

Capital Allowances When Refurbishing A Building

When a property owner is undertaking the refurbishment of a building, there are two key questions that need to be asked in order to establish the tax treatment of the expenditure.

Firstly, is the expenditure a repair or is it an improvement. The former is a revenue cost with a 100% deduction in the year it is incurred, the latter is a capital cost.

Secondly, if it is a capital item, is it plant and machinery?

Repairs

A repair is replacing an item in the same position on a like for like, or current modern equivalent basis. For example, installing UPVC windows are a revenue item even though they could be an improvement.

It should be noted, however, that where more than 50% of an integral feature is replaced the item has to be treated as capital (see CAA 2001, sections 33A & B) and will only receive tax relief currently at 10%. Integral features are

- Electrical systems, including lighting;
- Cold water systems;
- Space or water heating systems, powered systems of ventilation, air cooling or purification and any floor or ceiling comprised in such systems;
- Lifts, escalators and moving walkways.
- External solar shading

Expenditure that qualifies as a repair will follow the accountancy rules for accruals which differs from that for capital – see CAA 2001, section 5.

Plant and machinery

Where the expenditure cannot be treated as a repair, it has then to be established if it is plant or machinery. The starting point is CAA 2001, Section 23, list C which sets out the main qualifying categories. The rate at which these items can be claimed will depend on its nature, as follows;

- Expenditure on energy saving or water saving technologies that meet the specific Enhanced Capital Allowances rules – 100% first year allowance
- General plant and machinery items – 20% on a reducing balance basis (18% from April 2012).
- Integral features and Long Life Assets – 10% on a reducing balance basis (8% from April 2012).

There is, however, a major difference with refurbishment schemes in that items of a structural nature that would not usually be allowable, can be claimed if the works are “**incidental**” to the installation of the plant or machinery- see CAA 2001, section 25.

In 2007 there was a test case on section 25 works – JD Weatherspoon vs HMRC which gave some further insight on claiming incidental items.

Typical items that could be classified as incidental works include;

- Installing a new lift shaft
- Demolition and rebuilding of walls to gain access for large items of plant or machinery
- Construction of steel or concrete platforms to support plant items
- Strengthening of existing floors to take increased loadings due to plant installations

- Drainage installations where new kitchens or toilets have been installed

The main problem with claiming “incidental works” is one of identification. Firstly it is necessary to have a close understanding of the project works so that any potential items can be investigated.

Secondly, once the items have been established the costs of the works have to be calculated. Often these will be in the substructure or superstructure elements or could just be within lump sum costs. Obtaining copies of the construction drawings, before and after photographs and well as close liaison with the building contractor are all key to preparing a detailed claim for incidental works. This can be time consuming but section 25 works can often add up to more than 50%

of the overall claim so the investment can pay dividends.

One further point on incidental items, is that they should be allocated to the relevant pool based on what the works relate to. For example a new lift shaft would be in the Special rate pool for integral features.

Other issues

It should be remembered that for all expenditure after 1 April 2008 (Corporation tax) and 5 April 2008 (Income tax) the first £50,000 of a business’s expenditure on plant and machinery is given as the Annual Investment Allowance and can be claimed at 100%. This has been increased to £100,000 for expenditure in years ending April 2011 and 2012, however, from 1 April / 6 April 2012 the AIA will be reduced to £25,000.

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