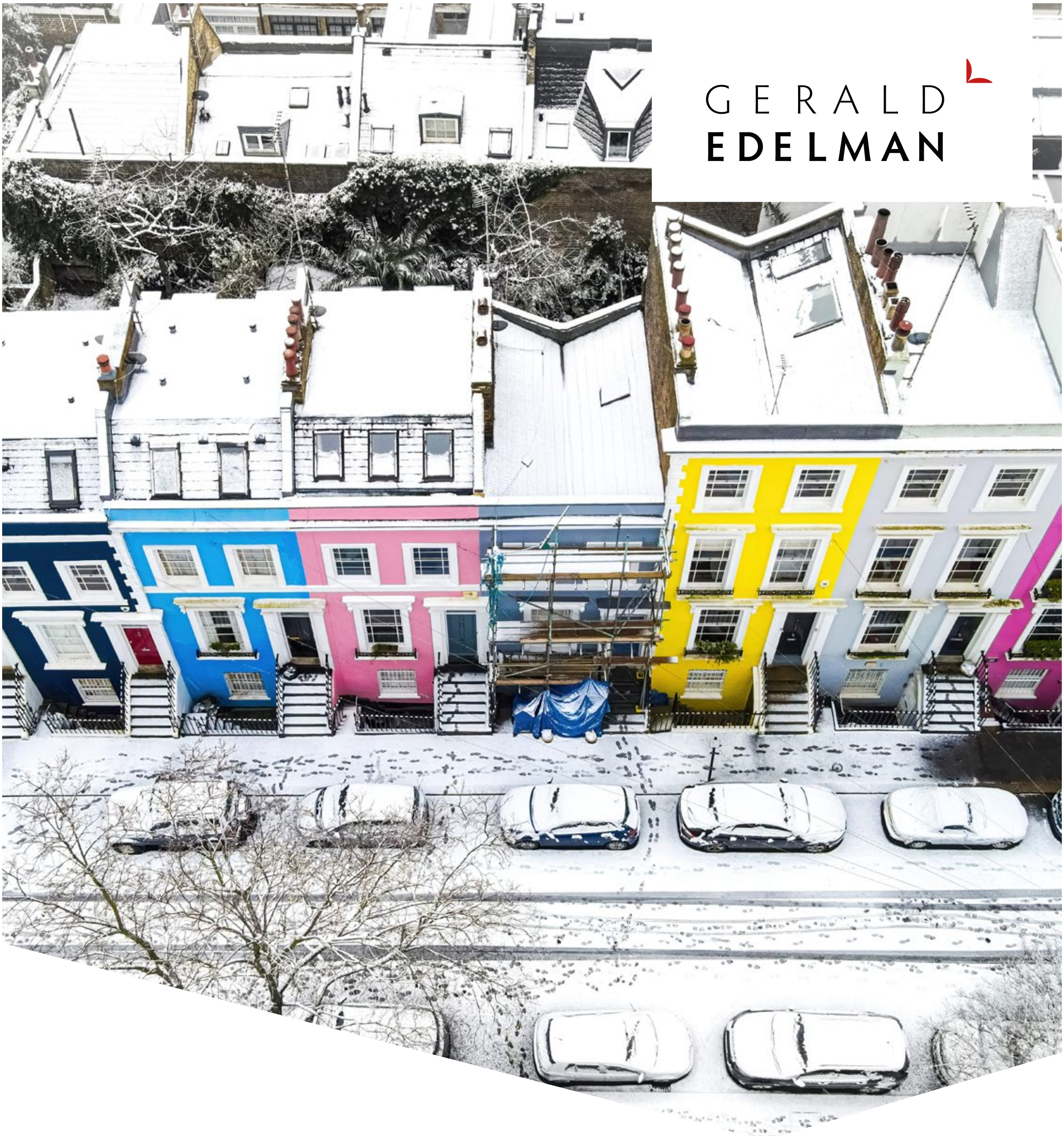


January 2024

The Property Round

In This Issue

This Issue's Contributors

Richard Kleiner
CHAIRMAN

Sonal Shah
INTERNATIONAL TAX PARTNER

Amal Shah
PARTNER

Richard Staunton
VAT PARTNER

Plus articles from John Forbes at John Forbes Consulting, Richard Clutterbuck at The Guild, Matt Karagul at Henry Dannell, and Jonathan Jex at Jex Capital Allowances.

GERALD EDELMAN

EDITORIAL

Welcome to the latest edition of Gerald Edelman's Property Round. It is with some relief that the we welcome in the new year and we look forward to calmer waters in 2024, given the hawkish and volatile nature of the macro-economic climate.

Whilst the US Federal Reserve mapped out potential interest rate cuts in 2024, the Bank of England held firm. But at least this provides some certainty around the outlook for the property investment community.

So why does this matter?

Another reason is that the bond markets are a strong alternative investment to bricks and mortar. And while they took a while for yields to increase during the year, increased yields mean greater returns – competing head on with property. This will have contributed to lower UK and European property transactional volumes for the year. A secondary impact of this, is that with the more frequent re-pricing of bonds and a lag in property valuations, the decline in bond capital values leads to the purchase of further fixed income investments to rebalance the portfolios of asset managers in accordance with their asset allocation investment strategies.

Another one is that for debt financing, which encompasses most transactions, the horizon has brightened with the medium and longer term cost of debt decreasing during Q4 2023. By way of illustration, the five year SONIA Swap Rate decreased from 4.8% in October through to 4.4% at the end of the year, whilst base rates held firm at 5.25%. Although debt financiers remain cautious in their lending, focusing on their current portfolios. Nevertheless, this encourages transactional activity in the residential and commercial markets. Indirect implications, such as the cost of living which impacts consumer spending and property tenants also contribute to the picture.

The good news is that whilst the medium term investment landscape is yet to crystallise, generally property valuations were stabilising towards the end of 2023. The clouds around the residential property market started to part, driven primarily by

Contact Us
73 Cornhill, London, EC3V 3QQ +44 (0)20 7299 1400 hello@geraldedelman.com

XLNC FOUNDING MEMBER

supply constraints for stock coming onto the market, and labour shortages for the construction of new properties. Although with a large number of requests for changes in asking prices compared to the long term norm over the past year, 2024 may still bring price sensitivity to negotiations. Turning to the commercial market, given the continued strength of e-commerce, distribution and logistics warehouses remained attractive as did residential and student accommodation, hotels and other accommodation linked property investments in prime locations. Geographically, London continues to attract transaction volume, relative to its European counterparts.

UK REAL ESTATE MEGATRENDS

Thematic investing is a key method for asset selection driven by underlying megatrends, which in turn provides some clarity when navigating choppy waters. This also helps the deployment of capital for the needs of the market of tomorrow to achieve long term returns. As discussed with our clients and supported by publications from property valuation firms, consultants, and industry bodies, whilst there is some variation on the themes, the key core similarities are set out below.

Environment

This not only affects the properties and their specifications in planning, construction and in use but the needs of their occupiers too. The latter may be driven by the occupational wants of the workforce and their values, where a focus on sustainable practices prevail. Opportunities will arise for niche real estate classes like the provision of car charging, battery storage solutions, solar and wind farms to meet the future demand. The UK market is well placed to encourage this investment due to its 2050 net zero ambition.

Demographics

The increase in the average age of the UK population will place strain on the social care system, however this also presents an opportunity, for example the provision of further care homes by the private sector. The housing market may be quite different for the younger generation due to the high capital values and financing costs, where renting for longer will create a need for more rental properties, in a market which is already supply constrained.

Urbanisation

The pandemic drove many out of the big cities in favour of longer commuting times and hybrid working, however now the overwhelming choice for those starting their careers is to either settle in cities that offer enhanced wellbeing or to embrace the pull of the big ones. With the continued shift to further urbanisation, those properties in great locations and condition will continue to do well, having regard to occupation costs and the desire of the workforce to work in that building. The full effect of hybrid working on the future space requirements of occupiers remains difficult to gauge, however, co-location, shorter leases and flexible office space will be part of the solution.

Digitilisation

Technology is rapidly changing how we work and interact. The same applies to property and an avenue to potentially maximise returns is to harness the potential of technology and digitalisation, whether that's through operational efficiencies or adding value to occupiers. One example may be the benefit of Artificial Intelligence (AI) in the property rental market, due to the volume of agreements. Another one is an expected advancement in 2024, being the use of AI on smartphones through Edge-AI technology, which will unlock further benefits to interact with the physical environment, including real estate.

IN CONCLUSION

There are no doubt strategies to rise above the unsettled UK property market. However, headwinds like debt re-financing on existing assets, the readiness of debt lenders to supply finance, the performance of secondary and tertiary offices, and the relatively high valuations, may require some careful maneuvering in the short to medium term. This edition includes thought leadership from my fellow partners, as well as contributions from John Forbes, Richard Clutterbuck, Richard Staunton, Matt Karagul and Jonathan Jex, which expand on some of the themes above, and provides you with the latest tax insights.

We hope that you find this edition informative, engaging and useful. As always, if you would like to contribute to our next edition, please contact one of the GE team.

Grant Lee

PROPERTY SECTOR UPDATE

The property sector is beginning to show signs of recovery. With inflation falling and interest rates peaking, the outlook for 2024 is a lot more positive.

THE HOUSING MARKET

In September 2023, according to the Office for National Statistics (ONS) the UK experienced its first fall in average house prices since April 2012. However, to put this into perspective, the provisional estimate for the average UK house price was £291,000 in September 2023, which was little changed from 12 months ago.

Interestingly, Zoopla reported that discounts to asking price average 5.5% or £18,000 – the highest in five years – and are even larger in the South of England, suggesting that people selling their homes are becoming more realistic and agreeing to larger discounts.

Indeed, reports from the Nationwide Building Society and Halifax suggest that prices rose by around one per cent in October 2023, meaning that house prices (on the Nationwide measure) are now just 4.6% below their summer 2022 peak (5.4% previously).

AVERAGE UK HOUSE PRICES

(Sources: HM Land Registry, Registers of Scotland, Land and Property Services Northern Ireland, and Office for National Statistics)

THREE AREAS TO WATCH OUT FOR IN 2024

Mortgage rates stabilising

There is cautious optimism for homebuyers, with mortgage interest rates stabilising and lenders now reducing rates on fixed mortgage deals. It comes after the rate of inflation remained at 6.7% in September 2023, according to the ONS.

Shortage of houses

According to Benham and Reeves, prospective sellers are cautious, concerned they may not achieve the price they had expected. But because of low stock levels, accurately priced properties are generating interest, and many are getting good offers quite quickly.

Increasing demand from overseas investors

According to Benham and Reeves, demand from overseas clients increased during 2023, boosted by the continuing weakness of sterling.

THE COMMERCIAL SECTOR

£7.9 billion of UK property assets changed hands in Q3 2023 (data from Lambert Smith Hampton). This was 8% down on Q2 2023's already weak outturn. However, the actual number of transactions rebounded by 25%, suggesting signs of recovery. Retail volumes appeared the most resilient in Q3 2023, hitting a five year high of £1.9 billion, while offices remain under greatest pressure.

When considering different asset classes, the Royal Institute of Chartered Surveyors (RICS) survey revealed that it is the non-traditional areas of the market which are delivering the strongest returns, such as aged care facilities, student housing, life sciences and data centres.

RENTAL MARKET

Rental prices are increasing. A report from Rightmove reveals that average advertised rents in London have reached a record high of £2,627 per month. Rightmove notes that they receive an average of 25 inquiries per rental property, a increase from just eight in 2019. This overwhelming demand, coupled with a limited supply of rental properties, has driven up rental prices by 12.1% compared to last year.

Meanwhile, the October RICS data provides the first sign that rental demand may be slowing in the face of elevated rental costs. Alongside this, landlord instructions fell at a slower pace in the latest survey, suggesting a narrowing in the gap between fresh demand and supply. That said, the Rental Expectations indicator remains firmly in positive territory.

PROPERTY SERVICES

Construction output saw a decrease of 0.3% in the three months to October 2023; this came solely from a decrease in new work (2.0% fall), as repair and maintenance increased by 2.2% (RICS).
This decrease is predicted to be because of increasing pressure on private residential development as housebuilders slow the pace of work. In contrast, infrastructure is proving to be resilient.

Challenges for the industry remain to be financial constraint with worsening credit conditions and the skills deficiency. The demographic challenge of an ageing workforce points to the skills issue becoming even more potent in the future.

Meanwhile, official data on building material costs shows the headline index to have fallen by almost 2% over the past twelve months. However, the level of material prices remains elevated, some 40% higher than in January 2020 (RICS).

MERGERS AND ACQUISITIONS

Date Acquired	Target/Company	Acquirer	Acquirer HQ	Deal Type	Deal Size
12/12/2023	OnTheMarket PLC	CoStar Group	USA	Acquisition	£100m
01/12/2023	London Square	Aldar Properties	UAE	Acquisition	£230m
23/10/2023	Chestertons	Emeria Europe	France	LBO	£100m
09/05/2023	Civitas Social Housing PLC	Wellness Unity	Hong Kong	Acquisition	£485m
06/03/2023	Shaftesbury PLC	Capital & Counties Properties PLC	UK	Merger	£3,500m
26/01/2023	Marsh & Parsons	Dexters London	UK	Acquisition	£29m

M&A activity within the UK real estate sector experienced a slowdown in 2023, primarily attributed to concerns surrounding asset valuation and borrowing costs. The commercial real estate segment, in particular, grappled with the ongoing impact of the post-pandemic landscape, marked by significant shifts in work and lifestyle patterns, thereby fostering an environment of uncertainty.

> Despite the challenging economic environment, the property sector is showing signs of recovery.

Looking ahead to 2024, we anticipate that current market conditions will give rise to new M&A opportunities. Investors aiming to capitalise on emerging trends, such as the experience-led paradigm, or seeking to establish and enhance their presence in the UK market, will likely find ample opportunities.

Additionally, we may witness companies strategically pursuing acquisitions to hedge against market volatility. A notable example is Foxtons, which, in 2023, expressed its intent to acquire rival letting agencies, in order to diversify away from the unpredictable sales market.

AUTUMN STATEMENT: KEY MEASURES AFFECTING THE PROPERTY SECTOR

AMAL SHAH
PARTNER, GERALD EDELMAN
+44 (0)20 8492 5653   +44 (0)7786 241 604   acshah@geraldedelman.com

At the Autumn Statement, Chancellor Jeremy Hunt outlined a series of measures aimed at boosting the UK economy and creating a more prosperous future for all.

Among the 110 initiatives, the property sector emerged as a key focus, with several welcome changes designed to enhance investment and stimulate growth.

PLANNING

The government announced that it will unlock tens of thousands of new homes by investing in the planning system.

A new planning service will be introduced to speed up planning decisions. Applicants will have to pay the full cost of the process, which will be refunded if the planning authority does not meet the stated timescale. This emphasis on efficiency will expedite the delivery of new infrastructure, such as housing developments, transport networks, and essential public facilities.

The Autumn Statement also included a proposal to make splitting a house into two flats easier under the planning system.

HOUSING AFFORDABILITY BOOSTED WITH INCREASED LOCAL HOUSING ALLOWANCE (LHA) RATES

The government has announced a significant increase in Local Housing Allowance (LHA) rates, effective from April 2024. This measure will align LHA payments with 30% of local market rents, benefiting around 1.6 million low-income households. On average, these households can expect an additional £800 annually in rental assistance.

> The government announced that it will unlock tens of thousands of new homes by investing in the planning system.

EXPANDING AFFORDABLE HOMES GUARANTEE SCHEME (AHGS) TO INCLUDE RETROFITTED HOMES

The government has expanded the scope of the Affordable Homes Guarantee Scheme (AHGS) to include retrofitted existing homes. This move aims to accelerate the delivery of affordable housing options by providing financing options for developers who renovate existing properties. The AHGS is now open to both non-profit housing associations and for-profit Registered Providers, further enhancing its reach and effectiveness.

> The government has expanded the scope of the Affordable Homes Guarantee Scheme (AHGS) to include retrofitted existing homes.

NUTRIENT MITIGATION FUND TO SUPPORT HOUSING DEVELOPMENT

The government has committed £110 million to the Local Nutrient Mitigation Fund to assist Local Planning Authorities (LPAs) affected by nutrient neutrality rules. This funding will enable LPAs to implement local nutrient offsetting schemes, addressing nutrient neutrality constraints and expediting the delivery of new housing developments.

INVESTMENT ZONES EXPANDED WITH INCREASED LIFESPAN AND INVESTMENT RELIEFS

The government has announced the addition of five new Investment Zones (IZs) in Manchester, the East and West Midlands, and North and South Wales. Existing IZs will also benefit from an extended lifespan of ten years, up from five, and doubled investment and tax reliefs from £80 million to £160 million. This expansion will attract further investment and boost economic activity in these regions.

FREEPORTS AND INVESTMENT ZONES EXTENDED FOR TEN YEARS TO FOSTER LONG-TERM INVESTMENT

Both Freeports and Investment Zones will now run for ten years, instead of the initial five, providing businesses with greater certainty and encouraging long-term investment in these areas.

MAKING TAX DIGITAL (MTD)

The £30,000 threshold for MTD for income tax self assessment will remain. This means people with gross income from self-employment and property below this threshold will not have to file tax returns using MTD.

The government will also simplify the requirements for all taxpayers providing quarterly updates and for taxpayers with more complex affairs, such as landlords with jointly-owned property. An end of period statement will no longer have to be provided. Overall, the government's measures aim to address the challenges faced by the housing sector, including affordability, development, and regeneration.

VOLATILITY IN THE HOUSING MARKET

RICHARD KLEINER
CHAIRMAN, GERALD EDELMAN
+44(0)20 7299 1405   +44 (0)7768 920 220   rkleiner@geraldedelman.com

There have been many articles in the press amongst professional commentators with regard to the impact on the housing market caused by the hikes in interest rates.

Whilst the Bank of England's recent decision to maintain interest rates at 5.25% was a positive indicator, the Monetary Policy Committee also stated that rates are forecast to remain reasonably high for a longer period than previously thought by the market.

As a result, it is anticipated that the current volatility in the housing market is set to continue with a potential further fall in values and, with regard to the construction industry, additional potential impairment on land values.

Based on data it appears that across the UK prices have fallen back over the last year by approximately 4-5%. Inevitably, some areas have seen weaker performance but overall 4-5% seems to be the average reduction.

With regard to the mortgage market, interest rates largely remain above 5% and the population of buyers are challenged by the market's requirement for an increase in the level of funds to be put down in deposits in order to attract the best mortgage interest rates. This includes first-time buyers.

In terms of the position going forward, there have been commentators stating that house price volatility may stabilise in the latter half of 2024 but that there may be further adjustments downwards in terms of values before the market stabilises.

> It appears that across the UK prices have fallen back over the last year by approximately 4-5%.

As referred to above, it is likely that interest rates will remain high although possibly not higher than the current level of 5.25% until at least Q2 2024 and even possibly later. If there continues to be weak growth for the UK economy and reducing inflation, then interest rates may start to fall earlier. This is likely to coincide with cash investors re-entering the housing market.

ECONOMIC CRIME AND CORPORATE TRANSPARENCY ACT 2023

SONAL SHAH
INTERNATIONAL TAX PARTNER, GERALD EDELMAN
+44(0)20 7299 1409   +44 (0)7775 703 015   scshah@geraldedelman.com

The new Economic Crime and Corporate Transparency Act 2023 (ECCTA) which received Royal Assent in October 2023 has made amendments to the previously introduced Economic Crime (Transparency and Enforcement) Act 2022 (ECTEA).

The ECTEA introduced in August 2022 the Register of Overseas Entities whereby foreign entities that hold interests in residential land and property here in the UK must register their company and beneficial owners with Companies House. This register brought in a great administrative burden for many companies and the new ECCTA seeks to further increase the compliance requirements of the register.

WHAT ARE THE NEW CHANGES BROUGHT IN?

The type of information provided will change and includes the following:

- Corporate owners will have to disclose their principal office in place of the registered office.
- Entities will have to disclose title numbers of property held which needs to be verified by an agent. Previously entities did not have to provide details of the individual properties held but will now have to supply each title number.
- In instances where the settlor of a trust was a company, the registrable beneficial owner of the settlor will need to be disclosed. Previously this did not have to be done and this change will increase the transparency of the structures.
- Trustees and trusts are now always disclosable. Previously corporate trustees were only considered registerable beneficial owners if they were subject to their own disclosure requirements. This change will increase the number of trustees registered.
- Entities that previously did not qualify as a registerable beneficial owner as they only held an interest in the estate as a nominee, would now be considered a registerable beneficial owner.

In conclusion, the ECCTA is a significant step towards further ensuring transparency in the UK property market. The act requires overseas entities to register with Companies House and disclose their beneficial owners or managing officers if they want to buy, sell or transfer property or land in the UK. Whilst this act has introduced more compliance for overseas entities, as of the date of writing, none of the provisions mentioned are in force and there is no published timeline for them coming into force.

UK SUSTAINABILITY DISCLOSURE REQUIREMENTS

JOHN FORBES

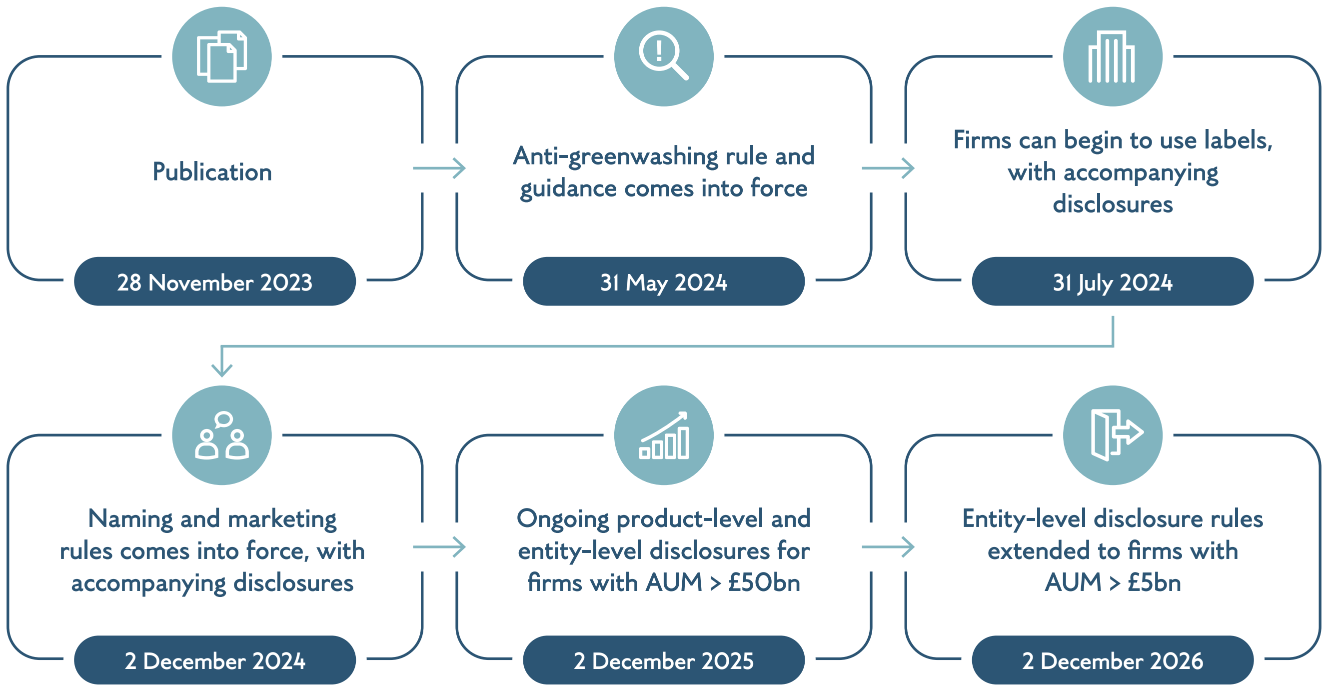
JOHN FORBES CONSULTING LLP

+44(0)20 7237 0374 +44(0)7885 912399 www.johnforbesconsulting.co.uk

The long-awaited FCA conclusions regarding Sustainability Disclosure Requirements (SDR) and investment labels have appeared as Policy Statement PS23/16.

The components and timetable for implementation have been set out by the FCA in a handy diagram:

IMPLEMENTATION TIMES



In its previous consultation, the FCA proposed an anti-greenwashing rule to be included in its ESG Sourcebook. It will be proceeding with this, and it will be the first part of the package to come into force on 31 May next year.

Detailed guidance will come into effect at the same time. This has been published for consultation. The consultation runs until 26 January 2024.

The contentious product labelling regime has been changed quite a bit, although perhaps not as much as some would have hoped. The three original labels have been renamed and a fourth added. In each case, 70% of the assets of the fund need to match the relevant label. The four labels and criteria are:

1. Sustainability Focus

Invests in assets that are environmentally and/or socially sustainable, determined using the robust, evidence-based standard that is an absolute measure of environmental and/or social sustainability.

> **The contentious product labelling regime has been changed quite a bit, although perhaps not as much as some would have hoped.**

2. Sustainability Improvers

Invests in assets that have the potential to improve environmental and/or social sustainability over time, and that are determined by their potential to meet the robust, evidence-based standard of sustainability.

Firms must obtain robust evidence for selecting those assets. Firms must also identify the period of time in which the product and/or its assets are expected to the meet the standard, including short and medium-term targets for improvements (commensurate with the investment horizon of the product).

3. Sustainability Impact

Invests with an aim to achieve a pre-defined positive, measurable, impact in relation to an environmental and/or social outcome.

Firms must:

- specify a theory of change setting out how they expect their investment activities and the product's assets to contribute to positive impact;
- specify a robust method for measuring and demonstrating the positive impact of both their investment activities and the product's assets.

4. Sustainability Mixed Goals

Mixed platter of the other three.

The labels are primarily intended for funds marketed to retail investors, but:

We envisage that the labels may gain importance beyond that, particularly for funds aimed at DC pension schemes. This is a personal view;

The overwhelming majority of retail investors in real estate funds come via model portfolios or discretionary wealth management. These are currently excluded. A separate consultation on this is promised next year. We are not sure how this will interact with the requirement for distributors to communicate the labels and provide access to consumer-facing disclosures to retail investors. The FCA also plans to set up an independent working group to look at how do enhance the skills of financial advisers.

The terms 'sustainable', 'sustainability' and 'impact' (or another variation of those terms) cannot be used in fund names for funds for retail investors.

The policy statement sets criteria for the product labelling in five areas:

- Sustainability objective;
- Investment policy and strategy;
- KPIs;
- Resources and governance;
- Stewardship.

CONSTRUCTION INDUSTRY SCHEME UPDATE

RICHARD CLUTTERBUCK

TAX ADVISOR, THE GUILD

+44(0)20 8515 2999 richard.clutterbuck@workersguild.co.uk

Businesses involved in the provision of construction services will hopefully be aware of the Construction Industry Scheme (CIS) tax regime.

Legislation requires the business (the contractor) who has engaged the services of a subcontractor to undertake construction operations on its behalf to deduct CIS tax and report the deductions and payments made to that subcontractor to HMRC monthly via an online submission process.

Whilst this might seem nothing more than an administrative inconvenience, the truth is that the operation of CIS is fraught with additional responsibilities that come with draconian costs and penalties should the business make any mistakes in its operation of the scheme.

PROPERTY INVESTMENT COMPANIES

One of the difficulties facing businesses that operate as a property investment company rather than a property developer is the potential for HMRC to judge that construction work undertaken by a property investment company might be substantial enough for HMRC to consider the business to be a mainstream contractor and required to operate the CIS immediately.

Normally, a property investment business would need to spend more than £3 million over 12 months on construction operations, which could include refurbishment work, to be considered a deemed contractor for the purposes of CIS. Only once the £3 million trigger point is reached would the business need to register as a contractor with HMRC and operate the scheme on payments it makes going forward to its subcontractors that fall within the scope of the scheme.

Difficulties can arise where a business that is normally operating as an investment company takes on a property that requires more than refurbishment or minor construction work, perhaps including a change of use. In these types of contracts, HMRC usually consider that the nature of the trade of the business has moved from investment to development, so care must be taken to consider the impact of CIS on each project the business undertakes.

Recent activity by HMRC suggests that it is actively looking to target property investment businesses that are operating under the misunderstanding that CIS does not apply to them because they have not breached the deemed contractor limit. However, due to the level of construction work undertaken on an investment property HMRC consider that the business is a mainstream contractor either for that particular contract or from day one and should therefore be registered and opening CIS.

IMPACT OF THE AUTUMN STATEMENT ON CIS

The recent Autumn statement provided some interesting changes which are to be introduced from 6 April 2024 to the CIS scheme, that were not initially obvious but need to be considered, especially by businesses that are or are looking to become a subcontractor within CIS and who qualify for gross payment status (GPS).

Subcontractors that register with HMRC can apply to have deductions made from payments received from their contractor at either the net standard rate of 20% or at the gross rate of 0%. Those subcontractors that wish to apply for gross payment status must satisfy 3 tests:

- Business test
- Turnover test
- Compliance test

The compliance test looks at the tax compliance history of the applicant to check that its tax affairs are up to date, and it has submitted its relevant tax returns and paid its payment on time.

The new changes to be introduced will add VAT compliance obligations to the GPS compliance test, meaning that for the first time a subcontractor must be able to demonstrate compliance with its VAT obligation. Failure of this test could result in an application being refused or removed under HMRC's annual compliance review.

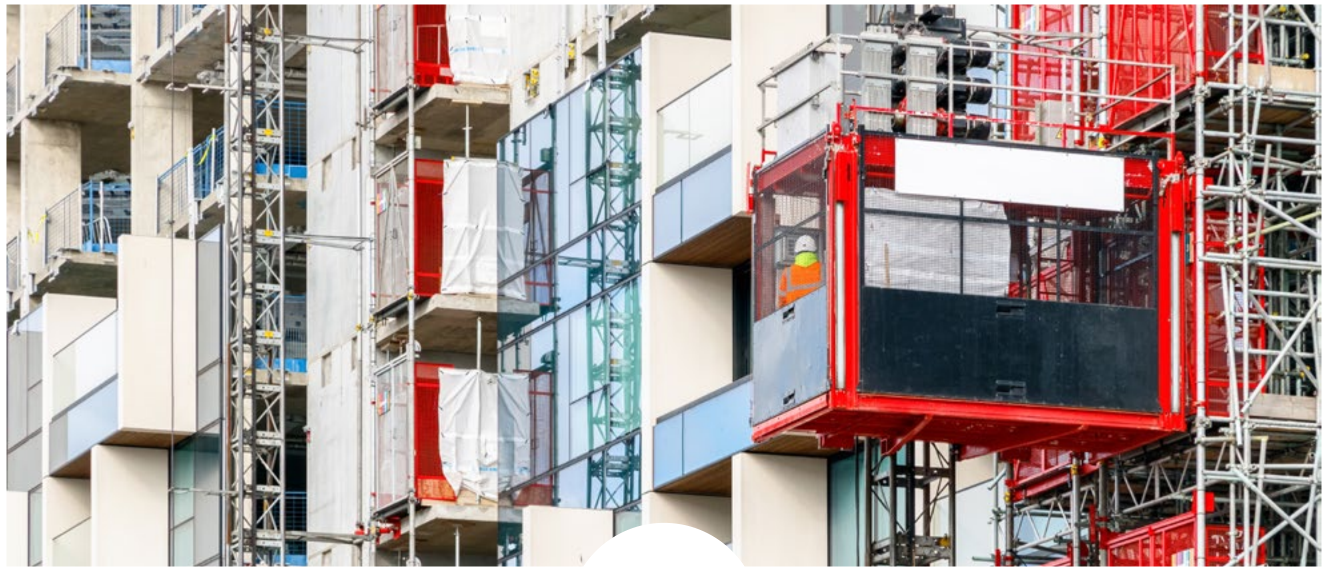
Further, legislation changes will be introduced regarding the compliance test meaning that when a subcontractor is first granted GPS, HMRC will bring forward the first review of the subcontractor's compliance check from 12 months to 6 months, reverting to standard 12-month period thereafter.

The grounds for immediate cancellation of GPS will also include VAT along with Income Tax, Self-Assessment (ITSA), Corporation Tax Self-Assessment (CTSA) and Pay As You Earn (PAYE) as the taxes where HMRC have reasonable grounds to suspect that the GPS holder has *fraudulently* provided an incorrect return or information.

Additional regulations are also being introduced from April 2024 that will remove from the scope of the CIS most of the payments that a landlord makes to tenants, which is very helpful as this compliance area has been overly complex for a long time.

HMRC have also announced that it will digitalise the CIS registration application and will no longer normally take telephone applications, apart from those who are digitally exempt. Postal applications will still be accepted for the foreseeable period before it eventually becomes mandatory to register digitally.

The Guild offers compliance solutions to the engagement of sub-contractors in the Construction Industry. If you are interested in speaking with Richard about the solutions The Guild can offer, please get in touch.



ENERGY-SAVING MATERIALS

RICHARD STAUNTON
VAT PARTNER, GERALD EDELMAN
+44(0)20 7299 1400 +44 (0)7841 207 370 rstaunton@geraldedelman.com

BACKGROUND AND HISTORY

COP 28 ended with a statement that there will be a transition from fossil fuels to renewables.

I pride myself on being able to add a VAT angle to any conversation but in respect of net zero and in particular the transition away from fossil fuels to renewables indirect tax can (and should) be used as a useful tool to encourage 'green' behaviours. Using a carrot and stick approach often produces the best results.

One example of the 'stick' to discourage 'bad' behaviour was the introduction of the fuel price escalator in March 1993. The aim was to increase fuel duty at a rate of 3% above inflation every year and increased to 6% above inflation in 1997.

However, this was frozen for several years and was replaced in 2011 by the fuel duty stabiliser. Successive budgets have generally seen fuel duty frozen partly because of high fuel prices and partly for political reasons.

The 'carrot' has a more successful history, particularly in relation to buildings. On 1 April 2000, the law was amended to include the supply and installation of energy-saving materials in all residential and charity buildings within the reduced rate schedule, which at the time was (and still is) 5%.

These include;

- insulation for walls, floors, ceilings, roofs, lofts, water tanks, pipes and other plumbing fittings
- draught stripping for windows and doors
- central heating system controls
- hot water system controls, and
- solar panels.
- ground and air source heat pumps,
- micro combined heat and power units, and
- wood-fuelled boilers

BREXIT

In 2013, the EU ruled that the reduced rate for energy-saving materials was incompatible with EU law and began infraction proceedings.
In response, the UK reduced the scope of the rate for those most in need, which meant for many residents in the UK there was no relief for energy-saving materials. The UK was also unable to apply the zero-rate of VAT again because that was contrary to EU Law, indeed the zero-rate was seen a transitional rate when the UK applied for

membership of the then Common Market and it was assumed that the UK would abolish the zero – rate as time passed.

When the UK left the single market in 2020 it was no longer bound by EU directives. Therefore, since 1 April 2022 the zero-rate has been applied to the installation of energy-saving materials within Great Britain and when the Windsor Framework is ratified it will also apply to Northern Ireland.

At the same time, in 2022, amendments to the EU Directive are likely to have allowed the above rules to apply if the UK had remained within the EU.

> Since 1 April 2022 the zero-rate has been applied to the installation of energy-saving materials within Great Britain.

PREDOMINANT PURPOSE OF THE WORKS

Unfortunately, the practical application of services that could benefit from the zero-rate is not always simple.

In some cases, where a construction service contains two or more services that attract differing VAT rates, a 'fair and reasonable' apportionment can be applied. For example, this would be relevant where there is the construction of a new building comprising both commercial and residential elements. In this case if the commercial element was in respect of the ground floor with, for example four storey's of residential above, then VAT could be charged on one fifth of the contract.

This does not apply to energy-saving materials. Where the service of installing energy-saving materials is provided with other services a business would need to decide what the predominant purpose of that supply is. The VAT treatment would then follow the main supply. This means that if there was a large contract for the refurbishment of a dwelling, which happened to include some installation of energy-saving materials, VAT at the standard rate would apply to the entire contract. In the circumstances described above it would be worth considering whether building works could legitimately be carried out at different times, particularly if the supply was to a homeowner where VAT would be a cost.

Conversely if the main element of any works are services subject to the relief, other incidental works carried out at the same time will also benefit from the zero-rate.

GRENFELL

It was hoped that the changes announced in 2022 is respect of energy-saving materials would assist with the issues regarding the installation of cladding to affected buildings post Grenfell. Initially HMRC did signal that the replacement of cladding to residential flats could be seen as zero-rated (albeit very late) snagging in respect of the original zero-rated construction. As most remedial works are not carried out by the original building company HMRC have not allowed this as a blanket policy although it may be relevant in certain circumstances.

Cladding could also be seen as insulation meaning that it would attract VAT under energy-saving materials rules. Unfortunately, HMRC have stated that in most cases replacement cladding is seen as being for aesthetic rather than insulation purposes and therefore the zero-rate cannot apply. It is shame that a pragmatic solution could not be applied to works of this nature especially in the context of the tragedy.

CONSULTATION AND CHANGES

On a more positive note, HMRC has carried out a consultation exercise to extend the application of the relief. The relief will shortly be extended to charitable buildings, as it was in the past, but it is also expected that the scope of the relief will be extended to other newer technologies. The relief is likely to include certain ground works necessary for the installation of ground and water source heat pumps. One suggestion still being considered has been for the relief to extend to battery storage.

Normally, HMRC are slow in introducing new changes, but as the zero-rate for energy-saving materials has at present a short shelf life until 2027, the zero-rate fits in with the government's net zero plans. The new technologies that are likely to be brought within the zero-rate will be minimal and therefore it is likely the law will be amended early in 2024.

CONCLUSION

Clearly indirect tax is not the answer to all of life's problems, but it can encourage or discourage behaviour which in this instance could help toward meeting the UK's COP28 obligations and aspirations. That is surely a good thing.

PURCHASING BUSINESS PREMISES – A STRATEGIC LEAP FORWARD

MATT KARAGUL

SPECIALIST FINANCE ADVISER, HENRY DANNELL

+44(0)204 5999 444 matt.karagul@henrydannell.co.uk www.henrydannell.co.uk

ARE YOU LOOKING TO EXPAND YOUR BUSINESS?

Part of the journey of expanding your business often involves acquiring business premises – a significant milestone for many entrepreneurs. This asset brings stability, ownership, and offers the potential for long-term growth and financial security. However, acquiring commercial property often requires substantial capital, making financing a crucial component of the process.

In this article, we will explore the various aspects of purchasing business premises with financing and the strategic considerations involved.

WHY OPT TO FINANCE YOUR BUSINESS PREMISES?

Choosing to finance your business premises instead of paying in full with cash can provide several advantages. Primarily, it enables you to preserve your liquid capital for essential day-to-day operations, emergencies, and investments in other aspects of your business.

Additionally, financing also spreads the cost of acquiring the property over an extended period, making it more manageable and less burdensome on your finances.

COMMERCIAL MORTGAGES: CONSIDERATIONS & BENEFITS

Commercial mortgages are a common option for financing the purchase of business premises. These loans are specifically designed for this purpose and often offer lower interest rates and extended terms compared to traditional mortgages. Typically, the property itself often acts as collateral, facilitating favourable loan terms.

> Part of the journey of expanding your business often involves acquiring business premises – a significant milestone for many entrepreneurs.

KEY CONSIDERATIONS

Deposit

A substantial deposit is often required, with the amount varying based on your chosen financing option.

Interest Rate

Interest rates can significantly impact the overall cost of financing. Considering whether a fixed or variable rate is more suitable for your financial situation is essential, while also ensuring you get the most competitive rate.

Professional Advice

Seeking the guidance of a specialist finance adviser in commercial properties is crucial to securing the right solution for you. Our expertise can help you navigate the complexities of property acquisition and financing.

Purchasing business premises with financing is a strategic move that can pave the way for long-term stability and growth. This approach allows you to leverage your existing assets and resources to acquire a new valuable asset while preserving liquidity for operational needs.

However, it's crucial to approach the process with careful consideration, thorough research, and professional guidance. By doing so, you can make an informed decision that aligns with your business goals.

Ready to take the next step in acquiring your business premises? Contact Henry Dannell today for expert guidance and support.

SOLVING SHORT-TERM FINANCE NEEDS WITH BRIDGING FINANCE

MATT KARAGUL
SPECIALIST FINANCE ADVISER, HENRY DANNELL
+44(0)204 5999 444 matt.karagul@henrydannell.co.uk www.henrydannell.co.uk

Bridging finance is a short-term financial tool designed to bridge the gap between immediate capital requirements and more permanent solutions. It provides flexibility and swiftness in accessing funds for diverse purposes.

Whether it's seizing a lucrative property deal, navigating a temporary cash-flow gap, or taking advantage of investment opportunities, bridging finance can be an effective solution.

COMMON USES

Property Transactions

Buyers can secure properties quickly, before selling an existing one. This is especially advantageous in competitive property markets.

Property Development

Developers often use bridge loans to finance construction or refurbishment projects, while awaiting long-term financing or the sale of completed units.

Auction Purchases

Bridging finance aids individuals participating in auctions by providing immediate funds to secure valuable assets such as artwork, collectables, or property, with the intent to sell or refinance the asset in the future.

Business Growth

Businesses leverage bridging finance for expansion, inventory investment, or supporting operational costs during rapid growth phases.

> Bridging finance is a short-term financial tool designed to bridge the gap between immediate capital requirements and more permanent solutions.

BENEFITS OF BRIDGING FINANCE

Speed and Accessibility

Swift access to funds with faster application and approval processes compared to traditional bank loans. This is a particularly valuable option in competitive markets.

Versatility

Bridging finance is incredibly flexible and can be tailored to meet individual needs, with lenders often collaborating closely with borrowers to craft custom solutions.

Deferred Repayments

Many bridging loans do not require monthly repayments, enabling borrowers to focus on their immediate financial goals, with principal and accrued interest typically repaid at the end of the loan term.

KEY CONSIDERATIONS

Costs

It's essential to consider the costs associated with bridging finance. Borrowers should conduct a thorough cost-benefit analysis as interest rates and fees may be higher compared to traditional loans.

Exit Strategy

A well-defined exit strategy is a necessary component when taking out a bridge loan. Establishing a clear repayment plan is crucial, potentially involving the sale of an asset, securing long-term financing, or using proceeds from a project.

Risk Management

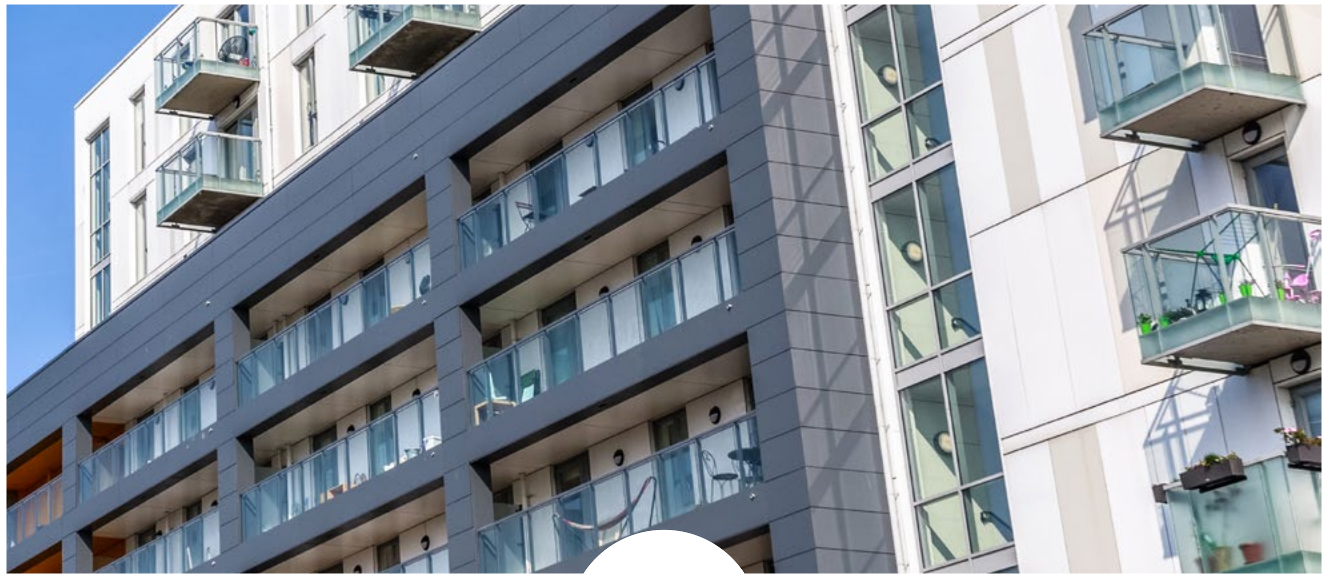
Borrowers should evaluate potential risks, such as market fluctuations or delays in project completion, and have contingency plans in place to mitigate these challenges.

> Many bridging loans do not require monthly repayments, enabling borrowers to focus on their immediate financial goals.

Reputable Lenders

Choosing a reputable lender involves due diligence, necessitating a thorough review of loan terms and conditions.

When obtaining bridging finance, seeking support from a specialist finance adviser is advised and can prove invaluable. For support arranging bridging finance, contact Henry Dannell who would be more than happy to review your circumstances and guide you through the process.



INVOICE FINANCING: ACCESSING FUNDING WHEN YOU NEED IT

MATT KARAGUL

SPECIALIST FINANCE ADVISER, HENRY DANNELL

+44(0)204 5999 444 matt.karagul@henrydannell.co.uk www.henrydannell.co.uk

Invoice financing is particularly beneficial for businesses that experience cash flow challenges from delayed payments.

WHY OPT FOR INVOICE FINANCING?

Invoice financing, also known as accounts financing, is a financial arrangement where a business sells its outstanding invoices or accounts receivable to a third-party lender or finance company. This process provides the business with an immediate cash advance, typically a significant portion of the invoice's face value, while the third party assumes responsibility for collecting payment from the customer.

It is commonly used by SMEs or businesses operating in industries with extended payment terms, such as manufacturing, wholesale, distribution or services.

BENEFITS OF INVOICE FINANCING

Improved Cash Flow

Invoice financing provides immediate access to cash by converting outstanding invoices into funds. This liquidity can help businesses manage operating expenses, invest in growth opportunities, or meet financial obligations.

Debt-Free Solution

Unlike traditional loans, invoice financing doesn't add debt to the business's balance sheet. It leverages the value of outstanding invoices, making it an attractive option for companies looking to manage cash flow without increasing overall debt and for those with lower credit ratings.

Flexible Funding

Invoice financing is a flexible solution that can be tailored to a company's specific cash flow requirements. This makes it suitable for both short-term needs and ongoing working capital management.

Growth & Expansion

Companies aiming for growth can use this strategic financial tool to invest in the business without disrupting ongoing business operations.

Invoice financing has emerged as a valuable financial tool for businesses, offering a means to address cash flow challenges caused by delayed payments from clients. By converting outstanding invoices into immediate cash, businesses can maintain financial stability, seize growth opportunities, and effectively manage their operations.

COMMERCIAL PROPERTY STANDARD ENQUIRIES

JONATHAN JEX

JEX CAPITAL ALLOWANCES

0845 345 4964 jpj@jexca.co.uk www.jexca.co.uk

Jonathan of JexCA explains how pre-contract enquiries are often misleading and the pitfalls of not scrutinising the replies.

CPSE is the best practice approach to seek information and clarification on a range of matters during the pre-contract negotiation process.

In CPSE.1 (version 4.0) General pre-contract enquiries for all commercial property transactions, capital allowances are dealt with under 33.1 to 33.11. The replies are the starting point for the buyer's capital allowances pre-acquisition due diligence, however, the replies are often less than adequate.

We regularly see "there are no capital allowances available" or "the capital allowances are not being sold" or "the seller is retaining the right to claim capital allowances" or often "not applicable".

The entitlement to claim capital allowances rests with the holder of an interest in land and transfers automatically to the new owner when property is sold.

CPSE 33 seeks to establish how the property is held by the seller, whether they have claimed capital allowances and/or entered into any agreement with a prior owner, and whether they are agreeable to meeting the pooling and fixed value requirements.

Often we see replies that make us chuckle, but in reality these are worrying as so many people do not challenge the replies and accept them at face value, for example:

One would have thought that 33.1 would be the easiest enquiry to answer as all commercial property will be held either on capital account as a fixed asset or as trading stock. Here are some replies we have seen

33.1 Do you hold the Property on capital account as an investor/ owner-occupier, or on revenue account as a developer/ property trader as part of your trading stock? Please specify which

- No
- N/A
- Not applicable for occupiers
- No enquiry has been made and the Buyer should rely on its own enquiries
- The Seller does not see the relevance of this section 33 as it is not an industrial building

The following is a recent example of replies we received to 33.1, 33.2 and 33.3

33.1 Do you hold the Property on capital account as an investor/ owner-occupier, or on revenue account as a developer/ property trader as part of your trading stock? Please specify which

Trading

33.2 Have you claimed capital allowances on plant or machinery fixtures or allocated any expenditure on such fixtures to a capital allowances pool? If so, please answer the supplementary questions in enquiry 33.9 in respect of that expenditure

Yes

33.3 If there is any expenditure on plant and machinery fixtures that you have not pooled, etc.

No expenditure has been pooled

The reply to 33.1 advises that the property is held as stock, meaning there is no entitlement to claim. However, 33.2 advises that capital allowances have been claimed, then 33.3 says that no expenditure has been pooled, i.e. no claims have been made. The replies to these first 3 enquires contradict each other entirely.

Another common reply when asked to list fixtures that have been claimed is to state a washing machine, tumble drier or motor car, clearly not fixtures falling with CAA 2001 s173. When carrying out pre-acquisition due diligence the replies to CPSE is not the end of investigations, merely the beginning, never accept at face value a reply such as "there are no capital allowances available". The statement may well be correct, but you need to know why and not just accept it.

The number of times we have heard that statement where the actual position is the opposite are too numerous to list.

Recently our client's solicitor advised "the seller's solicitor has confirmed there are no capital allowances available...maybe you thought you would get some and that informed your offer, hope not". Thankfully rather than accept that response the client referred to us to undertake our own due diligence.

Clearly from the outset our client had an entitlement to claim as the sellers had acquired pre April 2008. We asked for an explanation why there were no allowances available to which they replied, "why can't you just accept there are no allowances and let your client exchange contracts, you are holding up the transaction".

The property had been constructed and held by a pension fund who sold to an investor with a s198 joint election at £1, clearly this election was invalid and of no effect. However, the investor thought they couldn't claim capital allowances and also that they had to elect at £1 when they sold. The purchase completed without any election and our client was able to claim capital allowances of £1.4m on the acquisition of a regional office for £4m and providing tax relief in the region of £266,000, much of which was available in the first year utilising annual investment allowances.

> **CPSE is the best practice approach to seek information and clarification on a range of matters during the pre-contract negotiation process.**

Fortunately our client was well informed enough not to accept the advice given but to refer to a capital allowances specialist. I am sure though that many transactions proceed based upon incorrect replies to CPSE 33 and many opportunities for Buyers to claim tax relief goes unutilised.

The replies to CPSE are not the end of the capital allowances due diligence but the beginning. The replies should be drilled down into to ascertain why they are saying what they are and further enquiries made specific to the current transaction, as each transaction will have a different capital allowances position.

The following tables show the potential flow of tax relief for a property acquisition where specialist advice was taken and where it was *not* taken. Please don't be the latter!

Year End 31/03	Opening Main Pool	WDA's per Annum	Closing Main Pool	Opening Integral Features Pool	WDA's per Annum + AIA's	Closing Integral Features Pool	Total WDA's in Year	Tax Rate	Tax Saving
	£	£	£	£	£	£	£	%	£
2024	905,178	162,932	742,246	1,163,830	1,009,830	154,000	1,172,762	25%	293,190
2025	742,246	133,604	608,642	154,000	9,240	144,760	142,844	25%	35,711
2026	608,642	109,556	499,086	144,760	8,686	136,075	118,241	25%	29,560
2027	499,086	89,836	409,251	136,075	8,164	127,910	98,000	25%	24,500
2028	409,251	73,665	335,586	127,910	7,675	120,235	81,340	25%	20,335
2029	335,586	60,405	275,180	120,235	7,214	113,021	67,620	25%	16,905
							Tax Saving During First 6 Years		£420,202

Year End 31/03	Opening Main Pool	WDA's per Annum	Closing Main Pool	Opening Integral Features Pool	WDA's per Annum + AIA's	Closing Integral Features Pool	Total WDA's in Year	Tax Rate	Tax Saving
	£	£	£	£	£	£	£	%	£
2024	0	0	0	0	0	0	0	0	0
2025	0	0	0	0	0	0	0	0	0
							Tax Saving During First 6 Years		£0

GERALD
EDELMAN

Contact us

73 Cornhill, London, EC3V 3QQ +44 (0)20 7299 1400 hello@geraldedelman.com

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