

CAPITAL ALLOWANCES BUYING AND ACCELERATION

DRAFT CLAUSE AND EXPLANATORY NOTE

Draft legislation is published today to prevent avoidance of corporation tax through schemes that use arrangements intended to crystallise a balancing allowance on plant or machinery used for the purposes of a trade. These schemes are designed to make the balancing allowance available to a profitable group not intending to carry on the trade for the long term.

The clause will have effect, for example, where a loss-making company is sold to an unconnected profitable group prior to the trade (rather than the company) being sold to a third party a short time later. The measure will prevent the sale of the trade leading to a balancing allowance in the hands of the profitable group.

The clause will have effect where a company sells its trade, and so ceases to carry it on, on or after 12 March 2008.

Enquiries and comments relating to the draft should be addressed to:

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DRAFT CLAUSE

Balancing allowances on transfers of trade: anti-avoidance

[XX](1) After section 343 of ICTA insert –

“343ZA Transfers of trade to obtain balancing allowances

- (1) This section applies where –
 - (a) a company (“the predecessor”) ceases to carry on a trade,
 - (b) another company (“the successor”) begins to carry on the activities of that trade as its trade or as part of its trade,
 - (c) in the accounting period in which the predecessor ceases to carry on the trade the predecessor would (apart from this section) be entitled under Part 2 of the Capital Allowances Act to a balancing allowance in respect of the trade, and
 - (d) the predecessor’s ceasing to carry on the trade is part of a scheme or arrangement the main purpose, or one of the main purposes, of which is to entitle the predecessor to that balancing allowance.
- (2) This section also applies where –
 - (a) a company (“the predecessor”) ceases to carry on part of a trade,
 - (b) another company (“the successor”) begins to carry on the activities of that part of the trade as its trade or as part of its trade, and
 - (c) the predecessor’s ceasing to carry on the part of the trade mentioned in paragraph (a) is part of a scheme or arrangement the main purpose, or one of the main purposes, of which is to entitle the predecessor, on cessation of the trade, to a balancing allowance in respect of the trade under Part 2 of the Capital Allowances Act.
- (3) This section does not apply where section 343 applies.
- (4) Where this section applies, the Corporation Tax Acts have effect subject to section 343(2), but as if the words “and are subject to section 343A (company reconstructions involving business of leasing plant or machinery)” were omitted.
- (5) Where this section applies because of subsection (1), and the successor carries on the activities of the trade the predecessor ceased to carry on as part of the successor’s trade, for the purposes of section 343(2) that part of the successor’s trade is to be treated as a separate trade carried on by the successor.
- (6) Where this section applies because of subsection (2), for the purposes of section 343(2) –
 - (a) that part of the trade which the predecessor ceased to carry on is to be treated as a separate trade carried on by the predecessor, and
 - (b) where the successor carries on the activities of that part of the trade as part of its trade, that part of the successor’s trade is to be treated as a separate trade carried on by the successor.

(7) Where subsection (5) or (6) applies, such apportionment of receipts, expenses, assets and liabilities is to be made as may be just.

(8) Section 343(10) applies to an apportionment under subsection (7) as it applies to an apportionment under section 343(9).”

(2) The amendment made by this section has effect in relation to the cessation of a trade or part of a trade on or after 12 March 2008.

DRAFT EXPLANATORY NOTE

SUMMARY

1. Clause XX will prevent avoidance of corporation tax using arrangements intended to crystallise a balancing allowance on the transfer of a trade.

DETAILS OF THE CLAUSE

2. Clause XX introduces new section 343ZA into the Income and Corporation Taxes Act 1988 (ICTA).
3. Subsection (1) introduces new section 343ZA into ICTA.
4. New section 343ZA prevents a balancing allowance arising on the transfer of a trade where the transfer is part of arrangements the main purpose, or one of the main purposes, of which is to create a balancing allowance.
 - a. Subsection (1) provides that the section applies where a company (referred to as “the predecessor”) transfers a trade to another company (referred to as “the successor”) which carries it on, either as its only trade or as part of a wider trade. However, it only applies in circumstances where the transfer is part of other arrangements where the main purpose or one of the main purposes is to generate a balancing allowance for the predecessor.
 - b. Subsection (2) provides that the section also applies in similar fashion where part of a trade, rather than the whole trade, is transferred.
 - c. Subsection (3) provides that the section does not apply where the transfer of the trade falls within the scope of section 343 of ICTA (company reconstructions without a change of ownership).
 - d. Subsection (4) is the main operative provision. Where the section applies the provisions of section 343(2) will apply (without being subject to section 343A). This will have the effect of treating the trade as if it had not ceased and commenced with the result that the predecessor will not be entitled to a balancing allowance but the successor will be entitled to claim capital allowances on a larger pool of expenditure than would have otherwise been the case.

- e. Subsection (5) provides that, where the section applies, because the whole of the predecessor's trade has been transferred, the successor is to be treated as carrying on the acquired trade as if it were a separate trade.
 - f. Subsection (6) makes similar provision to that in subsection (5) but it applies in circumstances where the section applies as a result of the transfer of only part of the predecessor's trade.
 - g. Subsection (7) provides that where it is necessary to make apportionments to give effect to subsection (5) or (6) they should be made on a just basis.
 - h. Subsection (8) imports the provisions of section 343(10), which describes the procedure for deciding questions in respect of an apportionment in the event that more than one company is affected by such a matter.
5. Subsection (2) provides that new section 343ZA applies to cessations of trade on or after 12 March 2008.

BACKGROUND NOTE

6. As a general rule, where a company ceases to carry on a trade, and where the market value of the plant or machinery used in the trade is less than its tax written down value, the company becomes entitled to a balancing allowance equal to the difference between the market value of the plant or machinery and its tax written down value. However, section 343 of ICTA provides that this general rule does not apply where a company (the predecessor) ceases to carry on a trade and the same trade begins to be carried on by another trader (the successor) where the two companies are under common control.
7. The avoidance this measure is designed to counter relies on a trading company being acquired by a profitable group and, as part of the arrangements, the trading company selling its trade to an unconnected buyer a short time later. When the company is acquired by the profitable group, capital allowances are unaffected. However, when the trade is sold, and if the market value of the plant or machinery is substantially less than its tax written down value, the existing rules can lead to a substantial balancing allowance that becomes available to the profitable group. This can accelerate the rate at which expenditure is written off for tax purposes.
8. The overall effect is that, as well as allowing the capital allowances to be used by a profitable group that has no long-term interest in the trade, they are available sooner than they would have been had the trading company simply been sold by the original owner to the ultimate buyer.
9. This new section will counter this avoidance.