

# Tax in the construction industry

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A guide to tax issues in the construction industry. A high-level overview of the taxes and reliefs of particular relevance to the industry, the sources of those tax rules, the policy context, and developments on the horizon.

## Taxes specific to, or of particular relevance to, the industry

### Industry-specific taxes, duties and tax regimes

#### Construction industry scheme

The construction industry scheme (CIS) was introduced to prevent perceived tax evasion in the construction industry. It is a type of withholding at source, like pay-as-you-earn or interest withholding tax (see [Practice note, Withholding tax](#)). Under the CIS, those who make payments for construction services (contractors) under a “construction contract” may be required to deduct tax from payments to those who perform the services (sub-contractors). The focus of the CIS is on labour costs; no deduction is required if a payment is for building materials only.

Not all such payments made under a construction contract will fall under the CIS. The person making the payment must either be in the construction industry (a mainstream contractor) or have spent at least £3 million on construction expenditure in the last 12 months (a deemed contractor) to be required to register as a contractor under the CIS and make deductions.

The rate of deduction under the CIS, if the subcontractor is registered in its capacity as such with HMRC, is equal to the basic rate of income tax, currently 20%. The rate increases to 30% if the subcontractor is not registered with HMRC. It is also possible for subcontractors to apply to HMRC to obtain gross payment status if they have a good compliance history, enabling them to be paid without deduction under the CIS (see [Practice note,](#)

[Construction Industry Scheme \(CIS\): Contractor's gross payment status](#)).

There are exceptions to the CIS, including for payments made by a person for works on a property they use for their business and for reverse premiums to induce tenants to take new leases. The latter exemption was (subject to an anti-avoidance rule) extended to encompass the majority of landlord-to-tenant payments with effect from 6 April 2024, provided the relevant construction operations relate to works intended primarily for the benefit and use of the tenant. See [Practice note, Construction Industry Scheme \(CIS\): Exceptions](#) and [Practice note, Property inducement payments: tax: Construction Industry Scheme \(CIS\)](#).

For an overview of the CIS generally, see [Practice note, Construction Industry Scheme \(CIS\)](#).

#### Capital allowances for structures and buildings

Certain expenditure incurred on the construction, renovation or conversion of most UK commercial buildings and structures is eligible for capital allowances (“structures and buildings allowances” or SBAs). Since capital expenditure is non-deductible, the capital allowances regime provides a proxy for depreciation by spreading capital costs for tax purposes. SBAs are available at a flat rate of 3% per year (thereby “writing off” the capital expenditure over a period of 33.33 years). The expenditure will be “qualifying expenditure” if it is incurred on the construction (including renovation and conversion, and preparation of land as a site for construction) of a building or structure unless it is “excluded expenditure”. Excluded expenditure includes the acquisition or alteration (including reclamation or remediation) of the land. In its [Corporate Tax Roadmap 2024](#), published alongside the Autumn

2024 Budget, the government committed to maintain SBAs for the duration of the current Parliament.

For more information, see [Practice note, Capital allowances for structures and buildings](#).

### Residential property developer tax

The residential property developer tax (RPDT) was introduced with effect from 1 April 2022. The RPDT is intended to apply for a period of ten years and its purpose is to provide funds to remediate defective cladding on high-rise residential buildings. It applies to the trading profits of companies (and groups) arising from UK residential property development. The RPDT only applies to residential property developers that are corporation taxpayers. The rate is 4% and applies to profits over a threshold (in the form of an annual allowance) of £25 million. Special provisions apply in relation to the availability and use of deductions and loss reliefs.

RPDT is paid and collected as though it were corporation tax. For more information, see [Practice note, Residential property developer tax](#).

### Application of value added tax to the industry's main business activities

Supplies of construction goods and services are generally standard-rated for value added tax (VAT) purposes. This includes all supplies relating to commercial buildings and civil engineering works.

However, the VAT domestic reverse charge (DRC) can mean that the recipient, rather than the supplier, must account for VAT on certain construction services (see *VAT domestic reverse charge (DRC)*). In addition, certain supplies (relating to non-commercial property) can have several different VAT treatments

#### VAT domestic reverse charge (DRC)

The VAT domestic reverse charge (DRC) came into force on 1 March 2021. Like the CIS, the DRC is intended to counter fraud in the construction industry; in this case, a fraud by a supplier collecting output VAT from the customer but deliberately failing to account for that VAT to HMRC. The DRC solves this issue by requiring the customer to charge itself VAT as though it were the supplier, so that the VAT amount never passes through the supplier's hands.

The DRC applies to supplies of construction services, together with goods if they are supplied in the course of construction (unless there is a

separate supply of those goods). The definition of "construction services" is broadly aligned with the definition used for the CIS. As a result, the DRC does not generally apply in relation to supplies where the contractor is not required to operate the CIS (including where, for example, one of the CIS exemptions applies).

In addition, the DRC does not apply to what the legislation calls "end users", that is, those who are VAT and CIS registered businesses but who receive supplies of construction services for any purpose other than making further supplies of construction services. It also does not apply to supplies made to "intermediary suppliers" who make onward supplies of construction services (but without material alteration or further processing) provided they are either connected with end users or have an interest in the same property as an end user. The broad intent of these exclusions is to ensure that the DRC only applies to construction services supplied to other construction businesses. However, there is a notification requirement before the DRC is turned off for an end user or an intermediary supplier and if this administrative step is missed then the reverse charge obligation will still bite on the recipient.

For more information, see [Practice note, VAT reverse charge on construction services](#).

#### Dwellings

The supply of construction services in the course of the construction of a building designed as a dwelling or a number of dwellings (such as a house or a block of flats) is zero-rated. There are several conditions that have to be met for a building or unit to be a "dwelling", including a requirement for no internal access between units as well as the necessities of life (which include a kitchen and bathroom). In addition, planning permission must allow residential use and cannot prohibit the separate disposal of the units.

#### Relevant residential or charitable purpose

The supply of construction services in the course of construction of a building intended for use solely for a "relevant residential purpose" (RRP) or a "relevant charitable purpose" (this includes, for example, student accommodation and care homes) can also attract the zero rate.

However, unlike for dwellings, zero-rating applies only where those services are supplied directly to the person who is going to use the property for that purpose; the customer must issue a certificate to this effect. Construction services supplied to a

landlord or property developer may, therefore, still be subject to VAT at the standard rate (currently 20%). There is a “change of use” clawback rule (in effect triggering a deemed self-supply) which applies to recipients of zero-rated services for relevant residential or relevant charitable purposes where a change of use occurs within ten years of the zero-rated transaction.

Historically, HMRC took the view that as student accommodation fell within the RRP definition, the RRP rules rather than the dwelling rules applied to its construction. However, in 2014 they changed this position, accepting that student accommodation which met the conditions for being dwellings could be zero-rated under the more relaxed conditions that apply to dwellings (see [Practice note, VAT zero-rating of student accommodation](#)).

### Conversion and renovation

Supplies related to the conversion of non-residential property for residential use can attract the reduced rate of VAT (currently 5%). The reduced rate can apply to:

- A conversion where a dwelling is created where one did not exist before, or where the number of single dwellings is increased.
- A conversion of a building from a single household dwelling into a multiple occupancy dwelling.
- A conversion of a building for use for a RRP.
- A renovation of a qualifying residential building that has not been lived in for two or more years.

As for the zero rate, an additional requirement in the case of RRP is that the recipient of the construction services must be the person putting the property to use for the RRP.

### Building materials

The zero rate and the reduced rate also extend to supplies of building materials made as part of the same supply as the construction services. “Building materials” is defined by statute as “goods of a description ordinarily incorporated by builders in a building of that description” and does not include, for example, white goods. Other specified exclusions from “building materials” include fitted furniture, carpets and most electrical and gas appliances. The supply of such excluded items is likely to be standard rated.

### Energy saving materials

The zero rate applies to the installation and supply of energy saving materials in residential

buildings between 1 April 2022 and 31 March 2027. The special relief was extended, with effect from 1 February 2024, to installations of qualifying energy saving materials in buildings intended to be used by a charity (otherwise than in the course of a business). From 1 April 2027, all such eligible supplies will be subject to the reduced rate.

“Energy saving materials” is defined by statute and includes insulation, solar panels, wind and water turbines, and air and water heat pumps.

For more information, see [Practice note, VAT and property: an outline of the rules: Non-commercial buildings](#).

## Other general taxes

In respect of other general taxes, including corporation tax, there are no specific considerations that are particularly relevant to those operating in the construction industry. For a general summary of UK corporation tax, see [Practice note, Corporation tax: general principles](#).

## Tax reliefs

There are no tax reliefs, incentives or exemptions that apply solely to the construction industry.

However, corporation tax relief is available for the remediation of contaminated and derelict land in the form of Land Remediation Relief (LRR). LRR provides a deduction of 100%, plus an additional deduction of 50%, for “qualifying expenditure” incurred by companies in cleaning up land acquired from a third party in a contaminated state or in bringing long term derelict land back into use. Qualifying expenditure includes (in the case of contaminated land) the cost of establishing the level of contamination, removing the contamination or containing it so that the possibility of relevant harm is removed, and (in the case of derelict land) the cost of establishing what redundant structures are present and the cost of removing them. LRR is available in respect of both revenue and (subject to making an election) capital expenditure, and is claimed as a deduction in computing taxable profits for the purposes of corporation tax.

See also *Capital allowances for structures and buildings and Application of value added tax to the industry's main business activities*.

For more information, see [Practice note, Tax relief for remediation of contaminated and derelict land](#), and for discussion of the government's review of LRR, see *Future tax developments*.

### Taxes and ESG in the industry

#### Tax rules encouraging better environmental practices

There are no tax rules designed to encourage organisations in the construction industry to behave in a more environmentally friendly manner.

(For an overview of key considerations arising for the construction industry in relation to climate change, see Sector note, [Climate change and the construction industry](#), and for developments in relation to zero carbon buildings, see [Practice note, Zero carbon buildings](#).)

#### Tax rules designed to compensate for perceived detriment to society or the environment

The RPDT was introduced to provide funds to remediate defective cladding (see *Residential property developer tax*).

By way of background, in February 2021, the UK government had announced an additional £3.5m investment in building safety that included a commitment to fully fund the replacement of unsafe cladding in residential buildings six storeys and over in the UK. According to the Housing Secretary, this was partly funded by the RPDT as a “tax on developers to contribute to righting the wrongs of the past”.

As part of the same package, the government announced its intention to introduce a Building Safety Levy (BSL) to fund the remediation of safety defects. While the design and scope of the BSL has still not been fully finalised, it is expected to apply to developers of new residential buildings and be charged per square-metre of “chargeable floorspace”. It is anticipated the BSL will be collected and administered by local authorities, with rates depending on geographic region as well as whether the site is greenfield or brownfield land. Certain developments (including, for example, affordable housing, care homes, children’s homes, and developments with fewer than ten units) will be exempt. The government confirmed in the [Spring Statement 2025](#) that the BSL will be implemented from 1 October 2026 and will operate alongside the RPDT. For more information, see [Practice note, Building Safety Act 2022: Building Safety Levy](#).

### Avoidance, enforcement and penalties

#### Anti-avoidance measures or rules

HMRC appears to view the construction industry as an industry in which the opportunity for evasion is particularly heightened, and so there are now two separate regimes (the CIS and the VAT DRC) which are aimed at eliminating or reducing such opportunities by ensuring that the amount which is owed to HMRC is accounted for by the payer rather than the payee.

See *Construction industry scheme* and *VAT domestic reverse charge (DRC)*.

#### Key tax cases relevant to the construction industry

[Orsted West of Duddon Sands \(UK\) Ltd & Ors v Revenue And Customs \[2025\] EWCA Civ 279](#) is a case that considers when capital expenditure is “qualifying capital expenditure” for the purposes of claiming capital allowances.

The case concerns a Danish renewable energy group (Orsted) which carried out several preliminary environmental surveys in connection with the construction of offshore windfarm projects in the UK. The issue in dispute was whether Orsted could claim plant and machinery allowances on the cost of the pre-construction surveys, treating them as part of the “qualifying capital expenditure” on installing the windfarms. Whether it could or not depended on whether the cost of the surveys was a cost incurred “on the provision of” the windfarms (the relevant plant in the case). The Upper Tribunal had interpreted that requirement narrowly, holding that it does not extend to expenditure that merely enables a taxpayer to provide the plant.

After a lengthy and in-depth review of the relevant case law, the Court of Appeal held that the Upper Tribunal’s interpretation was too narrow. As a result, the court held that pre-construction capital expenditure could be “qualifying capital expenditure” where the expenditure fulfilled the following conditions, namely, that it:

- Informed the design of the plant or how it was to be installed.
- Related to the plant which was in fact acquired or constructed (confirming that expenditure on



purely speculative studies or on projects that are aborted will not qualify).

- Did not arise from characteristics or circumstances particular to the taxpayer.

In a helpful, obiter comment, the court referred directly to [section 270BB](#) of the Capital Allowances Act 2001 to support its conclusions. Section 270BB provides that, for the purposes of structures and buildings allowance (SBA), capital expenditure is “qualifying capital expenditure” if, among other things, it is “incurred on the construction of a building or structure”. The court also then referred to HMRC’s Capital Allowances Manual which states (at CA93110) that, “Expenditure treated as incurred on the construction of a building includes [...] professional fees relating to the design and construction of a building provided that the building is actually constructed” (see [HMRC: Capital Allowances Manual: CA93110](#)). Acknowledging the caution necessary when comparing the two separate regimes (for “plant and machinery” and “structures and buildings”), Newey LJ nevertheless states that, “it is hard to see why “professional fees relating to the design and construction of a building” should represent expenditure “on the construction of” a building if professional fees relating to the design and construction of plant do not amount to expenditure “on the provision of” the plant.”

The Orsted case provides comfort that if a pre-construction survey informs how to build a structure, and that structure is ultimately built, the cost of that survey should be “qualifying capital expenditure” for the purposes of SBA. (See [Legal update, Capital allowances available for expenditure on windfarm design and construction studies \(Court of Appeal\)](#)).

It should be noted that HMRC has been granted permission to appeal to the Supreme Court against the Court of Appeal’s decision (see [Orsted West of Duddon Sands \(UK\) Limited and others \(Respondents\) v Commissioners for His Majesty’s Revenue and Customs \(Appellant\) \(UKSC/2025/0069\)](#)).

### Recent HMRC investigations

There have not been any recent HMRC investigations focused on organisations in the construction industry.

### Reporting to HMRC

As well as being a mechanism for the collection of tax at source, the CIS also functions as a reporting mechanism. Contractors (that is, persons making payments in the construction industry) who are

required to be registered under the scheme must make monthly CIS returns to HMRC detailing the total amounts of payments they have made to each subcontractor, the cost of building materials, and the amount of tax withheld.

For more information, see *Construction industry scheme*.

## Policy and horizon scanning

### Key policy priorities governing the tax regime in the construction industry

For a discussion of the key policy priorities governing the tax regime in the construction industry, see *Tax rules designed to compensate for perceived detriment to society or the environment* and *Anti-avoidance measures or rules*.

### Future tax developments

In addition to the anticipated implementation of the BSL from 1 October 2026 (see *Tax rules designed to compensate for perceived detriment to society or the environment*), future tax developments in this area include potential changes to Land Remediation Relief (LRR).

In its [Corporate Tax Roadmap 2024](#), published alongside the Autumn 2024 Budget, the government announced that it would launch a consultation to review the effectiveness of LRR during 2025. The government previously consulted on the repeal of LRR in 2011 but decided to retain it at that time. The [consultation](#) was published in July 2025 with the stated intention of determining “whether [LRR] is still meeting its objective of boosting development of brownfield land”. In making that assessment, the review focuses on three core areas:

- The design of the relief (that is, its scope, eligibility and the type of relief given).
- The impact (or value) of LRR.
- How robust LRR is against error and abuse.

See [Legal update, Government consults on review of land remediation relief scheme](#).

It should be noted that the consultation takes the form of a request for information. It does not set out specific policy proposals or options. The consultation will close in September 2025, with responses and next steps to be published “in due course” (most likely at the time of the Autumn Budget 2025). For further discussion of LRR, see *Tax reliefs*.

### Sources of tax rules in the industry

#### Key legislation governing the tax regime in the construction industry

##### CIS

The CIS is contained in Part 3, Chapter 3 of the [Finance Act 2004](#), as well as the [Income Tax \(Construction Industry Scheme\) Regulations 2005 \(SI 2005/2045\)](#) (as amended).

##### VAT DRC

The VAT DRC is included in [section 55A](#) of the Value Added Tax Act 1994, with further detail in the [Value Added Tax \(Section 55A\) \(Specified Services and Excepted Supplies\) Order 2019 \(SI 2019/892\)](#).

##### RPDT

RPDT is contained in sections 32 to 52 of, and Schedules 7 to 9 to, the [Finance Act 2022](#).

#### Devolved matters

The Scottish Parliament and Welsh National Assembly do not have devolved powers relating to any aspects of the tax regime applicable to the construction industry.

### Relevant HMRC manuals and materials

Relevant HMRC manuals and other published HMRC materials that are of particular relevance to the construction industry include:

- CIS Reform Manual ([HMRC: CIS Reform manual](#)).
- VAT Construction Manual ([HMRC: VAT Construction](#)).
- VAT domestic reverse charge guidance ([HMRC: VAT domestic reverse charge technical guide](#)).
- Residential property developer tax manual ([HMRC: Residential Property Developer Tax manual](#)).
- VAT Notice 708: Buildings and Construction ([HMRC: Buildings and construction \(VAT Notice 708\)](#)).

### Industry codes of practice

There are no industry codes of practice that are particularly relevant to tax in the construction industry.

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