KEY PERSPECTIVES

When is a Repair is not a Repair - Replacing Integral Fixtures

The repair and renewal of fixtures within a commercial property used to be a relatively simple matter for tax purposes. Taxpayers could claim a 100% deduction from taxable income for qualifying repairs, like for like replacements or replacement of obsolete assets with the nearest modern equivalent.

"It is important to plan capital expenditure and seek advice."

LOIS STIRLING

However, The Finance Act 2008 introduced the concept of "integral features," which meant that the tax treatment of plant and machinery deemed to be an integral part of the building was altered. From 1 April 2008, expenditure incurred on the replacement of an integral feature, could no longer be treated as a revenue expenditure deductible for taxable profits. Instead expenditure now had to be capitalised even if it could otherwise be treated as a repair to the building concerned.

The main impact for taxpayers is that revenue expenditure is fully tax deductible in a longer time period, unless they qualify for a first year allowance.

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What is an Integral Feature?

Unlike other plant and machinery, the statute defines for us what an integral feature is. The item of expenditure must be included within the list of integral features as set out at CAA 2001 Section 33A, and currently it consists of the following:

(a) an electrical system (including a lighting system),

(b) a cold water system,

(c) a space or water heating system, a powered system of ventilation, air cooling or air purification, and any floor or ceiling comprised in such a system,

(d) a lift, an escalator or a moving walkway,

(e) external solar shading.

Where an item falls within any of these categories the total costs of replacing the fixtures will also include any costs associated with removing or demolishing the plant and machinery, together with any costs that are incidental to the installation of it in accordance with s25 CAA2001.

When is an Integral Feature replaced?

An asset which is an integral feature is treated as having been replaced, if the expenditure incurred on repairing or replacing parts of the specified asset has, in any 12 month period, amounted to more than 50% of the replacement cost of the integral feature. This is defined in Section 33, CAA 2001

So what are the implications for my tax liability?

It is clear that pre 2008, the taxpayer was obviously in a better position, in that they could immediately receive a full tax deduction for expenditure on repairs and replacements of assets now deemed to be in the year of expenditure rather than having expenditure which, although qualifies for capital allowances, is relieved over a number of years.

However, there are other considerations over and above this. Firstly, the first £200,000 of qualifying expenditure may qualify for 100% annual Investment Allowance. In addition, the capitalised expenditure will reduce any capital gain arising when the property is sold, assuming that, the property value increases by at least the cost of the integral feature. If the expenditure is treated as revenue expenditure, no addition will be made to the capital cost base and therefore, the gain on the sale of the building will not be reduced by the cost of the integral feature.

Conclusion

In order to truly understand the tax implications, consideration must be given to not just the current cashflow but also to the later cashflows and beyond as situations arise where the capitalisation of expenditure may be of benefit to the taxpayer. Comparison examples of this are beyond the scope of this short article. However, in general for most companies in most scenarios they should not be disadvantaged by capitalising the expenditure. For individuals, in the long term they may be disadvantaged, but in the short term this should not be the case especially if the allowances are retained.

Our Service

We offer a no obligation review of completed or potential schemes in order to determine whether a viable claim for property tax reliefs can be claimed. Our fee structure is tailored to take account of the tax status of the individual or business and is designed to add value to your business.

If you would like further information on this topic or any other capital allowances issues, please contact Lois or Alan. Alternatively, you can email us at info@cavettaconsulting.com.

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