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*Changes to legislation: There are currently no known outstanding effects for the Finance Act 2006, SCHEDULE 8. (See end of Document for details)*

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## SCHEDULES

### SCHEDULE 8

Section 81

#### LONG FUNDING LEASES OF PLANT OR MACHINERY

##### PART 1

##### CAPITAL ALLOWANCES

###### *Introductory*

1 CAA 2001 is amended as follows.

*Use for other qualifying activity of plant or machinery previously used for long funding leasing*

2 After section 13 (use for qualifying activity of plant or machinery provided for other purposes) insert—

**“13A Use for other purposes of plant or machinery previously used for long funding leasing**

- (1) This section applies if a person who has been using plant or machinery for the purpose of leasing it under a long funding lease (see Chapter 6A)—
  - (a) ceases to use the plant or machinery for that purpose without ceasing to use it for the purposes of a qualifying activity carried on by him, and
  - (b) on the date of the cessation, owns the plant or machinery as a result of having incurred capital expenditure on its provision for the purposes of the qualifying activity.
- (2) The person is to be treated—
  - (a) as having incurred capital expenditure (“notional expenditure”) on the provision of the plant or machinery for the purposes of the qualifying activity on the day after the cessation,
  - (b) as owning the plant or machinery as a result of having incurred that expenditure, and
  - (c) as if the plant or machinery on and after that day were different plant or machinery from the plant or machinery before that day.
- (3) The amount of the notional expenditure is an amount equal to the termination amount, determined in accordance with section 70YG, in the case of the long funding lease under which the plant or machinery was last leased before the cessation.”.

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*Expenditure on plant or machinery for long funding leasing not to be qualifying expenditure*

3 After section 34 insert—

**“34A Expenditure on plant or machinery for long funding leasing not qualifying expenditure**

Expenditure is not qualifying expenditure if it is incurred on the provision of plant or machinery for leasing under a long funding lease (see Chapter 6A).”.

*General exclusions applying to certain sections*

4 (1) Section 46 is amended as follows.

(2) In subsection (2) (the general exclusions) in general exclusion 8—

(a) for “Either” substitute “Any “, and

(b) after the entry relating to section 13 insert— “ section 13A (use for other purposes of plant or machinery provided for long funding leasing);”.

*Commencement of leasing under long funding lease: disposal events and disposal values*

5 (1) Section 61 (disposal events and disposal values) is amended as follows.

(2) In subsection (1) (disposal events) after paragraph (e) insert—

“(ee) the plant or machinery begins to be leased under a long funding lease (see Chapter 6A);”.

(3) In subsection (2) (disposal values) in the Table (disposal event, disposal value) after item 5 insert—

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“5A. Commencement of the term of a long funding finance lease of the plant or machinery.

An amount equal to that which would fall to be recognised as the lessor's net investment in the lease if accounts were prepared in accordance with generally accepted accounting practice on the date on which the lessor's net investment in the lease is first recognised in the books or other financial records of the lessor.

5B. Commencement of the term of a long funding operating lease of the plant or machinery.

An amount equal to the market value of the plant or machinery at the commencement of the term of the lease.”.

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(4) In item 6 in that Table (which refers to the occurrence of an event within items 1 to 5) for “5” substitute “ 5B ”.

*Lessee under long funding lease: capital allowances, disposal events and disposal values*

6 In Chapter 6 of Part 2 (hire-purchase etc and plant or machinery provided by lessee) after section 70 insert—

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*“Lessees under long funding leases*

**70A Entitlement to capital allowances**

- (1) This section applies if a person carrying on a qualifying activity incurs expenditure (whether or not of a capital nature) on the provision of plant or machinery for the purposes of the qualifying activity under a long funding lease.
- (2) In the application of this Part in the case of that person, the plant or machinery is to be treated as owned by him at any time when he is the lessee under the long funding lease.

That is so whether or not the lease also falls to be regarded as a long funding lease in the application of this Part in the case of the lessor.

- (3) The person is to be treated for the purposes of this Part as having incurred capital expenditure on the provision of the plant or machinery as follows.
- (4) The capital expenditure is to be treated as incurred at the commencement of the term of the long funding lease.
- (5) The amount of the capital expenditure varies, according to whether the long funding lease is—
  - (a) a long funding operating lease (subsection (6)), or
  - (b) a long funding finance lease (subsection (7)).
- (6) If the long funding lease is a long funding operating lease, the amount of the capital expenditure is to be found in accordance with section 70B.
- (7) If the long funding lease is a long funding finance lease, the amount of the capital expenditure is to be found in accordance with section 70C.
- (8) See Chapter 6A for interpretation of this section.

**70B Long funding operating lease: amount of capital expenditure**

- (1) This section applies by virtue of section 70A(6).
- (2) If the long funding lease is a long funding operating lease, the amount of the capital expenditure is the market value of the plant or machinery at the later of—
  - (a) the commencement of the term of the lease;
  - (b) the date on which the plant or machinery is first brought into use for the purposes of the qualifying activity.
- (3) This section is to be construed as one with section 70A.

**70C Long funding finance lease: amount of capital expenditure**

- (1) This section has effect by virtue of section 70A(7) for the purpose of determining the amount of the capital expenditure in the case of a long funding finance lease.

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- (2) If the lease is one which, under generally accepted accounting practice, falls (or would fall) to be treated as a loan, this section applies as if the lease were one which, under generally accepted accounting practice, fell to be treated as a finance lease.
- (3) The amount of the capital expenditure is the total of—
- (a) commencement PVMLP (see subsection (4)), and
  - (b) if subsection (6) applies, the unrelievable pre-commencement rentals (“UPR”),
- but subject, in a case falling within subsection (7), to the restriction imposed by subsection (8).
- (4) Commencement PVMLP is the amount that would fall to be recognised as the present value, at the appropriate date, of the minimum lease payments (see section 70YE) if appropriate accounts were prepared by the person.
- (5) For the purposes of subsection (4)—
- “appropriate accounts” are accounts prepared in accordance with generally accepted accounting practice on the date on which that amount is first recognised in the books or other financial records of the person;
- “the appropriate date” is the later of—
- (a) the commencement of the term of the lease;
  - (b) the date on which the plant or machinery is first brought into use for the purposes of the qualifying activity.
- (6) This subsection applies if—
- (a) the person has paid rentals under the lease before the commencement of the term of the lease, and
  - (b) in the case of some or all of those rentals, relief otherwise than by virtue of this subsection—
    - (i) is not available, and
    - (ii) if the case is one where the plant or machinery was not used for the purposes of a qualifying activity in the period before the commencement of the term of the lease, would not have been available had the plant or machinery been used in that period for the purposes of a qualifying activity,
- and in any such case UPR is the amount of the rentals for which relief is not, and (in a case falling within paragraph (b)(ii)) would not have been, so available.
- (7) Subsection (8) applies if the main purpose, or one of the main purposes, of entering into—
- (a) the lease,
  - (b) a series of transactions of which the lease is one, or
  - (c) any of the transactions in such a series,
- is to obtain allowances under this Part in respect of an amount of capital expenditure that materially exceeds the market value of the leased asset at the commencement of the term of the lease.

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- (8) In any such case, the amount of the capital expenditure described in subsection (3) is to be restricted to an amount equal to the market value of the asset at the commencement of the term of the lease.
- (9) In this section “relief” means relief by way of—
  - (a) an allowance under this Act,
  - (b) a deduction in computing profits for the purposes of income tax or corporation tax,
  - (c) a deduction from total profits or total income for the purposes of either of those taxes.
- (10) This section is to be construed as one with section 70A.

#### **70D Long funding finance lease: additional expenditure: allowances for lessee**

- (1) This section applies where the following conditions are met—
  - (a) a person is the lessee of plant or machinery under a long funding finance lease,
  - (b) as a result of section 70A, the person falls to be regarded as having incurred qualifying expenditure on the provision of the plant or machinery, and
  - (c) the lessor incurs expenditure in relation to the plant or machinery,
  - (d) as a result of the lessor incurring the expenditure, there is in the case of the lessee an increase (the “relevant increase”) in the present value of the minimum lease payments.
- (2) If the lease is one which, under generally accepted accounting practice, falls (or would fall) to be treated as a loan, this section applies as if the lease were one which, under generally accepted accounting practice, fell to be treated as a finance lease.
- (3) The person is to be treated for the purposes of this Part as having incurred further capital expenditure on the provision of the plant or machinery as follows.
- (4) The person is to be treated as having incurred the expenditure on the date of first recognition.
- (5) The amount of the expenditure is the amount that would fall to be recognised as the amount of the relevant increase if appropriate accounts were prepared by the person.
- (6) For that purpose, “appropriate accounts” are accounts prepared in accordance with generally accepted accounting practice on the date of first recognition.
- (7) For the purposes of this section, the “date of first recognition” is the date on which the relevant increase is first recognised in the books or other financial records of the person.
- (8) This section is to be construed as one with section 70A.

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### **70E Disposal events and disposal values**

- (1) This section applies where—
  - (a) a person is the lessee of plant or machinery under a long funding lease,
  - (b) as a result of section 70A, the person falls to be regarded as having incurred qualifying expenditure on the provision of the plant or machinery, and
  - (c) the lease terminates.
- (2) In the case of that person—
  - (a) the termination of the lease is a disposal event, and
  - (b) the person is required to bring into account a disposal value for the chargeable period in which that disposal event occurs.
- (3) The amount of the disposal value varies according to whether the lease is—
  - (a) a long funding operating lease (see subsections (4) to (6)), or
  - (b) a long funding finance lease (see subsections (7) and (8)).
- (4) If the lease is a long funding operating lease, the disposal value is the sum of—
  - (a) element A (see subsection (5)), and
  - (b) element B (see subsection (6)).
- (5) Element A is the amount (if any) by which—
  - (a) the market value of the plant or machinery at the later of—
    - (i) the commencement of the term of the lease,
    - (ii) the date on which the plant or machinery is first brought into use for the purposes of the qualifying activity,exceeds
  - (b) the aggregate amount of the reductions that fell to be made under section 502K of ICTA or 148I of ITTOIA 2005 for periods of account in which the person was the lessee.
- (6) Element B is the sum of any amounts payable to the person which are calculated by reference to the termination value.
- (7) If, in the case of the person, the lease is a long funding finance lease, the amount of the disposal value is found by first finding the sum of—
  - (a) any amounts payable to the person which are calculated by reference to the termination value, and
  - (b) if the lease terminates before the end of the term, the amount that would fall to be recognised as the present value, immediately before the termination, of the balance of the minimum lease payments (see subsection (8)) if appropriate accounts were prepared by the person, and then reducing that sum (but not below nil) by subtracting from it any amount payable by the person to the lessor for or in consequence of the termination.
- (8) For the purposes of subsection (7)(b)—

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- (a) the balance of the minimum lease payments is the amount by which MLP exceeds TMLP, where—
    - MLP is the amount of the minimum lease payments, and
    - TMLP is the amount that would have been the minimum lease payments if the term of the lease had been such as to expire on the day of the termination, and
  - (b) “appropriate accounts” are accounts prepared in accordance with generally accepted accounting practice immediately before the termination of the lease.
- (9) If the termination of the lease gives rise to a disposal event in the case of the person apart from this section, that disposal event is to be ignored.
- (10) This section is to be construed as one with section 70A.”.

*Interpretation of provisions relating to long funding leases*

7 In Part 2, after Chapter 6 insert—

**“CHAPTER 6A**

INTERPRETATION OF PROVISIONS ABOUT LONG FUNDING LEASES

*Introductory*

**Introductory**

70F This Chapter makes provision for the interpretation of this Part so far as relating to long funding leases.

*Meaning of “long funding lease” etc*

**“Long funding lease”**

70G(1) A “long funding lease” is a funding lease (see section 70J) which meets the following conditions—

- (a) it is not a short lease (see section 70I),
  - (b) it is not an excluded lease of background plant or machinery for a building (see section 70R),
  - (c) it not excluded by section 70U (plant or machinery leased with land: low percentage value).
- (2) Where, at the commencement of the term of a plant or machinery lease, the plant or machinery—
- (a) is not being used for the purposes of a qualifying activity carried on by the person concerned, but
  - (b) subsequently begins to be used for the purposes of a qualifying activity carried on by that person,

the plant or machinery lease is a long funding lease if the condition in subsection (3) is met.

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- (3) The condition is that (apart from section 70H) the plant or machinery lease would have been a long funding lease at its inception had the plant or machinery been used at that time for the purposes of a qualifying activity carried on by the person concerned.
- (4) This section is subject, in the case of the lessee, to—
  - (a) section 70H (requirement for tax return treating lease as long funding lease);
  - (b) section 70Q (leases excluded by right of lessor etc to claim capital allowances).
- (5) See also paragraph 91A of Schedule 22 to the Finance Act 2000 (tonnage tax: certain leases to be treated as not being long funding leases).

**Lessee: requirement for tax return treating lease as long funding lease**

- 70H(1) A lease is not a long funding lease in the case of the lessee unless he makes a tax return for the initial period on the basis that he falls to be taxed in respect of the lease in accordance with the provisions of—
- (a) Chapter 5A of Part 12 of ICTA (long funding leases: corporation tax), or
  - (b) Chapter 10A of Part 2 of ITTOIA 2005 (long funding leases: income tax).
- (2) Where, in the case of a lease, a person has made a tax return for the initial period—
- (a) on the basis that he falls to be taxed in respect of the lease in accordance with those provisions, or
  - (b) on the basis that he does not fall to be so taxed,
- he may not make a claim for relief under the error or mistake provisions in respect of the tax return having been made on that basis.
- (3) In this section—
- “the error or mistake provisions” means—
- (a) section 33 of the Taxes Management Act 1970; or
  - (b) paragraph 51 of Schedule 18 to the Finance Act 1998;
- “the initial period” is the first accounting period or, as the case may be, tax year in which there is a difference in the amount of the profits or losses falling to be shown in the return, according to whether the lease is a long funding lease or not;
- “tax return” means—
- (a) a company tax return under paragraph 3 of Schedule 18 to the Finance Act 1998, or
  - (b) a return under section 8 of the Taxes Management Act 1970 (income tax: personal return).

**“Short lease”**

- 70I (1) Construe “short lease” in accordance with this section.
- (2) A lease whose term is 5 years or less is a short lease.



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- (3) Where the term of a lease is—
- (a) longer than 5 years, but
  - (b) not longer than 7 years,
- the lease is a short lease if Conditions A, B and C are met.
- (4) Condition A is that the lease is one which, under generally accepted accounting practice, falls (or would fall) to be treated as a finance lease.
- (5) Condition B is that—
- (a) the residual value of the plant or machinery which is implied in the terms of the lease,
- is not more than
- (b) 5% of the market value of the plant or machinery at the commencement of the term of the lease, as estimated at the inception of the lease.
- (6) Condition C is that under the terms of the lease—
- (a) the total rentals falling due in the first reference year, if less than the total rentals falling due in the second reference year, are no more than 10% less than those rentals, and
  - (b) the total rentals falling due in the final year or in any reference year after the second reference year, if greater than the total rentals falling due in the second reference year, are no more than 10% greater than those rentals.
- (7) For the purposes of Condition C—
- (a) the first reference year is the period of 12 months beginning with the day next after the commencement of the term of the lease;
  - (b) the other reference years are successive periods of 12 months each beginning on an anniversary of that day and ending before the last day of the term of the lease;
  - (c) the final year is the period of 12 months ending with the last day of the term of the lease;
  - (d) any part of the final year, other than the last day, may accordingly also be part of a reference year.
- (8) In determining whether Condition C is met, exclude any variation in the rentals that results from changes in a standard published base rate for interest.
- (9) Where—
- (a) a person leases an asset to another (“S”) under a lease that would, apart from this subsection, be a short lease,
  - (b) the inception of that lease is on or after 7th April 2006,
  - (c) at or about the time of the inception of that lease, arrangements are entered into for the asset to be leased to one or more other persons under one or more other leases, and
  - (d) in the aggregate, the term of the lease to S and the terms of the leases to such of those other persons as are connected with S exceed 5 years,
- the lease to S is not a short lease.

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**“Funding lease”**

- 70J (1) A “funding lease” is a plant or machinery lease (see section 70K) which at its inception meets one or more of the following tests—
- (a) the finance lease test (see section 70N),
  - (b) the lease payments test (see section 70O),
  - (c) the useful economic life test (see section 70P).
- (2) Subsection (1) is subject to the following provisions of this section.
- (3) A plant or machinery lease is not a funding lease if—
- (a) section 67 applies (plant or machinery treated as owned by person entitled to benefit of contract, etc), and
  - (b) the lease is the contract mentioned in that section.
- (4) A plant or machinery lease is not a funding lease if—
- (a) before the commencement of the term of the lease, the lessor has leased the plant or machinery under one or more other plant or machinery leases,
  - (b) in the aggregate, the terms of those other leases exceed 65% of the remaining useful economic life of the plant or machinery at the commencement of the term of the earliest of them, and
  - (c) none of those earlier leases was a funding lease.
- (5) For the purposes of subsection (4), all persons who were lessors of the plant or machinery before 1st April 2006 are to be treated as if they were the same person as the first lessor of the plant or machinery on or after that date.
- (6) A plant or machinery lease is not a funding lease in the case of the lessor if—
- (a) before 1st April 2006, the plant or machinery had, for a period or periods totalling at least 10 years, been the subject of one or more leases, and
  - (b) the lessor under the plant or machinery lease was also lessor of the plant or machinery on the last day before 1st April 2006 on which the plant or machinery was the subject of a lease.

*Meaning of “plant or machinery lease”*

**“Plant or machinery lease”**

- 70K(1) A “plant or machinery lease” is any of the following—
- (a) any agreement or arrangement to which subsection (2) applies,
  - (b) any other agreement or arrangement, to the extent that subsection (3) applies to it,
  - (c) where plant or machinery is the subject of a sale and finance leaseback, as defined in section 221, the finance lease mentioned in subsection (1)(c) of that section,
- and “lease”, “lessor”, “lessee” and other related expressions are to be construed accordingly.
- (2) This subsection applies to an agreement or arrangement—

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- (a) under which a person grants to another person the right to use plant or machinery for a period, and
  - (b) which, in accordance with generally accepted accounting practice, falls (or would fall) to be treated as a lease.
- (3) This subsection applies to an agreement or arrangement to the extent that—
- (a) in accordance with generally accepted accounting practice, it falls (or would fall) to be treated as a lease, and
  - (b) it meets the conditions in subsection (4).
- (4) The conditions are that, for the purposes of generally accepted accounting practice,—
- (a) the agreement or arrangement conveys, or falls (or would fall) to be regarded as conveying, the right to use an asset, and
  - (b) the asset is plant or machinery.
- (5) In the case of an agreement or arrangement that falls (or would fall) within subsection (2) or (3) immediately after the commencement of the term of the lease, the condition in subsection (2)(b) or (3)(a) (as the case may be) is to be taken to be met as respects any time in the pre-commencement period.
- (6) For the purposes of subsection (5), the “pre-commencement period” is the period that—
- (a) begins with the inception of the lease, and
  - (b) ends with the commencement of the term of the lease.

#### **Plant or machinery leased with other assets: separate derived leases**

- 70L (1) This section applies in any case where an agreement or arrangement (the “mixed lease”) at any time relates, or is to relate, or has come to relate, to both—
- (a) plant or machinery of any particular description (the “relevant plant or machinery”), and
  - (b) other assets (whether or not also plant or machinery).
- (2) A mixed lease is an “eligible mixed lease” if—
- (a) under generally accepted accounting practice, it falls (or would fall) to be treated as a lease, or
  - (b) the relevant plant or machinery is the subject of a sale and finance leaseback, as defined in section 221, and the mixed lease is or includes the finance lease mentioned in subsection (1)(c) of that section.
- (3) In the case of an agreement or arrangement that falls (or would fall) within paragraph (a) of subsection (2) immediately after the commencement of the term of the lease, the condition in that paragraph is to be taken to be met as respects any time in the pre-commencement period.
- (4) For the purposes of subsection (3), the “pre-commencement period” is the period that—
- (a) begins with the inception of the lease, and
  - (b) ends with the commencement of the term of the lease.

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- (5) Where this section applies—
  - (a) the eligible mixed lease, so far as relating to the relevant plant or machinery, and
  - (b) the eligible mixed lease, so far as relating to other assets,
shall be treated for the purposes of this Part (other than this section) as if they were separate agreements or arrangements.
- (6) Any such notional separate agreement or arrangement is referred to in this Part as a “derived lease”.
- (7) Section 70M makes further provision with respect to derived leases of plant or machinery.

**Derived leases of plant or machinery: term and rentals**

- 70M(1) This section has effect in any case where, as a result of applying section 70L, there is a derived lease of the relevant plant or machinery.
- (2) This section makes provision with respect to—
    - (a) determining whether the derived lease is a plant or machinery lease (see subsection (3)),
    - (b) the term of the derived lease (see subsection (4)),
    - (c) the rentals to be regarded as payable under the derived lease (see subsections (5) to (7)).
  - (3) Any question whether the derived lease—
    - (a) is a plant or machinery lease, or
    - (b) if it is such a lease, whether it is also a long funding lease,
is to be determined in accordance with the provisions of this Part.
  - (4) The term of the derived lease—
    - (a) is limited to the remaining useful economic life of the relevant plant or machinery at the commencement of the term of the derived lease, but
    - (b) subject to that, is to be determined in accordance with section 70YF (the “term” of a lease).
  - (5) The rentals that are to be regarded as payable under the derived lease shall be such rentals (the “deemed rentals”) as are just and reasonable in all the circumstances of the case.
  - (6) It shall be assumed that rentals under the derived lease are payable in equal instalments throughout the term of the lease, unless it is reasonable to draw a different conclusion from all the circumstances of the case.
  - (7) In determining the amount of any deemed rentals, regard shall be had to—
    - (a) all the provisions of the eligible mixed lease,
    - (b) the nature of the relevant plant or machinery,
    - (c) the value of the relevant plant or machinery at the commencement of the term of the derived lease,

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- (d) the amount which, at the commencement of the term of the derived lease, is expected to be the market value of the relevant plant or machinery at the end of the term of the derived lease,
  - (e) the remaining useful economic life of the relevant plant or machinery at the commencement of the term of the derived lease;
  - (f) the term of the derived lease.
- (8) Expressions used in section 70L have the same meaning in this section.

*The tests for being a funding lease*

**The finance lease test**

- 70N(1) A lease meets the finance lease test in the case of any person if the lease is one which, under generally accepted accounting practice, falls (or would fall) to be treated as a finance lease or a loan in the accounts—
- (a) of that person, or
  - (b) where that person is the lessor, of any person connected with him.
- (2) In this section “accounts”, in relation to a company, includes any accounts which—
- (a) relate to two or more companies of which that company is one, and
  - (b) are drawn up in accordance with generally accepted accounting practice.
- (3) Where for any period—
- (a) a person is not within the charge to income tax or corporation tax by reason of not being resident in the United Kingdom, and
  - (b) accounts are not prepared in accordance with international accounting standards or UK generally accepted accounting practice,
- any question relating to generally accepted accounting practice is to be determined for the purposes of this section by reference to generally accepted accounting practice with respect to accounts prepared in accordance with international accounting standards.

**The lease payments test**

- 70O(1) A lease meets the lease payments test if—
- (a) the present value of the minimum lease payments (see section 70YE),  
is equal to
  - (b) 80% or more of the fair value of the leased plant or machinery.
- (2) The present value of the minimum lease payments is to be calculated by using the interest rate implicit in the lease.
- (3) In this section “fair value” means—
- (a) the market value of the leased plant or machinery,  
less
  - (b) any grants receivable towards the purchase or use of that plant or machinery.

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- (4) For the purposes of this section—
- (a) the interest rate implicit in the lease is the interest rate that would apply in accordance with normal commercial criteria, including, in particular, generally accepted accounting practice (where applicable), but
  - (b) if the interest rate implicit in the lease cannot be determined in accordance with paragraph (a), it is the temporal discount rate for the purposes of section 70 of the Finance Act 2005 (companies: film relief: valuation of “rights to guaranteed income” and “disposed rights”).

### **The useful economic life test**

70P A lease meets the useful economic life test if the term of the lease is more than 65% of the remaining useful economic life of the leased plant or machinery.

*Leases excluded by right of lessor etc to claim capital allowances*

### **Leases excluded by right of lessor etc to claim capital allowances**

- 70Q(1) A lease is not a long funding lease in the case of the lessee if it is excluded by virtue of subsection (2) (but see also subsection (5)).
- (2) A lease is excluded if the lessor, or any superior lessor (see subsections (7) to (9)),—
    - (a) is entitled, at the commencement of the term of the lease, to claim a relevant allowance (see subsection (6)),
    - (b) would have been so entitled at that time, but for section 70V (tax avoidance involving international leasing),
    - (c) has at any earlier time been entitled to claim such an allowance, but has not been required to bring a disposal value into account in accordance with section 61(1)(ee), or
    - (d) would fall within any one or more of paragraphs (a) to (c), if he had been within the charge to income tax or corporation tax at the inception of the lease and any earlier times.
  - (3) Where for any period the lessor, or any superior lessor, is a person—
    - (a) who is not within the charge to income tax or corporation tax by reason of not being resident in the United Kingdom, and
    - (b) who does not prepare accounts in accordance with international accounting standards or UK generally accepted accounting practice, subsection (4) applies.
  - (4) In determining whether the condition in subsection (2)(d) is met in any such case, any question relating to generally accepted accounting practice in relation to that person and that period is to be determined by reference to generally accepted accounting practice with respect to accounts prepared in accordance with international accounting standards.
  - (5) A lease is not excluded by virtue of subsection (2) if—

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- (a) the inception of the lease is before 28th June 2006, and
  - (b) by virtue only of section 70J(6), the lease is not a funding lease in the case of the lessor.
- (6) A “relevant allowance” is an allowance under this Act in respect of the leased plant or machinery.
- (7) There is a “superior lessor” only if the leased plant or machinery is the subject of a chain of superior leases.
- (8) Leased plant or machinery is the subject of a chain of superior leases if—
- (a) the lessor has his interest in relation to the plant or machinery under or by virtue of a lease from a third person (P), or
  - (b) the circumstances are as in paragraph (a), but P has his interest in relation to the plant or machinery under or by virtue of a lease from a fourth person (Q), or
  - (c) the circumstances are as in paragraph (b), but Q has his interest in relation to the plant or machinery under or by virtue of a lease from a fifth person (R),
- and so on, where there is more than a fifth person involved.
- (9) Where any leased plant or machinery is the subject of a chain of superior leases, the superior lessors are the persons described in subsection (8) as P, Q, R, and so on.
- (10) Subsections (6) to (9) have effect for the interpretation of this section.

*Excluded leases of background plant or machinery for a building*

**Excluded leases of background plant or machinery for a building**

- 70R (1) Construe references to an excluded lease of background plant or machinery for a building in accordance with this section.
- (2) This section applies where—
- (a) plant or machinery is affixed to, or otherwise installed in or on, any land which consists of or includes a building,
  - (b) the plant or machinery is background plant or machinery for the building (see subsections (4) and (5)),
  - (c) the plant or machinery is leased with the land under a mixed lease, and
  - (d) none of the disqualifications set out in section 70S applies.
- (3) In any such case, the derived lease of the plant or machinery is an excluded lease of background plant or machinery for a building.
- (4) The background plant or machinery for a building is any plant or machinery—
- (a) which is of such a description that plant or machinery of that description might reasonably be expected to be installed in, or in or on the sites of, a variety of buildings of different descriptions, and

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- (b) whose sole or main purpose is to contribute to the functionality of the building or its site as an environment within which activities can be carried on.
- (5) Subsection (4) has effect subject to the provisions of any order under section 70T.

### **The disqualifications**

70S (1) This section sets out the disqualifications mentioned in subsection (2)(d) of section 70R and is to be construed as one with that section.

- (2) Disqualification A is that the amounts payable—
  - (a) under the mixed lease, or
  - (b) under any other arrangement,

vary, or may be varied, by reference to the value from time to time to the lessor of allowances under this Act in respect of expenditure incurred by him in the provision of the background plant or machinery for the building.

- (3) Disqualification B is that the main purpose, or one of the main purposes, of entering into—
  - (a) the mixed lease,
  - (b) a series of transactions of which the mixed lease is one, or
  - (c) any of the transactions in such a series,

is to secure that allowances under this Act are available to the lessor in respect of expenditure incurred in the provision of background plant or machinery for a building.

### **Orders relating to background plant or machinery for a building**

70T (1) This section supplements section 70R and is to be construed as one with it.

- (2) The Treasury may by order prescribe—
  - (a) descriptions of plant or machinery to be used as examples of the kinds of plant or machinery that may be regarded as falling within the definition of background plant or machinery for a building in determining whether any particular plant or machinery does or does not fall within that definition;
  - (b) descriptions of plant or machinery to be deemed to be background plant or machinery for a building;
  - (c) descriptions of plant or machinery to be deemed not to be background plant or machinery for a building.
- (3) An order under this section—
  - (a) may make different provision for different cases (including different descriptions of building),
  - (b) may contain incidental, consequential, supplemental, or transitional provision or savings.

- (4) The first order made under this section may include provisions having effect in relation to times before the making of the order (but not times earlier than 1st April 2006).



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*Exclusion for certain plant or machinery leased with land*

**Plant or machinery leased with land: low percentage value**

70U(1) This section applies where—

- (a) any plant or machinery (the “relevant plant or machinery”) is affixed to, or otherwise installed, in or on any land,
  - (b) the plant or machinery is not background plant or machinery for any building situated in or on the land,
  - (c) the plant or machinery is leased with the land under a mixed lease, and
  - (d) none of the relevant disqualifications applies.
- (2) For the purposes of this section the “relevant disqualifications” are the disqualifications set out in section 70S, but for this purpose—
- (a) take the reference in subsection (1) of that section to subsection (2) (d) of section 70R as a reference to this subsection (and, accordingly, construe the second reference to that section as a reference to this section), and
  - (b) take references in section 70S to background plant or machinery for a building as references to relevant plant or machinery.
- (3) Where this section applies, the derived lease of the relevant plant or machinery is excluded by this section if the condition in subsection (4) is met at the commencement of the term of that lease.
- (4) The condition is that AMV does not exceed both—
- (a) 10% of BMV; and
  - (b) 5% of LMV.
- (5) For that purpose—
- AMV is the aggregate of—
- (a) the market value of the relevant plant or machinery, and
  - (b) the market value of any other plant or machinery that falls within subsection (1) in the case of the leased land;
- BMV is the aggregate market value of all the background plant or machinery leased with the land;
- LMV is the market value of the land (including buildings and fixtures).
- (6) For this purpose the market value of any land at any time is to be determined on the assumption of a sale by an absolute owner of the land free from all leases and other encumbrances.

*Avoidance*

**Tax avoidance involving international leasing**

70V(1) This section applies where matters are so arranged that there are plant or machinery leases such that—

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- (a) under a lease by a non-resident, an asset is provided directly or indirectly to a resident,
  - (b) the direct provision of the asset to the resident is by a lease which, in the case of the resident, is a long funding lease or a lease to which section 67 (hire purchase etc) applies,
  - (c) the asset is used by the resident for the purpose of leasing it under a lease (the “relevant lease”) that would not (apart from this section) be a long funding lease in the case of the resident, and
  - (d) under the relevant lease, the asset is provided directly or indirectly (but by a lease) to a non-resident.
- (2) Subsection (3) applies if the sole or main purpose of arranging matters in that way is to obtain a tax advantage by securing that allowances under this Part are available to a resident by virtue of—
- (a) section 67 (hire purchase), or
  - (b) section 70A (long funding leases).
- (3) In any such case, the relevant lease is deemed to be a long funding lease in the case of the resident who is the lessor under it.
- (4) The reference in this section to a person obtaining a tax advantage (see section 577(4)) also includes a reference to a person obtaining a tax advantage within the meaning of Chapter 1 of Part 17 of ICTA (see section 709 of that Act).
- (5) In this section—
- “non-resident” means a person who—
    - (a) is not resident in the United Kingdom, and
    - (b) does not use the plant or machinery exclusively for earning profits chargeable to tax;
  - “resident” means a person who—
    - (a) is resident in the United Kingdom, or
    - (b) uses the plant or machinery exclusively for earning profits chargeable to tax.

*Transfers, assignments, novations, leaseback, variations etc*

### **Transfers, assignments etc by lessor**

- 70W(1) This section applies in any case where the following conditions are met—
- (a) a person (the “old lessor”) is lessor of plant or machinery under a plant or machinery lease (the “old lease”),
  - (b) during the term of the lease, the old lessor transfers the plant or machinery to another person (the “new lessor”),
  - (c) the transfer is not the grant of a plant or machinery lease by the old lessor,
  - (d) immediately after the transfer, the new lessor is the lessor of the plant or machinery under a lease (“the new lease”) (whether or not the same lease as the old lease).
- (2) If it is not otherwise the case,—

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- (a) the old lessor is to be treated as if the old lease terminated immediately before the transfer, and
  - (b) the new lessor is to be treated as if the new lease had been entered into immediately after the transfer.
- (3) The new lessor is also to be treated as if the date of the transfer were the date of both—
  - (a) the inception of the new lease, and
  - (b) the commencement of the term of the new lease,if it is not otherwise the case.
- (4) If, immediately before the transfer, the old lease was (or was treated by virtue of this subsection as being) in the case of the old lessor a lease of either of the following descriptions—
  - (a) a long funding lease, or
  - (b) a lease which is not a long funding lease,the new lease is to be treated in the case of the new lessor as being a lease of the same description, if the conditions in subsection (5) are met.
- (5) The conditions are that—
  - (a) the term of the new lease is the unexpired portion of the term of the old lease, and
  - (b) the amounts receivable under the new lease are the same as would have been receivable under the old lease, assuming it to have continued in effect.
- (6) If—
  - (a) it is not otherwise the case, and
  - (b) the conditions in subsection (5) are met,the lessee is to be treated as if the old lease and the new lease were the same continuing lease.
- (7) Any reference in this section to a transfer of plant or machinery by a person includes a reference to—
  - (a) any kind of disposal of, or of the person's interest in, the plant or machinery,
  - (b) any arrangements under which the person's interest in the plant or machinery is terminated and another person becomes lessor of the plant or machinery,
  - (c) in a case where the plant or machinery is a fixture and the person is treated under section 176 as the owner, any cessation of ownership under section 188, 190, 191, 192 or 192A.

### **Transfers, assignments etc by lessee**

- 70X(1) This section applies in any case where the following conditions are met—
- (a) a person (the “old lessee”) is lessee of plant or machinery under a plant or machinery lease (the “old lease”),
  - (b) during the term of the lease, the old lessee transfers the plant or machinery to another person (the “new lessee”),

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- (c) the transfer is not the grant of a plant or machinery lease by the old lessee,
  - (d) immediately after the transfer, the new lessee is the lessee of the plant or machinery under a lease (“the new lease”) (whether or not the same lease as the old lease).
- (2) If it is not otherwise the case,—
  - (a) the old lessee is to be treated as if the old lease terminated immediately before the transfer, and
  - (b) the new lessee is to be treated as if the new lease had been entered into immediately after the transfer.
- (3) The new lessee is also to be treated as if the date of the transfer were the date of both—
  - (a) the inception of the new lease, and
  - (b) the commencement of the term of the new lease,if it is not otherwise the case.
- (4) If, immediately before the transfer, the old lease was (or was treated by virtue of this subsection as being) in the case of the old lessee a lease of one of the following descriptions—
  - (a) a long funding lease, or
  - (b) a lease which is not a long funding lease,the new lease is to be treated in the case of the new lessee as being a lease of the same description, if the conditions in subsection (5) are met.
- (5) The conditions are that—
  - (a) the term of the new lease is the unexpired portion of the term of the old lease, and
  - (b) the amounts payable under the new lease are the same as would have been payable under the old lease, assuming it to have continued in effect.
- (6) If—
  - (a) it is not otherwise the case, and
  - (b) the conditions in subsection (5) are met,the lessor is to be treated as if the old lease and the new lease were the same continuing lease.
- (7) Any reference in this section to a transfer of plant or machinery by a person includes a reference to—
  - (a) any kind of disposal of, or of the person's interest in, the plant or machinery,
  - (b) any arrangements under which the person's interest in the plant or machinery is terminated and another person becomes lessee of the plant or machinery,
  - (c) in a case where the plant or machinery is a fixture and the person is treated under section 176 as the owner, any cessation of ownership under section 188, 190, 191, 192 or 192A.

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### **Sale and leaseback, lease and leaseback etc: lessors**

70Y(1) Where—

- (a) a person (B) transfers plant or machinery to another person (A),
  - (b) the plant or machinery is directly or indirectly leased back to B, and
  - (c) immediately before the commencement of the term of the lease back to B, B is the lessor of the plant or machinery to another person under a lease which is, in B's case, a long funding lease,
- the lease back to B is, in the case of both A and B, a long funding lease.
- (2) If, in any such case, the plant or machinery is leased back from A to B indirectly, any leases by means of which the indirect lease back from A to B is effected are also long funding leases in the case of each of the parties to them.
  - (3) Any reference in this section to a transfer of plant or machinery by a person includes a reference to—
    - (a) any kind of disposal of, or of the person's interest in, the plant or machinery (including the grant of a lease),
    - (b) any arrangements under which the person's interest in the plant or machinery is terminated and another person becomes entitled to, or to an interest in, the plant or machinery,
    - (c) in a case where the plant or machinery is a fixture and the person is treated under section 176 as the owner, any cessation of ownership under section 188, 190, 191, 192 or 192A.

### **Change in accountancy classification of long funding lease**

70YA(1) This section applies in any case where—

- (a) a person is lessor or lessee under a long funding lease, and
  - (b) at any time after the inception of the lease, the accountancy classification of the lease as a finance lease or an operating lease changes in the relevant accounts.
- (2) The person is to be treated as if—
    - (a) the lease had terminated immediately before the time of the change,
    - (b) another lease (the “new lease”) had been entered into immediately after the time of the change, and
    - (c) the new lease were a long funding lease in the case of the lessor.
  - (3) The person is also to be treated as if the date on which the change occurs were the date of both—
    - (a) the inception of the new lease, and
    - (b) the commencement of the term of the new lease.
  - (4) The cases where the accountancy classification of a long funding lease as a finance lease or an operating lease changes at any time (the “relevant time”) in the relevant accounts are those set out in subsections (5) and (6).
  - (5) Case 1 is where—

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- (a) immediately before the relevant time, the lease is one that falls (or would fall) to be treated in the relevant accounts in accordance with generally accepted accounting practice as a finance lease for accounting purposes, and
  - (b) at the relevant time the lease becomes one that falls (or would fall) to be treated in the relevant accounts in accordance with generally accepted accounting practice as not being a finance lease for accounting purposes.
- (6) Case 2 is where—
- (a) immediately before the relevant time, the lease is one that falls (or would fall) to be treated in the relevant accounts in accordance with generally accepted accounting practice as not being a finance lease for accounting purposes, and
  - (b) at the relevant time the lease becomes one that falls (or would fall) to be treated in the relevant accounts in accordance with generally accepted accounting practice as a finance lease for accounting purposes.
- (7) The Treasury may by regulations make provision for or in connection with restricting the application or operation of this section.
- (8) In this section, any reference to a finance lease includes a reference to a loan.
- (9) In the application of this section in relation to any person, the “relevant accounts” are the accounts—
- (a) of that person, or
  - (b) where that person is the lessor, of any person connected with that person,
- but only to the extent that the treatment of the lease in those accounts as a finance lease or otherwise falls (or would fall) to be determined by reference to that person as the lessor or lessee under the lease.
- (10) Subsections (2) and (3) of section 70N (finance lease test: group accounts, and generally accepted accounting practice for persons outside the charge to tax) also apply for the purposes of this section.

**Long funding operating lease: extension of term of lease**

- 70YB(1) This section applies in any case where—
- (a) a person is lessor or lessee under a long funding operating lease (the “existing lease”),
  - (b) an event occurs which has the effect of extending the term of the lease (whether by variation of the provisions of the lease, the grant or exercise of an option or in any other way), and
  - (c) the event is not one by reason of which, within the meaning of section 70YA, the accountancy classification of the lease as an operating lease changes in the relevant accounts.
- (2) For this purpose an event has the effect of extending the term of the lease if it meets any of the following conditions—
- (a) it has the effect of making a further period a non-cancellable period;

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- (b) it is the grant of an option to the lessee to continue to lease the plant or machinery for a further period, where it is reasonably certain at the time the option is granted that the lessee will exercise it;
- (c) it is the exercise by the lessee of an option to continue to lease the plant or machinery for a further period;
- (d) it does not fall within the preceding paragraphs, but it has the effect that the lessee will continue, or is reasonably certain to continue, to lease the plant or machinery for a further period.

For this purpose “further period” means a period falling wholly or partly after the end of the pre-existing term.

- (3) The person is to be treated as if—
  - (a) the existing lease terminated at the end of the day before the effective date,
  - (b) another lease (the “new lease”) were entered into on the effective date, and
  - (c) the term of the new lease were the unexpired portion of the term of the existing lease, as extended.
- (4) The person is also to be treated as if the effective date were the date of both—
  - (a) the inception of the new lease, and
  - (b) the commencement of the term of the new lease.
- (5) The new lease is to be taken to be a long funding operating lease.
- (6) For the purposes of this section the “effective date” is the earlier of—
  - (a) the day after the end of the pre-existing term of the existing lease;
  - (b) if the rentals payable are varied as a result of or otherwise in connection with the event, the date on which the variation takes effect.
- (7) In this section—
  - “non-cancellable period” has the same meaning as in section 70YF (the “term” of a lease);
  - “pre-existing term”, in relation to a lease, means the term of the lease apart from the extension in question.

### **Extension of term of lease that is not a long funding lease**

- 70YQ1) This section applies where—
- (a) a person is lessor under a plant or machinery lease (the “existing lease”) that is not a long funding lease, and
  - (b) an event occurs which has the effect of extending the term of the lease (whether by variation of the provisions of the lease, the grant or exercise of an option or in any other way).
- (2) Subsection (2) of section 70YB (events having the effect of extending the term of a lease) also has effect for the purposes of this section.
  - (3) Make the following assumptions—
    - (a) the existing lease terminates immediately before the effective date,
    - (b) another lease (the “new lease”) is entered into on the effective date,

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- (c) the term of the new lease is the portion of the term of the existing lease, as extended, that remains unexpired as at the effective date;
  - (d) the effective date is the date of both—
    - (i) the inception of the new lease, and
    - (ii) the commencement of the term of the new lease.
- (4) If, on those assumptions, the new lease would be a long funding lease, the person is to be treated on those assumptions.
- (5) If subsection (4) does not apply, then, for the purposes of any subsequent application of this section or section 70YD in the case of the existing lease, the term of the existing lease is to be taken to be the term as extended (or further extended).
- (6) For the purposes of this section the “effective date” is the earlier of—
- (a) the day after the end of the pre-existing term of the existing lease;
  - (b) if the rentals payable are varied as a result of or otherwise in connection with the event, the date on which the variation takes effect.
- (7) In this section “pre-existing term”, in relation to a lease, means the term of the lease apart from the extension in question.

#### **Increase in proportion of residual amount guaranteed: review of status**

70YD(1) This section applies where—

- (a) a person is lessor under a lease (the “existing lease”) that is not a long funding lease,
  - (b) the person enters into an arrangement which meets, or arrangements which (taken together) meet, the conditions in subsection (2).
- (2) The conditions are that—
- (a) as a result of the arrangement or arrangements, there is an increase, after the inception of the lease, in the proportion of the residual amount that is guaranteed as mentioned in section 70YE(1)(b), and
  - (b) had the arrangement or arrangements been entered into before the inception of the lease, the lease would have been a long funding lease.
- (3) The person is to be treated as if—
- (a) the existing lease had terminated immediately before the time of the relevant transaction,
  - (b) another lease (the “new lease”) had been entered into immediately after the time of the relevant transaction,
  - (c) the term of the new lease were the portion of the term of the existing lease that remains unexpired as at the date of the relevant transaction;
  - (d) the date of the relevant transaction were the date of both—
    - (i) the inception of the new lease, and
    - (ii) the commencement of the term of the new lease.



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- (4) For the purposes of this section, the “relevant transaction” is the arrangement or, where two or more arrangements have been entered into, the latest of them.
- (5) The Treasury may by regulations make provision for or in connection with restricting the application or operation of this section.

### *Interpretation*

#### **“Minimum lease payments”**

70Y(F) In the case of any lease, the minimum lease payments are the minimum payments under the lease over the term of the lease (including any initial payment) together with—

- (a) in the case of the lessee, so much of any residual amount as is guaranteed by him or a person connected with him, or
- (b) in the case of the lessor, so much of any residual amount as is guaranteed by the lessee or a person who is not connected with the lessor.
- (2) In determining the minimum payments, exclude so much of any payment as represents—
- (a) charges for services, or
- (b) qualifying UK or foreign tax to be paid by the lessor.

(3) In this section—

“qualifying UK or foreign tax” means any tax or duty chargeable under the law of any part of the United Kingdom, or under the law of any foreign country, other than—

- (a) income tax,
- (b) corporation tax,
- (c) any tax chargeable under the law of a foreign country which is similar to income tax or corporation tax,

and here “foreign country” means any territory outside the United Kingdom;

“residual amount” means so much of the fair value of the plant or machinery subject to the lease as cannot reasonably be expected to be recovered by the lessor from the payments under the lease.

- (4) In the definition of “residual amount” in subsection (3), “fair value” means—
- (a) the market value of the leased plant or machinery,
- less
- (b) any grants receivable towards the purchase or use of that plant or machinery.

#### **The “term” of a lease**

70Y(F) The term of a lease is the period comprising—

- (a) so much of the post-commencement period as is a non-cancellable period, and

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- (b) any subsequent periods which meet the conditions in subsection (2).
- (2) The conditions are that—
- (a) the lessee has an option to continue to lease the asset for the period (whether with or without further payment), and
  - (b) it is reasonably certain, at the inception of the lease, that the lessee will exercise that option.
- (3) The “post-commencement period” is so much of the period of the lease as begins with the commencement of the term of the lease.
- (4) A “non-cancellable period” is any period during which the lessee may terminate the lease only—
- (a) upon the occurrence of some remote contingency, or
  - (b) upon payment by the lessee of such an additional amount that, at the inception of the lease, continuation of the lease is reasonably certain.
- (5) If, at the commencement of the term of the lease,—
- (a) the market value of the asset exceeds £1 million, and
  - (b) the estimated market value of the asset 5 years after the commencement of the term of the lease is more than half of the market value of the asset at the commencement of the term of the lease,
- subsection (6) applies.
- (6) If, in any such case, the term of the lease (apart from this subsection) would be 5 years or less, but—
- (a) the lessee has one or more options to continue to lease the asset,
  - (b) on the assumption that it is reasonably certain, at the inception of the lease, that the lessee will exercise those options, the term of the lease would exceed 7 years, and
  - (c) on failing to exercise any one of those options, the lessee may be required to make a payment to the lessor,
- it is to be assumed for the purposes of this section that any option to continue to lease the asset will be exercised, unless it is reasonably certain, at the inception of the lease, that the option will not be exercised.
- (7) Subsection (6) does not apply if, leaving out of account any options that would, by virtue of that subsection, result in the term of the lease exceeding 7 years, Conditions A, B and C in section 70I (meaning of “short lease”) are met.
- (8) See also section 70YC(5) (extension, for certain purposes, of term of lease that is not a long funding lease).

#### **“Termination amount”**

70YG(1) This section applies where plant or machinery is or has been, or is to be, leased under a long funding lease.

- (2) Construe “termination amount”, in the case of a long funding lease, in accordance with the following provisions of this section.
- (3) If—

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- (a) the lease terminates as a result of a plant or machinery disposal event, or
  - (b) a plant or machinery disposal event occurs as a result of, or otherwise in connection with, the termination of the lease,
- the termination amount is the disposal value that would have fallen to be brought into account by the lessor by reason of the plant or machinery disposal event on the assumptions in subsection (4).
- (4) Those assumptions are—
- (a) that section 34A (which prevents the lessor's expenditure for long funding leasing from being qualifying expenditure) did not apply in the case of the lessor, and
  - (b) that the lessor had claimed all the capital allowances that would in consequence have been available to him.
- (5) If—
- (a) subsection (3) does not apply, and
  - (b) the lease is a long funding finance lease,
- the termination amount is the value at which, immediately after the termination of the lease, the plant or machinery is recognised in the books or other financial records of the lessor.
- (6) If—
- (a) subsection (3) does not apply, and
  - (b) the lease is a long funding operating lease,
- the termination amount is the market value of the plant or machinery immediately after the termination of the lease.
- (7) For the purposes of this section a “plant or machinery disposal event” is an event that would have been a disposal event in relation to the plant or machinery in the case of the lessor on the assumptions in subsection (4).

### **“Termination value”**

- 70YH) This section applies where plant or machinery is or has been, or is to be, leased under a long funding lease.
- (2) Construe “termination value” in accordance with the following provisions of this section.
  - (3) The general rule is that the termination value of any plant or machinery is the value of the plant or machinery at or about the time when the lease terminates.
  - (4) Any reference to calculation by reference to the termination value includes a reference to calculation by reference to any one or more of—
    - (a) the proceeds of sale, if the plant or machinery is sold after the lease comes to an end,
    - (b) any insurance proceeds, compensation or similar sums in respect of the plant or machinery,
    - (c) an estimate of the market value of the plant or machinery.

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- (5) Any reference to calculation by reference to the termination value also includes a reference to—
- (a) determination in a way which, or by reference to factors or criteria which, might reasonably be expected to produce a broadly similar result to calculation by reference to the termination value, or
  - (b) any other form of calculation indirectly by reference to the termination value.

### General definitions

70Y(1) Construe these expressions as follows—

“absolute owner”, in the application of this Chapter in relation to Scotland, means the owner;

“arrangement” includes any transaction or series of transactions;

“background plant or machinery for a building” is to be construed in accordance with sections 70R to 70T;

“building” includes a reference to—

- (a) a structure,
- (b) part of a building or structure;

“commencement”, in relation to the term of a lease, means the date on and after which the lessee is entitled to exercise his right to use the complete leased asset under the lease;

for this purpose an asset is to be regarded as complete if its construction is substantially complete;

“derived lease” is to be construed in accordance with section 70L;

“the finance lease test” means the finance lease test in section 70N;

“fixture”—

- (a) means any plant or machinery that is so installed or otherwise fixed in or to a building or other description of land as to become, in law, part of that building or other land, and
- (b) includes any boiler or water-filled radiator installed in a building as part of a space or water heating system;

“funding lease” has the meaning given by section 70J;

“inception”, in relation to a plant or machinery lease, means the earliest date on which the following conditions are met—

- (a) there is a contract in writing for the lease between the lessor and the lessee,
- (b) either—
  - (i) the contract is unconditional, or
  - (ii) if it is conditional, the conditions have been met,
- (c) no terms remain to be agreed;

“initial payment”, in the case of a plant or machinery lease, means a payment by the lessee—

- (a) at or before the time when the lease is entered into, and
- (b) in respect of the plant or machinery which is the subject of the lease;

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“lease” includes any agreement or arrangement which is or includes a plant or machinery lease (and “lessor”, “lessee” and other related expressions are to be construed accordingly);

“lease”, in relation to land, includes—

- (a) an underlease, sublease or any tenancy,
- (b) in England and Wales or Northern Ireland, an agreement for a lease, underlease, sublease, or tenancy,
- (c) in Scotland, an agreement (including missives of let not constituting a lease) under which a lease, sublease or tenancy is to be executed,
- (d) in the case of land situated outside the United Kingdom, any interest corresponding to a lease as so defined,

and “lessor”, “lessee” and other related expressions are to be construed accordingly;

“lease”, in relation to plant or machinery, includes a sublease (and “lessor”, “lessee” and other related expressions are to be construed accordingly);

“lessee”, in relation to a lease, includes any person entitled to the lessee's interest under the lease;

“lessor”, in relation to a lease, includes any person entitled to the lessor's interest under the lease;

“long funding lease” has the meaning given by section 70G;

“long funding finance lease” means a long funding lease that meets the finance lease test by virtue of section 70N(1)(a);

“long funding operating lease” means a long funding lease which is not a long funding finance lease;

“market value”, in relation to plant or machinery, is to be construed in accordance with subsection (2);

“minimum lease payments” has the meaning given by section 70YE;

“mixed lease” is to be construed in accordance with section 70L;

“plant or machinery lease” has the meaning given by section 70K (and see also sections 70L and 70M);

“remaining useful economic life”, in the case of any leased plant or machinery, is the period—

- (a) beginning with the commencement of the term of the lease, and
- (b) ending when the asset is no longer used, and no longer likely to be used, by any person for any purpose as a fixed asset of a business;

“short lease” is to be construed in accordance with section 70I;

“the term”, in relation to a lease, is to be construed in accordance with section 70YF (but see also section 70YC(5) (extension, for certain purposes, of term of lease that is not a long funding lease));

“termination”, in relation to a lease,—

- (a) means the coming to an end of the lease, whether by effluxion of time or in any other way, and
- (b) includes in particular the bringing to an end of the lease by any person or by operation of law,

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and related expressions are to be construed accordingly;  
“termination amount” is to be construed in accordance with section 70YG;  
“termination value” is to be construed in accordance with section 70YH.

- (2) The market value of any plant or machinery at any time is to be determined on the assumption of a disposal by an absolute owner free from all leases and other encumbrances.
- (3) In relation to a lease, any reference to plant or machinery includes a reference to fixtures.
- (4) Section 839 of ICTA (connected persons) applies.
- (5) Any necessary apportionments under or by virtue of this Chapter are to be made on a just and reasonable basis.

**Power to vary the meaning of certain expressions**

- 70Y(J) The Treasury may by regulations make provision amending this Chapter so as to vary—
- (a) the meaning of “plant or machinery lease”, or
  - (b) the finance lease test.
- (2) A statutory instrument containing regulations under this section is not to be made unless a draft of the instrument has been laid before, and approved by a resolution of, the House of Commons.”.

*Cases in which short-life asset treatment is ruled out*

- 8 (1) The Table in section 84 is amended as follows.
- (2) In paragraph 1 after sub-paragraph (a) insert—

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“(aa)	section 13A (use for other purposes of plant or machinery provided for long funding leasing), or	”
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*Fixtures*

- 9 (1) In section 172 (scope of Chapter 14 of Part 2 (fixtures)) after subsection (2) insert—
- “(2A) Subsections (1) and (2) are subject to section 172A.”.
- (2) After section 172 insert—

**“172A Long funding leases etc: cases where this Chapter does not apply.**

- (1) This section applies where plant or machinery that is or becomes a fixture is the subject of a long funding lease (see Chapter 6A).
- (2) This section also applies if, in any such case,—

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- (a) the lessee under the long funding lease is or becomes the lessor of some or all of the plant or machinery under a further lease, and
  - (b) the further lease is not itself a long funding lease within subsection (1).
- (3) This Chapter does not apply to determine the entitlement of the lessor or the lessee (under either lease) to allowances under this Part in respect of expenditure on the plant or machinery.
- (4) This Chapter does not apply to determine whether the lessor or the lessee (under either lease) is to be treated as the owner of the plant or machinery.”.

## PART 2

### CORPORATION TAX

#### *Introductory*

<sup>F1</sup>10 .....

#### **Textual Amendments**

- F1** Sch. 8 paras. 10, 11 repealed (1.4.2010) by [Corporation Tax Act 2010 \(c. 4\)](#), s. 1184(1), **Sch. 3 Pt. 1** (with [Sch. 2](#))

#### *Special rules for long funding leases*

<sup>F1</sup>11 .....

#### **Textual Amendments**

- F1** Sch. 8 paras. 10, 11 repealed (1.4.2010) by [Corporation Tax Act 2010 \(c. 4\)](#), s. 1184(1), **Sch. 3 Pt. 1** (with [Sch. 2](#))

## PART 3

### INCOME TAX

#### *Introductory*

12 ITTOIA 2005 is amended as follows.

#### *Special rules for long funding leases*

13 In Part 2 (trading income) after Chapter 10 insert the following Chapter—

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for the Finance Act 2006, SCHEDULE 8. (See end of Document for details)*

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## “CHAPTER 10A

### LEASES OF PLANT OR MACHINERY: SPECIAL RULES FOR LONG FUNDING LEASES

#### *Lessors under long funding finance leases*

#### **Lessor under long funding finance lease: rental earnings**

- 148A) This section applies for the purpose of calculating the profits of a person carrying on a trade for a period of account in which he is the lessor of any plant or machinery under a long funding finance lease.
- (2) The amount to be brought into account as the lessor's taxable income from the lease for the period of account is the amount of the rental earnings in respect of the lease for the period of account.
  - (3) The “rental earnings” for any period is the amount which, in accordance with generally accepted accounting practice, falls (or would fall) to be treated as the gross return on investment for that period in respect of the long funding lease where it meets the finance lease test.
  - (4) If the lease is one which, under generally accepted accounting practice, falls (or would fall) to be treated as a loan in the accounts in question, so much of the rentals under the lease as fall (or would fall) to be treated as interest are to be treated for the purposes of this section as rental earnings.

#### **Lessor under long funding finance lease: exceptional items**

- 148B) This section applies for the purpose of calculating the profits of a person carrying on a trade for a period of account if he is or has been the lessor under a long funding finance lease.
- (2) This section has effect where a profit or loss (whether of an income or capital nature)—
    - (a) arises to the person in connection with the lease, and
    - (b) in accordance with generally accepted accounting practice falls to be recognised for accounting purposes in a period of account, but
    - (c) would not, apart from this section, be brought into account in calculating the profits of the person.
  - (3) The profit or loss is to be treated—
    - (a) in the case of a profit, as income of the person that is attributable to the lease,
    - (b) in the case of a loss, as a revenue expense incurred by the person in connection with the lease.
  - (4) Any reference in this section to an amount falling to be recognised for accounting purposes in a period of account is a reference to an amount falling to be recognised for accounting purposes—
    - (a) in the person's profit and loss account or income statement,



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- (b) in the person's statement of recognised gains and losses or statement of changes in equity, or
- (c) in any other statement of items brought into account in computing the person's profits or losses for that period.

#### **Lessor under long funding finance lease making termination payment**

148(1) This section applies for the purpose of calculating the profits of a person carrying on a trade for a period of account if he is or has been the lessor under a long funding finance lease.

- (2) Where—
  - (a) the lease terminates, and
  - (b) a sum calculated by reference to the termination value is paid to the lessee,

no deduction in respect of the sum paid to the lessee is allowed in calculating the profits of the person.

- (3) This section does not prevent a deduction in respect of a sum to the extent that the sum is brought into account in determining the person's rental earnings.

#### *Lessors under long funding operating leases*

#### **Lessor under long funding operating lease: periodic deduction**

148(1) This section applies for the purpose of calculating the profits of a person carrying on a trade in a period of account—

- (a) for the whole of which, or
- (b) for any part of which,

the person is the lessor of any plant or machinery under a long funding operating lease.

- (2) A deduction is allowed in calculating the profits of the person for the period of account.
- (3) The amount of the deduction for any period of account is determined as follows.
- (4) First, find the “relevant value” for the purposes of subsection (6)(a), which is—
  - (a) if the only use of the plant or machinery by the lessor has been the leasing of it under the long funding operating lease as a qualifying activity, cost;
  - (b) if the last previous use of the plant or machinery by the lessor was the leasing of it under another long funding operating lease as a qualifying activity, market value;
  - (c) if the last previous use of the plant or machinery by the lessor was the leasing of it under a long funding finance lease as a qualifying activity, the recognised value;
  - (d) if the last previous use of the plant or machinery by the lessor was for the purposes of a qualifying activity other than leasing under a long funding lease, the lower of cost and market value;

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- (e) if the lessor owns the plant or machinery as a result of having incurred expenditure on its provision for purposes other than those of a qualifying activity, but—
- (i) the plant or machinery is brought into use by the lessor for the purposes of a qualifying activity on or after 1st April 2006, and
  - (ii) that qualifying activity is the leasing of the plant or machinery under the long funding lease,
- the relevant value is the lower of first use market value and first use amortised value.
- (5) In subsection (4)—
- “cost” means the amount of the expenditure incurred by the lessor on the provision of the plant or machinery;
- “first use amortised value” means the value that the plant or machinery would have at the time when it is first brought into use for the purposes of the qualifying activity, on the assumption that—
- (a) the cost of acquiring the plant or machinery had been written off on a straight line basis over the remaining useful economic life of the plant or machinery, and
  - (b) any further capital expenditure incurred had been written off on a straight line basis over so much of the remaining economic life of the plant or machinery as remains at the time when the expenditure is incurred;
- “first use market value” means the market value of the plant or machinery at the time when it is first brought into use for the purposes of the qualifying activity;
- “market value” means the market value of the plant or machinery at the commencement of the term of the long funding operating lease;
- “recognised value” means the value at which the plant or machinery is recognised in the books or other financial records of the lessor at the commencement of the long funding operating lease.
- (6) From—
- (a) the relevant value determined in accordance with subsection (4), subtract
  - (b) the amount which, at the commencement of the term of the lease, is (or, in a case falling within subsection (4)(e), would have been) expected to be the residual value of the plant or machinery,
- to find the expected gross reduction in value over the term of the lease.
- (7) Apportion the amount of that expected gross reduction in value to each period of account in which any part of the term of the lease falls.
- (8) The apportionment must be on a time basis according to the proportion of the term of the lease that falls in each period of account.
- (9) The amount of the deduction for any period of account is the amount so apportioned to that period.

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### **Long funding operating lease: lessor's additional expenditure**

- 148E) This section applies if, in a period of account,—
- (a) a person carrying on a trade is the lessor of any plant or machinery under a long funding operating lease,
  - (b) the person incurs capital expenditure in relation to the plant or machinery, and
  - (c) that capital expenditure (the “additional expenditure”) is not reflected in the market value of the plant or machinery at the commencement of the term of the lease.
- (2) In a case falling within section 148D(4)(e), subsection (1)(c) has effect as if the reference to the commencement of the term of the lease were a reference to the time when the plant or machinery is first brought into use by the lessor for the purposes of the qualifying activity.
- (3) Where this section applies, an additional deduction is allowed in calculating the profits of the person for each post-expenditure period of account in which the person is the lessor of the plant or machinery under the lease.
- (4) The amount of the deduction for any such period of account is to be determined as follows.
- (5) Find ARV, CRV, PRV and TRV where—
- “ARV” is the amount which, at the time when the additional expenditure is incurred, is expected to be the residual value of the plant or machinery;
  - “CRV” is the amount which, at the commencement of the term of the lease, is expected to be the residual value of the plant or machinery;
  - “PRV” is the sum of any amounts that fell to be taken into account as RRV (see subsection (6)) in the application of this section in relation to any previous additional expenditure incurred by the person in relation to the leased plant or machinery;
  - “TRV” is the total of CRV and PRV.
- (6) Find RRV, where—
- (a) if ARV exceeds CRV, RRV is the portion of the excess that is a result of the additional expenditure, but
  - (b) if ARV does not exceed CRV, RRV is nil.
- (7) From—
- (a) the amount of the additional expenditure, subtract
  - (b) RRV,
- to find the expected partial reduction in value over the remainder of the term of the lease.
- (8) Apportion the amount of that expected partial reduction in value to each post-expenditure period of account in which any part of the term of the lease falls.
- (9) The apportionment must be on a time basis according to the proportion of the term of the lease that falls in each post-expenditure period of account.

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- (10) The amount of the additional deduction for any period of account is the amount so apportioned to that period.
- (11) In this section “post-expenditure period of account” means any period of account ending after the incurring of the additional expenditure.

**Lessor under long funding operating lease: termination of lease**

- 148(F) This section applies for the purpose of calculating the profits of a person carrying on a trade in a period of account if—
- (a) a long funding operating lease terminates in that period of account, and
  - (b) the person is the lessor under that lease immediately before the termination.
- (2) Step 1 is to find—
- (a) the termination amount (TA);
  - (b) the total of any sums paid to the lessee that are calculated by reference to the termination value (LP).
- (3) Step 2 is to find—
- (a) the relevant value for the purposes of section 148D(6)(a) (RV);
  - (b) the total of the deductions allowable under section 148D for periods of account for the whole or part of which the person was the lessor before the termination of the lease (TD1);
  - (c) the amount, if any, (ERV) by which RV exceeds TD1.
- (4) Step 3 is to find—
- (a) the total of any amounts of capital expenditure incurred by the person which constitute additional expenditure for the purposes of section 148E in the case of the lease (TAE);
  - (b) the total of any deductions allowable under section 148E for periods of account for the whole or part of which the person was the lessor before the termination of the lease (TD2);
  - (c) the amount, if any, (EAE) by which TAE exceeds TD2.
- (5) Step 4 is to find the total of ERV and EAE (T).
- (6) If  $(TA - LP)$  exceeds T, treat a profit of an amount equal to the excess as arising to the person in the period of account in which the lease terminates.
- (7) If T exceeds  $(TA - LP)$ , treat a loss of an amount equal to the excess as arising to the person in that period of account.
- (8) A profit or loss treated as arising to the person under subsection (6) or (7) is to be treated—
- (a) in the case of a profit, as income of the person attributable to the lease,
  - (b) in the case of a loss, as a revenue expense incurred by the person in connection with the lease.

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- (9) In calculating the profits of the person for the period, no deduction is allowed in respect of any sums paid to the lessee that are calculated by reference to the termination value.

*Lessees under long funding finance leases*

**Lessee under long funding finance lease: limit on deductions**

148(G) This section applies for the purpose of calculating the profits of a person carrying on a trade, profession or vocation for a period of account in which the person is the lessee of any plant or machinery under a long funding finance lease.

- (2) In calculating the person's profits for the period of account,—
- (a) the amount deducted in respect of amounts payable under the lease, must not exceed
  - (b) the amounts which, in accordance with generally accepted accounting practice, fall (or would fall) to be shown in the person's accounts as finance charges in respect of the lease.
- (3) If the lease is one which, under generally accepted accounting practice, falls (or would fall) to be treated as a loan, subsection (2) applies as if the lease were one which, under generally accepted accounting practice, fell to be treated as a finance lease.

**Lessee under long funding finance lease: termination**

148(H) This section applies where—

- (a) a person carrying on a trade, profession or vocation is or has been the lessee under a long funding finance lease, and
  - (b) in connection with the termination of the lease, a payment calculated by reference to the termination value falls to be made to the person.
- (2) The payment is not to be brought into account in calculating the profits of the person for any period of account.
- (3) Subsection (2) does not affect the amount of any disposal value that falls to be brought into account by the person under CAA 2001.

*Lessees under long funding operating leases*

**Lessee under long funding operating lease**

148(I) This section applies for the purpose of calculating the profits of a person carrying on a trade, profession or vocation for a period of account in which the person is the lessee of any plant or machinery under a long funding operating lease.

- (2) The deductions that may be allowed in calculating the profits of the person for the period of account are to be reduced in accordance with the following provisions of this section.

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- (3) The amount of the reduction for any period of account is to be determined as follows.
- (4) First, find the “relevant value” for the purposes of subsection (6)(a), which is—
- (a) the market value of the plant or machinery at the commencement of the term of the lease, unless paragraph (b) applies;
  - (b) if the lessee—
    - (i) owns the plant or machinery as a result of having incurred expenditure on its provision for purposes other than those of a qualifying activity, but
    - (ii) brings the plant or machinery into use for the purposes of a qualifying activity on or after 1st April 2006,
the lower of first use market value and first use amortised market value.
- (5) In subsection (4)—
- “first use amortised market value” means the value that the plant or machinery would have—
- (a) at the time when it is first brought into use for the purposes of the qualifying activity, but
  - (b) on the assumption that the market value of the plant or machinery at the commencement of the term of the lease had been written off on a straight line basis over the remaining useful economic life of the plant or machinery;
- “first use market value” means the market value of the plant or machinery at the time when it is first brought into use for the purposes of the qualifying activity.
- (6) From—
- (a) the relevant value determined in accordance with subsection (4), subtract
  - (b) the amount which, at the commencement of the term of the lease, is (or, in a case falling within subsection (4)(b), would have been) expected to be the market value of the plant or machinery at the end of the term of the lease,
- to find the expected gross reduction over the term of the lease.
- (7) Apportion the amount of that expected gross reduction to each period of account in which any part of the term of the lease falls.
- (8) The apportionment must be on a time basis according to the proportion of the term of the lease that falls in each period of account.
- (9) The amount of the reduction for any period of account is the amount so apportioned to that period.

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### *Interpretation of this Chapter*

#### **Interpretation of Chapter 10A**

- 148J) This section has effect for the interpretation of this Chapter.
- (2) In this Chapter—
- “qualifying activity” has the same meaning as in Part 2 of CAA 2001;
  - “residual value”, in relation to any plant or machinery leased under a long funding operating lease, means—
    - (a) the estimated market value of the plant or machinery on a disposal at the end of the term of the lease,
    - less
    - (b) the estimated costs of that disposal.
- (3) Any reference in this Chapter to a sum being written off on a straight line basis over a period of time (the “writing-off period”) is a reference to—
- (a) the sum being apportioned between each of the periods of account in which any part of the writing-off period falls,
  - (b) that apportionment being made on a time basis, according to the proportion of the writing-off period that falls in each of the periods of account, and
  - (c) the sum being written off accordingly.
- (4) Chapter 6A of Part 2 of CAA 2001 (interpretation of that Part so far as relating to long funding leases) also applies for the purposes of this Chapter.”.

#### *Application of Chapter 10A for calculating the profits of a property business*

- 14 (1) Section 272 is amended as follows.
- (2) In the Table in subsection (2), insert at the appropriate place—

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<b>“In Chapter 10A (long funding leases)—</b>	
Sections 148A to 148J	Leases of plant or machinery: special rules for long funding leases”

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## **PART 4**

### **COMMENCEMENT AND TRANSITIONAL PROVISIONS**

#### *Commencement*

- 15 (1) The amendments made by this Schedule have effect in the case of a lease if—
- (a) Condition A is met, or
  - (b) if Condition A is not met, Condition B is met,

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unless the lease was finalised (see paragraph 23) before 21st July 2005 and on 17th May 2006 the lessor was within the charge to tax.

As respects any time before 18th May 2006, this sub-paragraph has effect with the omission of the words “and on 17th May 2006 the lessor was within the charge to tax”.

This sub-paragraph is subject to sub-paragraphs (5) and (6).

- (2) Condition A is that—
- (a) the lease is finalised on or after 1st April 2006, or
  - (b) the commencement of the term of the lease is on or after that date,
- and the lease is not an excepted lease (see paragraph 17).
- (3) Condition B is that—
- (a) the commencement of the term of the lease was before 1st April 2006, but
  - (b) the plant or machinery is on or after that date brought into use for the purposes of a qualifying activity carried on by the person concerned.
- (4) The amendments made by this Schedule also have effect in relation to a lease, in the case of the lessor, if—
- (a) an election under paragraph 16 is in force in the case of the lease, and
  - (b) the election has effect in the case of the lessor.
- (5) Where the amendments made by this Schedule do not have effect in relation to a lease in the case of the lessor but—
- (a) there is a transfer of plant or machinery,
  - (b) immediately before the transfer, the lessor is within the charge to tax, and
  - (c) the transfer is in circumstances such that, if the amendments made by this Schedule did apply in relation to the lease, section 70W(4)(b) of CAA 2001 (transfers, assignments etc by lessor) would have effect in relation to the new lessor to treat the new lease as a lease which is not a long funding lease,
- the amendments made by this Schedule do not have effect in relation to the new lease in the case of the new lessor.

In this sub-paragraph—

“the new lease” means the lease that would be the new lease for the purposes of section 70W of CAA 2001, if that section applied;

“the new lessor” means the person who would be the new lessor for the purposes of that section, if that section applied;

and section 70W(7) of CAA 2001 (construction of references to transfer of plant or machinery) also has effect for the purposes of this sub-paragraph.

- (6) Where the amendments made by this Schedule do not have effect in relation to a lease in the case of the lessee but—
- (a) there is a transfer of plant or machinery,
  - (b) immediately before the transfer, the lessee is within the charge to tax, and
  - (c) the transfer is in circumstances such that, if the amendments made by this Schedule did apply in relation to the lease, section 70X(4)(b) of CAA 2001 (transfers, assignments etc by lessee) would have effect in relation to the new lessee to treat the new lease as a lease which is not a long funding lease,



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the amendments made by this Schedule do not have effect in relation to the new lease in the case of the new lessee.

In this sub-paragraph—

“the new lease” means the lease that would be the new lease for the purposes of section 70X of CAA 2001, if that section applied;

“the new lessee” means the person who would be the new lessee for the purposes of that section, if that section applied;

and section 70X(7) of CAA 2001 (construction of references to transfer of plant or machinery) also has effect for the purposes of this sub-paragraph.

- (7) In the application of section 70W(4)(b) or 70X(4)(b) of CAA 2001 for the purposes of sub-paragraph (5) or (6), the lease mentioned in the opening words of the sub-paragraph in question is to be regarded as a lease which is not a long funding lease.

*Election for lease to be treated as long funding lease for tax purposes*

- 16 (1) The Treasury may by regulations make provision enabling a person of a prescribed description who is, or is to be, the lessor under a plant or machinery lease of a prescribed description to make an election for the lease to be treated in his case as a long funding lease.
- (2) The power to make regulations under this paragraph includes power to make provision for or in connection with any of the following—
- (a) any conditions that must be met if an election is, or is to be, made;
  - (b) whether an election is irrevocable;
  - (c) the date on and after which an election has effect;
  - (d) the manner in which an election is to be made.
- (3) The power to make regulations under this paragraph includes—
- (a) power to make provision having effect in relation to times before the making of the regulations (but not before 1st April 2006),
  - (b) power to make different provision for different cases,
  - (c) power to make incidental, consequential, supplemental, or transitional provision or savings.
- (4) In this paragraph—
- “election” means an election under this paragraph;
  - “long funding lease” means a lease which is a long funding lease for the purposes of Part 2 of CAA 2001;
  - “prescribed” means specified in, or determined in accordance with, regulations under this paragraph.

*Excepted leases*

- 17 (1) A lease is an excepted lease if the following conditions are met.
- (2) Condition 1 is that before 21st July 2005 there was evidence in writing that there was agreement, or a common understanding, between the lessor's side and the lessee's side as to the principal terms of the lease (the “pre-existing heads of agreement”).

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The definitions of “the lessor's side”, “the lessee's side” and “the principal terms” are in paragraph 27.

- (3) Condition 2 is that the leased plant or machinery was under construction (see paragraph 24) before 1st April 2006.
- (4) Condition 3 is that the lease has been finalised before 1st April 2007 (but see sub-paragraph (8)).
- (5) Condition 4 is that the commencement of the term of the lease is before 1st April 2007 (but see sub-paragraph (8)).
- (6) Condition 5 is that the lessee is the particular person or persons identified as such in the pre-existing heads of agreement.
- (7) Condition 6 is that the principal terms of the lease are not (or, apart from section 70M of CAA 2001, would not be) materially different from those in the pre-existing heads of agreement.
- (8) Sub-paragraphs (4) and (5) have effect with the substitution of “ 2009 ” for “2007” if the additional conditions in paragraph 18 are met.

*Extended time limit: the additional conditions*

- 18
- (1) The additional conditions mentioned in paragraph 17(8) are as follows.
  - (2) Condition A is that the commencement of the term of the lease is before 1st April 2009.
  - (3) Condition B is that, at the latest, the commencement of the term of the lease is as soon as is reasonably practicable after construction of the asset is substantially complete.
  - (4) Condition C is that construction of the asset proceeded continuously on and after 1st April 2006.
  - (5) Condition D is that construction of the asset proceeded at the normal pace for an asset of its type.

For this purpose, “normal pace” is the pace required to construct the asset in a reasonable time without delays or interruptions and consistent with normal business practice.

- (6) This paragraph is supplemented by paragraph 19.

*Events beyond the control of the parties etc*

- 19
- (1) Condition B, C or D in paragraph 18 is not failed by reason only of breaches due to events that meet the conditions in sub-paragraph (2).
  - (2) The conditions are that—
    - (a) the event is abnormal or unusual,
    - (b) the event is unforeseen, and could not reasonably have been foreseen, at the date when the main contract for the construction of the leased asset is entered into,
    - (c) the event is beyond the control of each of the principal parties,

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- (d) as respects the Condition in question, the consequences of the event could not have been avoided by the exercise of all due care, or the taking of all reasonable steps, by the principal parties or any of them.
- (3) In this paragraph “the principal parties” are—
- (a) the lessor's side,
  - (b) the lessee's side,
  - (c) the main constructor (see the definition in paragraph 27).

*Pre-existing heads of agreement relating to two or more assets*

- 20 (1) This paragraph has effect for the purposes of this Part in any case where the pre-existing heads of agreement relates to two or more assets.
- (2) The treatment of any of the assets varies according to whether the asset—
- (a) is for use individually (see sub-paragraph (3)), or
  - (b) is a constituent asset of a combined asset (see sub-paragraph (4)).
- (3) Where any of the assets is for use individually, this Part has effect in relation to that asset separately, as if it were the subject of—
- (a) its own separate pre-existing heads of agreement, and
  - (b) if there is a finalised lease, its own separate finalised lease.
- See sub-paragraph (5) for the method of determining the terms.
- (4) Where any of the assets are constituent assets of a combined asset—
- (a) the combined asset is to be regarded as a single asset, and
  - (b) the constituent assets are to be regarded as if they were instead component parts of that single asset,
- and sub-paragraph (3) applies accordingly.
- (5) For the purposes of sub-paragraph (3), the principles in sections 70L and 70M of CAA 2001 are to be applied, with any necessary modifications, for the purpose of determining the terms of—
- (a) the deemed separate pre-existing heads of agreement, and
  - (b) the deemed separate finalised lease (if any).

*Expenditure incurred before passing of this Act where lease is not an excepted lease*

- 21 (1) This paragraph applies where the following conditions are met—
- (a) a person incurs expenditure on the provision of plant or machinery for leasing under a long funding lease,
  - (b) some or all of that expenditure was incurred before the day on which this Act is passed,
  - (c) the long funding lease is not an excepted lease,
  - (d) before 21st July 2005 there was a pre-existing heads of agreement in the case of the long funding lease.
- (2) In this paragraph—
- (a) “the old expenditure” means so much of the expenditure as is expenditure incurred before the day on which this Act is passed, and

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- (b) “the new expenditure” means so much of the expenditure as is expenditure incurred on or after that day.
- (3) Treat the old expenditure—
  - (a) as if it had been incurred on the provision of a separate asset for leasing under a separate long funding lease, and
  - (b) as if that separate long funding lease were an excepted lease.
- (4) Treat the new expenditure as if it had been incurred on the provision of a separate asset for leasing under a separate long funding lease in relation to which the amendments made by this Schedule have effect.

That is without prejudice to the application of any provisions of this Part which treat that deemed separate long funding lease as if it were two or more leases.

- (5) The rentals under the actual long funding lease are to be apportioned between the two deemed leases in such manner as is just and reasonable.
- (6) This paragraph has effect for the purpose of determining liability to income tax or corporation tax in the case of any person who is or has been the lessor or the lessee under the actual long funding lease.
- (7) Paragraph 22 has effect for determining when an amount of expenditure is to be treated for the purposes of this paragraph as incurred by the person mentioned in sub-paragraph (1).

*When expenditure is incurred for the purposes of paragraph 21*

- 22 (1) This paragraph has effect for determining, for the purposes of paragraph 21, when an amount of expenditure is to be treated as incurred by the person mentioned in sub-paragraph (1) of that paragraph.
- (2) The general rule is that an amount of expenditure is to be treated as incurred as soon as there is an unconditional obligation to pay it.
- (3) The general rule applies even if the whole or a part of the expenditure is not required to be paid until a later date.
- (4) There are the following exceptions to the general rule.
- (5) If, under an agreement,—
  - (a) an unconditional obligation to pay an amount of expenditure comes into being as a result of the giving of a certificate or any other event, and
  - (b) the giving of the certificate, or other event, occurs before the day that falls one month after the passing of this Act,
the expenditure is to be treated as incurred on the day before the passing of this Act.
- (6) If, under an agreement,—
  - (a) there is an unconditional obligation to pay an amount of expenditure on a date earlier than accords with normal commercial usage, and
  - (b) the sole or main benefit which might have been expected to be obtained thereby is that the amount would be treated, under the general rule, as incurred at an earlier time,
the amount is to be treated as incurred on the date on or before which it is required to be paid.

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- (7) If the terms of an agreement are varied on or after 22nd March 2006 with respect to the times for payment and—
- (a) apart from the variation, an unconditional obligation to pay an amount of expenditure would have come into being on or after the day on which this Act is passed, but
  - (b) as a result of the variation, the unconditional obligation to pay the amount comes into being before that day,
- the amount is to be treated as incurred on the date on which it would have been treated as incurred apart from the variation.
- (8) Sub-paragraph (7) does not apply if the long funding lease mentioned in paragraph 21 was finalised before 22nd March 2006.

*When a lease is “finalised”*

- 23 (1) For the purposes of this Part, a lease is “finalised” on the earliest day on which the following conditions are met.
- (2) Condition 1 is that there is a contract in writing for the lease between the lessor and the lessee.
- (3) Condition 2 is that either—
- (a) the contract is unconditional, or
  - (b) if it is conditional, the conditions have been met.
- (4) Condition 3 is that no terms remain to be agreed.

*When an asset is “under construction”*

- 24 (1) An asset is “under construction” at any time in the period which—
- (a) begins when construction of the asset begins, and
  - (b) ends when construction of the asset is completed.
- (2) An asset consisting of two or more component parts is to be taken to be under construction at any time after the start of construction of any of those component parts which meets the condition in subsection (3).
- (3) The condition is that the component part has been identified as a component part of the particular asset before construction of the component part begins.
- (4) Sub-paragraphs (1) and (2) are subject to sub-paragraph (5).
- (5) The leased asset is not to be regarded as under construction at any time after the commencement of the term of the lease.
- (6) This paragraph has effect for the purposes of this Part.

*Combined assets and constituent assets*

- 25 (1) A “combined asset” is an asset which meets the conditions in sub-paragraph (2).
- (2) The conditions are that—
- (a) the asset is for use individually,
  - (b) it consists of two or more items of plant or machinery (“constituent assets”),

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- (c) each of the constituent assets is constructed with a view to its use in conjunction with the others as a single asset (namely, the combined asset).
- (3) Plant or machinery that can be used individually is not a constituent asset just because—
- (a) it is one of a number of assets of the same or a similar description,
  - (b) each of those assets is intended for use individually, and
  - (c) the use individually of those assets is to be co-ordinated to any extent.
- (4) This paragraph has effect for the purposes of this Part.

#### *Mixed leases*

- 26 (1) This paragraph applies in any case where there is a mixed lease (see section 70L of CAA 2001).
- (2) In any such case, determine whether the mixed lease is an excepted lease.
- (3) If the mixed lease is an excepted lease, section 70L of CAA 2001 and the amendments made by this Schedule accordingly do not have effect in relation to it.
- (4) If the mixed lease is not an excepted lease, then apply sections 70L and 70M of CAA 2001 and determine separately in the case of each derived lease whether that derived lease is an excepted lease.

#### *Interpretation of this Part*

- 27 (1) In this Part—
- “combined asset” is to be construed in accordance with paragraph 25;
  - “constituent asset” is to be construed in accordance with paragraph 25;
  - “finalise”, in relation to a lease, is to be construed in accordance with paragraph 23;
  - “lease” includes—
    - (a) a plant or machinery lease, and
    - (b) a mixed lease,
  - and “lessor”, “lessee” and other related expressions are to be construed accordingly;
  - “the lessee's side” means any of the following—
    - (a) the lessee,
    - (b) a person who controls (or is to control) the lessee,
    - (c) any two or more persons who together control (or are to control) the lessee,
  - and for this purpose “control” has the meaning given by [F<sup>2</sup>section 574 of CAA 2001] ;
  - “the lessor's side” means any of the following—
    - (a) the lessor,
    - (b) a person who controls (or is to control) the lessor,
    - (c) any two or more persons who together control (or are to control) the lessor,

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and for this purpose “control” has the meaning given by [F2section 574 of CAA 2001] ;

“the main constructor” means the contractor under the main contract for the construction of the plant or machinery;

“pre-existing heads of agreement” is to be construed in accordance with paragraph 17(2);

“the principal terms”, in relation to a lease, are the following—

- (a) the identity of the lessee;
- (b) the identity or description of the asset to be leased;
- (c) particulars, or a description, of the rentals payable under the lease;
- (d) particulars, or a description, of the term of the lease;

“qualifying activity” has the same meaning as in Part 2 of CAA 2001;

“under construction”, in the case of an asset, is to be construed in accordance with paragraph 24.

- (2) Chapter 6A of Part 2 of CAA 2001 (interpretation of that Part so far as relating to long funding leases) also applies for the purposes of this Part.

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**Textual Amendments**

- F2** Words in Sch. 8 para. 27(1) substituted (6.4.2007 with effect as mentioned in s. 1034(1) of the amending Act) by [Income Tax Act 2007 \(c. 3\)](#), s. 1027, [Sch. 1 para. 624](#) (with transitional provisions and savings in Sch. 2)

**Changes to legislation:**

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