

*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 3: Industrial buildings allowances

Chapter 7: Balancing adjustments

Overview

1064. This Chapter provides for balancing adjustments. These are made on the occurrence of certain events, referred to in this Part as balancing events. A balancing adjustment is either a balancing allowance or a balancing charge.
1065. [Section 314](#) provides for balancing allowances and charges. It also provides that no balancing adjustment is made if a balancing event occurs more than 25 years after first use of the building.
1066. [Section 315](#) sets out the main balancing events and points to provisions which provide other balancing events.
1067. [Section 316](#) identifies the proceeds from balancing events.
1068. [Section 317](#) provides one of the other balancing events mentioned in section 315. It applies if a hotel has ceased to be a qualifying hotel (see section 279) for more than two years.
1069. [Sections 318 to 320](#) state the general rules for calculating a balancing adjustment. The calculation differs according to whether or not the building was used as an industrial building, or for R&D, throughout a person's relevant period of ownership.
1070. [Section 318](#) provides the rule if the building has been so used throughout.
1071. [Section 319](#) provides the rule if a building has not been in such use throughout.
1072. [Section 320](#) limits the amount of a balancing charge to the total allowances made.
1073. [Sections 321 to 324](#) define terms used in section 319.
1074. [Sections 325](#) and [326](#) restrict balancing allowances if:
- a sale subject to a subordinate interest is made involving connected persons; or
 - it appears that the main purpose was to obtain an allowance.
1075. [Sections 327 to 331](#) are concerned with expenditure on the construction of buildings in enterprise zones.

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1076. **Section 328** provides that a balancing event occurs if capital value is realised on a building. No balancing allowance is made for such an event. And there are special rules for calculating a balancing charge.
1077. **Section 329** gives the amount of the capital value attributable to a subordinate interest. This amount is treated in section 328 as the proceeds from the balancing event.
1078. **Section 330** provides an exception to section 328. That section does not apply if capital value is realised more than seven years after an agreement was made to incur qualifying expenditure.
1079. **Section 331** defines various terms for the purposes of sections 328 to 330.

Section 314: When balancing adjustments are made

1080. This section is based on section 4(1) and (2) of CAA 1990. It provides balancing adjustments for industrial buildings allowances. A balancing adjustment is made on the occurrence of a balancing event. See section 315.
1081. *Subsection (5)* provides a balancing adjustment only for the first balancing event to happen in a period when a building is not an industrial building. This prevents double allowances or charges.

Section 315: Main balancing events

1082. This section is based on parts of sections 4(1) and 161(2) of CAA 1990. It gives the main balancing events for industrial buildings allowances. It also provides signposts to sections within Part 3 which give additional balancing events.

Section 316: Proceeds from main balancing events

1083. This section is based on section 156 of CAA 1990. It gives the proceeds from four of the main balancing events.

Section 317: Balancing event where hotel not qualifying hotel for 2 years

1084. This section is based on part of section 7(1) and sections 6(3) and 7(2) of CAA 1990. It provides an additional balancing event for what was previously a qualifying hotel. This occurs if for a period of two years it is no longer a qualifying hotel. “Qualifying hotel” is defined in section 279.
1085. *Subsection (1)* sets out the circumstances in which the balancing event arises.
1086. *Subsection (2)* contains provisions for the application of balancing adjustments by treating the event as a sale with proceeds equal to the market value of the building.
1087. *Subsections (3) and (4)* provide that the general rule in section 285 about temporary disuse applies for up to two years in which the building is not a qualifying hotel but not beyond that period.
1088. *Subsection (5)* provides that this section does not apply to qualifying enterprise zone expenditure.

Section 318: Building an industrial building etc. throughout

1089. This section is based on section 4(3) and (4) of CAA 1990. It calculates the balancing adjustment if a building has been an industrial building throughout the relevant period of ownership. “The relevant period of ownership” is defined in section 321.
1090. *Subsection (2)* provides a balancing allowance if there are no proceeds from the balancing event or the proceeds are less than the residue of qualifying expenditure

before that event. “The residue of qualifying expenditure” is defined in section 313. *Subsection (3)* gives the amount of the balancing allowance.

1091. *Subsection (4)* provides a balancing charge if the proceeds from the balancing event are greater than the residue of qualifying expenditure before that event. *Subsection (5)* gives the amount.

Section 319: Building not an industrial building etc. throughout

1092. This section is based on section 4(5), (6), and (7)(a) and (b) of CAA 1990. It calculates balancing adjustments if a building was at some time during the relevant period of ownership not used as an industrial building or for R&D. “The relevant period of ownership” is defined by section 321.

1093. *Subsections (2)* and *(3)* provide a balancing allowance if the proceeds from a balancing event are less than the starting expenditure and the net allowances made are less than the adjusted net cost of the building. “The starting expenditure” is defined in section 322. “Net allowances” is defined in section 324. “Adjusted net cost” is defined in section 323. The amount of the balancing allowance is the difference between the adjusted net cost of the building and the net allowances made.

1094. *Subsections (4)* and *(5)* provide a balancing charge if the proceeds from the balancing event are equal to or greater than the starting expenditure. The proceeds from a balancing event are given by section 316. The amount of the balancing charge is the net allowances made.

1095. *Subsections (6)* and *(7)* provide a balancing charge if the proceeds from the balancing event are less than the starting expenditure (so subsection (4) does not apply) and the net allowances made are more than the adjusted net cost of the building. The amount of the balancing charge is the difference between the net allowances made and the adjusted net cost of the building.

Section 320: Overall limit on balancing charge

1096. This section is based on part of section 4(10) of CAA 1990. It limits the balancing charge that can be made to the amount of the net allowances.

Section 321: The relevant period of ownership

1097. This section is based on part of section 4(9) of CAA 1990. It defines the “relevant period of ownership”. This term is used in sections 318 and 319.

Section 322: Starting expenditure

1098. This section is based on part of section 4(9) of CAA 1990. It defines “starting expenditure” for the purposes of Chapter 7.

1099. *Subsection (2)* makes the starting expenditure equal to qualifying expenditure if the person on whom the balancing adjustment is made is the same person who incurred the qualifying expenditure.

1100. *Subsection (3)* provides that in cases not covered by subsection (2) above the starting expenditure will be the residue of qualifying expenditure at the beginning of the relevant period of ownership. “The residue of qualifying expenditure” is defined in section 313. “The relevant period of ownership” is defined in section 321.

1101. *Subsection (4)* is concerned with cases which fall within section 340. These are cases involving the demolition of a building if the person in respect of whom the balancing adjustment is made also incurs demolition costs. Under this subsection the starting expenditure is increased by “the net cost of the demolition” which is defined in section 340(3).

Section 323: Adjusted net cost

1102. This section is based on part of section 4(9) of CAA 1990. It defines the “adjusted net cost”. It employs the concept of “relevant period of ownership” which is defined by section 321.

Section 324: Net allowances

1103. This section is based on part of section 4(10) of CAA 1990. It defines “net allowances” for the purposes of Chapter 7.

Section 325: Balancing allowances restricted where sale subject to subordinate interest

1104. This section is based on section 5(1), (2), (3) and (5) of CAA 1990. It restricts balancing allowances in two situations involving the sale of the relevant interest in a building which is subject to a subordinate interest:

- *subsection (2)* – if at least two of the three persons involved are connected persons. “Connected persons” are defined in section 575;
- *subsection (3)* – if the sole or main benefit appears to be the obtaining of an allowance under this Part.

1105. *Subsection (4)* provides that in either of these situations the balancing adjustment is calculated with an increase in the net proceeds of the sale.

1106. *Subsection (5)* limits the amount that is added to the proceeds. This prevents subsection (4) imposing a balancing charge.

1107. *Subsection (6)* deals with a variation of the terms on which the subordinate interest is granted prior to the sale of the relevant interest. Anything received in return for that variation is to be treated as a premium under subsection (4). And the rent, if any, is to be taken as the rent payable under the terms applying immediately before the sale of the relevant interest.

1108. *Subsection (7)* provides that the residue of qualifying expenditure after the sale is to be calculated regardless of an adjustment made by this section. “The residue of qualifying expenditure” is defined in section 313.

Section 326: Interpretation of section 325

1109. This section is based on section 5(4) of CAA 1990. It defines terms used in this section and section 325.

Section 327: Capital value provisions: application of provisions

1110. This section is based on parts of section 120(7) and (8) of FA 1994. It introduces the application of sections 328 to 331. These provisions were introduced to prevent abuse of enterprise zone allowances.

Section 328: Balancing adjustment on realisation of capital value

1111. This section is based on sections 4(1)(dd), 4A(1), 5(2A) and (9A)(a) and (b) of CAA 1990. It provides an additional balancing event if capital value is realised in respect of a building which is or has been an industrial building in an enterprise zone. “Capital value” is defined in section 331(1).

1112. *Subsection (2)* prohibits a balancing event within this section from giving rise to a balancing allowance.

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- 1113. *Subsection (3)* provides that the proceeds from the balancing event are to be taken as the amount of capital value realised.
- 1114. *Subsection (4)* provides two special rules for calculating a balancing adjustment when there is a balancing event under this section.
- 1115. *Subsection (5)* provides that capital value is realised if capital value is paid in respect of a subordinate interest in land to which the relevant interest in the building is or will be subject. *Subsection (6)* gives the date that capital value is realised as the date that payment is made.
- 1116. *Subsection (7)* provides that “the amount of capital value realised” in subsection (3) is the capital value that is attributable to the subordinate interest under section 329.

Section 329: Capital value that is attributable to subordinate interest

- 1117. This section is based on section 4A(2), (4), (5), (6) and (8) of CAA 1990. It identifies what capital value is attributable to a subordinate interest.

Section 330: Exception for payments more than 7 years after agreement

- 1118. This section is based on section 4A(7), (11) and (12) of CAA 1990. It provides an exception to section 328 for certain payments made more than 7 years after the agreement to incur qualifying expenditure.
- 1119. *Subsections (1)* and *(2)* set out the circumstances in which the exception applies. And *subsections (3)* and *(4)* set out the circumstances when it does not. The latter are broadly relevant if arrangements are in place which make a disposal certain or substantially more likely.

Section 331: Capital value provisions: interpretation

- 1120. This section is based on section 4A(3), (9), (10) and (13) of CAA 1990. It defines terms used in the capital value provisions.
- 1121. *Subsection (1)* refers to section 34 of ICTA. Section 34 of ICTA provides for certain capital sums paid (for example as premiums under a lease) to be treated as rent or profits in the hands of the landlord.