

Trade Charges

Relief from Income Tax

Part 08-02-02

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1. What is a 'Trade Charge'?

The phrase 'trade charge', in this manual and for income tax purposes, is used to mean an annuity or annual payment which is paid wholly and exclusively for the purposes of a trade or profession. Such payments do not qualify as a deduction in computing Case I or Case II profits by virtue of section 81(2)(I) TCA 1997 but section 390 provides that relief for these payments may be available as a trading loss carried forward under section 382 or as part of a terminal loss relief claim under section 385.

2. How is relief given for Trade Charges?

2.1. Trade charge paid out of income brought into charge

Where the trade charge is paid out of income which is brought into charge:

- Section 237 provides that the payor of a trade charge **may** deduct and retain tax at the standard rate from the trade charge.
- Section 16 provides that profits or gains on which a person is assessed and charged with tax out of which a trade charge is paid is charged to tax at the standard rate. That is, the portion of an individual's total income which represents the amount of the trade charge is taxed at the standard rate.

The effect of section 237 and section 16 is the amount of tax retained by the payor (under section 237) is the same as the standard rate of tax which is payable on the income from which the payment is made (under section 16), meaning that effectively the payor bears no tax on income from which the payment was made.

Example 1 – Ignoring Personal Reliefs

Mr A, who is single, has Case I profits of €100,000. He makes an annual payment of €1,000 to Ms B and this payment is wholly and exclusively for the purposes of his trade.

Calculate Mr A's income tax liability for 2022

| | |
|-----------------------------|-----------------|
| Case I profits | €100,000 |
| Total Income | €100,000 |
| €36,800 @ 20% [s. 15(2)(a)] | €7,360 |
| €1,000 @ 20% [s. 16] | €200 |
| €63,200 @ 40% [s. 15(2)(a)] | €25,280 |
| Total amount due to Revenue | <u>€32,840</u> |

Cash flow position of Mr A as regards annual payment

Mr A paid €800 of the annual payment to Ms B, and withheld €200, being tax at the standard rate [section 237].

In computing Mr A's income tax liability for the year, the total income out of which the €1,000 annual payment was paid is subject to tax at the standard rate, meaning €200 tax is due on that income.

As Mr A withheld €200 from Ms B, he does not bear the cost of any tax due on the income out of which the annual payment is made.

2.2. Trade charge not paid out of income brought into charge

Where the amount of income brought into charge is less than the trade charge there is not enough Total Income to tax at the standard rate to ensure that 20% of the annual payment is paid to Revenue. Therefore, relief cannot be given as outlined above. Instead the relevant provisions are section 238 and section 390.

Unlike section 237, section 238 **obliges** the payor to deduct tax at the standard rate and to pay over any such tax to Revenue.

Section 390 provides that the amount of a trade charge (other than an amount not ultimately borne by the taxpayer or which is capital in nature) to which section 238, has applied, can be treated as a trading loss for the purposes of carry forward under section 382 and for terminal loss relief under section 385.

In this way, the taxpayer is able to carry forward the unused trade charge for offset against trading profits in future years, or where the trade has ceased, to carry back the unused trade charge for offset against trading profits in previous years.

Example 2 – Ignoring Personal Reliefs

Mr C, who is single, has Case I profits of €10,000 and trading losses of €10,000 carried forward under section 382. He makes an annual payment of €1,000 to Ms B and this payment is wholly and exclusively for the purposes of his trade.

Calculate Mr C's income tax liability

| | |
|---|-------------|
| Case I profits | €10,000 |
| Less: | |
| Loss forward [s.382] | (€10,000) |
| Total Income | Nil |
| Amounts withheld at source and due to Revenue | |
| €1,000 @ 20% [s. 238(3)] | €200 |
| Total amount due to Revenue | <u>€200</u> |

By virtue of section 390, the €1,000 trade charge which had tax deducted under section 238 is available for Mr C to carry forward as a loss under section 382 or if Mr C's trade ceases it may form part of a terminal loss claim.

Cash flow position of Mr C as regards annual payment

Mr C paid €800 of the annual payment to Ms B, and withheld €200, being tax at the standard rate. He must pay the €200 tax withheld over to Revenue.

Example 3 – Ignoring Personal Reliefs

Ms D, who is single, has Case I profits of €10,000, capital allowances of €2,000 and losses forward from a previous year of €7,300. She makes an annual payment of €1,000 to Ms B. This payment is wholly and exclusively for the purposes of Ms D's trade and is not capital in nature.

Calculate Ms D's income tax liability

| | |
|---|-----------------|
| Case I profits | €10,000 |
| Less: | |
| Capital allowances [s.284] | (€2,000) |
| Loss forward [s.382] | <u>(€7,300)</u> |
| Total Income | €700 |
| €700 @ 20% [s. 16] | €140 |
| Amounts withheld at source and due to Revenue | |
| €300 @ 20% [s. 238(3)] | €60 |
| Total amount due to Revenue | <u>€200</u> |

Note

The maximum amount of trade charges which are taxable at the 'increased standard rate band' is arrived at by taking Case I profits, less capital allowances less losses forward. In this case, the maximum allowed is €700. Therefore, the annual payment of €1,000 comprises two elements:

| | |
|---|-------------|
| Amount paid out of income brought to charge, subject to s.237 | €700 |
| Other amounts, subject to s.238 | <u>€300</u> |
| Total annual payment | €1,000 |

By virtue of section 390, the €300 trade charge which had tax deducted under section 238 is available for Ms D to carry forward as a loss under section 382 or if Ms D's trade ceases it may form part of a terminal loss claim.

Cash flow position of Ms D as regards annual payment

Ms D paid €800 of the annual payment to Ms B, and withheld €200, being tax at the standard rate.

In computing Ms D's income tax liability for the year, the income out of which €700 of the annual payment was paid is subject to tax at the standard rate, meaning Ms D owes €140 tax on that portion of her income. As in example 1, this is equivalent to the €140 tax withheld from Ms B. Therefore, Ms D does not bear the cost of the €140 tax due on the income out of which the annual payment is made.

The balance of the annual payment (€300) is not paid out of taxed profits. Therefore, the tax withheld in relation to the €300, being €60, must be remitted to Revenue under section 238(3).

Therefore, €200 was deducted at source from the annual payment and €200 in tax in total must be paid to Revenue (€140 due on Ms D's income and €60 as tax withheld at source).

3. Universal Social Charge (USC) and Pay Related Social Insurance (PRSI)

Trade charges are not deductible for the purposes of USC or PRSI.