These notes refer to the Corporation Tax Act 2009 (c.4) which received Royal Assent on 26 March 2009

CORPORATION TAX ACT 2009

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 3: Trading income

Overview

Chapter 4: Trade profits: rules restricting deductions

Overview

216. This Chapter contains provisions prohibiting various deductions in calculating the profits of a trade or restricting the extent to which such deductions can be made.

Section 53: Capital expenditure

217. This section prohibits deductions for capital expenditure and is based on section 74(1)(f) of ICTA. The corresponding rule for income tax is in section 33 of ITTOIA.

218. It is a long-established and generally accepted principle that capital items are ignored in calculating the profits of a trade and the question whether a sum is income or capital is ultimately a question of law, not accountancy. For judicial authority for this proposition, see, for example the words of Brightman J on page 173 of ECC Quarries Ltd v Watkis (1975), 51 TC 153 ChD[1]:

> …unchallenged evidence, or a finding, that a sum falls to be treated as capital or income on principles of correct accountancy practice is not decisive of the question whether in law the expenditure is of a capital or an income nature.

219. A sum which is of a capital nature may however be allowed as a deduction in calculating the profits of a trade because of a statutory exception to the general rule on the deduction of such items in this section. See, for example, section 89 (expenses connected with patents).

220. In the absence of general agreement on what constitutes capital expenditure "items of a capital nature" is not defined.

221. Section 74(1)(g) of ICTA is redundant as the deduction of capital employed in the improvement of premises is covered by the general prohibition on the deduction of "items of a capital nature". So this Act repeals section 74(1)(g) of ICTA without rewriting it.

Section 54: Expenses not wholly and exclusively for trade and unconnected losses

222. This section contains rules for the deduction of expenses and losses in calculating the profits of a trade. It is based on section 74(1)(a) (expenses) and (e) (losses) of ICTA. The corresponding rules for income tax are in section 34 of ITTOIA.

---

1 STC [1975] 578

223. Section 74(1)(a) of ICTA provides that in calculating the profits of a trade no deduction is allowed for expenditure which is not incurred "wholly and exclusively" for the purposes of that trade. This could be construed to mean that if expenditure is incurred partly for trade purposes and partly for some other purposes, no part of that expenditure can be deducted in arriving at the trade profits.

224. But section 74(1)(c) of ICTA, which prohibits any deduction in respect of the rent of premises used for residential or "domestic" purposes, provides for the *apportionment* of rent paid for premises used partly as residential accommodation and partly for the purposes of a trade. And in practice a deduction is allowed for any expenditure which can be apportioned between trade and non-trade expenditure – for example, expenditure on a car used partly for trade and partly for private purposes.

225. There is judicial support for allowing a deduction where expenditure incurred for more than one purpose can reasonably be apportioned between expenditure incurred for the purpose of the trade and non-trade expenditure. See, for example, Lochgelly Iron and Coal Company Ltd v Crawford (1913), 6 TC 267 CS, in which a deduction was allowed for part of a subscription to a trade association and Copeman v William Flood & Sons Ltd (1941), 24 TC 53 KB, in which the High Court remitted the case to the Commissioners to find as a fact whether the remuneration paid to certain directors who were also shareholders in the family company was wholly and exclusively expended for the purpose of the Company's trade, and if not, how much of the remuneration was so expended.

226. Conversely, the courts have held that if it is not possible to identify any part of the expenditure that is incurred wholly and exclusively for the purposes of the trade, no apportionment is possible. See, for example, Mallalieu v Drummond (1983), 57 TC 330 HL[2] in which no deduction was allowable for clothing worn for warmth and decency as well as being required by the taxpayer's profession.

227. So *subsection (2)* of this section provides for the deduction of any part or proportion of expenses incurred partly for the purposes of the trade and partly for some other purpose that can be identified as incurred wholly and exclusively for the purposes of the trade. Rent on dual purpose accommodation can be apportioned under subsection (2) of this section. So this Act repeals section 74(1)(c) of ICTA without rewriting it.

Section 55: Bad debts

228. This section is based on the rule restricting relief for some debts in section 88D of ICTA. It also rewrites the relief in section 89 of ICTA for debts proved irrecoverable after a trade is treated as having ceased. See *Change 8* in Annex 1. The corresponding rule for income tax is in section 35 of ITTOIA.

229. *Subsection (2)(a)* refers to a deduction "by way of impairment loss". That expression is not defined for the purpose of this section. But section 476(1) defines "impairment loss" for the purposes of the loan relationships legislation as "a debit in respect of the impairment of a financial asset". "Impairment" includes "uncollectability".

230. *Subsection (2)(b)* deals with debts released as part of a "statutory insolvency arrangement", which is defined in section 834(1) of ICTA.

231. *Subsection (3)* provides a definition that clarifies the scope of the section. All money debts (see section 303) arising in a trade that produce an impairment loss are within the loan relationships rules (see section 479). Even if a money trade debt is released as part of a statutory insolvency arrangement any loss on the debt is within the extended meaning of "impairment" in section 476(1).

232. There is a corresponding rule for income from holding an office in section 970.

---

2 STC [1983] 665

Section 56: Car or motor cycle hire

233. This section restricts the amount that a company can deduct in respect of the cost of hiring certain cars or motor cycles with a retail price (when new) of more than £12,000. The restriction increases in line with the retail price. The section is based on sections 578A and 578B of ICTA. The corresponding rule for income tax is in section 48 of ITTOIA.

234. Section 578B(1) of ICTA says that for the purposes of section 578A of ICTA "car" includes a motor cycle. So this section and section 57 refer to a "car or motor cycle" throughout.

235. Section 578A(4) of ICTA provides for amounts in respect of hire charges brought into account as a receipt of the trade under section 94 of ICTA (see section 94 of this Act) to be reduced in the same proportion as the deduction in respect of those charges is reduced under section 578A(3) of ICTA. *Subsection (4)* of this section extends the same treatment to amounts in respect of hire charges taxed as a post-cessation receipt under section 193 (debts released after cessation). See *Change 9* in Annex 1.

Section 57: Car or motor cycle hire: supplementary

236. This section defines various terms and is based on section 578B of ICTA. The corresponding rule for income tax is in section 49 of ITTOIA.

237. Section 578B(2) of ICTA defines "qualifying hire car" for the purposes of section 578A of ICTA as a car hired under a hire-purchase agreement subject to an option to purchase which is exercisable for a nominal amount.

238. Not all hire-purchase agreements require the hirer to exercise an option at the end of the hire period. Under some types of agreement, ownership of the vehicle passes automatically to the hirer at the end of the hire period. So *subsection (2)(a)* of this section extends the definition of "qualifying hire car or motor cycle" to include a car or motor cycle where ownership passes without the exercise of an option to purchase. See *Change 10* in Annex 1.

Section 58: Hiring cars (but not motor cycles) with low CO2 emissions before 1 April 2013

239. This section excludes certain cars hired before 1 April 2013 under a contract entered into before that date from the restriction in section 56. It is based on section 578A(2A) and (2B) of ICTA and section 60 of FA 2002. The corresponding rule for income tax is in section 50 of ITTOIA.

240. *Subsection (2)* defines low emissions by reference to section 45D of CAA. A transitional rule in Schedule 1 to this Act provides that, for a car hired on or before 31 March 2008, the carbon emissions limit in section 45D(4) of CAA remains 120 grams instead of the new limit of 110 grams.

Section 59: Patent royalties

241. This section prohibits a deduction for patent royalties. It is based on section 74(1)(p) of ICTA.

242. For most patent royalties this rule is overridden by the rules of the intangible fixed assets regime (rewritten in Part 8 of this Act) which provide relief for trades as well as other commercial activities (see, in particular, section 728(5) and Chapter 6 of Part 8 of this Act). But for a minority of cases, this section will remain relevant and will continue to prevent a deduction. That includes, for example, cases where the royalty is in respect of an intangible asset that is not a fixed asset of the payer's trade.

Section 60: Expenditure on integral features

243. This section draws attention to the rule in section 33A(3) of CAA. There is a signpost to that rule in section 74(1)(da) of ICTA. That subsection is repealed. The signpost is not formally rewritten but it is replaced in this section (and in the property income section 263).