LET THERE BE LIGHT...

Chattels Simon Yates, Paul Kenny and Rachel Wevill look at the distinction between fixtures and chattels and apply this age old question to the 21st century renewable energy market

There has been a long tradition of case law where the courts have analysed the distinction between fixtures and chattels for a variety of items. As investment in the renewable energy market increases, the courts are likely to be asked to determine the distinction in relation to increasingly modern technology affixed to property. For now, whether or not photovoltaic solar panels ("PV systems") are fixtures or chattels remains unanswered by the courts.

What are fixtures?

Fixtures are items that have been fixed to land or buildings to such an extent as to become a part of it. There is no statutory list or definition: the category depends on the degree of annexation or affixation of the item to the land or building in question. Whether something has been annexed or affixed to such a degree to become a fixture is a question of fact. The purpose for which that item was annexed or affixed is also relevant.

Degree and purpose of annexation

Quicquid solo plantatur, solo cedit (whatever is attached to land becomes part of that land) remains the common law approach today. To determine whether something is a fixture, the courts have historically asked:

- Can the item easily be removed without injury to itself or the fabric of the land/building to which it is attached?
- Is the item affixed for the permanent and substantial improvement of the land/building or merely for a temporary purpose for the better enjoyment of the item in question?

Frustratingly, case law is varied and historic decisions are heavily fact-specific. Modern technology and advanced techniques for annexation and removal have led the courts to give greater weight to the second question recently – see, for example, *Potton Developments Ltd* v *Thompson* [1998] PLSCS 98.

Landlord's and tenant's fixtures

Generally, landlord's fixtures must be left *in situ* at the end of a tenancy, while tenant's fixtures (often called "trade fixtures") may be removed by the tenant at the end of the tenancy in the absence of a contrary agreement with the landlord. An example of a landlord's fixture is an elevator in an office building, whereas a tenant's fixture could be internal demountable partitioning installed by the tenant.

Fixture or fitting?

The term "fitting" is imprecise and has no legal status in land law. It might be used to refer to an item that is attached to land or a building but which is not a fixture, owing to its nature, purpose or method of attachment. Use of the term "fitting" will not even necessarily differentiate between a landlord's or a tenant's item and is unhelpful in the context of this article, so we'll bid it farewell.

The practical implications

Transfer of ownership

Since a fixture becomes part of the property to which it is affixed, it follows that ownership of that fixture runs with ownership of the property. Any intended transfer of ownership of a fixture needs to follow the usual formalities applicable to the transfer or conveyance of land. The transferor must have title to transfer the land and section 2 of the Law of Property (Miscellaneous Provisions) Act 1989 (the "1989 Act") must be fulfilled.

Tax treatment

HMRC's treatment of fixtures is a vast topic in its own right. However, it is helpful to understand some of the more general implications of HMRC's fixture categorisation. It is not surprising that much of the finely-tuned case law is driven by financial imperative.

SDLT

HMRC's guidance *How much is chargeable: fixtures and fittings* (SDLTM04010) states:

> "Where a purchaser agrees to buy a property for a price that includes an amount properly attributed to chattels... that amount will not be charged to stamp duty land tax."

To the extent that purchase price is attributed to fixtures, it *is* chargeable to SDLT.

In keeping with the approach of the courts, each case is considered on its own merits and so there is no definitive HMRC list of chattels and fixtures. The HMRC guidance does advise that in a residential context, the following items will usually be regarded as chattels:

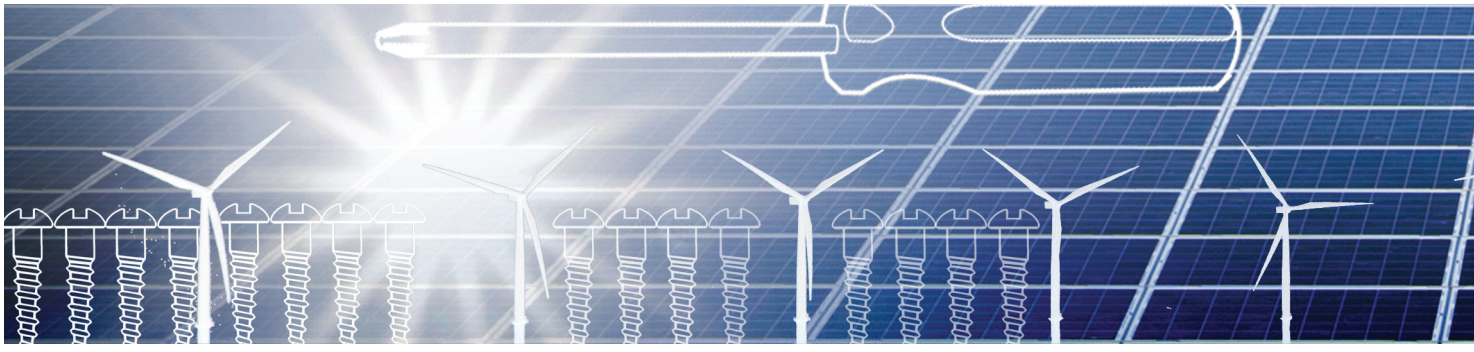
> "carpets, curtains and blinds, free standing furniture, kitchen white goods, electric and gas fires (provided they can be removed... without causing damage to the property), light shades and fittings (unless recessed)

whereas the following items will not:

> "fitted kitchen units, cupboards and sinks, agas and wall mounted ovens, fitted bathroom sanitary ware, central heating systems, intruder alarm systems, shrubs and trees growing in the soil which forms part of the land."

HMRC will treat tenant's fixtures as part of the land, notwithstanding that a tenant may have a right to sever them and the tenant's right of severance is also a chargeable interest under section 48(1) of the Finance Act 2003. HMRC will treat each case on its own facts but have indicated:

- Plant or machinery that can be relatively easily severed from the property to which it is fixed (eg by an expedient removal of some bolts securing it to the floor or walls), is unlikely to be a fixture.
- Plant or machinery that is integral to a building, the removal of which would damage the building or land, is likely to be a fixture (eg escalators, elevators, boilers, furnaces and restaurant cooking stations).



Capital allowances

Under the system of capital allowances, the costs of qualifying plant and machinery can be written off against tax at rates determined by statute – see section 56 of the Capital Allowances Act 2001 (the "2001 Act").

The standard rate of allowances is 18% pa on a reducing balance basis. "Integral features" of buildings (such as lifts and water systems), and assets with a long anticipated life, instead only attract allowances at the rate of 8%.

Where an asset is not a fixture, the position is straightforward – if someone spends money on the asset, that person presumably owns it and can claim allowances for it. The position is much more complex with fixtures.

First, the asset may not legally belong to the person that bought it – most obviously this will be the case with a tenant's fixture. Secondly, where a fixture is already in place when a building is acquired, any claim for allowances by the buyer will be limited by reference to the amount of historic claims (section 185 of the 2001 Act) to prevent fixtures effectively appreciating along with property values when in reality they have depreciated. Finally, there are rules permitting buyers and sellers of fixtures to choose the value attributed to them for tax purposes, subject to certain constraints, by way of an election under sections 198 or 199 of the 2001 Act.

Great care is needed when looking to obtain capital allowances on fixtures, as there are many pitfalls between incurring the expenditure and a successful claim.

PV systems

Renewable energy projects are an emerging source of revenue for investors and the installation of PV systems on residential and commercial properties is a popular income-producing investment under the government's "feed-in tariffs" scheme ("FiTs").

The financial viability of a PV system project is dependent on the status of PV systems as either fixtures or chattels. This status is important from a tax perspective (having regard to the SDLT and capital allowance treatment previously mentioned), and also from a land law perspective, since ownership of the PV system impacts on the ability of its owner to manage its investment and eligibility for income from FiTs.

Case law is yet to properly consider the fixture/chattel distinction in the context of a PV system. However, as can be seen from the preceding paragraphs, if a PV system is to be regarded as a fixture, then ownership of the PV system will run with the building or structure to which the PV system is attached. This means only the legal owner of the building or structure has title to transfer ownership in the PV system and the 1989 Act formalities must be met.

A common structure for a PV system project is for the investor (usually a special purpose vehicle to be granted a lease of the airspace above the roof of a building (typically for a term of 20-25 years) with rights granted to affix the PV system to the roof in order to generate electricity. Where a lease is used, the tenant will want to retain ownership in the PV system in order to preserve its investment and will intend the PV system to be treated as a tenant's fixture so that it can be removed, or ownership in the PV system transferred, at the end of the lease term. The use of a lease/tenant's fixture structure has both SDLT and capital allowance implications, and care must be taken with the timing of the installation of the PV system if the intention may be to transfer ownership to a third party (eg by an assignment of the lease).

Leases tend to be favoured by commercial landlords, who are often reluctant to allow PV systems to be installed on their property without ensuring that the arrangements will not give rise to security of tenure under the Landlord and Tenant Act 1954. Affixing a PV system to an exclusive area of a property (eg airspace) for a fixed period of time and which confers exclusive possession to the tenant would ordinarily give rise to a formal business tenancy.

In the absence of legislative clarity, practitioners are unlikely to give unequivocal advice on whether PV systems will definitely be treated as either fixtures or chattels. The general approach is likely to remain that each individual case must be assessed on its facts, having regard to the individual technical characteristics and specifications of the PV system in question, its intended purpose and its frequency and ease of removal.

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WHY THIS MATTERS

The common law approach and fact-specific case law treatment of fixtures and chattels, coupled with the absence of any statutory certainty, makes this a particularly complex and uncertain area of law.

Government incentives to invest in renewable energy are likely to increase the number of investors entering into renewable energy projects. The financial viability of these projects is heavily dependent on the fixture and chattel analysis. Improvements in modern technology and evolving methods of installation, affixation and removal of renewable energy systems suggest that this area of law is likely to see more analysis in the courts in the future.

FURTHER READING:

- Section 2 of the Law of Property (Miscellaneous Provisions) Act 1989
- Part II of the Landlord and Tenant Act 1954
- Capital Allowances Act 2001
- Section 48(1) of the Finance Act 2003
- www.hmrc.gov.uk/cgt/intro/when-to-pay.htm
- www.hmrc.gov.uk/manuals/sdltmanual/sdltm04010.htm
- www.hmrc.gov.uk/capital-allowances/buildings.htm
- www.energysavingtrust.org.uk/Generating-energy/Getting-money-back/Feed-In-Tariffs-scheme-FITs