



TAX TREATMENT OF PREDEVELOPMENT COSTS

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ICAEW welcomes the opportunity to comment on **Tax treatment of predevelopment costs consultation**, published by HMRC on 16 June 2026, a copy of which is available from this [link](#).

MAJOR POINTS

- The treatment of predevelopment costs as defined in the *Orsted West of Duddon Sands* decision creates a significantly increased commercial risk for long-term development projects, with businesses potentially receiving no relief for substantial predevelopment costs incurred in connection with long-term assets. This may unintentionally discourage investment in projects that support wider government objectives, including renewable energy and the transition to net zero. Similarly, this approach may disproportionately disadvantage the most responsible and innovative developers who are likely to incur more upfront feasibility and investigation costs.
- To provide businesses with certainty and support consistent compliance, HMRC should provide clear guidance on the treatment of historic claims following the *Orsted West of Duddon Sands* decision, including its expectations regarding closed periods and potential penalty exposure.
- The inconsistent tax outcomes that may arise depending on whether a business acquires an asset or develops it in house could lead to distortions in commercial decision making.
- The 'close connection' test should be supported by clear guidance and transitional easements. This represents a new approach and a significant departure from the established apportionment methodology and is likely to require businesses to make substantial changes to their systems and processes, increasing compliance costs and uncertainty.

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This response of 21 September 2026 has been prepared by ICAEW's Tax Faculty.

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EXISTING TAX TREATMENT

Question 1: How has the Supreme Court's judgment in *Orsted West of Duddon Sands (UK) Ltd and others v HMRC [2026]* affected your understanding of the tax treatment of predevelopment costs?

Question 2: To what extent has the judgment clarified the treatment of these costs in practice?

Question 3: In light of the judgment and HMRC's updated guidance, are there specific aspects where uncertainty remains? Please provide examples and explain why.

1. Members acknowledged that the Supreme Court's decision in *Orsted West of Duddon Sands* has provided greater legal clarity regarding the tax treatment of predevelopment expenditure in certain circumstances. However, they also noted that the decision represents a significant departure from the approach that many businesses have followed in practice for many years. As a result, the decision is expected to have a considerable impact on affected businesses, requiring changes to existing systems and processes. Members therefore expressed concern that, notwithstanding the increased legal certainty, the outcome is likely to be viewed unfavourably by many businesses and create both practical and commercial uncertainties.
2. The outcome creates a significantly increased commercial risk for businesses undertaking long-term development projects such as those in the *Orsted West of Duddon Sands* case. As many assets involving substantial predevelopment expenditure are held for the long term, businesses may ultimately receive no relief for these costs, despite the expenditure being essential the development of those assets.
3. Members expressed concern about HMRC's expectations in relation to prior accounting periods where businesses adopted a different interpretation of the law before the Supreme Court's decision in *Orsted West of Duddon Sands*. While businesses would be expected to correct any open returns where appropriate, there is uncertainty regarding HMRC's approach to closed periods and any associated penalty exposure. In order to give businesses greater certainty and promote consistent compliance, ICAEW recommends that HMRC provides clear guidance on its compliance expectations, including the treatment of historic claims and the circumstances in which penalties may arise.
4. Please note our comments at Question 4 regarding the 'close connection' test which is likely to have increased uncertainty for many businesses.

Question 4: What practical challenges do businesses face in applying the current rules to predevelopment costs?

5. The Supreme Court's decision in *Orsted West of Duddon Sands* introduces a materially different approach to determining whether predevelopment expenditure qualifies for capital allowances to that established in *JD Wetherspoon* (the 'close connection' test). Members are concerned that applying the 'close connection' test in practice will impose significant additional compliance burdens and create uncertainty for businesses undertaking large or complex capital projects.
6. Under the approach established in *JD Wetherspoon*, businesses were generally able to adopt a reasonable apportionment methodology where preliminary expenditure could not be attributed economically to particular assets. The Upper Tribunal recognised that many preliminary costs are, by their nature, overheads or project-wide costs for which detailed attribution would be impractical or disproportionate. This pragmatic approach was subsequently reflected in HMRC's published guidance.

7. The 'close connection' test requires businesses to undertake a significantly more granular analysis of expenditure. In practice, commercial projects rarely progress through clearly defined stages. Instead, they typically evolve over time through a series of interrelated activities undertaken by the same advisers and professional teams. For example, an engineering engagement may begin with a feasibility study before progressing to preliminary design work, structural assessments and detailed technical design. Determining the point at which these activities become sufficiently closely connected to the provision of a particular item of plant is unlikely to be straightforward and will often require businesses to make difficult judgement calls.
8. Members are concerned that many businesses do not currently record costs at the level of detail that the approach emerging from the *Orsted West of Duddon Sands* decision may require. Existing project management, accounting and invoicing systems have generally been designed around the long-standing apportionment approach accepted following *JD Wetherspoon*. As a result, businesses may need to redesign internal systems, revise project coding methodologies and obtain additional professional advice to demonstrate compliance with the new requirements. These changes are likely to increase both administrative burdens and compliance costs.
9. ICAEW therefore recommends that HMRC provides comprehensive guidance on the practical application of the 'close connection' test, supported by detailed examples covering common commercial scenarios. Consideration should also be given to transitional easements, recognising that businesses will require time to adapt their systems and processes to the new approach. This would help ensure that the policy objective of providing greater certainty is achieved without imposing disproportionate compliance costs.

Question 5: Has the judgment affected how businesses structure or incur predevelopment costs? If so, please provide examples, where possible.

10. It is too early to conclude how this might affect how businesses structure or incur predevelopment costs.
11. However, members expressed concern that the judgment may create inconsistent tax outcomes depending on whether a business acquires an asset or develops it in house. Where an asset is purchased, predevelopment costs will generally be reflected in the acquisition price and may benefit from relief, whereas businesses developing assets themselves may be denied relief for equivalent expenditure. This could create unintended distortions in commercial decision-making.
12. This also means that smaller businesses with less access to specialist tax resource are likely to be the most affected. Larger businesses may be more likely to seek professional advice and structure their affairs in a more tax-efficient way to maximise available reliefs.

TYPES OF COSTS

Question 6: What types of predevelopment costs are incurred in investment projects?

Question 7: Typically, what proportion of the total capital expenditure for an investment project is incurred on each type of predevelopment cost, and over how long are these costs incurred?

13. The type and proportion of cost varies considerably project to project but members advise us that it is not unusual for predevelopment costs to be more than 5% of total capital expenditure. Members also noted that businesses are unlikely to maintain records at a sufficiently granular level to quantify precisely the proportion of predevelopment costs falling within particular categories or tax treatments. Any such analysis would often require a

retrospective review of project expenditure and may therefore be difficult and costly to undertake.

Question 8: Why are these predevelopment costs incurred? For example, are they incurred for regulatory reasons, to inform business decisions, or other purposes? If costs are incurred for multiple purposes, please indicate where this is the case.

14. Members advise that predevelopment costs are incurred for a variety of purposes, often serving both regulatory and commercial objectives. A significant proportion of expenditure is incurred to satisfy planning, environmental and other regulatory requirements. Examples include environmental impact assessments, contaminated land investigations and remediation, archaeological surveys, ecological and habitat protection measures, noise and transport studies, and surveys relating to unexploded ordnance. These activities are frequently required before a project can obtain the necessary approvals to proceed.
15. Predevelopment costs are also incurred to protect the environment, preserve sites of historical or archaeological interest, and assess and mitigate potential impacts on local communities. In many cases, expenditure is undertaken to reduce risks rather than to create a tangible asset.
16. In addition, businesses incur predevelopment costs to inform investment decisions, including feasibility studies, site investigations and the assessment of new technologies. Members note that businesses seeking to pioneer new technologies or innovative developments are likely to be disproportionately affected, as they often face higher levels of upfront expenditure and greater uncertainty as to whether a project will proceed.
17. Many costs are therefore incurred for multiple purposes, making it difficult in practice to distinguish between expenditure undertaken for regulatory compliance, risk mitigation and commercial decision making.

Question 9: If an investment project does not go ahead, can any of the predevelopment costs be recovered? For example, through sale of surveys to another business interested in pursuing a similar project.

18. The members we engaged with indicated that, in their experience, these costs were never recoverable.

Question 10: To what extent do you consider that predevelopment costs should qualify for capital allowances or other forms of tax relief? Please explain your reasoning and indicate which types of predevelopment costs you believe are most important to have tax relief.

19. Members are concerned that the tax treatment of predevelopment costs following the *Orsted West of Duddon Sands* decision could disproportionately affect responsible developers who undertake extensive predevelopment activities, such as environmental and ecological surveys, noise and traffic assessments, community engagement and detailed risk assessments. These activities are often integral to responsible project planning and securing the necessary consents. Restricting relief for such expenditure may discourage best practice and produce outcomes that are inconsistent with wider government objectives to promote sustainable and well-planned development.

Question 11: For predevelopment costs where the tax treatment may be difficult to apply, what proportion of overall predevelopment costs do these typically represent?

20. Members advise us businesses are unlikely to maintain records at a sufficiently granular level to identify the proportion of predevelopment costs for which the tax treatment may be difficult to determine. Consequently, members were unable to provide a reliable estimate.

IMAPACTS

Question 12: Does the tax treatment of predevelopment costs impact business and investment decisions? If so, why is this and what are the impacts?

21. The tax treatment of predevelopment costs is typically reflected in investment appraisals and project modelling. Where there is a risk that expenditure will not qualify for tax relief, the after-tax cost of the project increases.
22. Members advise that costs for which no tax relief is available can increase the cost of funding and reduce expected returns. This may affect project viability and, in some cases, lead to investment decisions being delayed or projects not proceeding. Greater certainty around the tax treatment of predevelopment expenditure would therefore support investment by improving the predictability of project costs.

Question 13: What is your impression of the tax treatment of predevelopment costs in other jurisdictions? Does this treatment impact whether to invest in those other jurisdictions rather than the UK?

23. Members' understanding is that a number of other jurisdictions adopt tax treatments that more closely follow the accounting treatment of predevelopment expenditure, allowing costs to be capitalised and relieved through depreciation or equivalent deductions. Some jurisdictions also offer enhanced or accelerated reliefs for investment in environmentally sustainable or strategic infrastructure projects.
24. While investment decisions are driven by a range of commercial factors, members consider that the UK position can compare less favourably where significant predevelopment costs do not qualify for tax relief. This increases the after-tax cost of investment and may reduce the attractiveness of the UK relative to jurisdictions offering broader or more certain relief.
25. However, members note that the treatment varies considerably between jurisdictions and sectors. Further evidence and jurisdiction-specific analysis would be needed to quantify the impact on investment decisions.

Question 14: Are there other impacts that the government should be aware of, in relation to the tax treatment of predevelopment costs?

Question 15: How does the tax deductibility of predevelopment costs compare in value to other potential tax changes, such as features of the Corporation Tax system reducing the ability to claim Full Expensing? If there are particular incentives you would prefer to see, please set out what those are and any supporting evidence where possible.

26. Members considered that securing tax relief for predevelopment costs is an important issue in its own right. Such costs are often a necessary precursor to investment but, in some cases, do not attract tax relief despite being incurred wholly and exclusively for the purposes of a project.
27. Members were of the view that consideration should be given to introducing a specific mechanism to provide relief for appropriate predevelopment expenditure. For example, a targeted infrastructure relief could allow certain costs incurred in bringing forward major developments to qualify for tax relief where relief would not otherwise be available. We appreciate that such a relief would come at a cost to the Exchequer, and this would need to

be balanced against the government's aim to encourage investments of this nature to stimulate growth and investment in the UK and assist the UK in meeting emission targets and provide energy security.

28. As we stated at paras 101/2 in our recent Budget submission (ICAEW Representation 75/26):

101. Denying corporation tax relief on this element of the costs of major infrastructure projects acts as a disincentive to investment. It increases post-tax costs, makes it more difficult to calculate expected returns, and may cause suboptimal approaches to building infrastructure aimed at minimising any tax disallowance rather than delivering projects in the best and most efficient way.

102. Although there are several different ways to ensure that pre-development costs are allowable for tax, we suggest an explicit relief to avoid confusion or doubt and reduce the risk of further court cases that would take years to conclude. Any relief should be carefully designed to provide certainty, protect the exchequer, and avoid unnecessary boundary disputes. A clear and targeted regime would reduce tax uncertainty, support investment decisions, and help improve the delivery of projects of this nature.

APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory.** Tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament. A clear statutory basis ensures legitimacy, accountability, and public trust in the tax system.
2. **Certain.** As far as possible, the application of tax rules and compliance processes should be certain. Taxpayers should not normally need to resort to the courts to understand how the rules apply to their affairs.
3. **Simple.** The tax system should be easy to understand for all taxpayers and advisers. Complexity undermines trust, creates unfairness, and discourages compliance.
4. **Easy to administer.** Tax liabilities should be straightforward to administer for HMRC, agents, and all taxpayers. Taxes should be designed to work effectively in a digital environment, while administration must remain accessible to those with limited digital capability.
5. **Properly targeted.** Anti-avoidance rules and other targeted measures should be proportionate, clearly defined, and carefully scoped to achieve their policy objective without undermining simplicity or certainty. Poorly targeted measures add complexity and uncertainty, harming compliance.
6. **Stable.** Changes to the tax system should only be made when clearly justified by economic, social, or environmental goals. Transparent, purposeful reforms build confidence and move the system toward greater coherence and long-term stability.
7. **Subject to proper consultation.** Other than in exceptional circumstances, tax changes should be subject to open and meaningful consultation. Adequate time for stakeholder input improves policy quality, practicality, and public trust.
8. **Regularly reviewed.** Tax rules, reliefs, and policy-driven interventions should be subject to regular, transparent review to assess whether they remain relevant, effective, and aligned with current policy goals. Outdated or unjustified provisions should be reformed or repealed to maintain coherence.
9. **Fair and accessible.** The tax system should be fair and accessible in design and in operation, ensuring equitable treatment of taxpayers. Revenue authorities must exercise their powers proportionately, and all taxpayers should have timely access to HMRC assistance, independent appeal, and redress.
10. **Efficient.** The tax system should raise revenue in a way that minimises unnecessary distortions, compliance burdens, and resource misallocation. While all taxes affect behaviour to some degree, tax design should avoid cliff edges, unintended incentives, or inefficiencies that reduce economic wellbeing unless these serve a clearly defined policy aim.

For more information, please see [Ten Tenets for a Better Tax System | ICAEW](#)