

# **INCOME TAX (TRADING AND OTHER INCOME) ACT 2005**

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## **EXPLANATORY NOTES**

### **COMMENTARY ON SECTIONS**

#### **Part 2: Trading income**

##### ***Chapter 5: Trade profits: rules allowing deductions***

###### **Overview**

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

##### ***Section 56: Professions and vocations***

235. This section makes it unnecessary to specify repeatedly that the rules in this Chapter (apart from sections 87 to 90) apply to a profession or vocation as well as to a trade. It is new.

##### ***Section 57: Pre-trading expenses***

236. This section gives relief for expenses incurred before a trade starts. It is based on section 401(1) of ICTA.

237. Originally section 401 of ICTA gave relief by creating a loss for the tax year in which the expense was incurred. It was amended to allow the expense as a deduction on the first day of trading.

238. *Subsection (1)* sets the scene. Consistent with other rules in this Part, it refers to the “date” on which (instead of the “time” when) a person starts to trade.

239. *Subsection (2)* identifies the expenses that are allowed by the section. They are expenses that would be allowable if incurred after the start of the trade.

##### ***Section 58: Incidental costs of obtaining finance***

240. This section gives relief for certain costs incurred in obtaining a loan, or an abortive loan. It is based on section 77(1),(2),(6) and (7) of ICTA.

241. Without this section, no deduction would be allowed for the incidental costs of raising a loan on capital account.

242. *Subsection (2)* defines “incidental costs of obtaining finance”. Expenses incurred in the course of obtaining finance *other than* those listed in subsection (2) are subject to the rules restricting or allowing deductions in the usual way.

**Section 59: Convertible loans and loan stock etc.**

243. This section excludes from relief under section 58 costs relating to certain convertible securities. It is based on based on section 77(3),(4) and (5) of ICTA

**Section 60: Tenants under taxed leases: introduction**

244. This section and the following five sections entitle a tenant who uses land for the purposes of a trade to a deduction in calculating the profits of the trade for expenses which he or she is treated as incurring if the land is held under a lease which gives rise to an amount brought into account under Chapter 4 of Part 3 of this Act. Chapter 4 of Part 3 of this Act is based on sections 34 to 38 of ICTA. This section is based on section 87(1),(2) and (8) of ICTA.

245. **Sections 277 to 286** treat certain amounts received by landlords as receipts of a property business. Sections 291 to 294 give a tenant carrying on a property business relief in the form of a deduction for expenses which the tenant is treated as having incurred. In rewriting section 87 of ICTA, sections 60 to 65 follow the same approach as sections 291 to 294 of this Act by giving relief in the form of a deduction for expenses which the tenant is treated as having incurred.

246. Section 87(2) of ICTA treats a person who occupies for the purposes of a trade land in relation to which any amount “falls to be treated as a receipt of a Schedule A business” by virtue of section 34 or 35 of ICTA as paying rent. In accordance with the policy of treating UK and overseas property businesses in the same way as far as possible, section 60(1) of this Act extends relief under section 87(2) of ICTA to a person who occupies for the purposes of a trade land outside the United Kingdom in relation to which any amount falls to be treated as a receipt of an overseas property business by virtue of section 34 or 35 of ICTA as applied by section 65A(5) of ICTA. See *Change 13* in Annex 1.

247. The amount which a tenant can deduct in respect of rent which he or she is treated as paying under section 87(2) of ICTA is qualified by:

- the general rules as to deductions not allowable in computing the profits of a trade in section 74(1) of ICTA; and
- rules prohibiting or restricting the deduction of specific expenditure elsewhere in ICTA.

248. In this Act, the rules restricting deductions are to be found in Chapter 4 of Part 2. Section 74(1)(a) of ICTA is rewritten in section 34 of this Act. Section 60(3) of this Act preserves the interaction of section 87(2) of ICTA and the general and specific rules restricting deductions in ICTA by providing that a deduction for an expense which a tenant is treated as incurring under section 61 of this Act is subject to the application of any provision of Chapter 4 of this Act.

**Section 61: Tenants occupying land for purposes of trade treated as incurring expenses**

249. This section treats a tenant under a lease in respect of which an amount is brought into account by the landlord under sections 277 to 282 (a “taxed lease”) as incurring an expense for each day on which the property held under the lease is occupied for the purposes of his or her trade. It is based on section 87(2),(3) and (9) of ICTA.

250. **Sections 277 to 282** rewrite sections 34 and 35 of ICTA. Sections 34 and 35 of ICTA treat premiums and certain other amounts in respect of leases as rent. In sections 277 to 282, a person who receives a premium, or an amount treated as a premium in section 34 or 35 of ICTA, is instead treated as entering into a transaction mentioned in section 264 (if the land to which the lease relates is in the United Kingdom) or in section 265 (if the land is outside the United Kingdom). This gives rise to a UK or overseas property

business (as defined in sections 264 and 265) if the recipient is not already carrying on such a business.

251. [Sections 277 to 282](#) then require the recipient to bring an amount in respect of the premium or other amount payable under the lease into account as a receipt in calculating the profits of his or her property business.
252. Section 87(2) of ICTA treats a tenant who occupies land for the purposes of a trade as paying rent. This corresponds to the treatment in sections 34 and 35 of ICTA of a landlord who receives a premium, or an amount treated as a premium, as rent.
253. *Subsection (1)* instead treats the tenant as incurring an expense in respect of the land subject to the taxed lease. This corresponds to the treatment of the premium or other amount in respect of the land as a receipt in calculating the profits of the landlord's property business in sections 277 to 282 of this Act.
254. Section 87 of ICTA says that the tenant is treated as paying rent for the purposes of making deductions in calculating the profits of a trade. But the tenant is only entitled to a deduction if at least some of the property is used for the purposes of the trade. So *subsection (3)* defines a qualifying day as a day on which the tenant occupies all or a part of the land subject to the taxed lease for the purposes of carrying on a trade.
255. The formula in *subsection (4)* calculates the expense for each qualifying day by spreading the amount of the taxed receipt evenly over the receipt period of that receipt. Defining "A" in that formula as "the unreduced amount of the taxed receipt" makes clear that the amount of the expense which the tenant is treated as incurring for each qualifying day is calculated by reference to the amount of the taxed receipt *before* any reductions or deductions.
256. *Subsection (5)* modifies that formula for a qualifying day on which the tenant occupies only part of the land subject to the taxed lease for the purposes of a trade.
257. Section 87(3) of ICTA requires a "just apportionment" to be made where part only of the land subject to the lease is used for the purposes of the trade. *Subsection (5)* instead requires the fraction of the land which is occupied by the tenant for the purposes of the trade to be calculated "on a just and reasonable basis". See *Change 14* in Annex 1.

### ***Section 62: Limit on deductions if tenant entitled to mineral extraction allowance***

258. This section prevents a double deduction where a tenant is entitled under section 403 of CAA to an allowance in respect of qualifying expenditure on acquiring a mineral asset. It is based on section 87(7) of ICTA.
259. Section 87(7) of ICTA refers to an allowance for "any chargeable period". Section 832 of ICTA defines chargeable period (other than in the case of an accounting period of a company) as a year of assessment. So this section refers instead to an allowance for "a tax year".

### ***Section 63: Tenants dealing with land as property employed for purposes of trade***

260. This section applies to a tenant who, while not occupying a property, uses the property for the purposes of a trade – for example a trader who lets premises held under a taxed lease to a tenant who sells only goods supplied by that trader. It is based on section 87(4) and (6) of ICTA.
261. *Subsection (2)* treats the tenant as if he or she occupied the property for the purposes of relief under section 61 of this Act.
262. *Subsection (3)* is based on section 87(6) of ICTA which says that a tenant shall not be treated as paying rent under section 87(4) of ICTA for any chargeable period for which rent has, or will be, treated as paid under section 37(4) of ICTA. It prevents a tenant obtaining relief under section 61 to the extent that relief for the same day has been

allowed in calculating the profits of a property business under section 292. Section 292 rewrites section 37(4) of ICTA.

***Section 64: Restrictions on section 61 expenses: lease premium receipts***

263. This section is based on section 87(5) of ICTA. It restricts the expenses a tenant is treated as incurring under section 61 where a tenant under a taxed lease:
- grants a sublease in respect of a property which section 63 treats the tenant as occupying for the purposes of the trade; and
  - receives in respect of the sublease, an amount which is brought into account as a receipt under Chapter 4 of Part 3 of this Act (a “lease premium receipt”).
264. Section 87(5) of ICTA applies where there is a reduction in a receipt of a Schedule A business by virtue of section 34 or 35 of ICTA. This section also applies where there is a reduction in a receipt of an overseas property business by virtue of section 34 or 35 of ICTA as applied by section 65A(5) of ICTA. See *Change 13* in Annex 1.
265. **Section 61** treats a tenant who occupies land under a taxed lease for the purposes of a trade as incurring an expense for each qualifying day in the receipt period of the taxed receipt relating to the taxed lease. The expense is calculated by reference to the amount of the taxed receipt.
266. If there is a reduction under section 288 in the amount which the tenant brings into account as a receipt under Chapter 4 of Part 3 of this Act in respect of the sublease, section 64 makes a corresponding reduction in the amount of the expense which section 61 treats the tenant as incurring for a qualifying day in the receipt period of the lease premium receipt.
267. It is not clear how the rule in section 37(5) of ICTA (as applied to section 87(4) of ICTA by section 87(5)) of ICTA is intended to apply where there is more than one “amount chargeable” by reference to which relief can be claimed for the same qualifying day.
268. *Subsections (3) and (4)* treat the tenant as incurring an expense for a qualifying day of the amount by which the “daily amount” of the taxed receipt exceeds:
- the “daily reduction” of the lease premium receipt; or
  - if the qualifying day falls within the receipt period of more than one lease premium receipt, the *total* of the daily reductions of those lease premium receipts.
269. This corresponds to the treatment in section 293 of this Act of an expense under section 292 for a qualifying day which falls within the receipt period of more than one lease premium receipt. See *Change 15* in Annex 1.
270. The “daily amount” of a taxed receipt and the “daily reduction” of a lease premium receipt are calculated according to the formulas in *subsection (6)*:
- the formula for calculating the daily amount of the taxed receipt is the same formula used in section 61(4) to calculate the amount of the expense which the tenant is treated as incurring for each qualifying day in the receipt period of the taxed receipt; and
  - the formula for the daily reduction of the lease premium receipt allocates equal amounts of the reduction by reference to the taxed receipt under section 288 to each day in the receipt period of the lease premium receipt.

***Section 65: Restrictions on section 61 expenses: lease of part of premises***

271. This section is based on section 87(5) of ICTA. It adapts section 61:
- where section 64 applies; and

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Act 2005 (c.5) which received Royal Assent on 24 March 2005*

- the sublease granted by the tenant does not extend to the whole of the premises subject to the taxed lease.
272. *Subsection (4)* deals with the case where the conditions for relief in sections 64 and 65 are met on the same qualifying day in respect of more than one lease. This corresponds to the treatment in section 294(4) of this Act of expenses under sections 292 and 293 where more than one taxed receipt falls to be reduced by reference to the same taxed receipt. See *Change 15* in Annex 1.
273. *Subsection (5)* adapts the formulas in sections 61(4) and 64(6) by multiplying the unreduced amount of the taxed receipt in those formulas (“A”) by the fraction of the premises to which the sublease relates.
274. Section 87(3) of ICTA requires a “just apportionment” to be made where part only of the land to which section 87(2) of ICTA applies is occupied for the purposes of a trade. This section instead requires the fraction in subsection (5) to be calculated “on a just and reasonable basis”. See *Change 14* in Annex 1.

***Section 66: Corporation tax receipts treated as taxed receipts***

275. This section and the following section ensure that a tenant is entitled to relief for an expense under section 61 by reference to an amount treated as a result of section 34 or 35 of ICTA as a receipt of a Schedule A business, or an overseas property business, of a landlord liable to corporation tax in the same way as if the landlord was liable to income tax on an equivalent amount as a receipt of his or her property business under sections 277 to 282 of this Act. This section is new.
276. **Section 296** of this Act adapts certain terms used to give a tenant who is carrying on a property business relief under sections 287 to 290 by reference to an amount taken into account for income tax purposes under sections 277 to 282 so as to give relief instead by reference to an amount treated as a receipt under section 34 or 35 of ICTA for the purpose of corporation tax:
- subsection (1) of section 296 introduces the label “corporation tax receipt” for an amount treated as a receipt of a Schedule A business under section 34 or 35 of ICTA on the interest of a landlord liable to corporation tax for an accounting period ending after 5 April 2005, or which would be treated as such a receipt other than for relief under section 37(2) of ICTA;
  - subsection (2) of section 296 provides that, for the purposes of Chapter 4 of Part 3 of this Act, a corporation tax receipt is treated as a taxed receipt and the lease in respect of which it arose is treated as a taxed lease. “Taxed lease” and “taxed receipt” are defined in section 287(4);
  - subsection (3) of section 296 adapts the term “receipt period” (as defined in section 288(6)) to apply to a corporation tax receipt; and
  - subsection (4) of section 296 adapts the term “unreduced amount” (as defined in section 290(2) and (5)) to apply to a corporation tax receipt.
277. In applying section 296 for the purposes of sections 60 to 67, this section performs the same function as section 296 in relation to a tenant who occupies or otherwise employs property subject to a taxed lease for the purposes of his or her trade.

***Section 67: Restrictions on section 61 expenses: corporation tax receipts***

278. This section is new. It ensures that any relief given for corporation tax purposes under section 37(2) or (3) of ICTA for an accounting period ending after 5 April 2005 by reference to:

- a receipt brought into account under Chapter 4 of Part 3 of this Act where the landlord is liable to income tax; or
  - a receipt brought into account under section 34 or 35 of ICTA where the landlord is liable to corporation tax,
- is taken into account in applying section 61 in the same way as any relief under section 288.
279. *Subsections (1), (2) and (3)* refer to a reduction under section 37(2) or (3) of ICTA by reference to “the amount chargeable on the superior interest”.
280. Section 37(1) of ICTA defines “the amount chargeable on the superior interest” as an amount treated as a receipt of a Schedule A business under section 34 or 35 of ICTA, or which would be so treated other than for relief under section 37(2) or (3) of ICTA. The “superior interest” is the interest in the property held by the immediate landlord.
281. [Paragraph 20](#) of Schedule 1 to this Act amends section 37(1) of ICTA by extending the definition of “the amount chargeable on the superior interest” to include any amount treated as a receipt of a property business under sections 277 to 282 of this Act, or which would be treated as such a receipt other than for relief under the additional calculation rule in section 288.
282. So in this section “the amount chargeable on the superior interest” is an amount:
- treated as a receipt under section 34 or 35 of ICTA for *any* tax year; or
  - treated as a receipt under Chapter 4 of Part 3 of this Act for an accounting period ending after 5 April 2005 as a result of the amendments to section 37(1) of ICTA made under paragraph 20 of Schedule 1 to this Act.

### ***Section 68: Replacement and alteration of trade tools***

283. This section allows a deduction for the cost of replacing or altering trade tools if the *only* reason a deduction would not be allowed is that the expenditure is of a capital nature. It is based on that part of section 74(1)(d) of ICTA that relates to deductions in respect of the replacement (“supply”) or alteration of implements, utensils and other articles employed for the purposes of the trade.
284. Expenditure on repairing trade premises or tools is revenue under the normal rules. And following the Special Commissioners decision in *Jenners Princes Street Edinburgh Ltd v CIR* (1998), SpC000166<sup>1</sup>, it is generally accepted that the reference in section 74(1)(d) of ICTA to expenditure “beyond the sum actually expended” does not prohibit the deduction of a provision for repairs if the cost of the repairs would be allowable. So that part of section 74(1)(d) of ICTA which deals with repairs is not rewritten.

### ***Section 69: Payments for restrictive undertakings***

285. This section allows a trader to deduct certain amounts paid to employees for restrictive undertakings. Such amounts might not otherwise be deductible to the extent that they are capital in nature or fall foul of the “wholly and exclusively” rule. The section is based on section 73(2) of FA 1988.
286. Section 73(2) of FA 1988 applies only to amounts brought into charge on the employee as earnings under section 225 of ITEPA. The former cross-refers to the latter where the definition of the amounts concerned is set out.
287. *Subsection (1)* provides for the deduction. In so doing it focuses on the key element for the rule to apply: the fact of payment.

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<sup>1</sup> STC [1998] (SCD) 196

288. *Subsection (2)* provides a timing rule. The deduction allowed by section 73 of FA 1998 is taken in the period of account in which the payment is made and no deduction is allowed in any other period. Similar words are used in section 77(6) and section 88(2) so the timing rules for deductions in Chapter 5 of Part 2 of this Act are explicit and consistent.

### ***Section 70: Employees seconded to charities and educational establishments***

289. This section allows a trader to deduct the cost of an employee seconded to a charity or educational establishment in calculating the trade profits. It is based on section 86(1), (2) and (3) of ICTA.
290. Section 86 of ICTA allows a trader who seconded an employee to a charity or educational establishment to deduct the cost of employing the seconded person *to the extent that* those costs would have been deductible if the employee continued to be employed for the purposes of the employer's trade. This section allows the employer to deduct *all* costs attributable to the seconded employee during the period of the secondment, regardless of whether those costs would have been allowed if the employee had not been seconded. See *Change 16* in Annex 1.
291. *Subsection (3)* defines "educational establishment" by reference to various bodies listed in section 71 and to any other educational body approved by "the Secretary of State or, in Northern Ireland, the Department of Education". For the purposes of section 86 of ICTA and of this section, "the Secretary of State" is the Secretary of State for the Department for Education and Skills.

### ***Section 71: Educational establishments***

292. This section defines "educational establishments" for the purposes of section 70. It is based on section 86(3),(4),(5) and (6) of ICTA.
293. Section 86(4)(c) of ICTA refers to an independent school registered under section 465 of the Education Act 1996. Section 465 of the Education Act 1996 was repealed by the Education Act 2002. So *subsection (1)(c)* refers instead to an independent school registered under section 161 of the 2002 Act.

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

294. This section allows an employer a deduction for expenses incurred in operating the payroll deduction scheme. It is based on section 86A of ICTA.
295. The main rules for payroll deduction schemes are found in Part 12 of ITEPA. Under such a scheme, an employer deducts charitable donations from employees' salaries and pays them to an agent, who distributes them to the employees' chosen charities.
296. The agent's administrative costs may be deducted from the donations. But many employers voluntarily pay the costs themselves so that the employees' full donations can go to the chosen charities.
297. Normally, payments made voluntarily to meet someone else's expenses are not made wholly and exclusively for the purposes of a trade and therefore would not be deductible. Employers might get relief for donations to charitable agencies under the Gift Aid scheme. But there are restrictions on the operation of that section and relief would not be available if the agent was not itself a charity.
298. This section gives relief for the expenses as a trading deduction.
299. *Subsection (3)* defines "approved scheme" and "approved agent" by reference to the definitions in section 714 of ITEPA.
300. Section 714(2) of ITEPA defines "approved scheme" as:

“a scheme which is approved (or is of a kind approved) by the Inland Revenue and under which—

- (a) the payer is required to pay sums withheld to a body which is an approved agent at the time of the withholding, and
- (b) the approved agent is required—
  - (i) to pay sums withheld to the specified charity or charities, or
  - (ii) in a case where the agent is itself a specified charity, to retain any sum due to itself ...

301. Section 714(3) of ITEPA defines “approved agent”:

“For the purposes of this section a body is an “approved agent” if it is approved by the Inland Revenue for the purpose of paying donations to one or more charities.

### ***Section 73: Counselling and other outplacement services***

302. This section provides a deduction for certain expenses of counselling provided for employees. It is based on sections 589A and 589B of ICTA, section 108 of FA 1993 and Schedule 6 to ITEPA.

303. *Subsection (3)* cross-refers to ITEPA for the conditions that need to be met for the deduction to be allowed (section 310 of ITEPA exempts the employee from tax in respect of counselling received).

### ***Section 74: Retraining courses***

304. This section gives a deduction for certain expenses of retraining provided for employees. It is based on section 588 of ICTA and Schedule 6 to ITEPA.

305. *Subsection (2)* cross-refers to ITEPA for the conditions that need to be met for the deduction to be allowed (section 311 of ITEPA exempts the employee from tax in respect of qualifying retraining courses).

306. The section does not rewrite section 588(3)(b) of ICTA. That provision makes a deduction in calculating the employer’s trade profits conditional on the employee’s exemption under section 311 of ITEPA in respect of the expenditure in question. This condition is not consistent with the similar provision rewritten in section 73 and does not serve any material purpose. See *Change 17* in Annex 1.

### ***Section 75: Retraining courses: recovery of tax***

307. This section allows the recovery of tax when a deduction under section 74 subsequently proves to have been wrongly allowed. It is based on section 588 of ICTA and Schedule 6 to ITEPA.

308. *Subsection (2)*, like section 74(2) cross-refers to the relevant provisions in ITEPA to refer to the conditions that have not been met.

309. *Subsections (4) and (5)* refer to the Inland Revenue rather than, as in the source legislation, to the inspector. See *Change 149* in Annex 1.

### ***Sections 76 to 80: Redundancy payments etc***

#### **Overview**

310. These five sections are based on the trading income rules relating to redundancy payments in sections 90, 579 and 580 of ICTA. The rules that deal with the employee’s liability are in section 309 of ITEPA.



311. The trading income rules were introduced to reverse the decisions in *CIR v Anglo Brewing Co Ltd* (1925), 12 TC 803 and *Godden v A Wilson's Stores (Holdings) Ltd* (1962), 40 TC 161. In those cases the courts held that certain payments to employees on the closing down of a trade were not deductible in arriving at trading profits. In neither case was the payment made in accordance with a pre-existing obligation.
312. In 1999 the Inland Revenue announced (Tax Bulletin 39G, February 1999) that it will be guided by the decision in *Commissioner of Inland Revenue v Cosmotron Manufacturing Co Ltd* (1997), 70 TC 292<sup>2</sup>.
313. In that Hong Kong case the Privy Council decided that redundancy payments made under a pre-existing obligation were deductible. Although that decision is merely persuasive in the United Kingdom, the Inland Revenue no longer argue that payments made under a pre-existing obligation (including a statutory obligation) are covered by the *Anglo Brewing* and *Wilson's Stores* decisions. The announcement in Tax Bulletin means that it may not be necessary to give the employer a statutory right to a deduction in calculating trading profits. But these sections put the matter beyond doubt.

### ***Section 76: Redundancy payments and approved contractual payments***

314. This section sets out the circumstances in which the following three sections apply and explains the terms used in the main provisions. It is based on section 579(2) of ICTA.
315. The sections retain the label "redundancy payment" and the expression "additional payment" from the source legislation. This section also introduces the label "approved contractual payment" to describe the payments that may replace redundancy payments in some cases.

### ***Section 77: Payments in respect of employment wholly in employer's trade***

316. This section sets out the main rule governing redundancy payments made by an employer. It is based on section 579(2) of ICTA.
317. If a payment is otherwise allowable (possibly as a result of the *Cosmotron* decision – see the overview for this group of sections), this section does not interfere with the accountancy treatment of the payment. In that case, the normal accruals basis applies.
318. *Subsection (5)* is based on section 113(2) of ICTA. The timing rule in section 579(2) (b) of ICTA refers to the "discontinuance" of a trade. That word has to be interpreted in the light of section 113 of ICTA: the trade is not treated as discontinued unless there is a complete change in the persons carrying it on.
319. The deduction allowed by section 579 of ICTA is for "a redundancy payment ... made". It is clear that a deduction is allowed only if a payment has been made. It follows that the deduction is to be taken in the period of account in which the payment is made and that no deduction is allowed in any other period.
320. *Subsection (6)* has a timing rule expressed in similar words to those used in sections 69 and 88 of this Act. So the timing rules for deductions in Chapter 5 of Part 2 are explicit and consistent. This special timing rule applies if the payment is allowable only as a result of this section.

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

321. This section deals with the case where the employee is employed in more than one capacity. It is based on section 579(5) of ICTA. The section covers the case where there is a private element in the employment and makes clear what part of the payment is allowed as a deduction in calculating trade profits.

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322. Section 579(5) of ICTA does not specify the basis on which to apportion the payment. This section adopts the “just and reasonable” apportionment that is used consistently in this Act. See *Change 14* in Annex 1.

**Section 79: Additional payments**

323. This section deals with any voluntary payments that an employer makes in addition to the statutory (or approved) payments dealt with in section 77 of this Act. It is based on section 90 of ICTA.
324. Unlike the payments in section 77, these additional payments are allowable only if the sole reason for their disallowance is the cessation of the trade.
325. The section applies to payments in connection with the cessation of *part* of a trade in the same way as it applies to payments in connection with the cessation of a whole trade. See *Change 18* in Annex 1.
326. *Subsection (2)* is based on section 113(2) of ICTA. Section 90(3) of ICTA refers to the “discontinuance” of a trade. That word has to be interpreted in the light of section 113 of ICTA: the trade is not treated as discontinued unless there is a complete change in the persons carrying it on.
327. A redundancy payment is not disallowable solely on account of a partial change of persons carrying on a trade. But this subsection puts it beyond doubt that a partial change of persons carrying on a trade does not count as a cessation.

**Section 80: Payments made by the Government**

328. This section sets out what happens if it is not the employer who makes the redundancy payment to the employee. It is based on section 579(6) of ICTA.
329. In some cases the Government makes the payment and is reimbursed by the employer. This section ensures that the employer is allowed a trading deduction.
330. *Subsection (1)(b)* reflects the effect of the devolution settlements. See *Change 19* in Annex 1.

**Section 81: Personal security expenses**

331. This section allows the deduction of certain expenditure, by individuals trading alone or in partnership, on their personal security. It is based on sections 112 and 113 of FA 1989.
332. Expenditure within this section normally falls foul of the “wholly and exclusively” rule in section 34 (based on section 74(1)(a) of ICTA). That is because it is incurred for an essentially non-business purpose.
333. The source legislation expressly overrides, where appropriate, both sections 74(1)(a) and (1)(b) of ICTA. Section 74(1)(b) of ICTA is not rewritten because it is not necessary (see the commentary on that provision in the explanatory notes on paragraph 45 of Schedule 1 to this Act). So the condition in *subsection (1)(e)* refers only to the rule in section 34.
334. The source legislation allows a deduction only for expenditure of a revenue nature. Section 81 can accordingly apply only to expenses of a revenue nature because section 33 is not overridden. There are parallel rules in section 33 of CAA which deal with similar expenditure of a capital nature.
335. **Section 81** gives a narrowly targeted deduction which applies in particular and unusual circumstances. So it contains an extensive set of conditions which must be met for the deduction to succeed.

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336. *Subsection (1)(b)* states the main condition: if there is no special threat there is no need to improve security and the rule cannot apply.
337. *Subsection (1)(e)* makes it clear that it is only the wholly and exclusively prohibitive rule that is overridden.

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

338. This is the first of five sections that allow deductions for contributions to local enterprise agencies, training and enterprise councils (TECs), local enterprise companies in Scotland, business links and urban regeneration companies. The sections are based on sections 79, 79A and 79B of ICTA.
339. Contributions to these bodies are generally donations and are likely to be made for benevolent reasons, rather than wholly and exclusively for the purposes of the trade (see section 34 of this Act).
340. *Subsection (3)* is an anti-avoidance rule. It prevents a trader using the section to obtain a deduction for private expenditure, such as funding the training of a family member, by passing funds through one of these bodies. The source legislation disallows any deduction if there is a benefit to the trader. This section merely restricts the deduction by the value of the benefit. See *Change 20* in Annex 1.
341. *Subsection (5)* sets out what happens if the trader receives a benefit in connection with the contribution. The rules in ICTA charge the benefit to tax for a “chargeable period”, which, for income tax purposes, means a tax year. It is simpler to charge the benefit for a period of account. This is consistent with the similar charge on benefits in connection with gifts of trading stock (see section 108 of this Act). See *Change 21* in Annex 1.
342. The charge on the benefit applies if the benefit is received by a person “connected with” the trader. That expression is explained in section 878(5) of this Act.
343. *Subsection (6)(b)* deals with the case where the recipient’s trade has ceased before the benefit is received. It treats the benefit explicitly as a post-cessation receipt. See *Change 22* in Annex 1.
344. *Subsection (7)* makes clear the extent of the disallowance under subsection (3) or charge under subsection (6).
345. The subsection limits the “disqualifying benefit” in accordance with the Inland Revenue practice. See *Change 20* in Annex 1.

**Section 83: Meaning of “local enterprise organisation”**

346. This section lists some of the organisations that qualify for deductions to be allowed under section 82. It combines the definitions in sections 79(4) and 79A(5) of ICTA.
347. *Subsection (2)* deals with local enterprise agencies. These agencies may take a number of forms and do not have an approval procedure for any other purpose. So the tax legislation specifies that they must be approved for this purpose.
348. The subsection introduces the expression “relevant national authority”. The expression is used also in sections 84 and 85 of this Act.
349. The subsection reflects the effect of the devolution settlements. See *Change 19* in Annex 1. The National Assembly for Wales (Transfer of Functions) Order 1999 (SI 1999/672) devolves the functions of the Secretary of State under section 79 of ICTA to the National Assembly for Wales. So the “relevant national authority” may be the Assembly. But the Order does not refer to section 79A of ICTA. So the equivalent functions in subsections (3) and (5) of this section are still exercised only by the Secretary of State.

*These notes refer to the Income Tax (Trading and Other Income) Act 2005 (c.5) which received Royal Assent on 24 March 2005*

350. *Subsections (3) to (5)* deal with other bodies to which section 82 of this Act applies. These other bodies have to be set up in a particular way for other reasons and the tax legislation merely follows the existing procedures.

***Section 84: Approval of local enterprise agencies***

351. This section and section 85 set out the detailed rules that apply for the approval of local enterprise agencies and the withdrawal of such approval. They are based on section 79(4) to (7) of ICTA.
352. The section sets out the basic procedure for approving a local enterprise agency. The references to “relevant national authority” are explained in section 83(2) of this Act.

***Section 85: Supplementary provisions with respect to approvals***

353. This section and section 84 set out the detailed rules that apply for the approval of local enterprise agencies and the withdrawal of such approval. They are based on section 79(4) to (7) of ICTA.
354. The references to “relevant national authority” in this section are explained in section 83(2) of this Act.

***Section 86: Meaning of “urban regeneration company”***

355. This section sets out the detailed rules that apply for the designation of urban regeneration companies. It is based on section 79B(5) to (8) of ICTA.

***Section 87: Expenses of research and development***

356. This section gives relief for the cost of research and development undertaken by or on behalf of a trader. It is based on section 82A of ICTA.

***Section 88: Payments to research associations, universities etc***

357. This section gives relief for payments by a trader to various bodies engaged in scientific research. It is based on section 82B of ICTA.
358. Section 82B(1) of ICTA allows a deduction for “the sum paid”. So *subsection (2)* allows a deduction for the period in which the payment is made.
359. Section 82B of ICTA provides that “the Board” shall refer any question as to whether, or to what extent, activities constitute scientific research for the purposes of section 82B to the Secretary of State. Section 832(1) of ICTA defines “the Board” as the Commissioners of Inland Revenue.
360. *Subsection (6)* instead says that any question as to what constitutes scientific research must be referred to the Secretary of State by “the Inland Revenue”. “The Inland Revenue” is defined in section 878(1) of this Act as “any officer of the Board of Inland Revenue”. See *Change 149* in Annex 1.
361. For the purposes of section 82B of ICTA and of this section, “the Secretary of State” is the Secretary of State for the Department of Trade and Industry.

***Section 89: Expenses connected with patents***

362. This section allows a deduction for expenses connected with patents. It is based on section 83 of ICTA.
363. *Subsection (1)* sets out the expenses that are allowable. The deduction is on the basis of expenses incurred. This relaxes any requirement in the source legislation that fees have to be paid before a deduction can be made. See *Change 23* in Annex 1.

364. *Subsection (2)* establishes that the rule in this section is an exception to the general rule in section 56.

***Section 90: Expenses connected with designs or trade marks***

365. This section allows a deduction for expenses connected with designs or trade marks. It is based on section 83 of ICTA.
366. *Subsection (1)* sets out the expenses that are allowable. The deduction is on the basis of expenses incurred. This relaxes any requirement in the source legislation that fees have to be paid before a deduction can be made. See *Change 23* in Annex 1.
367. *Subsection (2)* establishes that the rule in this section is an exception to the general rule in section 56 of this Act.

***Section 91: Payments to Export Credits Guarantee Department***

368. This section allows a trader to deduct the cost of certain payments to the Export Credits Guarantee Department (“ECGD”). It is based on section 88 of ICTA.
369. Section 88 of ICTA refers to payments made under arrangements made by the Secretary of State in pursuance of section 11 of the Export Guarantees and Overseas Investment Act 1978. This section refers instead to arrangements made under section 2 of the Export and Investment Guarantees Act 1991 which replaced the 1978 Act.
370. Section 13(1) of the Export and Investment Guarantees Act 1991 delegates the functions of the Secretary of State under section 2 of the 1991 Act to the ECGD. So the reference to the Secretary of State in section 88 of ICTA is not rewritten in this section.
371. Section 88 of ICTA allows a trader to deduct “sums paid” to the ECGD. This section instead allows a deduction for any “sum payable” by the trader. See *Change 24* in Annex 1.

***Section 92: Expenses connected with foreign trades***

372. This is the first of three sections that set out the special rules for expenses of a foreign trade. The sections are based on sections 80 and 81 of ICTA.
373. The expenses to be allowed are those of a business trip: the condition in sections 80(3) and 81(4) of ICTA is that the trader’s absence from the United Kingdom should be wholly and exclusively for the purpose of a foreign trade (or for the purpose of a foreign trade and another trade).
374. The section sets out a single condition related to the purpose of the trader’s absence from the United Kingdom. That condition applies for all the expenses set out in subsection (3).
375. In the case of family expenses, section 80(5) of ICTA requires the absence to be for the purpose of one or more *foreign* trades. The section relaxes this requirement. It allows the absence to be either for the purposes of the foreign trade or for the purposes of that trade and one or more other trades. The “other trades” may include one that is not carried on wholly outside the United Kingdom. So the treatment of family expenses is brought into line with the treatment of other expenses. See *Change 25* in Annex 1.
376. In the case of travelling expenses, section 81(3) of ICTA seems to impose a further condition requiring the performance of “functions” at the place of departure. This section does not include that further condition. See *Change 25* in Annex 1.
377. *Subsection (1)(d)* makes it clear that the section applies if it is only the “wholly and exclusively” rule that would otherwise disallow the expenses. The normal trading rule (based on the courts’ explanation of the rule in section 34 of this Act) is that the cost of

home to work travel is not allowable for tax purposes. Other trading rules (such as the prohibition for capital expenditure in section 33) continue to apply.

378. *Subsection (2)* includes the rule that the special relief is not available if the income from the trade is assessable by reference to amounts received in the United Kingdom (the “remittance basis”). Section 80 of ICTA refers to section 65(4) of ICTA. This section refers directly to the remittance basis, which is explained in section 878(2) of this Act.
379. The section applies the special rules to the calculation of the profits of Irish trades (always assessed on the arising basis) even if the taxpayer’s other foreign income is assessed on the remittance basis. See *Change 26* in Annex 1.
380. *Subsection (3)* sets out the expenses that qualify for relief under this section.
381. *Subsection (4)* defines the term “foreign trade”. It replaces the reference in section 80 of ICTA to a trade carried on wholly abroad and the reference in section 81 of ICTA to a trade “in the case of which section 80 applies”.

### ***Section 93: Allocation of expenses***

382. This section sets out the rules for allocating the expenses of the trades if the trader carries on more than one foreign trade. It is based on sections 80 and 81 of ICTA.
383. Those sections provide that the apportionment should be “reasonable”. Other apportionments in this Act are made on a “just and reasonable” basis. This section uses “just and reasonable”. See *Change 14* in Annex 1.

### ***Section 94: Family expenses***

384. This section sets out the family expenses that qualify for an allowance. It is based on section 80(6) and (9) of ICTA. The 60 day condition in section 80(5) of ICTA is in section 92(3)(c) of this Act.
385. Section 1 of the Family Law Reform Act 1987 (broadly) treats illegitimate children in the same way as legitimate children. Section 831(4) of ICTA disapplies that section. So section 80(9) of ICTA needs specially to bring illegitimate children within the scope of the relief in that section. Section 831(4) of ICTA does not apply to this Act. So the Family Law Reform Act ensures that illegitimate children are within this section.