These notes refer to the Capital Allowances Act 2001 (c.2) which received Royal Assent on 22nd March 2001

CAPITAL ALLOWANCES ACT 2001

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Glossary

Part 3: Industrial buildings allowances

Chapter 10: Additional VAT liabilities and rebates

Overview

1162. This Chapter deals with the interaction of the industrial buildings allowances and the VAT capital items legislation.

1163. Section 345 applies for this Chapter definitions in Chapter 2 of Part 12.

1164. Sections 346 to 348 deal with additional VAT liabilities. Broadly they:

- give entitlement to initial allowances if the person was entitled to an initial allowance for qualifying enterprise zone expenditure and the additional VAT is incurred no more than 10 years after the site was included in an enterprise zone; or
- give rise to qualifying expenditure increasing the residue of qualifying expenditure and so increase allowances.

1165. Sections 349 to 351 deal with additional VAT rebates. The rebate:

- reduces the residue of qualifying expenditure (and so reduces allowances); and
- may give rise to a balancing charge.

Section 345: Introduction

1166. This section applies definitions in Chapter 2 of Part 12 for this Chapter.

Section 346: Additional VAT liabilities and initial allowances

1167. This section is based on section 1(1A) and parts of sections 1(5) and 159A(3) of CAA 1990. It provides for initial allowances to be given in respect of additional VAT liabilities incurred in respect of the qualifying expenditure.

1168. *Subsection (1)(a)* provides the main condition – that the original expenditure entitled the person incurring it to an initial allowance in respect of qualifying enterprise zone expenditure.

1169. *Subsection (1)(b)* to *(d)* provides the other conditions that need to be met for an initial allowance to be given.

1170. *Subsection (6)* makes it clear that the person entitled to the initial allowance in respect of the original expenditure need not be the person incurring the additional VAT liability.

1171. Initial allowances may also be due in respect of additional VAT liabilities arising if the original capital expenditure was incurred in the year ended 31 October 1993. This rule is now of limited application and is dealt with in paragraphs 75 to 77 of Schedule 3.

Section 347: Additional VAT liabilities and writing-down allowances

1172. This section is based on section 3(2A) and (2B) and part of section 159A(3) of CAA 1990. It provides the general rule for additional VAT liabilities.

1173. In order to ensure that the additional VAT liability (and increase in the residue of qualifying expenditure) gives rise to increased writing-down allowances, *subsection (3)* provides that the incurring of an additional VAT liability is a relevant event for the purposes of section 311.

Example

In 1998 U incurs qualifying expenditure of £500,000 on an industrial building. In 2003 U incurs an additional VAT liability of £10,000 in respect of the building. At that time the residue of qualifying expenditure is £400,000.

The £10,000 is added to the residue of qualifying expenditure giving a total of £410,000. Section 311 means that (subject to other relevant events) subsequent writing-down allowances must reflect the increased qualifying expenditure.

If from the time the additional VAT liability accrued 20 years remain, (out of the period of 25 years since first use of the building,) the revised writing-down allowance will be £20,500 for each year (£410,000 divided by 20).

Section 348: Additional VAT liabilities and writing off initial allowances

1174. This section is based on section 8(2)(a) and part of section 159A(3) of CAA 1990. It provides that an initial allowance in respect of an additional VAT liability is written off when the additional VAT liability accrues.

1175. Most initial allowances will relate to qualifying enterprise zone expenditure and will be given at 100%. In such cases the residue will be increased by this amount (under section 347(2)(b)) and immediately reduced again by this section.

1176. If a reduced initial allowance is made (or under paragraph 75(3) of Schedule 3 only a 20% initial allowance is available) then the net effect of these two rules is that the residue is increased by the difference between the additional VAT liability incurred and the initial allowance made.

Section 349 and 350: Additional VAT rebates

1177. These sections are based on parts of sections 3, 4 and 159A of CAA 1990. They deal with additional VAT rebates received in respect of qualifying expenditure.

1178. *Section 349* applies when the additional VAT rebate received is less than the residue of qualifying expenditure immediately before the rebate accrues. In such cases, *subsection (2)* provides that writing-down allowances are revised accordingly. Section 351 provides that the residue is first reduced by the amount of the rebate.

1179. *Section 350* applies in all cases when an additional VAT rebate is made. However, it is only relevant if the additional VAT rebate exceeds the residue of qualifying expenditure. *Subsection (1)* provides that the making of the additional VAT rebate is a balancing event. Under section 314, this can give rise to balancing allowances and balancing charges. However, *subsection (2)* provides that no balancing allowance can arise as a result of an additional VAT rebate.

1180. *Subsection (3)* provides that a balancing charge will only arise if the additional VAT rebate exceeds the residue of qualifying expenditure. *Subsection (4)* ensures that the balancing charge is equal to the difference.

1181. *Subsection (5)* deals with starting expenditure. If and only if:

- a balancing charge is made under this section; and
- the person to whom it is made is the person who incurred the qualifying expenditure,

then the starting expenditure is reduced by the amount of the balancing charge.

Section 351: Additional VAT rebates and writing off qualifying expenditure

1182. This section is based on section 8(12A) and part of section 159A(3) of CAA 1990. It provides that the residue of qualifying expenditure is reduced by the amount of any additional VAT rebate made.