Focus on

# Budget 2021 – Capital allowance super-deduction

## Is it as good as it seems for Motor Dealers?

SPRING 2021 Budget

The capital allowance super-deduction was announced in the Budget on 3 March 2021 and immediately caught the attention of headline writers as a good thing for businesses and a way to encourage investment. There are however a number of areas that Dealers should consider, in particular which assets and expenditure they can and should claim the super-deduction for, in order to maximise their post-tax profits and plan their cash flow accordingly.

### A summary of the new capital allowance reliefs

Two key capital allowance reliefs were announced in the Budget:

- The super-deduction is a 130% first-year allowance, that is you can deduct 130% of the full cost of a qualifying asset from your profits before tax in the year of purchase, to apply from 1 April 2021 to 31 March 2023 for investments in qualifying plant and machinery expenditure. This is expenditure that ordinarily would have been relieved at the main rate writing down allowance of 18%. The uplift that is applied means a tax deduction of £130k for every £100k spent on qualifying capital spend (an effective tax saving of 24.7p per £1).
- There is also a new 50% special rate first-year allowance ("FYA") which is expected to provide relief for qualifying expenditure that would ordinarily be relieved at the special rate writing down allowance of 6%. The temporary change in rate means a tax deduction of £50k for every £100k spent on qualifying capital spend (an effective tax saving of 9.5p per £1).

These reliefs are particularly valuable to Dealers spending in excess of the Annual Investment Allowance ("AIA"), which allows 100% tax relief for qualifying capital expenditure. The AIA is currently set at £1m, due to a temporary extension, and is set to return to £200k from 1 January 2022.

### Sounds good – what should dealers be mindful of?

*'Qualifying' spend*

Firstly, Dealers should be careful in determining what spend qualifies for each relief. As a high-level distinction, assets that are acquired 'with which' to carry on a trade should qualify for the super-deduction (for example, showroom furniture, service bay machinery and computer equipment). Expenditure which is incurred in bringing a qualifying asset into the business and enabling it to work is also seen as part of the qualifying spend.

This is distinct from assets that are acquired 'within' the trade that is carried on (for example heating and hot and cold-water systems and of increasing importance to the sector "electrical and power systems").

A showroom refurbishment is likely to have a mix of qualifying spend so Dealers should consider what qualifies up-front so they go into the refurbishment with clear expectations of the tax consequences and the subsequent cash impact.

The new reliefs will not apply to contracts entered into prior to Budget day on 3 March 2021, but any immediate spend should otherwise be pushed back until after 1 April 2021.

## Cars, LCVs and HGVs

Cars are not treated as 'Main Pool' Plant and Machinery for capital allowance purposes, so they will not qualify for these reliefs. LCVs and HGVs owned outright will however qualify as Plant and Machinery and are therefore eligible for the 130% super-deduction. However, care should be taken when making a super-deduction claim on such items, particularly where higher residual values are expected. Further details are outlined under the heading "balancing charges" below.

## What about EV chargers and infrastructure?

Capital expenditure on EV chargers and costs directly associated with their installation currently qualify for 100% FYA and this measure is set to last through to 31 March 2023.

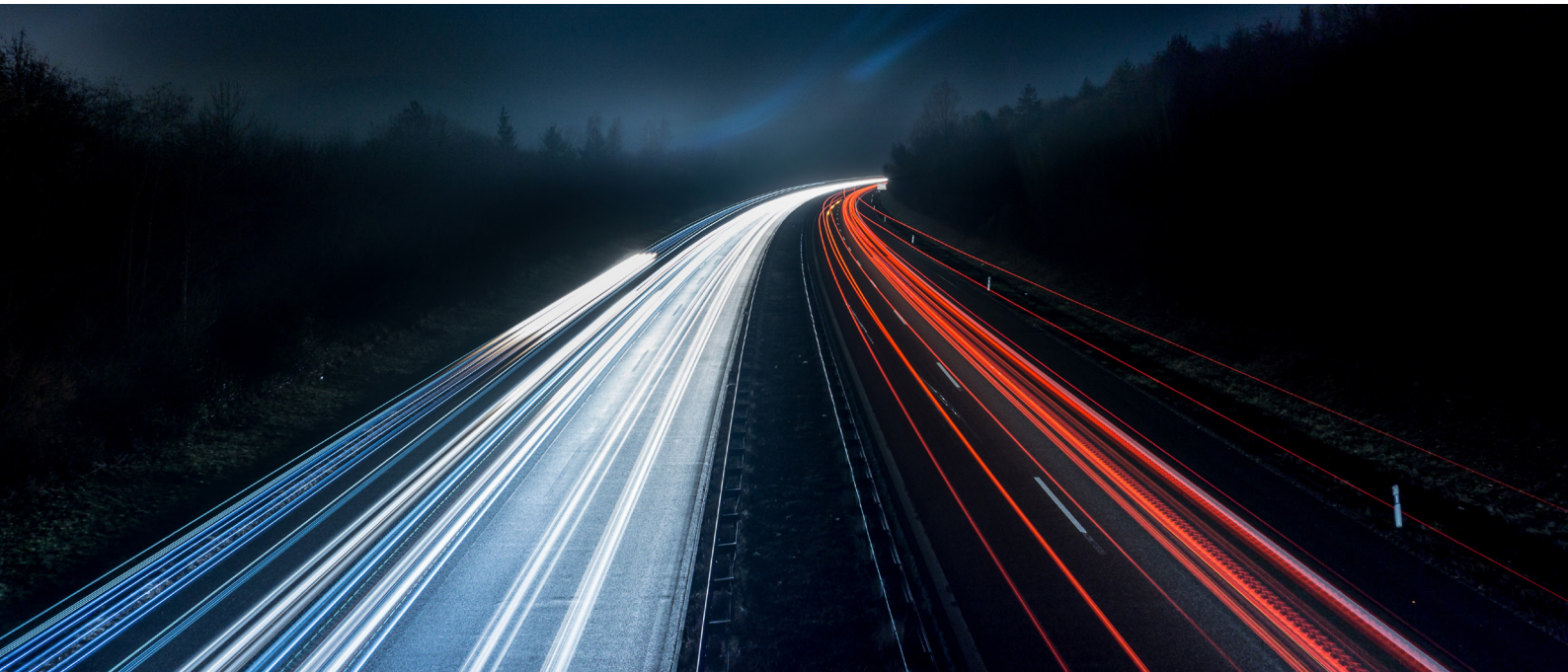
Should this spend qualify as Plant and Machinery, the additional 30% uplift will be welcomed by many dealers who are being required to spend significant amounts on upgrading their energy and EV charger infrastructure to meet the increasing proportion of EV's being sold leading up to the 2030 ban on the sale of ICE vehicles.

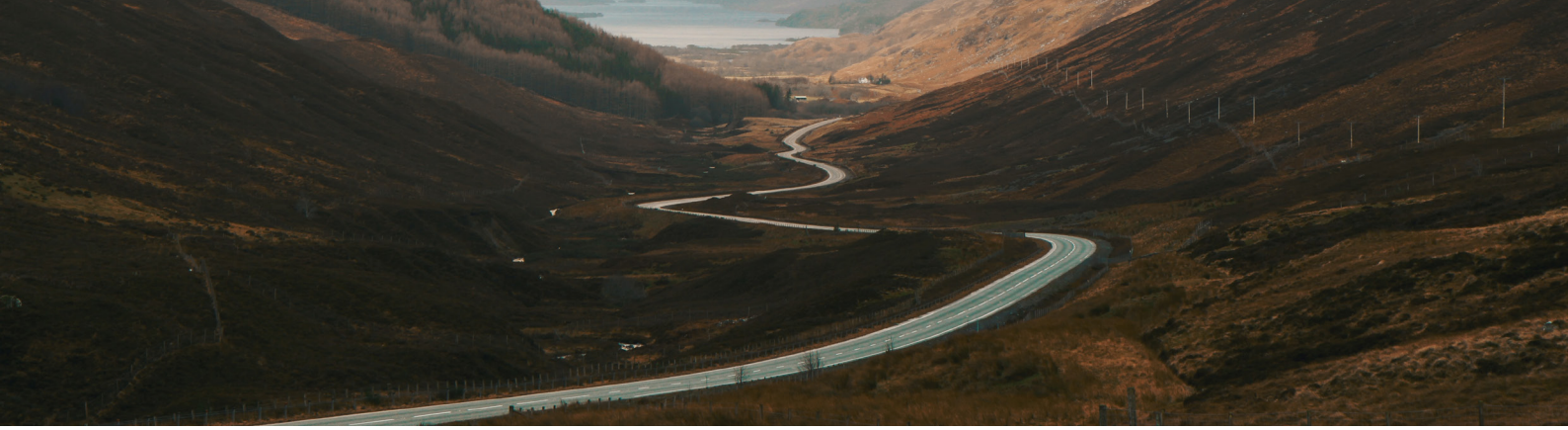
This expenditure can clearly be seen to be directly attributable to the recent change in Government policy on ICE vehicles leading to a major infrastructure investment requirement for the sector, something which the Government has signalled as being an important factor in their creating the new capital allowance super-deduction (i.e. infrastructure investment). This investment expenditure is strategically important to the sector as it is essential to the ability of the Dealership to continue to operate and sell the significantly increasing proportion of EV's as we approach 2030. We therefore think that this clearly differentiates such expenditure from purely being in the course of a 'normal' electrical supply to operate business facilities and have put the case to HMRC for it to qualify for the super-deduction.

There is a risk however that EV chargers and the related infrastructure spend may not qualify for the super-deduction. This is because the existing HMRC capital allowance legislation is written in such a way that they may fall to be classified as just part of the dealership's electrical systems and therefore would be classed as spend 'within' the trade that is carried out. For this reason we have already sought clarification from HMRC on this point and outlined the arguments contained in the previous paragraph on this capital spend being strategic investment for the business.

Turning to specific costs connected with the EV chargers, while it can be argued that such expenditure is necessary to bring the asset into use, the devil may well be in the detail as always, taking into account specific costs including:

- **Civils works - digging up the car park, trenching, ducting, cable laying, charger plinths and pillars.** These works may have a mixture of elements that could be argued to fall in to the 'with which' and the 'within' definitions and so they will need further careful consideration, based on the response we receive from HMRC.
- **Electrical works, including switchgear and EV chargers.** One specific condition could be that AC chargers that are provided off the existing supply would historically fall in the 'within' definition but it could be argued that a new supply for a DC charger is classified as 'with which'. It could be further argued that the DC charger may qualify as plant for the super-deduction allowance if it does something different to the AC charger and the general electrical system (for example, being a different power system). If HMRC agree with our view that the DC charger and associated expenditures can be classified as qualifying for the super-deduction there should also be an argument that the AC charger supply and costs, or at least part of should be allowable also. We will keep Dealers appraised as and when we hear back from HMRC. It would seem likely that moveable EV 'kit' would qualify for the super-deduction.





*Balancing charges*

Missing, among the headlines is the consideration of what happens to the purchased assets at the end of their useful life. Where the super-deduction and 50% FYA has been claimed the proceeds will be treated as balancing charges (i.e. immediately taxable profits) rather than the usual treatment of being deducted from capital allowance pool expenditure. This charge is also likely to be at the increased corporation tax rate of 25%. The modelling we have completed also shows that there are instances when it will be better to not claim the super-deduction and instead, for example, elect to treat the asset as a Short Life Asset. The key takeaway for dealers is extra care should be taken when looking to claim the new reliefs on any assets that are not expected to be scrapped at the end of their useful life but rather have a reasonable residual value.

Furthermore, we are starting to see an increase in merger and acquisition activity as we enter the final phase of lockdown in the UK and the nature of the UK automotive retail landscape is such that many transactions are in the form of the sale of the trade and assets of the business. Balancing charges in relation to the super deduction assets can be accelerated upon a sale and this could have a significant impact on the sale price and/or post-tax cash proceeds where the asset has not been fully written down for tax purposes. Tax structuring advice is therefore highly recommended.

*Losses*

Also announced in the Budget were changes to the loss carry back rules meaning losses could be carried back up to three years instead of the usual 12 months. Broadly, this measure will have effect for company accounting periods ending in the period 1 April 2020 to 31 March 2022. Some Dealers, who ordinarily make profits, may have swung to a loss during this period because of the impact of the COVID pandemic and other strategic challenges which the sector is experiencing.

Where Dealers do not have enough scope to utilise these losses against the prior year alone, this measure to allow further carry back of losses can lead to a welcome cash boost. Consideration should also be given as to whether it will, in fact, be better to carry forward these losses to potentially use against profits chargeable to tax at 25% when the main rate increases from 1 April 2023.

*Deferred tax*

The new relief may create deferred tax liabilities which could be interpreted, for example, by third parties as an indication that the company is capital intensive. The impact of deferred tax may therefore need to be assessed where there is interest from external stakeholders or buyers.

**What do I do now?**

An understanding of the rules is key for business planning - when completing cashflow forecasts and deciding the level of capital spend. We can provide specific sector tax analysis ahead of committing to significant capital spend so adjustments can be made accordingly.

Further consideration should be given where there may be potential M&A activity as there can be an impact on the sale price of a business and a material impact on post-tax cash following a sale.

## For more information please contact: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