

Corporation Tax: Bill 6
Leasing plant or machinery: the sales of lessors Chapters
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Part 1: Leasing plant or machinery

The sales of lessors Chapters

Overview

1. The paper with which this commentary is published presents Chapters rewriting Schedule 10 to FA 2006 (Sales etc of lessor companies etc) which are intended to form a Part of Bill 6 together with a Chapter rewriting Chapter 5A of Part 12 of ICTA (special rules for long funding leases of plant or machinery).

2. The expected structure of the Part is as follows:

- Chapter 1 will provide an introduction to the Part.
- Chapter 2 will rewrite Chapter 5A of Part 12 of ICTA.
- Chapters 3 to 5 will rewrite Schedule 10 to FA 2006.

3. This commentary relates to Chapters 1 and 3 to 5. Chapter 2 will be published for public consultation separately.

4. The commentary uses a number of abbreviations. They are listed below.

Bill 5 the draft Corporation Tax Bill published on 22 February 2008 (and references to numbered Parts, Chapters and clauses of, and Schedules to and paragraphs of Schedules to, Bill 5 are to the Parts, Chapters, clauses, Schedules and paragraphs so numbered in that draft)

CAA the Capital Allowances Act 2001

FA 2006 the Finance Act 2006 (and similarly for other Finance Acts)

HMRC Her Majesty's Revenue and Customs

ICTA the Income and Corporation Taxes Act 1988

ITA the Income Tax Act 2007

TCGA the Taxation of Chargeable Gains Act 1992.

Chapter 1: Introduction

Clause 1: Overview of Part

5. This clause provides an overview of the proposed Chapters of the Part and their subject matter. It is based on paragraph 1 of Schedule 10 to FA 2006.

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6. *Subsection (4)* defines the term “the sales of lessors Chapters” which is used throughout Chapters 3 to 5 and *subsections (5) to (7)* introduce, and provide signposts to the definitions of, a “qualifying change of ownership” and a “qualifying change in a company’s interest in a business”. These are the events which give rise to charges and reliefs under the sales of lessors Chapters.

Chapters 3 to 5: The sales of lessors Chapters

Overview

7. The sales of lessors Chapters, based on Schedule 10 to FA 2006, are designed to deter arrangements which have the effect of converting the corporation tax deferral arising from the availability of capital allowances to companies which carry on a business of leasing plant or machinery into a permanent deferral of tax.

8. Capital allowances on plant or machinery generally write off expenditure at 20% a year (25% for periods ending before 1 April 2008) on a reducing balance basis. Where the lessor is entitled to the allowances and the lease term is in excess of about five years, the capital allowances exceed the rental income in the early years of the lease. This generates tax losses. Once the capital allowances are exhausted, the lease moves to a tax profitable second phase. Over the life of the lease, the profits charged to tax equal the commercial profits.

9. Usually the group of which the leasing company forms part can take advantage of the losses in early years by surrender of group relief.

10. The mischief arises if the leasing company leaves the group when the business is about to become tax profitable and becomes a member of a loss making group which can shelter the subsequent rental income from tax by surrendering to the leasing company losses which it would not otherwise be able to use.

11. Any capital profit made by the selling group on the disposal of the shares in the subsidiary will typically not be taxable in the hands of the selling group, because it is a disposal of a substantial shareholding (see Schedule 7AC to TCGA). The selling group thus retains the benefit of the tax losses on a permanent basis, as well as receiving any consideration given for the sale of the income stream free of tax.

12. Similar arrangements can be made where the leasing company is a consortium company or the company carries on the leasing business in partnership with others. The sales of lessors Chapters also counter arrangements which operate by way of changes in the constituents of the consortium or in the members of the partnership or in the respective interests of the consortium members or partners in the leasing company or business.

13. The sales of lessors Chapters counter these arrangements by imposing a charge to corporation tax on the leasing company on any day:

- if there is a qualifying change of ownership of the company on that day or

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- in a case where the leasing business is carried on by the company in partnership, if there is a qualifying change on that day in the company's interest in the business.

14. The tax charge is broadly equivalent to the tax benefit enjoyed down to that day and the rules are designed to ensure that it is borne by the selling group.

15. In the case of a qualifying change in the ownership of the leasing company, a relief equivalent to the charge is given to the company on the day after the qualifying change and the rules ensure that the relief can only be accessed by the buying group. In the case of a qualifying change in the company's interest in a business carried on in partnership, relief is given to the other partner companies whose interest in the business carried on in partnership has increased.

16. The effect of this is that a tax-driven sale to a loss maker is unattractive as the charge recovers the tax benefits taken by the selling group and a loss making buying group will have no interest in an additional relief which merely increases its tax losses.

17. The intended tax effect on a commercially driven sale to another (profitable) group is that it should be broadly neutral, as the charge and the relief cancel each other out. The relief is valuable to the profit making buying group and so it can be expected that the price paid will reflect this and compensate the selling group for the tax charge.

18. It has been recognised that there are situations where this intention is not fully achieved. One such case has been addressed by the amendments to Schedule 10 to FA 2006 made by section 56 of FA 2008. On 29 July 2008, HMRC announced that it had prepared a discussion document addressing some other such issues with a view to considering changes to the legislation. A copy of the discussion document can be obtained on application by following the links at:

<http://www.hmrc.gov.uk/news/lessor-companies.htm>.

19. Where the discussion document considers amendment of the source legislation, this is noted in the commentary on the relevant clause.

Chapter 3: Sales of lessors: leasing business carried on by a company alone

Overview

20. This Chapter deals with cases where a leasing business is carried on by a company alone. Chapter 4 deals with cases where the business is carried on by one or more companies in partnership with others.

Clause 2: Income and matching expense in different accounting periods

21. This clause provides for an accounting period to end if there is a "qualifying change of ownership" in relation to a company within the charge to corporation tax

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carrying on a business of leasing plant or machinery otherwise than in partnership. It is based on paragraph 3 of Schedule 10 to FA 2006.

22. On the day the accounting period ends the company is treated as receiving an amount of income which is brought into account for that accounting period for corporation tax purposes. See *subsections (2) and (3)*.

23. On the following day the company is treated as incurring an expense which is brought into account for a new accounting period for corporation tax purposes. See *subsections (4) and (5)*.

Clause 3: Amount of income and expense

24. This clause contains a signpost to the clauses which contain the provisions for calculating the amount of the income to be brought into account in accordance with clause 2(2) and (3) and provides that the amount of the expense to be brought into account in accordance with clause 2(4) and (5) is the same as the amount of the income. It is based on paragraph 4 of Schedule 10 to FA 2006.

Clause 4: No carry back of the expense

25. This clause prevents any loss which arises in the later accounting period which derives from the expense from being carried back against profits of any earlier accounting period under the provisions of section 393A(1)(b) of ICTA. It is based on paragraph 5 of Schedule 10 to FA 2006.

26. Section 393A of ICTA is to be rewritten in this Bill. See clause 3[j4505rm](3)(b) published on 8 November 2007 under committee paper CC/SC (07) 38: Losses.

Clause 5: Relief for expense under section 2 otherwise giving rise to carry forward loss

27. This clause provides for the carrying forward of the expense to a later accounting period. It is based on paragraph 39 of Schedule 10 to FA 2006.

28. The clause applies if the company makes a loss in the accounting period which, in accordance with clause 2(4)(b), begins on the day after the qualifying change of ownership. In that case, the loss derived from the expense treated as incurred under clause 2(4)(a), which could otherwise only be carried forward and applied against the profits of the company's leasing trade, is instead to be treated as an expense of the next accounting period and so available for group relief in that period. This is subject to the condition in *subsection (1)(e)*.

29. Paragraph 39 of Schedule 10 to FA 2006 applies for the purposes of:

- paragraph 3 of that Schedule, in a case where the company carries on the leasing business alone; and

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- paragraphs 23(4A) and 33 of that Schedule, in a case where the company carries on the business in partnership.

30. It has been rewritten here for the purposes only of clause 2. It has also been rewritten in two places in Chapter 4: in clause 32 for the purposes of clause 30(5) and in clause 42 for the purposes of clause 39. It is considered that it is helpful to paint the complete picture in each Chapter rather than include the provision in Chapter 5 (sales of lessors: miscellaneous) and provide signposts.

Q1. We welcome comments on the proposal to rewrite paragraph 39 of Schedule 10 to FA 2006 separately in clause 5 for the purposes of clause 2, in clause 32 for the purposes of clause 30(5) and in clause 42 for the purposes of clause 39.

31. The discussion document seeks views on whether, and if so how, this provision should be amended to cater for cases where the buyer or the purchasing group has insufficient profits in the 24 months following the sale against which to set the relief.

Clause 6: Meaning of “business of leasing plant or machinery”

32. This clause, read with clauses 7 to 9, defines the term “business of leasing plant or machinery” for the purposes of Chapter 3. It is based on paragraph 6 of Schedule 10 to FA 2006.

Clause 7: Provision for the purposes of condition A in section 6

33. This clause sets out the method of calculating the accounting value of the plant or machinery owned by the company on any day for the purposes of condition A in clause 6(3). It is based on paragraph 7(1) to (3) of Schedule 10 to FA 2006.

Clause 8: Provision supplementing section 7

34. This clause contains further details of the basis of the calculation to be made in accordance with clause 7. It is based on paragraph 7(4) to (8) of Schedule 10 to FA 2006.

35. The discussion document proposes a technical amendment to paragraph 7(8)(b) of Schedule 10 to FA 2006, on which *subsection (5)(b)* is based, to alleviate a potential adverse effect of this provision in the case of acquisitions before 5 December 2005.

36. Paragraph 7(9) of Schedule 10 to FA 2006 is spent and has not been rewritten.

Clause 9: Provision for the purposes of condition B in section 6

37. This clause provides for the way in which income is to be calculated for the purposes of condition B in clause 6(5). It is based on paragraph 8 of Schedule 10 to FA 2006.

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Clause 10: Meaning of a “qualifying change of ownership”

38. This clause, read with clauses 11 to 15, determines what constitutes a “qualifying change of ownership” for the purposes of the sales of lessors Chapters. It is based on paragraph 10 of Schedule 10 to FA 2006.

39. A qualifying change of ownership is a “relevant change” in the relationship between the company carrying on a business of leasing plant or machinery (“A”) and its principal company. Clause 11 determines what constitutes a “relevant change” where the relationship between A and its principal company is that of subsidiary and parent and clause 12 deals with the case where the relationship is that of A and a member (or the parent company of a member) of a consortium, directly or indirectly, owning A.

40. A qualifying change of ownership triggers A being treated as receiving income and incurring a matching expense not only for the purposes of clause 2 in Chapter 3 where it carries on the business alone but also for the purposes of clause 39 in Chapter 4 where it carries on the business in partnership.

Clause 11: Qualifying 75% subsidiaries

41. This clause defines the relationship between a principal company and its subsidiary and determines what constitutes a “relevant change” in that relationship for the purposes of clause 10. It is based on paragraph 11 of Schedule 10 to FA 2006.

42. A company is only capable of being a principal company if it is not itself a 75% subsidiary of another company (see *subsections (1)(b), (3)(c) and (5)*).

43. A company carrying on a business of leasing plant or machinery (“A”) has another company (“B”) as its principal company if A is a qualifying 75% subsidiary, as defined in clause 15, of B unless B is a qualifying 75% subsidiary of another company (see *subsection (1)*).

44. If B is a 75% subsidiary of another company (“C”), then C is the principal company of A. But if C is a 75% subsidiary of another company (“D”), then D is the principal company of A. And so on.

45. There is a “relevant change” in the relationship of A and the principal company if the relationship of A to the principal company ceases to be that of a qualifying 75% subsidiary or the chain of 75% qualifying subsidiaries is broken (see *subsections (2), (4) and (6)*).

Clause 12: Consortium relationships

46. This clause defines the relationship between a company carrying on a business of leasing plant or machinery (“A”) and a principal company of A where A is owned, directly or indirectly, by a consortium and determines what constitutes a “relevant change” in that relationship for the purposes of clause 10. It is based on paragraph 12 of Schedule 10 to FA 2006.

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47. This clause applies if A is either owned by a consortium or is a qualifying 90% subsidiary of a company owned by the consortium (see *subsections (1)(b) and (5)(b)*).

48. A company is only capable of being a principal company if it is not itself a 75% subsidiary of another company (see *subsections (1), (5) and (7)*).

49. Each company which is a member of the consortium (“E”) is a principal company of A unless it is a qualifying 75% subsidiary of another company (see *subsection (1)*).

50. If E is a 75% subsidiary of another company (“F”), then F is the principal company of A. But if F is a 75% subsidiary of another company (“G”), then G is the principal company of A. And so on.

51. There is a “relevant change” in the relationship of A and a principal company on any day if E’s “ownership proportion” is less at the end of the day than it was at the start of the day (see *subsections (2), (6)(a) and (8)*).

52. E’s ownership proportion is measured by reference to the lowest of E’s interest in the share capital of A, A’s profits available for distribution and A’s assets available on a winding up (see *subsection (3)*), except where A is a qualifying 90% subsidiary of a company owned by the consortium. In that case it is E’s interest in the company of which A is a qualifying 90% subsidiary which is measured (see *subsection (4)*).

53. The term “ownership proportion” has been substituted for the term “relevant fraction” in paragraph 12 of Schedule 10 to FA 2006. Similarly “proportion” has been used in place of “percentage”. This change in language follows the change in language to be used in rewriting section 403C of ICTA (amount of relief in consortium cases) in this Bill. See clauses 47[j4807rm] and 48[j4807AArm] published on 6 September 2007 under committee paper CC/SC (07) 27: Group relief, and the Response Document published on 28 March 2008.

54. If a company other than E is the principal company of A in relation to E’s membership of the consortium, there is also a “relevant change” in the relationship of A and the principal company if E ceases to be a qualifying 75% subsidiary of the other company or the chain of 75% qualifying subsidiaries between the other company and E is broken (see *subsections (6)(b) and (8)(b)*).

Clause 13: No qualifying change of ownership in the case of certain intra-group reorganisations

55. This clause ensures that there is no qualifying change of ownership of A in the case of certain group reorganisations. It is based on paragraph 13 of Schedule 10 to FA 2006.

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56. The group reorganisations in question are ones following which A and all other companies involved remain qualifying 75% subsidiaries of the same principal company as before the reorganisation.

57. The discussion document proposes that similar provision be made in the case of reorganisations involving consortium companies where there is no change in the ultimate ownership of the interest in the consortium.

Clause 14: Meaning of “company owned by a consortium” etc

58. This clause defines what a company owned by a consortium means and who are the members of the consortium in relation to that company. It is based on paragraph 14 of Schedule 10 to FA 2006.

59. The clause applies for the purposes of the sales of lessors Chapters.

Clause 15: Meaning of “qualifying 75% or 90% subsidiary” etc

60. This clause sets out the tests for determining whether a company is a “qualifying 75% subsidiary” or a “qualifying 90% subsidiary” of another company. It is based on paragraph 15 of Schedule 10 to FA 2006.

61. The clause applies for the purposes of the sales of lessors Chapters.

62. Paragraph 15 of Schedule 10 to FA 2006 uses the same approach as is used for determining whether companies are in the same group for group relief purposes but with a modification. This is that companies without share capital, such as companies limited by guarantee, can be treated as subsidiaries if they fall to be treated as controlled by another company. Such companies are also accommodated by applying Schedule 18 to ICTA to treat their members as if they were equity holders.

63. Paragraph 15(1)(b) of Schedule 10 to FA 2006 defines control by reference to section 840 of ICTA. That definition is to be rewritten in this Bill, which will also include a clause equivalent to section 1021(2) of ITA applying that definition for the purposes of this Bill unless otherwise indicated. The reference to section 840 of ICTA in paragraph 15(1)(b) of Schedule 10 to FA 2006 has not, therefore, been rewritten in *subsection (3)*.

64. *Subsection (7)* cross-refers to the Chapter of this Bill rewriting Schedule 18 to ICTA (see the draft clauses published on 6 September 2007 under committee paper CC/SC (07) 27: Group relief). In those draft clauses, clauses 47[j4807rm] and 48[j4807AArm] are the two sections respectively referred to in *subsection (7)(a)* and clause 55[j4800Brm] is the section referred to in *subsection (7)(b)*.

Clause 16: The amount of the income: the basic amount

65. This clause gives the formula for determining the basic amount of income which is then to be adjusted in accordance with clauses 20 to 22 to determine the

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amount of income for the purposes of clause 2 on any day (“the relevant day”). It is based on paragraph 16 of Schedule 10 to FA 2006.

Clause 17: Meaning of “PM” in section 16

66. This clause determines the amount which is “PM” in the formula in clause 16 on the relevant day. It is based on paragraph 17(1) and (2) of Schedule 10 to FA 2006.

67. PM is the amount of the net book value (or carrying amount) of the plant or machinery plus the amount of the net investment in respect of finance leases of the plant or machinery on the “appropriate balance sheet” of the leasing company at the start of the relevant day (see *subsection (3)(a)* and clause 18). To this is added the amounts shown in the appropriate balance sheet of any associated company in respect of any plant or machinery which is transferred to the leasing company on that day (see *subsection (3)(b)*).

68. When calculating these amounts any plant or machinery that represents expenditure on plant or machinery that was not qualifying expenditure for the purposes of Part 2 of CAA as a consequence of section 34A or section 67 of that Act is excluded (see *subsection (2)(a)* and *(b)*). This exclusion ensures that a charge is not calculated when the company is prevented from claiming capital allowances because the asset is subject to a long funding lease or a hire purchase or similar contract.

69. *Subsection (2)(c)* is new. It provides a link to clause 23 which requires plant or machinery to be ignored in certain circumstances.

Clause 18: Provisions supplementing section 17

70. This clause contains further details of the basis of the calculation to be made in accordance with clause 17 and gives the meaning of “the amounts shown in the appropriate balance sheet” in relation to the leasing company or an associated company. It is based on paragraph 17(3) to (7) of Schedule 10 to FA 2006.

71. It is expected that, if the technical amendment to paragraph 7(8)(b) of Schedule 10 to FA 2006 mentioned in the commentary on clause 8 is made, an equivalent amendment will be made to paragraph 17(7)(b) of that Schedule, on which *subsection (5)(b)* is based.

Clause 19: Meaning of “TWDV” in section 16

72. This clause determines the amount which is “TWDV” in the formula in clause 16 on the relevant day. It is based on paragraph 18 of Schedule 10 to FA 2006.

73. The TWDV amount is made up of the unrelieved qualifying expenditure in all single asset, class pools and the main pool. This is the amount at the start of the new accounting period following the relevant day but excludes any expenditure on the acquisition of plant or machinery on the relevant day except for plant or machinery acquired from associated companies. This adjustment ensures that amounts in respect

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of plant and machinery acquired from associated companies on the relevant day are included in both the PM and the TWDV amounts.

Clause 20: Amount to be nil if basic amount negative

74. This clause ensures that, if the formula in clause 16(3) produces a negative basic amount, the amount of the company's income for the purposes of clause 2 is nil. It is based on paragraph 19 of Schedule 10 to FA 2006.

Clause 21: Adjustment to basic amount: qualifying 75% subsidiaries

75. This clause makes an adjustment to the basic amount when the company ceases to be a 75% subsidiary and becomes instead a consortium company or a qualifying 90% subsidiary of a consortium company. It is based on paragraph 20 of Schedule 10 to FA 2006.

76. In these circumstances the basic amount is reduced to reflect the change in the economic control of the lessor company. The amount of the income is limited to the "appropriate percentage" of the basic amount, that is the difference between 100 per cent and the "ownership percentage" after the qualifying change of ownership (see *subsections (4) and (5)*).

77. The term "ownership percentage" has been substituted for the term "relevant fraction" in paragraph 20 of Schedule 10 to FA 2006 and corresponds to the use of the term "ownership proportion" in clauses 12 and 22.

Clause 22: Adjustment to basic amount: consortium relationships

78. This clause makes an adjustment to the basic amount when the trigger event is a change in a consortium relationship. It is based on paragraph 21 of Schedule 10 to FA 2006.

79. If the qualifying change of ownership arises only because the ownership proportion (as defined in clause 12(3) and (4)) at the end of the day is less than the ownership proportion at the start of the day (see clause 12(2)), the amount of the income is limited to the "appropriate proportion" of the basic amount. The "appropriate proportion" is found by deducting the ownership proportion at the start of the day from the ownership proportion at the end of the day.

80. In cases where clause 12(6) or (8) applies, the amount of the income is limited to the ownership proportion of the basic amount at the start of the day.

Clause 23: Migration

81. This clause deals with situations where a company comes within the charge to corporation tax as a result of migration into the United Kingdom. It is based on paragraph 22 of Schedule 10 to FA 2006.

82. The clause prevents the migration of a company into the United Kingdom which is coupled with a qualifying change of ownership on the same day giving rise

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to an expense in its first accounting period in relation to plant or machinery owned by the company before its migration.

Clause 24: Meaning of associated company

83. This clause gives the meaning of “associated company” for the purposes of Chapter 3 only. It is based on paragraph 9 of Schedule 10 to FA 2006.

84. In *subsection (3)* the reference to section 416 of ICTA will in due course be replaced by a reference to the clause of this Bill rewriting that section. See clause 4[j7416] in the draft clauses published on 12 September 2008 under committee paper CC/SC (08) 38: Close companies.

Chapter 4: Sales of lessors: leasing business carried on by a company in partnership

Overview

85. This Chapter deals with cases where the company is carrying on a leasing business in partnership with others. It is necessary to provide not only for changes in the ownership of the company itself but also for changes to the partners’ interests in the partnership business, including the introduction and retirement of partners and changes in profit sharing ratios.

86. This Chapter is based on Part 3 of Schedule 10 to FA 2006. The opportunity has been taken to set out in full certain provisions which in the source legislation operate by applying provisions of Part 2 with modifications. See clauses 26 to 29 which restate in full the provisions of paragraphs 6 to 8 of Schedule 10 to FA 2006 as modified by paragraph 25 of that Schedule.

87. Clauses 30 to 38 deal with changes in the partnership and clauses 39 to 43 deal with changes in the ownership of a company carrying on business in partnership.

Clause 25: Introduction to Chapter

88. This clause introduces the Chapter and contains signposts to its principal provisions. It is based on paragraphs 23(1), 25(1) and (2) and 33(1) of Schedule 10 to FA 2006.

89. The source legislation provides no such introduction to Part 3 of Schedule 10 to FA 2006. It is considered helpful to have an introduction so as to highlight the two events which may give rise to a charge and relief where a company carries on a leasing business in partnership.

Q2. We welcome comments on the inclusion of clause 25.

Clause 26: Partnerships: meaning of “business of leasing plant or machinery”

90. This clause, read with clauses 27 to 29, defines the term “business of leasing plant or machinery” for the purposes of Chapter 4. It is based on paragraph 25 of Schedule 10 to FA 2006.

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91. This clause restates in full the provisions of paragraph 6 of Schedule 10 to FA 2006 as applied by paragraph 25(1) and modified by paragraph 25(2) of that Schedule.

92. Paragraph 25(2) of Schedule 10 to FA 2006 provides that:

Any reference in [paragraphs 6 to 8] to the relevant company is to be read as a reference to the partnership.

93. Paragraph 6(5) of Schedule 10 to FA 2006 refers to “any company” and “the company”. Although paragraph 25(2) of Schedule 10 to FA 2006 does not explicitly modify those references, it is implicit that for the purposes of Part 3 of that Schedule those references must include the partnership. This has been made explicit by including in *subsection (6)* references to the partnership, as well as the references to a company and the company.

Clause 27: Provision for the purposes of condition A in section 26

94. This clause sets out the method of calculating the accounting value of the plant or machinery which the partnership owns on any day for the purposes of condition A in clause 26(2). It is based on paragraph 25 of Schedule 10 to FA 2006.

95. This clause restates in full the provisions of paragraph 7(1) to (3) of Schedule 10 to FA 2006 as applied by paragraph 25(1) and modified by paragraph 25(2) and (3) of that Schedule.

96. *Subsection (3)* does, however, omit the closing words of paragraph 7(3) of Schedule 10 to FA 2006 on the basis that, because of the references to “on the relevant day” in paragraph 25(3)(b) and (e) of that Schedule (modifying the meaning of “associated company”), those words are unnecessary for the modified paragraph 7(3).

Clause 28: Provision supplementing section 27

97. This clause contains further details of the basis of the calculation to be made in accordance with clause 27. It is based on paragraph 25 of Schedule 10 to FA 2006.

98. This clause restates in full the provisions of paragraph 7(4) to (8) of Schedule 10 to FA 2006 as applied by paragraph 25(1) and modified by paragraph 25(2) of that Schedule. Paragraph 7(9) of Schedule 10 to FA 2006 is spent and has not been rewritten.

99. Explicit effect has been given to the implicit modifications made by paragraph 25(2) of Schedule 10 to FA 2006 to paragraph 7(4), (7) and (8) of that Schedule, by including in *subsections (1), (4) and (5)* references to the partnership, as well as to any company, a company or the company. See the commentary on clause 26.

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100. The discussion document proposes a technical amendment to paragraph 7(8)(b) of Schedule 10 to FA 2006, on which *subsection (5)(b)* is based, to alleviate a potential adverse effect of this provision in the case of acquisitions before 5 December 2005.

Clause 29: Provision for the purposes of condition B in section 26

101. This clause provides for the way in which the partnership's income is to be calculated for the purposes of condition B in clause 26(4). It is based on paragraph 25 of Schedule 10 to FA 2006.

102. This clause restates in full the provisions of paragraph 8 of Schedule 10 to FA 2006 as applied by paragraph 25(1) and modified by paragraph 25(2) of that Schedule.

Clause 30: Change in company's interest in business: income treated as received etc

103. This clause provides for the consequences of a "qualifying change" on any day in a company's interest in a leasing business carried on by it in partnership. It is based on paragraph 23 of Schedule 10 to FA 2006.

104. A "qualifying change" is defined in clause 33 and occurs if there is a reduction in the company's interest in the business.

105. On the day of the qualifying change, the company is treated as receiving an amount of income and the other companies carrying on the business are treated as incurring an expense. In this case, there is no ending of an accounting period such as in clause 2. The income and expense are recognised in the accounting period of the company which relates to the day of the qualifying change.

106. In relation to a company carrying on the business in partnership, the income or expense is treated for corporation tax purposes as a receipt or expense of the company's "notional business" (see *subsection (6)* which cross-refers to section 114(2) of ICTA). Section 114(2) of ICTA has been rewritten in clauses 1186 to 1189 of Bill 5 in a way which dispenses with the concept of notional business. All references to notional business in Schedule 10 to FA 2006 are to be consequentially amended. This clause will then be amended accordingly.

107. If a single company is carrying on the business alone after the qualifying change, *subsection (5)* provides that the expense is treated as incurred by it at a time when it is carrying the business alone and is allowed as a deduction in calculating the profits of the business for the accounting period in which it is treated as incurred.

Clause 31: Amount of income and expense

108. This clause contains a signpost to the clauses which contain the provisions for calculating the amount of the income to be brought into account in accordance with clause 30(2)(a) and (3) and to the clause determining the amount of the expense to be

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brought into account in accordance with clause 30(2)(b) and (4) or (5). It is based on paragraph 24 of Schedule 10 to FA 2006.

Clause 32: Relief for expenses under section 30(5) otherwise giving rise to carried forward loss

109. This clause applies where a single company succeeds to a partnership business and provides for the carrying forward of the expense incurred by the company to a later accounting period. It is based on paragraph 39 of Schedule 10 to FA 2006.

110. The clause applies if the company makes a loss in the accounting period in which it begins to carry on the business alone. In that case, the loss derived from the expense treated as incurred under clause 30(5)(a), which could otherwise only be carried forward and applied against the profits of the company's leasing trade, is instead to be treated as an expense of the next accounting period and so available for group relief in that period.

111. Paragraph 39 of Schedule 10 to FA 2006 applies for the purposes of:

- paragraph 3 of that Schedule, in a case where the company carries on the leasing business alone; and
- paragraphs 23(4A) and 33 of that Schedule, in a case where the company carries on the business in partnership.

112. It has been rewritten here for the purposes only of clause 30(5), It has also been rewritten in clause 5 for the purposes of clause 2 and in clause 42 for the purposes of clause 39. It is considered that it is helpful to paint the complete picture in each Chapter rather than include the provision in Chapter 5 (Sales of lessors: miscellaneous) and provide signposts.

113. The discussion document seeks views on whether, and if so how, this provision should be amended to cater for cases where the buyer or the purchasing group has insufficient profits in the 24 months following the sale against which to set the relief.

Clause 33: Meaning of “qualifying change” in company's interest in a business

114. This clause defines a “qualifying change” in a company's interest in a business by reference to a reduction in its “percentage share” in the profits or loss of the business. It is based on paragraph 27 of Schedule 10 to FA 2006.

Clause 34: Determining the percentage share in the profits or loss of business

115. This clause provides that a company's “percentage share” in the profits or loss of the business is to be determined on a just and reasonable basis but with due regard to the determination of the partner's share for the purposes of section 114(2) of ICTA. It is based on paragraph 28 of Schedule 10 to FA 2006.

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116. Section 114(2) of ICTA has been rewritten in clauses 1186 to 1189 of Bill 5.

Clause 35: The amount of the income: the basic amount

117. This clause gives the formula (PM – TWDV) for determining the basic amount of income of the partnership which is then to be adjusted in accordance with clause 36 or 37 to determine the amount of income of the company for the purposes of clause 30 on any day (“the relevant day”). It is based on paragraph 29 of Schedule 10 to FA 2006.

118. *Subsection (4)* applies the definition of PM in clause 17 with modifications. See the commentary on that clause and clause 18.

119. *Subsection (5)* determines the amount which is TWDV.

120. The TWDV amount is made up of the unrelieved qualifying expenditure in all single asset, class pools and the main pool. This is the amount that would be carried forward assuming that a chargeable period ends on the relevant day and a new one begins on the following day (see *subsection (6)(a)*).

121. But any expenditure on the acquisition of plant or machinery on the relevant day is excluded, except for plant or machinery acquired from associated companies (see *subsection (6)(b)*). This adjustment ensures that amounts in respect of plant and machinery acquired from associated companies on the relevant day are included in both the PM and the TWDV amounts.

Clause 36: Amount to be nil if basic amount negative

122. This clause ensures that, if the formula in clause 35(3) produces a negative basic amount, the amount of the company’s income for the purposes of clause 30 is nil. It is based on paragraph 30 of Schedule 10 to FA 2006.

Clause 37: Adjustment to the basic amount

123. This clause limits the amount of the company’s income for the purposes of clause 30 to a percentage of the basic amount. It is based on paragraph 31 of Schedule 10 to FA 2006.

124. The percentage of the basic amount is found by deducting the company’s percentage share in the profits or loss of the partnership at the end of the day from its percentage share at the beginning of the day.

Clause 38: The amount of expense

125. This clause determines the amount of expense treated as incurred by a company in accordance with clause 30(2)(b) as the result of a qualifying change in the partner company’s interest in the business on any day. It is based on paragraph 32 of Schedule 10 to FA 2006.

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126. Except where a single company is carrying on the business at the end of the day, the amount of the expense is determined by reference to any increase of the company's percentage interest in the profits or loss of the partnership which is attributable to the qualifying change in the interest in the business of the partner company (see *subsections (2) and (3)*).

127. The amount of the expense is expressed as a percentage of "the amount of the income". There is doubt that this achieves the intention of the legislation that the amount of the relief should in total equate to the full potential amount of income. The discussion document proposes a technical amendment to ensure that the legislation operates as intended.

128. Where a single company is carrying on the business at the end of the day, the amount of the expense is equal to the amount of the income (see *subsection (4)*).

Clause 39: Income and matching expense in different accounting periods

129. This clause provides for an accounting period to end if there is a "qualifying change of ownership" in relation to a company within the charge to corporation tax carrying on a business of leasing plant or machinery in partnership. It is based on paragraph 33 of Schedule 10 to FA 2006.

130. This clause is the equivalent of clause 2 which applies where the company is carrying on the business alone. "Qualifying change of ownership" has the same meaning in this clause as it does in clause 2 (see clauses 10 to 15).

131. On the day the accounting period ends the company is treated as receiving an amount of income which is brought into account in calculating the profits of the company's "notional business" (see the commentary on clause 30) for that accounting period for corporation tax purposes. See *subsections (2) and (3)*.

132. On the following day the company is treated as incurring an expense which is brought into account in calculating the profits of the company's "notional business" for a new accounting period for corporation tax purposes. See *subsections (4) and (5)*.

Clause 40: Amount of income and expense

133. This clause contains a signpost to the clause which contains the provisions for calculating the amount of the income to be brought into account in accordance with clause 39(2) and (3) and provides that the amount of the expense to be brought into account in accordance with clause 39(4) and (5) is the same as the amount of the income. It is based on paragraph 34 of Schedule 10 to FA 2006.

Clause 41: No carry back of the expense

134. This clause prevents any loss which arises in the later accounting period which derives from the expense from being carried back against profits of any earlier accounting period under the provisions of section 393A of ICTA. It is based on paragraph 35 of Schedule 10 to FA 2006.

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135. Section 393A of ICTA is to be rewritten in this Bill. See clause 3[j4505rm](3)(b) published on 8 November 2007 under committee paper CC/SC (07) 38: Losses.

Clause 42: Relief for expense under section 39 otherwise giving rise to carry forward loss

136. This clause provides for the carrying forward of the expense to a later accounting period. It is based on paragraph 39 of Schedule 10 to FA 2006.

137. The clause applies if the company makes a loss in its notional business in the accounting period which, in accordance with clause 39(4)(b), begins on the day after the qualifying change of ownership. In that case, the loss derived from the expense treated as incurred under clause 39(4)(a), which could otherwise only be carried forward and applied against the profits of the company's leasing trade, is instead to be treated as an expense of the next accounting period and so available for group relief in that period. This is subject to the condition in *subsection (1)(e)*.

138. Paragraph 39 of Schedule 10 to FA 2006 applies for the purposes of:

- paragraph 3 of that Schedule, in a case where the company carries on the leasing business alone; and
- paragraphs 23(4A) and 33 of that Schedule, in a case where the company carries on the business in partnership.

139. It has been rewritten here for the purposes only of clause 39. It has also been rewritten in clause 5 for the purposes of clause 2 and in clause 32 for the purposes of clause 30(5). It is considered that it is helpful to paint the complete picture in each Chapter rather than include the provision in Chapter 5 (Sales of lessors: miscellaneous) and provide signposts.

140. The discussion document seeks views on whether, and if so how, this provision should be amended to cater for cases where the buyer or the purchasing group has insufficient profits in the 24 months following the sale against which to set the relief.

Clause 43: The amount of the income

141. This clause sets out the rules for determining the amount of the company's income for the purposes of clause 39 on any day. It is based on paragraph 36 of Schedule 10 to FA 2006.

142. The rules adopt concepts from Chapters 3 and 4 for this purpose. The basic amount is found in accordance with clause 35 in Chapter 4 and is then adjusted in accordance with clauses 20 to 22 in Chapter 3. The "appropriate percentage" of the adjusted amount is then taken.

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143. *Subsection (5)* ensures that, if on the same day there is also a “qualifying change” in the company’s interest in the business carried on by the partnership, the percentage share in relation to which the amount of income under clause 30 is calculated is not also taken into account in calculating the income under clause 39.

Clause 44: Meaning of “associated company”

144. This clause gives the meaning of “associated company” for the purposes of Chapter 4 only. It is based on paragraph 26 of Schedule 10 to FA 2006.

145. In *subsection (3)* the reference to section 416 of ICTA will in due course be replaced by a reference to the clause of this Bill rewriting that section. See clause 4[j7416] in the draft clauses published on 12 September 2008 under committee paper CC/SC (08) 38: Close companies.

146. This clause is substantially similar to clause 24 which gives the meaning of “associated company” for the purposes of Chapter 3 but includes additional provisions in *subsection (5)* for the case where the company is a consortium company and there is a qualifying change in its interest in the business carried on by it in partnership.

Clause 45: Meaning of “profits” and “loss”

147. This clause provides that in calculating the amount of income and expense for the purposes of this Chapter a company’s percentage share does not include its share in any chargeable gains or losses. It is based on paragraph 37 of Schedule 10 to FA 2006.

148. In the case of some partnerships, different profit sharing ratios are agreed for income profits or losses and capital profits or losses. This provision ensures certainty in such cases by looking only at the profit sharing ratios for income profits or losses.

Chapter 5: Sales of lessors: miscellaneous

Overview

149. This Chapter includes anti-avoidance provisions, a provision dealing with the interaction of the sales of lessors Chapters and section 228K of CAA, and interpretative provisions.

Clause 46: Restrictions on relief for expenses treated as incurred under Chapter 3 or 4: introduction

150. This clause provides for the circumstances in which clause 47 applies. It is based on paragraph 38(1), (2), (6) and (7) of Schedule 10 to FA 2006.

151. Clause 47 applies if a company incurs an expense under Chapter 3 or 4 which arises in consequence of or in connection with arrangements the main purpose, or one of the main purposes, of which is to secure that the company is treated as incurring the expense (see *subsection (1)*).

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152. *Subsection (4)* defines “arrangements” for the purposes of this clause. Consideration is being given to including a general definition of arrangements in this Bill. Such a general definition would be in the same terms as subsection (4) excluding paragraph (b). If a general definition is adopted, subsection (4) may be replaced with a provision to the effect that it does not matter whether the company is party to the arrangements mentioned in subsection (1).

Clause 47: Restrictions applying to the restricted loss amount

153. This clause is an anti-avoidance provision. It is based on paragraph 38(2) to (5), (8) and (9) of Schedule 10 to FA 2006.

154. The clause restricts the manner in which the loss derived from the expense referred to in clause 46 may be utilised. It ensures that the loss can only be set against income from certain leases of plant or machinery entered into before the day on which the company is treated as incurring the expense.

155. The sections of ICTA referred to in *subsections (3) and (5)* are to be rewritten in this Bill. The relevant clauses as published on 8 November 2007 under committee paper CC/SC (07) 38: Losses are as follows:

Section of ICTA	Rewritten clause published on 8 November 2007 under committee paper CC/SC (07) 38
section 392A	clauses 25[j4101rm] and 26[j4101Arm]
section 392B	clause 29[j4102rm]
section 393	clause 15[j4513rm]
section 396	clause 31[j4551rm]
section 393A(1)	clause 3[j4505rm](3)(b)

156. Chapter 2 of Part 5 of this Bill rewrites section 403 of ICTA. See the draft clauses published on 6 September 2007 under committee paper CC/SC (07) 27: Group relief.

Clause 48: Introduction to sections 49 and 50

157. This clause explains when clauses 49 and 50 apply and what is meant by a question as to the application of Chapter 3 or 4. It is based on paragraphs 38A(1) and (4) and 38B(1) of Schedule 10 to FA 2006.

158. A question as to the application of Chapter 3 or 4 is one which concerns:

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- whether a company carries on a business of leasing plant or machinery (whether alone or in partnership); or
- the amount (if any) of any income or expense treated as received or incurred.

Clause 49: Disregard of increases and decreases in balance sheet amounts

159. This clause is an anti-avoidance provision. It is based on paragraph 38A(1) to (3) and (5) of Schedule 10 to FA 2006.

160. The clause targets arrangements that increase or reduce the amounts shown in a company's balance sheet in respect of plant or machinery.

161. *Subsection (1)* provides that this clause applies if:

- there is a question as to the application of Chapter 3 or 4 and the answer to the question relies on amounts in respect of plant or machinery shown in any balance sheet of any company;
- there has been an arrangement that results in an increase or reduction of the amount that would otherwise have been shown on the balance sheet; and
- that arrangement had as its main purpose, or one of its main purposes, securing a relevant tax advantage (see *subsection (2)*).

162. If this clause applies the increase or decrease in the amount in respect of plant or machinery is to be ignored (see *subsection (3)*).

163. *Subsection (4)* defines "arrangements" for the purposes of this clause. Consideration is being given to including a general definition of arrangements in this Bill. Such a general definition would be in the same terms as the definition in subsection (4) excluding paragraph (b). If a general definition is adopted, the definition in subsection (4) may be replaced with a provision to the effect that it does not matter whether the company for which the relevant tax advantage is intended to be secured is party to the arrangements mentioned in subsection (1).

Clause 50: Balance sheet amounts to be determined on assumption that company has no liabilities

164. This clause is an anti-avoidance provision. It is based on paragraph 38B of Schedule 10 to FA 2006.

165. The clause targets situations where the amount shown in a company's balance sheet in respect of plant or machinery is affected by the liabilities of the company.

166. It applies if, apart from this clause, on any day:

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- no amount would fall to be shown in the company's balance sheet in respect of plant or machinery (see *subsection (2)*), or
- the amount which would fall to be shown in the balance sheet of the company in respect of plant or machinery is less than the amount which would fall to be shown on the assumption that the company had no liabilities of any kind on that day (see *subsections (3) and (4)*).

167. In either of those cases, a question as to the application of Chapter 3 or 4 is to be answered applying the assumption that the company had no liabilities of any kind on that day (see *subsection (5)*).

Clause 51: Exception where section 228K of CAA 2001 applies

168. This clause gives precedence to section 228K of CAA over the sales of lessors Chapters. It is based on paragraph 40(1) to (3) and (5) of Schedule 10 to FA 2006.

169. Section 228K of CAA applies if there is a disposal of a leased asset and any part of the income stream is retained. That section requires the lessor to bring a disposal value into account. This clause deals with situations where section 228K has effect on the day on which there is a qualifying change of ownership of the company or a qualifying change in the company's interest in the partnership business. It avoids double taxation.

170. Paragraph 40(2) of Schedule 10 to FA 2006 provides that, in the circumstances set out in paragraph 40(1), no "person" is to be treated as receiving an amount of income or incurring an expense under Schedule 10. In rewriting paragraph 40(2) of Schedule 10 to FA 2006 in *subsections (1)(d) and (2)*, "company" has been substituted for "person" on the basis that Schedule 10 only applies to companies.

171. The discussion document has identified that, in circumstances where the whole of a leasing business carried on in partnership is sold to an unconnected party, there is also a potential double charge to tax under CAA and Schedule 10 to FA 2006. It proposes that provision be made to avoid this double charge.

172. Paragraph 40(4) of Schedule 10 to FA 2006 is not rewritten as it is spent.

Clause 52: Interpretation of the sales of lessors Chapters

173. This clause defines terms and provides interpretation for the purposes of the sales of lessors Chapters. It is based on paragraph 41 of Schedule 10 to FA 2006.

174. The definition of connected persons by reference to section 839 of ICTA in paragraph 41(9) of Schedule 10 to FA 2006 has not been rewritten as that definition will be rewritten in this Bill which will also include a provision, equivalent to section 1021(1) of ITA, applying the defined term for the purposes of this Bill unless otherwise indicated.

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175. Paragraph 42 of Schedule 10 to FA 2006 (index of definitions) has not been rewritten in this Part, but the Schedule to this Bill containing the Bill-wide index will contain the principal defined terms used in the sales of lessors Chapters.