Afilia
Capital Allowances

2023 Capital Allowances headlines for Architects & PMs

Maximising value for money

Introduction - managing the wish list

Matching a client's aspirations to their budget is perhaps the first and possibly the most difficult challenge to overcome on the journey to a successful build project. Indeed if the gap between the two appears irreconcilable then it could result in the loss of the appointment - and even if enough areas for compromise are found - the scheme may yet become fraught should cost overruns occur.

Although most architects and project managers will have an outline understanding of Capital Allowances, it remains an area that stays in the shadows as clients seldom seek advice on it. It also becomes difficult to bring it into budget discussions if there is no real sense of what value tax savings might be, and understandably not having a good basis of knowledge is a good reason not to talk about it.

The key point is that when a project is financially marginal - then tax savings could be the turnkey to viable delivery without a significant dilution of the original wish list.

The underlying problem

One issue is that the Capital Allowances regime is subject to frequent change which in turn undermines public understanding and reinforces a belief that Capital Allowances are overly complex. Many taxpayers accordingly do not take the full benefit of what is available - an effect that may become more marked as we move towards an era driven by energy performance.

Allowances will apply to any commercial property - only ordinary dwellings are outside the scope for relief - but even then there are opportunities for claims on the common parts of residential blocks with lifts or heating plant, and also serviced apartments, or furnished holiday lets.

What qualifies?

Plant & Machinery Special Rate Pool:

Hot & Cold water, Heating & Cooling, electrical systems, lifts and escalators - claimed at 6% per annum

Plant & Machinery Main or General Pool:

All the building systems and fit-out related to the trade carried out - claimed at 18% per annum

Structures and Buildings Allowances:

Other structural works (post 2019) - written down at 3% per annum.

AIA and the temporary tax reliefs

In most cases the writing down rates of 6 & 13% will be irrelevant because all of the value can be claimed in the first year through the Annual Investment Allowance. As most taxpayers will be entitled to an AIA of £1m per annum - this will entirely cover all of the plant & machinery allowances in most projects.

From the 2023 Budget, Temporary Tax Reliefs for corporate taxpayers, apply until 2026:-

- 50% of new Special Rate Pool expenditure may be claimed in the first year. If the client has unused Annual Investment Allowance (AIA) - this can be applied to the other 50%.
- The entirety of the Main Pool expenditure will be claimed in Year 1 under the heading of "Full Expensing."

Note that the Temporary Tax Reliefs are only available to corporate taxpayers (25% tax rate) - the reason being that those paying the 40% rate - i.e. individuals and partnerships - already receive almost double the value in actual tax savings.

Capital Improvements

Where a client undertakes a renovation or refurbishment - this will contain significant tax savings. Typically 50-75% of a budget will qualify as fixed Plant & Machinery or repairs, with the balance being allocated to the Structures and Buildings Allowance.

In most instances Capital Allowances are not considered at the design stage but left to be dealt with as post-project diligence.

An early review, however, might show 10-15% of the project cost being recouped through tax relief in the first year. This can help stretch a budget to enable a higher specification. The benefits are obvious if this reflects in the marketability of the building and its achievable rental.

Joint ventures

Without pre-planning, a joint venture will mean a division of the entitlement to claim allowances on a pro-rata basis to the value of the contributions made to the project. If one of the parties pays more tax (or one is a non-taxpayer) then carefully defining who pays for what can avoid loss of entitlement to claim.

The same thinking applies in scenarios where an individual or company has a pension fund and wishes to use this to pay for a new building or improvements.

Rather than paying for the asset or works directly, it may be better for the pension fund to make a loan to its related operating company which can then claim allowances and then repay the loan with interest.

Energy performance

Changes to Minimum Energy Efficiency Standards (MEES), were expected in 2022 but have been delayed by the government. It would nevertheless be sensible to assume that raising the sanction level to 'C' and then 'B' is still going to happen within the foreseeable future.
The impact is likely to be widespread with estimates of up to 80% of UK commercial buildings being affected.
In a building refurbishment having an early view of the scope for EPC improvement is essential to avoid disappointment at completion if the final banding result is below expectations. A good EPC consultant may be able to map the alternatives and their impact on the score. Improving energy performance is, of course, costly and factoring in Capital Allowances will help extend a budget to achieve the best outcome.
It is entirely possible to spend a good deal of money on improvements that are aesthetically pleasing but which have effect on energy performance. It could easily be a recipe for future unhappiness if a project undertaken today only a few years becomes sanctioned possibly leading to the need for considerable additional expenditure.

Office refurbishment example

Office refurbishment illustration	
Construction budget	£2.5m
Plant & Machinery content	£1.5m
-Special Rate Pool	£900,000
-Main Pool	£600,000
Year 1 tax calculation:-	
Special Rate Pool 50% Year 1 allowance	£450,000
Plus AIA for the other 50%	£450,000
Main Pool claimed under Full Expensing	£600,000
Repairs	£150,000
SBA - £850,000 annual claim at 3%	£25,500
Total year 1 claim	£1,675,500
Tax saved at 25% rate	£418,875
Percentage of budget saved in Year 1	17%

The example above shows the savings available to a corporate taxpayer undertaking extensive refurbishment of an office building.
This might typically include replacement of air conditioning plant and upgrading the lift capacity.
It is also important to note that the scope for claims for repairs can be significant. For example if the owner (or tenant on a full repairing lease) of an older office building undertakes a replacement of the existing cladding to both improve the look of the property and its energy performance then this will be accepted as a repair.

Section 25 works

These are for enabling works associated with the installation of Plant & Machinery. Some examples are:-

- Removal of a wall to allow access for removal and installation of new plant
- Building new lift shafts in an older building to increase capacity
- Installing additional structural support within a Listed Building to carry the weight of new air conditioning.

Our approach to pre-planning CAs

The example shows that the value of first year savings makes a real contribution to viability. We regularly review projects that are borderline and which have already been through aggressive value-engineering.
Our preliminary reviews are provided at no cost to identify the scope for Capital Allowances, and our experience is that this quickly removes the client's uncertainties and a decision is taken to proceed - also with an immediate review of the proposed list of cost cuts.
Also the value of the predicted tax savings is often added back to achieve a higher specification.
The early review also ensures a tax-friendly approach is adopted and entitlements are protected. Tax relief should not be the tail that wags the dog - but there are instances where modest changes can help optimise the savings - for example in offices, the use of plenum ceilings or demountable partitioning systems.

About us

Between us the team at Afilia Capital Allowances have over fifty years of shared experience in advising on projects and preparing claims for Capital Allowances. All initial advice is provided at no cost and fees for certifications of allowances on completed projects can be performance-related or fixed.

Disclaimer: this article is not a substitute for professional advice

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