

Not much relief

Steven Bone looks at how the property industry will be hit by the changes to capital tax allowances

Investors and owner-occupiers are well aware that capital allowances are an important form of tax relief for the construction or purchase of commercial property and can generate substantial tax savings. However, for the first time in many years, the 2007 Budget announced significant capital allowances changes. Although the Chancellor announced a welcome cut in the rate of corporation tax paid by the largest companies from 30% to 28%, this is being financed by changes to the capital allowances system, which will hit the commercial property sector hard. In addition, smaller property companies will not benefit from this rate reduction, but will see their rate increase from 19% to 22%, which means they will be hit twice.

industrial sector and scarcely encourages investment. Job losses and business closures cannot be ruled out and will, in turn, cause damage to the investment market. However, larger investors with steady income streams may be better able to ride out the storm and see their competitive position strengthened over their smaller rivals.

Tax relief for new industrial buildings is given at 4% a year over 25 years. So, a company spending £1m to build an industrial property and paying tax at the 30% full corporation tax rate, would have expected to receive total tax relief of £300,000 in 25 annual instalments of £12,000. Or an investor acquiring a second-hand industrial building for £1m, with, say, 10 years of its 25-year IBA life remaining, would have expected to receive the same amount of tax relief in 10 annual instalments of £30,000.

However, the phasing out of IBAs (which effectively has a retrospective effect, as highlighted below) will be achieved by reducing the rate by one-quarter each year over four years.

For a new building, the rate of 4% will reduce to 3% from April 2008, 2% from April 2009, 1% from April 2010 and nil from April 2011. From April 2011 any of the expenditure that has not already been written off for tax purposes will simply be lost and will not attract any tax relief, so industrial investors and their tenants are sitting on a tax time bomb that is set to explode in 2011.

Plant and machinery

The rates of tax relief will remain in place for a year, but from April 2008 there will be two major changes that are effectively 'stealth' taxes, the scope and details of which will be the subject of consultation (expected to commence late July).

Firstly, the conventional rate of tax relief will fall from 25% per year to 20%, so that the tax relief is given slightly more slowly. However, whereas the present rate applies to all plant and machinery, including business apparatus and plant fixtures in buildings (such as heating, cooling and hot water systems, sanitary installations, etc), the new rate is expected to apply only to moveable assets (i.e. chattels) and occupiers'/tenants' trade fixtures.

Secondly, the rate of tax relief for 'certain fixtures integral to a building' (with no further details available at the time of going to press), which presently qualify at 25% will fall to 10%. This is intended to reflect the Chancellor's concern that capital allowances should mirror true economic depreciation and be based on how long assets will actually last.



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“Larger investors with steady income streams may be better able to ride out the storm”

Industrial buildings

The main surprise presented in the Budget was the phasing out of industrial buildings allowances (IBAs), which have been available for more than 60 years for industrial premises (including manufacturing, transportation, and some storage) and since the 1970s for qualifying hotels. Treasury forecasts suggest that this move will raise additional tax of £1.15bn by 2011, which more than compensates for the £1.02bn tax the Treasury expects to lose as a result of reducing the large companies' corporation tax rate.

The abolition of IBAs has widely been viewed as an attack on the UK manufacturing and hotel industries, and their landlords. Coupled with the Chancellor's move to remove rate relief on vacant industrial properties, this is a huge blow to the

