

Budget 2007 – Capital allowances

The Chancellor announced sweeping reforms to the Capital Allowances regime in an effort to simplify and update the outdated system as well as reign in some current allowances. These changes will have an effect on most businesses and particularly those in the manufacturing and hotel sectors.

- Industrial building allowances and agricultural building allowances
- Plant & machinery allowances
- Long life assets
- Research & development tax credits
- Business premises renovation allowance
- Enhanced capital allowances
- Expensive cars
- Land remediation tax relief
- Landfill Tax

Industrial Buildings Allowances (IBAs) and Agricultural Buildings Allowances (ABAs)

The budget introduced the gradual phasing out of IBAs and ABAs over the next 4 years with the tax relief being completely withdrawn from April 2011. In general terms, this relief was available at 4% for qualifying building expenditure for use in a qualifying business.

In an effort to restrict the possibility of tax driven property transactions over this phasing out period, the measures have been introduced in respect of balancing events (ie usually sales of relevant interests) occurring on or after 21 March 2007, subject to those already in a 'pre-commencement contract' or in respect of qualifying enterprise zone allowances. This will affect manufacturing, transport, hotel and agricultural businesses in particular.

IBAs remain available for prior periods and transactions, so subject to the relevant entitlement conditions being in place, the maximum benefit available from these allowances should be claimed in the current accounting period. In the long term, shifting as much expenditure from IBAs qualifying expenditure to qualifying plant & machinery expenditure will go some way in mitigating the loss of this relief with the dual benefit of accelerating the rate of relief.

Plant & Machinery Allowances (PMAs)

The rate of relief of PMAs within the general pool will be reduced from 25% per annum on a reducing balance basis to 20% from April 2008. In addition the Chancellor has introduced an annual investment allowance for the first £50,000 of investment in plant & machinery from 2008 – the details of this will be subject to a consultation process commencing in the summer. The first year allowance of 50% for small enterprises will be extended for a further 12 months. For those in the charge to corporation tax this applies to expenditure incurred on or after 1 April 2007, and for income tax, on or after 6 April 2007.

From April 2008, a group of fixtures that are integral to the building (the definition and application of which will be subject to consultation starting in the summer) will be set at 10%.

It will be in businesses interest to shift as much expenditure as possible from these integral fixtures (when defined) to other fixtures, or perhaps qualifying energy efficient assets.

Long Life Asset Allowances (LLAs)

Available on plant & machinery in manufacturing businesses (generally) that have a useful economic life of 25 years or more from new. The rate of relief for LLAs has been increased from 6% to 10% from April 2008.

Research & Development (R&D) Tax Credits

The rate of relief available to large companies incurring qualifying R&D expenditure increases from 125% to 130% from April 2008. For small & medium size enterprises (SME) the rate increases from 150% to 175% from April 2008. A company is defined as SME if it has fewer than 250 employees, an annual turnover not exceeding €50 million and/or a balance sheet total not exceeding €43 million.

The Treasury intend to extend the R&D tax credit available to SME's to include larger businesses (those with less than 500 employees). However this is subject to EC state aid approval rules and therefore commencement of this extension to the relief is yet to be confirmed.

Business Premises Renovation Allowance (BPRA)

This relief was first introduced in the 2005 Finance Act, however no commencement date was given at that time. This relief is available to businesses or people who own or lease property that has been vacant for a year or more in designated disadvantaged areas of the UK. Qualifying businesses can claim 100% relief on the capital expenditure incurred in renovating or converting the property to bring it back to business use.

The scheme does exclude premises that are refurbished or used by certain businesses, however e.g. fisheries and shipbuilders. This relief will now come into effect for expenditure incurred on or after 11 April 2007.

This relief covers all capital expenditure on the renovation or conversion costs so is a substantial enhancement on the other Capital Allowances that may have been available on the expenditure.

Those considering undertaking this work should seek advice as to their entitlement to this deceptively complex relief.

Enhanced Capital Allowances (ECAs)

The Chancellor widened the ECAs regime. The ECAs scheme was introduced to encourage investment by business in energy and water efficient technologies as defined in the 'Energy Technology List' or the 'Water Technology List. The scheme has been widened to include:-

- more good quality combined heat and power (CHP) schemes including those that use solid refuse fuel;
- from 2007 widening the water technologies already supported by the ECA scheme to include vehicle wash water reclaim units, efficient industrial cleaning equipment and water management equipment for mechanical seals;
- Biofuels plant that meet certain qualifying criteria – subject to EU State aid clearance; and
- An enhanced capital allowance for companies not in taxable profit to encourage wider use of water efficient technologies, qualifying biofuels plants and energy efficient assets.

Expensive cars

The budget included provisions for the removal of the 'expensive car' rules, to be replaced by a system based on car CO2 emissions. It is proposed that those cars with low emissions (less than 165kg/km) be treated as other PMAs in the general pool, with an adjusted rate for those cars with higher emissions. These proposals are still subject to an ongoing consultation, with the Treasury hoping to publish results from the consultation in summer 2007.

Land Remediation Tax Relief (LRTR)

A consultation has been announced to improve the tax incentives for cleaning up contaminated land (LRTR). The consultation will consider whether the scheme should be extended to include long term derelict land, land contaminated by the invasive Japanese Knotweed (although it is open to debate as to whether this is already eligible for the relief) and remediation undertaken specifically to improve the development potential of the land. The consultation will also consider the landfill tax exemption currently available for waste from contaminated land.

The consultation will close on 14 June 2007.

Landfill Tax

The standard rate of landfill tax will increase from £21 to £24 per tonne for disposal on or after 1 April 2007. There will be a further rise to £32 per tonne for disposal on or after 1 April 2008.

The lower rate of landfill tax will also rise from £2 to £2.50 per tonne from 1 April 2008.

In order to encourage more sustainable waste management options, the Treasury has indicated that the standard rate of Landfill Tax will increase by £8 per tonne per year from 1 April 2008 until at least 2010-11.