

# A Confused Message on Tax Relief for Property Construction Expenditure

## Introduction

The Office of Tax Simplification (OTS) produced its final report on the review of tax reliefs on 3 March 2011 and recommended that 47 tax reliefs should be abolished. On 23 March 2011, the Chancellor announced in Budget 2011 that the government would be abolishing 43 tax reliefs, seven of which would be abolished in the Finance Act 2011, with 36 reliefs to be abolished in 2012 or later following consultation.

On 27 May 2011, the Treasury issued a consultation document on the abolition of the 36 tax reliefs. The consultation document calls for responses by 31 August 2011 on the proposed transitional arrangements prior to the abolition of each relief. In addition, the question as to whether or not the tax relief should be abolished forms part of the consultation in some cases, but not in others.

## Property construction

Of the 36 tax reliefs covered by the consultation document, only three provide relief from income tax or corporation tax for property construction expenditure. These three reliefs are as follows:

- Capital allowances; flat conversion allowances.
- Capital allowances; safety at sports grounds.
- Land remediation relief.

In the case of the two capital allowances reliefs, the cost to the exchequer is estimated to be negligible, but the consultation document calls for comments on the impact of abolition in both cases. On the other hand, the government has estimated that land remediation relief costs the exchequer £40 million each year, but the consultation will only deal with the transitional provisions and not whether the rationale for abolishing the relief is sound.

Furthermore, the two capital allowances reliefs will be abolished for expenditure incurred from April 2013, but it is intended to abolish land remediation relief one year earlier. Taken together, the inconsistencies between the abolition of land remediation relief and the other reliefs could be seen as sending out a confused message. On the one hand, the government is calling for feedback on their rationale when there is a negligible cost to the exchequer, but where the cost is £40 million a year, then the word "consultation" takes on a different and more restrictive meaning.

## Flat conversion allowances

This relief consists of 100% capital allowances in the year of expenditure for the conversion or renovation of empty or underused space above shops and other commercial premises to residential use. The consultation document sets

out the rationale for abolition as "take-up seems to have been much lower than had been anticipated, suggesting that the relief has been unsuccessful in achieving its policy objectives to any significant extent."

Whilst the rationale within the consultation document may well be sound, it is worth noting what was stated in the final report of OTS dated 3 March 2011 in respect of business premises renovation allowance (BPRA) as follows:

It is questionable whether the relief acts as an incentive and it has a negligible impact in terms of savings.

Notwithstanding the recommendation of OTS, the government went on to announce in Budget 2011, that the BPRA scheme would be extended for a further five years from 2012, at a likely cost to the exchequer of £90 million over the period. This does, therefore, raise the question whether the government has all the information that it needs to correctly assess the impact of abolishing flat conversion allowances.

## Safety at sports grounds

Expenditure on carrying out safety works at sports grounds qualifies for capital allowances as expenditure on plant and machinery, irrespective of the fact that the expenditure is actually incurred on buildings and would otherwise not qualify for relief. This relief is only available for work to existing sports grounds in order to conform to the safety requirements of the Safety at Sports Grounds Act 1975 and the Fire Safety and Safety of Places of Sport Act 1987.

The rationale for abolition given in the consultation document is that "the stock of existing sports grounds should have been brought up to the standards appropriate for their size and use." As the relief does not apply to the construction of new stadia, which should be designed to meet all relevant safety requirements, it is perhaps very difficult to argue with the rationale for abolition of this relief.

## Land remediation relief

This relief is only available to companies (i.e., corporation tax payers) for expenditure incurred in cleaning up contaminated land in the U.K. provided certain conditions are met, a deduction equal to 150% of the qualifying expenditure is available, irrespective of whether the expenditure is capital and revenue in nature. The relief was intended to encourage developers to bring back into use land that has been contaminated by previous industrial use, that would otherwise remain unused, or land on which there are derelict structures that are so expensive to remove, that the land has become long-term derelict land.

The rationale for abolishing this relief is that “the remedial work would have been done irrespective of the availability of the relief and some sites remain undeveloped as they are in the wrong place.” The consultation document also states that “the relief does not always influence behaviour, but in many cases is seen as a tax bonus for work that would have been done anyway.” We believe that this rationale is flawed.

It is highly debatable whether any tax relief truly influences investment decisions. One could use the same argument to withdraw enhanced tax relief for research and development expenditure and probably for BPPA. More likely, tax relief usually operates as a reward for good behaviour and it seems inherently sensible to reward the decontamination of land, whether or not it would have taken place anyway.

Furthermore, the abolition of this relief would hit one business sector much harder than any other, that being the house building sector. It is true that there will always be winners and losers when a tax relief is abolished, but in the case of land remediation relief, the timing should be reviewed at the very least. The house building sector is still struggling to recover from the recession, so if abolition of this relief must take place, then it should be delayed, rather than implemented ahead of the abolition of the other reliefs.

### Summary

The consultation document contains some confused rationale for the abolition of certain tax reliefs that impact on property construction expenditure. Firstly, the government's decision to extend the BPPA scheme for a further five years is in contradiction to the recommendations of OTS and looks inconsistent with the approach to the abolition of flat conversion allowances and land remediation relief. Secondly, the decision to abolish land remediation relief on the basis that it has failed to influence investment decisions, seems to indicate an unrealistic expectation of what can be achieved through tax relief.

The fact that responses are invited on the rationale for abolishing certain reliefs that cost the exchequer a negligible amount, but not on land remediation relief, raises the question as to whether the government is committed to the consultation process. It does not seem fair that one business sector will be particularly hard hit and sooner than expected, so it is hoped that the government will listen to all the feedback it receives.

For further advice concerning any of the issues raised, please contact one of our key individuals detailed below or alternatively call our helpline on 0800 526262. Information on other property tax related topics can also be found on our website at <http://bankingtaxfinance.davislangdon.com>.

#### London

Paul Farey  
+44 (0)20 7061 7139  
paul.farey@  
davislangdon.com

#### Scotland

Michael Murray  
+44 (0)131 550 9473  
michael.murray@  
davislangdon.com

#### North

Christine Weaver  
+44 (0)161 819 7600  
christine.weaver@  
davislangdon.com

#### Midlands

Tim Beresford  
+44 (0)121 710 1333  
tim.beresford@  
davislangdon.com

#### South

David Rees  
+44 (0)23 8068 2801  
david.rees@  
davislangdon.com

#### Ireland

Lois Stirling  
+44 (0)28 9024 9800  
lois.stirling@  
davislangdon.com

#### Program, Cost, Consultancy

<http://bankingtaxfinance.davislangdon.com>  
[www.davislangdon.com](http://www.davislangdon.com)  
[www.aecom.com](http://www.aecom.com)

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