EXPLANATORY MEMORANDUM TO

THE CAPITAL ALLOWANCES (FIRST-YEAR TAX CREDITS) ORDER 2013

2013 No. 464

1. This Explanatory Memorandum has been prepared by Her Majesty's Revenue & Customs on behalf of the Treasury and is laid before the House of Commons by Command of Her Majesty.

2. Purpose of the instrument

2.1 The period during which relevant first-year expenditure must be incurred in respect of which a first-year tax credit may be claimed is due to end on 31 March 2013. This Instrument extends that period to 31 March 2018.

3. Matters of special interest to the Select Committee on Statutory Instruments

3.1 None

4. Legislative Context

4.1 Schedule A1 to the Capital Allowances Act 2001 ("CAA") contains provision about the payment of first-year tax credits to companies in connection with certain first-year expenditure.

4.2 Paragraph 3(1) of Schedule A1 defines relevant first-year expenditure, that is, the expenditure in respect of which a first-year tax credit may be claimed. Paragraph 3(1)(b) of Schedule A1 provides that the first-year expenditure, in respect of which a first-year tax credit may be claimed, must be incurred between 1 April 2008 and 31 March 2013 inclusive.

4.3 At Budget 2012 it was announced that the availability of first-year tax credit would be extended for a further five years.

4.4 Paragraph 3(3) of Schedule A1 provides the power to enable the Treasury to extend the period in which the relevant first-year expenditure must be incurred. This Order extends the period from 31 March 2013 to 31 March 2018.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

Although subject to the negative resolution procedure, this instrument amends primary legislation. The Exchequer Secretary, David Gauke MP has made the following statement regarding Human Rights:

"In my view the provisions of the Capital Allowances (First-year Tax Credits) Order 2013 are compatible with the Convention rights."

7. Policy Background

- ***What is being done and why***

7.1 One hundred per cent first-year allowances for energy-saving and environmentally beneficial technologies, commonly known as enhanced capital allowances or ECAs, enable business to claim accelerated tax relief on expenditure incurred on qualifying energy-saving and water efficient technologies. The cash-flow benefit of accelerated tax relief can encourage businesses to invest in technologies that reduce water use and improve water quality.

7.2 First-year tax credits were originally introduced in 2008 for a five year period ending on 31 March 2013. They are designed to further encourage investment in energy-efficient and environmentally beneficial plant or machinery by allowing companies within the charge to corporation tax, to surrender tax losses attributable to these ECAs, for a payable tax credit (known as a first-year tax credit).

7.3 The losses that may be surrendered are specifically those attributable to ECAs claimed on energy-saving or environmentally beneficial plant and machinery. The amount of first-year tax credit that a company will receive is 19 per cent of the surrenderable loss for the relevant period, although this is subject to an upper limit. The upper limit of the tax credit is the greater of –

- the total of the company's PAYE and NICs liabilities for the relevant period; or

- £250,000.

7.4 This Order extends the period during which relevant first-year expenditure on designated energy-saving and environmentally beneficial technologies must be incurred in respect of which a first-year tax credit may be claimed for a further five years to 31 March 2018.

8. Consultation outcome

8.1 The Government does not generally consult on legislation containing straightforward technical changes to dates. However, the draft regulations and explanatory memorandum were published on 11 December 2012 as part of the consultation process for Finance Bill 2013 clauses and other tax updates.

9. Guidance

9.1 All guidance will be updated as appropriate as part of the normal process of review**.**

10. Impact

10.1 A Tax Information and Impact Note covering this instrument was published on 11 December 2012 alongside the draft Finance Bill 2003 and is available on the HMRC website at http://www.hmrc.gov.uk/thelibrary/tiins.htm. It remains an accurate summary of the impacts that apply to this instrument.

11. Regulating small business

11.1 The legislation only applies to companies. This includes all small companies but not the wider small business community.

11.2 To minimise the impact of the requirements on small firms (in this case small companies) employing up to 20 people, the legislation provides a simple process for qualifying companies of all sizes to benefit from the scheme.

11.3 When the first-year tax credit scheme was introduced in 2008, following a consultation exercise, it was limited to companies only because it was considered that the compliance and Exchequer risks involved in extending the scheme to self-employed individuals and partnerships would require complex additional rules, which would make the system too cumbersome, and undermine the scheme. In addition self-employed individuals already have the benefit of a loss relief not available to companies; an individual may claim for losses made in the first four years of a trade to be deducted in calculating his or her net income for the three tax years before the one in which the loss is made.

Although companies of all sizes may claim the benefit of first-year tax credits, it is only where a company has losses that cannot be utilised in any other way that they may benefit from tax credits, for example companies starting up who may not have other profits to absorb any arising losses. As larger companies are more likely to be able to set losses against other profits (particularly those companies in a group situation), it is smaller companies that are more likely to claim first-year tax credits.

12. Monitoring and review

12.1 The take-up and annual cost of first-year tax credits are monitored through boxes on tax returns.

13. Contact

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