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

INCOME TAX (TRADING AND OTHER INCOME) ACT 2005

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 9: Partnerships

Section 861: Sale of patent rights: effect of partnership changes

3234. This section sets out what happens when there is a sale of patent rights by a trader and there is change in the membership of any firm that carries on the trade. It is based on section 558 of CAA.

3235. The rules for intellectual property are split:

- the rules that give capital allowances are in CAA;
- the rules that charge non-trading profits from the sale of patent rights are in Chapter 2 of Part 5 of this Act; and
- the special rules that apply to firms are set out in this section and section 862.

3236. If a trader receives a sum from the sale of patent rights in the ordinary course of the trade the sum is a trade receipt. In that case, it is not a "capital sum" and section 524(1) of ICTA ensures that the special rules do not apply. In this Act the treatment is the same because section 575(1) ensures that a charge under Part 2 of this Act takes precedence over a charge under Part 5 of this Act (which includes income from intellectual property in Chapter 2 of that Part).

3237. If a trader receives a capital sum from the sale of patent rights, the sum is excluded from the calculation of the trade profits by the general rule that excludes capital receipts. Instead, the sum is separately charged to income tax under section 587 of this Act. The profit on the sale is charged to tax over six years. But the seller may elect to have the sum charged in the year in which the proceeds of sale are received. Or the charge may be spread in accordance with section 591 or 592.

3238. *Subsection (2)* sets out the "tax condition" for the section to apply. The condition is that the charge on the proceeds from the sale of patent rights is spread over several tax years.

3239. *Subsection (3)* sets out the "partnership condition" for the section to apply. The condition is that the trade that gives rise to the sale of patent rights is carried on in partnership, either at the time of the sale or at any time during the tax spreading period. In this case the charge under section 524 of ICTA "falls to be made on two or more persons jointly" (section 525(3) of ICTA).

3240. *Subsection (4)* sets out the "non-cessation condition" for the section to apply. The condition is that the there is not a complete change in the persons carrying on the trade. If there is such a change, section 862 applies instead.

3241. *Subsection (5)* sets out the what happens if all the conditions in the previous three subsections are met: the charge on the proceeds of sale of the patent rights is made on the current partners in the firm. This subsection is based on section 558(3) of CAA.

3242. *Subsection (6)* makes clear the assumptions on which the charge on the current partners is to be calculated. All the current partners step into the shoes of the persons who were partners at the time of the original sale.