

### Deductible Expenditure - General Rule

Expenses are deductible if they are incurred wholly and exclusively for the purposes of the trade.

### Classes of Allowable Expenditure

Expenses must be wholly and exclusively for trade purposes. Key allowable costs include:

1. **Interest** (except on overdue tax).
2. **Legal & professional fees** (unless for capital items).
3. **Damages & compensation payments.**
4. **VAT unable to reclaim.**
5. **Trade subscriptions.**
6. **Employees' remuneration** (genuine salaries; excessive payments to relatives disallowed).
7. **Theft by staff** (unless they control the business).
8. **Travel expenses** (excluding home-to-work commutes, unless home is the work base).
9. **Patent royalties & trademark registration costs.**
10. **Incidental loan costs** (for business loans).

### Current Year Basis

**CYB** when business profits are taxed in the owner's tax returns.

- During the main years of operation, CYB is the standard method.

**Example** A trader with a 31st December 2023 year-end would have profits taxed in the 2023/2024 tax year.

### Disallowed Expenditure

Certain expenses are disallowed for tax purposes under Case Law or Statute Law:

1. **Capital Expenditure** (ITTOIA 2005) No clear definition, but includes items providing an "Enduring Benefit" (Atherton v British Insulated & Helsby Cables).
2. **Drawings** Owner's personal withdrawals, salary, or benefits (e.g., tax/NI payments).
3. **Provisions** Generally allowed if following accounting standards, but general provisions for bad debts are disallowed.
4. **Entertainment and Gifts** **Customer entertainment** is generally disallowed.  
  
**Allowed deductions:** Staff parties (employees may be taxed). Gifts to employees (wholly & exclusively for trade). Samples of trading goods (PR exercise).
5. **Political Donations and Subscriptions** Generally not allowed, unless providing a definite trade benefit (Morgan v Tate & Lyle).

### Disallowed Expenditure (cont)

6. **Fines and Penalties** Generally **not allowed**, but parking fines for employees using company vehicles are permitted (employee may incur a benefit-in-kind tax).

7. **Illegal Payment** Payments like bribes or blackmail are not allowed.

### Expenditure not shown in accounts

Depreciation (a capital item) is added back and replaced with **Capital Allowances**, the tax-equivalent deduction for capital expenditure. Details follow in the next lecture.

### Adjustments relating to Income

To calculate taxable profit, income adjustments are needed:

#### 1. Remove Non-Trading Income

Examples:

- Interest and income are taxed elsewhere.
- Profits/losses from capital asset disposal.
- Changes in general provisions (already noted under expenses).

#### 2. Insert Missing Trading Income

- Typically includes owner consumption of own goods, treated at market value (ITTOIA 2005).