Taxation – Mini Budget? Maxi Gamble? Or Tax Bonfire! Summary of the Capital Allowances Changes

15 March 2023

ALUN OLIVER FRICS, Managing Director of E³ Consulting, discusses our initial reaction to the Property Taxation aspects of the 'Spring Budget' announced today (15 March 2023) by Jeremy Hunt MP, Chancellor of the Exchequer.

This review highlights the measures impacting the built environment as well as the wider property, construction and infrastructure sectors.

These are largely drawn from the Budget 'Red Book' and will be augmented, in time, with explanations and commentary on draft legislation - as further details become available.

Positioned by The Chancellor as a Budget for growth and investment, there have been a mix of policy announcements around Investment Zones and Levelling Up and Regeneration initiatives across the UK (and particularly Northern England) – potentially pandering to the 'blue wall' constituencies perhaps.

As well as replacement of the successful 130% Super deduction and 50% Special Rate Allowances, with a new three year 'fully expensed' 100% relief (from April 2023) on Plant & Machinery Allowances (PMAs) and retaining a 50% First Year Allowance (FYA) on Integral Features Allowances (IFAs) – accelerating the relief for companies within the charge to Corporation Tax. Sadly, many businesses that operate as partnerships or individuals (such as farming, medical or dental practices etc., as well as those across professional services) – will not benefit from these enhanced tax savings as they do not appear to be available against Income Tax.

The measures include:

1.28 Beyond this year, GDP growth increases, with the economy growing by 1.8% and 2.5% in 2024 and 2025 respectively, as interest rates begin to fall and energy price falls take inflation below the 2% target. The Office of Budget Responsibility (OBR) notes that the recovery is driven by private consumption, as real household incomes rise, and increased business investment, aided by changes to capital allowances. In 2026 and 2027, GDP then grows by 2.1% and 1.9% respectively.

3.68 A competitive corporate tax system is a vital lever to encourage enterprise and investment. To get debt falling, at Spring Budget 2021, the government took the difficult decision to increase the headline rate of Corporation Tax to 25% from April 2023.

Box 3.B Tax and investment
The UK has one of the most pro-business tax regimes in the world. At 25%, the UK will still have the lowest rate of Corporation Tax in the G7. *At Spring Budget, the government is going further and announcing a policy of full expensing which will mean that the UK has the joint most generous capital allowance regime in the OECD with a Net Present Value (NPV) of 100%. NPV measures the value of tax relief today, reflecting that relief upfront is better than relief later.* *Capital allowances allow businesses to write off the cost of qualifying expenditure against taxable income, thus cutting businesses' overall tax bill.* *This means that until April 2026, for every £1 invested in qualifying expenditure, companies can save up to 25p on their tax bill.*

3.70 The reliefs and allowances within the corporate tax system are an important factor in business investment decisions. The decision in the autumn to permanently set the Annual Investment Allowance at £1 million, means 99% of businesses receive 100% tax relief on their qualifying plant and machinery investments in the year of investment.

3.71 In 2021, the government introduced the super-deduction to go further to encourage companies to invest. This was due to end on 31 March 2023. The government is now introducing full expensing, a 100% First Year Allowance, from 1 April 2023 until 31 March 2026. This means that companies across the UK will be able to write off the full cost of qualifying main rate plant and machinery investment in the year of investment. Companies investing in special rate (including long life) assets will also benefit from a 50% first-year allowance during this period. Moving to full expensing means the UK's plant and machinery allowances will be joint first in the OECD in Net Present Value terms, instead of dropping to 33rd.

3.73 An important part of ensuring prosperity is encouraging more businesses to invest in R&D, helping them to create the technologies, products and services which advance living standards.

3.74 At Autumn Statement 2022, the government announced that from 1 April 2023 the rate of the Research & Development Expenditure Credit (RDEC) would be increased from 13% to 20%. This means that the UK's R&D tax relief for large companies has the joint highest uncapped headline rate in the G7.

3.75 The government also committed to considering the case for further support for R&D intensive SMEs. From 1 April 2023, the government will introduce an increased rate of relief for loss-making R&D intensive Small and Medium size Enterprises (SMEs). Eligible companies will receive £27 from HMRC for every £100 of R&D investment. The government remains committed to supporting R&D and recognises the important role that R&D and innovation play for the economy and society.

3.76 The government will continue to support the UK's world-leading creative industries by reforming the audio-visual tax reliefs into expenditure credits with a higher rate of relief than under the current system. The expenditure threshold for high-end TV will remain at £1 million per hour. The government will also extend the temporary higher rates of theatre, orchestra, and museums and galleries tax reliefs for 2 further years from April 2023.

3.77 The government also continues to recognise the importance of the UK's world-leading shipping and maritime services industries. From June 2023, for the first time in nearly 18 years, the government will open an election window to permit shipping companies that left the Tonnage Tax regime to return to the UK, bringing with them investment and jobs. This follows reforms to the regime announced at Autumn Budget 2021, which aimed to increase the number of firms headquartered in the UK, following the UK's departure from the EU.

Box 3.C Tax simplification
The government wants the tax system to be simple, fair and to support growth. Simplifying the tax system reduces the time and money businesses and individuals spend on tax administration, helps boost productivity and supports growth. Progress towards these principles can often align, but sometimes there are trade-offs to consider between them. *Following the closure of the Office of Tax Simplification, officials were given a clear mandate to focus on simplicity of tax policy design throughout the policy making process and on simplifying existing tax rules and administration. The government has increased direct engagement with business organisations and tax professionals to better understand where problems for businesses and individuals arise, building on existing HMRC evidence and insight. New policy, as well as existing tax rules, will be subject to increased scrutiny to ensure new changes are as easy to administer as possible. The Budget announces a number of consultations which build on this approach, including on customs processes.* *The government is focused on ensuring that meeting tax obligations is as straightforward as possible at key events for a growing business, such as when a business is set up or takes on a first employee. Small businesses account for almost half of employment and around a third of turnover in the UK's private sector. As a first step, Spring Budget announces a consultation to expand the 'cash basis' – a simplified way for over four million sole traders to calculate and pay their Income Tax - and a systematic review of HMRC guidance and key forms for small businesses, to ensure the tax system is easy for them to understand.* *For small businesses not applying the cash basis, the Annual Investment Allowance (AIA) provides 100% first-year relief for plant and machinery investments. From April 2023, this will be permanently set at £1 million, simplifying the tax treatment of capital expenditure for 99% of businesses. Larger businesses will benefit from full expensing for the next three years, simplifying claims and investment decisions.* *For individuals Spring Budget also simplifies pension tax. Increasing the Annual Allowance and removing the Lifetime Allowance charge will reduce the number of taxpayers that need to report and pay pensions tax.* *Spring Budget also includes a discussion document on modernising HMRC's Income Tax services so taxpayers can quickly and easily manage their own tax affairs online, reducing the need to contact HMRC. This builds on the government's commitment to make HMRC services simpler and more efficient, for example through introducing a Single Customer Account so taxpayers can interact with all their tax information in one place.* *Tax simplification is an ongoing priority for the government and will be kept at the core of the policy development process as tax and administration changes are considered for future fiscal events.*

4.45 Capital allowances: Full expensing – From 1 April 2023 until 31 March 2026 investments made by companies in qualifying plant and machinery will qualify for a 100% first-year allowance for main rate assets. This means companies across the UK will be able to write off the full cost in the year of investment, known as full expensing. Companies investing in special rate (including long life) assets will also benefit from a 50% first-year allowance in the year of investment. Expenditure on plant or machinery for leasing is excluded from first -year capital allowances due to longstanding concerns about abuse and wide scope for error. The government will work with industry to identify possible policy solutions that appropriately mitigate these risks.

The HMRC has confirmed within its Full Expensing (FE) Fact Sheet that the standard exclusions to FYAs under Section 46 CAA01 will apply, most notably the exclusions of expenditure on cars, and plant and machinery for leasing except where it is under an excluded lease of background plant or machinery for a building. Expenditure must be incurred by a company within the charge to corporation tax and the plant or machinery must be unused and not second-hand.

4.59 Amendments to Corporate Interest Restriction – The government will be making a number of modifications in connection with the Corporate Interest Restriction rules in order to protect Exchequer revenue, remove unfair outcomes and reduce administrative burdens for businesses. In most cases, these will take effect for periods of account commencing on or after 1 April 2023.

4.60 Amendments to the rules for Real Estate Investment Trusts (REIT) – Amendments will be made to the REIT regime to enhance its competitiveness. In addition to changes announced in the Edinburgh Reforms launched on 9 December 2022, which will address unnecessary barriers to entry and ensure the rules are operating as intended, the government will also reduce administrative burdens for certain partnerships investing in REITs. The changes will variously apply from 1 April 2023 and Royal Assent of the Spring Finance Bill 2023.

4.61 Amendments to the Qualifying Asset Holding Companies (QAHC) rules – Following the successful introduction of the new QAHC tax regime from April 2022, the government will legislate to make a number of targeted changes so that the regime is more widely available to investment fund structures which fall within its intended scope and the rules better achieve their intended effect. This will further enhance the attractiveness of the UK as a location for establishing asset holding companies by allowing more relevant companies to make use of the regime. Changes will variously take effect from Royal Assent of the Spring Finance Bill 2023, 20 July 2022 and 15 March 2023, or are deemed to have always had effect.

4.62 Amendments to the Genuine Diversity of Ownership (GDO) Rules – The government will make changes to the GDO condition in the QAHC, REIT and Non-Resident Capital Gains (NRCG) rules. The GDO condition is intended to prevent funds that are only open to a small number of predetermined investors from benefitting from those regimes. The changes will improve the operation of the GDO condition for fund structures involving multiple pooling vehicles and take effect from Royal Assent of the Spring Finance Bill 2023.

4.79 VAT relief for energy saving materials – The government has published a call for evidence on options to reform the VAT relief for the installation of energy saving materials in the UK. The call for evidence will consider the inclusion of additional technologies and the possible extension of the relief to include buildings used solely for a relevant charitable purpose.

4.81 VAT: DIY Housebuilders Scheme Digitisation Project – The government will legislate to digitise the DIY housebuilders' scheme and will also extend the time limit for making claims from 3 to 6 months. These measures should improve the overall customer experience and reduce the administrative burden for claimants and HMRC.

4.98 Two-Year extension of the Climate Change Agreement scheme – The government will extend the Climate Change Agreement scheme by two years. Participants that meet agreed energy efficiency targets will be entitled to reduced rates of Climate Change Levy in 2025-26 and 2026-27. The extension will be open to new participants in currently eligible sectors. Department for Energy Security and Net Zero (DESNZ) will consult on the details of the extension and proposals for any potential future Climate Change Agreement scheme.

4.99 Carbon Capture, Usage and Storage (CCUS) – The government will also provide up to £20billion funding for early deployment of CCUS, to help meet the government's climate commitments. A shortlist of projects for the first phase of CCS deployment will be announced later this month. Further capture projects will be able to enter a selection process for Track 1 expansion to be launched this year, and 2 additional clusters will be selected through a Track 2 process, with details announced shortly.

4.100 CCUS – tax treatment of payments into decommissioning funds – Certain oil and gas assets can be repurposed for use in CCUS projects, generating cost and development time savings. The government will introduce legislation in a future Finance Bill to establish the tax treatment of payments made into decommissioning funds by oil and gas companies in relation to the repurposing of oil and gas assets for use in CCUS projects.

4.123 Levelling Up Partnerships – The Spring Budget announces the rollout of new Levelling Up Partnerships, providing over £400 million and bringing the collective power of government to provide bespoke place-based regeneration in twenty of England's areas most in need of levelling up over 2023-24 and 2024-25. The government will ensure a fair geographic spread across the regions of England, inviting the following areas to develop a partnership including: City of Kingston upon Hull, Sandwell, Mansfield, Middlesbrough, Blackburn with Darwen, Hastings, Torbay, Tendring, Stoke-on-Trent, Boston, Redcar and Cleveland, Wakefield, Oldham, Rother, Torridge, Walsall, Doncaster, South Tyneside, Rochdale, and Bassetlaw. Apportionment of this investment will be made on a case-by-case basis, and in each of these places, the government will work with local leaders and mayors in councils and combined authorities, local businesses from all sectors, community organisations and residents to identify and address the biggest barriers to levelling up.

From the Government Investment Zone prospectus, it is noted the following areas in England to begin discussions with Government and co-develop proposals for an Investment Zone. The eight places are those covered by:

- The proposed East Midlands Mayoral Combined County Authority
- Greater Manchester Mayoral Combined Authority

- Liverpool City Region Mayoral Combined Authority
- The proposed North East Mayoral Combined Authority
- South Yorkshire Mayoral Combined Authority
- Tees Valley Mayoral Combined Authority
- West Midlands Mayoral Combined Authority
- West Yorkshire Mayoral Combined Authority

Subject to the relevant site's proposals meeting specified requirements, Government will offer Investment Zone areas a total funding envelope of £80m over five years, which can be used flexibly between spending and a single five-year tax offer, scalable based on number of sites. This would consist of:

- **£35m flexible spend**, split 40:60 between resource spending (RDEL) and capital spending (CDEL), to use across a portfolio of interventions based on the opportunities of each cluster;
- **Tax incentives**, which can cover up to 600ha across up to 3 sites, lasting for 5 years. Where places do not opt for the maximum tax offer of 600ha, tax incentives can be exchanged for a greater amount of spend.

4.124 Levelling Up Regeneration Projects – The Spring Budget announces £211 million for 16 regeneration projects in England. These projects have been assessed as high quality and will commence delivery later this year. Investment has been targeted towards the left-behind places in the Levelling Up White Paper or projects that are under £10 million to ensure quick delivery and a good spread of funding across England. All funding is subject to final subsidy checks.

4.125 Levelling Up Capital Projects – £58 million will be invested in three levelling up capital projects in the North West of England. This will see a new community hub in Stockport, the transformation of Bootle town centre, and the redevelopment of markets as well as transport connectivity improvements in Rossendale.

4.126 City and Metropolitan Regeneration Projects – The government has provided a further £161million for high-value capital regeneration projects in city regions across England, including business premises and food science facilities in Tees Valley, and unlocking investment in a research campus in the Liverpool City Region.

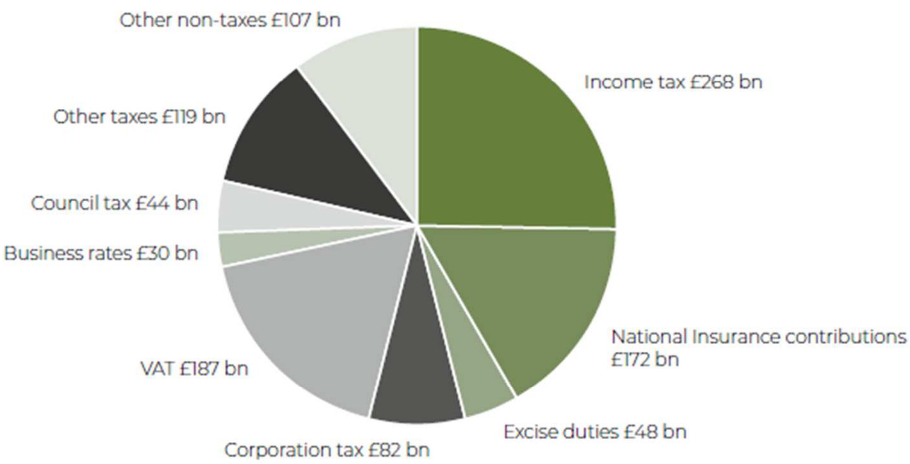
4.127 Community Ownership Fund – The government is announcing funding for a further 30 projects across the UK as part of the existing £150 million Community Ownership Fund.

4.128 Levelling Up Fund Round 3 update – A third round of the Levelling Up Fund will proceed as planned later in 2023 with a further £1 billion to level up places across the UK.

Lastly, the updated table B1 below shows the overall make up of UK tax take by the Government:

B.1 Chart B.1 shows public sector receipts by main type. Public sector receipts are expected to be around £1,058 billion in 2023-24.

Chart B.1: Public sector current receipts 2023-24



Figures may not sum due to rounding.
Other taxes includes capital taxes, stamp duties, vehicle excise duties and other smaller tax receipts.. Other non-taxes includes interest and dividends, gross operating surplus and other smaller non-tax receipts.

Source: Office for Budget Responsibility.

Thankfully, the immediate response was largely positive and considerably more muted to last year's 'mini-Budget' that saw Mr Hunt's predecessor, Kwasi Kwarteng MP forced out of the role after only 38 days in office.

Over the coming days and weeks, various Government departments will publish fuller details that will assist in understanding how these announcements will impact UK businesses. As with the 1980/90s Enterprise Zones before, tax relief and wider fiscal incentives can certainly help to bolster regeneration and growth across regions, businesses and the wider economy – particularly when carefully focussed to help support Net Zero and innovation – aligning with the recently released Skidmore Report – "*Mission Zero*".

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