

Capital Allowances - Flat Conversion Allowances: Repeal of Relief

Who is likely to be affected?

Those businesses that have renovated or converted vacant or under-used space above shops and other commercial premises to provide flats for rent, or that are planning to renovate or convert such space.

General description of the measure

Flat conversion allowances (FCAs) were introduced in 2001. The scheme was designed to increase the availability of low cost rental accommodation in urban areas by providing 100 per cent capital allowances for the conversion of empty or under-used space above shops and other commercial premises to residential use. The flats must be available for short term letting. FCAs are not available if the flats are of high value or the property in which they are situated was built after 1980. Take-up of the scheme has been much lower than anticipated, suggesting that the relief has not been successful in achieving its objective and is now being repealed.

Policy objective

The repeal supports the Government's objective to simplify the tax system and is part of a package of measures which will repeal reliefs that are no longer necessary, have not achieved their policy rationale or are distortive.

Background to the measure

Following the Office of Tax Simplification review of reliefs, the Government announced at Budget 2011 that it would repeal seven reliefs in Finance Act 2011 and confirmed its intention to abolish a further 36 reliefs in Finance Bill 2012 and beyond, subject to a period of consultation.

Consultation on the abolition of 36 tax reliefs was published on 27 May 2011 and views were requested on the Government's proposal to repeal this relief. The Government response was published on 6 December 2011. All documents are available on both the HM Treasury and HM Revenue & Customs (HMRC) websites.

Detailed proposal

Operative date

This relief will be withdrawn for expenditure incurred on or after 1 April 2013 for businesses within the charge to corporation tax, and on or after 6 April 2013 for businesses within the charge to income tax.

The entitlement to claim writing down allowance on any outstanding residue of qualifying expenditure will also cease with effect from the same dates.

Current law

FCAs, which were introduced in 2001, are available under part 4A of the Capital Allowances Act 2001. The relief provides a 100 per cent initial allowance to encourage the conversion or development of empty or under-used space above shops and other commercial premises into residential property for letting.

Where the full allowance is not claimed, the relief provides that any residue of qualifying expenditure is written off at a rate of 25 per cent of the value of the original qualifying expenditure per annum on a straight-line basis.

Proposed revisions

Legislation will be introduced in Finance Bill 2012 to repeal FCAs in respect of qualifying expenditure incurred on or after 1 April 2013 for businesses within the charge to corporation tax, and on or after 6 April 2013 for businesses within the charge to income tax.

The entitlement to claim writing down allowances on any residual expenditure will also be withdrawn from that date. However, where the chargeable period of a business falls in more than one financial or tax year, the writing down allowance should be apportioned on a time basis between the financial or tax years in order to determine the amount of the writing down allowance that may be set-off against profits. For example:

- A company has a 12 month chargeable period of 1 January 2013 to 31 December 2013 (365 days);
- It originally incurred £10,000 of FCA qualifying expenditure and has residual FCA expenditure of £5,000;
- For the period 1 January 2013 to 31 December 2013, a maximum writing down allowance of £2,500 (£10,000 x25 per cent) could have been claimed;
- As a result of the repeal, only the period 1 January 2013 to 31 March 2013 (90 days) qualifies for FCA relief;
- Therefore for its 2013 chargeable period the company would be entitled to a maximum writing down allowance of: $90/365 \times £2,500 = £616.44$.

Summary of impacts

Exchequer impact (£m)	2011-12	2012-13	2013-14	2014-15	2015-16
	-	-	negligible	negligible	negligible
	This measure is expected to have a negligible impact on the Exchequer. Any impact will be set out at Budget 2012.				
Economic impact	This change is not expected to have any significant economic impacts on the rented accommodation sector as very few businesses have chosen to claim the allowance.				
Impact on individuals and households	Due to the low uptake of the relief, the impact on individuals and households is considered to be minimal.				

Equalities impacts	The low uptake of the scheme means that there is not expected to be any significant impacts on the supply of rental accommodation to people with protected characteristics.
Impact on business including civil society organisations	<p>One of the FCAs' target groups includes small businesses who own their business premises, e.g. shops, and have unused domestic accommodation over it. It is difficult to estimate how many businesses might be affected by the relief's withdrawal, but as evidence suggests that take-up of the relief has been low (in 2009/10 only around 100 companies made claims) it is expected that any impact will be small.</p> <p>The abolition of FCAs may also impact on some property investment businesses. But again based on the low take-up this is likely to be small.</p> <p>The decision to withdraw the entitlement for writing down allowances in respect of residual expenditure for those chargeable periods starting on or after the operative dates could also have impacts. It is difficult to estimate the number of businesses affected, but based on take up and the assumption that the majority of businesses will have claimed the full 100 per cent initial allowances, the number is likely to be small. Those affected could include both unincorporated and incorporated businesses, and businesses large and small.</p> <p>A 2006 evaluation found that 69 per cent of FCA claims were made by an accountant. Consequently abolition would reduce taxpayers' need for an accountant or agents to calculate the entitlement to FCA with the consequent reduction in administration costs. Overall this measure is expected to have a negligible impact on businesses' administrative burdens.</p> <p>As these changes only apply to business expenditure the changes will have little or no impact on charities who do not generally pay tax on business profits.</p>
Operational impact (£m) (HMRC or other)	There will be a negligible operational impact for HMRC.
Other impacts	<u>Small firms impact test:</u> While the relief is available to small firms, the actual take up is low. The consultation did not identify anything to suggest that its abolition would have a significant impact on small firms.

Monitoring and evaluation

This change does not require monitoring or evaluation. It removes an under-used relief. Any correspondence received on the impact of the repeal will be dealt with on a case by case basis.

Further advice

If you have any questions about this change, please contact Nick Williams on 020 7147 2541 (email: nicholas.williams@hmrc.gsi.gov.uk).

