New Temporary Tax Reliefs

From April 1st 2021

Afilia

Capital Allowances

Incorporating DavidRees.Co

The Annual Investment Allowance

Before considering the impact of the newly arrived 130% Super Deduction and the 50% First Year Allowance - it will help if we consider how these will interface with the existing system.

The Annual Investment Allowance (AIA) is a First Year Allowance for plant & machinery which has been with us for many years, and has been raised and lowered over time in successive Budgets. Its effect is to bring the first £1m of any plant & machinery claim into that year's tax computation - with any remaining balance then written down over time at the normal 6% and 18% rates.
In 2018 the AIA was raised from £200,000 to £1m for two years as a financial cushion to help businesses facing additional costs in preparing for leaving the EU. It was set to fall back to the £200,000 rate on the 31st December 2020, but shortly before that the government relented and extended the £1m rate by one year to 31st December 2021.

The new temporary reliefs are in addition to the AIA and so it will be important to ensure they are properly applied in order to maximise tax savings.

The new temporary reliefs

The new "Super Deduction" and 50% First Year Allowance were an unexpected announcement in the Budget. A key point is understanding the treatment of the separate pools of allowances.

It is important to note that they not available to non-corporates e.g. partnerships or private individuals - and while this may seem unfair it must be remembered that as 40% taxpayers, they receive more than twice the value in tax savings than a corporate incurring the same expenditure.

Also excluded is plant & machinery intended for leasing and so landlords will not be entitled to the temporary reliefs. The Treasury's rationale being that the intention is to stimulate investment by businesses for immediate impact on the economy - whereas property investment is seen as only having long-term effects.
The Super Deduction is solely applicable to the Main (or General) 18% Pool of allowances and is calculated as 130% of the qualifying value. It is then claimed as a First Year Allowance. The effect on value is that at the 19% tax rate - a claim with Super Deduction added becomes the equivalent of a 24.7 pence in the pound saving on the expenditure.

The Integral Features or Special Rate Pool is given a different incentive with a new First Year Allowance of 50%. The remainder of a claim would then be subject to the annual 6% writing down rate.

The new temporary reliefs, however, do not replace or exclude the use of the Annual Investment Allowance. The key difference is that the AIA is an acceleration of some or all of the basic claim, while the Super Deduction is also a First Year Allowance - but with a multiplier of 30% added to the base claim value.

The choice is obvious, which is that if the AIA is available it should be directed at the Integral Features pool with its much lower 6% writing down rate. Where an Integral Features claim is less than £1m it will be entirely covered by the AIA.

If the claim is greater than £1m - the balance will then benefit from the First Year Allowance of 50% - and the remaining 50% then written down at the usual 6% rate.

The Super Deduction being applied to the Main (General) Pool creates a 30% uplift in value and so to use the AIA against it would be less beneficial.

Lastly it is important to note that the temporary reliefs only apply to expenditure contracted after 3rd March 2021.

Timeframe

The new temporary reliefs will run from 1st April 2021 until 31st March 2023 and are available for companies investing in qualifying new plant and machinery. This two year life cycle is important as it allows a reasonable timeframe for project delivery - but it is particularly important to recognise that both are defined as "temporary tax reliefs" - and so a further extension should be considered unlikely.

The new reliefs do not change any of the rules relating to the availability of Capital Allowances and so for all projects the analysis process remains unchanged. If anything the increased tax savings underline the importance of a detailed cost segregation exercise if claims are to be optimised.

Date of first use

A key point is that where a building is either new or being refurbished, then in most instances the claim for Capital Allowances will only be available after the plant & machinery is brought into use for the first time. This makes March 31st 2023 an important deadline to be considered from the outset of any scheme. Project planning should start with that date as the latest possible time for completion in order to avoid missing the cut-off for qualification.

Many construction companies have maintained reasonable order books through the pandemic, and so early preparation is crucial if the services of a preferred contractor are to be secured.

An investment perspective

In an historical context this is probably the most generous tax-break ever given to commercial property. Only if the economy seriously struggles to pick up once the pandemic recedes might such a generous measure be extended. For this reason there is a real impetus to take advantage of it at the earliest time. This may mean considering what possible expenditures might be required over the next five years - and perhaps bringing them forward. If a potential sale is likely and some improvements will maximise the disposal value, then making an earlier start has obvious benefits.

Another issue is the looming impact of the zero carbon agenda - which is likely to bring increases in compliance levels for Minimum Energy Efficiency Standards. Taking advantage of the temporary reliefs may be very useful in helping future-proof buildings - as well as improving their marketability. Over time it is likely that corporate tenants will become increasingly sensitive to Energy Performance Certificate ratings as they seek to demonstrate greener policies to their shareholders. Accordingly improvements that uplift an EPC rating will be helpful in protecting asset values.

Commercial office £5m refurbishment			
	Expenditure	**Tax relief**	**First year claim**
Project cost	£5,000,000		
Repairs	£250,000	100%	£250,000
Integral Features (IF)	£1,600,000		
AIA		£1,000,000	£1,000,000
Balance of IF		50% FYA	£300,000
Fit-out (Main Pool)	£1,500,000		
Super Deduction		130%	£1,950,000
Total Year 1 claim			£3,500,000
Tax saving at 19%			**£665,000**
Percentage of cost			13%

Example

The process of preparing a Capital Allowances claim for plant & machinery is unchanged and the chart shows the possible outcome of a £5m office refurbishment.
Expenditure on qualifying repairs remains as a current year revenue expense.
Integral Features shows a split treatment with the first £1m utilising the AIA - and then 50% of the balance taken as a First Year Allowance.
The Main Pool items are subject to a 30% Super Deduction uplift in the base value of the claim and taken entirely as a First Year Allowance.
In total the effect of the combined reliefs is a 13% saving on the project cost in the first year. N.B. First Year Allowances are only available in the year of expenditure. Where there is more tax relief than profits to offset, the unused relief will roll forward in the company accounts until used up.

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