



Retaining Capital Allowances on Property Disposals

Background

If capital allowances have been claimed in respect of fixtures on a property, the sale of that property is deemed to be the cessation of ownership of that fixture, and the owner is therefore required to bring into account a disposal value for that fixture.

Section 196 of the Capital Allowances Act 2001 gives an indication of how the disposal value is to be calculated. In essence, the disposal value should be a part of the expenditure that is incurred by the purchaser of the property on the provision of the fixture. This all sounds rather complicated, as is the case with the interpretation of a lot of the Capital Allowances Act 2001.

However, what it means is that if, as a seller, your property has increased in value over the period of your ownership, then when the purchaser apportions his expenditure on the property, he could assess that the cost of those fixtures to him is more than you as seller actually paid for them.

There is of course a restriction limiting the purchaser to claiming no more tax relief than the seller had claimed. In very simple terms, this legislation could force the seller of a property to pay back all of the allowances that they have received in respect of the plant and machinery.

What can be done to protect the seller's position?

CAA2001 Section 198 provides a mechanism whereby the seller and purchaser of a property can 'elect' to fix the disposal value of the fixture in relation to the sale and purchase of a particular property.

As the seller's objective is to fix the disposal value as low as possible and the purchaser's objective is to have it as high as possible, we can appreciate that this element of the transaction can become a point for negotiation.

For example, if the seller has submitted a claim of £1 million for plant and machinery allowances and claimed two years' worth of those allowances in their tax computation, the written-down value of those plant and machinery allowances will be £562,500.

If the buyer and seller agree that this is the amount to be inserted in the Section 198 election, then the seller will suffer no clawback of allowances and the purchaser will be able to claim the £562,500 in their tax computation.

However, if the seller insists that the elected amount is £2, then the seller will not only retain the allowances that they have had to date but also the residual £562,498, which will remain in the general pool of allowances. Therefore, even though the property is no longer owned by the seller, they will retain the benefit of the plant and machinery allowances attached to it.

Obviously, this latter position may appear inequitable to a purchaser and they or their agents may attempt to negotiate the disposal value upwards.

In any sale negotiation, the commercial value of allowances should not be underestimated.

For example, if a taxpayer such as an insurance institution, with a composite low rate of tax of around 8 or 9% is selling the property and a high net worth individual paying tax at 40% is purchasing that property, the allowances are worth significantly more to the high net worth individual than they are to the insurance institution. In these circumstances, both the buyer and seller of the property can calculate the commercial value of the allowances to the buyer. The buyer may then be prepared to offer an additional capital sum to reflect the increased value of the allowances to him.

Therefore, it may benefit the seller to dispose of the allowances at the full amount that they claimed and suffer the clawback if the purchaser can offer suitable recompense.

There are many scenarios that can arise out of the disposal of plant and machinery fixtures, and these issues should always be addressed in Heads of Terms and at pre-contract stage in all situations.

Capital allowances should never be overlooked by either the seller or the buyer, as they will always have a value to one party or the other.