

Capital Allowances

Overview

The cost of purchasing capital equipment in a business is not a revenue tax deductible expense. However tax relief is available on certain capital expenditure in the form of capital allowances.

The allowances available depend on what you are purchasing. Here is an overview of the types of expenditure which qualify for capital allowances and the amounts available.

Capital allowances are not generally affected by the way in which the business pays for the purchase. So where an asset is acquired on hire purchase (HP), allowances are generally given as though there were an outright cash purchase and subsequent instalments of capital are ignored. However finance leases, often considered to be an alternative form of "purchase" and which for accounting purposes are included as assets, are denied capital allowances. Instead the accounts depreciation is usually allowable as a tax deductible expense.

Any interest or other finance charges on an overdraft, loan, HP or finance lease agreement to fund the purchase is a revenue tax deductible business expense. It is not part of the capital cost of the asset.

If alternatively a business rents capital equipment, often referred to as an operating lease, then as with other rents this is a revenue tax deductible expense so no capital allowances are available.

Plant and machinery

This includes items such as machines, equipment, furniture, certain fixtures, computers, cars, vans and similar equipment you use in your business.

Note there are special rules for cars and certain 'environmentally friendly' equipment and these are dealt with below.

Acquisitions

The Annual Investment Allowance (AIA) provides a 100% deduction for the cost of most plant and machinery (not cars) purchased by a business up to an annual limit and is available to most businesses. Where businesses spend more than the annual limit, any additional qualifying expenditure generally attracts an annual writing down allowance of only 18% or 8% depending on the type of asset.

The maximum amount of the AIA depends on the date of the accounting period and the date of expenditure. The changes in the amount of the maximum AIA can be summarised as follows:

Period from:	Annual limit
*1 April 2012	£25,000
1 January 2013	£250,000
*1 April 2014	£500,000
1 January 2016	£200,000

*From 6 April for unincorporated businesses

Where a business has a chargeable period which spans 1 January 2016 there are transitional rules for calculating the maximum AIA for that period and there will be two important elements to the calculations:

- a calculation which sets the maximum AIA available to a business in an accounting period which straddles 1 January 2016

- a further calculation which limits the maximum AIA relief that will be available for expenditure incurred from 1 January 2016 to the end of that accounting period.

It is the second figure that can catch a business out as demonstrated by the following example:

Example	
If a company has a 31 March year end then the maximum AIA in the accounting periods to 31 March 2016 will be:	
9 months to December 2015 three quarters of £500,000	£375,000
3 months from January 2016 one quarter of £200,000	£50,000

Total annual AIA using first calculation	£425,000

This is still a generous figure. However if expenditure is incurred between 1 January and 31 March 2016 the maximum amount of relief will only be £50,000. This is because of the restrictive nature of the second calculation. Alternatively, the business could defer its expenditure until after 31 March 2016. In the accounting period to 31 March 2017, AIA will be £200,000. However tax relief will have been deferred for a full year.	

Where purchases exceed the AIA, a writing down allowance (WDA) is due on any excess in the same period. This WDA is currently at a rate of 18%. Cars are not eligible for the AIA, so will only benefit from the WDA (see special rules for cars).

Please contact us before capital expenditure is incurred for your business in a current accounting period, so that we can help you to maximise the AIA available.

Pooling of expenditure and allowances due

- Expenditure on all items of plant and machinery are pooled rather than each item being dealt with separately with most items being allocated to a main rate pool.
- A writing down allowance (WDA) on the main rate pool of 18% is available on any expenditure incurred in the current period not covered by the AIA or not eligible for AIA as well as on any balance of expenditure remaining from earlier periods.
- Certain expenditure on buildings fixtures, known as integral features (eg lighting, air conditioning, heating, etc) is only eligible for an 8% WDA so is allocated to a separate 'special rate pool', though integral features do qualify for the AIA.
- Allowances are calculated for each accounting period of the business.
- When an asset is sold, the sale proceeds (or original cost if lower) are brought into the relevant pool. If the proceeds exceed the value in the pool, the difference is treated as additional taxable profit for the period and referred to as a balancing charge.

Special rules for cars

There are special rules for the treatment of certain distinctive types of expenditure. The first distinctive category is car expenditure. Other vehicles are treated as general pool plant and machinery but cars are not eligible for the AIA. The treatment of car expenditure depends on when it was acquired and is best summarised as follows:

From 1 / 6 April 2015

The capital allowance treatment of cars is based on the level of CO₂ emissions.

Type of car purchase	Allocate	Allowance
New low emission car not exceeding 75g/km CO ₂	Main rate pool	100% allowance
Not exceeding 130 g/km CO ₂ emissions	Main rate pool	18% WDA
Exceeding 130 g/km CO ₂ emissions	Special rate pool	8% WDA

Acquisitions from April 2013 to 31 March / 5 April 2015

Type of car purchase	Allocate	Allowance
New low emission car not exceeding 95g/km CO ₂	Main rate pool	100% allowance
Not exceeding 130 g/km CO ₂ emissions	Main rate pool	18% WDA
Exceeding 130 g/km CO ₂ emissions	Special rate pool	8% WDA

Acquisitions from April 2009 to March 2013

Type of car purchase	Allocate	Allowance
New low emission car not exceeding 110g/km CO ₂	Main rate pool	100% allowance
Not exceeding 160 g/km CO ₂ emissions	Main rate pool	18% WDA
Exceeding 160 g/km CO ₂ emissions	Special rate pool	8% WDA

Pre April 2009 acquisitions

Type of car purchase	Allocate	Allowance
New low emission car not exceeding 110g/km CO ₂	Main rate pool	100% allowance
Not exceeding £12,000 cost and not low emissions	Main rate pool	18% WDA
Exceeding £12,000 cost and not low emissions	Single asset pool for each car	18% WDA but restricted to £3,000 max. pa

Cars purchased pre April 2009 that are used wholly for business use will attract WDA as detailed above. However any expenditure remaining in a single asset pool after a transitional period of around 5 years (unless there is any non-business use of the car) will then be transferred to the main rate capital allowances pool.

Non-business use element

Cars and other business assets that are used partly for private purposes, by the proprietor of the business (ie a sole trader or partners in a partnership), are allocated to a single asset pool irrespective of costs or emissions to enable the private use adjustment to be made. Private use of assets by employees does not require any restriction of the capital allowances.

The allowances are computed in the normal way so can in theory now attract the 100% AIA or the relevant writing down allowance. However, only the business use proportion is allowed for tax purposes. This means that the purchase of a new 94g/km CO₂ emission car which costs £15,000 with 80% business use will attract an allowance of £12,000 (£15,000 x 100% x 80%) when acquired.

On the disposal of a private use element car, any proceeds of sale (or cost if lower) are deducted from any unrelieved expenditure in the single asset pool. Any shortfall can be claimed as an additional one off allowance but is restricted to the business use element only. Similarly any excess is treated as a taxable profit but only the business related element.

Environmentally friendly equipment

This includes items such as energy saving boilers, refrigeration equipment, lighting, heating and water systems as well as cars with CO₂ emissions up to 95 g/km (110g/km prior to 1 April 2013).

A 100% allowance is available to all businesses for expenditure on the purchase of new environmentally friendly equipment.

- www.etl.decc.gov.uk gives further details of the qualifying categories.
- where a company (not an unincorporated business) has a loss after claiming 100% capital allowances on green technology equipment (but not cars) they may be able to reclaim a tax credit from HMRC.

Capital allowance boost for low-carbon transport

A 100% first year allowance is available for capital expenditure on new electric vans from 1 April 2010 for companies and 6 April 2010 for an unincorporated business.

Short life assets

For equipment you intend to keep for only a short time, you can choose (by election) to keep such assets outside the normal pool. The allowances on them are calculated separately and on sale if the proceeds are less than the balance of expenditure remaining, the difference is given as a further capital allowance. This election is not available for cars or integral features.

For assets acquired from 1 April 2011 (6 April for an unincorporated business) the asset is transferred into the pool if it is not disposed of by the eighth anniversary of the end of the period in which it was acquired. For assets acquired prior to April 2011 the deadline is the fourth anniversary of the end of the period in which it was acquired.

Long life assets

These are assets with an expected useful life in excess of 25 years. These assets are combined with integral features in the 8% special rate pool.

There are various exclusions including cars and the rules only apply to businesses spending at least £100,000 per annum on such assets so that most smaller businesses are unaffected by these rules.

Other assets

Capital expenditure on certain other assets qualifies for relief. Please contact us for specific advice on areas such as qualifying expenditure in respect of enterprise zones and research and development.

Claims

Unincorporated businesses and companies must both make claims for capital allowances through tax returns.

Claims may be restricted where it is not desirable to claim the full amount available - this may be to avoid other allowances or reliefs being wasted.

For unincorporated businesses the claim must normally be made within 12 months after the 31 January filing deadline for the relevant return.

For companies the claim must normally be made within two years of the end of the accounting period.

How we can help

The rules for capital allowances can be complex. We can help by computing the allowances available to your business, ensuring that the most advantageous claims are made and by advising on matters such as the timing of purchases and sales of capital assets. Please do contact us if you would like further advice.