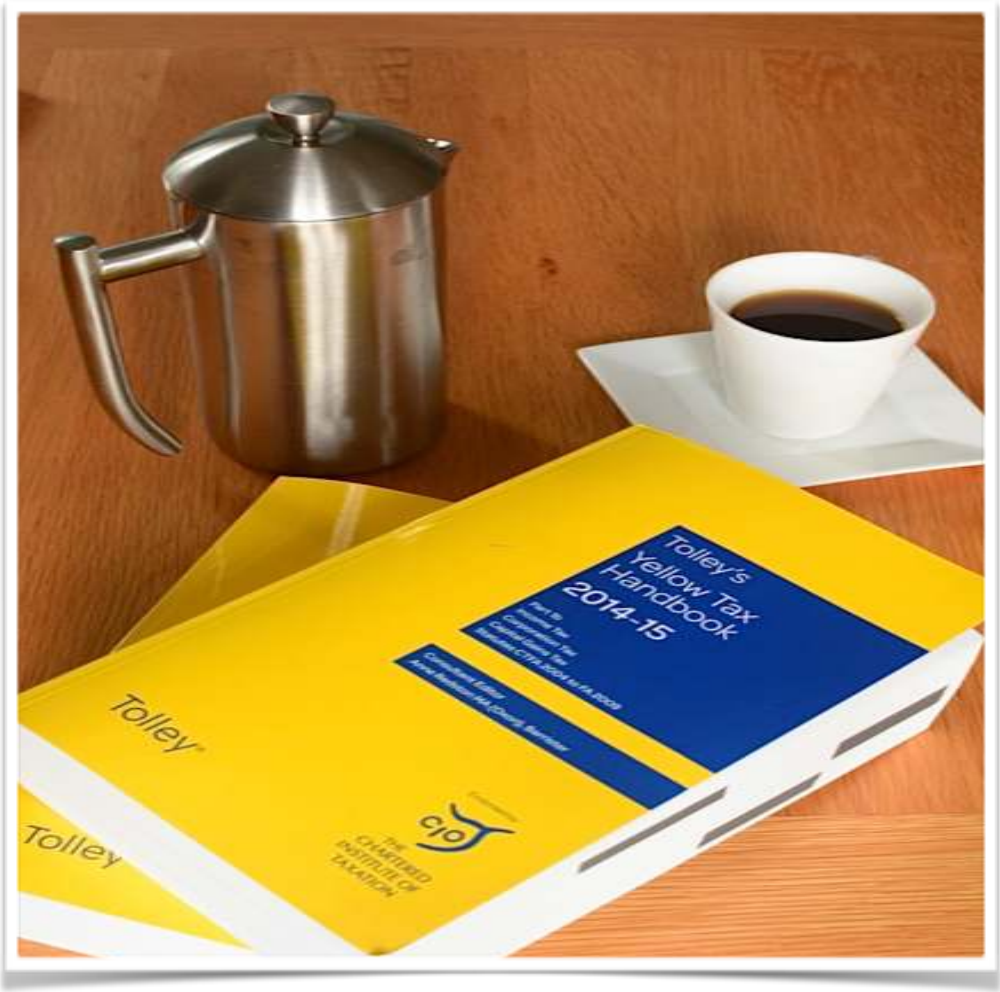
KEY PERSPECTIVES



Copyright G Stirling Photography

EFFECTS OF THE 2014 "POOLING" REQUIREMENT

18 months on, how are the new rules affecting claims?

The Finance Act 2012 introduced new rules on capital allowances (CA's) for sellers and purchasers but it wasn't until the April 2014 that the full effect of the "pooling" requirement was felt. We have been working with Richard Whittaker of Incentax Limited to look at the effects, so, 18 months and some 100 purchase claims later how are the new rules affecting claims:

> **"Potential PI issues have thrown the spotlight onto CA's meaning their value is being considered much earlier."**
>
> *LOIS STIRLING*

- potential PI issues have thrown the spotlight onto CA's, meaning their value is having to be considered much earlier;
- advisors are becoming aware of the need to agree CA's before exchange;
- it is now purchasers mostly driving the CA's negotiation;
- old £2 joint election clauses previously inserted by sellers advisors are increasingly being challenged;
- significant numbers of sellers who had previously not bothered with allowances are now having to "pool" their allowances entitlement before they can sell;
- the overall effect of legislation will be to reduce friction as was intended and proper due diligence will therefore now be key to maintaining client confidence.

Section 198 (199) elections

When elections were introduced in 1997, it triggered a realisation that sellers could legitimately keep some of the benefit of the allowances after the sale. By matching a low disposal value to the new buyer's CA's entitlement, in theory, HMRC wouldn't lose out. The problem was, over the years, as properties changed hands several times, the due diligence in some sectors was not as robust as it should've been; leading to some successive purchasers obtaining much higher levels of CA's than they were entitled to.

Following the changes, HMRC is now faced with much simpler checks for disposals under FA 2012, therefore, it is much easier to police and enforce rogue double claims.

Much has been published on applying the new rules, so we are not going to cover this again, but more importantly cover what effect is the pooling requirement having in practice and upon clients and their advisors?

Buyers have woken up

…to the effect that unless CA's are now addressed before the exchange of contracts, a buyer will, in all likelihood, lose most if not all of their potential claim value.

So, whereas under the 'old rules' it was (wrongly) considered that the CA issue could be dealt with long after the completion date, a few well-placed technical publications have recently highlighted that advisers who fail to consider the buyer's entitlement during the transaction could well be held accountable for any financial loss.

This message seems to been received clearly in the accounting world, but not by solicitors and, only recently, we are aware of multi-million pound hotel acquisition in London, where there is no mention of the CA's position. An awful lot of tax relief was gambled and any purchaser would be right question the quality of the advice having just lost over millions in capital allowances. The client was only able to salvage an overage claim, as completion had already occurred, but only as the seller's original acquisition date being before April 2008.

This is not an isolated case but is the largest example about planning so far we are aware of. The message is clear - consult an adviser before any exchange, even if this is only a few days away, something is always possible.

Image courtesy of dreamtime.com

So who is in control?

We are finding that it is now buyers who are driving the CA's position, which is not how it used to be.

This has meant that those sneaky £1 and £2 joint election clauses, which used to be slipped in and not questioned by the buyers advisors, are now very rare because CA's are firmly in the spotlight. So, the new rules have at least brought the consideration of CA's to the forefront.

For accountants particularly, this means ensuring your client's property portfolios have been reviewed for possible claims before they come to sell, to avoid a) embarrassment that it took a third party to flag this benefit to them and not you and b) if a buyer insists they want the CA's and nothing yet has been pooled, this is not a distraction during the sale, something nobody wants.

Buyers beware

As buyers have the most to lose under the new rules, the seller's CA's position must be established before exchange to avoid financial loss, and entitlement issues resolved.

Usually, the CPSE responses will provide a clue but they will not necessarily give the full picture without further investigation, especially if they are crossed through or "not applicable" is used. This must always be questioned, otherwise 'n/a' will stand for no allowances!!

Before exchange, a buyer must establish that the the seller has or will pool all allowances to which they were entitled. If they have not done so, appoint a specialist to estimate the cash savings involved, and where significant and as part of the negotiations to purchase, insist the seller pools their entitlement and passes the benefit on to the buyer in an election.

Sellers who have to yet claimed their CA entitlement

We are finding that in most cases, the seller is keen to cooperate with the buyer so as to avoid delaying the purchase completion.

Correctly worded warranties are now inserted in the contract that require the seller to pool the allowances and execute the election for the buyer thereafter, usually within three months of completion. It is a matter of negotiation who pays for this work, as it will be the buyer who is really benefiting from the tax relief, but the seller may get a slightly enhanced sale price.

Overage claims

Under the new rules a seller can only pool allowances to which they were entitled, and, in some cases, they may not be entitled to claim Integral Features were they brought the property prior to April 2008, and so can't pool as they were not entitled to claim upon them.

This means the buyer could be entitled to undertake a CA Act 2001 S562 apportionment valuation on this element. And in our experience, the likely value for typical office commercial premises representing the value of IF's will be around 10% of the purchase price. With an overage claim, it is still necessary to prove that no claim for integral features has been made by any former owner and a disposal value brought in regardless of when the seller acquired building.

Image courtesy of dreamtime.com

Non-taxpayers

Buying from a non-taxpayer can require more due diligence than buying from a taxpayer, especially for non-taxpayer acquired the property during the transitional period between April 2012 and April 2014. This is because the fixed value requirement will have been in force, and some pension funds may have overlooked the allowances position with potentially disastrous consequences all future owners.

Types of non-taxpayer include charities, pension funds and developer traders, with proper due diligence in many cases buying from a non-taxpayer will often mean an unrestricted claim for the new owner. However, this must be subject to investigating a previous owners disposal values, back to 1996 where a non-taxpayer required prior to April 2012.

Annual Investment Allowance (AIA)

It is a relief, that the annual investment allowance will continue in 2016, albeit at a lower £200,000 threshold, down from the current £500,000. By maintaining the AIA, it does mean the smaller property acquisitions can still be worthwhile economically for both clients and advisors. If this was ever to disappear it would probably mean that the viable threshold for a s562 apportionment claim, due to low tax rates rising to £1 million or more.

Impact of FA 2012 the so far

The further we go from April 2014, as buildings change hands, checks will eventually only need to be made back to this date. In the meantime, we will still see many properties which still require investigation for any previous owners disposal values as required by CAA 2001 s185. Checks back to July 1996, are now mostly in the sub £1million value category. However, these can still yield valuable and often unexpected tax relief for clients.

If you would like to further information on the opportunities and necessities around the 2014 "pooling" changes , please contact either Lois or Alan. Alternatively you can email us at info@cavettaconsulting.com.

Key Contacts

Scotland (East)
Lois Stirling
07909 962279
lois.stirling@cavettaconsulting.com

Scotland (West)
Alan Cadden
0770 333 4317
alan.cadden@cavettaconsulting.com

Incentax Limited

Contact
Email:richard@incentax.uk
Tel: 01926 270038
Mob: 07831 440038
Web:
www.incentax.uk

Image courtesy of dreamtime.com