

Capital Allowances on surgery improvements

David Rees explains the tax advantages that can be gained from capital allowances during premises upgrades

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Very few GPs are aware that when they undertake building works to improve their surgery premises, they will be entitled to claim valuable tax reliefs in the form of Capital Allowances. These are part of the UK's tax system of writing down the cost of building systems and fit-out over time. This will specifically include the hot and cold water, heating and cooling, plumbing, electrical system, and lifts. The other qualifying expenditure is the fitting-out of the building for the purposes of the business being undertaken and can cover a wide range of items.

What are Capital Allowances?

The UK's system of Capital Allowances tax reliefs dates to the end of World War II when they were introduced to stimulate reconstruction. Over the decades, as buildings have become increasingly complex, so the opportunities for tax savings have steadily grown. Essentially, the external structure will not qualify, but much of what goes inside can be tax depreciated, and today GP surgeries are becoming some of the most sophisticated

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buildings – a trend likely to continue as more services are devolved from hospitals to primary care.

What qualifies can be a very long list starting with business-related installations such as data-cabling, audio-visual and CCTV; and extending to staff facilities, toilets, kitchens, built-in cupboards, even door closers. In all it has been estimated that there are around 1,400 categories of items that can qualify under the legislation as Fixed Plant and Machinery.

Surgeries have, of course, come a long way since the time when they were often just the front room of a GP's residence – in terms of the scale of value of savings, typically, around a third of the construction cost of a new surgery is likely to qualify for Capital Allowances – but in some instances this figure can climb to around 40% of the budget.

The value of the tax relief savings

The cash value of the allowances will be based on the rate of tax being paid and, as doctors are marginal rate 40% taxpayers, this results in significant savings. To translate this into numbers, if a new surgery costs £2m to build of which 35% qualifies as Capital Allowances – then that equates to £700,000 in tax relief, and at the 40% tax rate this means £280,000 saved over time by the GP partners. That level of tax relief equates to a bottom-line saving of 14% of the surgery build cost.

Given that during the project planning process there will often be a good deal of hand-wringing over cost when making

specification choices, and it goes without saying that if the GPs have an early awareness of the scale of the tax savings, it can make some of these decisions a lot easier. It is not unusual to find that by knowing they will benefit from tax savings, the partners decide to plough some of this back and increase the total budget to enable preferred specification choices.

Banks like Capital Allowances because given that they will typically be prepared to lend a high proportion of a surgery development cost, it gives them comfort to know that the partners will benefit from tax savings and have some rainy-day financial flexibility. It can therefore be very helpful to have a preliminary review of the availability of Capital Allowances attached to the loan submission, as it will be well received by the bank's credit committee when considering the application.

Tax savings and greener buildings

Today, many practices have a leaning towards sustainability and are keen to approach a new surgery in as green a way as possible. To this end, the Enhanced Capital Allowances (ECA) scheme can help enhance these credentials by providing 100% first year tax relief on qualifying energy and water-saving technologies.

Generally, Capital Allowances are written down over time, taking percentages of the allowances each year to set against the partners' tax bills. The incentive of the ECA scheme is that the entire cost of the item is claimed against tax in the year of purchase. Parts of a heating or cooling installation may qualify, and items such as water-efficient taps. A real gain is if the lighting system can qualify for ECAs as an entirety, which requires the support of the manufacturer. The lighting in a new £2m surgery is likely to cost at least £60,000 and so the initial tax saved following build completion is dramatic. The importance, however, of early pre-planning by the project team to secure this relief cannot be overstated. Diligence left until the end of the project is almost invariably unsuccessful.

Surgery improvements and grants

There are of course, not just new surgery schemes, but numbers of improvement projects, both refurbishments and extensions



to existing surgery premises, supported with grants from the NHS.

The usual effect of this cash injection is a dilution of the available tax relief on a pro-rata basis, e.g. a 33% grant means a 33% loss of allowances. This situation is not specific to surgery premises and is a fundamental tenet of Capital Allowances. Claims are only available to a taxpayer incurring expenditure with their own money (or their commercially-borrowed funds). Where two parties contribute to the cost of a project, the entitlement to claim relief is split according to their contributions. Sometimes on larger surgery projects it can be permissible to

Table 1. Year 1 tax savings on a surgery development

Construction cost (excluding land)	£2,000,000
Total Capital Allowances – 35% of build cost	£700,000
First year claim items	
1. Annual Investment Allowance	£200,000
2. Enhanced Capital Allowances	£60,000
3. Writing down allowances	£59,700
Total Year 1 allowances	£319,700
Tax rate	40%
Year 1 tax savings	£127,880
Remaining allowances to be written down over future years	£380,300

claim the entirety of some of the early costs such as design fees or laying foundations and structural works. This may have the effect of reducing the level of subsidy to the fit-out cost incurred later in the build project and increase the proportion of allowances available to the GPs.

The aftermath of Grenfell

The tragedy of the Grenfell Tower fire will mean that fire precautions will be reviewed and many buildings are likely to require improvement. To this end, Capital Allowances will be applicable to much of the cost relating to upgraded fire protection systems. Should a surgery have a cladding system that in due course is judged to be sub-standard then the cost of replacement can be allowable as expenditure on repairs.

Minimum energy efficiency standards

From April 2018 it will be no longer possible to let or renew the lease of a property which has an Energy Performance Certificate rating of ‘F’ or ‘G’. In principle, this would not appear to be a problem as most surgeries are owned freehold by the partners. It may apply, however, where part of the building is leased to a pharmacy operator. This would then bring the premises within the regulations and require a compliant EPC rating when a lease is renewed.

This will be cost that is just as unwelcome as upgraded fire safety, but again expenditures incurred on for example, adding insulation, more modern lighting, a new boiler etc will

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all be tax relievable. There will also be a benefit in some savings in energy bills.

Illustration of first year tax savings in a new surgery

Capital Allowances are principally written down over time, but there is also a first-year benefit – the £200,000 Annual Investment Allowance. This enables the taxpayer to take £200,000 of the total available allowances in the first year following completion of the project – to which are added ECAs and the usual writing down allowances for that year. The table below shows the calculation of the first-year cash savings from a typical £2m surgery build.

Summary

In summary, Capital Allowances are a significant cash flow benefit to GPs undertaking improvements or a new surgery development, but are often overlooked until the end of the build process and only considered when it is time to prepare tax computations. While this does not mean that there will have been a serious loss of entitlement, opportunities for optimisation will have been lost. These will include:

- Making the best specification choices by utilising some of the tax savings
- Supporting a bank-funding proposal
- Enhanced Capital Allowances for accelerated tax relief, a greener building, and reduced running costs
- Optimising the availability of Capital Allowances within a partly NHS-funded project.

A GP partnership embarking on a build project can be overwhelmed by the number of professional advisers that are needed to ensure delivery and, inevitably, the Capital Allowances consultant can often be well down the list – but as the figures show, it is best not to be forgotten completely. **PM**