

FINANCE ACT 2010

EXPLANATORY NOTES

INTRODUCTION

Section 28: Cushion Gas

Summary

1. [Section 28](#) amends Part 2 of the Capital Allowances Act 2001 (CAA) in relation to expenditure on cushion gas used in a gas storage facility. The section provides that all new leases of cushion gas effective from 1 April 2010, will be treated as funding leases and that all capital expenditure on cushion gas, incurred on or after the same date, will be treated as special rate expenditure, qualifying for writing-down allowances (WDAs) at 10 per cent a year.

Details of the Section

2. Subsection (3) inserts new subsection (1A) into section 70J of CAA. The new subsection provides that a lease of “cushion gas” is also a “funding lease” whether or not it would otherwise be so regarded. Previously, a lease of plant or machinery was only a “funding lease” if it met the tests in section 70J(1).
3. Subsection (5) inserts new subsection 7 into section 70J. The new subsection explains what is meant by “cushion gas” and defines it as gas that functions or is intended to function as plant in a particular gas storage facility. The meaning also applies for the amended section 104A of CAA (see paragraph 4 below) and new section 104G.
4. Subsection (6) amends section 104A of CAA by adding a new paragraph in subsection (1). The new paragraph provides that expenditure incurred on or after 1 April 2010 on the provision of cushion gas is to be treated as special rate expenditure.
5. Subsection (7) inserts new section 104G after section 104F of CAA.
6. New section 104G gives the rules in relation to disposal events in respect of cushion gas that consists of both “new” and “old” expenditure. “New” and “old” expenditure are later defined in new section 104G(5).
7. New section 104G(1) explains that the section applies only if a person has incurred expenditure on the provision of cushion gas in a particular gas storage facility both before 1 April 2010 (old expenditure) and on or after 1 April 2010 (new expenditure).
8. New section 104G(2) provides that any disposal event in relation to the cushion gas is to be treated as a disposal event in relation to the “new expenditure” before it is treated as relating to the “old expenditure”. The rule effectively ensures that if the “old expenditure” was in the main pool, then that expenditure is retained, and will continue to attract allowances at 20 per cent, in preference to later expenditure which has been allocated to the special rate pool.
9. New section 104G(3) sets out the consequences of the rule in new section 104G(2).

*These notes refer to the Finance Act 2010 (c.13)
which received Royal Assent on 8 April 2010*

10. New section 104G(4) provides and clarifies that disposals of cushion gas that qualified for relief under the pre 1 April 2010 rules are treated as separate from disposals of cushion gas that qualified for relief under the post 1 April 2010 rules, even if there is, in fact, only one event, such as a single contract for sale.
11. Subsection (8) gives the commencement provision in respect of subsections (2) to (5). Any lease whose inception is on or after 1 April 2010 will be a funding lease. There is a definition of “inception” in section 70YI(1) of CAA.
12. Subsections (9) and (10) give the commencement provisions in respect of subsections (6) and (7) respectively, and provide that the amendments made relate to expenditure incurred or disposal events taking place on or after 1 April 2010.

Background Note

13. At Budget 2009 the Government announced that capital expenditure on cushion gas that functions as plant in a gas storage facility qualifies for plant and machinery capital allowances, but said it would discuss, with the industry, certain technical and revenue protection issues arising from this treatment.
14. A number of points in relation to cushion gas were discussed with stakeholders. After considering the stakeholders’ views and helpful comments the Government decided that no action (other than a watching brief) would be taken in relation to some points but that the matters (now addressed by this section) did require specific legislation.

Rate of WDAs

15. In the prior discussions with the industry, it was accepted that, in the main, expenditure on cushion gas would normally qualify for 10 per cent allowances as “long-life asset expenditure” (that is, expenditure on an asset that may reasonably be expected to have a useful economic life of at least 25 years when new, as defined in section 91 of CAA). However, the industry also suggested that the expected use of cushion gas in certain gas storage facilities might be less than 25 years if the facility itself had an expected useful life of less than 25 years and, in these circumstances, the gas should qualify for main rate WDAs. The Government decided that as cushion gas does not wear out, nor necessarily lose its value by the mere passage of time, the 10 per cent “special rate” of WDA is the more appropriate rate for expenditure on an unusual asset of this kind.
16. The legislation, therefore, specifies that expenditure on cushion gas will be a further type of special rate expenditure in order to fix the rate of WDA at 10 per cent a year.

Leases of cushion gas

17. As it is accepted that cushion gas in a gas storage facility constitutes plant, it may be leased under a plant and machinery lease. However, cushion gas is different from most other plant and machinery in that it does not wear out. It would, therefore, have been possible to write very long operating leases of cushion gas, without ever triggering the application of the long funding lease rules. This could have meant that leases of cushion gas would have been taxed by reference to their legal form, rather than commercial substance, which would have been at variance with the 2006 leasing reforms.
18. The legislation therefore specifies that all leases of cushion gas are to be funding leases for the purposes of the Taxes Acts. This means that, from the perspective of the lessor, any lease of cushion gas for five years or more will be taxed by reference to the commercial substance rather than the legal form. The lessee, where UK resident, will have the choice of claiming a deduction for the lease rentals in accordance with the accounting treatment, or of opting to claim capital allowances with a restricted deduction in respect of the lease rentals. Overseas lessees will be entitled to claim under the rules applicable to their particular jurisdiction and will not be affected by these changes.