

Capital allowances and gains on property (Lecture B1382 – 14.50 minutes)

When a business is buying a property, it will typically negotiate a price for the building as a single entity and consider if that figure can be split in order to get a better tax outcome.

The cost of a building is going to be capital in nature and the legislation specifically states that you cannot get capital allowances on buildings unless you have a building which has a function beyond that of just being a building. This is rare and commonly challenged by HMRC. However, the price being paid might include the purchase of assets which do qualify for capital allowances.

Fixtures

The most obvious example is integral features. These are specific assets which can qualify for allowances although the expenditure falls within the special rate pool and so attracts a lower rate of writing down allowance than the main pool. Subject to falling within one of the specific exclusions, such expenditure can qualify for annual investment allowance.

Integral plant is defined as:

- Electrical systems including lighting systems;
- Cold water systems;
- Space or water heating systems, air conditioning or ventilation systems and any floor or ceiling forming part of those systems;
- Lifts, escalators and moving walkways; and
- External solar shading and active facades.

These items are often referred to as 'fixtures' although the legislation refers to these as integral plant.

It is important, however, to acknowledge that you cannot always get capital allowances on the fixtures within a building which is purchased.

If you are buying a building which includes fixtures, the availability of capital allowances depends on the meeting of two requirements:

1. The pooling requirement;
2. The fixed value requirement (occasionally replaced by the disposal value statement).

The pooling requirement applies only where the vendor could have claimed capital allowances in the past. If they could not (perhaps because the expenditure was incurred before 2008 when the integral features provisions were introduced) then the purchaser does not have to meet either of the above requirements and can claim capital allowances on an apportionment of the sale price. The pooling requirement is that the vendor has pooled the expenditure into a capital allowances pool before sale – there is no need to have claimed any allowances but it must have been pooled.

The fixed value requirement is that the value of the assets has been agreed between someone who has brought a disposal value into account and the purchaser. This is to ensure that the same value is used on both sides of the transaction.

How does this affect the capital gains position of either party? The simple answer is that it doesn't. Any amount which is allocated to integral features does not alter the price of sale or purchase for capital gains purposes.

Example

A is selling property to B for £3million. The base cost was £1.5million.

A has pooled value of fixtures and claimed capital allowances; the current tax written down value is £100,000 and the original value allocated to that in the purchase of this property was £225,000.

The parties want to know what the best figure is to allocate to the fixtures in terms of optimising the tax position for each party. Indexation is ignored.

Capital gains

The capital allowances position has no impact on the capital gain of the company:

Sale price	3,000,000
Less Cost	<u>1,500,000</u>
Gain	<u>1,500,000</u>

The purchase price for the new owner is £3million.

Capital allowances

We will consider three options: we allocate (a) £225,000, (b) £100,000 or (c) nil.

<i>Fixtures sale price</i>	<i>BA for A</i>	<i>BC for A</i>	<i>Acquisition cost for B (eligible for CAs)</i>	<i>B is likely to be able to claim annual investment allowance on</i>
(a) £225,000 (max.)	Nil	£125,000	£225,000	
(b) £100,000	Nil	Nil	£100,000	
(c) £1	£99,999	Nil	£1	

the expenditure, assuming the assets qualify in general terms and the parties are not connected. The final decision may well depend on the negotiating powers of each side.

Structures and buildings allowance

If someone is buying a building from a previous owner (who is not the one who has built the property), then they will only be able to claim structures and buildings allowance (SBA) if the previous owner has incurred qualifying expenditure. No balancing charge or allowance arises to the vendor and the new owner simply continues to claim what the previous owner was claiming. The new owner may be able to claim their own SBA if they undertake renovation subject to the relevant conditions being met.

There is an impact on the capital gains calculation though. Any SBA that has been claimed has to be added to the proceeds, thus increasing the gain or reducing the losses.

Example

X Ltd constructs offices for rental for £2 million excluding land and it is determined that £500,000 relates to fixtures. SBAs are claimed on the balance of £1.5 million. This is allowed at a rate of 3% per annum, so £45,000 per year.

After seven years, the office is sold to a business for £3 million and (for a reason which is never particularly specified) agrees to allocate only £1 to the fixtures so that X Ltd does not get a balancing charge on the sale (all the value having been relieved using AIA)

The gain appears to be £1 million – as noted above, the value of the fixtures is not adjusted in either the sale price or the cost. But the SBA claimed (being £315,000 on the basis of £45,000 for 7 years) is added to the gain, so the total gain is £1.315 million.

The new owner can continue to claim £45,000 per year of SBA.

Contributed by Ros Martin