

CAPITAL ALLOWANCES: INDUSTRIAL BUILDINGS ALLOWANCES,
ENTERPRISE ZONE ALLOWANCES AND AGRICULTURAL BUILDINGS
ALLOWANCES: DRAFT LEGISLATION

HM Revenue and Customs are publishing draft legislation to show how the phasing out of industrial buildings allowances and agricultural buildings allowances and also the withdrawal of enterprise zone allowances will be effected.

The draft legislation also includes an anti-avoidance rule, effective from today, that potentially limits the amount of a WDA, on a time apportioned basis, where property qualifying for IBAs is transferred or sold between connected parties as part of an arrangement where the purpose, or one of the main purposes, is the obtaining of a tax advantage.

Draft clauses and draft explanatory notes are attached below. Further information can be obtained from

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1 Abolition of allowances from 2011

- (1) Parts 3 and 4 of CAA 2001 (industrial buildings allowances and agricultural buildings allowances) –
 - (a) do not apply in relation to expenditure incurred on or after the relevant date, and
 - (b) are repealed in relation to chargeable periods beginning on or after the relevant date.
- (2) The relevant date is –
 - (a) for corporation tax purposes, 1 April 2011, and
 - (b) for income tax purposes, 6 April 2011.
- (3) Schedule 1 contains consequential amendments and savings.

2 Phasing out of allowances before abolition

- (1) For a chargeable period to which this section applies (“a transitional chargeable period”), a person’s entitlement to a writing-down allowance under Part 3 or 4 of CAA 2001 in respect of qualifying expenditure is to be determined in accordance with this section.
- (2) This section does not apply to a writing-down allowance in respect of qualifying enterprise zone expenditure.
- (3) If the whole of a transitional chargeable period falls within a financial year listed in column 1 of the table (for corporation tax purposes) or a tax year listed in column 2 of the table (for income tax purposes), the writing-down allowance to which the person is entitled for that chargeable period is –

$$\text{WDA} \times \text{P}$$

where –

WDA is the writing-down allowance to which the person would be entitled for the chargeable period apart from this section, and

P is the percentage specified in relation to that year in column 3 of the table.

- (4) If subsection (3) does not apply in relation to a transitional chargeable period, the writing-down allowance to which the person is entitled for that chargeable period is to be determined by –
 - (a) calculating the apportioned writing-down allowance for each financial year (for corporation tax purposes) or tax year (for income tax purposes) in which part of the chargeable period falls, and
 - (b) adding the amounts of the apportioned writing-down allowance for each of those years.

- (5) For the purposes of Part 3 of CAA 2001 (industrial buildings), the apportioned writing-down allowance for a financial year or tax year in which part of a transitional chargeable period falls is –

$$\frac{\text{DCPY}}{\text{DCP}} \times \text{WDA} \times \text{P}$$

where –

DCPY is the number of days in the chargeable period which fall in that year,

DCP is the number of days in the chargeable period,

WDA is the writing-down allowance to which the person would be entitled for the chargeable period apart from this section, and

P is the percentage specified in relation to that year in column 3 of the table.

- (6) For the purposes of Part 4 of CAA 2001 (agricultural buildings), the apportioned writing-down allowance for a financial year or tax year in which part of a transitional chargeable period falls is –

$$\frac{\text{RDCPY}}{\text{RDCP}} \times \text{WDA} \times \text{P}$$

where –

RDCPY is the number of relevant days in the chargeable period which fall in that year,

RDCP is the number of relevant days in the chargeable period,

WDA is the writing-down allowance to which the person would be entitled for the chargeable period apart from this section, and

P is the percentage specified in relation to that year in column 3 of the table.

- (7) The relevant days in the chargeable period are the days in that period for which the person was entitled to the relevant interest in relation to the qualifying expenditure (within the meaning of Part 4 of CAA 2001).
- (8) For the purposes of CAA 2001, the residue of the qualifying expenditure at any time is to be calculated as if the writing-down allowance made to a person under Part 3 or 4 of that Act in respect of the qualifying expenditure for any transitional chargeable period were the writing-down allowance which would have been made apart from this section.
- (9) This section applies –
- for corporation tax purposes, to chargeable periods which begin before the relevant date and end on or after 1 April 2008, and
 - for income tax purposes, to chargeable periods which begin before the relevant date and end on or after 6 April 2008.
- (10) In this section, references to the table are to the following table –

<i>Column 1</i>	<i>Column 2</i>	<i>Column 3</i>
Financial year beginning 1 April 2007 and earlier financial years	Tax year 2007-08 and earlier tax years	100%

<i>Column 1</i>	<i>Column 2</i>	<i>Column 3</i>
Financial year beginning 1 April 2008	Tax year 2008-09	75%
Financial year beginning 1 April 2009	Tax year 2009-10	50%
Financial year beginning 1 April 2010	Tax year 2010-11	25%
Financial year beginning 1 April 2011 and later financial years	Tax year 2011-12 and later tax years	0%

- (11) In this section –
 “the relevant date” has the same meaning as in section 1, and
 “qualifying expenditure”, in relation to a writing-down allowance under Part 3 or 4 of CAA 2001, means the qualifying expenditure in respect of which the allowance is made.

3 Qualifying enterprise zone expenditure: transitional provision

- (1) For a chargeable period which begins before, and ends on or after, the relevant date, a person’s entitlement to a writing-down allowance under Part 3 of CAA 2001 in respect of qualifying enterprise zone expenditure is to be determined in accordance with subsection (2).
- (2) The writing-down allowance to which the person is entitled is –

$$\frac{\text{DCPB}}{\text{DCP}} \times \text{WDA}$$

where –

DCPB is the number of days in the chargeable period which fall before the relevant date,
 DCP is the number of days in the chargeable period, and
 WDA is the writing-down allowance to which the person would be entitled for the chargeable period apart from this section.

- (3) In this section “the relevant date” has the same meaning as in section 1.

4 Phasing out of industrial buildings allowance: anti-avoidance

- (1) After section 313 CAA 2001 insert –

“313A Calculation of allowance after sale of relevant interest: anti-avoidance

- (1) This section applies where –
- there is a sale of the relevant interest in the building which is a balancing event to which section 314 applies,
 - the buyer and seller have different chargeable periods,
 - the control test (within the meaning of section 567) is met, and
 - the purpose, or one of the main purposes, of the sale is the obtaining of a tax advantage by the buyer under this Part.

- (2) The writing-down allowance to which the buyer is entitled for the chargeable period in which the sale takes place is –

$$\frac{DI}{CP} \times WDA$$

where –

DI is the number of days in the chargeable period for which the buyer is entitled to the relevant interest,

CP is the number of days in the chargeable period, and

WDA is the writing-down allowance to which the buyer would be entitled apart from this section.”

- (2) This section applies in relation to the sale of a relevant interest on or after 12 March 2008, except for such a sale in pursuance of a relevant pre-commencement contract (and for this purpose “sale” has the same meaning as for the purposes of Part 3 of CAA 2001).
- (3) A contract is a relevant pre-commencement contract if –
- (a) the contract is a contract in writing made before 12 March 2008,
 - (b) the contract is unconditional or its conditions have been satisfied before that date,
 - (c) no terms remain to be agreed on or after that date, and
 - (d) the contract is not varied in a significant way on or after that date.

SCHEDULES

SCHEDULE 1

Section 1

ABOLITION OF ALLOWANCES: CONSEQUENTIAL AMENDMENTS AND SAVINGS

PART 1

CONSEQUENTIAL AMENDMENTS

CAA 2001

- 1 CAA 2001 is amended as follows.
- 2 In section 1 (capital allowances) omit—
 - (a) subsection (2)(b) and (c) (entitlement to industrial and agricultural buildings allowances), and
 - (b) in subsection (3) “, industrial buildings or agricultural buildings,”.
- 3 In section 2(3) (general means of giving effect to capital allowances) omit—
 - (a) “sections 352 to 355 (industrial buildings allowances);”, and
 - (b) “sections 391 and 392 (agricultural buildings allowances);”.
- 4 In section 3 (claims for capital allowances), omit subsections (4)(b) and (5)(b).
- 5 In section 443(3) (disposal values and disposal events), omit “or 3” and “and industrial building allowances”.
- 6 In section 448(3) (additional VAT rebate generates disposal value), in subsection (3) omit “or 3” and “and industrial buildings allowances”.
- 7 In section 537 (contribution allowances), omit “, 3, 4” in—
 - (a) subsection (1),
 - (b) subsection (2)(b)(ii), and
 - (c) the heading.
- 8 Omit section 539 (contribution allowances: industrial buildings).
- 9 Omit section 540 (contribution allowances: agricultural buildings).
- 10 In section 542(1) (effect of transfers of trade on contribution allowances), for “Parts 3, 4 and 5” substitute “Part 5”.
- 11 In section 546 (introduction to Chapter 2 of Part 12), omit paragraph (b).
- 12 In section 564 (application of procedure in section 563) —
 - (a) in subsection (1), for “3” substitute “3A”, and
 - (b) omit subsection (3).
- 13 In section 567(1) (sales treated as for alternative amounts) omit “3,” and “4,”.

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- 14 In section 569 (election to treat sale as being for an alternative amount), omit—
- (a) in subsections (3)(a) and (5)(a), “3 or”, and
 - (b) in subsection (5), “319 (building not an industrial building, etc throughout) or”.
- 15 In section 570 (elections: supplementary) omit—
- (a) in subsection (1), “, 4”, and
 - (b) in subsection (3), “3”.
- 16 In section 570A(1) (avoidance affecting proceeds of balancing event) omit “3,” and “4”.
- 17 In section 573(1) (transfers treated as sales) omit “3,” and “4”.
- 18 (1) Part 2 of Schedule 1 (index of defined expressions) is amended as follows.
- (2) Omit the entries relating to the following defined expressions—
- “adjusted net cost (in Chapter 7 of Part 3)”,
 - “agricultural building”,
 - “balancing adjustment (in Part 3)”,
 - “balancing adjustment (in Part 4)”,
 - “balancing event (in Part 3)”,
 - “balancing event (in Part 4)”,
 - “building (in Part 3 - includes structure)”,
 - “commercial building (in Part 3, in relation to qualifying enterprise zone expenditure)”,
 - “developer, carrying on a trade as (in Chapter 4 of Part 3)”,
 - “enterprise zone (in Part 3)”,
 - “expenditure on the construction of a building (in Part 3)”,
 - “expenditure on the construction of a building (in Part 4)”,
 - “highway concession (in Chapter 9 of Part 3)”,
 - “husbandry (in Part 4)”,
 - “industrial building”,
 - “lease and related expressions (in Part 3)”,
 - “lease and related expressions (in Part 4)”,
 - “proceeds from a balancing event (in Part 3)”,
 - “proceeds from a balancing event (in Part 4)”,
 - “qualifying enterprise zone expenditure (in Part 3)”,
 - “qualifying hotel (in Part 3)”,
 - “qualifying trade (in Part 3)”,
 - “related agricultural land (in Part 4)”,
 - “relevant interest (in Part 3)”,
 - “relevant interest (in Part 4)”,
 - “residue of qualifying expenditure (in Part 3)”,
 - “residue of qualifying expenditure (in Part 4)”, and
 - “writing-down period (in Part 4)”.
- (3) In the entry relating to “sale, transfers under Parts 3, 3A, 4, 4A and 10 treated as”, omit “3,” and “4”.
- 19 In Schedule 3 (transitional provision and savings) omit—

- (a) paragraphs 56 to 83, and
- (b) paragraph 110.

ICTA 1988

- 20 In section 495 of ICTA (regional development grants), omit –
- (a) in subsection (1)(b) “, 3” and “, industrial buildings”, and
 - (b) in subsection (3)(b) “, 3”.

FA 2001

- 21 (1) FA 2001 is amended as follows.
- (2) In Schedule 19 (insertion of Part 4A of CAA 2001: consequential amendments), omit paragraph 4.
 - (3) In Schedule 21 (capital allowances: minor amendments), omit paragraphs 5 and 6.

ITTOIA 2005

- 22 In Schedule 1 of ITTOIA 2005 (consequential amendments), omit paragraphs 552 to 558.

ITA 2007

- 23 (1) ITA 2007 is amended as follows.
- (2) In section 24(1)(b) (reliefs deductible at Step 2), omit the entry relating to Part 3 of CAA 2001.
 - (3) In section 25(3) (reliefs deductible at Steps 2 and 3: supplementary), omit the entry relating to section 355 of that Act.
 - (4) In Schedule 1 (minor and consequential amendments), omit paragraph 406.

FA 2007

- 24 In FA 2007, omit section 36 (industrial and agricultural buildings allowances: balancing adjustments).

Commencement

- 25 This Part of this Schedule has effect in relation to chargeable periods (within the meaning of CAA 2001) beginning on or after –
- (a) for corporation tax purposes, 1 April 2011, and
 - (b) for income tax purposes, 6 April 2011.

PART 2

SAVINGS

Enterprise zone expenditure

- 26 (1) Sub-paragraph (2) applies if –

- (a) an initial allowance or a writing down allowance has been made under Part 3 of CAA 2001 in respect of qualifying enterprise zone expenditure, and
 - (b) an event occurs in relation to the building on which the expenditure was incurred which, if that Part of that Act remained in force, would be a balancing event in respect of which a balancing charge would be made.
- (2) Unless the event occurs more than 7 years after the building was first used, a balancing charge is to be made in respect of the event as if that Part of that Act remained in force.

Definition of structure

- 27 Despite the repeal of Part 3 of CAA 2001 by section 1, Chapter 2 of that Part continues to have effect for the purposes of paragraph (a) of item 7 in List B in section 22(1) of that Act (structures which are not plant and machinery).

Definition of qualifying trade

- 28 Despite the repeal of Part 3 of CAA 2001 by section 1, the following provisions continue to have effect for the purposes of section 484 of that Act (dredging allowances: definition of qualifying trade) –
- (a) section 274(1) (definition of qualifying trade), and
 - (b) sections 276(3) and 341(4) of that Act (parts of trades and undertakings; meaning of “highway concession”) so far as they relate to the Tables in that section.

Commencement

- 29 This Part of this Schedule has effect in relation to chargeable periods (within the meaning of CAA 2001) beginning on or after –
- (a) for corporation tax purposes, 1 April 2011, and
 - (b) for income tax purposes, 6 April 2011.

DRAFT EXPLANATORY NOTE

CLAUSE 1 SCHEDULE 1: ABOLITION OF ALLOWANCES
FROM 2011

SUMMARY

1. This clause abolishes Parts 3 and 4 of the Capital Allowances Act 2001, which provide allowances for industrial and agricultural buildings. The allowances will cease to apply to expenditure incurred, or to chargeable periods beginning, on or after 1 April 2011 (for corporation tax purposes) and 6 April 2011 (for income tax purposes). The clause also introduces a schedule containing consequential amendments and savings.

DETAILS OF THE CLAUSE

2. Subsection (1) provides that Parts 3 and 4 of Capital Allowances Act 2001 (CAA) are repealed from the 'relevant date' in relation to:
 - qualifying expenditure incurred on or after the relevant date, and
 - chargeable periods beginning on or after the relevant date.

3. Subsection (2) gives the relevant dates referred to in subsection (1). The dates are
 - for corporation tax purposes, 1 April 2011, and
 - for income tax purposes, 6 April 2011.
4. Subsection (3) introduces Schedule 1, which makes consequential amendments and savings.

DETAILS OF THE SCHEDULE

SCHEDULE 1

ABOLITION OF ALLOWANCES: CONSEQUENTIAL AMENDMENTS AND SAVINGS

PART 1

CONSEQUENTIAL AMENDMENTS

5. Paragraph 1 is introductory and provides that the Capital Allowances Act (CAA) 2001 is amended in the ways described in the schedule.
6. Paragraphs 2 to 4 make consequential amendments to Part 1 CAA 2001.
7. Paragraphs 5 and 6 make consequential amendments to Part 6 CAA 2001.

8. Paragraphs 7 to 10 make consequential amendments to Part 11 CAA 2001.
9. Paragraphs 11 to 17 make consequential amendments to Part 12 CAA 2001.
10. Paragraph 18 makes consequential amendments to Part 2 of Schedule 1.
11. Paragraph 19 makes two consequential amendments to Schedule 3.
12. Paragraphs 20 to 24 make consequential amendments to other enactments.

Commencement

13. Paragraph 25 provides that Part 1 of the Schedule has effect in relation to chargeable periods (within the meaning of CAA 2001) beginning on or after-
 - for corporation tax purposes, 1 April 2011,
and
 - for income tax purposes, 6 April 2011.

PART 2

SAVINGS

Enterprise zone expenditure

14. Paragraph 26 is a saving provision that retains balancing charges in respect of certain qualifying enterprise zone expenditure where two conditions are met:
- a. The first condition is that an initial or writing down allowance has been made under Part 3 of CAA in respect of qualifying enterprise zone expenditure.
 - b. The second condition is that an event occurs that would have been a balancing event, in respect of which a balancing charge would have been made, if Part 3 CAA 2001 had remained in force.
15. If the two conditions are met then, unless the event occurs more than seven years after the first use of the building, a balancing charge is to be made in respect of the event as if Part 3 of CAA 2001 remained in force. For example, if a person made a claim to an initial allowance in 2010 and the building was first used on 1 December 2010, then if the relevant interest in the building is sold or otherwise disposed of before 1 December 2017, any balancing event that would have given rise to a balancing charge (and only a balancing charge) will result in a balancing charge being made as if Part 3 of CAA 2001 was still in force.

Definition of structure

16. Paragraph 27 is a saving provision that ensures that despite the abolition of Part 3, Chapter 2 of Part 3 continues to have effect to preserve the existing treatment of certain structures, so that they are not prevented from qualifying for plant and machinery allowances because of section 22.

Definition of qualifying trade

17. Paragraph 28 is a saving provision ensuring that the scope of dredging allowances, given under Part 9 of CAA 2001, is not limited or reduced following the abolition of Part 3.

Commencement

18. Paragraph 29 provides that Part 2 of the Schedule has effect in relation to chargeable periods (within the meaning of CAA 2001) beginning on or after-
- for corporation tax purposes, 1 April 2011, and
 - for income tax purposes, 6 April 2011.

BACKGROUND NOTE

19. IBAs and ABAs were introduced over 60 years ago as an incentive for post-war reconstruction and agricultural recovery. They are available under Parts 3 and 4 respectively, of CAA 2001. In general, the

annual rate of writing-down allowances (WDAs) for a person who constructs an industrial or agricultural building, or buys it unused, is 4 per cent of the qualifying expenditure (the construction cost or purchase price) on a “straight-line” basis. This means that the whole cost may be written-off over a 25-year period.

20. There is an exception for qualifying expenditure on buildings in enterprise zones, which qualifies for a special type of IBA, under Part 3 of CAA 2001, often called Enterprise Zone Allowances (EZAs). EZA expenditure attracts an initial allowance of 100 per cent, or where the full initial allowance has not been claimed, a WDA of 25 per cent in respect of any unrelieved expenditure. In all cases, the allowances are given to the holder of the “relevant interest” who has incurred the qualifying expenditure on the building.
21. Budget 2007 announced a significant package of reforms to the business tax system, designed to promote investment and growth, reduce administrative burdens and ensure fairness between tax payers. The package included a significant number of proposed changes to the capital allowances system, designed to reduce the distortive impact of capital allowances, including the abolition of IBAs and ABAs, under Parts 3 and 4 of the Capital

Allowances Act 2001. The Government decided to withdraw these allowances on the basis that they had become a poorly focused subsidy, selectively available on a disparate range of assets. The abolition of IBAs and ABAs from April 2011 is also designed to simplify the tax system and reduce compliance burdens. However, in order to give businesses time to adapt to the change, Budget 2007 announced that the allowances would be gradually phased out over a four year period.

22. The abolition of Parts 3 and 4 of CAA 2001 is the subject matter of this clause, which also introduces a schedule of consequential amendments and savings. One such saving is the potential preservation of a balancing charge in the event of a sale of a qualifying EZ building within seven years of first use, notwithstanding the repeal of Part 3 of CAA, with effect from 1 April 2011 (corporation tax) or 6 April 2011 (income tax).
23. The rules concerning the phasing-out of industrial or agricultural building WDAs between April 2008 and April 2011 are provided in clause 2. Clause 3 contains the transitional provision relating to the 25 per cent WDA for qualifying EZ expenditure, and clause 4 contains an anti-avoidance provision to prevent the exploitation of IBA WDAs in the phasing-out period.

DRAFT EXPLANATORY NOTE**CLAUSE 2: PHASING OUT OF ALLOWANCES BEFORE ABOLITION****SUMMARY**

1. This clause provides how a person's entitlement to industrial building or agricultural building writing-down allowances is to be progressively reduced in the three year phasing out period before abolition.

DETAILS OF THE CLAUSE

2. Subsection (1) explains that this new section will determine a person's entitlement to a writing-down allowance (WDA) under Part 3, industrial buildings allowances (IBAs), or under Part 4, agricultural buildings allowances (ABAs), of the Capital Allowances Act (CAA) 2001, for any chargeable period that is a transitional chargeable period. "Chargeable period" has the meaning given to it by section 6 CAA 2001.
3. Subsection (2) explains that this section does not apply to WDAs in respect of qualifying enterprise zone (EZ) expenditure. Qualifying EZ expenditure can attract WDAs at 25 per cent per annum on a straight-line basis. There is a separate transitional provision

in respect of these WDAs in cases where the chargeable period spans 1 April 2011 (corporation tax) or 6 April 2011 (income tax) in the next clause, clause 3.

4. Subsection (3) gives the rules for calculating a person's entitlement to a WDA in respect of a transitional chargeable period under Part 3 or Part 4 of CAA 2001, where the whole of the chargeable period falls within a financial year (for corporation tax purposes) or a tax year (for income tax purposes). The rule works by restricting the amount of the WDA a person would have been entitled to, apart from this section, by a set percentage dependent on which financial year or tax year the transitional chargeable period falls in. The appropriate percentage for that year is to be found in column 3 of the table at subsection 10.
5. The calculation of the WDA the person would have been entitled to is determined under the normal provisions of Part 3 (IBAs) or Part 4 (ABAs), as the case may be. For example, a person owning and holding the original relevant interest in an industrial building is entitled to a writing-down allowance of 4 per cent of the expenditure (see section 310 CAA 2001). Where the relevant interest has changed hands within 25 years of first use, the subsequent owner(s) is/are entitled to a 'recalculated' writing-

down allowance under section 311 CAA 2001. But if the transfer of the relevant interest took place on or after 21 March 2007, then the rules in section 311 are modified by section 36 Finance Act (FA) 2007.

6. Subsection (4) gives the rules where subsection (3) does not apply. The subsection requires businesses to calculate an apportioned WDA for each financial year, or tax year in which part of their chargeable period falls, and then to add all the amounts of apportioned WDAs for each of those years together, to arrive at the amount of WDA that may be claimed for the chargeable period.
7. Subsection (5) sets out, for the purposes of calculating an industrial buildings apportioned WDA, exactly how this is to be calculated for a financial year or tax year. It is to be calculated using the formula -

$$\frac{\text{DCPY}}{\text{DCP}} \times \text{WDA} \times \text{P}$$

Subsection (5) then gives the meaning for DCPY, DCP, WDA, and P:

- DCPY is the number of days in the chargeable period that fall in that year,
- DCP is the total number of days in the chargeable period,

- WDA is the amount of the writing-down allowance calculated in accordance with Part 3 (subject to the changes made by section 36 FA 2007, where the relevant interest changes hands on or after 21 March 2007).
- P is the percentage specified in relation to that year in column 3 of the table in subsection 10.

The effect of the formula is that the business calculates the WDA as normal (that is, ignoring the phasing-out provisions) for the chargeable period, time apports the WDA between the relevant financial (or tax) years and then applies the set percentage to the time apportioned WDAs.

8. Subsection (6) sets out, for the purposes of calculating an agricultural buildings apportioned WDA, exactly how this is to be calculated for a financial year or tax year. Because ABAs are calculated in a slightly different manner to IBAs on transfers of the relevant interest, the apportioned WDA formula is slightly different to reflect this, in order to be fair to both parties.

Subsection 6 provides the formula to be used -

$$\frac{\text{RDCPY}}{\text{RDCP}} \times \text{WDA} \times \text{P}$$

Subsection 6 then gives the meaning for RDCPY, RDCP, WDA, and P.

- RDCPY is the number of relevant days in the chargeable period that fall in that year,
 - RDCP is the total number of relevant days in the chargeable period,
 - WDA is the amount of the writing-down allowance calculated in accordance with Part 3 (subject to the changes made by section 36 FA 2007, where the relevant interest changes hands on or after 21 March 2007), and
 - P is the percentage specified in relation to that year in column 3 of the table in subsection 10.
9. Subsection (7) explains what is meant by 'relevant days' in the formula in subsection 6. The 'relevant days' in the chargeable period are the days in that period for which the person was entitled to the relevant interest in the asset giving rise to the agricultural building allowance.
10. Subsection (8) ensures that the amount of unrelieved expenditure or residue of qualifying expenditure (RQE) for the purposes of CAA 2001, is calculated as if the WDA made to a person under Part 3 or 4 for any

transitional chargeable period were the WDA which would have applied apart from this section.

11. Subsection (9) defines the transitional chargeable periods -

- for corporation tax purposes, they are chargeable periods which begin before the relevant date (that is, 1 April 2011) and end on or after 1 April 2008.
- for income tax purposes, they are chargeable periods that begin before the relevant date (that is, 6 April 2011) and end on or after 6 April 2008.

The “relevant date” in each case is defined in subsection (11).

12. Subsection (10) gives the table of percentages to be used for each financial and tax year for the transitional chargeable periods. In broad terms, the effect is that a person’s entitlement to a WDA is decreased by 25 per cent in relation to each financial or tax year (as the case may be) on a cumulative basis, until it is reduced to nil and allowances cease to be available.

13. Subsection (11) provides that “the relevant date” has the same meaning as in subsection (2) of clause 1. The relevant date is

- for corporation tax purposes, 1 April 2011, and
 - for income tax purposes, 6 April 2011.
14. Subsection 11 also clarifies what is meant by “qualifying expenditure” in relation to a WDA under Part 3 or 4 of CAA 2001.

BACKGROUND NOTE

15. IBAs and ABAs were introduced over 60 years ago as an incentive for post-war reconstruction and agricultural recovery. They are available under Parts 3 and 4 respectively, of CAA 2001.
16. Budget 2007 announced a significant package of reforms to the business tax system, designed to promote investment and growth, reduce administrative burdens and ensure fairness between tax payers. The package included a significant number of proposed changes to the capital allowances system, designed to reduce the distortive impact of capital allowances.
17. The changes announced included the phased withdrawal of IBAs and ABAs. The Government explained that it had decided to withdraw these allowances because they had become a poorly focused subsidy, selectively available on a disparate

range of assets. Abolition is also intended to simplify the tax system and reduce compliance burdens.

18. In order to give businesses time to adapt to the change, Budget 2007 announced that the allowances would be gradually phased out over a four year period. The rules concerning the phasing-out of industrial and agricultural building writing-down allowances (WDAs) are the subject matter of this clause.
19. In general, the annual rate of WDA for a person who constructs an industrial or agricultural building, or buys it unused, is 4 per cent of the qualifying expenditure (the construction cost or purchase price) on a “straight-line” basis. This means that the whole cost may be written-off over a 25-year period.
20. Prior to Budget 2007, when a person ceased to have the relevant interest in an industrial or agricultural building within 25 years of first use (typically when the building was sold or a leasehold interest came to an end) there was a balancing adjustment (giving rise to either a balancing charge or a balancing allowance), based on any difference between the residue of qualifying expenditure (RQE) and the proceeds from the event. The person acquiring the building would then be entitled to a recalculated WDA, based on the expenditure that had not yet been written off (taking

into account the balancing adjustment) divided by the remainder of the 25-year period. For example, if the remainder of the 25-year period was 10 years, and the RQE after the sale was £10,000, the buyer would be entitled to a recalculated WDA of $£10,000/10 = £1,000$ a year over the remaining ten years.

21. To prepare the way for final abolition, Budget 2007 announced the withdrawal of balancing adjustments and the recalculation of WDAs. Broadly speaking, this meant that the person acquiring the relevant interest in the building would effectively “stand in the shoes” of the person who had disposed of his interest, and so would effectively be entitled to the same amount of WDAs as the previous owner.
22. This clause provides that the basic calculation of the amount of the WDA is unchanged and as explained above, but the amount of the WDA (whether original or recalculated) is to be stepped-down by 25 per cent a year, in relation to the time apportioned part of a business’s transitional chargeable period falling in each financial year or tax year, as the case may be, of the phasing-out period.

DRAFT EXPLANATORY NOTE**CLAUSE 3: QUALIFYING ENTERPRISE ZONE****EXPENDITURE: TRANSITIONAL PROVISION****SUMMARY**

1. This clause provides for the time apportionment of a writing-down allowance in respect of qualifying enterprise zone expenditure, where the business's chargeable period straddles the relevant date for abolition, that is, 1 April 2011 for corporation tax purposes, or 6 April 2011 for income tax purposes.

DETAILS OF THE CLAUSE

2. Subsection (1) explains that for a chargeable period that begins before and ends on or after the relevant date, a person's entitlement to a writing-down allowance (WDA) in respect of qualifying enterprise zone expenditure (see sections 299 and 300 CAA 2001 for the meaning of qualifying enterprise zone expenditure) is to be determined in accordance with subsection (2).
3. Subsection (2) restricts a person's entitlement to a WDA in the chargeable period falling within subsection (1) by a simple time apportionment formula, which restricts the WDA to the part of the

chargeable period that falls before the relevant date.

The formula is:

$$\frac{\text{DCPB}}{\text{DCP}} \times \text{WDA}$$

- DCPB is the number of days in the chargeable period which fall before the relevant date,
 - DCP is the number of days in the chargeable period, and
 - WDA is the writing-down allowance the person would have been entitled to for the chargeable period apart from this section.
4. Subsection (3) provides that “the relevant date” has the same meaning as in subsection 2 of clause 1. The relevant date is
- for corporation tax purposes, 1 April 2011, and
 - for income tax purposes, 6 April 2011.

BACKGROUND NOTE

5. Budget 2007 announced a significant package of reforms to the business tax system, designed to promote investment and growth, reduce administrative burdens and ensure fairness between tax payers. The package included a significant number of proposed changes to the capital allowances system, designed to reduce the distortive impact of capital allowances, including the abolition of

industrial and agricultural buildings allowances (IBAs and ABAs), under Parts 3 and 4 of the Capital Allowances Act 2001. The Government decided to withdraw these allowances on the basis that they had become a poorly focused subsidy, selectively available on a disparate range of assets.

6. A special form of IBAs, commonly known as Enterprise Zone Allowances (EZAs), was introduced in 1980 for expenditure on buildings within designated enterprise zones. EZA expenditure attracts an initial allowance of 100 per cent, or where the full initial allowance has not been claimed, a WDA of 25 per cent in respect of any unrelieved expenditure.
7. As a consequential issue arising from its decision to phase-out IBAs and ABAs, the Government announced, in the December 2007 technical note on the “Business tax reform capital allowances changes”, that EZAs would be included in the abolition of IBAs from April 2011. In that technical note, the Government explained that the time was right to withdraw EZAs, because of the withdrawal of IBAs, the artificial extension of EZAs beyond the previous Government’s originally intended time-limit, and the disclosure of schemes seeking to avoid tax through EZAs. The Government also explained that, since taking office in 1997, it had adopted a different

approach to regeneration from the approach taken by the previous administration.

8. The abolition of EZAs, as a special form of IBAs included in Part 3 of CAA 2001, will be effected through the abolition of allowances from 2011 provided in clause 1. In cases where businesses have not claimed an initial allowance in full, but have instead claimed a 25 per cent WDA that spans the relevant date for abolition, this clause provides for the time-apportionment of that WDA. The relevant date in this context is 1 April 2011 for corporation tax purposes and 6 April 2011 for income tax purposes.
9. The schedule introduced by clause 1 also includes a saving provision to preserve a balancing charge in the event of a disposal of a building that qualified for EZAs within seven years of first use, notwithstanding the repeal of Part 3 from April 2011. Furthermore, potential balancing charges under sections 314 and 328 will similarly be retained for a limited period.

DRAFT EXPLANATORY NOTE**CLAUSE 4: PHASING OUT OF INDUSTRIAL BUILDINGS
ALLOWANCE: ANTI-AVOIDANCE****SUMMARY**

1. This clause provides an anti-avoidance rule to prevent connected parties from seeking to obtain multiple writing-down allowances by transferring a building qualifying for industrial buildings allowances to a series of owners in quick succession.

DETAILS OF THE CLAUSE

2. Subsection (1) introduces new section 313A into the Capital Allowances Act 2001 (CAA2001).

New section 313A Calculation of allowance after sale of relevant interest: anti-avoidance

3. New section 313A applies in very limited circumstances and, where applicable, limits the amount of writing-down allowance (WDA) a buyer is entitled to in the chargeable period where the buyer acquires the relevant interest giving rise to an entitlement to industrial buildings allowances. The section counteracts attempts by persons (mainly groups of companies) to obtain multiple industrial

building writing-down allowances (WDAs) by transferring a building or structure to a series of owners in rapid succession. The section does not apply to agricultural buildings allowances.

a. Subsection (1) gives the four conditions that have to be met before the section applies -

- i) The first condition is that there has to be a sale (or transfer) of the relevant interest,
- ii) The second condition is that the buyer and seller have different chargeable periods. (In typical group structures this is uncommon.)
- iii) The third condition is that the control test, within the meaning of section 567, is met. The control test is met where -
 - the buyer is a body of persons over whom the seller has control, or
 - the seller is a body of persons over whom the buyer has control, or
 - both the seller and the buyer are bodies of persons and another

person has control of them both,
or

- The seller and the buyer are connected persons.

iv) The fourth and final condition is that the purpose, or one of the main purposes, of the sale is the obtaining of a tax advantage by the buyer under Part 3.

b. Subsection (2) then gives the rule to determine how much WDA the buyer is entitled to in the chargeable period in which the sale takes place. The rule is expressed as a formula -

$$\frac{DI}{CP} \times WDA$$

- DI is the number of days in the chargeable period for which the buyer is entitled to the relevant interest (basically the number of days from the date of acquisition to the end of the chargeable period),
- CP is the total number of days in the chargeable period, and

- WDA is the WDA the buyer would have been entitled to if this clause did not apply.

Put simply, this is a time apportionment rule that limits the amount of the WDA to the fraction of WDA that relates to the period from the date of acquisition to the end of the chargeable period. For example, if a buyer bought a building on 15 April 2009 and had a chargeable period that started on 1 May 2008 and ended on 30 April 2009, the amount of WDA given by section 311 CAA 2001 would have reflected the whole of the buyer's chargeable period. This clause limits the buyer's entitlement to 16/365ths of the WDA.

4. Subsection (2) gives the commencement rules relating to which transactions are within the scope of the clause. The clause applies to sales and transfers of relevant interests that occur on or after 12 March 2008 unless in pursuance to a relevant pre-commencement contract.
5. Subsection (3) defines when a contract is a relevant pre-commencement contract. There are 4 conditions to be met -

- the contract has to be in writing and made before 12 March 2008,
- the contract is unconditional, or its conditions have been satisfied before that date,
- no terms remain to be agreed on or after that date, and
- the contract is not varied in a significant way on or after that date.

BACKGROUND NOTE

6. Budget 2007 announced a significant package of reforms to the business tax system, designed to promote investment and growth, reduce administrative burdens and ensure fairness between tax payers. The package included a significant number of proposed changes to the capital allowances system, designed to reduce the distortive impact of capital allowances, including the abolition of industrial and agricultural buildings allowances (IBAs and ABAs), under Parts 3 and 4 of the Capital Allowances Act 2001.
7. The Government decided to withdraw these allowances on the basis that they had become a poorly focused subsidy, selectively available on a disparate range of assets. The abolition of IBAs and ABAs from April 2011 is also designed to simplify the tax system and reduce compliance burdens. However, in order to give businesses time to adapt to the change, Budget 2007 announced that the

allowances would be gradually phased out over a four year period.

- 8.** The abolition of allowances under Parts 3 and 4 of CAA 2001 from 2011 is provided by draft clause 1, and the phasing-out and transitional provisions are provided by draft clauses 2 and 3. This clause provides an anti-avoidance rule, effective from Budget day on 12 March 2008, that will limit an entitlement to a WDA on a time apportioned basis, where property qualifying for IBAs is sold or transferred between connected parties, and the purpose, or one of the main purposes of the sale, is the obtaining of a tax advantage by the buyer under Part 3 of CAA 2001.