"Cash is King"… Boost Post Coronavirus Cash Flows by Revisiting Historic Property Expenditure
E³ Consulting Tax Update for Real Estate Investors

"Cash is king" an oft cited mantra by business gurus such as Jack Welch, (former CEO General Electric) and for many businesses in a post Covid-19 world it will be essential to optimise all available cash flows to help 'weather the storm' as businesses look to stabilise and rebuild their finances, brands, market share and profitability.

Tax efficiency is an important element of any cash flow review and particularly those businesses that have, in the past, invested significantly in their property assets, be it their head office, factory, warehousing, restaurant outlets or investment portfolio across the UK.

For many property owning taxpayers improving cash flows can be relatively challenging in any economic climate, in these exceptional times a property tax review may facilitate a cost effective, and more importantly, a fairly quick way to improve their cash flow.

Revisiting previous claims to ensure they have claimed all of the relief and fiscal incentives available. Or reviewing all current and historic property costs to identify any entitlements that had been overlooked. Specifically, there are significant opportunities to claim capital allowances (CAs), repair & maintenance (R&M) and land remediation tax relief (LRTR) – to recover overpaid tax previously paid to HM Revenue & Custom (HMRC).

Alun Oliver, MD of property taxation specialists E³ Consulting stated that *"in nearly thirty years of operating in the field of property tax, I still consistently see over 80% of cases reviewed, where either no claim, or a superficial claim has been made – meaning that additional tax savings can be achieved."* So it is essential that UK taxpayers consider re-visiting previous tax returns and bring in experienced and independent property taxation specialists to re-assess and review past expenditure to enhance their tax savings and where applicable obtain any applicable tax rebates.

Clients often perceive that it is all too late to change things, that the quantum of tax is simply too little to worry about, or that the costs are prohibitive. Sometimes their tax advisers even reinforce this 'do nothing' approach – occasionally because they don't wish to illustrate tax savings they had previously overlooked or missed – resulting in unnecessary tax payments, by their overly loyal clients! However, on condition that the assets are still owned, it is worthwhile reviewing all expenditure to see if additional allowances could be claimed. Stakeholders will require the directors and senior managers of businesses to explore all available options post COVID-19 to help protect jobs and deliver sustainable recovery and, in time, long term growth and success.

Historic Reviews

One recent project, involved a review of historic purchases within an investment portfolio for an off-shore non-resident landlord, paying income tax[1] at 20%. We reviewed seven properties which had been acquired between 2003 and 2016, each for between £3m and £7m. The later project had a s.198 election for £1 on the plant & machinery allowances, but the others pre-dated the 'New Fixtures Rules' and had either silent contracts, or were bought from pension funds. They had never claimed the capital allowances on these properties, still held within their investment portfolio. Their total tax saved over time will equate to nearly £1m (£4.9m x 20%). By amending a prior year tax return they will be able to obtain a significant tax rebate from HMRC, as well as further allowances going forward, also reducing their future tax payments, until all of the allowances are consumed.

Attention to Detail

Another recently completed project, was a review of recent construction costs for a GP surgery in South Wales, following a significant refurbishment of their existing premises - the practice partners largely paying income tax at 40% or 45%. We reviewed the final account and liaised with the project architect to obtain the project data on this 2018/9 project. Their accountant had made a claim for capital allowances, but had not fully optimised the available tax savings. Our further review enhanced their capital allowances claims for plant & machinery, integral features and also repairs & maintenance deduction, over and above the prior claims and NHS grant adjustment, of over £150K. Their total tax saved over time will equate to over £67K (£150 x 45%). As all the GP partners are individuals, the capital allowances will also be eligible for the accelerated 100% Annual Investment Allowances (AIAs)[2] ensuring their tax saving will be fully utilised in their amended tax return for the year ending 5th April 2019.

Enhanced Capital Allowances (ECAs)

ECAs are given at 100% in the first year and were available on energy and water efficient assets that meet either a performance criteria or are approved by The Carbon Trust up until March 2020 (Energy & Water Technology Lists).

Normally tax claims can be processed within the last two available tax periods, so ECA claims may still be relevant on expenditure up until their abolition. ECAs are time

[1] From April 2020 Non-resident Landlords now operate under UK Corporation Tax rather than Income Tax. This potentially brings further tax saving opportunities from Land Remediation Tax Relief (LRTR) – see later.
[2] Annual Investment Allowances are currently available on the first £1m of expenditure eligible for capital allowances as plant & machinery, integral features and long-life asset allowances – until 31 December 2020.

sensitive, so can be adjusted within this two year tax enquiry period, but thereafter the expenditure would revert to the other allowances, typically integral features, or plant & machinery allowances. Where claiming ECAs results in a loss, an incorporated taxpayer may elect to surrender the loss for a tax credit – a direct payment from HMRC. The tax credit will be calculated by reference to two thirds of the prevailing corporation tax rate and the amount spent on eligible ECA assets. HMRC do cap ECA tax credit payments to the greater of the company’s total PAYE and NIC liabilities for payment periods ending in the chargeable period or £250K.

Election under s.198 CAA2001

Purchasers of second-hand property often believe (or are encouraged to do so by their vendor) that there is no further tax relief available on a purchase involving an election under s.198. However this is rarely the case and contrary to the legislative wording of the Capital Allowances Act 2001 (CAA2001) – in fact there are often ‘latent’ allowances available.

In absence of specific contract wording, there is normally up to two years for the parties to agree the optional s.198 election, which determines the value of any capital allowances that can pass between the parties. Elections are complicated and rarely properly understood by the conveyancing lawyer (seldom property tax aware) – so tax relief is frequently overlooked or a limited election value presented as a ‘fait accompli’. However experienced property tax specialists will regularly identify significant tax relief over and above any proposed or completed election. These may include Integral Feature only claims, on account of the vendor having acquired the property before the IFA legislation (April 2008) or whereby tenant expenditure or prior capital contributions may be available to the purchaser. These ‘overage’ claims can amount to between 5-15% of the purchase consideration and are generally calculated as a valuation apportionment of the purchase price. Hence a review of past transactions – whether involving s.198, or not - may still yield additional tax allowances and thus result in further tax savings or rebate.

Repairs & Maintenance (R&M)

Repairs are eligible for 100% tax deduction and thus HMRC takes great care in scrutinising claims from taxpayers, often seeking to determine capital improvements and thus deny tax relief. Again, we regularly see taxpayers under claim or not claim at all, perceiving their expenditure to be ineligible. Furthermore, we have often seen some accountants historically claim all property expenditure as R&M without any real scrutiny of the reason, purpose or nature of expenditure, which helps to determine the ‘correct’ tax treatment. Our experience and knowledge of the precedent case law means that we regularly exceed client expectation in achieving favourable outcomes from our comprehensive claim analyses, as well as claim resolution where negotiated through to settlement with HMRC, irrespective of who (taxpayer, other consultant or E³) originated the claim.

Land Remediation Tax Relief (LRTR)

Land remediation tax relief (LRTR) can provide valuable tax relief across both commercial and residential projects for companies subject to UK corporation tax. LRTR is available on qualifying expenditure in tackling the barriers to development caused by contaminated and/or long term derelict land. Property investors get 150% relief, whilst developers get 50% of their qualifying expenditure, having already benefiting from 100% relief on the base expenditure as a trade expense. This targeted incentive was introduced by s.70 Finance Act 2001 to help regenerate brownfield sites throughout the UK; and amended within the Tax Law Re-write Project, becoming Part 14 Corporation Tax Act 2009.

Furthermore, if a LRTR claim results in the company making a loss in the accounting period it may surrender that loss and receive a payable tax credit from HMRC. The amount of tax credit which can be claimed is 16% of the qualifying land remediation loss foregone. For both investors and developers, the cash return is equivalent to 24% of the qualify land remediation expenditure incurred (16% x 150%). Unlike ECAs (above) the rate of the credit has not been adjusted since inception and is thus very favourably compared to current corporation tax rate of 19%.

Conclusion

If you hold property either for investment purposes, or as function of your business (hotel, car dealership or logistics centre, etc.), then a fresh review of your property tax position could result in a significant tax rebate and/or future savings. These few examples may help illustrate some of the potential additional claim opportunities that might be available to you (or your clients). To see how you might gain, contact E3 Consulting and speak with one of our property taxation specialists for a no obligation initial HEALTHCHECK review.

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