

INCOME TAX ACT 2007

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 13: Tax avoidance

Overview

Chapter 5: Avoidance involving trading losses

Overview

2317. The Chapter provides for the recovery of certain loss reliefs if regulations apply to reduce an individual's contribution to the firm so that the contribution becomes lower, or even lower, than relief already given to the individual.
2318. This Chapter also sets out provisions about avoidance involving trade losses made by individuals in a trade exploiting a film or licence. The provisions tackle schemes used by individuals to try to convert a tax deferral into a permanent tax gain.
2319. The Chapter is based on Chapter 9 of Part 3 of FA 2004 and Chapter 7 of Part 2 of FA 2005.

Section 790: Overview of Chapter

2320. This section provides an overview of the Chapter. It is new.
2321. *Subsection (1)* signposts the sections dealing with the three sets of circumstances addressed by the Chapter.
2322. The definition of "capital gains relief" refers to section 261B of TCGA, which is inserted by Schedule 1 to this Act.

Section 791: Charge to tax on income treated as received under section 792

2323. This section imposes a charge to tax on income treated as received under section 792. It is based on section 74(4) of FA 2005.
2324. The section follows the approach to charging provisions adopted in ITTOIA.

Section 792: Partners claiming excess sideways or capital gains relief

2325. This section treats an individual as receiving income in certain cases where regulations made under section 114 of this Act result in the individual having claimed excessive sideways relief or capital gains relief for post-1 December 2004 trade losses made by the individual as a limited partner, a member of a limited liability partnership or a non-active partner. It is based on section 74 of FA 2005.
2326. The section specifies that income is treated as arising when a "chargeable event" occurs, and that such an event occurs at any time when the regulations result in the

individual having claimed excessive relief. Such excesses (of losses so claimed over the individual's contribution to the firm) arise because the individual's contribution to the firm is treated by the regulations as reduced on the occurrence of certain events. Such an event might be, for example, the release of a loan taken out to finance the individual's contribution to the firm (see Condition 3 of Regulation 4(1) of [SI 2005/2017](#), as consequentially amended by Schedule 2 Part 5 (application of existing regulations under sections 114 and 802)).

2327. *Subsection (2)(b)* refers to “capital gains relief” as part of making explicit the interaction between section 72 of FA 1991 and the provisions in ICTA, FA 2004 and FA 2005 which restrict the giving of sideways relief. See *Change 13* in Annex 1.
2328. There is a change from “contribution to the trade” in the source legislation to “contribution to the firm”. See the overview commentary on Chapter 3 of Part 4 (restrictions on relief for certain partners) and *Change 16* in Annex 1.

Section 793: Calculating the amount of income treated as received

2329. This section specifies how the amount of income treated as received by the previous section is to be calculated. It is based on section 75 of FA 2005.
2330. The basic proposition is that the amount is the reduction in the individual's contribution to the firm resulting from the application of the regulations. Nevertheless, the amount of income treated as received cannot exceed the amount of post-1 December 2004 trade losses claimed (and not reclaimed). Neither can it exceed the excess of the trade losses claimed (and not reclaimed) over the contribution to the firm.
2331. There is a change from “contribution to the trade” in the source legislation to “contribution to the firm”. See the overview commentary on Chapter 3 of Part 4 (restrictions on relief for certain partners) and *Change 16* in Annex 1.

Section 794: Meaning of “the total amount of trade losses claimed” etc

2332. This section defines “the total amount of the trade losses claimed”, “the individual's contribution to the firm” and other terms. It is based on section 74 of FA 2005.
2333. There is a change from “contribution to the trade” in the source legislation to “contribution to the firm”. See the overview commentary on Chapter 3 of Part 4 (restrictions on relief for certain partners) and *Change 16* in Annex 1.

Section 795: Meaning of “post-1 December 2004 loss”

2334. This section defines “post-1 December 2004 loss”. It is based on section 76 of FA 2005.

Section 796: Charge to tax on income treated as received under section 797

2335. This section imposes a charge to tax on income treated as received under section 797. It is based on section 119(4) of FA 2004.
2336. The section follows the approach to charging provisions adopted in ITTOIA.

Section 797: Individuals claiming sideways or capital gains relief for film-related losses

2337. This section sets out circumstances in which an individual, who has claimed sideways or capital gains relief for film-related losses, is treated as receiving income. It is based on section 119 of FA 2004.
2338. The section specifies that income is treated as arising when a “chargeable event” occurs, and that such an event occurs at the time that the last of three conditions (relevant claim, relevant disposal and exit event) become satisfied.

2339. *Subsection (2)* specifies that an exit event will occur every time an individual receives non-taxable consideration for a relevant disposal, as well as certain times when the individual makes a further claim for sideways relief or capital gains relief or the individual's contribution to the firm is reduced. So a number of exit events may occur for any particular relevant disposal. And a number of chargeable events may occur for a particular tax year.
2340. There is a change from "contribution to the trade" in the source legislation to "contribution to the firm". See the overview commentary on Chapter 3 of Part 4 (restrictions on relief for certain partners) and *Change 16* in Annex 1.

Section 798: Meaning of "non-taxable consideration" etc

2341. This section defines "non-taxable consideration". It is based on sections 122(3) and 123(2) of FA 2004.
2342. In particular, the section makes it clear that, if the consideration is received after deduction of costs or any other payment relating to the relevant disposal or exit event, it is the gross amount that is treated as the non-taxable consideration.

Section 799: Meaning of "disposal of a right of the individual to profits" etc

2343. This section specifies a number of things that are to count as a disposal of a right of an individual to profits arising from a trade. It is based on section 120 of FA 2004.

Section 800: Meaning of "film-related losses" etc

2344. This section defines various terms. It is based on sections 121(1) and (1A) and section 123(1) of FA 2004.
2345. There is a change from "contribution to the trade" in the source legislation to "contribution to the firm". See the overview commentary on Chapter 3 of Part 4 (restrictions on relief for certain partners) and *Change 16* in Annex 1.

Section 801: Meaning of "capital contribution"

2346. This section defines "capital contribution". It is based on sections 121 and 122(1) of FA 2004.
2347. There is a change from "contribution to the trade" in the source legislation to "contribution to the firm". See the overview commentary on Chapter 3 of Part 4 (restrictions on relief for certain partners) and *Change 16* in Annex 1.

Section 802: Exclusion of amounts in calculating capital contribution by a partner

2348. This section enables regulations to be made, which can apply on a retrospective basis, to exclude certain amounts from the calculation of an individual's capital contribution. It is based on section 122A of FA 2004.
2349. Regulations under this provision are subject to the affirmative resolution procedure.
2350. There is a change from "contribution to the trade" in the source legislation to "contribution to the firm". See the overview commentary on Chapter 3 of Part 4 (restrictions on relief for certain partners) and *Change 16* in Annex 1.
2351. Some regulations have been made under section 122A of FA 2004. See the [Partnerships \(Restrictions on Contributions to a Trade\) Regulations 2005 \(SI 2005/2017\)](#) and the [Partnerships \(Restrictions on Contributions to a Trade\) Regulations 2006 \(SI 2006/1639\)](#). See also the commentary on Parts 5 and 13 of Schedule 2 about consequential amendments made to these regulations by this Act.

2352. In *subsection (5)*, the reference to Act includes references to Acts of the Scottish Parliament and Northern Ireland legislation. See *Change 152* in Annex 1, section 1018 and the commentary on that section.

Section 803: Prohibition against double counting

2353. This section ensures that consideration is only brought into account once. It is based on section 122(2) of FA 2004.
2354. There is a change from “contribution to the trade” in the source legislation to “contribution to the firm”. See the overview commentary on Chapter 3 of Part 4 (restrictions on relief for certain partners) and *Change 16* in Annex 1.

Section 804: Charge to tax on income treated as received under section 805

2355. This section imposes a charge to tax on income treated as received under section 805. It is based on section 127(2) of FA 2004.
2356. The section follows the approach to charging provisions adopted in ITTOIA.

Section 805: Partners claiming relief for licence-related trading losses

2357. This section sets out circumstances in which an individual, who was a non-active partner in an early year, and who has claimed sideways relief or capital gains relief for a loss deriving from expenditure related to a licence, is treated as receiving income. It is based on sections 126 and 127 of FA 2004.
2358. The meaning of non-active partner is explained in section 809, by reference to provisions in Chapter 3 of Part 4.
2359. There must be a relevant disposal of the licence which requires that the individual receives non-taxable consideration (defined in *subsection (5)*).
2360. Income is treated as arising when a “chargeable event” occurs which could be at any time when an individual receives non-taxable consideration for a disposal or the individual makes a further claim for sideways relief or capital gains relief. So a number of chargeable events may occur for a particular tax year.

Section 806: Calculation of amount of income treated as received by the individual

2361. This section sets out a step calculation for finding the income which the individual is treated as receiving. It is based on section 127(4) to (6) of FA 2004.

Section 807: Supplementary provision relating to calculation in section 806

2362. This section supplements section 806. It is based on section 128 of FA 2004.

Section 808: Meaning of “disposal of the licence” etc

2363. This section specifies a number of things that are to count as a disposal of a licence. It is based on section 129 of FA 2004.

Section 809: Other definitions

2364. This section includes various definitions used in relation to the restrictions for losses related to a licence. It is based on sections 126, 127(7) and 130 of FA 2004.