

CORPORATION TAX ACT 2010

EXPLANATORY NOTES

INTRODUCTION

Part 19: Sale and lease-back etc

Chapter 4: Leased assets: capital sums

Overview

2572. This Chapter is based on section 781 of ICTA.
2573. It deals with cases such as that of a taxpayer which, having had tax relief in respect of a payment under a lease of an asset other than land or buildings, receives or has received at any time a capital sum in respect of the lessee's interest in the lease.
2574. If the Chapter applies, corporation tax is charged on (broadly speaking) the amount on which relief has been obtained or, if less, on the capital sum.
2575. The Chapter has the following structure.
- Section 870 summarises the Chapter.
 - Sections 871 to 873 state when the Chapter applies.
 - Sections 874 to 876 concern the charge to corporation tax.
 - Sections 877 to 879 deal with obtaining the capital sum.
 - Sections 880 and 881 are about apportionment.
 - Sections 882 to 886 are interpretative.

Section 870: Overview

2576. This section summarises the Chapter. It is new.
2577. The expressions "capital sum" and "lease" appear in this section for the first time in this Chapter. They are defined in sections 883 and 884 respectively.

Section 871: Application of the Chapter

2578. This section introduces the five conditions relating to the application of this Chapter and explains their logical relationship. It is based on section 781(1) of ICTA.

Section 872: Payment under lease

2579. This section specifies a necessary condition (condition A) for the Chapter to apply, namely that a tax-deductible payment is made under a lease of a relevant asset. It is based on sections 781(1) and (3) and 782(1) of ICTA.

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2580. The expressions “relevant asset” and “relevant tax relief” appear in *subsection (1)(a)* and *(b)* respectively for the first time in this Chapter. They are defined in sections 885 and 886 respectively.
2581. The person entitled to a deduction by way of tax relief under section 781(1)(a) of ICTA is not necessarily the person obtaining the capital sum and charged to tax under that subsection. It follows that, if the person obtaining the capital sum is charged to corporation tax, the person entitled to a deduction by way of tax relief is not necessarily a corporation tax payer. Subsection (1)(b) of this section therefore refers to “relevant tax relief”, rather than “relevant corporation tax relief”.
2582. *Subsection (2)* stipulates that if Chapter 3 of this Part applies to the payment then condition A is not met (and, therefore, this Chapter does not apply to the payment). For that reason, Chapter 3 appears in this Part before this Chapter, reversing the order of the source legislation.
2583. *Subsection (3)* similarly stipulates that if Chapter 3 of Part 12A of ITA (the income tax provision corresponding to Chapter 3 of this Part) applies to the payment then condition A is not met (and, therefore, this Chapter does not apply to the payment). Subsection (3) is unlikely to apply in practice, but omitting it would change the law to the taxpayer’s disadvantage.
2584. *Subsection (4)* preserves the rule that, if the lease was created before the legislation was first introduced, receiving a capital sum after that date does not activate the legislation.

Section 873: Sum obtained

2585. This section specifies four alternative additional conditions for the Chapter to apply. It is based on sections 781(1) and (9) and 783(3) of ICTA.
2586. All four of the conditions concern the obtaining of a capital sum by a person of the description specified in the condition. In particular, the person obtaining the capital sum need not be the person making the tax-deductible payment.
2587. In conditions B and C in *subsections (1)* and *(2)*, the capital sum is obtained in respect of the lessee’s interest in the lease. In condition B, the capital sum is obtained by the person making the payment. In condition C, the capital sum is obtained by an associate of that person.
2588. Subsection (1)(a) is the first provision in this Chapter which refers to obtaining a sum in respect of an interest in a lease and, specifically, to obtaining a sum in respect of the lessee’s interest in a lease. The former expression is defined in section 877. The latter expression is defined in section 878.
2589. The word “associate” appears in subsection (2) for the first time in this Chapter. It is defined in section 882.
2590. In conditions D and E in *subsections (3)* and *(4)*, the capital sum is obtained in respect of the lessor’s interest in the lease, or of any other interest in the asset. In condition D, the capital sum is obtained by an associate of the person making the payment. In condition E, the interest belongs to an associate of that person and the capital sum is obtained by an associate of that associate.
2591. *Subsection (5)* makes it clear that, for the purposes of this section, it is irrelevant when the payment is made.
2592. *Subsections (6)* and *(7)* relate to hire-purchase agreements for plant and machinery. Subsection (6) makes an exception to conditions B and C. Subsection (7) makes an exception to conditions D and E.

Section 874: Charge to corporation tax

2593. This section imposes the charge to corporation tax on the company obtaining the capital sum. It is based on sections 781(1), (1B), (2) and (6) of ICTA.
2594. Under *subsection (1)*, there is a charge to corporation tax on income for the accounting period in which the sum is obtained.
2595. *Subsection (2)* measures the amount on which tax is charged.
2596. *Subsection (3)* introduces four subsections limiting the effect of subsections (1) and (2).
2597. *Subsection (4)* caps the amount on which tax is charged.
2598. To prevent double taxation, *subsections (5) and (6)* ensure that once a payment (or part of a payment) has been taken into account in making a charge under this section it cannot be taken into account in making a further charge in respect of another sum.
2599. *Subsection (7)* is a timing rule supplementing subsections (5) and (6).

Section 875: Hire-purchase agreements

2600. This section concerns hire-purchase agreements. It is based on section 784 of ICTA.
2601. This section may be in point if section 873(6) and (7) (sum obtained: exceptions for hire-purchase agreements) do not prevent this Chapter from applying. If this Chapter applies, *subsection (1)* states the conditions for this section to apply.
2602. *Subsection (2)* requires the total to be found of:
- non-tax-deductible payments under the lease; and
 - if the lessee's interest in the lease was assigned to the company before it obtained the capital sum in respect of that interest, any capital payment made by the company as consideration for the assignment.
2603. This total is then compared with the capital sum. If it is equal to or greater than the capital sum, then under *subsection (3)* the capital sum is treated for the purposes of section 874(4) as £nil. If the total found under subsection (2) is less than the capital sum, then under *subsection (4)* it is deducted from the capital sum in applying section 874(4).
2604. *Subsection (5)* covers the special case in which the capital sum is the consideration for part only of the lessee's interest in the lease.
2605. Section 784(4) of ICTA provides that:
- “the amount to be deducted ... shall be such proportion of the capital expenditure which is still unallowed *as is reasonable*” (emphasis added).
2606. Rewriting this, subsection (5)(a) requires the unallowed amount to be reduced to a proportion which is not only reasonable but also just. This is a minor change in the law: see *Change 33* in Annex 1.
2607. To prevent double relief, *subsections (6) and (7)* ensure that if a payment has been taken into account under subsection (2) in respect of a capital sum it cannot be taken into account in respect of another capital sum.
2608. *Subsection (8)* is a timing rule supplementing subsections (6) and (7).

Section 876: Adjustments where sum obtained before payment made

2609. This section provides for adjustments to be made if a capital sum is obtained as mentioned in section 873 and later a payment is made as mentioned in section 872. It is based on section 781(7) to (8A) of ICTA.

Section 877: Sum obtained in respect of interest

2610. This section is concerned with the meaning, in this Chapter, of “a sum obtained in respect of an interest in an asset”. It is based on section 783(1) and (2) of ICTA.

Section 878: Sum obtained in respect of lessee’s interest

2611. This section is concerned with the meaning, in this Chapter, of “a sum obtained in respect of the lessee’s interest in a lease of an asset”. It is based on section 783(1) and (2) of ICTA.

Section 879: Disposal of interest to associate

2612. This section determines the amount which a company is deemed to obtain if it disposes of an interest in an asset to a person who is the company’s associate. It is based on sections 781(1) and 783(4) and (5) of ICTA.

Section 880: Apportionment of payments made and of sums obtained

2613. This section provides for apportionments to be made of payments made and sums obtained. It is based on section 783(6) to (8) of ICTA.

2614. *Subsection (3)* requires apportionments to be not only just but also reasonable. This is a minor change in the law. See *Change 33* in Annex 1.

2615. *Subsections (4) and (5)* omit references to a profession and to a vocation where the source legislation refers to the carrying on by a company of a trade, profession or vocation. See the commentary on section 837 and *Change 4* in Annex 1. This Change is not made in *subsection (2)*, as the reference in that subsection to “relevant tax relief” is not limited to corporation tax.

Section 881: Manner of apportionment

2616. This section provides for apportionments to be made by the tribunal in certain circumstances. It is based on section 783(9) of ICTA.

Section 882: Associates

2617. This section defines “associates” for the purposes of this Chapter. It is based on section 783(10) and (11) of ICTA.

Section 883: Capital sum

2618. This section defines “capital sum” for the purposes of this Chapter. It is based on the definition of “capital sum” in section 785 of ICTA.

2619. *Paragraph (a)* omits references to a profession and to a vocation where the source legislation refers to the carrying on by a company of a trade, profession or vocation. See the commentary on section 837 and *Change 4* in Annex 1.

Section 884: Lease

2620. This section defines “lease” for the purposes of this Chapter. It is based on the definition of “lease” in section 785 of ICTA.

Section 885: Relevant asset

2621. This section defines “relevant asset” for the purposes of this Chapter. It is based on the definition of “asset” in section 785 of ICTA.

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2622. The source legislation uses the term “asset”, which is defined to exclude land and interests in land. Since many readers may find this counter-intuitive, this section uses the new term “relevant asset”.

Section 886: Relevant tax relief

2623. This section defines “relevant tax relief” for the purposes of this Chapter. It is based on section 781(4) of ICTA.
2624. *Paragraph (a)* omits references to a profession and to a vocation where the source legislation refers to the carrying on by a company of a trade, profession or vocation. See the commentary on section 837 and *Change 4* in Annex 1.