



PRESS RELEASE

Key Changes to the Land Remediation Relief Legislation

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1. Introduction

The Pre-Budget Report announced the draft legislation to support the introduction of modifications to the brownfield incentives regime, which has been the subject of an ongoing consultation since 2005. The Treasury's intentions for the new legislation were published in December 2007 and the pre-budget report 2008 publication contained the legislation to support those intentions. Whilst the draft legislation is clearly aligned to the December 2007 intentions in parts, there have been some notable additions that could have a significant impact on both the quantum of the relief and on the number of companies able to benefit. This paper summarises some of the key changes and will form part of the Environmental Industries Commission's formal response to the Treasury.

The Treasury's intent is to consult on the proposed legislation with a view to publishing guidance notes in late February 2009 which will also be the subject of consultation. The legislation will come into effect on 1 April 2009 and the final guidance notes are likely to be published around May/June 2009. Clause References are to the Draft Corporation Tax Bill 2009, which is based on Schedule 22 Finance Act 2001.

2. HM Revenue & Customs (HMRC) change of view on Japanese Knotweed (JKW)

Historically HMRC's view was that the costs to treat or remove JKW was not an allowable cost for the tax relief on the basis that it did not fall within the definition of a 'substance'. HMRC now accepts that JKW is sufficiently invasive and destructive that it satisfies the 'harm' test and that land infested with JKW is contaminated for the purposes of land remediation relief (LRR).

HMRC, therefore, now accept that all treatment and removal costs qualify for the relief under the existing legislation and will settle any open claims and any new claims for indate years on the same basis.

This means that developers and investors will be able to review historic costs and claim any previously unclaimed tax relief, provided all other entitlement conditions are met and that the time limits are satisfied.

Time limits to make retrospective claims vary depending on the status of the company making the claim:

- For investors (incurring capital expenditure) the rule is that they have two years after the year end in which the expenditure is incurred to make the claim. So, a company with a December year end can reclaim on any capital costs back to 1st January 2006, provided the claim is made before the end of this year.

- For traders (incurring stock in trade/wip) the rule is that they have six years after the year end in which the expenditure became a deduction for tax purposes to make a claim. So, a company with a December year end can reclaim costs taken to the profit and loss account in the December 2003 year end and beyond.

The only exception to these rules is that it may be possible to make a claim under the error and mistake provisions if the expenditure falls outside these time periods.

3. Land Remediation Relief: Derelict Land

As expected the 150% tax relief currently available to companies incurring expenditure on qualifying remediation costs will be extended to the costs to remove dereliction. The extended costs, however, will only be claimable on qualifying derelict sites which are defined as follows:

- Land that is not in productive use and cannot be put into productive use without the removal of buildings or other structures.
- Land that has been derelict continuously since 1st April 1998. This date can be amended periodically by Treasury Order.
- In keeping with the 'polluter pays' principle, the relief will be denied if the definitions above were not satisfied when first acquired by the present owner or a connected party.

Guidance will be published by HMRC to show how a listing on The National Land Use Database and the Scottish Vacant and Derelict Land Survey may be used as evidence of satisfying this definition and guidance will also be published on methods of proving that land is derelict in the absence of a listing on those databases.

The list of qualifying expenditure will be created through secondary legislation and will be capable of being added to if HMRC gain evidence to support the inclusion of further qualifying costs.

The initial list is expected to comprise:

- Removal of post tensioned concrete heavyweight construction.
- Removal of building foundations and machinery bases.
- Removal of reinforced concrete pile caps.
- Removal of reinforced concrete basements.
- Below ground demolition of redundant services.

The cost of relevant preparatory activities related to the above items will also qualify for the relief. So, professional fees and contractors preliminaries are two obvious areas where the relief could apply. The boundaries of this definition will evolve over time, but could include for example, the cost of removing buildings above concrete basements on the basis that the basement can't be removed until the building above has also been removed.

4. Changes to the existing LRR legislation.

HMRC have made a number of notable changes to the legislation which will apply from April 2009. They are focused on changes in a number of areas including:

Focus on land contaminated by former industrial use

The Treasury have indicated that LRR will not be allowable for costs incurred in dealing with natural substances that cause contamination. The exception to this rule is that the costs of dealing with arsenic, radon and JKW will remain allowable. Substances specifically excluded are contamination caused by air or water. The legislation deals with this by stating that land is not deemed to be contaminated if contaminated for any reason other than as a result of industrial activity. There are two aspects to this change:

- Air and water exclusion: The types of expenditure likely to be affected by this amendment are the previously contentious elements of a claim, namely flood risk mitigation costs, mine shaft grouting costs and potentially dry and wet rot treatment works. Substances within air or water that cause contamination will remain allowable, namely methane or contaminated ground water.
- The term 'industrial activity' is not as restrictive as first thought, being deemed to mean contamination caused by anthropogenic activity. Further clarification of this term will be provided in the guidance notes.
- The costs of upgrading concrete specification to resist high sulphates in the ground are only likely to qualify if they are sulphates from an industrial activity, not naturally occurring substances.

A desire to use soil guidance values (SGV's) as a way of demonstrating that a site is contaminated.

The Treasury has stated that if SGV's are exceeded and a remediation strategy is subsequently recommended after further risk assessment, then those remediation works will qualify for the relief. This is arguably no different

to the current regime, but offers a clear indication of the circumstances in which a claim can be made. The principle here is that a developer should be able to get greater certainty as to the potential scope of the claim once the site investigation has been carried out and would, therefore, be better placed to factor the tax relief into their investment decision.

There has also been a substitution of the term 'harm' with the term 'relevant harm'. Whilst the new definition is more akin to Part IIA type situations, HMRC have confirmed that any works done as a consequence of SGV levels being exceeded will still qualify for the relief. The term 'relevant harm' is defined as:

- Death of living organisms or significant injury or damage to living organisms.
- Significant pollution of controlled waters.
- Significant adverse impact on ecosystems.
- Significant damage to buildings or other structures.

A desire to reinforce the intention to disincentivise the removal of contaminated material to landfill

With effect from 1 April 2009, LRR will not be claimable on any landfill tax costs incurred. With landfill tax set to rise to £48/tonne, the relative cost of 'dig and dump' to alternative on-site strategies is only going to widen further with the removal of the tax relief. Sites particularly affected will be those which cannot avoid off site removal due to constraints on the ability to utilise alternatives either because the site is too small to adopt on site methods, or because the material type is incapable of remediation, namely asbestos. The inability to claim tax relief on these unavoidable costs appears punitive and is an area which will be raised with HMRC.

Furthermore, with effect from 1 April 2009 LRR will only be given on costs for the on site treatment of

JKW, not the costs to remove it to landfill. This is to remain consistent with the move away from landfill as a method of remediation. In addition, the condition requiring the substance to be on site at the date of purchase will not apply to JKW, so treatment costs on JKW discovered post purchase will also be allowed, provided the claimant did not plant it themselves!

Interest in Land now required to be a 'major interest'

With effect from 1 April 2009 there will be a requirement to acquire a 'major interest' in the land in order to benefit from the tax relief. A major interest includes the freehold or a leasehold interest of more than seven years unexpired. This more onerous requirement will mean that a number of entities will now potentially be prevented from claiming, namely some PFI companies and contractors who incur losses on building contracts. Much more care will also need to be taken when structuring development partnerships/ventures, because it will no longer be possible to rely on a licence or other smaller interest to claim the relief.

Further anti-avoidance rules to prevent polluters from benefiting from relief

New anti-avoidance provisions have been brought in to prevent sale and buy backs of land that allow polluters to benefit from the relief indirectly. The new provisions will mean that if a company buys land off a polluter and the polluter retains a relevant interest in the land, then the company will not be entitled to claim the relief. A relevant interest is any interest in, right over or licence to occupy the land, including options to acquire any of those interests. Those most likely to be affected are polluters who enter into 'tax planning' arrangements to extract the benefit out of the relief through the involvement of a third party.

A polluter also has a relevant interest if they sold the land for a consideration that to any extent reflects the impact or likely impact,

on the value of the land of the remediation of its contamination. This would seem to mean that companies who buy land off polluters will be prevented from claiming the relief where the cost of the remediation is reflected in the purchase price paid. However, the Treasury have confirmed that where a company pays the open market value of a site on an arms length basis, that company will be entitled to claim the relief even when purchased from a polluter. Whether the definition of "relevant interest" will be amended in the final version of the legislation to clarify this point remains to be seen.

Intention to only allow costs of removing contamination

The guidance notes published with the draft legislation states an intention to only allow the cost to remove the contamination, not the subsequent costs to reinstate the land or buildings to their former state. The potential impact of this is that only those costs directly linked to the remediation strategy will attract the relief, not the cost of any consequential works.

Typical examples of expenditure affected are:

- Backfilling holes where contamination removed unless the backfilling is part of the remediation strategy.
- Additional sub-structure costs incurred as a consequence of the remediation strategy.e.g. Take some land that has sufficient ground bearing capacity to take traditional footings, but contains a hotspot of contamination that has to be removed. The current regime would allow the excavation, removal and backfill of the hole, as well as the subsequent increase in costs between traditional footings and the deep pad foundations that are now required in the vicinity of the hotspot due to the loss of ground bearing capacity as a result of the hotspot removal.

5. Works required under Statutory Order not qualifying.

Finance Bill 2009 will introduce powers to exclude expenditure that a company is required to incur under specified statutory provisions which require work to be carried out. Expenditure likely to be affected includes:

- The cost of work required on land/buildings adversely affecting the amenity of neighbourhood.
- The cost incurred on work required on defective premises, dangerous buildings, ruinous and dilapidated buildings and neglected sites would also be excluded.
- Expenditure on work required for the abatement or prohibition of a nuisance.
- Expenditure on work on a listed building under a repairs notice

A number of measures are also being put forward by the Environmental Industries Commission for consideration by the Treasury, namely:

1. Increase tax credit rate from 16% to 18%.
2. Increase tax relief rate from 150% for a two year period to encourage developers to undertake remediation in readiness for an upturn in the housing market.
3. To exempt asbestos from landfill tax until such time as technologies advance for its onsite treatment.

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