



Income Tax (Trading and Other Income) Act 2005

2005 CHAPTER 5

PART 9

PARTNERSHIPS

Introduction

846 Overview of Part 9

This Part contains some special rules about partnerships.

847 General provisions

- (1) In this Act persons carrying on a trade in partnership are referred to collectively as a “firm”.
- (2) The provisions of this Part are expressed to apply to trades but unless otherwise indicated (whether expressly or by implication) also apply—
 - (a) to professions, and
 - (b) in the case of this section and sections 849, 850, 857 and 858 to businesses that are not trades or professions.
- (3) In those sections as applied by subsection (2)(b)—
 - (a) references to a trade are references to a business, and
 - (b) references to the profits of a trade are references to the income arising from a business.

848 Assessment of partnerships

Unless otherwise indicated (whether expressly or by implication), a firm is not to be regarded for income tax purposes as an entity separate and distinct from the partners.

*Calculation of partners' shares***849 Calculation of firm's profits or losses**

- (1) If—
- (a) a firm carries on a trade, and
 - (b) any partner in the firm is chargeable to income tax,
- the profits or losses of the trade are calculated on the basis set out in subsection (2) or (3), as the case may require.
- (2) For any period of account in which the partner is a UK resident individual, the profits or losses of the trade are calculated as if the firm were a UK resident individual.
- (3) For any period of account in which the partner is non-UK resident, the profits or losses of the trade are calculated as if the firm were a non-UK resident individual.

850 Allocation of firm's profits or losses between partners

- (1) For any period of account a partner's share of a profit or loss of a trade carried on by a firm is determined for income tax purposes in accordance with the firm's profit-sharing arrangements during that period.

This is subject to subsections (2) and (4).

- (2) If for the period of account the calculation under section 849 in relation to the partner produces a profit, but there is at least one loss-making partner—
- (a) each loss-making partner's share is neither a profit nor a loss, and
 - (b) each profit-making partner's share is given by the formula in subsection (3).
- (3) The formula is—

$$FP \times \frac{PP}{TP}$$

where—

FP is the amount of the firm's profit calculated under section 849 in relation to the partner,

PP is the amount determined under subsection (1) to be the profit of the profit-making partner in question, and

TP is the total of the amounts determined under subsection (1) to be the profits of all the profit-making partners.

- (4) If for the period of account the calculation under section 849 in relation to the partner produces a loss, but there is at least one profit-making partner—
- (a) each profit-making partner's share is neither a profit nor a loss, and
 - (b) each loss-making partner's share is given by the formula in subsection (5).

- (5) The formula is—

$$FL \times \frac{PL}{TL}$$

where—

FL is the amount of the firm’s loss calculated under section 849 in relation to the partner,

PL is the amount determined under subsection (1) to be the loss of the loss-making partner in question, and

TL is the total of the amounts determined under subsection (1) to be the losses of all the loss-making partners.

(6) In this section—

“loss-making partner” means a partner whose share is determined under subsection (1) to be a loss,

“partner”, in relation to a firm, means any partner in the firm, whether or not chargeable to income tax,

“profit-making partner” means a partner whose share is determined under subsection (1) to be a profit, and

“profit-sharing arrangements” means the rights of the partners to share in the profits of the trade and the liabilities of the partners to share in the losses of the trade.

851 Calculations etc. where firm has other income or losses

(1) This section applies if—

- (a) sections 849 and 850 apply in relation to the profits or losses of a trade carried on by a firm, and
- (b) the firm has other income or losses.

(2) Those sections also apply as if references to the profits or losses of the trade were references to the other income or losses.

Firms with trading income

852 Carrying on by partner of notional trade

(1) For each tax year in which a firm carries on a trade (the “actual trade”), each partner’s share of the firm’s trading profits or losses is treated, for the purposes of Chapter 15 of Part 2 (basis periods), as profits or losses of a trade carried on by the partner alone (the “notional trade”).

(2) A partner starts to carry on a notional trade at the later of—

- (a) when becoming a partner in the firm, and
- (b) when the firm starts to carry on the actual trade.

This is subject to subsection (3).

(3) If the partner carries on the actual trade alone before the firm starts to carry it on, the partner starts to carry on the notional trade when the partner starts to carry on the actual trade.

(4) A partner permanently ceases to carry on a notional trade at the earlier of—

- (a) when the partner ceases to be a partner in the firm, and
- (b) when the firm permanently ceases to carry on the actual trade.

This is subject to subsections (5) and (6).

- (5) If the partner carries on the actual trade alone after the firm permanently ceases to carry it on, the partner permanently ceases to carry on the notional trade when the partner permanently ceases to carry on the actual trade.
- (6) If—
- (a) the firm carries on the actual trade wholly or partly outside the United Kingdom, and
 - (b) the partner becomes or ceases to be UK resident,
- the partner is treated as permanently ceasing to carry on one notional trade when the change of residence occurs and starting to carry on another immediately afterwards.
- (7) Subsection (6) does not prevent a loss made before the change of residence from being carried forward under section 385 of ICTA and set against profits arising after the change.

853 Basis periods for partners' notional trades

- (1) The basis period of a partner's notional trade is determined by applying the rules in Chapter 15 of Part 2 as if—
- (a) the trade were carried on by an individual, and
 - (b) its accounts were drawn up to the same dates as the accounts of the actual trade.

This is subject to subsection (2).

- (2) If, on the assumption that the actual trade is carried on by an individual,—
- (a) section 216 (change of accounting date in later tax year) would apply in relation to the actual trade, but
 - (b) the basis period for the actual trade would be given by subsection (4) of that section (ineffective change of accounting date), because the conditions in section 217 (conditions for basis period to end with new accounting date) would not be met in relation to that trade,
- the accounts of the actual trade are treated for the purposes of subsection (1) as drawn up to the old accounting date.
- (3) For the purposes of determining whether, on the assumption that the actual trade is carried on by an individual, the conditions in section 217 would be met in relation to that trade—
- (a) a notice under section 217(2) must be given by one of the partners in the firm nominated by them for the purposes of this subsection, and
 - (b) any appeal under section 218(4) against a notice by the Inland Revenue must be made by a partner so nominated.
- (4) Section 207 (treatment of business start-up payments received in overlap period) applies as a result of this section in relation to a partner's notional trade so that—
- (a) the requirement in subsection (1)(a) of that section becomes a requirement that the partner's share of the firm's profits so far as attributable to a business start-up payment falls within two basis periods, and
 - (b) the reference in subsection (2) of that section to the payment is a reference to any part of the partner's share of the firm's profits which is so attributable.

Firms with trading and other source income

854 Carrying on by partner of notional business

- (1) For each tax year in which a firm—
 - (a) carries on a trade, and
 - (b) has untaxed income or relieviable losses from other sources,each partner's share of the firm's untaxed income or relieviable losses other than trading profits or losses is treated, for the purposes of Chapter 15 of Part 2, as profits or losses of a trade carried on by the partner alone (the "notional business").
- (2) A partner starts to carry on a notional business at the later of—
 - (a) when becoming a partner in the firm, and
 - (b) when the firm starts to carry on a trade.
- (3) A notional business continues even if either or both of the following occur—
 - (a) separate sources of income that comprise the business start and cease, and
 - (b) no income arises during a particular tax year.

This is subject to subsections (4) and (5).

- (4) A partner permanently ceases to carry on a notional business at the earlier of—
 - (a) when the partner ceases to be a partner in the firm, and
 - (b) when the firm permanently ceases to carry on a trade.
- (5) If—
 - (a) the firm carries on the trade wholly or partly outside the United Kingdom, and
 - (b) the partner becomes or ceases to be UK resident,the partner is treated as permanently ceasing to carry on one notional business when the change of residence occurs and starting to carry on another immediately afterwards.
- (6) In this section "untaxed income" means any income that is not—
 - (a) income from which income tax has been deducted,
 - (b) income from or on which income tax is treated as having been deducted or paid, or
 - (c) dividends or other distributions of a company chargeable under Chapter 3 of Part 4.

855 Basis periods for partners' notional businesses

- (1) The general rule is that the basis period for a partner's notional business is the same as the basis period for a partner's notional trade, but subject to the exceptions in subsections (2) and (3).
- (2) If the partner carries on the actual trade alone before the firm starts to carry it on the partner is treated as starting to carry on the notional business when the partnership is set up.
- (3) If the partner carries on the actual trade alone after the firm permanently ceases to carry it on the partner is treated as permanently ceasing to carry on the notional business when the firm permanently ceases to carry on the actual trade.

856 Overlap profits from partners' notional businesses

- (1) This section applies if—
- (a) the basis period for a partner's notional business for a tax year is given by—
 - (i) section 215 (change of accounting date in third tax year), or
 - (ii) section 216(3) (change of accounting date in later tax year),
 - (b) a deduction is to be made for overlap profit under section 220 in calculating the profits of the notional business of the tax year, and
 - (c) the amount to be deducted exceeds the amount which would otherwise be the amount of the profits of the notional business of the tax year.
- (2) This section also applies if—
- (a) the basis period for a partner's notional business for a tax year is given by section 202 (final tax year),
 - (b) a deduction is to be made for overlap profit under section 205 in calculating the profits of the notional business of the tax year, and
 - (c) the amount to be deducted exceeds the amount which would otherwise be the amount of the profits of the notional business of the tax year.
- (3) The amount of the excess is to be deducted in calculating the partner's income for the tax year.

*Firms with a foreign element***857 Partners to whom the remittance basis may apply**

- (1) This section applies if—
- (a) a firm carries on a trade wholly or partly outside the United Kingdom,
 - (b) the control and management of the trade is outside the United Kingdom, and
 - (c) a partner who is a UK resident individual—
 - (i) meets condition A or B in section 831 (conditions to be met for income to be charged on the remittance basis), and
 - (ii) makes a claim to that effect for a tax year.
- (2) The partner's share of the profits of the trade arising in the United Kingdom is determined in accordance with sections 849 to 856.
- (3) The partner's share of the profits of the trade arising outside the United Kingdom is treated as relevant foreign income for the purposes of this Act (see Part 8).

858 Resident partners and double taxation agreements

- (1) This section applies if—
- (a) a UK resident (“the partner”) is a member of a firm which—
 - (i) resides outside the United Kingdom, or
 - (ii) carries on a trade the control and management of which is outside the United Kingdom, and
 - (b) by virtue of any arrangements having effect under section 788 of ICTA (“the arrangements”) any of the income of the firm is relieved from income tax in the United Kingdom.

- (2) The partner is liable to income tax on the partner's share of the income of the firm despite the arrangements.
- (3) If the partner's share of the income of the firm consists of or includes a share in a qualifying distribution—
 - (a) made by a UK resident company, and
 - (b) chargeable to tax under Chapter 3 of Part 4,the partner (and not the firm) is, despite the arrangements, entitled to the share of the tax credit which corresponds to the partner's share of the distribution.

Miscellaneous

859 Special provisions about farming and property income

- (1) The rule in section 9(2) (farming trades) operates in relation to firms so that—
 - (a) all farming in the United Kingdom which a firm carries on, other than farming carried on as part of another trade, is treated as one trade, but
 - (b) the farming carried on by a firm which is treated as one trade is not included in any farming trade of any partner in the firm.
- (2) Section 264 (UK property business) operates in relation to firms so that—
 - (a) every business and transaction mentioned in that section carried on, or entered into, by a firm constitutes the firm's UK property business, but
 - (b) each business or transaction included in the firm's UK property business is not included in any UK property business of any partner in the firm.
- (3) Section 265 (overseas property business) operates in relation to firms so that—
 - (a) every business and transaction mentioned in that section carried on, or entered into, by a firm constitutes the firm's overseas property business, but
 - (b) each business or transaction included in the firm's overseas property business is not included in any overseas property business of any partner in the firm.

860 Adjustment income

- (1) A change in the persons carrying on a trade from one period of account to the next does not prevent Chapter 17 of Part 2 (adjustment income) applying in relation to the trade so long as a person carrying on the trade immediately before the change continues to carry on the trade immediately after the change.
- (2) A change in the persons carrying on a trade does not constitute the permanent cessation of the trade for the purposes of Chapter 17 of Part 2 so long as a person carrying on the trade immediately before the change continues to carry on the trade immediately after the change.
- (3) In the case of a trade carried on by a firm the amount of any adjustment under Chapter 17 of Part 2 is calculated as if the firm were a UK resident individual.
- (4) Each partner's share of any amount of adjustment income is determined according to the firm's profit-sharing arrangements for the 12 months ending immediately before the date on which the new basis was adopted.

- (5) Any election under Chapter 17 of Part 2 must be made jointly by all the persons who have been members of the firm in that 12 month period.
- (6) For the purposes of this section—
- (a) “adjustment income” and “change of basis” have the same meaning as in Chapter 17 of Part 2,
 - (b) “profit-sharing arrangements” means the rights of the partners to share in the profits of the trade, and
 - (c) references to the date on which a new basis was adopted are to the first day of the first period of account for which the new basis was adopted.
- (7) Sections 849 to 856 do not apply so far as this section applies.

861 Sale of patent rights: effect of partnership changes

- (1) This section applies if—
- (a) a person (“the trader”) sells the whole or part of any patent rights in carrying on a trade, and
 - (b) the tax condition, the partnership condition and the non-cessation condition are met.
- (2) The tax condition is that—
- (a) tax is charged under section 587 on the proceeds of the sale or on any instalment of those proceeds, and
 - (b) by virtue of any of sections 590(2) or (4), 591(2) or 592(2), one sixth of the amount chargeable is charged in the tax year in which the trader receives the proceeds or the instalment and in each of the 5 subsequent tax years.
- (3) The partnership condition is that—
- (a) the trader is a firm at the time of the sale, or
 - (b) the trade is carried on in partnership at any time during the period beginning with the tax year in which the trader receives the proceeds or the instalment and ending with the last of the 5 subsequent tax years (“the tax spreading period”).
- (4) The non-cessation condition is that—
- (a) there is a change in the persons carrying on the trade during the tax spreading period, and
 - (b) a person who carried on the trade immediately before the change continues to carry on the trade immediately after the change.
- (5) Any amounts chargeable under section 587 during the remainder of the tax spreading period are charged on the person or persons for the time being carrying on the trade.
- (6) Such amounts are charged as if—
- (a) that person or those persons had at all times been carrying on the trade, and
 - (b) everything done to or by the predecessors of that person or those persons in carrying on the trade had been done to or by that person or those persons.

862 Sale of patent rights: effect of later cessation of trade

- (1) This section applies if—

Status: This is the original version (as it was originally enacted).

- (a) a person (“the trader”) sells the whole or part of any patent rights in carrying on a trade,
 - (b) by virtue of section 861 a charge under section 587 falls to be made on any person for the time being carrying on the trade in partnership,
 - (c) any such person permanently ceases to carry on the trade thereafter, and
 - (d) no person who carried on the trade immediately before the cessation continues to carry on the trade immediately after the cessation.
- (2) Any amounts which would have been chargeable in later tax years are charged in the tax year in which the cessation occurs.
- (3) Each partner’s share (or, if the partner is dead, the share of the partner’s personal representatives) of any additional amount chargeable under subsection (2) is determined in accordance with the firm’s profit-sharing arrangements immediately before the cessation.
- (4) If an additional amount is chargeable under subsection (2), the person liable may elect that the amount of income tax payable should be reduced to the amount that would have been payable on the assumptions mentioned in subsection (5).
- (5) The assumptions are—
- (a) that subsection (2) does not apply, and
 - (b) that the total of the amounts that would have been charged in later tax years is charged in equal instalments in each of the tax years—
 - (i) beginning with the year in which the trader received the proceeds of the sale or instalment of those proceeds, and
 - (ii) ending with the year in which the cessation occurs.
- (6) The election must be made on or before the first anniversary of the normal self-assessment filing date for the tax year in which the cessation occurred.
- (7) For the purposes of this section “profit-sharing arrangements” means the rights of the partners to share in the profits of the trade.

863 Limited liability partnerships

- (1) For income tax purposes, if a limited liability partnership carries on a trade, profession or business with a view to profit—
- (a) all the activities of the limited liability partnership are treated as carried on in partnership by its members (and not by the limited liability partnership as such),
 - (b) anything done by, to or in relation to the limited liability partnership for the purposes of, or in connection with, any of its activities is treated as done by, to or in relation to the members as partners, and
 - (c) the property of the limited liability partnership is treated as held by the members as partnership property.

References in this subsection to the activities of the limited liability partnership are to anything that it does, whether or not in the course of carrying on a trade, profession or business with a view to profit.

- (2) For all purposes, except as otherwise provided, in the Income Tax Acts—

Status: This is the original version (as it was originally enacted).

- (a) references to a firm include a limited liability partnership in relation to which subsection (1) applies,
 - (b) references to members of a firm include members of such a limited liability partnership,
 - (c) references to a company do not include such a limited liability partnership, and
 - (d) references to members of a company do not include members of such a limited liability partnership.
- (3) Subsection (1) continues to apply in relation to a limited liability partnership which no longer carries on any trade, profession or business with a view to profit—
- (a) if the cessation is only temporary, or
 - (b) during a period of winding up following a permanent cessation, provided—
 - (i) the winding up is not for reasons connected in whole or in part with the avoidance of tax, and
 - (ii) the period of winding up is not unreasonably prolonged.

This is subject to subsection (4).

- (4) Subsection (1) ceases to apply in relation to a limited liability partnership—
- (a) on the appointment of a liquidator or (if earlier) the making of a winding-up order by the court, or
 - (b) on the occurrence of any event under the law of a territory outside the United Kingdom corresponding to an event specified in paragraph (a).