

INCOME TAX (TRADING AND OTHER INCOME) ACT 2005

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 3: Property income

Chapter 3: Profits of property businesses: basic rules

Section 268: Charge to tax on profits of a property business

1068. This section charges the profits of a property business to tax. It is based on sections 15 and 18 of ICTA.

Section 269: Territorial scope of charge to tax

1069. This section sets out the limitations on the charge to tax on a UK property business and an overseas property business. It is based on sections 18 and 65A of ICTA.

1070. *Subsection (1)* establishes that the profits of a UK property business are charged to tax whatever the residence status of the taxpayer.

1071. *Subsection (2)* establishes that the profits of an overseas property business are charged to tax only if the taxpayer is a UK resident.

1072. Income from an overseas property business is assessable under Schedule D Case V. So the charge to tax is subject to the territorial restriction in Schedule D. A non-resident person is taxable only on income from “property” in the United Kingdom (see paragraph (a)(iii) of Schedule D in section 18(1) of ICTA). So a non-resident is not charged to tax on the income from overseas property.

1073. *Subsection (3)* is the special rule for Irish income. It is based on section 68 of ICTA. Even if a person is entitled to the remittance basis for other foreign income Irish income is assessable on the basis of the income arising. But it is not clear how the rules in sections 65(4) and 68 of ICTA interact. This section makes it clear that the rules for an overseas property business are used in calculating the income from Irish property. See *Change 67* in Annex 1.

1074. *Subsection (4)* is a signpost to the special rule in Chapter 11 of Part 2 of this Act for the non-Irish foreign income of a person who is assessable on the remittance basis. The overseas property business rules in section 65A of ICTA are disapplied in the case of a remittance basis person by section 65(4) of ICTA.

Section 270: Income charged

1075. This section states the amount charged to tax. It is based on sections 21 and 65 of ICTA.

1076. The section refers simply to “profits” rather than “annual profits” used in the source legislation. Omitting “annual” is consistent with the approach adopted for trading and savings and investment income - the word adds nothing to the meaning of “profits”.

Section 271: Person liable

1077. This section states who is liable for any tax charged. It is based on sections 21 and 59 of ICTA.

Section 272: Profits of a property business: application of trading income rules

1078. This is the main rule for calculating the profits of a property business. It is based on sections 21A and 65A of ICTA.
1079. The same basic rules apply to the calculation of both UK and overseas property businesses.
1080. From 1995, the profits of a Schedule A business charged to income tax are calculated by treating the business as similar to a trade and applying the calculation rules of Schedule D Case I.
1081. In the source legislation this is achieved by section 21A of ICTA. But, at the margins, the application of certain of the Case I rules to Schedule A is not altogether clear.
1082. First, the relationship of section 21A(2) of ICTA to section 21A(1) of ICTA is uncertain. Section 21A(2) of ICTA refers to provisions that apply “in accordance” with section 21A(1). It is open to debate whether section 21A(2) of ICTA merely contains examples of the Schedule D Case I provisions that apply in accordance with the general rule in section 21A(1) of ICTA or whether it contains an exhaustive list of those provisions. The former appears the better view and the one best reflecting the underlying policy.
1083. Second, some Schedule D Case I provisions that are applied to Schedule A are inherently incapable of applying to income from land. The “herd basis” provisions in section 97 of and Schedule 5 to ICTA (rewritten in Chapter 8 of Part 2 of this Act) are an example. They are among the provisions of Chapter V of Part 4 of ICTA that are applied to Schedule A specifically (subject to stated exceptions) by section 21A(2) of ICTA. But they are not among the exceptions referred to in section 21A(4) of ICTA.
1084. On the other hand, some Schedule D Case I provisions outside Chapter V of Part 4 of ICTA that seem potentially more relevant, such as the car hire provisions in sections 578A and 578B of ICTA, are not applied specifically.
1085. ***Section 272*** clarifies these matters by listing all the sections in Part 2 of this Act that are relevant to property business profits.
1086. Some of the sections in Part 2 of this Act that are applied to a property business contain rewrite changes. Those changes are carried through to property income. Details of those changes are recorded in the Annex 1 notes on the particular sections in Part 2 of this Act.
1087. *Subsection (1)* states the general principle that the profits of a property business are calculated in the same way as the profits of a trade. This reflects the fact that there are provisions not included in Part 2 of this Act which may affect the calculation of profits. For example, the pension contributions deductions provisions in FA 2004 and certain anti-avoidance provisions in ICTA that apply to all income types.
1088. *Subsection (2)* lists all the sections in Part 2 of this Act that are relevant to property business income. It reflects the principle that section 21A(1) of ICTA applies all Schedule D Case I calculation provisions to Schedule A unless they are expressly disapplied elsewhere. Provisions that are expressly disapplied in the source legislation are excluded from the list.

1089. Also excluded are provisions which are attracted to Schedule A in the source legislation either expressly by section 21A(2) of ICTA or under the general principle expressed in section 21A(1) of ICTA, but which are incapable of applying once carried over to the context of the property business. Exclusion is achieved simply by omitting them from the list of provisions that do apply.
1090. The majority of the provisions in Part 2 of this Act that can apply to a property business are applied by subsection (2). But in some cases later sections set out the provisions specifically (Chapter 7 (adjustment income) and Chapter 10 (post-cessation receipts)).
1091. The following sections that are applied by subsection (2) merit specific mention. These are:
- sections 48 to 50: expenses of car hire;
 - sections 188 to 191: deduction for unremittable amounts.
1092. Including these accurately reflects the effect of section 21A(1) of ICTA.
1093. Although the list in subsection (2) excludes sections in Part 2 of this Act that are inherently incapable of applying to a property business it does not exclude those that are merely unlikely to apply. This recognises the possibility of certain provisions applying in unusual circumstances. Examples are section 87 and section 88 (scientific research). Although their relevance to a property business is unlikely, it is not inconceivable and they are needed to cater for the possibility of a landlord funding an activity that would qualify as “scientific research”. An example might be research on the decontamination of brown land with a view to building an investment property on it.
1094. *Subsection (3)* ensures that the trading income provisions cross-referred to in subsection (2) work properly in the context of the property business.

Section 273: Amounts not brought into account as part of a property business

1095. This section excludes from the profits of a property business certain income from land that, exceptionally, may be taxed as profits of a trade. It is based on sections 15 and 65A of ICTA.
1096. *Subsection (1)* signposts to the relevant provisions.
- See *Change 3* in Annex 1 in respect of caravans.
 - See *Change 4* in Annex 1 in respect of surplus business accommodation.
 - See *Change 5* in Annex 1 in respect of payments for wayleaves.

Section 274: Relationship between rules restricting and permitting deductions

1097. This section determines the interaction between those provisions that allow a deduction and those provisions that prohibit a deduction. It is new. See *Change 6* in Annex 1.
1098. This section does a similar job in the property income Part to that which section 31 does in the trading income Part. The general principle is that a rule allowing a deduction takes priority over a rule prohibiting a deduction. But that is subject to the exceptions the section mentions.
1099. *Subsection (4)* makes it clear that the effect of this priority rule extends to the large number of trading income rules that apply to property income indirectly through section 272.

Section 275: Apportionment of profits to tax year

1100. This section deals with cases where the period of account does not coincide with a tax year. It is based on sections 21A, 72 and 65A of ICTA.

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

1101. This section is necessary because the charge under section 270 is on the property business profits arising in the *tax year*.
1102. In the source legislation section 72 of ICTA is one of the provisions applied to Schedule A specifically by section 21A(2) of ICTA. Section 72 of ICTA is rewritten for trade profits in section 203. But simple cross-reference to that trading income section would not work very well for property income because that section is drafted in terms of basis periods and basis periods are not relevant to property income. So section 275 is a specific property income version.
1103. *Subsection (4)* adopts the approach of section 203(4) in permitting an alternative basis of apportionment if its use is reasonable and consistent. See *Change 52* in Annex 1. The wording of subsection (4) makes it clear that the option to choose an alternative basis of apportionment is exercisable only by the taxpayer, not the Inland Revenue.