

Budget 2008



BN12

12 March 2008

CAPITAL ALLOWANCES: PLANT AND MACHINERY: ANNUAL INVESTMENT ALLOWANCE

Who is likely to be affected?

1. Businesses investing in plant and machinery.

General description of the measure

2. Legislation will be included in Finance Bill 2008 to introduce a new annual investment allowance (AIA) for the first £50,000 of a business's expenditure on most plant and machinery each year. This change is part of the business tax reform package announced at Budget 2007.
3. The new AIA will be available to:
 - any individual carrying on a qualifying activity (this includes trades, professions, vocations, ordinary property businesses and individuals having an employment or office);
 - any partnership the consisting only of individuals; and
 - any company (subject to the limitations described below).

Operative date

4. The measure will have effect for expenditure incurred on or after 1 April 2008, for businesses within the charge to corporation tax, and on or after 6 April 2008, for businesses within the charge to income tax.

Current law and proposed revisions

5. Capital allowances allow business to write off the costs of capital assets, such as plant and machinery, against their taxable income. They take the place of commercial depreciation, which is not allowed for tax. On and after 1 April 2008 (for corporation tax), or 6 April (for income tax), the rate of writing down allowances (WDAs) will be 20 per cent per annum for general plant and machinery, and 10 per cent per annum for "special rate" plant and machinery, (see BN08), both on a reducing balance basis.

6. On or before 31 March 2008 (for companies) or 5 April 2008 (for unincorporated businesses), small and medium-sized enterprises (SMEs) can continue to claim a first-year allowance (FYA) on certain expenditure on plant or machinery. For expenditure incurred on or before those dates, the FYA rate for small enterprises is 50 per cent and for medium-sized enterprises the rate is 40 per cent of the expenditure incurred. The SME first-year allowance will no longer be available for any expenditure incurred on or after 1 April (corporation tax) or 6 April 2008 (income tax).
7. On and after 1 April 2008 (corporation tax) or 6 April 2008 (income tax) most businesses, regardless of size, will be able to claim the new AIA on the first £50,000 spent on plant or machinery (subject to the exclusions set out in paragraphs 18-19). Businesses will be able to claim the AIA in respect of expenditure on long-life assets and integral features (see BN07), as well as on general plant and machinery.
8. Where businesses spend more than £50,000 in any chargeable period, any additional expenditure will be dealt with in the normal capital allowances regime, entering either the special rate or main pool, where it will attract WDAs at the appropriate rate, (BN08).
9. Where a business has a chargeable period which is more or less than a year, the maximum allowance is proportionately increased or reduced. However, where a business has a chargeable period that spans 1 April 2008 (corporation tax) or 6 April 2008 (income tax) the maximum allowance is calculated as if the chargeable period began on either 1 or 6 April 2008 (as the case may be) and ended at the end of the chargeable period. So, for example, a company with a chargeable period from 1 January 2008 to 31 December 2008 would calculate its maximum entitlement to an AIA for that chargeable period based on the period from 1 April 2008 to 31 December 2008. Its maximum allowance for the transitional period would therefore be $\frac{9}{12} \times £50,000 = £37,500$.
10. The AIA complements and does not replace any of the existing 100 per cent FYA schemes. Similarly, expenditure that qualifies for 100 per cent allowances under separate capital allowances codes (for example, Research & Development Allowances or Business Premises Renovation Allowances) will be unaffected by the introduction of the AIA.

Targeting the AIA

Companies

11. Companies that fall within the company law definition of a group are legally and economically inter-dependent and will therefore receive a single allowance per group. Where a person, or persons together, control a singleton company, but do not control any “related” company each such company will be entitled to its own AIA.

Individuals and partnerships

12. Where an individual or individuals control(s) an unincorporated business or more than one unincorporated business, but he/she/they do not control a “related” unincorporated business, each separate and distinct business will be entitled to its own AIA.

“Related” companies and businesses

13. The rules on “related” companies and businesses under common control will only have effect for a very small minority of businesses. Most people do not control a multiplicity of related businesses, and so will not be affected by these rules. The rules will only have effect where a person (or persons) control(s) a company or unincorporated business in their own right. The wider “connected persons” and “associated company” rules are not relevant for the purposes of determining an entitlement to AIA.

14. Where a person or persons control(s) one or more unincorporated businesses or companies, (but not a combination of the two, as the entitlement to an AIA for companies is considered totally separately from that for unincorporated businesses, and vice versa) then the entitlement to one or more AIA will depend on whether either “the shared premises” or “similar activities” condition is met. If either of the conditions is met then the companies, or as the case may be, the unincorporated businesses will be “related” and so only entitled to a single AIA between them.

15. For businesses under common control, the two conditions are considered on a financial year basis for companies and on a tax year basis for unincorporated businesses:

- The “shared premises” condition has effect, if in a tax or financial year (as the case may be), at the end of the chargeable period for one or both of the businesses the activities are carried on from the same premises.
- The “similar activities” condition has effect, if in a tax or financial year (as the case may be), at the end of the chargeable period for one or both of the businesses, more than 50 per cent of each business’s activities (measured by turnover) are within the same “NACE classification”.

16. The “NACE classification” is the common statistical classification of economic activities in the European Union established by Regulation (EC) No 1893/2006 of the European Parliament and the Council of 20 December 2006 and is generally accepted as a convenient way of classifying activities into a common structure. Some general background and a description of the first level of statistical classification that will have effect for AIA purposes is available on the Office of National Statistics’.

Freedom of allocation for groups and “related” businesses

17. In addition to the freedom to allocate the AIA between different types of plant and machinery expenditure mentioned in paragraph 7, groups of companies and “related” companies, individuals and partnerships will be free to allocate their AIA between businesses as they see fit.

Exclusions

18. The AIA will have effect for most plant and machinery expenditure, but certain exceptions that apply to FYAs (SME FYAs are mentioned earlier at paragraph 6) will continue to have effect for the purposes of the AIA. The main exception is expenditure on cars. However, unlike SME FYAs, the AIA will be available for expenditure on long-life assets and assets for leasing.
19. Furthermore the AIA will not be available where transactions are entered into where the main purpose or one of the main purposes is to enable a person to obtain an annual investment allowance to which they would not otherwise have been entitled.

Further advice

20. If you have any questions about this change, please contact Joy Guthrie on 020 7147 2610 (email: Joy.Guthrie@hmrc.gsi.gov.uk) or Malcolm Smith on 020 7147 2555 (email: Malcolm.Smith3@hmrc.gsi.gov.uk). Information about Budget measures is available on the HM Revenue & Customs website at www.hmrc.gov.uk