

## **Lease premium relief: effective duration of a lease**

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### **Who is likely to be affected?**

Individuals, partnerships and companies that carry on trades or property businesses and pay or receive lease premiums on leases granted after the operative date.

### **General description of the measure**

This measure limits the availability of lease premium relief where leases are of more than 50 years duration.

By removing relief where a long lease is treated as a short lease for tax purposes, the regime will be simplified. An imbalance where the recipient of this type of lease premium is tax exempt and the payer is chargeable to tax will be removed. Revenue will be protected and HM Revenue & Customs' (HMRC) costs reduced.

### **Policy objective**

This measure is designed to simplify a complex element of the lease premium rules and protect tax revenue.

### **Background to the measure**

In 2011 the Office of Tax Simplification (OTS) recommended the lease premium relief regime as an area which could benefit from simplification.

The Government announced at Budget 2012 that it would consult on an informal basis on the potential implications of amending a complex element of lease premium relief rules concerning the tax treatment of long leases as shorter leases. The informal consultation ran from April 2012 to June 2012.

## **Detailed proposal**

### **Operative date**

The measure will have effect for leases granted on or after 1 April 2013 for companies and on and after 6 April 2013 for individuals and partnerships.

### **Current law**

The current law taxes a lease premium payment, made on granting a lease of less than 50 years, on the recipient landlord and relieves it on the tenant where that tenant is a trader or a subsidiary landlord. The premium would otherwise be a capital payment for tax purposes. Where the payment relates to a lease of more than 50 years, a premium is also treated as being within the regime in certain specific circumstances relating to the expected length of the lease. The legislation also treats work required to be carried out by a tenant as a premium in certain circumstances.

Chapter 4 of Part 4 Corporation Tax Act 2009 (CTA 2009) and Chapter 4 of Part 3 Income Tax (Trading and Other Income) Act 2005 (ITTOIA 2005) cover lease premiums.

Section 216 CTA 2009 and section 276 ITTOIA 2005 define a 'short-term lease' as a lease whose effective duration is 50 years or less.

Section 217 CTA 2009 and section 277 ITTOIA 2005 apply if a premium is required to be paid under a short-term lease or under the terms subject to which a short-term lease is granted. The company is treated as receiving a proportion of the premium as a property business receipt for the accounting period for which the lease is granted.

Section 218 CTA 2009 and section 278 ITTOIA 2005 contain the rules for treating expenditure on required work as a premium.

Sections 231 and 232 CTA 2009 and sections 291 and 292 ITTOIA 2005 describe the way in which relief for premiums paid (and similar) is given where the tenant is carrying on a property business.

Sections 62 and 63 CTA 2009 and sections 60 and 61 ITTOIA 2005 cover the situation where the tenant is not carrying on a property business but is trading.

Section 243 CTA 2009 and section 303 ITTOIA 2005 set out three rules that need to be applied to determine the effective duration of a lease.

Rule 1 applies (a) if the terms of the lease, or any other circumstances, make it unlikely that the lease will continue beyond a date before the end of the term for which the lease was granted, and (b) the premium was not substantially greater than it would have been had the term been one ending on that date. In these circumstances the lease is treated as ending on the earlier date.

Section 244 CTA 2009 and section 304 ITTOIA 2005 state that the rules in s243 and s303 respectively apply by reference to the facts known or ascertainable at the time of the grant of the lease and that it is assumed that the parties act as if they were at arm's length.

### Proposed revisions

Legislation will be introduced in Finance Bill 2013 to amend sections 61 ITTOIA and 63 CTA 2009 and sections 292 ITTOIA and 232 CTA 2009.

From the operative date relief will no longer be available to a trader or intermediate landlord that pays a lease premium on a lease that is only deemed to be short because of the operation of the rule 1 in section 243 CTA 2009.

### Summary of impacts

Exchequer impact (£m)	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
	-	nil	nil	nil	nil	nil
	This measure is not expected to have an Exchequer impact. This measure supports the Exchequer in its commitment to protect revenue.					
<b>Economic impact</b>	This measure is not expected to have any economic impacts.					
<b>Impact on individuals and households</b>	There is no impact on individuals or households because this is a change that affects businesses only.					
<b>Equalities impacts</b>	No specific group has been identified as being adversely affected.					
<b>Impact on business including civil society organisations</b>	This measure is expected to have a negligible impact on businesses and civil society organisations. The measure is designed to amend a complex element of the lease premium rules and the number of businesses affected is unknown. The impact on administrative burden and one-off costs are expected to be negligible.					
<b>Operational impact (£m) (HMRC or other)</b>	Initial HMRC operational impact is estimated to be less than £2 million resource savings. Includes a saving of 25 per cent of Valuation Office Agency specialist technical team resource.					

<b>Other impacts</b>	<u>Small firms impact test:</u> an informal consultation was held on the possible impact on small businesses and no responses were received indicating that there is such an impact.  Other impacts have been considered and none have been identified.
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### **Monitoring and evaluation**

This measure will be kept under review through communication with affected taxpayer groups.

### **Further advice**

If you have any questions about this change, please contact Allana Sheil on 020 7147 2565 (email: [allana.sheil@hmrc.gsi.gov.uk](mailto:allana.sheil@hmrc.gsi.gov.uk)) or Brian Stokes on 020 7147 2546 (email: [brian.stokes@hmrc.gsi.gov.uk](mailto:brian.stokes@hmrc.gsi.gov.uk)).

**1 Lease premium relief**

Schedule 1 makes provision in relation to relief for lease premiums.

## SCHEDULES

### SCHEDULE 1

Section 1

#### LEASE PREMIUM RELIEF

##### *Income tax*

- 1 ITTOIA 2005 is amended as follows.
- 2 In section 61 (tenants occupying land for purposes of trade treated as incurring expenses) after subsection (5) insert –
  - “(5A) No expense is to be determined under this section by reference to the taxed receipt if section 292(4B) or (4C) applies.”
- 3 In section 292 (tenants under taxed leases treated as incurring expenses) after subsection (4) insert –
  - “(4A) No expense is to be determined under this section by reference to the taxed receipt if subsection (4B) or (4C) applies.
  - (4B) This subsection applies if there would have been no taxed receipt but for the application of Rule 1 in section 303 in determining the effective duration of the lease.
  - (4C) This subsection applies if there would have been no taxed receipt but for the application of Rule 1 in section 243 of CTA 2009 in determining the effective duration of the lease for the purposes of Chapter 4 of Part 4 of that Act.”
- 4 The amendments made by paragraphs 2 and 3 above have effect in relation to leases granted on or after 6 April 2013.

##### *Corporation tax*

- 5 CTA 2009 is amended as follows.
- 6 In section 63 (tenants occupying land for purposes of trade treated as incurring expenses) after subsection (5) insert –
  - “(5A) No expense is to be determined under this section by reference to the taxed receipt if section 232(4B) or (4C) applies.”
- 7 In section 232 (tenants under taxed leases treated as incurring expenses) after subsection (4) insert –
  - “(4A) No expense is to be determined under this section by reference to the taxed receipt if subsection (4B) or (4C) applies.

- (4B) This subsection applies if there would have been no taxed receipt but for the application of Rule 1 in section 243 in determining the effective duration of the lease.
  - (4C) This subsection applies if there would have been no taxed receipt but for the application of Rule 1 in section 303 of ITTOIA 2005 in determining the effective duration of the lease for the purposes of Chapter 4 of Part 3 of that Act.”
- 8 The amendments made by paragraphs 6 and 7 above have effect in relation to leases granted on or after 1 April 2013.

**EXPLANATORY NOTE**

**LEASE PREMIUM RELIEF**

**SUMMARY**

1. This clause and Schedule limits lease premium relief available to a trader or intermediate landlord where leases are of more than 50 years duration. The measure has effect for leases granted on or after 1 April 2013 in respect of companies and 6 April 2013 in respect of individuals or partnerships.

**DETAILS OF THE SCHEDULE**

2. Paragraph 2 adds new section 61(5A) to Income Tax (Trading and other Income) Act 2005 (ITTOIA). New section 61(5A) precludes the deduction of a trade expense where the charge on the landlord (the “taxed receipt”) in respect of the lease premium is within new section 292(4B) or (4C)
3. New section 292(4A) precludes the deduction of a property business expense where the charge on the landlord (the “taxed receipt”) in respect of the lease premium is within new section 292(4B) or (4C)
4. New section 292(4B) applies where the lease is only a long lease because of the operation of Rule 1 in section 303 ITTOIA 2005.
5. New section 292(4C) applies where the lease is only a long lease because of the operation of Rule 1 in section 243 Corporation Tax Act 2009 (CTA 2009).
6. Paragraph 6 adds new section 63(5A) to CTA 2009. New section 63(5A) precludes the deduction of a trade expense where the charge on the landlord (the “taxed receipt”) in respect of the lease premium is within new section 232(4B) or (4C)
7. New subsection 232(4A) precludes the deduction of a property business expense where the charge on the landlord (the “taxed receipt”) in respect of the lease premium is within new section 232(4B) or (4C)
8. New section 232(4B) applies where the lease is only a long lease because of the operation of Rule 1 in section 243 CTA 2009.
9. New section 232(4C) applies where the lease is only a long lease because of the operation of Rule 1 in section 303 ITTOIA 2005.

**BACKGROUND NOTE**

10. A lease premium payment, made on granting a lease of less than 50 years, is taxed on the recipient landlord and relieved on the tenant where that tenant is a trader or an intermediate landlord. The premium would otherwise be a capital payment for tax purposes. Where the payment relates to a lease of more than 50 years, a premium is also treated as being within the lease premium regime if it falls within Rule 1 of section 303 ITTOIA 2005 or section 243 CTA 2009.
  
11. If you have any questions about this change, or comments on the legislation, please contact Allana Sheil on 020 7147 2565 (email: [allana.sheil@hmrc.gsi.gov.uk](mailto:allana.sheil@hmrc.gsi.gov.uk)).