

Structures and Buildings Allowance – Impact of Leases

(Lecture B1122 – 7.28 minutes)

In the October 2018 Budget, the Chancellor announced the introduction of the new Structures and Buildings Allowance (SBA), which gives a writing down allowance of 2% p.a. (straight-line basis) on qualifying costs incurred on/after 29 October 2018.

This article looks at the impact of the SBA on leased properties and, in particular, which party will be entitled to claim the allowance. (See technical notice published by HMRC on 29 October at www.gov.uk/government/publications/capital-allowances-for-structures-and-buildings-technical-note.)

Where the granting of a lease is substantially no different from a purchase of the interest in land, the SBA will be allocated to the lessee, but the allowances will remain with the lessor if the term of the lease is less than 35 years.

Where neither of the above applies, a calculation will be required. The lessee will become entitled to the full amount of the SBA if the amount paid as a capital sum for a lease [C] is $\geq 75\%$ of the sum of:

- that capital amount [C], and
- the value of the retained interest in the property (RV).

The income tax rules (ITTOIA 05, s.277) treat part of a lease premium as chargeable to income tax, leaving the balance as capital proceeds. This is the 'capital amount' referred to above.

Example – Pep Ltd leases a property to Jurgen Ltd

Pep Ltd owns a building on which it claims the SBA. It then grants a 40-year lease over the entire building to Jurgen Ltd, which will use it in its trade. Pep Ltd receives a premium of £35 million, but only a peppercorn rent is payable. Pep Ltd's retained interest in the property is agreed to be £10 million.

The income tax rules mean that, for a 40-year lease, 22% of the premium is chargeable to income tax, leaving £27.3 million (78% of £35m) as capital proceeds.

Using the above formula, the proportion is: $C / (C + RV)$. This is $27.3 / (27.3 + 10)$, i.e. 73.2%.

Because the lease is for over 35 years and the proportion is $< 75\%$, Pep Ltd will continue to be entitled to claim SBA, rather than Jurgen Ltd.

Had the reversionary value of the property been £9m rather than £10m, the calculation would have given a figure of 75.2%, in which case any SBA would be available to Jurgen Ltd rather than Pep Ltd.

In the latter case, when the lease expires in 40 years' time, any remaining SBA will be able to be transferred to the person holding the retained interest at that time, if they hold their interest as part of a qualifying activity.

It is important to appreciate that how much you receive as the capital sum for a lease may impact on your ability to continue to claim the SBA.

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