

# TAX RELIEF FOR EXPENDITURE ON PROPERTY

Many business owners are aware of the tax allowances available for items of plant and machinery acquired to use in the course of their trade, but not so many understand how tax relief can be obtained for expenditure on their business property, whether that be an office, a factory, or a room at home.

## Expenditure incurred on fitting-out a property

Should you incur costs in buying, enhancing or fitting-out a property, tax relief may be available. This document summarises some of the tax reliefs available for expenditure on property.

Expenditure that does not fall within one of these categories will generally be treated as ineligible and no relief will be available for income tax or corporation tax purposes other than on the disposal of the property.

## Revenue expenditure

Expenditure such as repairs and maintenance are treated as revenue expenditure and are deductible when calculating taxable profits of a business. Examples of revenue expenditure are painting and replacing part of a guttering system. Repairs are fully deductible for tax purposes as long as they are incurred wholly and exclusively for the purpose of the business, are charged to the profit and loss account and do not include any element of improvement.

Particular care has to be taken when repairs undertaken on a new building are treated as revenue, as HM Revenue & Customs will look closely and may seek to recategorise it as capital.

*If expenditure is treated as capital in nature, tax relief may be available in the form of capital allowances.*

## Structures and buildings allowance

For expenditure incurred on or after 29 October 2018, a structures and buildings allowance (SBA) is available for qualifying expenditure on commercial buildings and structures. The relief is not available where the construction contract was entered into before 29 October 2018.

Qualifying expenditure may include the costs constructing, improving and converting buildings for commercial use but not on the cost of land, rights over land or obtaining planning permission.

Relief may be claimed in respect of buildings and structures located anywhere in the world as long as the business is within the charge to UK tax.

Claimants must carry on qualifying activities, which includes any trade, profession or vocation and UK and overseas property businesses but not furnished holiday letting.

The SBA gives relief at the rate of 2% on a straight line basis. If the claimant disposes of the property on which SBAs are being claimed, the purchaser will continue to claim the annual 2% allowance. There are no balancing charges or allowances for the seller.

## 100% first year allowances (Enhanced capital allowances "ECAs")

Certain types of expenditure will attract first year allowances at 100% and therefore a deduction for the full costs of such assets is available in the year in which the expenditure is incurred. In some circumstances a repayable tax credit may be claimed of two-thirds of the corporation tax rate. There are several categories of assets which qualify for ECAs, of which the following may be relevant to property owners:

- Energy saving plant and machinery
- Water saving equipment

These allowances will no longer be available after 5 April 2020.

## Capital allowances

### Main pool expenditure

Capital allowances are a tax relief designed to allow the cost of certain business assets to be written off against taxable profits. They take the place of the depreciation shown in the financial accounts, which is not allowable for corporation tax purposes.

General items of "plant and machinery" will be allocated to the "main pool" for capital allowances purposes and be written down for tax purposes at the rate of 18%, on a reducing balance basis.

An item will generally qualify as plant where it fulfils a "function" in the trade, or is specifically treated as plant in the legislation.

Examples would include furniture (such as cupboards, racking, shelving), fire safety and security equipment, moveable office partitioning that you intend to move in the course of the trade, and IT equipment etc.

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Many fixtures and fittings of a building fit-out are likely to qualify for allowances under this category, provided they are not a permanent addition to the structure of the building itself. For example, carpet tiles may qualify for allowances, but it would be more difficult to show that hardwood flooring was not an improvement to the fabric of the building itself.

### *Annual Investment allowance*

In addition, the annual investment allowance provides a 100% first year allowance for investment in plant and machinery (excluding cars) up to the AIA limit. The current AIA limit is £1,000,000 per year. Only one AIA is available per group of companies/ associated businesses, so it may be the case that the AIA is not available for capital expenditure within the new building, as it is already being used against other eligible expenditure.

As the annual investment allowance may be allocated flexibly, it should be allocated in the first instance to expenditure that would otherwise qualify for the lowest rates of relief, for example integral features (see below).

### *Integral features*

Allowances are available in respect of expenditure incurred on the provision of an 'integral feature' of a building. These assets should be put into a separate special rate capital allowances pool where the writing down allowance of 6% is applied.

Integral features include electrical systems (including wiring and ordinary lighting), cold water systems, space or water heating systems, powered ventilation systems, air cooling or purification systems, passenger lifts, escalators or moving walkways and external solar shading.

The speed at which relief can be obtained will be significantly increased by ensuring as much of this type of "integral" expenditure as possible can qualify for the AIA outlined above.

### *Research and Development Allowance*

Research and developments allowances give relief for capital expenditure incurred for research and development activities by a person or company carrying on a trade. The allowances are given as a deduction for 100% of the expenditure on such assets in the year in which the expenditure is incurred.

Such allowances do not extend to expenditure on the acquisition of land, but can include the costs of constructing or purchasing a building, which is for example used as a laboratory. The relief is therefore more generous than standard capital allowances which are only available on 'plant and machinery'.

### *Making the capital allowances claim*

Capital allowances should be claimed through a self-assessment tax return.

In order to reduce the risk of HMRC opening a compliance check in respect of capital allowances claims, the tax computation should include a clear and detailed breakdown of project expenditure showing what relief or allowances have been claimed in respect of eligible amounts.

### **Land Remediation Relief**

Land remediation relief is available for expenditure on contaminated land by companies within the charge to corporation tax. In addition, relief is also available on derelict land which has been derelict since the earlier of acquisition or 1 April 1998. The land must be within the UK.

Examples of contaminated land include land containing asbestos, Japanese knotweed, sulphate resistant concrete, or that may otherwise cause harm to wildlife, waters, the ecosystem or other buildings.

The relief provides for an enhanced deduction for 150% of certain capital expenditure incurred which would not have been incurred if the land had not been contaminated. Relief is given in the year in which the expenditure is incurred. Loss making companies may claim a repayable tax credit of up to 16% of the enhanced expenditure, i.e. 24% of the expenditure actually incurred.

The relief cannot be claimed if the company was responsible for the original contamination.

### **Sale or purchase of a property that includes fixtures**

Fixtures are items which qualify as plant and machinery for capital allowances purposes but which are legally part of a building. Examples might include air conditioning systems or lifts. The costs of these items will generally be included in the cost of a building when it changes hands.

A buyer will only be able to claim capital allowances on fixtures in an acquired building if the seller has previously "pooled" the qualifying expenditure. The pooling can happen at any time after the seller has built or bought the property, but must be done before the property is subsequently sold on, otherwise no capital allowances will ever be available to the buyer or any future owner of the property.

The seller and buyer are then required to enter into a joint election within two years of the sale in order for the buyer to be entitled to allowances on fixtures. The agreed price will be the deemed expenditure by the purchaser and the deemed disposal value for the seller. There can therefore be a clash of interest as both parties will want to maximise their proportion of the available allowances.

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If the parties cannot agree, then the matter can be referred to the First Tier Tribunal for a determination.

There are special rules that apply to the purchase of properties which have been held by the seller since before April 2008 and which include assets which would qualify as integral features. In this case it can be possible for the buyer to claim allowances on such assets despite them having never been pooled by the seller.

### Construction projects

If you are constructing a new building it is important to involve your tax adviser at the planning stage to ensure that the information that is provided by the building contractor or a quantity surveyor correctly identifies expenditure on which allowances are available.

*The above provides a brief summary of the major factors to consider when incurring expenditure on property. This should not be relied upon without taking further advice. Please get in touch with our team if you would like to discuss this in greater depth.*