

Budget 2008

Implications for the Property Sector

Prepared by the WK Property & Construction Group



Budget 2008:

Property Sector Impact

As is usual, nowadays, the annual Budget tends not to hold any great surprises, with most of the changes already being disclosed in pre-budget reports. Following the Budget announcement and as we move into a new tax year, we take a look as to how some of these changes may affect this industry sector.

CAPITAL GAINS TAX (CGT)

Following the announcement of the simplification of CGT to a 'one size fits all' rate of 18% as from 6th April 2008, and the withdrawal of both Taper Relief and Indexation Allowance, it soon became evident that this was a bit too simplistic an approach.

At the end of February 2008, HM Revenue & Customs published draft legislation, and guidance with regard to the newly announced CGT Entrepreneurs Relief. Much of this is derived from the old 'Retirement Relief' which was withdrawn in 2003/04.

The new relief is on the disposal of the whole or part of the trading business, and provides for a 'lifetime allowance' of £1 million which commences when the relief is first claimed. Disposals within this 'lifetime allowance' will be subject to a charge to tax of 10%, whilst disposals above the £1million will be charged at 18%. This relief does not apply to past disposals.

Entrepreneurs Relief has no minimum age limit and in general will be available where the relevant conditions have been met for a period of one year.

As with all changes there are winners and losers and some of the main points to bear in mind, with regard to property are as follows:

- 1) Gains on disposals of let residential properties will not qualify for entrepreneurs relief, however they do benefit from the fact that the 18% rate is lower than the effective rate of tax under the previous regime.
- 2) Gains on the disposal of furnished holiday lettings (FHL) will qualify. Previously FHL's qualified for Business Asset Taper Relief, which providing that all conditions were met, would have attracted a 10% tax charge.
- 3) The sale of an asset in isolation, for example the part disposal of farm land, will not qualify for the relief.
- 4) If a property is let to a trading partnership of which you are a member, or to a trading company of which you are an officer or employee, then you may be entitled to a measure of relief on the disposal of that property, providing that disposal is associated with the disposal of your interest in the partnership, or of your shares in the company, and that other disposal meets all the conditions of the relief.
- 5) A disposal of let commercial property will not qualify for Entrepreneurs' Relief. There must be a disposal of the whole or part of the trading business and commercial property letting is not a trading activity. Previously, providing that the property was let to a qualifying business, for the purpose of a qualifying trade, and that all the conditions were met, then the commercial property would have been treated as a business asset and as such attracted the more favourable Business Asset Taper Relief.

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CAPITAL ALLOWANCES

The Government announced a series of wide-ranging reforms with regard to the structure of Capital Allowances, and in December 2007 issued a Technical Note which set out its intended way forward.

A) INDUSTRIAL AND AGRICULTURAL BUILDINGS ALLOWANCES

The Budget 2007 announced the abolition of IBA's and ABA's. These are to be phased out over 4 years so that they will no longer be available from April 2011. To this end the rate of writing down allowances would be reduced by 1 percentage point each successive year. The rate of allowance for the tax year 2008/09 will therefore be 3%, 2009/10 - 2%, and 2010/11 - 1%.

With effect from 21st March 2007, balancing adjustments and the recalculation of writing down allowances in respect of balancing events was withdrawn.

B) ENTERPRISE ZONE ALLOWANCES (EZA's)

EZA's will be withdrawn from 1st April 2011. This is an initial allowance of 100% available for expenditure on industrial or commercial building by businesses within enterprise zones.

Until this point of withdrawal, the full 100% initial allowance will still be available. It is hoped that this advance notice will enable businesses to complete their building construction or acquisition plans, in order to access the relief in full before it is finally withdrawn.

C) WRITING-DOWN ALLOWANCES

Reduction in the main rate of capital allowances on the general pool of plant and machinery from 25% to 20%. This is effective from 1st April 2008. That for long life assets will be increased from 6% to 10%.

D) FEATURES INTEGRAL TO A BUILDING

Over successive years the boundary, for capital allowances purposes, between plant and machinery, and commercial buildings, has become less clear. As such this has been an area of considerable doubt and uncertainty in tax law.

Furthermore, over time, assets that are commonly regarded as integral to a modern building, have come to attract standard plant and machinery capital allowances at a rate that does not generally reflect their average rate of economic depreciation.

In an attempt to simplify this area the budget introduced a separate classification of features that are integral to a building, so that expenditure on these assets may be included in a new 10% pool.

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This will include replacement expenditure where either the whole or more than 50% of the integral feature is replaced in a 12 month period.

The six asset classes that qualify for the new 10% rate of writing down allowances are as follows;

- 1) electrical systems (including lighting systems),
- 2) cold water systems,
- 3) space or water heating systems, powered systems of ventilation, air cooling or air purification, and any floor or ceiling comprised in such systems,
- 4) lifts, escalators and moving walkways,
- 5) external solar shading, and,
- 6) active facades.

Currently WDA's at 25% are available for expenditure on adding thermal insulation to an industrial building. From April this will be extended to cover all existing buildings used for any qualifying business purpose, other than residential property businesses. However such allowances will be restricted to the new 10% rate.

E) ENHANCED CAPITAL ALLOWANCES

Enhanced Capital Allowances (ECA's) enable a business to claim 100% first year allowances on their spending on qualifying plant and machinery.

Historically, expenditure on electrical and cold water systems had not usually been classified as 'plant and machinery' and so many businesses had been unable to claim ECA's when their expenditure on these systems had included specific items on the 'Green Technology' ECA list.

Classifying these systems, within the six asset classes given above, will therefore enable businesses to claim ECA's on such specific items.

The Budget 2008 also added waste water recovery and re-use systems to the Water Technology Criteria List and included four additional sub-technologies on the Energy Technology Criteria List.

Furthermore, the Finance Bill 2008 will introduce new legislation to enable loss making companies to surrender losses attributable to 100% first year allowances (ECA's) on designated energy saving or environmentally beneficial plant and machinery in exchange for a cash payment from government. This will take the form of a tax credit of 19% subject to a maximum of the greater of £250,000 or the company's PAYE and NI liabilities for the period for which the loss is surrendered. This credit applies to companies only and there are claw-back provisions where the asset is sold within 4 years.

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VAT

Legislation will be introduced for a simplification of the option to tax land and/or buildings. It will also introduce minor changes to enable tax payers to revoke an option to tax after 20 years and make a number of associated changes to improve practical administration of the option to tax.

The rewritten legislation will have effect on and after 1st June 2008. The earliest date an option to tax will be revocable will be 1st August 2009.

STAMP DUTY LAND TAX (SDLT)

A) RELIEF FOR NEW ZERO CARBON FLATS

Finance Act 2007 brought in a time limited relief from SDLT for new zero carbon homes. The Finance Bill 2008 will extend this relief to cover new zero carbon flats. The relief will expire on the 30th September 2012. A government department will carry out an assessment as to whether the home meets zero carbon standards.

B) ANTI AVOIDANCE LEGISLATION

Legislation will be introduced in the Finance Bill 2008 to amend provisions inserted in the Finance Act (FA) 2003 by FA 2007 to ensure that where there is a transfer of an interest in a property within an investment partnership there will be no charge to SDLT. The measure will be retrospective and have effect for all transactions that occurred on and after 19th July 2007.

Furthermore, legislation will be introduced to amend provisions that enable groups to transfer assets within a group and then sell the purchasing company on to a third party without incurring SDLT.

PROPERTY AUTHORISED INVESTMENT FUNDS

New regulations will come into effect on and after 6th April 2008 that will affect Authorised Investment Funds (AIF's) and UK REIT's.

Under the new regulations an AIF that invests mainly in property and certain related securities will be able to elect for the AIF regime to have effect.

The new regulations will enable a property AIF to provide an open ended fund alternative to the existing closed ended UK REIT's.

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Contact Information

For further information please contact the Wilkins Kennedy Partner who usually handles your affairs, or your nearest WK office on the details below:

London

Tel : 020 7403 1877
Fax: 020 7403 1605
E: london@wilkinskennedy.com

Cambridge

Tel: 01223 301 166
Fax: 01223 462 054
E: cambridge@wilkinskennedy.com

Guildford

Tel: 01483 306 318
Fax: 01483 565 384
E: guildford@wilkinskennedy.com

Orpington

Tel: 01689 827505
Fax: 01689 831478
E: Orpington@wilkinskennedy.com

Southend-on-Sea

Tel: 01702 348 646
Fax: 01702 330 148
E: Southend@wilkinskennedy.com

Winchester (JB Wilkins Kennedy)

Tel: 01962 852 263
Fax: 01962 841 197
E: Winchester@wilkinskennedy.com

Amersham

Tel: 01494 725 544
Fax: 01494 431 571
E: amersham@wilkinskennedy.com

Egham

Tel: 01784 435 561
Fax: 01784 430 584
E: egham@wilkinskennedy.com

Hertford

Tel: 01992 550 847
Fax: 01992 554 515
E: hertford@wilkinskennedy.com

Reading

Tel: 0118 951 2131
Fax: 0118 951 2161
E: reading@wilkinskennedy.com

Falkland Islands

Tel: 00 500 22918
Fax: 00 500 22918
E: Falklands@wilkinskennedy.com

Romsey (JB Wilkins Kennedy)

Tel: 01794 515 441
Fax: 01794 830 705
E: romsey@wilkinskennedy.com

Visit our website www.wilkinskennedy.com

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