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# Income and Corporation Taxes Act 1988

## 1988 CHAPTER 1

### PART XII

#### SPECIAL CLASSES OF COMPANIES AND BUSINESSES

VALID FROM 19/07/2006

#### CHAPTER 5A

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

*[<sup>F1</sup>Introductory*

#### Textual Amendments

- F1** [Pt. 12 Ch. 5A](#) (ss. 502A-502L) inserted (with effect in accordance with [Sch. 8 para. 15](#) of the amending Act) by [Finance Act 2006 \(c. 25\)](#), [Sch. 8 para. 11](#)

#### **502A** Scope of Chapter 5A

This Chapter has effect for the purposes of corporation tax only.

*Lessors under long funding finance leases*

#### **502B** Lessor under long funding finance lease: rental earnings

- (1) This section applies for determining for the purposes of corporation tax the profits of a company for any period of account in which it is the lessor of any plant or machinery under a long funding finance lease.

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- (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 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.

**Modifications etc. (not altering text)**

- C1 [S. 502B](#) excluded (21.7.2008) by [Finance Act 2008 \(c. 9\)](#), [Sch. 20 para. 11\(2\)](#)  
 C2 [S. 502B](#) excluded (21.7.2009) by [Finance Act 2009 \(c. 10\)](#), [Sch. 33 para. 5](#)

**502C Lessor under long funding finance lease: exceptional items**

- (1) This section applies for determining for the purposes of corporation tax the profits of a company which 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 company 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 computing the profits of the company for the purposes of corporation tax.
- (3) The profit or loss is to be treated—
  - (a) in the case of a profit, as income of the company attributable to the lease,
  - (b) in the case of a loss, as a revenue expense incurred by the company 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 company's profit and loss account or income statement,
  - (b) in the company'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 company's profits or losses for that period.

**Modifications etc. (not altering text)**

- C3 [S. 502C](#) excluded (21.7.2008) by [Finance Act 2008 \(c. 9\)](#), [Sch. 20 para. 11\(8\)](#)  
 C4 [S. 502C](#) excluded (21.7.2009) by [Finance Act 2009 \(c. 10\)](#), [Sch. 33 para. 7](#)

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#### **502D Lessor under long funding finance lease making termination payment**

- (1) This section applies for determining the liability to corporation tax of a company which 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 computing the profits of the company.
- (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 company's rental earnings.

*Lessors under long funding operating leases*

#### **502E Lessor under long funding operating lease: periodic deduction**

- (1) This section applies for determining for the purposes of corporation tax the profits of a company for any period of account—
  - (a) for the whole of which, or
  - (b) for any part of which,the company is the lessor of any plant or machinery under a long funding operating lease.
- (2) A deduction is allowed in computing the profits of the company for the period of account.
- (3) The amount of the deduction for any period of account is to be determined as follows.
- (4) First, find the “relevant value” for the purposes of subsection (6)(a) below, 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;
  - (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 operating lease,the relevant value is the lower of first use market value and first use amortised value.

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(5) In subsection (4) above—

“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) above, subtract
  - (b) the amount which, at the commencement of the term of the lease, is (or, in a case falling within subsection (4)(e) above, 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.

## **502F Long funding operating lease: lessor's additional expenditure**

(1) This section applies if in any period of account—

- (a) a company is the lessor of any plant or machinery under a long funding operating lease,
- (b) the company 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.

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- (2) In a case falling within section 502E(4)(e) above, subsection (1)(c) above 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 computing the profits of the company for each post-expenditure period of account in which the company 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 company in relation to the leased plant or machinery;
  - “TRV” is the total of CRV and PRV.
- (6) Find RRV, where—
  - (a) if ARV exceeds TRV, RRV is the portion of the excess that is a result of the additional expenditure, but
  - (b) if ARV does not exceed TRV, 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.
- (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.

#### **502G Lessor under long funding operating lease: termination of lease**

- (1) This section applies for determining the liability to corporation tax of a company which is the lessor immediately before the termination of a long funding operating lease.

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- (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 502E(6)(a) (RV);
  - (b) the total of the deductions allowable under section 502E for periods of account for the whole or part of which the company 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 company which constitute additional expenditure for the purposes of section 502F in the case of the lease (TAE);
  - (b) the total of any deductions allowable under section 502F for periods of account for the whole or part of which the company 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 company 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 company in that period of account.
- (8) A profit or loss treated as arising to the company under subsection (6) or (7) above is to be treated—
  - (a) in the case of a profit, as income of the company attributable to the lease,
  - (b) in the case of a loss, as a revenue expense incurred by the company in connection with the lease.
- (9) In computing the profits of the company, no deduction is allowed in respect of any sums paid to the lessee that are calculated by reference to the termination value.

VALID FROM 21/07/2008

*Lessors under long funding finance or operating leases: avoidance etc*

**502GA Cases where ss. 502B to 502G do not apply: plant or machinery held as trading stock**

- (1) Sections 502B to 502G do not apply in the case of a company which is or has been the lessor of any plant or machinery under a long funding lease if the following condition is met.
- (2) The condition is that any part of the expenditure incurred by the company on the acquisition of the plant or machinery for leasing under the lease—

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- (a) is (apart from those sections) allowable as a deduction in calculating its profits or losses for the purposes of corporation tax, and
  - (b) is so allowable as a result of the plant or machinery forming part of its trading stock.
- (3) For the purposes of this section the cases in which expenditure incurred by a company on the acquisition of any plant or machinery for leasing under a lease is allowable as such a deduction include any case where—
- (a) the company becomes entitled to the deduction at any time after the expenditure is incurred, and
  - (b) the deduction arises as a result of the plant or machinery forming part of its trading stock at that time.
- (4) If—
- (a) at any time any of sections 502B to 502G has applied for determining the amounts to be taken into account in calculating the profits or losses of the company for the purposes of corporation tax, and
  - (b) the condition in subsection (2) is met at any subsequent time,
- those amounts, and any other amounts which (as a result of this section) are to be so taken into account, are subject to such adjustments as are just and reasonable.
- (5) All such assessments and adjustments of assessments are to be made as are necessary to give effect to subsection (4).

**[<sup>F2</sup>502GB Cases where ss. 502B to 502G do not apply: lessor also lessee under non-long funding lease**

- (1) This section applies if—
- (a) a company is the lessee of any plant or machinery under a lease (“lease A”) that is not a long funding lease,
  - (b) it enters into a lease (“lease B”) of any of that plant or machinery (as lessor), and
  - (c) lease B is a long funding lease.
- (2) Sections 502B to 502G do not apply in relation to lease B.
- (3) If by virtue of section 70H of the Capital Allowances Act (tax return by lessee treating lease as long funding lease) lease A becomes a long funding lease (and does not cease to be such a lease), treat this section as never having applied in relation to lease B.]

**Textual Amendments**

- F2** S. 502GB inserted (with effect in accordance with Sch. 20 para. 9(6) of the amending Act) by Finance Act 2008 (c. 9), Sch. 20 para. 9(3)

**[<sup>F3</sup>502GC Cases where ss. 502B to 502G do not apply: other avoidance**

- (1) Sections 502B to 502G do not apply in the case of a company which is or has been the lessor of any plant or machinery under a long funding lease if conditions A to C are met.

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- (2) Condition A is that the long funding lease forms part of any arrangement entered into by the company which includes one or more other transactions (whether the arrangement is entered into before or after or at the inception of the lease).
- (3) Condition B is that the main purpose, or one of the main purposes, of the arrangement is to secure that, over the relevant period, there would be a substantial difference between—
  - (a) the total amount of the amounts under the arrangement which are, in accordance with generally accepted accounting practice, recognised in determining the company's profit or loss for any period or taken into account in calculating the amounts which are so recognised, and
  - (b) the total amount of the amounts under the arrangement which are taken into account in calculating the profits or losses of the company for the purposes of corporation tax.
- (4) For the purposes of condition B “the relevant period” means the period which begins with the inception of the lease and ends with the end of the term of the lease.
- (5) Condition C is that the difference would be attributable (wholly or partly) to the application of any of sections 502B to 502G in relation to the company by reference to the plant or machinery under the lease.
- (6) The reference in this section to an amount being recognised in determining a company's profit or loss for a period is to an amount being recognised for accounting purposes—
  - (a) in the company's profit and loss account or income statement,
  - (b) in the company'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 calculating the company's profits and losses for that period.
- (7) For the purposes of this section it does not matter whether the parties to any transaction which forms part of the arrangement differ from the parties to any of the other transactions.
- (8) For the purposes of this section the cases in which two or more transactions are to be taken as forming part of an arrangement include any case in which it would be reasonable to assume that one or more of them—
  - (a) would not have been entered into independently of the other or others, or
  - (b) if entered into independently of the other or others, would not have taken the same form or been on the same terms.
- (9) If—
  - (a) at any time any of sections 502B to 502G has applied for determining the amounts to be taken into account in calculating the profits or losses of the company for the purposes of corporation tax, and
  - (b) conditions A to C are met at any subsequent time,
 those amounts, and any other amounts which (as a result of this section) are to be so taken into account, are subject to such adjustments as are just and reasonable.
- (10) All such assessments and adjustments of assessments are to be made as are necessary to give effect to subsection (9).]



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#### Textual Amendments

- F3** S. 502GC inserted (with effect in accordance with Sch. 20 para. 9(7) of the amending Act) by Finance Act 2008 (c. 9), Sch. 20 para. 9(4)

VALID FROM 21/07/2009

#### [<sup>F5</sup>502GI<sup>F4</sup> Cases where ss 502B to 502G do not apply: films]

- (1) If a company is or has been a lessor under a long funding lease of a film, sections 502B to 502G do not apply in respect of the lease.
- (2) “Film” has the same meaning as in Part 15 of CTA 2009 (see section 1181 of that Act).]

#### Textual Amendments

- F4** S. 502GA and preceding cross-heading inserted (with effect in accordance with Sch. 20 para. 9(5) of the amending Act) by Finance Act 2008 (c. 9), Sch. 20 para. 9(2)
- F5** S. 502GD inserted (with effect in accordance with Sch. 33 para. 3 of the amending Act) by Finance Act 2009 (c. 10), Sch. 33 para. 1

### *Insurance company as lessor*

#### **502H Insurance company as lessor**

- (1) This section applies to a company carrying on life assurance business if it is the lessor under a long funding lease in a period of account.
- (2) In this section—
  - (a) subsections (3) to (7) have effect in relation to—
    - (i) basic life assurance and general annuity business, and
    - (ii) long-term business which is not life assurance business, and
  - (b) subsections (8) to (10) have effect in relation to certain computations falling to be made in accordance with the provisions of this Act applicable to Case I of Schedule D.
- (3) Subsection (4) below applies in the case of each of the following amounts—
  - (a) an amount of rental earnings which the company is required by section 502B (long funding finance lease) to bring into account as taxable income,
  - (b) an amount treated under section 502C(3)(a) (long funding finance lease: lessor's exceptional items) as a profit arising to the company,
  - (c) an amount of rental income arising to the company from a long funding operating lease,
  - (d) an amount treated under section 502G(8)(a) (long funding operating lease: lessor's excess termination amount) as a profit arising to the company,
 but only if the leased asset is an asset of the company's long-term insurance fund.

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- (4) In determining for the purposes of the Corporation Tax Acts in any such case the extent to which any such amount is referable to—
- (a) basic life assurance and general annuity business, or
  - (b) long-term business which is not life assurance business,
- section 432A (apportionment of insurance companies' income) is to have effect in relation to the amount as it has effect in relation to the income arising from an asset.
- This subsection is subject to subsections (5) and (6) below.
- (5) Before applying subsection (4) above in a case where—
- (a) that subsection applies by virtue of subsection (3)(a) above in relation to an amount of rental earnings, and
  - (b) there is an amount which is deductible as a revenue expense by virtue of section 502C(3)(b) (long funding finance lease: lessor's exceptional items),
- the amount so deductible is to be given effect by applying it, so far as possible, in reducing the amount of the rental earnings.
- (6) Before applying subsection (4) above by virtue of subsection (3)(c) above in relation to an amount of rental income,—
- (a) any deduction falling to be made under section 502E, or
  - (b) any reduction falling to be made under section 502F,
- is to be given effect by applying it, so far as possible, in reducing (or further reducing) the amount of the rental income.
- (7) Where, after applying amounts in making reductions required by subsection (5) or (6) above, there remains unapplied an amount in respect of—
- (a) a deduction falling to be made under section 502E,
  - (b) a reduction falling to be made under section 502F, or
  - (c) an amount deductible as a revenue expense by virtue of section 502C(3)(b),
- the amount is to be apportioned under section 432A in the same way as income.
- (8) Where—
- (a) the leased asset is an asset of the company's long-term insurance fund, and
  - (b) a computation falling within subsection (9) below falls to be made,
- subsection (10) below applies to the computation.
- (9) A computation falls within this subsection if it is a computation of profits of—
- (a) life assurance business carried on by the company, or
  - (b) any category of life assurance business carried on by the company,
- and falls to be made in accordance with the provisions of this Act applicable to Case I of Schedule D.
- (10) In making the computation, no amount shall be brought into account by virtue of any of the following provisions—
- (a) section 502B (long funding finance lease: rental earnings),
  - (b) section 502C(3)(a) or (b) (long funding finance lease: profit or loss in respect of exceptional items),
  - (c) section 502E (long funding operating lease: periodic deduction),
  - (d) section 502F (long funding operating lease: lessor's additional expenditure),

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- (e) section 502G(8)(a) or (b) (long funding operating lease: lessor's profit or loss in respect of termination amount).

*Lessees under long funding finance leases*

**502I Lessee under long funding finance lease: limit on deductions**

- (1) This section applies for determining for the purposes of corporation tax the profits of a company for any period of account in which it is the lessee of any plant or machinery under a long funding finance lease.
- (2) In calculating the company'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 company'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) above applies as if the lease were one which, under generally accepted accounting practice, fell to be treated as a finance lease.

**502J Lessee under long funding finance lease: termination**

- (1) This section applies where—
  - (a) a company 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 company.
- (2) The payment is not to be brought into account in determining for the purposes of corporation tax the profits of the company for any period of account.
- (3) Subsection (2) above does not affect the amount of any disposal value that falls to be brought into account by the company under the Capital Allowances Act.

*Lessees under long funding operating leases*

**502K Lessee under long funding operating lease**

- (1) This section applies for determining for the purposes of corporation tax the profits of a company for any period of account in which it is the lessee of any plant or machinery under a long funding operating lease.
- (2) The deductions that may be allowed in computing the profits of the company for the period of account are to be reduced in accordance with the following provisions of this section.
- (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) below, which is—

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- (a) the market value of the plant or machinery at the commencement of the term of the lease, unless paragraph (b) below applies;
  - (b) if the lessee—
    - (i) has the use of 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) above—
- “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) above, subtract
  - (b) the amount which, at the commencement of the term of the lease, is (or, in a case falling within subsection (4)(b) above, 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.

### *Interpretation of Chapter]*

#### **502L Interpretation of this Chapter**

- (1) 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 the Capital Allowances Act;
  - “residual value”, in relation to any plant or machinery leased under a long funding operating lease, means—

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*Status:* Point in time view as at 11/05/2001. This version of this chapter contains provisions that are not valid for this point in time.

**Changes to legislation:** Income and Corporation Taxes Act 1988, Chapter 5A is up to date with all changes known to be in force on or before 31 May 2024. There are changes that may be brought into force at a future date. Changes that have been made appear in the content and are referenced with annotations. (See end of Document for details)

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- (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 the Capital Allowances Act (interpretation of provisions about long funding leases) applies in relation to this Chapter as it applies in relation to that Part.

**Status:**

Point in time view as at 11/05/2001. This version of this chapter contains provisions that are not valid for this point in time.

**Changes to legislation:**

Income and Corporation Taxes Act 1988, Chapter 5A is up to date with all changes known to be in force on or before 31 May 2024. There are changes that may be brought into force at a future date. Changes that have been made appear in the content and are referenced with annotations.