10.4 The problem of ownership

One of the key conditions for giving plant and machinery allowances is that of ownership. Section 11(4) of CAA 2001 reads as follows:

> "The general rule is that expenditure is qualifying expenditure if—
>
> (a) it is capital expenditure on the provision of plant or machinery wholly or partly for the purposes of the qualifying activity carried on by the person incurring the expenditure, and
>
> (b) the person incurring the expenditure owns the plant or machinery as a result of incurring it."

Most of the time, this condition poses no problems. However, particular issues arise from point (b) above in relation to fixtures in property. Suppose, for example, that a tenant with 20 years remaining on a lease installs air conditioning in the property. Legally, the building belongs to the landlord; as the air conditioning – once installed – forms part of the property, it immediately belongs to the landlord.

Without special rules, the landlord could not obtain allowances on the expenditure as he has not incurred the cost and the tenant could not claim allowances as he does not own the air conditioning system.

The point came to a head in the case of *Costain Property Investments Ltd*. The Courts considered the meaning of the terms "belong" and "belonging" and concluded that they were ordinary English words to be interpreted in an ordinary sense. If a person merely had the right to use an asset for a limited period then it could not be said that the asset belonged to him. Landlords' fixtures could therefore not be said to belong to a leaseholder:

> "he cannot remove them from the building, he cannot dispose of them except as part of the hereditament and subject to the provisions of the lease and for the term of the lease."

Although it felt compelled to reach that decision, the Court could see no reason of principle to justify the outcome:

> "I cannot, however, regard the state of the law as satisfactory. The purpose of the statutory provisions must be to encourage investment in machinery and plant. In this case very large sums were expended on such investment but, under the enactment as it stands, nobody will receive the tax allowance in respect of it. The

freeholder will not, because the freeholder did not incur the expenditure and is not carrying on the trade. And the taxpayer will not because the items did not belong to the taxpayer. The Revenue are unable to suggest any policy reason why a person in the position of the taxpayer should be refused relief. It is to be hoped that the ambit of the legislation will be reconsidered."

The legislation was indeed reconsidered and new provisions relating to fixtures were introduced from 1985. Those provisions, as amended since their introduction, can now be found in CAA 2001, Pt. 2, Ch. 14.

See **10.3.1** above for an illustration of the difference between legal and beneficial ownership.

Law: CAA 2001, s. 172*ff.*

Case: *Costain Property Investments Ltd v Stokes* [1984] BTC 92

10.5 Deemed ownership

10.5.1 Introduction

To overcome the problem of ownership identified at **10.4**, the fixtures rules create a legal pretence of ownership so that plant and machinery allowances may be given for fixtures in certain defined circumstances.

The following are identified in the legislation as potential claimants of capital allowances by virtue of the special fixtures rules:

- persons with an interest in relevant land;
- equipment lessors;
- energy service providers;
- purchasers of land giving consideration for fixtures;
- purchasers of land discharging the obligations of an equipment lessee;
- purchasers of land discharging obligations under energy services agreement; and
- incoming lessees (with different rules according to whether or not the lessor is entitled to allowances).

Each of the above is considered in turn in the following paragraphs.

The rules described here are subject to special provisions if the fixtures in question are the subject of a long funding lease (see **Chapter 7**), and in certain other circumstances involving such long funding leases.

HMRC seem to have had a moment of forgetfulness about the existence of these deemed ownership provisions, as alluded to at para. 85 of the First-tier Tribunal judgment in *Cheshire Cavity Storage*. As stated in that judgment:

> "The appellant could only speculate on why HMRC held this view, as although the appellants were only tenants of the sites under which the cavities were created, since 1985 the law has been that in some circumstances a tenant can obtain capital allowances for expenditure on leasehold property."

Fortunately, however, HMRC did not pursue the point at the appeal, and the tribunal accepted that the ownership condition was satisfied.

Law: CAA 2001, s. 172, 172A

Case: *Cheshire Cavity Storage 1 Ltd and EDF Energy (Gas Storage Hole House) Ltd v HMRC* [2019] UKFTT 498 (TC)

10.5.2 Persons with an interest in relevant land

This is an important category. It treats a person as owning fixtures, for the purposes of claiming plant and machinery allowances, where:

- the person incurs capital expenditure on plant or machinery, for the purposes of a qualifying activity that that person is carrying on;
- the plant or machinery becomes a fixture; and
- the person has an interest in the relevant land at the time the item in question becomes a fixture.

This therefore covers the classic case of a tenant who installs plant or machinery in the property owned by his landlord.

An interest in land will typically be a freehold or leasehold interest, but see **10.3.1** above for a fuller definition.

"Relevant land" is the building or other description of land of which the fixture becomes part. In relation to boilers and water-filled radiators, the relevant land is the building in which that item is installed as part of a space or water heating system.

The legislation recognises that there may be different interests in the same land and, broadly, gives the right to claim allowances to the person with the lowest interest – the tenant rather than the landlord in a simple tenancy arrangement. If landlord and tenant wish to share the cost of installing plant or machinery, the tenant will be able to claim under these

rules. The landlord will be able to make a contribution and to claim allowances by virtue of the special rules for such contributions (s. 537: see **31.3.2**).

HMRC confirm that if two people with the same level of interest incur expenditure on the same fixture, they can each claim for the expenditure they incur. For example, two tenants may agree to share the cost of a new lift or a reception area desk.

Law: CAA 2001, s. 173(2), 176

Guidance: CA 26150

10.5.3 Equipment lessors

A person may buy equipment and lease it to a tenant, who installs it as a fixture in leased property. In technical terms, there is an equipment lease where:

- a person incurs capital expenditure on the provision of plant or machinery for leasing;
- an agreement is entered into for the lease of the plant or machinery, directly or indirectly from that person to another person;
- the plant or machinery becomes a fixture; and
- the agreement is not an agreement for the plant or machinery to be leased as part of the relevant land.

Without special rules, no allowances would be due to the lessor, as ownership has legally passed to the freeholder of the property. Nor would any allowances be due to the tenant or to the landlord, as they have not incurred capital expenditure.

The equipment lessor may make a joint election with the tenant to treat the lessor as owning the fixture. The election is not possible if the two parties are connected. Subject to that, the election normally takes effect from the time the lessor incurs the qualifying expenditure. However, it takes effect instead from the time the equipment lessee begins to carry on the qualifying activity, if the equipment lessor incurs the capital expenditure before that time.

Various conditions and exclusions apply. In particular, one of the following sets of conditions must be met:

Qualifying activity

- the equipment lease must be for the purposes of a qualifying activity carried on by the equipment lessee;
- the equipment lessee would have been entitled to fixtures allowances if he or she had incurred the expenditure directly; and
- the plant or machinery is not for use in a dwelling-house.

Right to sever

- the item in question becomes a fixture by being fixed to land that is neither a building nor part of a building;
- the equipment lessee has an interest in the land when taking possession of the plant or machinery in question;
- under the terms of the equipment lease, the equipment lessor is entitled to sever the plant or machinery, at the end of the period for which it is leased, from the land to which it is then fixed (and will then own it);
- the nature of the asset and the way it is fixed to land are such that its use on one set of premises does not, to any material extent, prevent it from being used (once severed) for the same purposes on a different set of premises;
- the equipment lease would fall to be treated, under generally accepted accounting practice, as an operating lease in the accounts of the equipment lessor; and
- the plant or machinery is not for use in a dwelling-house.

Affordable warmth programme

A third option existed for expenditure incurred by the end of 2007.

Law: CAA 2001, s. 174, 177-180
Guidance: CA 26200

10.5.4 Energy service providers

Overview

A provider of "energy services" who incurs capital expenditure may be treated as owning fixtures as a result. Without special rules, no allowances would be due to the provider as that person does not have an interest in the land.

According to HMRC guidance:

> "An energy services provider is a business that provides a range of energy management services, including the provision, operation and maintenance of plant or machinery, aimed towards reducing their client's energy bills. They are contracted by other businesses (clients) to manage their energy usage. This can take a variety of forms, from giving advice on how to reduce energy consumption, negotiating lower supply charges with energy providers, to designing, installing, operating and maintaining facilities on the client's premises to achieve energy efficiencies or savings."

This must be under a formal energy services agreement and is subject to a joint election by the provider and his client. Once more, certain restrictions and conditions apply.

Detail

The following conditions must be met if an energy services provider (abbreviated below to "the provider") is to be treated as incurring expenditure on fixtures so as to be able to claim allowances:

- there must be a formal energy services agreement (see below);
- the provider must, under the terms of that agreement, incur capital expenditure on plant or machinery;
- at the time the plant or machinery becomes a fixture, the client must have an interest in the relevant land, but the provider must have no such interest;
- the asset in question must not be provided for leasing;
- it must not be provided for use in a dwelling-house;
- the operation of the plant or machinery must be carried out "wholly or substantially" by the provider or by a person connected with him;
- the provider and the client must not be connected persons;
- the client would (normally, but see below) have been entitled to claim allowances under CAA 2001, s. 176 were it not for the election; and
- the two parties must elect for these rules to apply.

The time limit for submitting the election is, for corporation tax purposes, two years from the end of the chargeable period in which the

capital expenditure is incurred. For income tax purposes, the deadline is the normal self-assessment deadline for amending a return for the tax year in which the chargeable period ends (i.e. 31 January some 22 months after the end of that tax year).

An election is normally possible only if the client would have been entitled to allowances under s. 176 ("Person with interest in relevant land having fixture for purposes of qualifying activity": see **10.5.2**); the allowances for the provider are then given in lieu of the allowances that would have been due to the client. However, this requirement does not apply if the plant or machinery belongs to a class specified by Treasury order.

Definition of "energy services agreement"

An energy services agreement is defined to mean an agreement between the provider and another person "with a view to saving energy or using energy more efficiently". The agreement must cover all of the following:

- the design of plant or machinery, or one or more systems incorporating plant or machinery;
- obtaining and installing the plant or machinery;
- the operation and maintenance of the plant or machinery; and
- the amount of any payments in respect of the operation of the plant or machinery to be linked (wholly or in part) to energy savings or increases in energy efficiency resulting from the provision or operation of the plant or machinery.

Law: CAA 2001, s. 175A, 180A
Guidance: CA 23150

10.5.5 Purchasers of land with fixtures

This is the category that applies most frequently. It covers an ordinary purchase of a commercial property, where:

- plant or machinery has become a fixture;
- a person thereafter acquires an interest in the relevant land (which must exist before the purchaser acquires it, so the granting of a new lease is not covered under this section, though the assignment of an ongoing leasehold interest from one tenant to another would be);
- the amount paid by the purchaser for the interest is, or includes, a capital sum; and

- that capital sum falls to be treated as expenditure on the provision of a fixture.

Where these conditions are met, there is a disposal of the fixtures by the vendor and an acquisition by the new owner. Subject to various conditions, the new owner can then claim allowances on an amount paid for the fixtures in the property. Determining that amount can be straightforward (where an election is made) or complicated (where a valuation apportionment is needed), and the rules were subject to important changes in FA 2012.

Prior right

The new owner is not, however, entitled to claim allowances to the extent that someone else has a prior right to the allowances. A person will have a prior right if he owns the fixture immediately before the property sale, and makes a claim for capital allowances. HMRC have illustrated the point as follows:

HMRC example

Xanadu Properties Plc owns the freehold of Kane House, an office block, which it leases to its tenant, Budokan Computers. Xanadu Properties Plc installs central heating before it leases Kane House to Budokan computers and claims PMAs on the central heating. Budokan Computers installs air conditioning on which it claims PMAs. After the air conditioning has been installed in Kane House, Budokan assigns its lease to Shangri-la Software for a capital sum.

After the assignment of the lease Shangri-la Software can claim PMAs on the air conditioning but not on the central heating. Xanadu Properties Plc has the freehold interest in the relevant land (Kane House) and a prior right in relation to the central heating. The air conditioning is different. Budokan computers had a leasehold interest in the relevant land for the air conditioning when they installed it and they no longer have it after the assignment of the lease. Shangri-la Software has acquired that interest.

In other words, it is important when acquiring a tenanted property – whether from the landlord or the tenant – to be clear about which parties have a right to claim allowances on which fixtures. This will in turn determine the expenditure on which the buyer can claim allowances. In addition to the split between landlord and tenant, as illustrated in the HMRC example immediately above, it is possible that there will be integral features for which neither party has been able to make a claim.

These rules are subject to transitional provisions if the purchase of the interest in the land was before 24 July 1996 (Sch. 3, para. 34).

Law: CAA 2001, s. 181, 562
Guidance: CA 26250

10.5.6 Purchaser of land discharging existing obligations

A person acquiring land may take on the legal liability for an equipment lease; HMRC give the example of a lift that is leased to a trading company. If the new owner pays a capital sum to discharge the obligations under the equipment lease, the fixture is treated as belonging to the person as a consequence of that payment. Plant and machinery allowances can then be claimed accordingly.

Once more, this is subject to the question of whether another person has a prior right.

Equivalent rules apply where the new owner discharges obligations under an energy services agreement.

These rules are subject to transitional provisions if the purchase of the interest in the land was before 24 July 1996 (Sch. 3, para. 35).

Law: CAA 2001, s. 182, 182A
Guidance: CA 23150, 26300

10.5.7 Incoming lessees – overview

An incoming tenant (lessee) may incur capital expenditure (a lease premium) on land that contains fixtures. Where the necessary conditions are met, the tenant may be treated as the owner of the fixtures for the purposes of claiming capital allowances. The intention of the legislation is therefore to resolve the question of who is entitled to claim where two (or more) persons have an interest in the land.

Section 183 deals with the position where (broadly) the lessor is entitled to claim allowances. See **10.5.8** below.

Section 184 covers the situation where the lessor is not entitled to claim. See **10.5.9** below.

In practice, the distinction is less clear cut, as explained in the commentary that follows.

Where the transaction does not involve the granting of a new lease, but is rather the sideways assignment of an existing lease, different rules apply – see **10.5.10** below.

Finally, see **10.5.11** below for a complex worked example involving various different transactions.

Law: CAA 2001, s. 183-184

Guidance: CA 26350