

FINANCE ACT 2012

EXPLANATORY NOTES

INTRODUCTION

Section 46: Plant and Machinery Long Funding Leases

Summary

1. [Section 46](#) ensures that the rules for calculating the disposal value for the lessee at the end of a long funding lease operate as intended so that the relief available by way of capital allowances does not exceed the net expenditure of the lessee not otherwise relieved.

Details of the Section

Section 70E of CAA 2001

2. Subsection (1) introduces the amendments to section 70E of the Capital Allowances Act 2001 (CAA).
3. Subsection (2) amends section 70E(2A) of CAA to extend the definition of “R” referred to in the formula in that subsection. It will now include not only any “relevant rebate” but also any other “relevant leased-related payment”.
4. Subsection (3) inserts new sections 70E(2FA) to (2FC).
5. New section 70E(2FA) defines “relevant lease-related payment” setting out a number of conditions to be met.
6. New section 70E(2FA)(a) contains the first condition and requires a payment to be payable for the direct or indirect benefit of the lessee or a person connected with the lessee. This is irrespective of when the payment was payable and is not therefore restricted only to payments at the termination of the lease.
7. New section 70E(2FA)(b) contains the second condition. It requires the payment to be connected either to the long funding lease or with any arrangement that is connected with that long funding lease.
8. New section 70E(2FA)(c) provides that “relevant lease-related payment” does not include certain types of payment.
9. New section 70E(2FA)(c)(i) and (ii) exclude payments made by the lessee to the lessor if they are initial or any other payments made under the long funding lease or under a guarantee of any residual amount. For these purposes “residual amount” is as defined in section 70YE of CAA.
10. New section 70E(2FA)(c)(iii) excludes initial or other payments made under a relevant superior lease, defined in new Section 70E(2FB), by the lessee under that superior lease to the lessor under that superior lease.
11. New Section 70E(2FA)(c)(iv) excludes a payment of sale proceeds of plant or machinery to the seller where that sale meets the conditions set out in new section 70E(2FC)

*These notes refer to the Finance Act 2012 (c.14)
which received Royal Assent on 17 July 2012*

12. The final part of new section 70E(2FA) excludes as “relevant lease-related payments” any payment, or part of any such payment, that has otherwise been brought into tax either as income or as a disposal receipt by the person for whose benefit the payment was payable. This exclusion is extended to persons that would have brought the payment so into account for tax purposes if they had been within the charge to tax.
13. New section 70E(2FB) provides that for the purposes of new section 70E(2FA) “payment” includes the passing of benefit in any form and that “relevant superior lease” is any lease to which the long funding lease in new section 70E(2FA)(1)(a) is inferior.
14. New section 70E(2FC) provides the conditions to be met for new section 70E(2FA)(c) (iv) to apply. The conditions are that a person has entered into a relevant transaction within section 213(1)(a) of CAA, the plant or machinery is the subject of a sale and leaseback within section 216(1)(b) of CAA and in relation to that sale and leaseback the conditions in section 227(2) of CAA are met.
15. Subsection (4) amends section 70E(2G) by extending substitution of an arm’s length amount for “relevant lease-related payment”, as well as for “relevant rebate”, where the lease is not a transaction at arm’s length.
16. Subsection (5) provides the amendments made to section 70E of CAA have effect in cases where a “relevant event” occurs on or after 21 March 2012. “Relevant event” is defined in section 70E(1A).

Background Note

17. The long funding lease rules were introduced into CAA, and other relevant parts of the Tax Acts, by Schedule 8 of Finance Act 2006.
18. These rules provide that where the relevant conditions are satisfied, the lessee, rather than the lessor, is entitled to claim capital allowances for expenditure on the plant or machinery which is the subject of the long funding lease.
19. Sections 70B and 70C of CAA provide the rules for how the lessee’s qualifying expenditure for capital allowances at the commencement of, respectively, a long funding operating lease or a long funding finance lease is to be calculated. At commencement of the lease this is necessarily an estimate because the lessee actually incurs the expenditure over the course of the lease
20. The rules in section 70E of CAA deal with disposal events and disposal values. For all long funding leases a formula is used though the definition of one part of the formula, “QA” (Qualifying Amount), differs depending upon whether the lease in question is a finance or operating lease.
21. The purpose of the formula is to adjust the amount of capital allowances available to the lessee, which were initially based on estimated expenditure, to match the lessee’s actual expenditure less any rebates received (i.e. net expenditure).
22. These amendments address disclosed avoidance schemes that involve arrangements which include transactions, the claimed effect of which is that an amount is received by the lessee in connection with a long funding lease but which is not taken into account in the prescribed formula for disposal value. The tax effect claimed is that capital allowances are due to the lessee in excess of the net expenditure (not otherwise relieved) by the lessee on the leased asset.