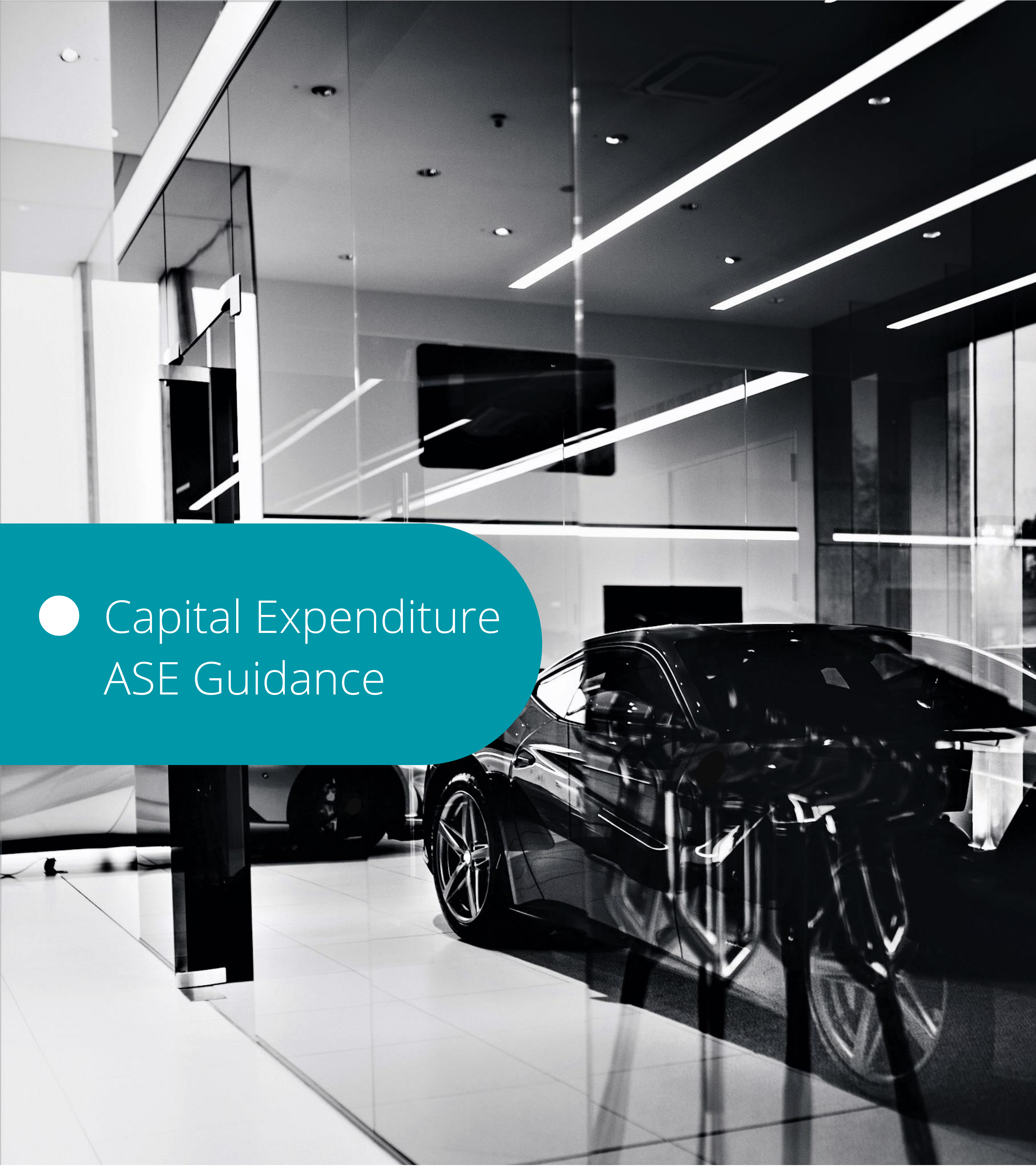

Capital Expenditure ASE Guidance

The Automotive Industry's Trusted Advisor

Capital Expenditure- How to make the most of the Super Deduction?

Background

The Motor Industry is well versed in investing capital both in terms of the manufacture of vehicles and in terms of the distribution and sales of vehicles.

In relation to distribution and motor vehicle sales, the capital invested in dealerships has been an ongoing and seemingly ever increasing cost with the manufacturer requiring franchises to refurbish and build new buildings in order to promote the sale of vehicles.

Buildings and the land they are sited upon are primarily capital items and as such, the costs are only generally allowable when the building / land is sold.

However, whilst some of the costs associated with refurbishment may be allowable as a deduction for tax purposes as necessary repairs, in many more instances, the costs associated with a capital upgrade or a new build will have a considerable and identifiable proportion that is also allowable as a deduction for tax purposes as capital allowances.

The budget in March 2021 introduced two new types of tax allowance for capital expenditure – a super deduction of 130% and a First Year Allowance of 50%. The intention is to increase the amount of capital spend overall but also to bring forward planned expenditure to aid the economic recovery from the pandemic. With many brands and retailers pausing CI projects during the pandemic, we are expecting a rush of changes over the coming year which, managed correctly, should see retailers able to capitalise on this new deduction.

Items upon which the new 130% super deduction is claimable include Furniture, IT Equipment, Workshop Equipment, Sanitary Fittings, Fire Alarms.

Items upon which the new 50% first year allowance is claimable include Electrical Installations, Heating and Water Installations together with Re-Cladding Works where that work improves the insulation of existing buildings.

In order to help your own business recovery, this note sets out what you need to consider and how you can best benefit from both the new and existing reliefs currently available for asset purchases.

If capital is to be expended, there are now five types of capital allowances and a specific structures and buildings allowance available to enable some of the capital expenditure to be allowed as tax deductible. As a number of these reliefs are time limited, action should be taken now to bank entitlement and maximise the positive cash flow impact where possible.

How do I obtain tax relief for capital expenditure I incur?

When you acquire an asset you will normally write off its value in your accounts by charging depreciation. Depreciation is not usually tax deductible, but the tax equivalent, called capital allowances, may be available dependent upon what it is that you have acquired.

In addition, the structures and buildings allowance entitles you to reconsider how and when you use the capital cost as a tax deductible cost.

Currently there is a range of capital allowances available depending on the type of asset you acquire and when it is purchased.

The key allowances are:

- Writing down allowances
- Annual Investment Allowance
- First Year Allowances
- New Super-deduction
- New 50% First Year Allowance
- Structures and Buildings Allowance

Writing down allowances

Writing down allowances depend on the type of asset acquired with purchases being categorised as falling within either the main rate pool or special rate pool. Main rate pool expenditure attracts a writing down allowance on a reducing balance basis of 18%, whilst the special rate percentage is only 6%.

The greatest number of items will qualify for the main pool. Typically, main pool items include Furniture, IT Equipment, Workshop Equipment, Sanitary Fittings, Fire Alarms etc.

Special rate expenditure generally relates to integral features in a building, for example air-conditioning, water and electrical systems, together with thermal insulation added to existing buildings.

Annual Investment Allowance

The annual investment allowance is a specific 100% relief for qualifying plant and machinery purchases up to an annual threshold of £1m until 31 December 2021. This would be claimed instead of writing down allowances.

From December 2021, it has been widely forecast that this limit will reduce to £200,000.

Expenditure in excess of the annual investment allowance is automatically transferred to the writing down pool or pools and as such whilst it is not lost, it is carried forward as a deduction that will unravel over many years in future.

First Year Allowances

HMRC, in support of expenditure classed as environmentally beneficial qualified for 100% first year allowance arising in year of acquisition but without an upper limit. These first year allowances were withdrawn from 1/6 April 2020 so there is a limited time to amend earlier tax returns to take advantage.

Budget 2021 and the New Super Deduction and 50% First Year Allowance

These new allowances were introduced in the March 2021 Budget and apply to qualifying expenditure incurred from 1 April 2021 up to and including 31 March 2023.

The rates are:

- 130% on additions that ordinarily qualify for 18% main rate writing down allowances
- 50% on most new plant and machinery investments that ordinarily qualify for 6% special rate writing down allowances

Specific Exclusions in relation to capital expenditure includes:

- Used and second-hand assets
- Expenditure on contracts entered into prior to 3 March 2021 even if expenditures are incurred after 1 April 2021.
- Connected party transactions
- Provision of plant and machinery for leasing (assets acquired under a hire purchase contract will qualify but must be in use by the year-end in order for allowances to be claimed). This leased assets exclusion is particularly relevant if properties are held in a separate property entity and leased in their entirety to a trading entity – the new super deduction and first year allowance are denied.

Claiming back tax deductions

Normally when an asset that qualifies for allowances is sold / scrapped, any proceeds reduce the amount of future allowances available spreading the tax effect of a disposal over a number of years.

In relation to the new super deductions, assets that qualified for the deductions are to be kept in separate pools up to 31 March 2023 to enable the proceeds to be computed at 130% of the amount received. After this date, the proceeds will be computed at 100% only.

Consequently, it is possible to buy and sell / scrap an asset at a different tax deductible value just as it will be equally possible that the reversal of relief could take place at a time when the business is subject to a higher rate of tax.

From experience, we know that many dealers tend to continue to use assets until they are scrapped which will mean nil proceeds on disposal and no reversal of relief.

Examples

Looking at the three most common types of project, tax deductible / non-deductible expenditure falls within the following parameters;

Minor Refurbishments –	Eligible for capital allowance treatment	**40-55%**
	Revenue deductible	**10-15%**
	Ineligible	**30-50%**
Major Refurbishments -	Eligible for capital allowance treatment	**22-43%**
	Revenue deductible	**0-5%**
	Ineligible	**52-68%**
New Dealerships -	Eligible for capital allowance treatment	**25-37%**
	Revenue	**0-1%**
	Ineligible	**38-75%**

Structures and Buildings Allowance

Where a construction contract has been signed on or after 29 October 2018, Structures and Buildings Allowances (SBA) may be available at an annual rate of 3% on a straight-line basis. Costs on either construction or renovation of a non-residential building could qualify.

Qualifying costs include:

- Fees for design
- Preparing the site for construction
- Construction works
- Renovation, repair and conversion costs
- Fitting out works

Costs that do not qualify for relief include those qualifying for another type of allowance, financing and planning permission costs and the cost of landscaping or land reclamation.

This relief is modest and will probably be attractive to buyers who intend to retain assets for many years writing off the cost over a 30-year period.

However, if the intention is to sell or demolish the building in the short-term, it is sometimes better to not claim SBA. This is because any allowances claimed represent part of the tax base cost of the building and therefore the allowance claimed would be added to proceeds of sale of the building or create proceeds in the case of demolition.

How can I maximise claims for tax allowances?

For simple purchase of equipment, the identification and claiming of these new allowances will be relatively straightforward and require little in the way of planning. For construction projects, particularly CI upgrades, involvement of a property capital allowances specialist is recommended in order to maximise the level of allowances. The best way to maximise relief is to look at the range of allowances as a whole and see how they can be interlinked. This means for example that it is sometimes better not to claim the new 50% allowance on special pool expenditure and instead claim Annual Investment Allowances if available. This is an area where specialist tax advice is essential. We are able to provide both specialist property capital allowances and tax advice to maximise the allowances and prepare tax returns in the most advantageous way.

My business is not currently profit making, is there any point claiming allowances?

All of the allowances detailed in this article can be claimed even if you are in a loss making position.

If you have been in a profit situation up until now, this is the perfect time to maximise allowances due to a further announcement in the March 2021 Budget in relation to loss carry back rules.

Normally, a business can only carry back losses against profits it has made in the previous 12 months, but the Chancellor announced an extension to this for accounting periods ending between 1 April 2020 and 31 March 2022. Subject to certain caps, losses arising in these periods can be carried back for three years, with losses set against profits of the most recent years first before being carried back to earlier years.

Unused losses can be carried forward against future profits of the business, and with the corporation tax rate due to rise in 2023, this could actually provide savings at a higher rate than now. The big advantage of a loss carry back however is that it will generate positive cash flow savings more immediately as a tax refund will become due.

If you'd like to know more details about the above information, please contact our experts on the below details.

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