

## Capital Allowances and Jersey Property Unit Trusts

### What are capital allowances?

Capital allowances are tax reliefs for certain capital expenditure. Depreciation of fixed assets is a non-allowable expense and is not, therefore, deducted from income when calculating taxable profits. Instead of depreciation, capital allowances are given for expenditure on certain capital assets as a tax allowable expense. Capital allowances reduce taxable profits (but not cash flow) and therefore, save money. The tax relief is written down on a reducing balance over a number of years.

### Integral features of special rate pool — 10% reducing balance basis (8% from April 2012)

- Electrical systems.
- Hot and cold water systems.
- Heating, ventilation and air-conditioning installations.
- Lifts, escalators and moving walkways.
- External solar shading.
- Thermal insulation added to an existing commercial building.

### Main pool items — 20% reducing balance basis (18% from April 2012)

- Sanitary ware.
- Carpets.
- Furniture, fittings and equipment.
- Fire alarm systems.
- Intruder alarms, access control and closed-circuit television.
- Signage.

### Enhanced capital allowances

Enhanced capital allowances are 100 percent first-year allowance tax reliefs to encourage investment in certain qualifying energy and water-saving technologies.

The items being claimed as enhanced capital allowances must be from an approved government list, which stipulates certain performance criteria required to qualify.

### Types of developments giving rise to capital allowances

- Commercial offices.
- Industrial, distribution and manufacturing.
- Shopping centres and retail parks.
- Hotels and leisure facilities.
- Private healthcare facilities.
- Student accommodation.
- Commercial refurbishments.
- Combined heat and power schemes.
- Energy from waste plants.
- Wind and solar energy farms.
- Anaerobic digestion plants.
- Small-scale hydro schemes.

### Entitlement to claim

The three key qualifying criteria for claiming capital allowances are that the claimant must:

- Be a UK taxpayer.
- Have incurred the expenditure on the provision of the qualifying equipment.
- Hold the relevant interest in land, or have made a contribution to another person's expenditure.

### Who can and cannot claim capital allowances?

- Property investors can claim if:
  - They hold the property as a fixed asset in accounts and the rental business has commenced.
  - They are either UK based or a non-resident.
- Owner occupiers can claim.
- Developers/property traders (who do not incur capital expenditure) and non-taxpayers are unable to claim.

### What are Jersey Property Unit Trusts (JPUTs)?

JPUTs have been widely used for some time now as a vehicle for acquiring and holding UK property. A JPUT is an "offshore" unit trust governed by Jersey law and used to hold UK real estate. A unit trust is not a separate legal entity like a limited company, although it is often referred to as a legal structure. Legal ownership of the trust assets is vested in a trustee, who holds the property on trust for the benefit of the unit holders — the beneficial owners in accordance with the terms of the trust instrument.

JPUTs are a recognised vehicle for collective investment into high-value properties. It is likely that any JPUT we encounter will generally be a Very Private Unit Trust in so far as it will have a maximum of 15 unit holders and does not issue an offering document to potential investors. A JPUT offers greater potential liquidity than, for example, a Limited Partnership because holding a unit in a JPUT is legally similar to holding a share in a company.

A prime attraction of a JPUT is that it can be structured as a Baker Trust and is, therefore, transparent for UK income tax purposes. The unit holders are treated as receiving the income directly as it accrues. The trust document needs to contain provisions that ensure that the unit trust's income is vested directly in the unit holders as it arises and does not form part of the trust fund.

An added advantage of a JPUT is that this type of property ownership vehicle is familiar to UK property investors. The administration of the fund is relatively straightforward. The trustees have day-to-day control over the management of the

business and they are likely to instruct the preparation of capital allowances claims on behalf of eligible unit holders.

The unit holders in a Baker Trust claim capital allowances on the property on a pro-rata basis to the units they hold. The trustees of a Baker Trust do not claim capital allowances. Unless the unit holders arrange the assessment of capital allowances themselves, the trustees will need to provide the unit holders with details of the capital allowances for insertion into their tax returns, together with the proportion of the income and expenses related to each individual holding. Multiple capital allowances assessments do not have to be arranged by the trustees for the unit holders.

When they sell their units in a Baker Trust, the unit holders will need to know their share of the disposal value of the plant and machinery to subtract it from their capital allowances pools. In the case of either a property sale or a unit sale, it is currently possible for the unit holders to retain their proportion of the capital allowances, provided that the appropriate legal and tax documentation is correctly drafted.

### The opportunity

Significant tax-saving potential is available for property-owning clients, including high net worth individuals, trusts, occupiers and property investors who own commercial property.

There can be a level of ignorance over issues that arise with capital allowances in relation to transactions involving JPUTs, particularly in the area of unit and property sales.

The allowances can provide tax savings even when a property investment is unprofitable since allowances can be set against other property investor's income/profits.

### The potential values

Over 30 years of experience in preparing capital allowances claims provides us with a huge databank of benchmarking information for different types of investment property. The expected values of allowances for certain investment property types are set out below:

	Purchase price	Development cost
City office	20% to 30%	30% to 40%
Hotel	25% to 35%	35% to 50%
Retail centre	10% to 15%	15% to 25%

However, these values are only available if there are no restrictions from previous claims by other owners of the property.

### Due diligence prior to purchase

If any previous owner from July 1996 has made a claim for allowances there are restrictions to these values that will require due diligence to verify ownership history. The right

questions need to be addressed before any purchase and it can be possible to negotiate for the allowances in some circumstances.

We hold a significant database of past transactions and developments and will often have been involved with properties or will know the past owners.

### Our services

We undertake the majority of claims for capital allowances tax relief on property expenditure that cross the desks of HM Revenue & Customs on an annual basis. We have a proven track record of getting claims agreed at values submitted.

Our objective is to identify, analyse and maximise the values our clients are able to claim. We advise on liabilities and technical risks surrounding the acquisition of existing assets or construction of new property, which can often relate to the way ownership is structured.

### The future

Tax planning can help in the decision-making process and there is often a balance of risk and reward. Within developments, the high-value allowances now being targeted are towards energy-saving and environmentally beneficial technologies. In turn, we now have feed-in-tariffs and the renewable heat incentive, which can provide additional income when using renewable technology. Increasing environmental awareness pushes us to consider the use of less carbon-generating technologies. Part L of the Building Regulations and the carbon reduction commitment reinforce these behaviours and set increasingly stringent targets.

All this will mean:

- Energy-efficient and environmentally friendly buildings should command a higher investment value.
- There will be investment opportunities relating to the purchase and refurbishment of older stock, which can bring significant tax relief.

### More information

There is a significant amount of technical information about these subjects on our website at <http://bankingtaxfinance.davislangdon.com> and we are pleased to answer telephone enquiries and assist clients in early stages of transactions so no opportunity is missed.

Our fees are often charged on a contingency basis, with the fee being a very small portion of the benefit the client realises from the allowances. Generally, they will only become payable upon submission of any claim that entitles the client to the relief.

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