

### Introduction - using knowledge

Most surveyors will have an understanding of Capital Allowances but it remains an area that stays in the shadows as clients seldom seek advice on it. A fear that bringing the subject up could add complexity or delay to the project in hand is often a disincentive.

The other side of the coin is that when a project is financially marginal - then tax savings could be the turnkey to viable delivery.

A further 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 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 tax savings.

### Lease negotiations

The typical inducement offered is a rent holiday - simple and straightforward - but unprofitable for the landlord. A more valuable route is to offer to meet some or all of the tenant's fit-out requirements - which will then be reflected in the rent to be agreed. The added advantage is that this cost will be tax-relieved thereby improving the landlord's return on capital and the overall profitability of the investment. Where a direct cash incentive is used to try and close a lease negotiation, then from the landlord's perspective this should be tied to the tenant's fit-out works. If it is agreed that a £20,000 contribution is for, say, a new lift then allowances can be claimed by the landlord - clear documentation of the agreement will be needed.

### 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 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.

### 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.

## New-builds

Developers do not claim Capital Allowances as the build cost is part of their business cost, and deducted from their trading profit upon sale of the completed asset. The purchaser will be entitled to claim allowances as a price apportionment of their purchase figure. As an example for an office, 15-25% of the cost might become tax relief.

## Purchases of second-hand buildings

Today the purchase of an existing building from another taxpayer has only a limited possibility for a claim on the price paid. Nevertheless, it is important to make careful enquiries of a vendor in case they have undertaken improvements but failed to establish a claim for CAs. Before contracts are exchanged it will be possible to negotiate the transfer by an election of unused allowances. After exchange a vendor is less likely to want to be helpful.

N.B. a purchase of an existing building from a non-taxpayer - i.e. a pension fund, charity, or government body - is likely to be a claim opportunity.

## 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' will happen within the foreseeable future. The impact is likely to be widespread with estimates of up to 80% of the commercial buildings affected. Improving energy performance is, of course, costly and factoring in Capital Allowances will help extend a budget to achieve the best outcome.

## Disposals

The normal process in selling an asset is to enter an election with the purchaser to set the value of the fixed plant & machinery, usually at the current tax-written down value. It is nevertheless up to the parties to negotiate a figure, bearing in mind that a higher figure

will cause the vendor to repay some of their tax savings, whilst a lower figure will enable them to retain unused relief - often done by portfolio owners. As mentioned above where all allowances have been claimed under the AIA then the current tax written-down value will be nil.

## Office refurbishment example

The example below 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.

Office refurbishment illustration	
Construction budget	£2.5m
Plant & Machinery content	£1.5m
-Special Rate Pool	£900,000
-Main Pool	£600,000
<b>Year 1 tax calculation:-</b>	
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%

## Our approach to pre-planning CAs

In the above example the value of first year savings will make a real contribution to viability. Our preliminary reviews are provided at no cost to identify the level of potential tax savings and ensure a tax-friendly approach is adopted and entitlements are protected. Modest changes can sometimes help optimise the savings e.g. the use of plenum ceilings or demountable partitioning systems.

**Disclaimer: this article is not a substitute for professional advice**

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