Schedule D. There are very few of these and the effect of section 161(3) has therefore been incorporated in the relevant provisions of the Act (sections 27(1) and 468(1) and paragraph 94(2) of Schedule 3).

Note 75 Amendment of sections 117, 118 and 393A of ICTA and paragraph 2 of Schedule 2 to the Social Security Contributions and Benefits 1992: Schedule 2, paragraphs 22, 23, 32, 75 and 76)

Paragraphs 22, 23, 32, 75 and 76 of Schedule 2 repeal various provisions that are deadwood, essentially because there are no longer any allowances that can be given to traders by way of discharge or repayment of tax. The point is similar in relation to each of the repeals.

Paragraphs 22 and 23 of Schedule 2 repeal provisions in sections 117 and 118 of ICTA.

Section 117(1)(b) of ICTA, and the definition of "the aggregate amount" in section 117(2), refer to an allowance under section 141 of CAA 1990 which falls to be made to a person either in taxing the trade or by way of discharge or repayment of tax and to which he is entitled by reason of his participation in a trade. Section 118 makes provision corresponding to section 117 for companies (but refers to an allowance under section 145 of CAA 1990).

Section 141 of CAA 1990 (and its precursor, section 71 of CAA 1968) does not provide for allowances in taxing the trade. Similarly, section 145 of CAA 1990 (and its precursor, section 74 of CAA 1968) does not provide for allowances in taxing the trade. So the references to allowances given under sections of CAA 1990 in taxing the trade appear to be unnecessary. There are now no allowances that can be made under section 141 or 145 of CAA 1990 by way of discharge or repayment of tax to which the individual is entitled by reason of his participation in a trade.

It used to be possible for allowances to be given to traders by way of discharge or repayment in respect of agricultural buildings. But paragraph 11 of Schedule 15 to FA 1986 got rid of this rule and provided for agricultural buildings allowances to be made in taxing the trade.

Paragraph 32 of Schedule 2 repeals subsections (5) and (6) of section 393A of ICTA for similar reasons. Section 393A was inserted by section 73 of FA 1991 but the references to allowances "in respect of the trade" being made by discharge or repayment of tax are no longer needed. Although the system of giving effect to agricultural buildings allowances by discharge or repayment was replaced in 1986 (see above), section 393A could have continued to give relief until 1997 (because of the 10 year writing off period for allowances under the old system). But subsections (5) and (6) are now redundant.

Paragraphs 75(2) and 76(2) of Schedule 2 repeal parts of paragraph 2 of Schedule 2 to the Social Security Contributions and Benefits Act 1992 and the corresponding Northern Ireland Act (as amended by section 59(2) of the Social Security Act 1998). The amendment made by the Social Security Act 1998 appears to be a mistake. There was no need for the 1998 Act to amend paragraph 2 so as to refer to allowances given by way of discharge or repayment of tax, because the only allowances that paragraph 2 could have referred to were the old agricultural buildings allowances that by 1998 were no longer available.

Note 76 "Relevant period" in new section 40B(2) of F(No.2)A 1992: Schedule 2, paragraph 82

Paragraph 82 of Schedule 2 inserts new sections 40A to 40D into F(No.2)A 1992. The new sections come from section 68 of CAA 1990, which makes provision for the tax treatment of expenditure relating to films.

The new section 40B deals with the allocation of revenue expenditure on films to "relevant periods". Section 40B(3) defines "relevant period" as (a) a period for which accounts are drawn up or (b) if no accounts are drawn up for a period, the accounting period of a company within the corporation tax charge or (in other cases) the period the profits or gains of which are taken into account in assessing the income for the tax year.

Section 40B(3) comes from the closing words of section 68(3) of CAA 1990. Section 68(3) defines "relevant period" in different terms but the effect is the same.

In section 68(3), "relevant period" is defined as a period for which accounts are made up or "if those accounts are not made up for any period" a period the profits or gains of which are taken into account in assessing the income for "any chargeable period".

Section 68(3) describes the second case as one in which "those accounts are not made up for any period". "Those accounts" must mean accounts of the trade or business concerned. But the other words are ambiguous: the case described could be one where accounts of the trade or business are drawn up, but are not drawn up for a period. Alternatively, it could be one where no accounts are drawn up, either in relation to a particular period or at all.

The first interpretation of the words would be nonsensical: it is implicit that accounts relate to a period. So section 40B(3)(b) makes clear that the second case is one where no accounts are drawn up for a particular period. (The alternative would be for it to describe the second case as one where no accounts had ever been drawn up; but that would probably be more restrictive than section 68(3) and would mean that cases where accounts had been drawn up for some previous years were not covered.)

For the "no accounts" case, section 68(3) defines the relevant period in terms of the period the profits or gains of which are taken into account in assessing income for a "chargeable period". "Chargeable period" is defined in section 161(2) of CAA 1990 as an accounting period of a company or a period of account.

So, for a company, "relevant period" means the period the profits or gains of which are taken into account in assessing income for an accounting period of the company. Where the company is within the charge to corporation tax, section 12(1) of ICTA provides for that period to be the accounting period. So section 40B(3)(b)(i) provides simply for the accounting period to be the relevant period in that case.

The other alternative for the "no accounts" case is the period the profits or gains of which are taken into account in assessing income for a period of account. "Period of account" is defined in section 160 of CAA 1990. Section 160(2) provides for "period of account" to mean the period for which accounts are made up, in the case of a person carrying on a trade profession or vocation. This cannot be relevant for the "no accounts" case. In the case of other persons, section 160(5) defines "period of account" as the tax year.

So, for taxpayers who have not drawn up accounts, other than companies within the charge to corporation tax, "relevant period" must mean the period the profits or gains of which are taken into account in assessing the income of the tax year. Section 40B(3)(b)(ii) reflects this.

Note 77 Provisions re-phasing expenditure incurred before 1st April 1987, etc. not reproduced in Schedule 3

Sections 39(2)(a) and (8)(a), 40(4)(a) and (b)(ii), 45, 47 and 49 of CAA 1990 ("the old expenditure provisions") are not reproduced in Schedule 3 for the reasons which follow.

The old expenditure provisions are either spent or are very nearly spent. They re-phase excessive relief for expenditure on the provision of plant or machinery where—

(a) the expenditure was incurred before 1st April 1987 or, in the case of expenditure to which section 22 of CAA 1990 applies by virtue of subsection (2) or (3) of that section ("section 22 expenditure"), a written offer of financial assistance was made in respect of it before 14th March 1984;

(b) a first-year allowance has been made in respect of the expenditure or, in the case of expenditure as respects which section 70(3) of FA 1982 had effect ("section 70(3) expenditure"), writing-down allowances have been made in respect of it; and

(c) the plant or machinery has been used for a non-qualifying purpose during the requisite period.

The requisite period is the period of 4 years beginning with the date on which the plant or machinery was brought into use or, in the case of section 70(3) expenditure, the period of 10 years beginning with that date.

It follows that the only cases in which the old expenditure provisions can still apply are those where the plant or machinery is or was brought into use after 1st April 1996 or, in the case of section 70(3) expenditure, after 1st April 1990. Such cases would require the taxpayer—

(a) in the case of expenditure which is neither section 22 nor section 70(3) expenditure, to delay bringing the plant or machinery into use for a period of at least 9 years;

(b) in the case of section 22 expenditure which is not also section 70(3) expenditure, to delay incurring the expenditure, and bringing the plant or machinery into use, for an aggregate period of at least 12 years;

(c) in the case of section 22 expenditure which is also section 70(3) expenditure, to delay incurring the expenditure, and bringing the plant or machinery into use, for an aggregate period of at least 6 years;

(d) in the case of section 70(3) expenditure which is not also section 22 expenditure, to delay bringing the plant or machinery into use for a period of at least 3 years.

Delays of this magnitude are not completely unknown. But they are the exception rather than the rule. There is no point in incurring expenditure on the provision of plant or machinery for use for the purposes of a trade unless it needs to be used within months rather than years.

The old expenditure provisions operate to delay allowances or deny them altogether. Not reproducing them would either have no effect (if they are wholly spent) or have a wholly relieving effect (if they are not).

Section 111, which reproduces section 46 of CAA 1990 (new expenditure for overseas leasing), cannot readily be adapted to save the effect of the old expenditure provisions. And reproducing those provisions in Schedule 3 would oblige users of the Act to plough through some very convoluted material only to conclude (in every or almost every case) that it was of no relevance whatever.

Finally the old expenditure provisions operate by reference to the pool for leased assets and inexpensive cars. Subsection (1) of section 74 of FA 2000 abolishes that pool for chargeable periods ending on or after relevant date (the appropriate day in April 2000 or, if the taxpayer so elects, in April 2001). Subsections (2) and (3) of that section make provision for dealing with expenditure already allocated to the pool. But that section does nothing for expenditure which, but for the pool's abolition, might have been allocated to the pool in the future. It is doubtful therefore whether, to the extent that they are not spent, the old expenditure provisions are still capable of having effect.

Note 78 Tunnel undertakings: section 18(11) of CAA 1990 not reproduced in Schedule 3

Item 7 in Table B in section 274 is a tunnel undertaking. This comes from section 18(1)(c) of CAA 1990. Section 18(1)(c) is subject to section 18(11). But there is nothing in Schedule 3 to reflect section 18(11) since the need for it has long since passed.

Subsections (1)(c) and (11) of section 18 derive from section 25(1) and (3) of FA 1952 (by way of section 7(1)(c) and (7) of CAA 1968).

Section 25 was the product of an amendment at the Report Stage of the Finance Bill 1952. The purpose of section 25(3) was to ensure that there were not even any hypothetical circumstances in which a charge could be imposed when the provision was introduced. This was necessary for reasons of parliamentary procedure when the amendment was being made at Report Stage to ensure that the amendment was not out of order. The need for this provision has long since passed and nothing will be lost by not reproducing it.