

CAPITAL ALLOWANCES ACT 2001

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Glossary

Part 5: Mineral extraction allowances

Chapter 4: Qualifying expenditure: second-hand assets

Overview

1404. This Chapter treats, in certain cases, expenditure on a mineral asset as if it were expenditure on mineral exploration and access. The rate at which allowances are given for qualifying expenditure on mineral exploration and access is higher than for qualifying expenditure on a mineral asset. In certain cases the Chapter also limits, by reference to the position of previous owners of the asset, qualifying expenditure on acquiring an asset.
1405. [Section 407](#) treats part of the cost of a mineral asset as qualifying expenditure on mineral exploration and access if part of the value of the mineral asset is attributable to expenditure of “the previous trader” on mineral exploration and access.
1406. [Section 408](#) reduces, in certain cases, the cost of an interest in an oil licence acquired from someone who was not a mineral extraction trader. Some of the reduction may be treated as qualifying expenditure on mineral exploration and access.
1407. [Section 409](#) limits qualifying expenditure on an asset if it represents expenditure on mineral exploration and access incurred by a seller who was not a mineral extraction trader.
1408. [Section 410](#) limits qualifying expenditure if the mineral asset is an interest in a UK oil licence.
1409. [Section 411](#) limits qualifying expenditure if a “previous trader” has owned the asset concerned. The limit is to the previous traders unrelieved residue of expenditure.
1410. [Section 412](#) and section 413 prevent “groups” from increasing the capital expenditure on a mineral asset by means of intra-group transfers.

Section 407: Acquisition of mineral asset owned by previous trader

1411. This section is based on section 115 and parts of sections 113 and 114 of CAA 1990. There is a minor change in subsection (1)(a) as in sections 400 and 403 (paragraphs 1381 and 1396 above). See *Change 47* in Annex 1.
1412. *Subsection (5)(a)* treats part of the trader’s expenditure on acquiring the mineral asset as qualifying expenditure on mineral exploration and access in those cases if this section applies.

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1413. *Subsection (5)(b)* makes a corresponding reduction to the trader's expenditure on acquiring the mineral asset.

Example

Assume that:

- (a) mineral extraction trader B acquires for £1,000 a mineral asset that used to be owned by a previous trader P; and
- (b) P had incurred £50 capital expenditure on mineral exploration and access and this capital expenditure is reflected as to £100 (of B's purchase price) in the value of the mineral asset.

£50 is the lower of the two amounts in (b). B is treated as incurring:

- (i) £50 of qualifying expenditure on mineral exploration and access; and
- (ii) only £950 on the purchase of the mineral asset – but it may not all be qualifying expenditure because other restrictions in Chapter 3 or 4 may apply.

1414. There is nothing in this section for section 115(2)(b) of CAA 1990 which is unnecessary. See *Note 52* in Annex 2.

Section 408: Acquisition of oil licence from non-trader

1415. This section is based on section 118(2) and sections 118(1) and 138A of CAA 1990. It sets out the proposition in section 118(2) after the necessary adaptations required by section 138A.

1416. *Subsection (1)* applies this section if:

- the trader acquires an interest in an oil licence the value of which is partly attributable to mineral exploration and access expenditure of the seller; and
- the seller has not carried on a mineral extraction trade.

1417. There is a minor change in subsection (1)(a) as in sections 400, 403 and 407 (paragraphs 1381, 1396 and 1412 above). See *Change 47* in Annex 1.

1418. *Subsection (2)(b)* reduces the trader's expenditure on acquiring the mineral asset by "E2".

1419. *Subsection (2)(a)* treats the trader as incurring qualifying expenditure on mineral exploration and access of an amount that is capped at "E2".

Example

Assume that:

mineral extraction trader, B, acquires an oil licence for £1,000 from S;
S is not a mineral extraction trader, but S has incurred expenditure of £50 on mineral exploration and access; and
it is just and reasonable to attribute £300 of B's purchase price to the £50 spent by S.

B is treated as incurring:

£50 of qualifying expenditure on mineral exploration and access; and

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only £700 (£1,000 - £300) on the purchase of the oil licence – but it may not all be qualifying expenditure because other restrictions in Chapter 3 or 4 may apply.

Section 409: Acquisition of other assets from non-traders

1420. This section is based on sections 118(1) and 121(3) of CAA 1990. If the seller of an asset has not been a mineral extraction trader it caps the buyer's qualifying expenditure on acquiring an asset, if that asset represents the seller's expenditure on mineral exploration and access. The cap is the amount of the seller's mineral exploration and access expenditure represented by that asset.
1421. There is a minor change in *subsection (1)(a)* as in sections 400, 403, 407 and 408 (paragraphs 1381, 1396, 1412 and 1417 above). See *Change 47* in Annex 1.

Section 410: UK oil licence: limit is original licence payment

1422. This section is based on section 116 of CAA 1990. It caps the qualifying expenditure on acquiring an interest in a UK oil licence to the amount originally paid to obtain the oil licence (or a reasonable part of the original payment).
1423. *Subsection (4)* makes it explicit that the cap does not affect any part of the expenditure that is treated as qualifying expenditure on mineral exploration and access by the first two sections in this Chapter.

Section 411: Assets generally: limit is residue of previous trader's qualifying expenditure

1424. This section is based on sections 113 and 114 of CAA 1990. It prevents an increase in qualifying expenditure if the trader acquires an asset that, broadly, has previously been owned by another mineral extraction trader for the purposes of that earlier owner's mineral extraction trade. The qualifying expenditure on acquiring the asset is limited to the residue of the previous trader's qualifying expenditure.

Example

Assume that:

mineral extraction trader, B, buys a mineral asset for £1,000;

the mineral asset was previously owned by a previous trader, P; and

P's residue of qualifying expenditure related to the asset is £500.

B's qualifying expenditure cannot exceed £500.

1425. *Subsection (8)* makes it explicit that the cap does not affect any part of the expenditure that is treated as qualifying expenditure on mineral exploration and access by the first two sections in this Chapter.

Section 412: Transfers of mineral assets within group: limit is initial group expenditure

1426. This section is based on part of section 117 of CAA 1990. It prevents an increase of qualifying expenditure on a mineral asset through a transfer between companies under common control.
1427. This is done by limiting the acquiring company's capital expenditure on acquiring the mineral asset to the selling company's capital expenditure on acquiring that mineral asset. This restriction is wider, in one sense, than the restriction in section 411 because this restriction applies even if a previous trader has not owned the mineral asset. Both restrictions can apply to the same acquisition.

Example

Assume that parent company A sells a mineral asset (originally bought for £500) to its subsidiary B for its then market value of £1000.

This section limits B's capital expenditure to £500 – but it may not all be qualifying expenditure because other restrictions in Chapter 3 or 4 may apply.

1428. Subsection (2), in referring to “just and reasonable apportionment”, is a minor change. See *Change 40* in Annex 1.
1429. Subsection (5) modifies the application of section 404 so that, broadly, the undeveloped market value of land is computed at the time the group first acquired the mineral asset. This is because the group's capital expenditure is effectively limited to the capital expenditure that the group incurred (ignoring group transfers) on acquiring the mineral asset.
1430. Subsections (6) and (7) make corresponding modifications of section 405 if subsection (5) has applied. They put the buyer in broadly the same position as if the buyer had owned the interest in land from the time that it was purchased by the first group company.

Section 413: Transfers of mineral assets within group: supplementary

1431. This section is based on part of section 117 of CAA 1990.
1432. Subsection (2)(b) makes explicit that section 412 does not apply if an election is made for “step-in-shoes” treatment to apply to the buying company in relation to the mineral asset. That treatment will reflect an earlier deduction for the undeveloped market value of land.
1433. Subsection (4) makes it explicit that the cap in the previous section does not affect any part of the expenditure that is treated as qualifying expenditure on mineral exploration and access by the first two sections in this Chapter.