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Note from the editor



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Since our last newsletter we have seen the Chancellor of the Exchequer George Osborne present his 2011 Budget to Parliament on 23 March and, a few days later, the government published the Finance (Number 3) Bill which will enact tax measures announced in the June 2010 Budget and the 2011 Budget. For our 2011/12 budget summary and tax tables please go to www.landtax.co.uk/resources.

This issue looks at capital allowance changes introduced by the coalition

government that will start to affect businesses in the coming months and HMRC consultants. We also have a guest article from Edmund Bailey of Carter Jonas LLP that looks at hydroelectric power.

The next edition of our newsletter will be available by email so if you would prefer to receive a copy electronically, please send your name, post code and email address to info@landtax.co.uk with subject line showing as 'E-newsletter'.

Capital allowances – the recent changes

Graham Boddington

Since the coalition government came to power in May 2010 they have announced a number of changes to capital allowances that are likely to affect businesses that have invested heavily in plant and machinery or are likely to invest more than £25,000 a year in plant and machinery from April 2012.

The capital allowance changes published in the Finance Bill 2011, which is actually called Finance (Number 3) Bill because it is the 3rd Bill published this Parliament session, are as follows:

Plant and machinery writing-down allowances

Since April 2008 the main rate of

writing-down allowance that may be claimed on new and unrelieved plant and machinery expenditure has been 20% per year (previously 25%). However, from 1 April 2012 for corporation tax and 6 April 2012 for income tax, this main rate is to be reduced from 20% to 18%.

Certain types of plant or machinery, such as integral features of a building or structure (electrical systems, cold water systems, space or water heating systems, lifts escalators and moving walkways; and external solar shading), thermal insulation, long-life assets and cars bought from April 2009 that have CO2 emissions of more than 160g/km do not go into the main pool but, instead, go into the 'special rate' pool.

From April 2012 the rate of writing down allowance on expenditure in the special rate pool will reduce from 10% to 8%.

Traditionally, electrical and cold water systems have been treated as part of the building or structure and so did not normally qualify for any plant and

Bits and pieces...

Payback time for VAT fraudster

A convicted fraudster from Berkshire who was jailed for evading VAT of £1.3m in 2009 was ordered to payback almost £69,000 by 6 June 2011, or face a further 21 months in jail.

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machinery allowances. However, the introduction of the integral features rules in Finance Act 2008 meant that expenditure incurred on the provision or replacement (see below) of such systems on or after 1 April 2008 for corporation tax and 6 April 2008 for income tax, would qualify for writing down allowances as part of the special rate pool.

If expenditure is incurred on the replacement of an integral feature within 12 months of the initial expenditure being incurred and it represents more than 50% of the cost of replacing the feature, then it will count as special rate pool expenditure. If, however, the expenditure does not exceed 50% of the cost of replacing the whole feature, then it is likely that it will qualify as a repair.

For businesses whose chargeable period straddles 1 April 2012 for corporation tax and 6 April 2012 for income tax, a 'hybrid' rate will apply to unrelieved expenditure on plant and machinery in any pool. This will mean that an individual whose business has a 30 September 2012 year end will have a hybrid rate for the main pool of 19.03% ($188/366 \times 20\%$ plus $178/366 \times 18\%$) and a hybrid rate for the special pool of 9.03%.

Annual investment allowance

Also since April 2008 most businesses (see below), regardless of their size, have been able to claim the annual investment allowance (AIA) on up to £50,000 of their expenditure each year on plant and machinery, but excluding cars. From 1 April 2010 for corporation tax and 6 April 2010 for income tax the AIA was increased from £50,000 to £100,000 for expenditure incurred on or after those dates.

In the June 2010 Budget, George Osborne announced a package of corporation tax reform measures that included the phased reductions in the main rate of corporation tax and changes to the small profits rate.

Bits and pieces...

Furnished holiday lettings: new legislation

The 2011 Finance Bill finally introduced new furnished holiday lettings legislation. Some of the changes have effect from 2011/12 (1 April 2011 for companies), but the extended availability period of 210 days (instead of 140) and actual letting period of 105 days (instead of 70) will not take effect until 2012/13 (1 April 2012 for companies).

Amongst these measures was a reduction in the AIA from £100,000 to £25,000 for expenditure incurred on or after 1 April 2012 for corporation tax and on or after 6 April 2012 for income tax. The Government expect over 95% of business to be unaffected by this reduction in the AIA. However, we would expect significantly more than 5% of our clients will be affected by this change.

By way of a reminder, the AIA is available to:

- any individual carrying on a qualifying activity (this includes trades, professions, vocations, ordinary property businesses and individuals having an employment or office)
- any partnership consisting only of individuals (a partnership with a trust or company as a partner does not qualify); and
- any company (subject to certain restrictions). Only one AIA is available to all the companies in a group.

For businesses that have a chargeable period that spans 1 April 2012 for corporation tax and 6 April 2012 for income tax (the relevant day), transitional rules apply. The maximum allowance for a business for the transitional chargeable period comprises two parts:

1. the proportion of a year falling before the relevant day at the old £100,000 annual cap; and
2. the proportion of a year falling on or after the relevant day at the new £25,000 annual cap.

It should be noted that in relation to the second period (on or after the relevant day) the maximum expenditure that may be relieved for that period is the amount of the allowance for that period.

For example, a company with a transitional chargeable period from 1 October 2011 to 30 September 2012 will be entitled to a maximum AIA for the transitional chargeable period of £62,500 ($6/12 \times £100,000$ plus $6/12 \times £25,000$). If the company incurred no qualifying expenditure in the six months to 31 March 2012 and spent, say, £50,000 in the remainder of the year the maximum AIA available to the company would be only £12,500. The remaining qualifying expenditure in excess of the maximum AIA (£37,500) will only qualify for writing-down allowances, see above.

The timing of qualifying expenditure on plant and machinery over the next couple of years will be important for the cash flow benefit of obtaining earlier tax relief, at least as far as the AIA is concerned. In the above example, if it had been possible for the company to incur the qualifying

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expenditure in the six months to 31 March 2012, then it is likely that an AIA claim may have been made in respect of all of the £50,000 of expenditure.

To maximise the AIA (and writing-down allowances) on an item of plant or machinery acquired under a hire purchase agreement, it is essential that the item is brought into use before 5 April 2012, so that the full capital cost of the plant or machinery attracts allowances. If the item is not brought into use by 5 April 2012, only capital expenditure incurred under the agreement on or before that date will qualify for allowances with the benefit of the higher rate of AIA.

Short-life assets

In the recent Budget, the Chancellor announced an increase to the 'cut-off' period over which expenditure on items of plant and machinery (other than cars and certain other exceptions) can be given 'short-life asset' (SLA) treatment from four years to eight years from the end of the chargeable period in which the expenditure is incurred.

This increase from four to eight years, which applies to qualifying expenditure incurred on or after 1 April 2011 for corporation tax and 6 April 2011 for income tax, is likely to increase the range of assets for which a SLA election may be beneficial. In general, an election will be beneficial if the asset depreciates faster than the rate at which capital allowances are given and

it is disposed of before the cut-off date.

If the item has not been sold or disposed of by the end of the cut-off period, the remaining expenditure in the SLA pool is transferred to the main capital allowances pool.

A SLA election is therefore usually beneficial with high value items of technological equipment, such as computer systems, but will probably not be beneficial for farm machinery, which in recent years has generally held its value well.

Agricultural buildings allowance

I would remind you that agricultural buildings allowances ceased on 1 April 2011 for corporation tax and on 6 April 2011 for income tax.

Put your energy into something new



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....or into something old with a new twist....**Hydro Power is not a new phenomenon; indeed it is one of the oldest methods of generating energy.**

In its' simplest form, hydro-electric power requires a sufficient volume of water, and a height difference between the source and the waters outflow (referred to as the 'head'). The technology required to measure head can be as simple as utilising a length of spare garden hose, where the fall can be assessed at the bottom of a slope by measuring the top height at which the pipe can be held whilst remaining full, or by a pressure meter on a pipe – one to try at home!

The Technology

The designs of the turbines are very basic. There are those which sit in the air with water passing underneath, an example of which is the mill; there are those mounted in a tube through which water is channelled; and there are those that rely on the weight of the water falling through an open screw which drives a shaft. All types drive a generator which is mounted clear of the water. Thereafter inverters convert the power that runs through cables from DC to AC, and transformers feed the power either to a point of use on a property or into the grid.

The Motivation to Invest

The much written about Feed-in Tariff (FiT) is a financial incentive scheme from the Department of Energy and Climate Change (DECC) aimed at encouraging the development of renewable energy.

- It is a renewable energy subsidy offering a fixed payment per kilowatt hour of renewable energy generated, varying across technologies. It also has a proposed guaranteed minimum payment per kWh of energy exported to the grid.

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- Under FiTs, electricity suppliers will be obligated by law to buy energy from renewable generators at above-average prices, with this extra cost then spread over each consumer's energy bill.
- There is a proposed cap of 5MW for projects eligible for the subsidy, meaning that the scheme will only benefit micro through to medium scale generation.
- The Department of Energy and Climate Change (DECC) has proposed to set FiTs at a level which will offer projects a 5-8% return on investment.
- Feed-in Tariffs are set to be offered for a 20 year period, with the exception of solar PV projects for which the period will be 25 years.

Bits and pieces...

Tax receipts

Tax receipts from Income Tax, National Insurance Contributions and Capital Gains Tax increased from 2009/10 to 2010/11 by 4.2% to £247.4 billion, but this figure is still less than the receipts in 2007/08 (£253 billion) and 2008/09 (£252.6 billion).

There is also a wide range of reliefs available to hydropower developers, which has included reduced VAT, Business Property Reliefs, and Small Business Rate relief (where the business has a rateable valued below £15,000). Businesses that invest in plant and machinery used to generate electricity, or heat from renewable sources can claim the usual capital allowances, even if they are claiming FiT payments. The Annual Investment Allowance provides a 100% allowance on the first £100,000 of expenditure and Writing Down Allowances at a rate of 20% or 10% for any unrelieved expenditure.

There is also the means by which the full capital cost of the equipment can be offset against taxable profits made in the same period for energy saving equipment referred to as Enhanced Capital Allowances.

Presumably with such incentives, hydro-electric to be made possible has to be carried out on a large scale?

For any renewable facility to make an appreciable contribution – a contribution at all comparable to our current consumption – it has to be country-sized. To provide one quarter of our current energy consumption by growing energy crops, for example, would require 75% of Britain to be covered with biomass plantations.

A recent visit to the Dinorwig Power Station in Llanberis, North Wales put it into perspective. Water is stored at a high altitude in one reservoir and is discharged into another through the turbines during times of peak electricity demand. It is pumped back during off-peak times.

Although it uses more electricity to pump the water back than it generates on the way down, pumping is generally done at periods of low demand, when the energy is cheaper to consume.

The power station comprises six 300MW GEC generator/motors coupled to Francis type reversible turbines. The generators are vertical shaft, salient pole, air cooled units each having 12 electromagnetic poles weighing 10 tonnes a piece, producing a terminal voltage of 18kV, synchronous speed is 500rpm. From standstill, a single 450-tonne generator can synchronise and achieve full load in approximately 75 seconds. With all six units synchronised and spinning-in-air (compressed air), 0MW to 1800MW load can be achieved in approximately

16 seconds. Once running, the station can provide power for the whole of Wales for up to 6 hours before running out of water.

It goes without saying that not all properties have this potential!!

Big is not always beautiful - Micro – hydro the future?

Those that registered with the FiT before 1st April 2011 have already received the first increase of 4.8% with the payment being indexed linked. However those considering investing big should consider the following:

- Significant up front development costs involved in pursuing licence(s) from the Environment Agency, and planning from the Local Planning Authority. The bigger the proposal the tougher the negotiation.
- Grid connection. There are areas where a 17kw single phase connection is all that will be permitted due to the larger alternatives involving prohibitive upgrade costs.
- The FiT rate is banded. Even if water was available for a 101kw turbine, there would be little sense in pursuing it for loss of the higher rate of support for smaller schemes.
- Enterprise Investment Schemes and Venture Capital Trusts are set to only now be made available where commercial generation starts before 6th April 2012.
- The Annual Investment Allowance limit is to be reduced to £25,000 from April 2012.
- Writing Down Allowances rate set to be 18% from April 2012 or 8% from April 2012 for any unrelieved expenditure.

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- Government reviewing the need for Enhanced Capital Allowances on renewable energy plant and machinery

Bits and pieces...

New task forces to tackle tax dodgers

HMRC are launching new task forces to tackle tax dodgers, which aim to raise an additional £7bn each year by 2014/15. The specialist teams will target specific high risk trade sectors and locations across the UK. The first task force will focus on the restaurant trade, targeting businesses in London.

This is said to be required to ensure a better focus on smaller schemes. The reality, with lead in times for all of the above from anywhere from 12 to 24

months, could see those most exposed to the risk of cost (being smaller operators) worst affected.

However we have a number of really interesting examples of hydro-electric schemes which have also made possible something more than simply power; including restoration of previously disused reservoirs; improvement of domestic and agricultural water supplies and the recreation of wetland habitats. There is also the means by which the financing of such schemes can, with careful accountancy advice, provide for much needed strategic estate tax planning.

Please get independent professional advice

It is important that no matter what size

scheme being is proposed that owners / developers get the complete professional package of advice from accountants, lawyers and agents. The make up of the company structure within the timing and delivery of the scheme is crucial. The process of securing the entirety of the consents is very much likely to take longer than envisaged. I was interestingly reminded that the construction of the Dinorwig Power Station consisted of 16 km of tunnels, 1 million tons of concrete, 200,000 tons of cement and 4,500 tons of steel. It took only 3.5 years to deliver. The average lead in time for micro-hydro these days can take anywhere up to 2 years!! That's progress for you!

HMRC Consultations

Graham Boddington

Since the beginning of May 2011, the Coalition Government has published no fewer than 19 tax related consultation documents covering specific areas that the Government wish to change.

Each HMRC consultation set out what is being proposed, the scope to influence aspect of the policy detail that have not yet been decided and summaries the expected impacts of the proposed changes and the assumptions made by the Government in their assessment. Consultations normally last for at least 12 weeks, during which time the Government welcome views on their proposals from anyone who has an interest in the specific subject under consultation, such as groups representing taxpayers and their advisors.

We would expect the majority of our client's to be unaffected by most of these consultations, but a number of the proposals will affect some clients to a greater or lesser degree. I have identified the following seven HMRC consultations that I believe may be of most relevance to our clients, although other consultations may also be relevant:

- consultation on the removal of 36 tax reliefs. Please see the article below concerning the abolition of mineral royalties relief.
- Capital allowances on fixtures.
- Capital allowances: feed-in tariffs & the renewable heat incentive.

- a new incentive for charitable legacies - a lower rate of Inheritance Tax when leaving 10% of an estate to charity.
- Statutory residence test.
- reform of the taxation of non-domiciled individuals.
- the Simplification of Regulatory Penalties.

The closing date for responses to the first four consultations is 31 August 2011, and for the last three the closing date is 9 September 2011.

Details of the consultation documents may be found at www.hmrc.gov.uk/consultations

Mineral Royalties relief

Graham Boddington

On 27 May 2011, the Treasury issued a consultation document on the abolition of 36 tax reliefs that are “obsolete, unnecessary and distortive”, including relief for mineral royalties which will be of particular interest for landowners.

Briefly, the 50:50 split of mineral royalty income between Income and Capital Gains treatment (s157 ITTOIA 2005 & s201 TCGA 1992 for individuals) is to be abolished from 6 April 2013 with all mineral royalties thereafter being liable to Income Tax (or Corporation Tax for companies from 1 April 2013). This will increase the tax payable by individuals and trusts, as there will be no Capital Gains annual exemption available. Also the rate of tax payable on Income is greater than on Capital Gains.

The consultation is not on the proposed abolition of the relief, but only on whether “transitional arrangements for the removal of reliefs are fair and proportionate”.

One could become very cynical about the Office of Tax Simplification’s project for a clearer and more straightforward tax system. The changes all appear to have been revenue raising and although they may simplify the tax system, there must be a question mark over their “fairness”. I was interest to see in the consultation document that HM Treasury were unable to estimate the revenue impact of this removal as the tax return does not require tax payers to indicate whether they are obtaining this relief.

Finally, you may like to note that the exemption from excise duty for “black beer” will be abolished from April 2013. This exemption was originally put in place (in 1901) due to the historic belief that black beer has medicinal and nutritional properties and apparently black beer was the original black in a rum and black (rather than blackcurrant). However, black beer is generally of high alcoholic strength (around 8.5% abv) and so the Treasury have concluded that it can no longer be considered a “health” product.

your feedback...

We would like to know if there are any particular issues which are important to you and that you feel we should cover. Please do get in touch.

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