

Real Estate Matters

Issue 18



Construction & Real Estate Newsletter
April 2021

Now, for tomorrow





Introduction



Welcome to the latest issue of Real Estate Matters from MHA.

This is the second issue this year and, in many ways, things have not changed much for the sector, although the speed of vaccinations is giving us all hope of a summer holiday somewhere in the UK. One wonders if we could become like France where the whole country will close down in August, due to accumulated holiday entitlements.

We had a budget in March and the general feeling was that this was supportive. The furlough scheme, although not being extensively used, still helps as does the ability of firms to extend the repayment of VAT, deferred a year ago.

The budget gave the house builders continued support with the decision to spread the withdrawal of stamp duty reliefs over 12 months. The 95% government backed mortgage, if used sensibly, should maintain a stimulus for the market as a whole. In this issue we give analysis of the capital allowance claims that are available, including the super deduction for capital expenditure has caused mixed views. However, no one can deny there is an opportunity to get additional tax relief which may tip potential projects into being. In practice, the 50% special rate pool may produce wider benefits.

We also reflect on HMRC's obvious need to fund the deficit arising from the financial support that has been put in place. We identify tax compliance as an area of risk and also draw your attention to a few areas where legislation has changed.

Government is playing a part and its commitment to infrastructure with the extension of HS2 being approved along with other schemes. The introduction of freeports appears to provide many opportunities for the sector and we have written an article reflecting on how this could be a positive step for many business and investors.

If there are any topics within this issue you would like further information on, please do get in touch.

MHA Construction & Real Estate team

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key points from the Budget 2021

1



Investment into Innovation

A “super deduction” in tax for companies for the next 2 years that invest in plant and machinery.

2



Corporation Tax

Corporation tax on company profits to rise from 19% to 25% in April 2023. Rate to be kept at 19% for companies with profits up to £50k and gradually increases to the full rate at £250k.

3



VAT Cut

VAT cut for hospitality firms to be maintained at 5% until September. An interim 12.5% rate to apply for the following six months.

4



Covid-19 Support

A new COVID recovery loan scheme launched offering 80% guarantees by the government. To replace the Bounceback and other coronavirus loans for businesses.

5



Furlough Scheme Extension

Furlough to be extended until the end of September, and employers will be asked to contribute 10% in July and 20% in August and September.

6



Introduction of Freeports

Locations of 8 new freeports to make it easier and cheaper to do business.

7



Stamp Duty

Up-to-£500,000 “nil-rate band” for stamp duty will be extended until the end of June, with a phasing out of the relief until 1st October.

8



Skills & Training

A new set of UK schemes called “Help To Grow” to include management training, plus training small businesses in digital skills.

9



Retail, Leisure & Hospitality

Restart Grants for retail and non-essential businesses in April of up to £6k per premises, and for leisure and hospitality of up to £18k.

10



Arts & Culture

£400m to help arts venues in England, including museums and galleries re-open.

Capital Allowances following the 2021 Budget

Rishi Sunak, after announcing that the main rate of corporation tax was increasing to 25% with effect from 1 April 2023, then announced a “super-deduction” of 130% for qualifying plant and machinery additions to reward companies for investing over the next two years.

This will apply to expenditure incurred by companies from 1 April 2021 to 31 March 2023, but there is a notable exclusion for expenditure where the contract was entered into prior to 3 March 2021 (to exclude already committed investment from the relief).

Qualifying plant & machinery is:

- 1 Not used or second hand
- 2 Not a car
- 3 Not a long life asset
- 4 Not an asset for leasing (we expect HMRC to release further guidance on how this impacts property investors)
- 5 Not for use in a ring fence trade
- 6 Not special rate expenditure

For special rate expenditure (e.g. thermal insulation, solar panels, integral features - electrical/lighting/cold water/space or water heating/ventilation systems - and lifts / escalators / external solar shading), there will instead be a 50% first year allowance.

The Annual Investment Allowance will still be available (£1m for 2021 reducing to £200k from 1 January 2022) so this is likely to be used against special rate expenditure first to obtain a 100% deduction.

The super-deduction is not capped, but the rate is reduced (to a minimum of 100%) where the accounting period ends after 31 March 2023 and there are provisions to claw back the relief if a quick sale of the plant and machinery takes place. Proceeds are also taxed as balancing charges no matter when disposal takes place so in some cases it could be worth disclaiming the super deduction (where the asset will have a high residual value).

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Is the super-deduction really that super?

The real logic behind the super-deduction is to stop companies delaying investment decisions until the 25% corporation tax rate comes in. This is why it is only available to companies.

Without the super deduction an investment made today would actually cost a company more in real “cash tax” terms than one made in 2023. This can be illustrated with a simple example of a company investing £750k on 1 April 2021 and depreciating the asset over 5 years:

	31 March 2022	2023	2024	2025	2026	Total
Capital Allowances (AIA)	(750,000)	0	0	0	0	(750,000)
Depreciation	150,000	150,000	150,000	150,000	150,000	750,000
Tax Adjustment	(600,000)	150,000	150,000	150,000	150,000	0
Tax Cost / (Saving) @ 19%	(114,000)	28,500	0	0	0	(85,500)
Tax Cost / (Saving) @ 25%			37,500	37,500	37,500	112,500
Total Tax Cost						27,000

	31 March 2022	2023	2024	2025	2026	Total
Capital Allowances (Super-Deduction)	(975,000)	0	0	0	0	(975,000)
Depreciation	150,000	150,000	150,000	150,000	150,000	750,000
Tax Adjustment	(825,000)	150,000	150,000	150,000	150,000	(225,000)
Tax Cost / (Saving) @ 19%	(156,750)	28,500	0	0	0	(128,250)
Tax Cost / (Saving) @ 25%			37,500	37,500	37,500	112,500
Total Tax (Saving)						(15,750)

If businesses can see an investment costs more in real terms today than it does in two years' time, many will defer the investment.

The super-deduction is only really super if you invest early for expenditure incurred after 31 March 2021 (to increase the amount of depreciation added back at 19%) and once the super-deduction ends then businesses should expect to get 100% relief in the normal way through AIA and 18% allowances as allowances and depreciation will match off.

If you are a small company and will continue to benefit from the 19% rate of tax, then it really is a super-deduction.

Freeports



The introduction of 8 Freeport areas within England was a key policy announcement in the recent budget and one which the Chancellor has long since been a proponent of. It is also anticipated that a Freeport area will be established within each of Northern Ireland, Scotland and Wales, in due course.

The concept of Freeports however is neither new nor novel, with a total of 7 existing in the UK between 1984 and 2012.

The government is clearly signalling its assessment that each named location has strong investment potential. In the meantime, the policy aims to achieve three goals:

- 1** Generate national hubs, for global trade and investment across the UK.
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- 2** Promote regeneration and job creation.
.....
- 3** Create hotbeds for innovation.

What are Freeports?

The current incarnation of a Freeport is a region containing an approved port (air, rail or sea) where normal tax and customs rules do not apply. As an example, the announced Teesside Freeport will be the largest in the UK, covering 4,500 acres, including Teesworks, the Port of Hartlepool, Wilton International, Teesside International Airport, the Port of Middlesbrough, LV Shipping and PD Ports.

On receipt at a freeport, imports can enter with simplified customs documentation and without paying customs tariffs. Companies who operate inside the designated freeport area can store or manufacture using the imported goods before exporting again without ever being subject to customs tariffs or import procedures in the UK.

It is only if the imported goods move out of the freeport zone and into another part of the UK that they will be subject to full import declarations and payment of any customs duties.

Usually, a freeport is designed specifically to encourage companies in high-tariff jurisdictions, that import, process and then re-export goods, but the focus of the current initiative also encompasses more general business support and regeneration objectives.

This will benefit those areas as it is expected there will be movement of manufacturing and warehousing into these zones to minimise their customs obligations and take advantage of UK tax reliefs that have been announced in the Budget.

What are the benefits for Businesses?

One of the benefits of operating within a Freeport is that a company can store goods without the need for a customs warehouse authorisation. This reduces costs and administrative burden but would likely require links to the Freeport's inventory system.

Freeports will be particularly attractive to those businesses that import goods which attract a high Customs tariff, for example, textiles and footwear as well as food products, and which are processed in some minor way before being sold on to the EU. The use of a Freeport will avoid a double customs duty hit without having to use expensive Customs Warehousing regimes.

The addition of a Tax Site within the Freeport creates other attractive benefits for businesses:

- An enhanced 10% rate of Structures and Buildings Allowance
- An enhanced capital allowance of 100%
- Full relief from Stamp Duty Land Tax
- Full Business Rates relief
- The government also intends to allow an employer National Insurance contributions relief

What are the benefits for the sector?

It is primarily these tax breaks which will attract international investors and create the thousands of jobs for the supply chain, construction, and service sectors. It is hoped that business investment which otherwise would have been injected into mainland Europe will instead flow in to one of the 8 Freeports, helping to achieve the political promise of levelling up economic activity and prosperity across the country.

Sustainable and expanding businesses tend to operate in areas where there is adequate infrastructure and transport. Ensuring these areas are swiftly addressed appears to represent a path towards the long-term success of this policy, perhaps more so than any upfront or shorter term tax breaks.

Ensuring that such development is expedited should therefore be at the forefront of all stakeholders' minds. Streamlining the planning process using planning freedoms will assist, providing a strong signal of certainty that developments will indeed proceed as promised. As a consequence construction and infrastructure projects become both more attractive and plentiful, increasing opportunities for all in the wider supply chain.

A further avenue for our sector is the likely requirement for increased housing provision. If Freeports successfully achieve the desired levels of investment, they will also become a honey pot to families attracted by enhanced employment opportunities. This will not be a blanket issue and the housing deficit will obviously be more acute in the vicinity of certain Freeport areas.

There appears to be real potential for both housing associations and residential housing developers to thrive, if part of a wider joined up strategy, driven by local authorities. The government also notes that Local Development Orders, or other zonal planning regulations, could assist such housing stock delivery.

There will undoubtedly be scrutiny over the green credentials of Freeport areas. Some business leaders believe they could help the country meet its '2050 net zero' climate obligations, through reduced carbon emissions. This will be realised via the application of new technology, implementing sustainable modes of transport and using decentralised zero-carbon energy generation. The latter two points in particular will require a significant investment in new infrastructure that should provide bountiful opportunities to those forward-thinking operations within our sector.

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Such innovation will present challenges for those involved in the construction of a Freeport and the surrounding infrastructure. Many of our clients used the Covid-19 pandemic to accelerate the adoption of new technology and we see the ensuing sector activity within Freeport areas as something which will further this shift.

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These technical challenges will also provide an opportunity for those involved to be able to consider whether they undertake qualifying Research & Development (R&D) activity which will result in additional tax breaks. For a small and medium sized business an additional deduction of 130% of qualifying R&D costs can be claimed resulting in a net tax benefit of 24.7%. For large businesses, the benefit is reduced however a tax credit of 13% of the qualifying R&D expenditure is available.

An update on some common issues and considerations

HMRC Construction Industry Scheme



Background

Businesses required to operate CIS are either "Mainstream" or "Deemed" Contractors

A Mainstream contractor is any business carrying on a business which includes construction operations, irrespective of construction turnover

A Deemed contractor is any business with an average annual expenditure on construction operations >£1m over last 3 years. This continues until their expenditure on construction operations averages <£1m in each of three successive years

A business can be a Subcontractor to another Contractor or Customer as well as a Contractor engaging its own Subcontractors.

All businesses involved in CIS must register with HMRC in order to gain their own Verification status to ensure they can be paid by their Contractor/Customer and to be able to operate CIS on payments to their Subcontractors.

Where a Contractor pays Subcontractors a Monthly CIS return will need to be completed to account for payments to Subcontractors and any tax deducted, similar to PAYE. Any tax deducted from Subcontractors is paid to HMRC with the monthly PAYE tax and NIC payments, even though the monthly CIS return is separate to the PAYE RTI filings.

Changes from 6th April 2021:

1 CIS set-off amendment power

A new power will be introduced to allow HMRC to amend the CIS deduction amounts claimed by sub-contractors on their Real Time Information (RTI) Employer Payment Summary (EPS) returns.

It will apply where employers do not provide evidence of eligibility and/or evidence of the sums deducted, and do not correct their EPS at HMRC's request, new power allows HMRC to:

- correct errors or omissions relating to claims,
- remove claims, and
- prevent certain employers from making further similar claims

HMRC will remove the claim altogether where there is no evidence of any CIS deductions in respect of that company or where the employer is not entitled to set-off in this way and the employer liabilities will be recalculated following the amendment.

Where HMRC has to amend the CIS credit claimed on an EPS, the employer may also be prevented from making further CIS set-offs in the same tax year.

2 Cost of materials

A new measure is being introduced to clarify that it is only where a sub-contractor directly incurs the cost of materials purchased to fulfil a construction contract, that the cost is not subject to deduction under the CIS.

The newly substituted provisions will clarify that:

- On making a contract payment to a sub-contractor, the contractor deducts a sum from the payment which is equal to the relevant percentage of the net payment,
- In calculating the net payment, the contractor must work out the amount of the contract payment less deductible materials costs, and
- A materials cost will only be deductible if it represents the direct cost of materials purchased by a sub-contractor in respect of that particular contract.

3 Deemed contractors

A change to the rules for determining which entities operating outside the construction sector need to operate the CIS ('deemed contractors') is being applied.

Rather than looking back at the end of each year end to determine the level of construction expenditure these businesses will need to monitor that expenditure more regularly and apply the CIS when construction expenditure exceeds £3 million within the previous rolling 12 months period.

Where average annual expenditure on construction operations exceeds £1 million in each of the last 3 years,

the business has to operate CIS on any construction expenditure from the start of the next period of account. The new rules will require a business to monitor construction expenditure more regularly.

4 CIS registration penalty

This change expands the scope of the penalty for supplying false information when applying for gross payment status (GPS) or payment under deduction within the CIS.

Individuals and companies will now be liable to a penalty if they are in a position to exercise influence or control over the person making the application, and either encourages that person to make a false statement or supply a false document in support of that application; or where they themselves make a false statement or supply a false document for the purpose of enabling another person to register for GPS or payment under deduction.

Currently the penalty for providing false information when registering applies only to the individual or business to whom the registration applies.

It will now apply to a wider group of individuals or companies who are able to exercise influence or control over a person who is registering for the CIS, this will include agents, directors, company secretaries, or anyone HMRC believes is in a position to exercise influence and control over the business and/or the person making the CIS registration.

National Minimum Wage/National Living Wage (NMW/NLW)

Changes from 1st April 2021:

	23 and over	21 to 22	18 to 20	Under 18	Apprentice
April 2021 (new rate)	£8.91	£8.36	£6.56	£4.62	£4.30
April 2020 (current)	£8.72	£8.20	£6.45	£4.55	£4.15

Annual Tax on Enveloped Dwellings (ATED)

In 2013, the Annual Tax on Enveloped Dwellings (ATED) was introduced, which needs to be considered by companies that own UK dwellings worth over £500k.

This tax also applies to partnerships including one or more corporate partners, and to collective investment schemes. The taxpayer is required to file an ATED return within 30 days of acquisition of such a dwelling and then each year thereafter by 30 April.

Where the ATED tax charge is due, the amount depends on the band into which the value of the dwelling falls. The amounts change each year. ATED charges for the year ending 31 March 2022 will be falling due by 30 April 2021.

The amounts for 2021/2022 are as follows:

Property Value	Annual Charge
More than £500,000 up to £1 million	£3,700
More than £1 million up to £2 million	£7,500
More than £2 million up to £5 million	£25,300
More than £5 million up to £10 million	£59,100
More than £10 million up to £20 million	£118,600
More than £20 million	£237,400

The tax is charged on dwellings. A dwelling is an individual residential property unit, subject to certain exceptions. Non-residential properties are not within the charge to ATED.

There are various reliefs which can be claimed against ATED liabilities, in the following situations:

- Property rental businesses,
- Dwellings opened to the public,
- Property developers,
- Property traders,
- Financial institutions acquiring dwelling in the course of lending,
- Regulated home reversion plans,
- Dwellings occupied by certain employees,
- Farmhouses, or
- Registered providers of social housing.

If one of the reliefs is available, it needs to be claimed each year in a return, even if there is no ATED to pay.

Penalties are charged for late filing of returns and further penalties and interest are charged for late payment of the tax. In all cases where residential property worth £500k or more is acquired by a company, a corporate or mixed partnership, or a collective investment scheme, the potential ATED exposure and compliance obligations should be considered very carefully.



Tax Risk Management

The government has been borrowing heavily to support the economy throughout the pandemic, and it will be no surprise to anyone that this debt must be reduced over time. As the economy starts to recover, it is likely that there will be an increasing focus on corporate tax, income tax and indirect taxes, such as VAT and customs duty, to raise tax receipts.

There may be changes in the rates of tax that apply to help increase receipts, particularly where rates have been temporarily reduced during the pandemic. But given the current inability for many businesses to bear an increased tax burden, the need to maintain the UK as an attractive place to do business, and the inflationary impact that increases in transaction taxes have, a more likely approach will be to focus on perceived "tax gaps" to maximise revenue.

That this is to be the focus is evident from the recent budget. There were no overt statements made in the budget, but it was announced that the government is to invest a further £180m in HMRC over the course of the next year. This is to allow HMRC to recruit additional staff and invest in new technology, and the expectation is that this will yield more than £1.6 billion in additional tax revenue over the next four to five years. This will not be through new taxes or increasing tax rates, but purely by collecting existing taxes that would otherwise remain unpaid. It seems clear that there will be an increasing emphasis by HMRC, through more rigorous audit processes, to make sure taxpayers are fully compliant, and to impose stiffer penalties on those that are not.

In light of this, the key for all businesses should be to put in place the necessary processes and controls to ensure that the correct amount of tax is being reported and paid at the correct time.

This does typically require work to be undertaken and is not something that will look after itself. Mapping out processes, putting in place effective controls, assigning clear roles and responsibilities with escalation protocols, and then testing the framework periodically to make sure it is working are needed. Somebody in the business needs to champion this. Most importantly, the business as a whole needs to buy in and understand the impact that poor tax compliance could have – paying too much tax too soon, or not enough and then receiving large penalties on assessment can quickly erode margins, and dent stakeholder confidence.

By focusing on its tax compliance processes now, a business will be in a position to effectively manage its tax risk and avoid costly tax errors arising. Having a robust tax framework in place will help you not only avoid unnecessary tax costs, but also gain better visibility over your tax position, and allow you to drive tax efficiencies through your business.

House price growth

The Office for National Statistics (ONS) has released a public statement on the coronavirus (COVID-19) and the production of statistics; Section 7: Measuring the data describes the situation in relation to the UK House Price Index (HPI).

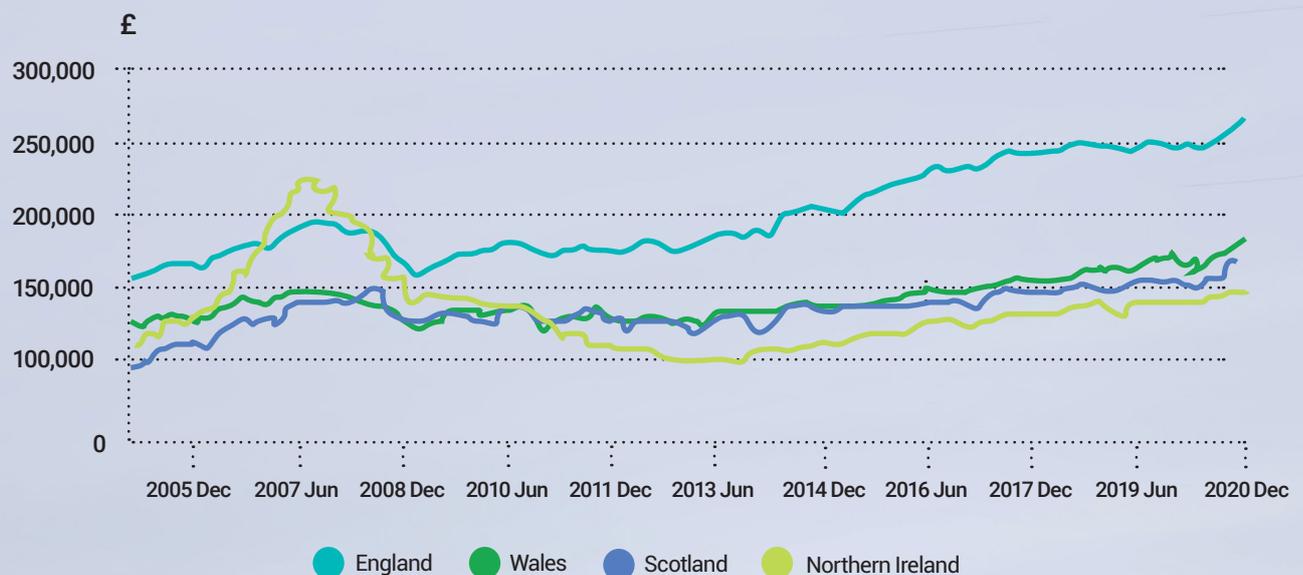
UK average house prices increased by 7.5% over the year to January 2021, down from 8.0% in December 2020.

Average house prices increased over the year in England to £267,000 (7.5%), in Wales to £179,000 (9.6%), in Scotland to £164,000 (6.9%) and in Northern Ireland to £148,000 (5.3%).

The North West was the English region which saw the highest annual growth in average house prices (12.0%), while the West Midlands saw the lowest (4.7%).

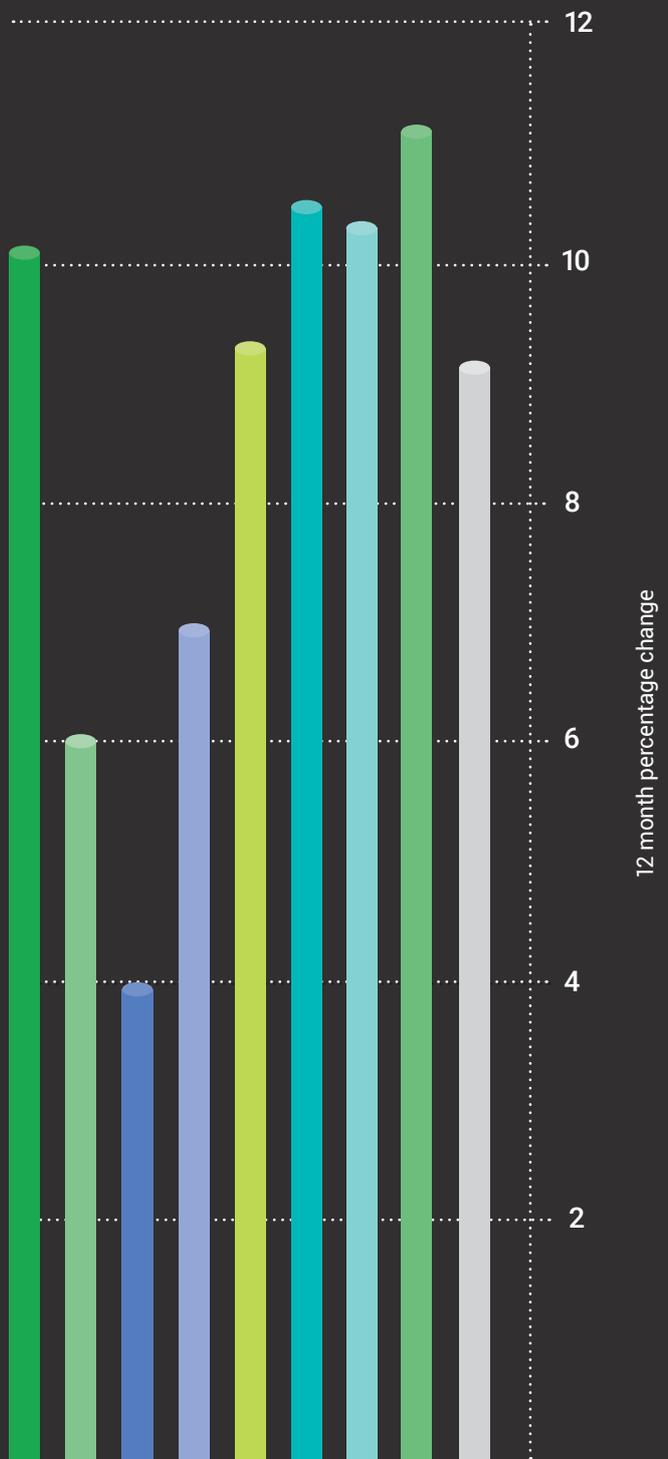
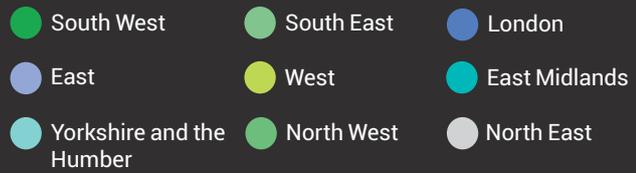
England house prices remain the highest in the UK

Average house price by country, UK, January 2005 to December 2020



The highest regional house price growth was in the North West

All dwellings annual house price rates of change, by English region, year to December 2020



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MHA Construction & Real Estate Team



Our Construction & Real Estate experts understand the challenges and opportunities within the sector, which remains a vital part of the UK economy.

A national Construction & Real Estate team with local specialists that understand the sector in your area.

Our service is partner-led and we aim to build a strong working relationship with you to understand your business and goals.

We have a wealth of experience in providing professional advice to a diverse range of clients within the property and real estate arena, including commercial and residential investment, facilities management, developers, and property-related service providers.

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A wide range of tailored services: assurance, tax, compliance, advisory, training and more, delivered with practical understanding.

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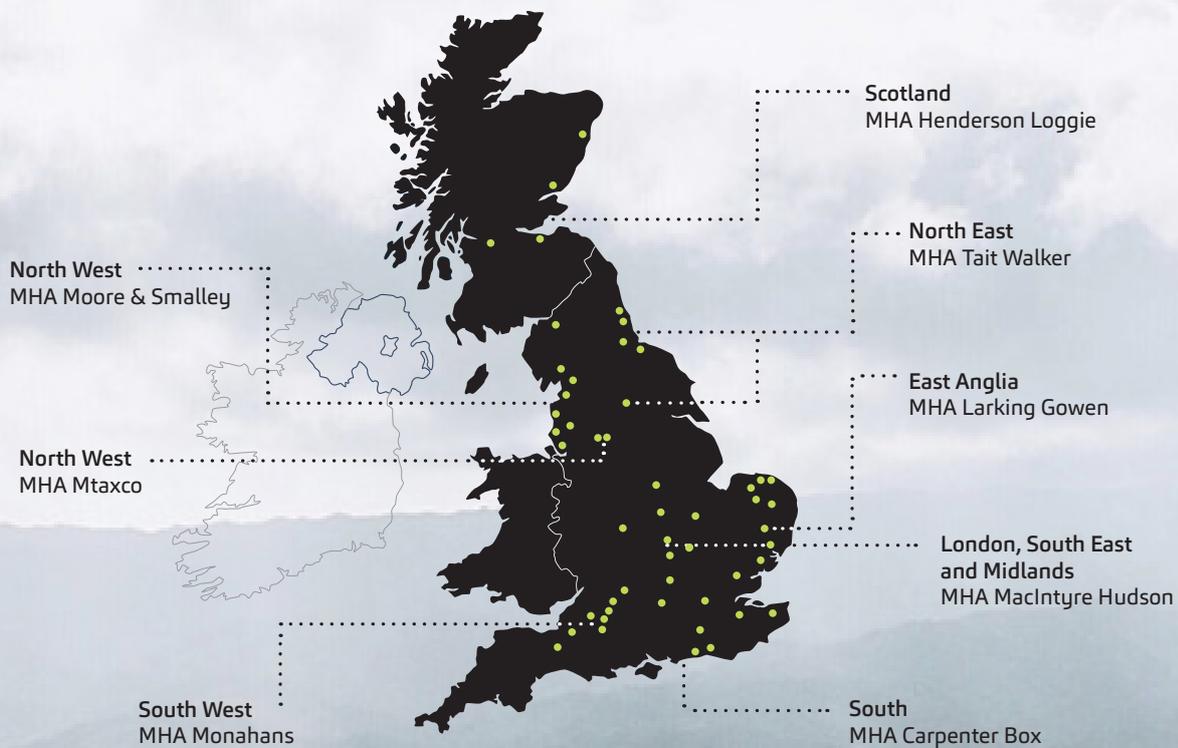
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About MHA

MHA is an association of progressive and respected accountancy and advisory firms with offices in over 50 locations across the UK. We provide both national expertise and local insight to clients. As an independent member of Baker Tilly International, a top 12 global advisory network, MHA offers clients unparalleled access to a broad range of in-country international specialists where overseas projects are on the horizon.

Our Sector Approach

MHA allows clients to benefit from in depth sector knowledge in addition to specialist accountancy services and expert business advice. Construction and Real Estate is a key sector for MHA, and our industry experts understand the challenges and opportunities within the sector. With MHA's sector experience, and local, national and international knowledge, our team is well placed to provide leading advice.



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