CHAPTER 37

SALE AND LEASEBACK

37.1 Introduction

CTA 2010 ss.834-886 set out anti-avoidance rules relating to sale and leaseback. The provisions are split into two types, those dealing with land and those dealing with other assets.

37.2 Sale and leaseback of land

The provisions are very widely drawn to catch any transaction involving the **transfer of land.** If, following the transfer of land, the person who was the **transferor, or any person associated with them, has to pay rent under a lease of the land,** then the scenario is caught by the provisions. CTA 2010, s.834

This is to stop traders from taking land which is a capital asset not receiving any tax deductions, and converting it to a lease with rental payments which will receive tax deductions. This is normally achieved by selling the land to a bank then immediately leasing it back. The capital sum received on the sale of the land is normally sheltered from capital gains tax in some way. The lease payments are usually front loaded to ensure the bank gets its money back as soon as possible.

A typical scenario may be a sale of land for £1m with rentals to be paid of £200,000 in each of the first five years then £50,000 in years 7 and 8 dropping to £1,500 a year. As we can see the bank only has to wait five years to recover its money and then effectively gets interest on the amount paid for the land.

The anti-avoidance legislation limits the deduction available for the rentals to the **commercial rents** that would be payable on the lease. However to the extent that rent is **disallowe**d it can be **carried forward** for relief in the future provided that **amounts are paid under the lease** in the future. CTA 2010, s.838 CTA 2010, s.838(3)

Year	*B/fwd*	*Rent*	*Total*	*Trade profits deduction*	*C/fwd*
1	-	200,000	200,000	75,000	125,000
2	125,000	200,000	325,000	75,000	250,000
3	250,000	200,000	450,000	75,000	375,000
4	375,000	200,000	575,000	75,000	500,000
5	500,000	200,000	700,000	75,000	625,000

6	625,000	50,000	675,000	75,000	600,000
7	600,000	50,000	650,000	75,000	575,000
8	575,000	1,500	576,500	75,000	501,500
9	501,500	1,500	503,000	75,000	428,000
10	428,000	1,500	429,500	75,000	354,500

We see that for the first five years the disallowed rent grows then once the rentals drop the company begins to recover the rent carried forward. This speeds up as we reach the peppercorn rent. The company will need to continue making payments under the lease for another 5 years to obtain tax relief on all the rents paid.

If the lease had only been for ten years then the £354,500 rent carried forward would be lost. This would not be good news for the company.

As it says above, the legislation is widely drawn. **An associate** is defined very widely as

1) Persons acting in concert or parties to reciprocal arrangements CTA 2010, s.847

2) Any two or more corporate bodies incorporated for or participating in a scheme for reconstruction or amalgamation of other corporate bodies.

3) Relatives and their spouses, spouses and their relatives

4) Trustees and settlors and their associates

5) Bodies where there is control

6) Joint owners of a joint venture and their associates

37.3 Sale of a short lease

These rules apply where a lease with **less than 50 years** to run is **assigned, or surrendered to the landlord,** and a new lease is granted to the original lessee for less than **15 years**. CTA 2010, s.850

The **premium** received on assignment of the lease will **partly be taxed to income** using the formula

(16 – n) / 15 x Premium CTA 2010, s.851(4)

where n is the length of the new lease

This will be taxed as trading income if the rent qualifies for a trading income deduction, or under the charge to corporation tax on income in any other case. CTA 2010, s.851(7)(8)

Normally the rentals payable on these leases are commercial. They are often entered into when the rent has fallen below the market rent. The trader is happy to enter the new lease as he receives a premium and can have a tax deduction for the higher rents payable.

Illustration 1

Ganga Ltd has a lease with 45 years to run. The rent is currently £18,000 per annum. They agree to assign the lease to a bank for £55,000 and be assigned a new lease for 12 years with a rent of £24,000 which is the commercial rent for this lease.

Part of the premium will be taxed as income

£55,000 x (16-12)/15 = £14,667

The rentals of £24,000 will be tax deductible in full as they are commercial.

For determining the length of a lease it is deemed to **end on the earlier of** any power of the lessor or lessee to terminate it; any power of the lessee to vary his obligations in order to reduce his rent or reduce his obligations in any other beneficial manner; Or CTA 2010, s.854

Where, the total payment in respect of a rental period which ends at that date (and before the 16^{th} anniversary of the lease) exceeds the rent payable for the next period.

37.4 Assets other than land

CTA 2010 s871 makes provision where there has been a deduction available for lease payments on any asset other than land and a capital sum is received by the lessee in respect of his interest in the lease.

The **lower** of the **amount received and the tax deductions received** under the lease will be taxed **under the charge to corporation tax on income**.

Illustration 2

Bienes Ltd has a lease of plant paying £3,000 per annum for 5 years after which it will pay £100 a year for 20 years. After 4 years Bienes Ltd assigns the lease to a bank for £7,000.

The amount to be assessed to corporation tax will be the lower of (4 x £3,000) = £12,000 and £7,000, the amount received.

A capital sum is defined as any sum of money or money's worth unless it is already brought into the charge to tax.

A lease is defined very widely and can include HP contracts. However it is specifically provided that it will not include any capital sum under the HP contract that has to be brought into the capital allowances computation.

These rules do not apply to the sale and leaseback of assets.

37.5 Sale and leaseback other than land

If an asset is owned and used in a trade by the owner then it is sold and leased back, the rentals deductible will be limited to a commercial rent CTA 2010, s.864

The provisions are similar to those for land with **disallowed rent** being **carried forward** for offset in the future so long as rentals continue to be paid under the lease.

These provisions do not apply to long funding leases. CTA 2010, s.866