



# Capital Allowances Act 2001

## 2001 CHAPTER 2

### [<sup>F1</sup> PART 4A

#### FLAT CONVERSION ALLOWANCES

##### Textual Amendments

- F1** Pt. 4A (ss. 393A-393W) inserted (with effect as mentioned in s. 67 of the amending Act) by [Finance Act 2001 \(c. 9\)](#), s. 67, [Sch. 19 Pt. 1](#)

##### Modifications etc. (not altering text)

- C1** Pt. 4A modified (24.2.2003) by [Proceeds of Crime Act 2002 \(c. 29\)](#), s. 458(1), [Sch. 10 para. 22](#) (with [Sch. 10 para. 25](#)); [S.I. 2003/120](#), art. 2, [Sch.](#) (with arts. 34) (as amended (20.2.2003) by [S.I. 2003/333](#), art. 14)
- C2** Pt. 4A (ss. 393A-393W) modified (prosp.) by [Proceeds of Crime Act 2002 \(c. 29\)](#), ss. 448, 458(1), [Sch. 10 para. 22, 25](#)

## CHAPTER 1

### INTRODUCTION

#### **393A Flat conversion allowances**

- (1) Allowances are available under this Part if a person incurs qualifying expenditure in respect of a flat.
- (2) Allowances under this Part are made to the person who—
  - (a) incurred the expenditure, and
  - (b) has the relevant interest in the flat.
- (3) In this Part “ flat ” means a dwelling which—
  - (a) is a separate set of premises (whether or not on the same floor),

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- (b) forms part of a building, and
  - (c) is divided horizontally from another part of the building.
- (4) In this Part “ dwelling ” means a building or part of a building occupied or intended to be occupied as a separate dwelling.

## CHAPTER 2

### QUALIFYING EXPENDITURE

#### **393B Meaning of “qualifying expenditure”**

- (1) In this Part “ qualifying expenditure ” means capital expenditure incurred on, or in connection with—
- (a) the conversion of part of a qualifying building into a qualifying flat,
  - (b) the renovation of a flat in a qualifying building if the flat is, or will be, a qualifying flat, or
  - (c) repairs to a qualifying building, to the extent that the repairs are incidental to expenditure within paragraph (a) or (b).
- (2) Expenditure within subsection (1)(a) or (b) is not qualifying expenditure unless the part of the building, or the flat, in respect of which the expenditure is incurred—
- (a) was unused, or
  - (b) was used only for storage,
- throughout the period of one year ending immediately before the date on which the conversion or renovation work began.
- (3) Expenditure is not qualifying expenditure if it is incurred on or in connection with—
- (a) the acquisition of land or rights in or over land,
  - (b) the extension of a qualifying building (except to the extent required for the purpose of providing a means of getting to or from a qualifying flat),
  - (c) the development of land adjoining or adjacent to a qualifying building, or
  - (d) the provision of furnishings or chattels.
- (4) For the purposes of this section, expenditure incurred on repairs to a building is to be treated as capital expenditure if it is not expenditure that would be allowed to be deducted in calculating the profits of a [F2UK property business or ] Schedule A business for tax purposes.
- (5) Treasury regulations may make further provision as to expenditure which is, or is not, qualifying expenditure.

#### **Textual Amendments**

- F2** Words in s. 393B(4) inserted (with effect in accordance with s. 883(1) of the amending Act) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\)](#), [Sch. 1 para. 559](#) (with [Sch. 2](#))

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## CHAPTER 3

### QUALIFYING BUILDINGS AND QUALIFYING FLATS

#### 393C Meaning of “qualifying building”

- (1) In this Part “qualifying building” means a building in respect of which the following requirements are met—
  - (a) all or most of the ground floor of the building must be authorised for business use,
  - (b) it must appear that, when the building was constructed, the storeys above the ground floor were for use primarily as one or more dwellings,
  - (c) the building must not have more than 4 storeys above the ground floor, and
  - (d) the construction of the building must have been completed before 1st January 1980.
- (2) In subsection (1)(a) “authorised for business use” means—
  - (a) in the case of a building in England or Wales, authorised for use within class A1, A2, A3, B1 or D1(a) specified in the Schedule to the Town and Country Planning (Use Classes) Order 1987;
  - (b) in the case of a building in Scotland—
    - (i) authorised for use within class 1, 2, 3 or 4 specified in the Schedule to the Town and Country Planning (Use Classes) (Scotland) Order 1997,
    - (ii) authorised for a use specified in Article 3(5)(j) of that Order, or
    - (iii) authorised for use for the provision of medical or health services other than from premises attached to the residence of the consultant or practitioner;
  - (c) in the case of a building in Northern Ireland—
    - (i) authorised for use within class 1, 2, 3, 4 or 15(a) specified in the Schedule to the Planning (Use Classes) Order (Northern Ireland) 1989, or
    - (ii) authorised for a use specified in Article 3(5)(b), (c) or (h) of that Order.
- (3) The attic storey does not count for the purposes of subsection (1)(c) unless it is or has been in use as a dwelling or part of a dwelling.
- (4) The requirement in subsection (1)(d) is met even if the building has been extended on or after 1st January 1980, provided any extension was completed on or before 31st December 2000.
- (5) Treasury regulations may make further provision as to the circumstances in which a building is, or is not, a qualifying building.

#### 393D Meaning of “qualifying flat”

- (1) In this Part “qualifying flat” means a flat in respect of which the following requirements are met—
  - (a) the flat must be in a qualifying building,
  - (b) the flat must be suitable for letting as a dwelling,
  - (c) the flat must be held for the purpose of short-term letting,

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- (d) it must be possible to gain access to the flat without using the part of the ground floor of the building that is authorised for business use (as defined in section 393C(2)),
  - (e) the flat must not have more than 4 rooms,
  - (f) the flat must not be a high value flat,
  - (g) the flat must not be (or have been) created or renovated as part of a scheme involving the creation or renovation of one or more high value flats, and
  - (h) the flat must not be let to a person connected with the person who incurred the expenditure on its conversion or renovation.
- (2) In subsection (1)(c) “ short-term letting ” means letting as a dwelling on a lease for a term (or, in Scotland, period) of not more than 5 years.
- (3) For the purposes of subsection (1)(e), the following are ignored in determining the number of rooms in a flat—
- (a) any kitchen or bathroom, and
  - (b) any closet, cloakroom or hallway not exceeding 5 square metres in area.
- (4) For the purposes of this Part, if a flat is a qualifying flat immediately before a period when it is temporarily unsuitable for letting as a dwelling, it is to be treated as being a qualifying flat during that period.
- (5) Treasury regulations may make further provision as to the circumstances in which a flat is, or is not, a qualifying flat.

### **393E High value flats**

- (1) For the purposes of section 393D(1) a flat is a high value flat if the notional rent exceeds the relevant limit set out in the Table in subsection (5).
- (2) The “ notional rent ” means the rent that could reasonably be expected for the flat on the relevant date, on the assumption that, on that date—
- (a) the conversion or renovation has been completed,
  - (b) the flat is let furnished,
  - (c) the lease does not require the tenant to pay a premium or make any other payments to the landlord or a person connected with the landlord,
  - (d) the tenant is not connected with the person incurring the expenditure on the conversion or renovation of the flat, and
  - (e) in the case of a flat in England or Wales or Scotland, the flat is let on a shorthold tenancy.
- (3) The “ relevant date ” means the date on which expenditure on—
- (a) the conversion of part of the building into the flat, or
  - (b) (as the case may be) the renovation of the flat,
- is first incurred.
- (4) “ Shorthold tenancy ” means—
- (a) in the case of a flat in England or Wales, an assured shorthold tenancy;
  - (b) in the case of a flat in Scotland, a short assured tenancy.
- (5) The limit for the notional rent is as shown in the Table—

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TABLE: NOTIONAL RENT LIMITS

Number of rooms in flat	Flats in Greater London	Flats elsewhere
1 or 2 rooms	£350 per week	£150 per week
3 rooms	£425 per week	£225 per week
4 rooms	£480 per week	£300 per week

- (6) Treasury regulations may make provision amending the notional rent limits in the Table in subsection (5).
- (7) Section 393D(3) (determination of number of rooms in flat) applies for the purposes of this section.

## CHAPTER 4

### THE RELEVANT INTEREST IN THE FLAT

#### **393F General rule as to what is the relevant interest**

- (1) The relevant interest in a flat in relation to any qualifying expenditure is the interest in the flat to which the person who incurred the expenditure was entitled when it was incurred.
- (2) Subsection (1) is subject to the following provisions of this Chapter and to section 393V (provisions applying on termination of lease).
- (3) If—
- the person who incurred the qualifying expenditure was entitled to more than one interest in the flat when the expenditure was incurred, and
  - one of those interests was reversionary on all the others,
- the reversionary interest is the relevant interest in the flat.
- (4) An interest does not cease to be the relevant interest merely because of the creation of a lease or other interest to which that interest is subject.
- (5) If—
- the relevant interest is a leasehold interest, and
  - that interest is extinguished on the person entitled to it acquiring the interest which is reversionary on it,
- the interest into which the leasehold interest merges becomes the relevant interest when the leasehold interest is extinguished.

#### **393G Interest acquired on completion of conversion**

- For the purposes of determining the relevant interest in a flat, a person who—
- incurs expenditure on the conversion of part of a building into the flat, and
  - is entitled to an interest in the flat on or as a result of the completion of the conversion,
- is treated as having had that interest when the expenditure was incurred.

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## CHAPTER 5

### INITIAL ALLOWANCES

#### **393H Initial allowances**

- (1) A person who has incurred qualifying expenditure in respect of a flat is entitled to an initial allowance in respect of the expenditure.
- (2) The amount of the initial allowance is 100% of the qualifying expenditure.
- (3) A person claiming an initial allowance under this section may require the allowance to be reduced to a specified amount.
- (4) The initial allowance is made for the chargeable period in which the qualifying expenditure is incurred.

#### **393I Flat not qualifying flat or relevant interest sold before flat first let**

- (1) No initial allowance is to be made under section 393H if, at the relevant time, the flat is not a qualifying flat.
- (2) An initial allowance which has been made in respect of a flat which is to be a qualifying flat is to be withdrawn if—
  - (a) the flat is not a qualifying flat at the relevant time, or
  - (b) the person to whom the allowance was made has sold the relevant interest in the flat before the relevant time.
- (3) All such assessments and adjustments of assessments are to be made as are necessary to give effect to this section.
- (4) In this section “ the relevant time ” means the time when the flat is first suitable for letting as a dwelling.

## CHAPTER 6

### WRITING-DOWN ALLOWANCES

#### **393J Entitlement to writing-down allowances**

- (1) A person is entitled to a writing-down allowance for a chargeable period if he has incurred qualifying expenditure in respect of a flat and, at the end of the chargeable period—
  - (a) the person is entitled to the relevant interest in the flat,
  - (b) the person has not granted a long lease of the flat out of the relevant interest in consideration of the payment of a capital sum, and
  - (c) the flat is a qualifying flat.
- (2) In subsection (1)(b) “ long lease ” means a lease the duration of which exceeds 50 years.
- (3) Whether the duration of a lease exceeds 50 years is to be determined—
  - (a) in accordance with section 38(1) to (4) and (6) of ICTA, and

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- (b) without regard to section 393V(3) (new lease granted as a result of the exercise of an option treated as continuation of old lease).
- (4) A person claiming a writing-down allowance may require the allowance to be reduced to a specified amount.

### **393K Amount of allowance**

- (1) The writing-down allowance for a chargeable period is 25% of the qualifying expenditure.
- (2) The allowance is proportionately increased or reduced if the chargeable period is more or less than a year.
- (3) The amount of the writing-down allowance for a chargeable period is limited to the residue of qualifying expenditure.
- (4) For this purpose the residue is ascertained immediately before writing off the writing-down allowance at the end of the chargeable period.

### **393L Meaning of “the residue of qualifying expenditure”**

The residue of qualifying expenditure is the qualifying expenditure that has not yet been written off in accordance with Chapter 8.

## **CHAPTER 7**

### **BALANCING ADJUSTMENTS**

#### **393M When balancing adjustments are made**

- (1) A balancing adjustment is made if—
  - (a) qualifying expenditure has been incurred in respect of a flat, and
  - (b) a balancing event occurs.
- (2) A balancing adjustment is either a balancing allowance or a balancing charge and is made for the chargeable period in which the balancing event occurs.
- (3) A balancing allowance or balancing charge is made to or on the person who incurred the qualifying expenditure.
- (4) No balancing adjustment is made if the balancing event occurs more than 7 years after the time when the flat was first suitable for letting as a dwelling.
- (5) If more than one balancing event occurs, a balancing adjustment is made only on the first of them.

#### **393N Balancing events**

- (1) The following are balancing events for the purposes of this Part—
  - (a) the relevant interest in the flat is sold;
  - (b) a long lease of the flat is granted out of the relevant interest in consideration of the payment of a capital sum;

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- (c) if the relevant interest is a lease, the lease ends otherwise than on the person entitled to it acquiring the interest reversionary on it;
  - (d) the person who incurred the qualifying expenditure dies;
  - (e) the flat is demolished or destroyed;
  - (f) the flat ceases to be a qualifying flat (without being demolished or destroyed).
- (2) Section 393J(2) and (3) (meaning of “ long lease ”) apply for the purposes of subsection (1)(b).

### **393O Proceeds from balancing events**

- (1) References in this Part to the proceeds from a balancing event are to the amounts received or receivable in connection with the event, as shown in the Table—

TABLE: BALANCING EVENTS AND PROCEEDS

<i>1. Balancing event</i>	<i>2. Proceeds from event</i>
1. The sale of the relevant interest.	The net proceeds of the sale.
2. The grant of a long lease out of the relevant interest.	If the capital sum paid in consideration of the grant is less than the commercial premium, the commercial premium.  In any other case, the capital sum paid in consideration of the grant.
3. The coming to an end of a lease, where a person entitled to the lease and a person entitled to any superior interest are connected persons.	The market value of the relevant interest in the flat at the time of the event.
4. The death of the person who incurred the qualifying expenditure.	The residue of qualifying expenditure immediately before the death.
5. The demolition or destruction of the flat.	The net amount received for the remains of the flat, together with—  (a) any insurance money received in respect of the demolition or destruction, and  (b) any other compensation of any description so received, so far as it consists of capital sums.
6. The flat ceases to be a qualifying flat.	The market value of the relevant interest in the flat at the time of the event.

- (2) The amounts referred to in column 2 of the Table are those received or receivable by the person who incurred the qualifying expenditure.
- (3) In Item 2 of the Table “ the commercial premium ” means the premium that would have been given if the transaction had been at arm’s length.

### **393P Calculation of balancing adjustments**

- (1) A balancing allowance is made if—



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- (a) there are no proceeds from the balancing event, or
  - (b) the proceeds from the balancing event are less than the residue of qualifying expenditure immediately before the event.
- (2) The amount of the balancing allowance is the amount of—
  - (a) the residue (if there are no proceeds);
  - (b) the difference (if the proceeds are less than the residue).
- (3) A balancing charge is made if the proceeds from the balancing event are more than the residue, if any, of qualifying expenditure immediately before the event.
- (4) The amount of the balancing charge is the amount of—
  - (a) the difference, or
  - (b) the proceeds (if the residue is nil).
- (5) The amount of a balancing charge made on a person must not exceed the total amount of—
  - (a) any initial allowances made to the person in respect of the expenditure, and
  - (b) any writing-down allowances made to the person in respect of the expenditure for chargeable periods ending on or before the date of the balancing event giving rise to the balancing adjustment.

## CHAPTER 8

### WRITING OFF QUALIFYING EXPENDITURE

#### **393Q Introduction**

For the purposes of this Part qualifying expenditure is written off to the extent and at the times specified in this Chapter.

#### **393R Writing off initial allowances and writing-down allowances**

- (1) If an initial allowance is made in respect of the qualifying expenditure, the amount of the allowance is written off at the time when the flat is first suitable for letting as a dwelling.
- (2) If a writing-down allowance is made in respect of the qualifying expenditure, the amount of the allowance is written off at the end of the chargeable period for which the allowance is made.
- (3) If a balancing event occurs at the end of the chargeable period referred to in subsection (2), the amount written off under that subsection is to be taken into account in calculating the residue of qualifying expenditure immediately before the event to determine what balancing adjustment (if any) is to be made.

#### **393S Treatment of demolition costs**

- (1) This section applies if—
  - (a) a qualifying flat is demolished, and
  - (b) the person who incurred the qualifying expenditure incurs the cost of the demolition.

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- (2) The net cost of the demolition is added to the residue of qualifying expenditure immediately before the demolition.
- (3) “ The net cost of the demolition ” means the amount, if any, by which the cost of the demolition exceeds any money received for the remains of the flat.
- (4) If this section applies, neither the cost of the demolition nor the net cost of the demolition is treated for the purposes of any Part of this Act as expenditure on any other property replacing the flat demolished.

## CHAPTER 9

### SUPPLEMENTARY PROVISIONS

#### 393T Giving effect to allowances and charges

- (1) This section applies if a person is entitled or liable under this Part to an allowance or charge for a chargeable period.
  - (2) If the person’s interest in the flat is an asset of <sup>F3</sup> a UK property business, or a Schedule A business, ] carried on by him at any time in that period, the allowance or charge is to be given effect in calculating the profits of that business for that period, by treating—
    - (a) the allowance as an expense of that business, and
    - (b) the charge as a receipt of that business.
- [ If the person is within the charge to income tax in respect of the allowance or charge <sup>F4</sup>(2A) and his interest in the flat is not an asset of a UK property business carried on by him at any time in that period, the allowance or charge is to be given effect by treating him as if he had been carrying on a UK property business in that period and as if—
- (a) the allowance were an expense of that business, and
  - (b) the charge were a receipt of that business.]
- (3) If <sup>F5</sup> the person is a company within the charge to corporation tax in respect of the allowance or charge and its] interest in the flat is not an asset of a Schedule A business carried on by <sup>F6</sup> the company] at any time in that period, the allowance or charge is to be given effect by treating <sup>F6</sup> the company] as if <sup>F7</sup> it] had been carrying on a Schedule A business in that period and as if—
    - (a) the allowance were an expense of that business, and
    - (b) the charge were a receipt of that business.

#### Textual Amendments

- F3** Words in s. 393T(2) substituted (with effect in accordance with s. 883(1) of the amending Act) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\), Sch. 1 para. 560\(2\)](#) (with Sch. 2)
- F4** S. 393T(2A) inserted (with effect in accordance with s. 883(1) of the amending Act) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\), Sch. 1 para. 560\(3\)](#) (with Sch. 2)
- F5** Words in s. 393T(3) substituted (with effect in accordance with s. 883(1) of the amending Act) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\), Sch. 1 para. 560\(4\)\(a\)](#) (with Sch. 2)
- F6** Words in s. 393T(3) substituted (with effect in accordance with s. 883(1) of the amending Act) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\), Sch. 1 para. 560\(4\)\(b\)](#) (with Sch. 2)

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**F7** Word in s. 393T(3) substituted (with effect in accordance with s. 883(1) of the amending Act) by Income Tax (Trading and Other Income) Act 2005 (c. 5), **Sch. 1 para. 560(4)(c)** (with Sch. 2)

### **393U Apportionment of sums partly referable to non-qualifying assets**

- (1) If the sum paid for the sale of the relevant interest in a flat is attributable—
  - (a) partly to assets representing expenditure for which an allowance can be made under this Part, and
  - (b) partly to assets representing other expenditure,  
only so much of the sum as on a just and reasonable apportionment is attributable to the assets referred to in paragraph (a) is to be taken into account for the purposes of this Part.
- (2) Subsection (1) applies to other proceeds from a balancing event in respect of a flat as it applies to a sum given for the sale of the relevant interest in the flat.
- (3) Subsection (1) does not affect any other provision of this Act requiring an apportionment of the proceeds of a balancing event.

### **393V Provisions applying on termination of lease**

- (1) This section applies for the purposes of this Part if a lease is terminated.
- (2) If, with the consent of the lessor, the lessee of a flat remains in possession of the flat after the termination without a new lease being granted to him the lease is treated as continuing so long as the lessee remains in possession.
- (3) If on the termination a new lease is granted to the lessee as a result of the exercise of an option available to him under the terms of the first lease, the second lease is treated as a continuation of the first.
- (4) If on the termination the lessor pays a sum to the lessee in respect of a flat comprised in the lease, the lease is treated as if it had come to an end by surrender in consideration of the payment.
- (5) If on the termination—
  - (a) another lease is granted to a different lessee, and
  - (b) in connection with the transaction that lessee pays a sum to the person who was the lessee under the first lease,  
the two leases are to be treated as if they were the same lease which had been assigned by the lessee under the first lease to the lessee under the second lease in consideration of the payment.

### **393W Meaning of “lease” etc.**

- (1) In this Part “lease” includes—
  - (a) an agreement for a lease if the term to be covered by the lease has begun, and
  - (b) any tenancy,  
but does not include a mortgage (and “lessee”, “lessor” and “leasehold interest” are to be read accordingly).
- (2) In the application of this Part to Scotland—

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- (a) “ leasehold interest ” (or “ leasehold estate ”) means the interest of a tenant in property subject to a lease, and
- (b) any reference to an interest which is reversionary on a leasehold interest or on a lease is to be read as a reference to the interest of the landlord in the property subject to the leasehold interest or lease.]

**Status:**

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