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21 September 2017

TAXATION

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£8.50
No: 4616
ISSN 0040-0149

THE VISION IS DIGITAL

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Making capital allowances claims for property fixtures.
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explains the practicalities of making capital allowances claims for property fixtures.

The benefits of capital allowances 'fixtures' claims on commercial property are well established. The timing of relief, the entitlement of property syndicates to the annual investment allowance, and the use of capital allowance related losses are all important. As well as these, practitioners need to be aware of how and why reports are prepared in the format that they are.

All references are to the Capital Allowances Act 2001 unless stated otherwise.

Benefit of fixtures claims

The potential value of fixtures claims for commercial property can give significant relief against income for the qualifying parts of a capital asset. ***Table 1*** indicates typical proportions of fixtures by building type although the ranges can be higher or lower than indicated depending on circumstances such as unusual features and whether both main and special rate pools are available.

Dwelling houses are excluded from claims by s 35, although fixtures within furnished holiday lets will qualify.

'Fixtures' refers to fixed plant and machinery in buildings, such as electrics, water systems, air-conditioning and lifts. Section 173 describes fixtures as 'plant or machinery that is so installed or otherwise fixed in or to a building or other description of land as to become, in law, part of that building or other land'.

HMRC's *Capital Allowances Manual* at CA26025 adds:

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'Property law distinguishes between chattels and fixtures. A chattel is an asset which is tangible and moveable. A chattel may become a fixture if it is fixed to a building or land. For example, before it is installed in a building as part of a central heating system, a central heating radiator is a chattel. Once installed, it becomes a fixture.'

Remember that claims are relevant to properties used in a trade or let to third parties. There are a several situations when a fixtures claim on a property is possible:

- A property that is built, extended or refurbished.
- Property acquired some time ago; as long as it is still owned and used it is possible to look back indefinitely.
- Commercial property bought directly from the developer.
- Second-hand commercial property when bought or sold. This is a critical time for the purchaser and if the owner has not claimed by now this is their last chance.

If the property is later sold at a profit, a fixtures claim will not increase the capital gain because the cost of fixtures will remain part of the capital gains tax base cost. However, disposal is the

KEY POINTS

- The proportions of commercial property value relating to fixtures means that significant tax relief can be claimed.
- Dwelling houses are excluded from claims by CAA 2001, s 35, but fixtures in furnished holiday lets can qualify.
- A fixtures claim does not increase the capital gain because the tax base cost is unchanged.
- Worked examples of claim methodology.
- Losses can be claimed by capital allowances claims, but remember possible restrictions to the relief.
- Do not neglect the negotiating position of parties to the property transaction or the election requirements.

TABLE 1

Average claim per property type

Type	*% of fixtures*
Hotels	15 – 40
Care homes	20 – 40
Offices	12 – 40
Retail	3 – 25
Industrial	5 – 25
Furnished holiday lets	10 – 25

time when the value of the capital allowances claim itself can be carelessly lost through balancing charges on previous writing-down allowances, or failing to keep the remaining pool. To prevent this, attention should be paid to the vendor's negotiating position in the sale process. So double tax relief is possible, and within the rules.

CLAIM METHODOLOGY – STEP 1

			Claim £
Estimated main pool – restricted claim		116,132 x	
Restricted to vendor's original cost:	Vendor's original property cost =	275,000	22,025
	Purchaser's property cost	1,450,000	
Estimate integral features – unrestricted claim			93,617
			115,642

Timing of relief and 'old' claims

Ensuring a client understands the timing of relief is important in not turning a 'big win' into a slightly disappointing one along the lines of 'but I booked a holiday to Bermuda next month on the back of this…'

Many fixtures claims are made years after the expenditure was incurred. Special rules apply to acquisitions from 1 April 2012 when availability may be lost without the correct action being taken on the transaction. If, instead, a property was acquired before 2012, there is no time limit for the owner to make a claim (but see the impact of 'methodology' later and how it affects the claim value). Because the annual investment allowance (AIA) is available only 'for the chargeable period in which the AIA qualifying expenditure is incurred' (s 51A) it is often out of time limits. In such cases, only the normal writing-down allowances of 18% or 8% are available.

To speed up relief, attention turns to kick-starting the claim by amending the earliest in-date years. For income tax, the deadline for submitting a capital allowance claim is the 31 January that is 22 months after the end of the tax year. For corporation tax, it is two years after the end of the accounting period. Under self-assessment, the earliest year for which a claim may now be made is 2015-16 and this will remain the case until 31 January 2018.

Without the AIA, and assuming that no enhanced allowances are available on energy-saving equipment, within the first five years of claim 63% of the available main pool allowances will have been claimed, or 34% of special rate pool allowances.

Claim methodology – Step 1

What follows is a rough guide to how a valuation-based fixtures claim is calculated. In our example of a 2016 acquisition of a second-hand property, a client acquired offices in Leeds for £1.45m from a vendor who had themself acquired the property in 1997 for £275,000.

After establishing the previous ownership history and the new owner's entitlement to claim allowances, the values of qualifying assets within the main and special rate pools were established after a site visit by the surveyor.

The claim includes fixtures such as:

- lift;
- hand basins, soap dispensers and warm-air hand-dryers;
- telephone and data connections;
- fire alarms and smoke detectors;
- door signage;
- entrance door intercom;
- emergency lighting;
- general lighting and power;
- mains switchgear; and
- hot water installation.

The valuer, having used the published rate ranges for each item (as set out by *Spon's Architect's and Builders' Price Book 2017*, BCIS pricing books and building cost information (formerly Wessex) and the Valuation Office Agency), adjusted these for date and location and their own knowledge and judgment to arrive at a main pool and special rate pool value of the fixtures. The figures will include a notional allowance for 'preliminaries' and professional fees of the construction of the property.

> ***"Many fixtures claims are made years after the expenditure was incurred. Special rules apply to acquisitions from 1 April 2012."***

The main pool of £116,132 is restricted pro rata to the vendor's own cost of the property as a fraction of the current purchase price (£1.45m) against the vendor's purchase price (£275,000), in this case giving a main pool of £22,025. The further back in time the vendor acquired the property, the less valuable a restricted claim will become because property inflation reduces the fraction.

Because the vendor acquired the property before April 2008 – and thus could not themself qualify for integral features – the purchaser has full entitlement to the integral features allowances, which has been valued at £93,617, without needing to restrict the claim by reference to the vendor's purchase price. As shown in ***Claim methodology – Step 1***, this gives total main and special rate pool figures at this point of £115,642 – but this will not be the final claim.

Claim methodology – Step 2

The requirement of s 562 is that a 'just and reasonable apportionment' should be made, as shown in ***Claim***

CLAIM METHODOLOGY – STEP 2

	£	
P =	1,450,000	Purchase price
A =	115,642	Purchase date replacement cost of P&M
B =	797,436	Purchase date replacement cost of non-P&M building
C =	388,059	Purchase date land value

$$P \times \frac{A}{A + B + C}$$

Claim £

$$£1{,}450{,}000 \times \frac{115{,}642}{115{,}642 + 797{,}436 + 388{,}059} = 128{,}873$$

Or to put it another way...

$$\frac{1{,}450{,}000}{1{,}301{,}137} = 1.11 \text{ ('The multiplier')} \times 115{,}642$$

Add: apportionment of stamp duty land tax 5,155

134,028

methodology* – *Step 2. The capital allowances figure of £115,642 is further adjusted based on the Valuation Office Agency's preferred formula. That is an apportionment of the replacement cost of the plant and machinery, replacement cost of the non-plant and machinery building, and land value against the total property cost which again are for the valuer's skills set. The method was tested and accepted recently in the 2015 case of *Bowerswood House Retirement Home Ltd* (TC4299), when the taxpayer disputed HMRC's apportionment methodology and lost.

> ***"Joint letting does not, of itself, make the activity a partnership. Usually, there won't be a partnership."***

Note that Parts A to C of the apportionment formula shown in ***Claim methodology* – *Step 2*** will not add up to the purchase price because we are required to use the replacement cost of the plant rather than the amount actually paid for them. The function of the formula is that the claim will be pro-rated to the purchase price through the 'multiplier' factor within the formula. In other words, £115,642 is multiplied by 1.11 here and becomes £128,873.

Note that, depending on the land values, the multiplier can be less than one, in which case the £115,642 would have reduced rather than increased.

Finally, the correct portion of purchaser's SDLT is claimed for both pools based on the fraction of the qualifying claim over the purchase cost, in this case giving a further £5,155 and a total claim of £134,028. In reality, the end claim will comprise two separate pools, with the SDLT apportioned between both.

Although on the face of it 14% of the building comprised qualifying items, in this case, the main pool restriction brought down the claim value significantly. Yet a £134,000 corporation tax relief claim with an annual investment allowance fully available was still a significant tax saving.

The vendor had not claimed capital allowances, but could have done on the main pool. To effect the purchaser's claim, it was necessary for both parties to enter into a s 198 election for the main pool.

Property syndicates and AIA

Property letting syndicates are a popular way of holding commercial property assets, usually with a bare trustee holding the beneficial interest on behalf of each individual. Joint property ownership through syndication often functions similarly to a partnership, but there are some nuanced differences. What is unclear is whether the £200,000 AIA is available as a single allowance to the syndicate as a whole – to be allocated among its members – or whether each member is entitled to a full £200,000 allowance to use at their own discretion against their syndicate interest and any other relevant business assets.

HMRC's guidance in its *Property Income Manual* at PIM1030 states:

> 'Joint letting does not, of itself, make the activity a partnership. Usually, there won't be a partnership and the taxpayer's share from the jointly owned property will be included as part of their personal rental business profits… For there to be a partnership there must be a business. This is defined in Partnership Act 1890, s 45 as including "every trade, occupation or profession" and is a wider concept than "trade". *Griffiths v Jackson* [1982] 56 TC 583 suggests that letting property may sometimes be a business. Most cases of jointly owned property will fall short of the degree of business organisation needed to constitute a partnership. To accept that a partnership exists you would have to be satisfied that there is a similar degree of business organisation as in an ordinary commercial business. This means more than treating rental income as derived from a business of letting property – it must be business apart from that.'

In *Griffiths v Jackson*, the case report describes the business, noting that 'various services were available, including the provision of laundry, food, flowers and car hire, although some applied only to a particular property. The taxpayers spent approximately five hours of each day on work connected with letting the properties.'

HMRC's view on the absence of a partnership is based on the Partnership Act 1890, s 2, which states: 'In determining whether a partnership does or does not exist, regard shall be had to the following rules:

(1) Joint tenancy, tenancy in common, joint property, common property, or part ownership does not of itself create a

partnership as to anything so held or owned, whether the tenants or owners do or do not share any profits made by the use thereof.

(2) The sharing of gross returns does not of itself create a partnership, whether the persons sharing such returns have or have not a joint or common right or interest in any property from which or from the use of which the returns are derived.'

The point is the same as that regarding partnerships and stamp duty land tax (SDLT) if the 'sum of lower proportions' calculation within FA 2003, Sch 15 gives a nil charge. This overrides the deemed market value provision of FA 2003, s 53 if the transfer is to a company for nil consideration. However, that also needs there to be a partnership rather than mere property letting.

I asked HMRC to comment directly on its position on syndicates and the AIA. The department made several points.

- 'There is no specific tax provision for a 'syndicate'.
- 'HMRC would treat as a partnership, irrespective of its designation, any arrangement which satisfies the UK test for partnership (Partnership Act 1890, s 1(1)).
- 'So we would need to consider the specifics of the grouping before we could determine its tax provision.
- 'AIA applies to a qualifying person, which includes a partnership of individuals.
- 'The rules prevent more than one AIA being claimed for the same business, or in some cases disallow AIA altogether.'

Noticeably, HMRC did not refer to Partnership Act 1890, s 2 in its response, compared to PIM1030. If HMRC is treating syndicates as partnerships, this would also mean – as well as there being just one AIA – that any syndicate with a corporate member would be precluded from the allowance. This is due to the restriction of s 38A(3), which requires a partnership to be comprised wholly of individuals.

I note that CAA 2001 has a number of AIA entitlement restrictions, including s 51H(4) which states: 'Where the qualifying activities are carried on by more than one qualifying person, those persons are entitled to a single annual investment allowance between them in respect of the relevant AIA qualifying expenditure.'

For that to apply, it is also a requirement of s 51H(1)(a) – (c) that two or more qualifying activities are carried out by the same person and are related to one another. This is a reference to shared premises or similar activities (s 51J).

I am not convinced that HMRC has a fully thought-out position on AIA for syndicate members that is consistent with its position on partnership versus property letting elsewhere, nor that s 51H is applicable. It is arguable that AIA is available to each individual member, but it is unclear.

Losses created by capital allowances

A loss could be created by a capital allowance claim. Options for use of such a loss will include the following.

- The loss could be carried forward.
- Although for individuals a rental income loss can only be used against other rental profits of the same or future years, if the loss arises due to capital allowances an individual's property rental business can offest that loss sideways against general income under ITA 2007, s 120. However, bear in mind the 'limit on income tax reliefs' in ITA 2007, s 24A, which will limit the sideways loss to the greater of £50,000 or 25% of the taxpayer's 'adjusted total income'.
- A company can relieve a property loss against current year total profits and, if still unrelieved, against total profits of the next period (as long as the property business continues in that later period, under CTA 2010, s 62(5)).
- A 75% corporate group can relieve losses around its members.
- Corporates should bear in mind the more flexible approach envisaged for losses in the original Finance Bill 2017, before it became truncated before the general election, although those changes have been reintroduced in the Finance Bill published on 8 September.

> ***"For property acquisitions since April 2012, the buyer must be able to prove the provenance of their claim to fixtures allowances."***

Entitlement and CPSEs

For second-hand property purchases, the nuances of the elections requirements form a broad area. The key message is that, for property acquisitions since April 2012, the buyer must be able to prove the provenance of their claim to fixtures allowances. For older buildings, this can entail going back as far as 24 July 1996 to work through Land Registry records, previous elections and enquiries of previous owners.

The commercial property standard enquiries (CPSE) forms are key starting points to win or lose fixtures allowances on the transfer of a property, and responses should, at times, be taken with a pinch of salt because they can be from the misinformed or misunderstood.

Properly made, fixtures claims are a safe and robust form of tax planning and can create substantial tax savings. At the same time, cutting corners or not understanding the negotiating position of parties or the election requirements could cost clients dear in lost opportunities.

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