

Capital allowances: renovation of business premises in disadvantaged areas

A consultation document

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Summary

In his 2003 Pre-Budget Report, the Chancellor of the Exchequer announced that the Government would introduce a scheme: Business Premises Renovation Allowance (BPRA), which would provide 100 per cent capital allowances for the capital costs of renovating or converting unused business premises in disadvantaged areas.

In this document we outline the design of the scheme and ask for your views on certain aspects of it. We also publish the draft legislation that will govern the scheme, and would like your views on whether it is technically correct and will meet the scheme's objectives.

The consultation period begins today 2 December 2004 and will run until 1 March 2005.

Please ensure that your comments on this Consultation Document and replies to any questions asked in it reach us by **1 March 2005**

Comments should be sent by email to: Paul.Thomas@ir.gsi.gov.uk

If you comment by post, please note that we will be moving offices on 15 December 2004, so the address to write to will depend on the date of your letter. The addresses are:

Up until 15 December 2004 at:

Paul Thomas
Inland Revenue
Business Tax
Room 4E1
22 Kingsway
LONDON WC2B 6NR
Tel: 020 7438 7143
Fax: 020 7438 7190

And from 16 December 2004 at

Room 3C/15
1 Parliament Street
LONDON SW1A 2BQ
Tel: 020 7147 2541
Fax: 020 7147 2639

Telephone enquiries on this consultation should be addressed, in the first instance, to Paul Thomas at either his current number or his future number depending on the date of your enquiry. (Both numbers are shown above.)

Paper copies of this document may be obtained free of charge from Paul Thomas at the first address above (if your request is made by 15 December 2004) or at the second address above (if your request is made on or after 16 December 2004).

This document can also be accessed from the Inland Revenue's Internet site:

<http://www.inlandrevenue.gov.uk>

Confidentiality

Responses to the consultation, together with the names and addresses of respondents, may be published unless confidentiality is specifically requested. We will assume that if you are replying by email, any confidentiality disclaimed that is generated by your organisation's IT system is overridden unless you specifically include a request to the contrary in the main text of your submission to us. Please note that confidentiality cannot be guaranteed where a response includes evidence of a serious crime.

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CHAPTER 1 - INTRODUCTION

Enterprise Areas

1.1 The Government believes that raising levels of enterprise and economic activity is essential to sustainable regeneration in the most disadvantaged communities of the UK. The 2002 Pre-Budget Report designated almost 2,000 of the most disadvantaged areas in the UK as “Enterprise Areas”, on which measures to boost enterprise are being focused. The measures are designed to reinforce local economic development. They include -

- stamp duty exemption for all non-residential property transactions and exemption up to £150,000 for residential property transactions;
- offering special investment help through the Community Investment Tax Relief and risk capital from the Community Venture Capital Fund;
- giving local planning authorities power to create business planning zones that cut red tape for growing businesses by removing the need to apply for planning permission and
- the Phoenix Development Fund, which is providing resources for several measures focused on Enterprise Areas.

1.2 A list of the Enterprise Areas is available from the Inland Revenue’s stamp duty website, at www.inlandrevenue.gov.uk/so/disadvantaged.htm. The website also includes a postcode search tool, at www.inlandrevenue.gov.uk/so/pcode_search.htm, which allows you to find out whether a postcode is within an Enterprise Area.

1.3 Further information about the UK’s Enterprise Areas is at **Annex A**.

The proposed Business Premises Renovation Allowance (BPRA) scheme

- 1.4 In the 2003 Pre-Budget Report, the Government announced that it had decided to use capital allowances to tackle specific market failures in Enterprise Areas, through a Business Premises Renovation Allowance (BPRA) scheme.
- 1.5 This scheme would provide *100 per cent first-year capital allowances in Enterprise Areas, for the capital costs a business incurs in converting or renovating business premises that have been vacant for at least a year, in order to bring them back into business use.*
- 1.6 Because BPRA would be targeted selectively on these 2,000 designated, disadvantaged areas in the UK, it would constitute a State aid¹. The Government is, therefore, in the course of discussing the State aid aspects of the scheme with the European Commission. Budget 2004 announced that, subject to State aid approval, BPRA will be introduced in 2005 and that the draft legislation would be published for public consultation.
- 1.7 We have therefore designed a scheme that will be open to individuals and companies who own or lease business property that has previously been unused for 12 months or more. The scheme will allow them to claim up-front tax relief on all their capital spending on the renovation or conversion of the property in order to bring it back into business use. The property must be in a designated Enterprise Area and the capital allowances will be available to the person or company (whether landlord or tenant) who in fact incurs the capital expenditure - as a deduction from their trading profits.

¹ A state aid is aid, whether provided directly by a state or indirectly through state resources, which distorts or threatens to distort competition within the European Community.

The scheme will run for five years from the date of introduction, which has yet to be determined.

Operational aspects

- 1.8 BPRA is intended to operate through the normal capital allowances system and may be claimed in the same way as other capital allowances. It is envisaged that there will be a box on businesses' annual income tax or corporation tax (as the case maybe) self-assessment returns, which claimants should complete if they have incurred "qualifying expenditure" (see paragraph 3.3) in any accounting period.

Structure of this document

- 1.9 The remainder of this consultation paper is laid out as follows:

Chapter 2: Raises some specific issues underlying the design of the scheme, on which we would be grateful for any views or for any further information.

Chapter 3: Provides an overview of the draft legislation.

Chapter 4: Contains the relevant draft legislation itself, on which detailed comments are invited.

Chapter 5: Summarises the questions raised throughout this paper.

Chapter 6: Contains the Code of Practice on Written Consultation and who to contact if you have any complaints about this consultation.

Annex A: Provides some further background on Enterprise Areas.

Annex B: Contains general information about capital allowances as background to the proposed new scheme and

Annex C: Contains the partial regulatory impact assessment.

Timetable

1.10 This consultation will close on 1 March 2005 and we will publish the results after the end of the consultation. The Government will consider the responses and, subject to that, will legislate to bring the scheme into operation following EC approval. We will publish guidance on how it will operate before it comes into force.

CHAPTER 2: SPECIFIC ISSUES

2.1 We would welcome views on the following specific design issues:

Issue 1: Length of time that the premises should have remained unused

2.2 The proposal currently provides that the business premises must have remained unused for **12 months or longer**. The Government's aim is to target the scheme appropriately, so as to overcome potential barriers to regeneration and the start-up of new business in disadvantaged areas in a cost efficient manner. We would, therefore, welcome views on whether a minimum of 12 months is the most appropriate length of void period for this new scheme. If, for example, premises typically lie vacant between lets, or pending sale, for this sort of period without any adverse consequences, a longer period could be indicated. On the other hand, we would also welcome reasoned evidence to support any view that a shorter period would be more appropriate (perhaps to prevent increasing the risk of long-term dereliction).

Q1. (a) Is a minimum of 12 months the most appropriate void period?

(b) If not, what period would you suggest?

Issue 2: Whether the scheme would be likely to create a "perverse incentive"

2.3 It could be suggested that some businesses would deliberately leave their premises vacant for a year or more in order to benefit from BPRA. This might create a perverse incentive to leave premises unused, contrary to the policy purpose of the scheme.

- 2.4 Our present assumption is that this is unlikely to happen because, under current tax law, the costs a business incurs on repairs and renewals of its business premises are chargeable in full in its trading account under normal accounting practice, and are allowable in full as deductions when computing profits for tax purposes. Existing businesses would, therefore, gain no advantage by deferring any repairs or renewals and leaving their premises vacant for 12 months or more in order to claim relief under BPRA.
- 2.5 Furthermore, the scope of BPRA is limited. Expenditure on converting or refurbishing business premises will not constitute *capital* expenditure for tax purposes (and thus be within the scope of BPRA) unless it is incurred -
- in connection with substantial alterations to a building (for example, to convert or sub-divide it into separate business units ready for business use) or
 - in connection with substantial improvements to a building, or
 - by a new owner to bring the premises up to the standard necessary for use in the new business.
- 2.6 Thus relief under BPRA would be neither available nor needed for the ordinary operating expenses incurred by an existing business. And, even if BPRA were available in such circumstances, it seems inherently unlikely that an existing business would forgo for a year or more the income that could be generated by making use of the premises, in order to access the relief available from BPRA.

Q2. (a) Are we correct in assuming that the scheme will not create a perverse incentive to leave premises vacant?

(b) We would welcome reasoned views, evidence or examples to support or contradict our assumptions that this undesired effect would be unlikely.

Issue 3: Impact on small and medium-sized enterprises (SMEs)

- 2.7 BPRA would be available to all SMEs that incur qualifying renovation or conversion costs, whether as landlords or tenants.
- 2.8 However, it is not proposed to restrict the measure to SMEs because evidence suggests that the majority of capital renovation expenditure to buildings is, in fact, incurred by larger businesses.
- 2.9 Our assumption is that smaller businesses would benefit from the measure both directly (in the form of tax relief whenever they incurred the relevant expenditure) and indirectly, through an increase in the stock of available business premises to let.

Q3. (a) Should BPRA be available to all businesses?

(b) We would welcome views and any data to support or contradict our assumption that BPRA is likely to benefit smaller firms both directly and indirectly (see paragraph 2.9 above).

(c) We would also welcome any data on the proportion of SMEs that (i) own or (ii) lease their premises, and in particular, the probability of SMEs either owning or leasing premises in disadvantaged areas.

CHAPTER 3 – OVERVIEW OF THE DRAFT LEGISLATION

- 3.1 This chapter provides an overview of, and commentary on, the draft legislation for the Business Premises Renovation Allowance (BPRA) scheme. The legislation itself is set out in full in chapter 4.

Capital allowances

- 3.2 BPRA is a proposed capital allowances scheme. Some general background about the current capital allowances regime is provided at **Annex B**. Capital allowances allow businesses to write-off the costs they incur on capital expenditure against their taxable profits. The capital allowances legislation is contained in the Capital Allowances Act 2001. That Act provides for allowances within separate codes, each covered by a separate part of the Act. BPRA would comprise a new code within a new Part 3A of the act. The scheme would cover expenditure on any “qualifying building” (the term is described below) and on plant and machinery that is or becomes an integral fixture of the building.

The new scheme

- 3.3 The draft legislation introduces the new Part 3A. In outline, Part 3A provides-

► **Who may qualify for the new allowances?** (Chapter 1 of Part 3A.)

The answer is: *A person with a “relevant interest” in a “qualifying building” who incurs “qualifying expenditure” in order to bring the premises back into*

productive use- that is, in order to create “qualifying business premises”.
These terms are then defined in the remaining Chapters of Part 3A.

► **What is “qualifying expenditure”?** (Chapter 2 of Part 3A)

The answer is: *Capital expenditure, incurred on or before a specified date in (say) 2011² on the conversion or renovation of a “qualifying building” into “qualifying business premises”. Chapter 2 also specifies certain types of expenditure that will not qualify, namely expenditure on: (i) the acquisition of land or rights over land; (ii) the extension of the building (except where required to provide access); (iii) the development of adjoining land or (iv) the provision of plant or machinery (except where these provide a fixture, as defined in section 173(1) of the Capital Allowances Act 2001). Also, expenditure on repairs that would normally be deductible in calculating the business’s profits for tax purposes, will not constitute “qualifying expenditure”, except to the extent that the repairs are incidental to the conversion or renovation work being undertaken under the new scheme.*

► **What is a “qualifying building”?** (Chapter 3, section 360C)

A “qualifying building” is a building which -

- Is situated in one of the designated, disadvantaged areas (see Annex A)
- has been unused for a year or longer

² The scheme is intended to run for an initial period of 5 years, but because its start date will depend on the date of state aid approval from the EC, the end date can only be provisionally estimated meantime.

- was last used for business purposes (and not as a dwelling)
- is a whole building or part of a building and
- if a part of a building, the other parts of the whole must either -
 - * (a) also have been unused for at least a year -

or, if the other part(s) has/have been in use within the previous year, then that or those other part(s) must

- * (b) not been occupied in common with the part in respect of which the new allowances are being claimed.

Parts of buildings: In broad terms, this last condition means that, if for example, half of a warehouse had not been used for a year, but the other half had been in use, renovation of the unused portion of the building would not qualify under the scheme. But if the part to be renovated was, for example: (i) a wing of a whole building, *all* of which had been unused for at least a year, or (ii) an empty unit in a shopping centre, where the other units had been *separately used and occupied by other businesses*, then renovation of that wing or that empty unit could still qualify.

There is **an exception** to cover the situation where the other part in common occupation is a **dwelling**, for example, a flat over a shop. In that case, if the shop part has lain empty for more than a year, but the former shopkeeper has continued to reside in the flat above it, renovation of the unused shop floor could qualify under the new scheme.

► **What are “qualifying business premises”?** (Chapter 3, section 360D)

“Qualifying business premises” is the term used to describe the effect or end result to be achieved by the qualifying expenditure. In other words, the conversion or renovation expenditure must result in the premises

actually being *brought back into productive use* or, where the premises have been renovated for leasing to a new tenant, the premises must be suitable, ready and held out for letting for business purposes.

► **What is the “relevant interest”?** (Chapter 4)

The “relevant interest” is defined as the interest in the qualifying building to which the person who incurred the qualifying expenditure was entitled when the expenditure was incurred. In broad terms this means that people and companies who incur capital costs on the renovation of qualifying buildings, in order to bring them back into productive use, can claim the allowances, whether they are the owners or tenants of the newly renovated premises. There are some further technical provisions in Chapter 4 to cover situations where the person has more than one interest in the property (section 360E) or where an interest is acquired on completion of a conversion (section 360F).

► **100% first-year allowances** (Chapter 5)

The scheme provides 100% up-front tax relief for the capital costs of the renovation or conversion work, for the chargeable period in which the qualifying expenditure is incurred.

Businesses claiming an initial allowance are also provided with the flexibility to claim less than 100%, if they prefer to do so (perhaps because they have made insufficient profits in a particular year to use the full amount). In that case, the balance of unrelieved expenditure may qualify for writing-down allowances (see below).

Initial allowances are not due and may be withdrawn if the premises are not “qualifying business premises” when they are ready to be brought back into use, or if they are sold by the claimant before they are brought back into productive use.

► **Writing-down allowances** (chapter 6)

The scheme provides writing-down allowances at 25% a year on any balance of unrelieved expenditure, provided that the person who incurred the expenditure still has the relevant interest in the premises and the premises are still “qualifying business premises” at the end of the chargeable period. Once again, claimants have the flexibility to claim less than the full amount if they prefer to do so.

► **Grants** (chapter 7)

No allowances are to be made under the new scheme to the extent that the expenditure has already been taken into account for the purposes of a relevant grant or relevant payment. A grant or payment is relevant if it is a notified State aid or if it is a subsidy which is declared to be relevant by Treasury Order.

► **Balancing adjustments** (Chapter 8)

The scheme provides for an adjustment to be made if certain events occur **within 7 years** of the premises being used or made available and suitable for letting for business use. These events and the proceeds to be brought into account are detailed in the Table at section 3600 of the draft legislation, and include, for example:-

<i>Balancing Event</i>	<i>Proceeds from the event</i>
Sale of the relevant interest	Net proceeds of sale
The grant of a long lease	The capital sum paid or commercial premium, if greater
Demolition or destruction of the	The net amount received for the

qualifying building	remains and any capital sums in respect of insurance or compensation for the event.
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If the proceeds from the event are **less** than the residue of qualifying expenditure, then a balancing allowance in respect of that difference is due. If the proceeds are **more**, then a balancing charge in respect of that difference is made, but the charge must not exceed any initial allowance or writing-down allowances made before the event occurred.

► **Additional VAT liabilities and rebates** (Chapter 10)

In broad terms, Chapter 10 provides how additional VAT liabilities and rebates (as defined in section 547 of the Capital Allowances Act 2001) should be taken into account for the purposes of initial allowances, writing-down allowances and balancing adjustments, in respect of qualifying expenditure under the new scheme.

► **Supplementary provisions & Consequential** (Chapter 11)

Chapter 11 contains supplementary provisions and consequential amendments required to the Capital Allowances Act 2001 because of the new scheme.

The supplementary provisions include:

- A section (360Z) on how to give effect to the new BPRA allowances or charges. Broadly: (a) the allowances are treated as a charge of the trade, profession or vocation and (b) the balancing charge is treated as a receipt of the trade, profession or vocation, as the case may be.

- A section (360Z1) requiring apportionment of sale proceeds, where these include consideration for assets, the expenditure on which did not constitute “qualifying expenditure” in terms of the new scheme.
- Sections (360Z2 & 360Z3) which apply on the termination of a lease and which define a lease, respectively.

CHAPTER 4: THE DRAFT LEGISLATION

4.1 The draft clause introduces the draft schedule, which inserts a new Part 3A into the Capital Allowances Act 2001. Both drafts are reproduced below. Comments are invited on the technical accuracy and detail of what is proposed.

Draft Clause

Capital allowances: renovation of business premises in disadvantaged areas

Schedule 1³ (capital allowances in respect of expenditure on the conversion or renovation of qualifying business premises in disadvantaged areas) has effect in relation to expenditure incurred on or after such day as the Treasury may by order appoint.

Draft Schedule 1

The draft Schedule, containing the detail of the proposed scheme, is reproduced in full in the following pages.

³ The numbering of the Schedule as “Schedule 1” is provisional and does not imply that the Schedule will be the first schedule of the Finance Bill, when this is eventually published. Numbering will be subject to change as the Bill is drafted, published and taken through the Parliamentary process.

SCHEDULES

SCHEDULE 1

Section 1

CAPITAL ALLOWANCES: RENOVATION OF BUSINESS PREMISES IN DISADVANTAGED AREAS

PART 1

NEW PART 3A OF THE CAPITAL ALLOWANCES ACT 2001 5

1 After Part 3 of the Capital Allowances Act 2001 (c. 2) insert—

PART 3A

BUSINESS PREMISES RENOVATION ALLOWANCES

CHAPTER 1

INTRODUCTION 10

360A Business premises renovation allowances

- (1) Allowances are available under this Part if a person incurs qualifying expenditure in respect of a qualifying building.
 - (2) Allowances under this Part are made to the person who—
 - (a) incurred the expenditure, and
 - (b) has the relevant interest in the qualifying building.
- 15

CHAPTER 2

QUALIFYING EXPENDITURE

360B Meaning of “qualifying expenditure”

- (1) In this Part “qualifying expenditure” means capital expenditure incurred on or before [31st March 2011] on, or in connection with—
 - (a) the conversion of a qualifying building into qualifying business premises,
 - (b) the renovation of a qualifying building if it is or will be qualifying business premises, or
 - (c) repairs to a qualifying building or, where the qualifying building is part of a building, to the building of which the qualifying building forms part, to the extent that the repairs are incidental to expenditure within paragraph (a) or (b).
 - (2) Expenditure is not qualifying expenditure if it is incurred on or in connection with—
- 20
- 25
- 30

- (a) the acquisition of land or rights in or over land,
 - (b) the extension of a qualifying building (except to the extent required for the purpose of providing a means of getting to or from qualifying business premises),
 - (c) the development of land adjoining or adjacent to a qualifying building, or 5
 - (d) the provision of plant and machinery, other than plant or machinery which is or becomes a fixture as defined by section 173(1).
- (3) For the purposes of this section, expenditure incurred on repairs to a building is to be treated as capital expenditure if it is not expenditure that would be allowed to be deducted in calculating the profits of a [Schedule A business] [property business], or of a trade, profession or vocation, for tax purposes. 10
- (4) Treasury regulations may make further provision as to expenditure which is, or is not, qualifying expenditure. 15

CHAPTER 3

QUALIFYING BUILDINGS AND QUALIFYING BUSINESS PREMISES

360C Meaning of “qualifying building”

- (1) In this Part “qualifying building”, in relation to any conversion or renovation work, means any building or structure, or part of a building or structure, which—
- (a) is situated in a disadvantaged area,
 - (b) was unused throughout the period of one year ending immediately before the date on which the conversion or renovation work began, 25
 - (c) on that date, had last been used—
 - (i) for the purposes of a trade, profession or vocation, or
 - (ii) as an office or offices (whether or not for the purposes of a trade, profession or vocation), 30
 - (d) on that date, had not last been used as, or as part of, a dwelling, and
 - (e) in the case of part of a building or structure, on that date had not last been occupied and used in common with any other part of the building or structure other than a part— 35
 - (i) as respects which the condition in paragraph (b) is met, or
 - (ii) which had last been used as a dwelling.
- (2) In this section “disadvantaged area” means—
- (a) an area designated as a disadvantaged area for the purposes of this section by Treasury regulations, or 40
 - (b) if no regulations are made under paragraph (a), an area for the time being designated as a disadvantaged area for the purposes of Schedule 6 to the Finance Act 2003 (stamp duty land tax: disadvantaged areas relief). 45
- (3) Regulations under subsection (2)(a) may—
- (a) designate specified areas as disadvantaged areas, or

- (b) provide for areas of a description specified in the regulations to be designated as disadvantaged areas.
- (4) If regulations under subsection (2)(a) so provide, the designation of an area as a disadvantaged area shall have effect for such period as may be specified in or determined in accordance with the regulations. 5
- (5) Regulations under subsection (2)(a) may –
 - (a) make different provision for different cases, and
 - (b) contain such incidental, supplementary, consequential or transitional provision as appears to the Treasury to be necessary or expedient. 10
- (6) Where a building or structure (or part of a building or structure) which would otherwise be a qualifying building is situated partly in a disadvantaged area and partly outside it, only so much of the expenditure incurred in accordance with section 360B as, on a just and reasonable apportionment, is attributable to the part of the building or structure located in the disadvantaged area shall be treated as qualifying expenditure. 15
- (7) Treasury regulations may make further provision as to the circumstances in which a building or structure or part of a building or structure is, or is not, a qualifying building. 20

360D Meaning of “qualifying business premises”

- (1) In this Part “qualifying business premises” means any premises in respect of which the following requirements are met –
 - (a) the premises must be a qualifying building, 25
 - (b) the premises must be used, or available and suitable for letting for use, –
 - (i) for the purposes of a trade, profession or vocation, or
 - (ii) as an office or offices (whether or not for the purposes of a trade, profession or vocation), 30
 - (c) the premises must not be used, or available for use as, or as part of, a dwelling.
- (2) In this section “premises” means any building or structure or part of a building or structure.
- (3) For the purposes of this Part, if premises are qualifying business premises immediately before a period when they are temporarily unsuitable for use for the purposes mentioned in subsection (1)(b), they are to be treated as being qualifying business premises during that period. 35
- (4) Treasury regulations may make further provision as to the circumstances in which premises are, or are not, qualifying business premises. 40

CHAPTER 4

THE RELEVANT INTEREST IN THE QUALIFYING BUILDING

360E General rule as to what is the relevant interest

- (1) The relevant interest in a qualifying building in relation to any qualifying expenditure is the interest in the qualifying building to which the person who incurred the qualifying expenditure was entitled when it was incurred. 5
- (2) Subsection (1) is subject to the following provisions of this Chapter and to section 360Z2 (provisions applying on termination of lease).
- (3) If— 10
 - (a) the person who incurred the qualifying expenditure was entitled to more than one interest in the qualifying building when the expenditure was incurred, and
 - (b) one of those interests was reversionary on all the others, the reversionary interest is the relevant interest in the qualifying building. 15
- (4) An interest does not cease to be the relevant interest merely because of the creation of a lease or other interest to which that interest is subject.
- (5) If— 20
 - (a) the relevant interest is a leasehold interest, and
 - (b) that interest is extinguished on the person entitled to it acquiring the interest which is reversionary on it, the interest into which the leasehold interest merges becomes the relevant interest when the leasehold interest is extinguished. 25

360F Interest acquired on completion of conversion

For the purposes of determining the relevant interest in a qualifying building, a person who—

- (a) incurs expenditure on the conversion of a qualifying building into qualifying business premises, and 30
- (b) is entitled to an interest in the qualifying building on or as a result of the completion of the conversion, is treated as having had that interest when the expenditure was incurred.

CHAPTER 5

35

INITIAL ALLOWANCES

360G Initial allowances

- (1) A person who has incurred qualifying expenditure in respect of any qualifying building is entitled to an initial allowance in respect of the expenditure. 40
- (2) The amount of the initial allowance is 100% of the qualifying expenditure.

(3)	A person claiming an initial allowance under this section may require the allowance to be reduced to a specified amount.	
(4)	The initial allowance is made for the chargeable period in which the qualifying expenditure is incurred.	
360H	Premises not qualifying business premises or relevant interest sold before premises first used or let	5
(1)	No initial allowance is to be made under section 360G if, at the relevant time, the qualifying building does not constitute qualifying business premises.	
(2)	An initial allowance which has been made in respect of a qualifying building which is to be qualifying business premises is to be withdrawn if –	10
	(a) the qualifying building does not constitute qualifying business premises at the relevant time, or	
	(b) the person to whom the allowance was made has sold the relevant interest in the qualifying building before the relevant time.	15
(3)	All such assessments and adjustments of assessments are to be made as are necessary to give effect to this section.	
(4)	In this section “the relevant time” means the time when the premises are first used by the person with the relevant interest or, if they are not so used, the time when they are first suitable for letting for either of the purposes mentioned in section 360D(1)(b).	20

CHAPTER 6

	WRITING-DOWN ALLOWANCES	25
360I	Entitlement to writing-down allowances	
(1)	A person is entitled to a writing-down allowance for a chargeable period if he has incurred qualifying expenditure in respect of a qualifying building and, at the end of the chargeable period –	
	(a) the person is entitled to the relevant interest in the qualifying building	30
	(b) the person has not granted a long lease of the qualifying building out of the relevant interest in consideration of the payment of a capital sum, and	
	(c) the qualifying building constitutes qualifying business premises.	35
(2)	In subsection (1)(b) “long lease” means a lease the duration of which exceeds 50 years.	
(3)	Whether the duration of a lease exceeds 50 years is to be determined –	40
	(a) in accordance with [section 38(1) to (4) and (6) of ICTA] [section 299 of the Income Tax (Trading and Other Income) Act 2005], and	

(b)	without regard to subsection 360Z2(3) (new lease granted as a result of the exercise of an option treated as continuation of old lease).	
(4)	A person claiming a writing-down allowance may require the allowance to be reduced to a specified amount.	5
360J Amount of allowance		
(1)	The writing-down allowance for a chargeable period is 25% of the qualifying expenditure.	
(2)	The allowance is proportionately increased or reduced if the chargeable period is more or less than a year.	10
(3)	The amount of the writing-down allowance for a chargeable period is limited to the residue of qualifying expenditure.	
(4)	For this purpose the residue is ascertained immediately before writing off the writing-down allowance at the end of the chargeable period.	15
360K Meaning of “the residue of qualifying expenditure”		
	The residue of qualifying expenditure is the qualifying expenditure that has not yet been written off in accordance with Chapter 9.	
CHAPTER 7		
	GRANTS IN RESPECT OF QUALIFYING EXPENDITURE	20
360L Grants affecting entitlement to allowances		
(1)	No initial allowance or writing-down allowance under this Part is to be made in respect of expenditure to the extent that it is taken into account for the purposes of a relevant grant or relevant payment made towards that expenditure.	25
(2)	A grant or payment is relevant if it is –	
(a)	a notified State aid other than an allowance under this Part, or	
(b)	a grant or subsidy, other than a notified State aid, which the Treasury by order declares to be relevant for the purposes of the withholding of initial allowances or writing-down allowances.	30
(3)	For the purposes of subsection (2), “notified State aid” means a State aid notified to and approved by the European Commission.	
(4)	If a relevant grant or relevant payment towards the expenditure is made after the making of an initial allowance or a writing-down allowance, the allowance is to be withdrawn to that extent.	35
(5)	If the amount of the relevant grant or relevant payment is repaid by the grantee to the grantor, in whole or in part, the grant or payment is treated, to that extent, as never having been made.	
(6)	All such assessments and adjustments of assessments are to be made as are necessary to give effect to subsection (4) or (5).	40

- (7) Any such assessment or adjustment is not out of time if it is made within 3 years of the end of the chargeable period in which the grant, payment or adjustment was made.

CHAPTER 8

BALANCING ADJUSTMENTS

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360M When balancing adjustments are made

- (1) A balancing adjustment is made if—
- (a) qualifying expenditure has been incurred in respect of a qualifying building, and
 - (b) a balancing event occurs. 10
- (2) A balancing adjustment is either a balancing allowance or a balancing charge and is made for the chargeable period in which the balancing event occurs.
- (3) A balancing allowance or balancing charge is made to or on the person who incurred the qualifying expenditure. 15
- (4) No balancing adjustment is made if the balancing event occurs more than 7 years after the time when the premises were first used, or suitable for letting, for either of the purposes mentioned in section 360D(1)(b).
- (5) If more than one balancing event within section 360N occurs, a balancing adjustment is made only on the first of them. 20

360N Balancing events

- (1) The following are balancing events for the purposes of this Part—
- (a) the relevant interest in the qualifying building is sold;
 - (b) a long lease of the qualifying building is granted out of the relevant interest in consideration of the payment of a capital sum; 25
 - (c) if the relevant interest is a lease, the lease ends otherwise than on the person entitled to it acquiring the interest reversionary on it; 30
 - (d) the person who incurred the qualifying expenditure dies;
 - (e) the qualifying building is demolished or destroyed;
 - (f) the qualifying building ceases to be qualifying business premises (without being demolished or destroyed).
- (2) Section 360I (2) and (3) (meaning of “long lease”) apply for the purposes of subsection (1)(b). 35

360O Proceeds from balancing events

- (1) References in this Part to the proceeds from a balancing event are to the amounts received or receivable in connection with the event, as shown in the Table— 40

TABLE: BALANCING EVENTS AND PROCEEDS

<i>1 Balancing Event</i>	<i>2 Proceeds from event</i>	
1 The sale of the relevant interest	The net proceeds of the sale	
2 The grant of a long lease out of the relevant interest	If the capital sum paid in consideration of the grant is less than the commercial premium, the commercial premium In any other case, the capital sum paid in consideration of the grant	5
3 The coming to an end of a lease, where a person entitled to the lease and a person entitled to any superior interest are connected persons	The market value of the relevant interest in the qualifying building at the time of the event.	10
4 The death of the person who incurred the qualifying expenditure	The residue of qualifying expenditure immediately before the death.	15
5 The demolition or destruction of the qualifying building	The net amount received for the remains of the qualifying building, together with – (a) any insurance money received in respect of the demolition or destruction, and (b) any other compensation of any description so received, so far as it consists of capital sums.	20 25
6 The qualifying building ceases to be qualifying business premises	The market value of the relevant interest in the qualifying building at the time of the event.	30

(2) The amounts referred to in column 2 of the Table are those received or receivable by the person who incurred the qualifying expenditure.

(3) In Item 2 of the Table “the commercial premium” means the premium that would have been given if the transaction had been at arm’s length. 35

360P Calculation of balancing adjustments

(1) A balancing allowance is made if –
 (a) there are no proceeds from the balancing event, or
 (b) the proceeds from the balancing event are less than the residue of qualifying expenditure immediately before the event. 40

(2) The amount of the balancing allowance is the amount of –

- (a) the residue (if there are no proceeds);
 - (b) the difference (if the proceeds are less than the residue).
- (3) A balancing charge is made if the proceeds from the balancing event are more than the residue, if any, of qualifying expenditure immediately before the event. 5
- (4) The amount of the balancing charge is the amount of –
- (a) the difference, or
 - (b) the proceeds (if the residue is nil).
- (5) The amount of a balancing charge made on a person must not exceed the total amount of – 10
- (a) any initial allowances made to the person in respect of the expenditure, and
 - (b) any writing-down allowances made to the person in respect of the expenditure for chargeable periods ending on or before the date of the balancing event giving rise to the balancing adjustment. 15

CHAPTER 9

WRITING OFF QUALIFYING EXPENDITURE

360Q Introduction

For the purposes of this Part qualifying expenditure is written off to the extent and at the times specified in this Chapter. 20

360R Writing off initial allowances and writing-down allowances

- (1) If an initial allowance is made in respect of the qualifying expenditure, the amount of the allowance is written off at the time when the qualifying business premises are first used, or suitable for letting for use, for either of the purposes mentioned in section 360D(1)(b). 25
- (2) If a writing-down allowance is made in respect of the qualifying expenditure, the amount of the allowance is written off at the end of the chargeable period for which the allowance is made. 30
- (3) If a balancing event occurs at the end of the chargeable period referred to in subsection (2), the amount written off under that subsection is to be taken into account in calculating the residue of qualifying expenditure immediately before the event to determine what balancing adjustment (if any) is to be made. 35

360S Treatment of demolition costs

- (1) This section applies if –
- (a) a qualifying building is demolished, and
 - (b) the person who incurred the qualifying expenditure incurs the cost of the demolition. 40
- (2) The net cost of the demolition is added to the residue of qualifying expenditure immediately before the demolition.

- (3) “The net cost of the demolition” means the amount, if any, by which the cost of the demolition exceeds any money received for the remains of the qualifying building.
- (4) If this section applies, neither the cost of the demolition nor the net cost of the demolition is treated for the purposes of any Part of this Act as expenditure on any other property replacing the qualifying building demolished. 5

CHAPTER 10

ADDITIONAL VAT LIABILITIES AND REBATES

360T Introduction 10

For the purposes of this Chapter –

- (a) “additional VAT liability” and “additional VAT rebate” have the meanings given by section 547,
- (b) the time when –
 - (i) a person incurs an additional VAT liability, or 15
 - (ii) an additional VAT rebate is made to a person, is given by section 548, and
- (c) the chargeable period in which, and the time when, an additional VAT liability or an additional VAT rebate accrues are given by section 549. 20

360U Additional VAT liabilities and initial allowances

- (1) This section applies if –
 - (a) a person was entitled to an initial allowance under this Part in respect of qualifying expenditure on a qualifying building,
 - (b) that person incurs an additional VAT liability in respect of that expenditure, and 25
 - (c) the additional VAT liability is incurred at a time when the qualifying building is, or is about to be, qualifying business premises.
- (2) If this section applies, the person entitled to the relevant interest is entitled to an initial allowance on the amount of the additional VAT liability. 30
- (3) The amount of the initial allowance is 100% of the amount of the additional VAT liability.
- (4) A person claiming an initial allowance under this section may require the allowance to be reduced to a specified amount. 35
- (5) The allowance is made for the chargeable period in which the additional VAT liability accrues.

360V Additional VAT liabilities and writing-down allowances

- (1) This section applies if the person entitled to the relevant interest in relation to qualifying expenditure incurs an additional VAT liability in respect of that expenditure. 40
- (2) If this section applies –

(a)	the additional VAT liability is treated as qualifying expenditure, and	
(b)	the amount of the residue of qualifying expenditure is accordingly increased at the time when the liability accrues by the amount of the liability.	5
360W Additional VAT liabilities and writing off initial allowances		
	If an initial allowance is made in respect of an additional VAT liability incurred after the qualifying business premises are first used or suitable for letting for business use, the amount of the allowance is written off at the time when the liability accrues.	10
360X Additional VAT rebates and balancing adjustments		
(1)	If an additional VAT rebate is made in respect of qualifying expenditure to the person entitled to the relevant interest in relation to that qualifying expenditure –	
(a)	the making of the rebate is a balancing event for the purposes of this Part, but	15
(b)	the making of balancing adjustments as a result of the event is subject to subsections (2) and (3).	
(2)	No balancing allowance is to be made as a result of the event.	
(3)	A balancing charge is not to be made as a result of the event unless –	20
(a)	the amount of the additional VAT rebate is more than the amount of the residue of qualifying expenditure immediately before the time when the rebate accrues, or	
(b)	there is no such residue.	
(4)	The amount of the balancing charge is –	25
(a)	the amount of the difference, or	
(b)	the amount of the rebate (if there is no residue).	
360Y Additional VAT rebates and writing off qualifying expenditure		
	If an additional VAT rebate is made in respect of qualifying expenditure, an amount equal to the rebate is written off at the time when the rebate accrues.	30

CHAPTER 11

SUPPLEMENTARY PROVISIONS

360Z Giving effect to allowances and charges		
(1)	This section applies if a person is entitled or liable under this Part to an allowance or charge for a chargeable period.	35
(2)	If the person's interest in the qualifying building is an asset of a [Schedule A business] [property business] carried on by him at any time in that period, the allowance or charge is to be given effect in calculating the profits of that business for that period, by treating –	40
(a)	the allowance as an expense of that business, and	
(b)	the charge as a receipt of that business.	

- (3) If the person’s interest in the qualifying building is not an asset of a [Schedule A business] [property business] carried on by him at any time in that period, the allowance or charge is to be given effect by treating him as if he had been carrying on a [Schedule A business] [property business] in that period and as if— 5
- (a) the allowance were an expense of that business, and
 - (b) the charge were a receipt of that business.

360Z1 Apportionment of sums partly referable to non-qualifying assets

- (1) If the sum paid for the sale of the relevant interest in a qualifying building is attributable— 10
- (a) partly to assets representing expenditure for which an allowance can be made under this Part, and
 - (b) partly to assets representing other expenditure,
- only so much of the sum as on a just and reasonable apportionment is attributable to the assets referred to in paragraph (a) is to be taken into account for the purposes of this Part. 15
- (2) Subsection (1) applies to other proceeds from a balancing event in respect of a qualifying building as it applies to a sum given for the sale of the relevant interest in the qualifying building.
- (3) Subsection (1) does not affect any other provision of this Act requiring an apportionment of the proceeds of a balancing event. 20

360Z2 Provisions applying on termination of lease

- (1) This section applies for the purposes of this Part if a lease is terminated.
- (2) If, with the consent of the lessor, the lessee of the qualifying building remains in possession of the qualifying building after the termination without a new lease being granted to him, the lease is treated as continuing so long as the lessee remains in possession. 25
- (3) If on the termination a new lease is granted to a lessee as a result of the exercise of an option available to him under the terms of the first lease, the second lease is treated as a continuation of the first. 30
- (4) If on the termination the lessor pays a sum to the lessee in respect of business premises comprised in the lease, the lease is treated as if it had come to an end by surrender in consideration of the payment.
- (5) If on the termination— 35
- (a) another lease is granted to a different lessee, and
 - (b) in connection with the transaction that lessee pays a sum to the person who was the lessee under the first lease,
- the two leases are to be treated as if they were the same lease which had been assigned by the lessee under the first lease to the lessee under the second lease in consideration of the payment. 40

360Z3 Meaning of “lease” etc.

- (1) In this Part “lease” includes—
- (a) an agreement for a lease if the term to be covered by the lease has begun, and 45

- (b) any tenancy,
but does not include a mortgage (and “lessee”, “lessor” and
“leasehold interest” are to be read accordingly).
- (2) In the application of this Part to Scotland –
- (a) “leasehold interest” or “leasehold estate” means the interest 5
of a tenant in property subject to a lease, and
- (b) any reference to an interest which is reversionary on a
leasehold interest or on a lease is to be read as a reference to
the interest of the landlord in the property subject to the
leasehold interest or lease.” 10

PART 2

CONSEQUENTIAL AMENDMENTS

- 2 In section 1(2) of the Capital Allowances Act 2001 (capital allowances
provided for by Act), after paragraph (b) insert –
“(ba) Part 3A (business premises renovation allowances)” 15
- 3 In section 2(3) of that Act (provisions about giving effect to allowances and
charges), after the entry in the list for sections 352 to 355 of that Act insert –
“section 360Z (business premises renovation allowances)”.
- 4 In subsection 537(1) of that Act (general conditions for making contribution
allowances under Parts 2 to 4 and 5), and in the section heading and the
cross-heading preceding that section, for “Parts 2 to 4 and 5” substitute
“Parts 2, 3, 4 and 5”. 20
- 5 In section 546 of that Act (interpretation of VAT provisions), before the
“and” at the end of paragraph (b) insert –
“(ba) Chapter 10 of Part 3A (business premises renovation 25
allowances: additional VAT liabilities and rebates)”.
- 6 In section 570(1) of that Act (Parts of Act for purposes of which provisions
about sales not at market value apply), before “4” insert “3A,”.
- 7 In section 570A(1) of that Act (avoidance affecting proceeds of balancing
event), after “Part 3” insert “3A”. 30
- 8 In section 573(1) of that Act (transfers treated as sales), after “3,” insert “3A,”.
- 9 (1) Part 2 of Schedule 1 to that Act (list of defined expressions) is amended as
follows.
- (2) Insert the following entries in the appropriate places –
- “balancing adjustment (in Part 3A) section 360M” 35
- “balancing event (in Part 3A) section 360N”
- “lease and related expressions (in section 360Z3”
Part 3A)
- “proceeds from a balancing event section 360O”
(in Part 3A) 40

“qualifying building (in Part 3A)	section 360C”	
“qualifying business premises (in Part 3A)	section 360D”	
“qualifying expenditure (in Part 3A)	section 360B”	5
“relevant interest (in Part 3A)	Chapter 4 of Part 3A”	
“residue of qualifying expenditure (in Part 3A)	section 360K”	
(3) In the entry for “sale, transfers under Parts 3, 4, 4A and 10 treated as”, after “3” insert “,3A”.		10

CHAPTER 5: SUMMARY OF RESPONSES SOUGHT

Q1. (a) Is a minimum of 12 months the most appropriate void period (Chapter 2.2)?

(b) If not, what period would you suggest?

Q2. (a) Are we correct in assuming that the scheme will not create a perverse incentive to leave premises vacant (Chapter 2.3 to 2.6)?

(b) We would welcome reasoned views, evidence or examples to either support or contradict our assumption that this undesired effect would be unlikely.

Q3. (a) Should BPRA be available to all businesses (Chapter 2.7 to 2.9)?

(b) We would welcome views and data that either support or contradict our assumption that BPRA is likely to benefit SMEs both directly and indirectly.

(c) We would also welcome any data on the proportion of SMEs that (i) own or (ii) lease their premises, and, in particular, the probability of SMEs either owning or leasing premises in disadvantaged areas.

Q4. Comments are invited on the technical detail of the draft legislation outlined at Chapter 3 and reproduced in full in Chapter 4.

Q5. Responses are invited on the merits or otherwise of introducing a targeted scheme, such as BPRA to regenerate deprived areas, rather than a UK-wide measure, no measure at all or some other, alternative scheme (Annex C.17).

Q6. Any views or data on the annual number of buildings that are likely to be renovated under the scheme, and the probable extent of the benefits to businesses - especially SMEs – would be welcome (Annex C.23).

Q7. Views and data on the possible wider effects of BPRA on, for example, job creation and the environment in disadvantaged areas are also requested (Annex C.27).

Q8. Responses are specifically invited to either confirm or qualify our belief that the business compliance costs of BPRA are likely to be negligible (Annex C.29).

CHAPTER 6: THE CODE OF PRACTICE ON WRITTEN CONSULTATIONS

About the consultation process – the consultation criteria:

- 6.1 Timing of consultation should be built into the planning process for a policy (including legislation) or service from the start, so that it has the best prospect of improving the proposals concerned, and so that sufficient time is left for it at each stage.
- 6.2 It should be clear who is being consulted, about what questions, in what timescale and for what purpose.
- 6.3 A consultation document should be as simple and concise as possible. It should include a summary, in two pages at most, of the main questions it seeks views on. It should make it as easy as possible for readers to respond, make contact or complain.
- 6.4 Documents should be made widely available, with the fullest use of electronic means (though not to the exclusion of others), and effectively drawn to the attention of all interested groups and individuals.
- 6.5 Sufficient time should be allowed for considered responses from all groups with an interest. Twelve weeks should be the standard minimum period for a consultation.
- 6.6 Responses should be carefully and open-mindedly analysed, and the results made widely available, with an account of the views expressed, and the reasons for decisions finally taken.
- 6.7 Departments should monitor and evaluate consultations, designating a consultation co-ordinator who will ensure the lessons are disseminated.

The Inland Revenue confirms that, where possible, these consultation criteria have been, and will continue to be, followed.

COMPLAINTS

If you have any complaints about any element of the consultation process leading from the issue of this document, please contact:

	Steve Webster
	Inland Revenue
<i>Up until 15 December 2004 at</i>	New Wing
	Somerset House
	Strand
	LONDON WC2R 1LB
	Tel: 020 7438 6535
	Fax: 020 7438 9191
<i>And from 16 December 2004 at</i>	Room 3/37
	3 rd Floor
	1 Parliament Street
	London SW1A 2BQ
	Tel: 020 7147 2382

E-mail: Steve.Webster@ir.gsi.gov.uk

THE ENTERPRISE AREAS

- A.1 “Our comprehensive solution to...poverty and unemployment has to involve raising levels of economic activity – more businesses rather than more benefit offices” - The Chancellor of the Exchequer, November 2002.
- A.2 The Enterprise Areas, announced in the 2002 Pre-Budget Report, reflect the Government’s broadly based approach to tackling disadvantage by tackling the barriers to enterprise, economic activity and opportunity for all, drawing together the range of policy tools available to tackle the problems that disadvantaged communities face.
- A.3 The current Enterprise Areas are the 1,997 most deprived areas of the UK. In England, Wales and Northern Ireland the areas are defined at ward level, using indices of deprivation. In Scotland, the areas are defined using postcode sectors. The indices are based on measures of key deprivation such as income, unemployment, health and poverty.
- A.4 In England and Scotland the areas selected are the most deprived 15% of wards/areas, in Wales and Northern Ireland they are the most deprived 42% of wards to reflect higher levels of deprivation in these countries¹.

¹ The Enterprise Areas were selected using the Index of Multiple Deprivation 2000 (England); the Welsh index of Multiple Deprivation 2000; the Scottish Area Deprivation Index 1998; and Northern Ireland Measures of Deprivation 2001.

A.5 Lists of the areas are available from the Inland Revenue's stamp duty website, at www.inlandrevenue.gov.uk/so/disadvantaged.htm. The website also includes a postcode search tool, at www.inlandrevenue.gov.uk/so/pcode_search.htm, which allows you to find out whether a postcode is within an Enterprise Area. Postcode information is readily available for any given postal address from the Postcode Enquiry Line on 08457 111 222 or via the internet at www.royalmail.co.uk/quick_tools/postcodes/ Please note that if you are not reading this document on our website, clicking on this link will take you to the Royal Mail homepage, where you can link to the postcode finder page. If you enter the above URL in an internet browser yourself, please note that there is an underscore “_” between the words “quick” and “tools” which must be shown or the URL will not work.

A.6 Currently there are several measures to tackle the market failures and barriers to enterprise that can be most severe in Enterprise Areas. This “toolkit” includes:

- Stamp duty relief on property transactions to stimulate local property markets
- Community Investment Tax Relief to improve access to finance for small businesses through Community Development Finance Institutions
- Bridges Community Development Venture Fund; a £40m fund from Government and the private sector to provide venture capital funding.
- A wide range of innovative projects, through the Phoenix Development Fund, developing new approaches to providing business support for under pressure groups such as women and ethnic minorities.

- Enhanced and targeted advice and support from HM Revenue and Customs.

A.7 The Government is aware that England and Scotland have updated their respective Indices of Deprivation. In England, the new indices are based on a smaller, “Super Output Area” (SOA) level measure, and in Scotland the move is from a postcode basis to a data zone basis. These zones are similar to SOAs, but they target smaller populations of between 500 and 1,000 residents. The national reviews of the Indices also involve modifications to the measures of deprivation.

A.8 The Government appreciates that these reviews could make the current Enterprise Area boundaries seem somewhat dated. However, there are currently no plans to change the list of qualifying areas prior to December 2006. In its full form, the SDLT (formerly stamp duty) disadvantaged area relief (mentioned at A.6) has only been available since April 2003. People are becoming familiar with the areas that currently qualify for relief and any sudden change in indicia could increase uncertainty for people engaged in large scale projects. Further, the terms of the EC state aid approval require evaluation of the relief to December 2006 and early changes to the qualifying areas would complicate this.

A.9 The proposed BPRA scheme would comprise a further measure in the Government’s Enterprise Area “toolkit”. As such, it would be part of the Government’s holistic approach to tackling deprivation.

CAPITAL ALLOWANCES

B.1 In broad terms, capital allowances allow the cost of capital assets to be written-off against a business's taxable profits. They take the place of depreciation, deducted in a firm's commercial accounts, which is not deductible for tax purposes. Different classes of assets qualify for allowances at different rates. Two of the main rates are currently:-

- 25% a year on the “reducing balance basis”, for most plant and machinery expenditure (with a 40% first-year capital allowance (“FYA”) for small and medium-sized enterprises² investment in plant and machinery);
- 4% a year, on the “straight-line” basis, for industrial buildings, agricultural buildings and certain hotels.

B.2 In addition, **enhanced rates of allowance** are provided to support investment in certain areas. For example, 100% FYAs for business expenditure on "Green Technologies", that is, for spending on designated,

²Broadly, the Companies Act 1985 defines a company as “small” if it meets two or more of the following requirements: its turnover, balance sheet total and number of employees do not exceed £5.6 million, £2.8 million and 50 respectively. And the Act defines a company as “medium” if two or more of its turnover, balance sheet total and number of employees do not exceed £22.8million, £11.4 million and 250 respectively. These limits apply to accounting periods ending after 30 January 2004.

energy-saving plant and machinery (section 45A of the Capital Allowances Act 2001).

- B.3 As mentioned earlier, the proposed new Business Premises Renovation Allowance (BPRA) scheme would provide 100% FYAs for capital expenditure on renovating vacant business properties in designated disadvantaged areas. So the relief would potentially be available for:
- (a) Expenditure that already qualifies for allowances under the plant and machinery regime (at 25% a year or 40% FYAs in the case of expenditure by SMEs) or under the industrial etc building regime (at 4% a year) and
 - (b) Expenditure that does not currently qualify for any relief, for example, expenditure on alterations to the fabric of non-industrial, commercial buildings, such as shops and offices.
- B.4 Thus, in the case of expenditure falling under head (a) above, BPRA would provide an enhanced or accelerated rate of relief and in the case of expenditure falling under head (b) above, BPRA would constitute a new tax relief.

PARTIAL REGULATORY IMPACT ASSESSMENT (RIA)

Consultation on the proposed Business Premises Renovation Allowance (BPRA) scheme

Purpose and intended effect of the measure

The policy objectives

C.1 To increase private investment, enterprise and employment in the UK's most disadvantaged communities (designated as "Enterprise Areas"), by bringing longer-term vacant business properties, in those areas, back into productive use. The measure is part of the UK's holistic approach to regeneration. Regeneration has wider social and environmental objectives as well as economic goals. The BPRA scheme aims to contribute to those objectives and goals through the mechanism of new and enhanced capital allowances, designed to encourage and support investment in business property renovation.

Background and introduction

C.2 A key feature of the Government's policy for enterprise is the recognition that social factors, the business environment and specific market failures can present barriers to enterprise within disadvantaged areas. In the 2002 Pre-Budget Report, the Chancellor of the Exchequer, Gordon Brown, announced the designation of approximately 2,000 Enterprise Areas, on which measures would be targeted to address the barriers to enterprise and regeneration affecting the most disadvantaged communities in the United Kingdom.

- C.3 The Government has already introduced complementary measures that can contribute towards encouraging investment in property in deprived areas, including stamp duty relief, the Property Support Scheme and the Land Remediation scheme.
- C.4 Generally speaking, spending on *repairs* to business premises can qualify for tax relief as a *revenue* deduction in the business's profit and loss account.
- C.5 **Capital expenditure** (on substantial alterations or improvements to premises, or by a new owner, to bring premises into business use) can already qualify for some capital allowances under the existing rules (see Annex B). The relevant capital allowances are –
- At **25% a year** (on the “reducing balance basis”) for expenditure on plant and machinery (P&M) that is, or becomes, an integral fixture of the building. If the business is a SME, then it will also be entitled to a **40%** initial or first year allowance in respect of such P&M expenditure.
 - At **4%** a year (on the “straight-line” basis) for expenditure on the fabric of industrial buildings (including certain qualifying hotels) and agricultural buildings.

However, expenditure on the fabric of commercial buildings (such as offices and shops) does not generally qualify for any capital allowances.

- C.6 So the proposed new scheme, which would provide **100%** first-year capital allowances for the capital costs of renovating or converting premises that have been unused for a year or more in Enterprise Areas, would potentially comprise partly an **enhanced** rate of allowances and partly a **new relief**.

The risk(s) being addressed

- C.7 Boarded-up rows of derelict shops and empty business properties are a common sight in the most deprived areas of the UK. The Government has identified that further barriers to regeneration in these areas are caused by the presence of such properties. Available data³ shows: (i) that there is a significantly greater proportion of long-term empty properties in the 2,000 Enterprise Areas than in other areas of the UK and (ii) that market prices can hit a floor below which the costs of maintaining/refurbishing the premises would be higher than the expected yield the owner could expect to obtain as a result of incurring such costs. This is the so-called “negative rent” effect, which acts as a barrier to regeneration.
- C.8 There are also wider social benefits to regeneration that are not always captured in the returns to the private investor. So empty properties in deprived areas can be left empty and run-down even when the economically efficient solution would be redevelopment. This adds to “visual blight” and increased crime and vandalism.
- C.9 The presence of such properties can also act as a drag on the whole neighbourhood. This is sometimes referred to as the “broken window” effect, which can deter new people and businesses from locating in these disadvantaged areas⁴.
- C.10 Over time, the degree of dereliction can increase, until such time as the costs of renovation could outweigh any private returns. At this point the

³ Supplied to the Inland Revenue in the first half of 2004 by Investment Property Databank (IPD) Ltd.

⁴ The fact that the quality and availability of properties can influence business investment decisions is a finding confirmed by a 2003 study from the University of Ulster: “Factors Affecting the Levels and Form of Private Investment in regeneration”, a report sponsored by ODPM.

site will not be brought back into use without some form of public support. However, earlier intervention could have saved significant public funds and so would have led to economic efficiency gains. The BPRA scheme will encourage early remediation, thus preventing the costs of remedying dereliction from spiralling until they become unaffordable.

C.11 There is also evidence⁵ of an “enterprise gap” in the UK’s most disadvantaged communities, where business start-up rates can be around ten times lower than in more prosperous areas. The proposed BPRA scheme is designed to alleviate these problems, by encouraging and supporting private investment in enterprise in these areas.

C.12 Finally, buildings in disadvantaged areas can often be in need of significant redevelopment and refurbishment to bring them back up to standard suitable for occupation. While the prices for purchase or lease may reflect this, the need for significant up-front investment can act as a disincentive compared to the more straightforward occupation of a building in other areas. This can increase the risk of greenfield, rather than brownfield development, with a corresponding reduction in amenity and biodiversity.

Options

C.13 Option 1: Do nothing. Investment decisions are about weighing-up risks and rewards. Many businesses may feel unable to bear the uncertainties associated with investing in renovating empty properties in Enterprise Areas, because they may not consider that there is a reasonable balance

⁵ A fairly recent study, in 2000, by the Bank of England concluded that “the negative relationship between deprivation and entrepreneurial activity appears to be clear cut in the case of the 50 most deprived local authorities” and found, more generally, that high levels of local deprivation appear to be associated with low business formation rates.

between the perceived risks and rewards. Doing nothing will not help to redress any imbalance. It will result in the status quo continuing and will not help to regenerate disadvantaged areas.

C.14 Option 2: Introduce a targeted measure, such as BPRA, to help redress the balance and to encourage increased investment and enterprise in disadvantaged areas. The advantages include the fact that the BPRA scheme should help to: (a) foster physical and social regeneration of pockets of deprivation by tackling apparent market failures; (b) increase private investment, enterprise and employment in these areas and (c) encourage brownfield development, thus reducing pressure on greenfield sites. The disadvantages include the fact that tax measures can be blunt instruments (they cannot, for example, help businesses that make insufficient profits to be liable for tax) and the fact that BPRA, on its own⁶, is a relatively modest measure, so its direct impact on regeneration could also be modest.

C.15 Option 3: Introduce a measure that would apply throughout the UK, which would not be restricted to the 2,000 most disadvantaged areas. The main advantage of a country-wide scheme would be the fact that it would encourage brownfield development and regeneration more generally. The disadvantages would include a very much higher Exchequer cost and the fact that a general scheme would not target private investment on those areas of the country that appear to need it most.

C.16 The Government believes that Option 2, the targeted relief that BPRA would provide, is the best of the three options identified above as potential

⁶ Because deprivation is a multi-faceted problem, the UK Government adopts a holistic approach to regeneration. Thus BPRA would be only one of a series of measures that the Government has put in place, or plans to introduce, to tackle deprivation.

response to the problems found in the most disadvantaged areas of the UK.

C.17 Question 5: Responses are invited on the merits or otherwise of introducing a targeted scheme, such as BPRA to regenerate deprived areas, rather than a UK-wide measure, no measure at all or some other, alternative scheme.

Business sectors affected

C.18 The Government wants BPRA to have the maximum possible impact by attracting the maximum investment into the regeneration of Enterprise Areas. So the proposed BPRA scheme would be available to all property owners and lessees who incur qualifying expenditure and who have a liability to United Kingdom tax, operating in any sector of the economy. It would be available to sole traders, partnerships, stand-alone or subsidiary companies. It is proposed that it would be available to all businesses, regardless of size, including small and medium-sized enterprises (SMEs). It is also hoped that BPRA will benefit SMEs indirectly, by increasing the stock of available and affordable properties for all businesses to let. This should be of particular help to new business start-ups, the bulk of which are SMEs. **(This issue is raised in Chapter 2 and is included in the summary of questions as Q3 in Chapter 5.)**

Issues of equity and fairness

C.19 One of the reasons why development is not occurring is due to problems in local property markets. Wards are a close fit to those markets. By designating disadvantaged areas at the level of electoral wards (postcodes in Scotland) the Government is able to target more accurately these

smaller pockets of deprivation⁷. Also, targeting regeneration support on disadvantaged areas enables the Government to tackle perceived differences in economic performance at the sub-regional level. Thus restricting BPRA to spending in Enterprise Areas is designed to target the relief where it can do the most good.

Benefits

C.20 BPRA will benefit businesses renovating empty properties in disadvantaged areas by providing them with certainty that their qualifying expenditure will be eligible for up-front tax relief. That up-front tax relief will provide businesses with a cash-flow benefit and a shorter payback period on their investment

C.21 Bringing premises back into commercial use can stimulate the local economy, helping to provide jobs for local people and creating a better environment for the local community.

C.22 It is difficult to quantify the annual number of unused building renovations in Enterprise Areas that are likely to qualify for BPRA over the five-year period of the relief's life, and also the possible wider effects in terms of job creation and environmental benefits.

⁷ The expression "pockets of deprivation" refers to the incidence of deprived communities, often close to prosperous areas, which is a particularly marked feature of the UK economy. Historically, this situation seems to have arisen because some UK communities are still struggling to cope with the transition from a traditional economy to a new one, and suffer from a lack of skills, innovation and enterprise. Other of these communities have faced decades of disinvestments in housing and job creation. In any event, there is evidence of a significant "enterprise gap" between the UK's most disadvantaged and most prosperous communities (see C.11) and of the fact that there are significant sub-regional differences in GDP per capita, unemployment rates and in levels of economic activity.

- C.23 Question 6: Any views or data on the annual number of buildings that are likely to be renovated under the scheme, and the probable extent of the benefits to businesses - especially SMEs - would be very welcome.**
- C.24 The regeneration of brownfield sites can also reduce pressure on Greenfield sites. An estimate⁸ of the external benefits associated with Greenfield preservation puts this in the region of £180,000 per hectare.
- C.25 Finally, there are potential spill-over benefits to the area in general and to neighbouring properties, as well as wider social benefits by way of reductions in visual blight and possible reductions in graffiti and vandalism.
- C.26 However, although the benefits could be wide and difficult to quantify, it is also relevant to bear in mind that BPRA's effects would be likely to be modest and worthwhile mainly as part only of the Government's holistic approach to the multi-faceted issues involved in regeneration.
- C.27 Question 7: Views and data on the possible wider effects of BPRA on job creation and the environment in disadvantaged areas are also requested.**

Implementation (compliance) costs

- C.28 These are considered to be negligible. Capital allowances are a long-standing and well-understood feature of the tax system. The introduction of BPRA will not introduce any special additional compliance costs for businesses. Businesses will need to compute their claims as they do currently for other capital allowances. Claims will be made on income tax or corporation tax returns in the usual way and it is envisaged that the returns will include a new box for individuals or companies to complete if

they wish to claim BPRA. Before the scheme comes into effect, the Inland Revenue will publish guidance on BPRA to help businesses ensure that their claims are correct.

C.29 Question 8: Responses are specifically invited to either confirm, or qualify our belief that the business compliance costs of BPRA are likely to be negligible.

Exchequer effect/distributional impacts

C.30 At Budget 2004 the Chancellor announced that subject to State aid approval BPRA will be introduced in 2005. The Exchequer cost of BPRA is estimated at £10 million in 2005/ 06, £35 million in 2006/ 07, and £30 million a year for each of the next three years from 2007-08 until 2009-10.

Small Business impacts

C.31 There should be no additional compliance costs for small businesses.

C.32 Small businesses that incur qualifying expenditure will be able to claim the new allowances by completing a box on their income tax or corporation tax return (as the case may be).

C.33 It is likely that the majority of premises renovated under the scheme will be tenanted by smaller businesses⁹. This should be an indirect benefit to

⁸ By the Office of the Deputy Prime Minister (ODPM).

⁹ Data supplied by IPD Ltd to the Inland Revenue in the first half of 2004 suggests that of new leases taken out on premises vacant for more than one year, 31% are by large businesses and the remaining 69% by SMEs. This finding is more pronounced in deprived areas where the split is 26% and 74% for large businesses and SMEs respectively. This suggests that large businesses are less likely to take out a new lease on premises with a vacancy history, and that ,

SMEs to the extent that the stock of available and/or affordable business premises may be increased by the measure, and to the extent that landlords may feel more able to reduce rents because of the support provided by BPRA tax relief. **(This issue is raised in Chapter 2 and our assumptions are listed for question in Chapter 5 at Q3.)**

Other costs and benefits (public & private sector)

C.34 This new measure will result in negligible administrative costs to the Government. There will be some new costs if a new BPRA claim box is added to the tax returns and in producing staff guidance for the new scheme, but it is believed that these costs are unlikely to be significant.

Unintended consequences

C.35 It might be suggested that some businesses would deliberately keep premises vacant in order to benefit from BPRA. On this view, BPRA could be seen as providing a perverse incentive to leave premises empty.

C.36 We consider, however, that this is unlikely to be the case because, under current tax law, the costs that a business incurs on its business premises for repairs and renewals are chargeable in full in the trading account under normal accounting practice, and are allowable in full as deductions when computing profits for tax purposes. Existing businesses would, therefore, gain no advantage by deferring any repairs and renewals and leaving premises vacant for 12 months or more in order to claim relief under BPRA. **(This issue was raised earlier in Chapter 2 and is listed in Chapter 5 as Q2.)**

in deprived areas, newly renovated buildings which have been vacant for a longer period, are *almost three times more likely to be occupied by smaller than by larger firms.*

C.37 Furthermore, the scope of BPRA is limited. Expenditure on refurbishing business premises will not constitute capital expenditure for tax purposes (and thus be within the scope of BPRA) unless:

- It is expenditure on substantial alterations or improvements to the premises, or
- It is incurred by a new business – either as landlord or lessee – in order to bring the premises up to the standard necessary for business use.

C.38 Relief under BPRA is, therefore, not available for the ordinary operating expenses incurred by an existing business. And even if BPRA were available in such circumstances (which it is not) it seems inherently unlikely that an existing business would forgo for a year the income that could be generated by making use of the premises, in order to access the limited benefits available from BPRA.

C.39 **We would welcome views or evidence to support or contradict this view. (This question is included in the summary of Questions in Chapter 5 at Question 2.)**

Other impacts

Devolution

C.40 BPRA is designed to apply to Enterprise Areas throughout the United Kingdom. In England and Scotland the areas selected are the most deprived 15% of wards/areas, in Wales and Northern Ireland they are the most deprived 42% of wards to reflect higher levels of deprivation in these

countries¹⁰. The Government is aware that the Indices of Deprivation have been updated in England and Scotland and will keep the current designation of Enterprise Areas under review.

Human Rights

C.41 No Human Rights issues have been identified.

E-policy

C.42 No e-policy issues have been identified.

Environmental impacts

C.43 BPRA will support the recycling of existing premises that have fallen out of use. Typically, these premises will be on existing brownfield sites. Recycling existing premises can reduce the pressure for new build on greenfield sites, with the negative effects that greenfield development often has in terms of loss of amenity and biodiversity. An estimate¹¹ of the external benefits associated with greenfield preservation puts this in the region of £180,000 per hectare.

C.44 Increased investment in disadvantaged areas can help to revitalise local communities, improve the local environment and make them better places to live and work. **Views or data on the potential environmental effects of BPRA were requested earlier at Question 7. (See C.27 above and Q7 in the summary of questions at Chapter 5.)**

¹⁰ The Enterprise Areas were selected using the Index of Multiple Deprivation 2000 (England); the Welsh index of Multiple Deprivation 2000; the Scottish Area Deprivation Index 1998; and Northern Ireland Measures of Deprivation 2001.

¹¹ Made by the Office of the Deputy Prime Minister (ODPM).

Rural proofing

C.45 No issues identified. Rural communities and agricultural businesses can benefit from disadvantaged area measures (and so could be eligible for BPRA) just as other communities and business sectors are eligible. The 2,000 designated disadvantaged areas are based on the national Indices of Multiple Deprivation (IMD). These are considered to be the best available way of targeting deprived areas, since they are based on hard statistical measures of key features of deprivation such as income, unemployment, health and poverty. So although there is, in fact, a concentration of the targeted areas in urban locations, this is a consequence of applying the key measures of deprivation uniformly to all communities.

Competition assessment

C.46 The competition filter shows that this policy is not expected to give rise to competition issues.

Securing compliance

C.47 The policy will be monitored and kept under review. Compliance will be secured using normal Inland Revenue risk assessment methods.

Consultation

C.48 The Chancellor has decided to introduce BPRA in the form of a 100% first-year capital allowances scheme for the renovation of unused business premises in disadvantaged areas. He has also announced the aim of introducing the scheme in 2005, subject to state aid approval. Consultation is needed on

- The detail of the relevant draft legislation

- The extent to which the scheme may be expected to assist smaller businesses
- Whether a minimum vacancy period of 12 months is the most appropriate period in terms of the policy's objectives
- Whether the scheme may create a perverse incentive to leave premises empty for a year in order to qualify for BPRA relief
- Other, potential effects of BPRA, including any evidence to support the view that the scheme is likely to have wider social benefits, such as a positive impact on job creation, or wider environmental benefits and
- The number of buildings likely to be renovated under the scheme, and any inadvertent compliance burdens the scheme could create for businesses.

The consultation questions are separately listed in Chapter 5.

Monitoring and evaluation

C.49 The overall impact of the scheme will be monitored through feedback, the examination of a sample of tax return entries and the collection of data to assess its effects. This monitoring will continue throughout the life of the relief.

Summary

The specific points arising from this RIA on which responses are invited are summarised in Chapter 5. The contact point for any questions on any aspect of this RIA is:

Paul Thomas
Business Tax, Capital Allowances Policy
Tel: 020 7438 7143 (on or before 15/12/04)

Or,

Tel 020 7147 2541 (from 16/12/04)

E-mail: Paul.Thomas@ir.gsi.gov.uk