



# The Interaction of Capital Gains Tax with Capital Allowances

## Background

It is a common belief that if capital allowances are retained when disposing of a property, there will be an increase in the amount of capital gains tax to be paid. Generally, this is wrong.

There are two occasions when capital allowances do have an impact on the calculation of capital gains and these are in respect of: -

- a) when the asset is sold at a loss
- b) the asset sold is a wasting asset

## Disposal at a loss

Where a property is sold at a loss, the capital allowances are taken into account when calculating the allowable loss. In calculating the allowable loss, the value of the retained capital allowances is deducted from the unadjusted cost of the property thereby reducing the adjusted cost of the property and subsequent allowable loss. See example 1 on the following page.

## What are wasting assets?

In simple terms, wasting assets are items of plant or machinery that are not fixed to the building. Those items of plant or machinery which are affixed to a building are referred to by the Capital Allowances Act 2001 as fixtures and under property law, they are deemed to be part of the building. The sale of a property containing fixtures is viewed for the purposes of capital gains, as the disposal of a single asset, namely the building.

The Taxation of Chargeable Gains Act 1992 (TCGA 1992) states in s44 (1) (a) that "freehold land shall not be a wasting asset whatever its nature and whatever the nature of the buildings or works on it".

## All other property disposals

With the exceptions outlined above, the disposal of property at a profit does not require capital allowances to be considered when calculating the capital gains position. See example 2 on the following page.



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### Example 1 – Property Sold At Loss

Property purchased in January 2000 for £6 million  
Capital Allowances claim in 2000 of £1.5 million  
Property sold in January 2007 for £5 million  
Disposal value fixed by CAA 2001, s198 at £0.5 million  
No indexation applicable to capital loss

CGT Calculation		£
Disposal proceeds of property		5,000,000
Adjustments for Capital Allowances (CAs):		
Total CAs	1,500,000	
Less disposal	500,000	
Value retained CAs	1,000,000	
Unadjusted cost of property	6,000,000	
Less retained CAs	1,000,000	
Adjusted cost of property		5,000,000
<b>Allowable Loss</b>		<b>NIL</b>

#### Result

Allowable loss - NIL  
£1,000,000 capital allowances retained

### Example 2 – Property Sold At Gain

Property purchased in January 2000 for £6 million  
Capital Allowances claim in 2000 of £1.5 million  
Property sold in 2007 for £8 million  
Disposal Value fixed by CAA 2001, s198 at £0.5 million

RPI in January 2000: 166.6  
RPI in January 2007: 201.6

CGT Calculation		£
Disposal of Property		8,000,000
Less Cost of Property		6,000,000
Unindexed Gain		2,000,000
Less Indexation Allowance		
$(201.6 - 166.6) / 166.6 = 0.210 \times 6,000,000$		1,260,000
<b>Chargeable Gain</b>		<b>740,000</b>

#### Result

£740,000 chargeable gain  
£1,000,000 capital allowances retained