

*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 12: Supplementary provisions

Chapter 2: Additional VAT liabilities and rebates: interpretation, etc.

Overview

1900. This Chapter provides the interpretation for the provisions in Parts 2, 3 and 6 dealing with additional VAT liabilities and rebates. It is based on section 159A of CAA 1990.
1901. These provisions apply if taxpayers are required to make adjustments under the VAT capital items legislation (commonly known as the capital goods scheme) which is dealt with in regulations 112 to 116 of [VAT Regulations 1995 \(SI 1995/2518\)](#)).

Background

1902. The capital goods scheme is relevant to businesses that, under VAT legislation, make both exempt and non-exempt supplies. These traders are known as “partially exempt traders”. When a VAT-registered business incurs VAT on its purchases (input tax), it can usually offset these amounts against the tax it owes to HM Customs & Excise on its sales (output tax). However, partially-exempt businesses are not able to do so in respect of purchases attributable to exempt sales (or “supplies”).
1903. Generally with VAT, the rules for capital expenditure do not differ from the rules for revenue items. However, the capital goods scheme is an exception. For certain types of capital expenditure, it is necessary for partially-exempt businesses to make an annual adjustment over a period of five or ten years so that the reclaimable input tax reflects the proportion of use attributable to the making of non-exempt supplies during the period.
1904. The types of expenditure covered by the scheme can be broadly divided into three categories:
- computers or computer equipment worth £50,000 or more;
 - land and buildings worth £250,000 or more; and
 - building works worth £250,000 or more.

Adjustments are made over a five-year period in respect of the first category; and they are made over a ten-year period in respect of the other categories.

1905. It is a general principle of income tax and corporation tax that any non-recoverable VAT should be relieved as a cost for direct tax purposes. When the capital goods scheme was introduced in 1990, it became necessary to ensure that the capital allowances provisions could cater for VAT adjustments made under the Scheme so far as they

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related to expenditure covered by CAA 1990. The legislation to do this was introduced in FA 1991. And to simplify matters, the legislation was only introduced to cover cases in which the original expenditure was covered by the rules for plant and machinery allowances, industrial buildings allowances or R&D allowances.

1906. Broadly under these rules, if a taxpayer incurs an additional VAT liability (because the proportion of exempt use has risen) then the additional VAT liability is treated as additional capital expenditure incurred. And if a taxpayer receives an additional VAT rebate (because the proportion of exempt use has fallen) then the taxpayer is treated as receiving disposal proceeds equal to the amount received. However, the rules differ between the various Parts. This reflects the different schemes for allowances and charges under these Parts.

Section 546: Introduction

1907. This section is new and introduces the Chapter.

Section 547: “Additional VAT liability” and “additional VAT rebate”

1908. This section is based on section 159A(6) of CAA 1990. It provides a definition of the terms “additional VAT liability” and “additional VAT rebate”.

Sections 548 and 549: Time when additional VAT liability or rebate is incurred, made, accrues etc.

1909. These sections are based on section 159A of CAA 1990. They determine when additional VAT liabilities and rebates are treated as arising.
1910. Section 159A(1) to (4) of CAA 1990 determines when additional VAT liabilities and rebates are treated as arising for the purposes of CAA 1990. It is clear that such rules are necessary to ensure that calculations of allowances and charges reflect the additional VAT liabilities and rebates in the correct chargeable periods.
1911. The legislation, however, provides two different sets of rules to determine the time an additional VAT liability or rebate is treated as arising. One of these sets of rules is applied when determining in which chargeable period a liability or rebate is to be brought into account (or for which chargeable period an allowance or charge is to be made under the 1990 Act). The other set of rules is used in all other circumstances. In particular, it is used when the legislation requires certain conditions to be met at the time when the additional VAT liability or rebate arises.
1912. However, there are instances in which the same terminology is used with two different meanings in the same sentence. This Act has removed this obstacle to the understanding of the rules and uses two different labels to refer to the two different sets of rules.
1913. The time, determined in CAA 1990 by section 159A(1) and (2), is now referred to as the time when the additional VAT liability is incurred or the additional VAT rebate is made. This is the meaning that applies in all cases except when determining the chargeable period in which a liability or rebate is to be brought into account (or for which chargeable period an allowance or charge is to be made under the 1990 Act). This is dealt with in section 548.
1914. The time, determined in CAA 1990 by section 159A(3) and (4), is now referred to as the time when the additional VAT liability or rebate accrues. This is dealt with in section 549. This time will generally be later than the time determined in section 548.
1915. One advantage of using the later time in the legislation is to ensure that the appropriate capital allowances calculations do not generally need to be made until after the adjustment has been calculated for VAT purposes.

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1916. Section 159A(4) of CAA 1990 may appear to determine only the chargeable period in which the additional VAT liability or rebate arises (or in the language of the new Act “accrues”). But CAA 1990 requires in various provisions the time (rather than just the chargeable period) in which the additional VAT liability or rebate accrues. This Act provides this. See *Note 70* in Annex 2.

Section 550: Apportionment of additional VAT liabilities and rebates

1917. This section is based on section 159A(5) and part of section 159A(7) of CAA 1990. It deals with cases in which it is necessary to apportion either the qualifying expenditure or the allowances or charges arising.
1918. In such cases, any additional VAT liability or rebate is subject to the same apportionment.

Section 551: Supplementary

1919. This section is based on section 159A(6) and part of section 159A(7) of CAA 1990. It provides definitions of terms used in the Chapter.