



Faculty of Taxation

TAXREP 22/03

TAX LAW REWRITE: PARTNERSHIPS AND CHANGES OF OWNERSHIP

Memorandum submitted in July 2003 by the Tax Faculty of the Institute of Chartered Accountants in England and Wales in response to Paper CC/SC(03)04 on Partnerships and Changes of Ownership of a Trade, Profession or Property Business issued in June 2003 by the Revenue

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TAX LAW REWRITE: PAPER CC/SC(03)04 PARTNERSHIPS AND CHANGES OF OWNERSHIP

A GENERAL COMMENTS

1. We welcome the opportunity to comment on paper CC/SC(03)04 published on 17 June 2003 at <http://www.inlandrevenue.gov.uk/rewrite/ccsc0304.pdf>.
2. The sections considering partnerships and successions in ICTA 1988 Part IV Chapter VII, so far as they concern income tax, are surprisingly brief; but, despite this, are not reader friendly (as Commentary 5). The rewritten clauses are reader friendly; in particular the improved presentation of the contents of s 111 ICTA (Treatment of partnerships). It is also helpful that the reader should not normally need to refer to the basis period rules in order to understand how the partnership rules work.
3. We note from Part 2, para 15 (Other Partnership Rules, Change of accounting basis) that the special rules for partnerships in para 13, Schedule 22 FA 2002 are expected to be moved to the partnership Part of Bill 3.
4. The references to Commentary are to the commentary included in the Explanatory Notes to Part 1 of CC/SC(03)04, and to the paragraph numbers in that commentary.

B RESPONSE TO QUESTIONS

5. As the Part is concerned with partnerships, we agree that it is appropriate to use the word ‘partnerships’ in the Part 9 title and in the title to the clause on limited liability partnerships (Commentary 3).
6. We have no objection to the use of the term ‘firm’ as a reference collectively to persons carrying on a trade in partnership as in the 1890 Partnership Act. A shorthand reference of this type is clearly a considerable drafting convenience, and it could be said a necessity.
7. Change 202 is in line with current practice and, in the case of an allocation of trade profits which results in a loss being otherwise allocated to one or more partners is supported by Special Commissioners’ decisions. In the converse situation (draft clause 667(3)) where the allocation of a trade loss results in a profit being otherwise allocated to one or more partners, and current practice is to allocate that profit to the partners with losses, there is no such support. It is probably reasonable to assume that if tested before the Commissioners, they would take the view that such practice is correct. This is an area which might perhaps give rise to further dispute by taxpayers in future, which would be

precluded by changing the law now in the way proposed. On balance, we consider that it is preferable to establish the law in these respects with certainty (and as in accordance with prevailing practice). We accordingly support this change.

8. Change 203 is also in line with current practice, where a non-trading firm starts to trade, and is appropriate to avoid the apparent requirement otherwise (under s 111(8)(b) ICTA) of re-determining the basis periods for non-trading income for all years since a partner joined the firm.
9. We welcome Change 207 (Partnerships: resident partners and double taxation agreements: clause 673), as enacting the Inland Revenue practice of giving a narrow interpretation to the word 'affect' in s 112(4) ICTA and hence making it clear that it is only a partner's chargeability to tax that is preserved and that the partner is not also denied any relief under a double taxation treaty.
10. We note that work continues on the correct interpretation of the definition of a 'Schedule A business' in s 832(1) ICTA (Commentary 71-73) and that, for the purposes of both overseas and UK property businesses in drafting clause 674(2)-(6), it is read as referring to the whole collection of businesses and activities as a single composite business rather than to the businesses and activities which constitute that single business. We also note that in consequence s 113(2) ICTA as applied to a property business by s 21B ICTA is rewritten so as to apply to both UK and overseas property businesses as so read (Note 151, fourth to sixth paragraphs). This is a logical drafting of clause 674, based on the single business interpretation of the s 832(1) ICTA definition of 'Schedule A business' adopted.
11. On the person-based approach (as referred to in Part 3, paragraph 3 (Change of Ownership)) we agree that there is no need for a general rule as in s 113(1) ICTA and accordingly that this need not be rewritten. We also agree that in consequence s 113(2) ICTA need not be rewritten, and that its continuity effect on a partial change in the members of a firm could instead be maintained by reproducing the continuity rule in those particular provisions affected (as indicated in Part 3, paragraph 22). As also indicated in Part 3, paragraphs 9 and 11, this approach in the rewrite is provisional subject to anything arising from your work on the consequential amendments.
12. We agree that it is unnecessary to rewrite ss 60(4) and 113(6), following the introduction of self-assessment and the adequacy of s 74 TMA 1970 (that the personal representatives inherit the tax liabilities of the deceased).
13. We agree that, on the person-based approach, there is no need to rewrite s 89 ICTA (Debts proving irrecoverable after event treated as discontinuance). However, is the deemed continuity of the trade as far as bad debts are concerned still preserved in the rewritten rule for bad debts (last published as clause 33 in ED13)? Is a loss on the assigned debt in fact a loss connected with or arising out of 'the (new) trade' referred to in s 74(1)(e) ICTA, as stated in Part 3, paragraph 28? Clause 33 in ED13 refers of course more widely to 'a debt owed to the person carrying on the trade', which would evidently include a (loss on a) debt assigned in the circumstances postulated. Clarification is sought on this.

C SPECIFIC COMMENTS

14. *cl 665 (Introductory)*

(2)

The drafting makes it quite clear that a firm is not to be regarded as an entity separate and distinct from the partners (as it is legally in Scotland) ‘*for tax purposes*’ only and this appears as a sensible way of treating all firms in the same way.

15. *cl 666 (Calculation of firm’s profits)*

(2)

To make the contrast with clause 666(3) clearer, should the word ‘chargeable to income tax’ be replaced by the words ‘resident in the United Kingdom’?

16. *cl 667 (Allocation of firm’s profits between partners)*

(2), (3)

Is it made sufficiently clear that ‘TP’ and ‘TL’ respectively include the profits or losses of any corporate partners?

17. *cl 668 (Basis periods for notional trades)*

We have no objection to the use of the description ‘notional trade’ in this clause.

18. *cl 670 (Basis periods for notional businesses)*

We agree the use of the term ‘notional businesses’ (as referred to in Commentary 37), as regards the untaxed income of a firm carrying on a trade, as being clearer than s 111(8) ICTA. Clause 670(2) is also helpful in making clear that the basis period for the notional business is the same as that for the partner’s share of the firm’s trade profits; subject to clause 670(3) and (4).

19. *cl 671 (Carrying on by partner of notional business)*

(2)

Commentary 48 makes explicit that the basis periods for a partner’s notional business are determined when the firm starts the notional trade if not trading when the partner joins it, and even before the firm starts to receive untaxed income. In this context, would it be clearer in clause 671(2) to replace the word ‘continues’ by ‘exists’ as referring to notional businesses starting as well as continuing?

D DETAILED COMMENTS ON DRAFTING

20. *cl 671 (Carrying on by partner of notional business)*

(4)

Perhaps a pedantic point; but, consistent with the terminology used elsewhere in this clause, should the words ‘to carry on’ be inserted after ‘ceasing’, and ‘starting’ respectively in the penultimate and ultimate lines?

21. In Commentary 56 – second line – ‘in’ should be ‘on’.
22. In Commentary 94 – second bullet point – ‘would’ should be ‘wound’.
23. In Part 3, paragraph 8 – second line – delete ‘on’ after the second ‘carry’.
24. In Annex 1, Change 202 – in the second line of the penultimate paragraph, delete the first ‘the’ after ‘that’.

14-13-36
TJH/PCB
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