Annual Investment Allowance

Capital expenditure is not necessarily an allowable deduction in computing trade profits but it may attract capital allowances. Capital allowances are treated as a trading expense and are deducted in arriving at taxable trade profits.

The Annual Investment Allowance (AIA) is available for expenditure on most plant and machinery, with certain exceptions. In the last five years the AIA has varied from £25,000 to the current allowance of £500,000. The chancellor had planned a reduction to £25,000 in January 2016 but he announced in June that the AIA will be reduced from £500,000 to £200,000.

While many businesses will not notice a practical difference as they do not spend over £200,000 on plant and machinery in a year, farming businesses spending over £200,000 will notice a difference in their tax liability. The timing of a large purchase could have tax implications.

The allowance is apportioned and maximum allowances for the year, and the period from 1st January 2016 are shown below:

Accounting year ending	Maximum AIA for the year	Maximum AIA from 1st January 2016 to accounting year end
31/12/2015	£ 500,000	N/A
31/01/2016	£ 475,000	£ 16,667
28/02/2016	£ 450,000	£ 33,333
31/03/2016	£ 425,000	£ 50,000
30/04/2016	£ 400,000	£ 66,667
31/05/2016	£ 375,000	£ 83,333
30/06/2016	£ 350,000	£ 100,000
31/07/2016	£ 325,000	£ 116,667
31/08/2016	£ 300,000	£ 133,333
30/09/2016	£ 275,000	£ 150,000
31/10/2016	£ 250,000	£ 166,667
31/11/2016	£ 225,000	£ 183,333
31/12/2016	£ 200,000	£ 200,000

Using an example of an accounting period ending on 31st May 2016, if you were to spend £400,000 on new plant and machinery in the Autumn of 2015, you would be able to claim Capital Allowances of £375,000 to reduce your taxable profit. If, however you waited until the Spring of 2016 to purchase the plant and machinery for £400,000, the maximum Capital Allowances you could claim to reduce your taxable profit would only be £83,333. The balance of the expenditure will secure writing down allowance at 18% in perpetuity.

Please note that purchases early in 2016 will have very limited allowances. This is worth considering carefully when Basic Payment Scheme payments are received.

If you are considering expenditure on plant and machinery, please do not hesitate to contact us to help ensure the timing of the expenditure is as advantageous as possible from a tax perspective.

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VAT on Grazing and Keep

For VAT purposes it is important to differentiate between a simple grant of grazing rights (zero rated) and the supply of the keep of animals, which might include a grant of grazing, but is standard rated.

HMRC would consider the supply to be one of keep where the landowner takes on the responsibility for the care and welfare of the animals while on his land. A daily inspection of the field would not constitute care for this purpose. A landowner might call in a vet to a sick or injured animal without reference to its owner in order to save time in a recognised emergency, or because he is aware that this is what the owner would do himself. This would only be evidence of care if it were understood between the parties that it was the landowner's actual responsibility to do so under the terms of the contract between them.

From 1st October 2012, new rules came into force which mean businesses that supply space for self storage of goods now have to charge the standard rate of VAT. A farming business which rents out shed space for the storage of crops, feeds, fertilisers or farm machinery to name a few examples should be aware of the changes. However, the renting out of sheds for storage of livestock does not count as self storage of goods and remains exempt.

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Sage Accreditation

We are pleased to advise that Gillian Dixon and Gail Kristiansen have again successfully completed their Sage Accreditation, making them official Sage Account Partners. They are always happy to help with software choices, training or general processing advice, so please do not hesitate to give them a call on our main Kelso number.

What would you like to see covered?

If there are topics that you would like to see covered in future issues please let us know and we will endeavour to include these going forward. Please contact Isla Young CA on 01573 224 391 (Isla.Young@renniewelch.co.uk).

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Farming Matters

Information and advice to help you grow your business | **renniewelch.co.uk**

Inside this issue...

RENNIE WELCH
accountants : audit . tax . investment . IT

Welcome

to our second edition of Farming Matters.

So far this autumn the yields seem to be holding up, the weather is a bit mixed and we all know about the general commodity price trend. In addition to this there is the introduction of the new basic payment scheme and all the uncertainty that that brings. At such challenging times for farming businesses I hope that you will find the articles contained in farming matters both practical and helpful.

For those of you contemplating capital expenditure there are some thoughts on the new annual investment allowance limits and the impact of the timing of expenditure, plus a comparison between hire purchase contracts and operating lease contracts as ways of financing such expenditure. In the summer budget the chancellor decided to seek consultation on extending farmers averaging to five years from the current two – we wait with baited breath for the outcome. Some readers will be considering how to save money and there is a piece outlining options to computerise financial records. Finally, as farms diversify and try to develop new income streams, the thorny issue of VAT raises its head and Laura covers off the grazing rent and self store aspects of these income sources.

I do hope that you find these articles helpful. However, if there are topics that you would like us to cover then please let us know as we want to make the bulletin dynamic and interactive.

Gordon Chisholm CA
Senior Partner

Keeping your own records

Many traditional businesses still operate traditional book keeping records, and work on the notion that "if it ain't broke don't fix it!"

Time and expense spent on updating to a computerised system can be seen as unessential in times where margins are tight, but the benefits can outweigh the initial cost. If you currently use a ledger book and hand this into your Accountant at the year end, they will then need to spend time analysing and entering it onto their own software. A compatible system can save time, and save you money. A computer system will also allow greater control of where your costs are going, rather than waiting for the year-end accounts to be prepared. Furthermore, keeping track of who owes you money can greatly help your cash flow.

When deciding to change systems it can be difficult to know what system to get, but your Accountants Practice can help with this decision. They will have their own recommendations and some are accredited Business Partners of various software companies. Asking your Accountant for advice will also ensure that what you get will link into their systems.

There are two basic options – a PC installed program or a "cloud" based solution. Generally a PC installed program will be put onto one computer where all the processing will be done. A "cloud" solution allows you access wherever you have an internet connection so a PC, Tablet, Mobile etc. Many "cloud" options also include links to download your bank statements directly from internet banking, to keep you up to date with your bank balances.

Next you need to consider what you actually want the program to do for you – would you like to be able to raise invoices, do you want to be able to use budgets, or enable your customers to pay online? Getting a demonstration of a couple of different programs will help you decide which features you need.

Finally, both setting up and training need to be considered. It is of little benefit to have a shiny new program and no idea which buttons to press! It is worth investing in training and again your Accountant can usually help – they know your business and are able to tailor both the system and training to meet your personal needs.

If you are looking at upgrading your accounting system we are happy to advise on the various software and cloud accounting packages available and which of these will best suit your needs.

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Fixed Asset Purchases – Hire Purchase v Leasing.

Many businesses require assets in order to operate but they may not have the capital available to buy the assets outright. However there are other options available to them in the form of purchasing the asset though a hire purchase agreement, or leasing the asset via an operating lease.

Hire purchase is attractive to most as it allows the purchase of expensive equipment while at the same time helps manage your cash flow. The finance company will purchase the equipment and repayments will be spread over a specified period. Ownership of the asset transfers to you on conclusion of the finance, therefore building up your equity. This is sometimes favoured over a bank loan as the interest is often cheaper. The tax advantages of hire purchase include the ability to claim capital allowances on the full asset value once the asset is in use, and the interest cost is tax deductable.

Operating leases are often used if a business has a high turnover of assets i.e. the assets become outdated quickly. Equipment can be renewed on a regular basis without incurring the large payments and charges of settling a hire purchase agreement early. There are cash flow savings to be made in the upkeep and insurance of the asset as the responsibility for these costs normally lie with the lessor. From a tax perspective the only benefit of an operating lease is that the total lease payments are usually wholly tax deductable. As the ownership of the asset remains with the lessor no capital allowances can be claimed.

When faced with whether to opt for a hire purchase or operating lease agreement, often the deciding factor is the you expect to require the asset, in relation to the assets useful life. Cash flow and your individual tax position may also play a part in the decision making process.

Should you wish to discuss any of the above situations before your next asset acquisition please do not hesitate to contact us.

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Extension of Farmer's Averaging to 5 years

Following a lengthy period of lobbying, the NFU were pleased when the chancellor announced in the budget in March that he would extend the provision for Farmer's Averaging to 5 years.

Farmer's Averaging is currently available over two years to smooth profits. It is advantageous when a farmer's top rate of tax is different in consecutive years. When used effectively, averaging shifts profits from a higher rate of tax in one year to a lower rate in another year, resulting in a tax saving to the farmer.

The consultation period ended on 7th September and the suggested options available to farmers were rather more restrictive than expected.

The first option considered in the consultation is an annual claim based on the average of the previous 4 years taxable profits being less than 70% of the current year, or the current year taxable profits being less than 70% of the average of the previous 4. In this case, all 5 years may be averaged to smooth out the profits.

The second option considered does not include the annual volatility test described above but is an irrevocable election for 5 years. The profits for each of the 5 years following the election are averaged with the four years immediately preceding each respective year. For example, an election made in 2016/17 to average profits from 2011/12 to 2016/17 would then remain in place until 2021/22.

Some farming clients may not wish to commit to an irrevocable election, perhaps as the rate of tax ultimately payable would be uncertain. The recent regime around 100% Capital Allowances claims has also brought volatility in taxable profits and for many an inherent profit that remains to be taxed. This would seem to be weighed against the merits of more consistent taxable profit levels and resultant consistency of tax payments.

Given the uncertainty and historic volatility of farming profits, along with the encouragement to increase diversification and continued effect of Capital Allowance claims, we are interested to see the results of the consultation and assess how the outcome will affect our farming clients.

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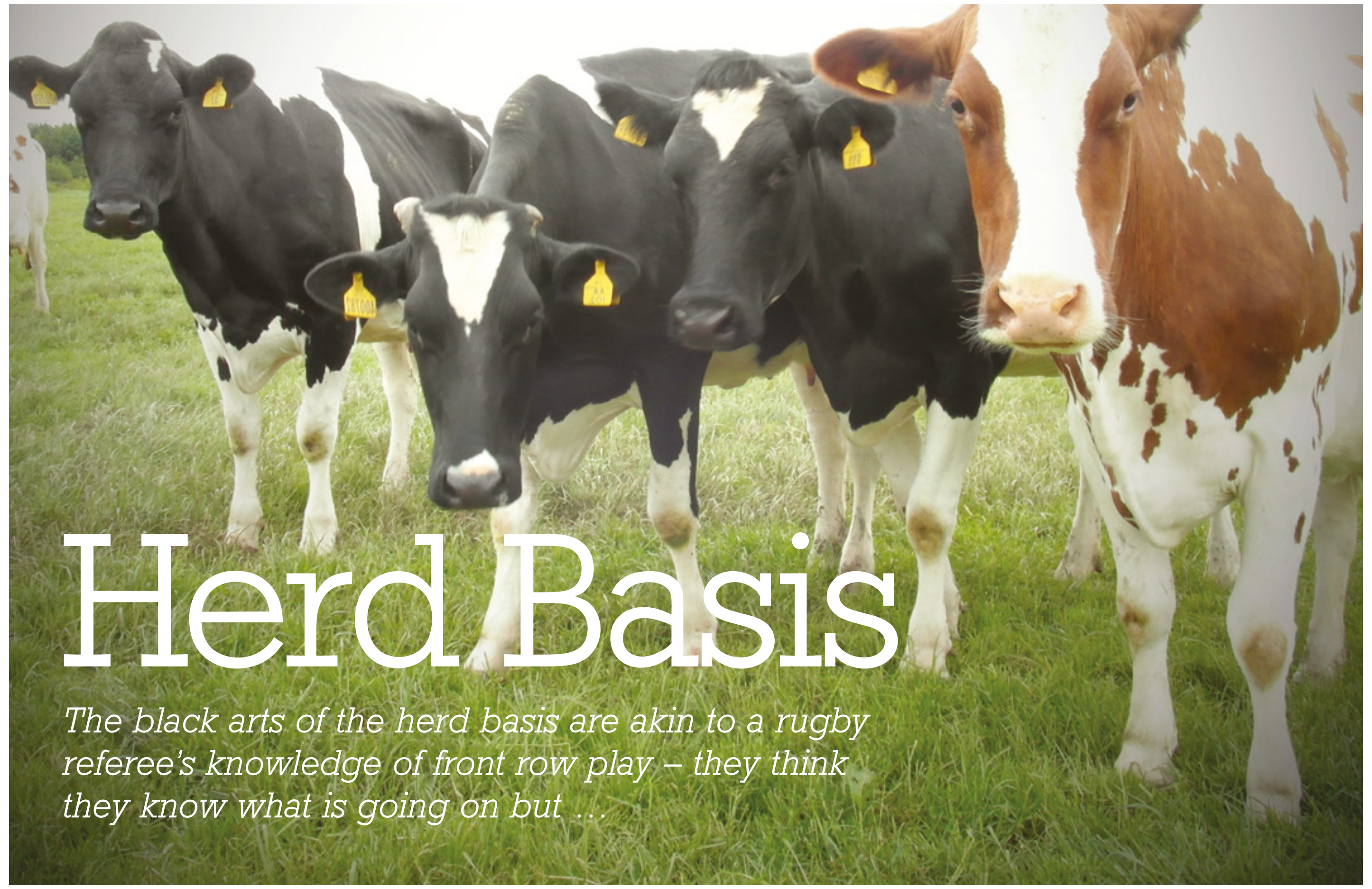

Herd Basis

The black arts of the herd basis are akin to a rugby referee's knowledge of front row play – they think they know what is going on but …

Normally stock is valued at the lower of cost or net realisable value and this is known as the trading basis for valuation purposes. Farmers can elect to use the herd basis which treats their herd or flock more like a capital asset. In order to qualify for the election you need to have a production herd which can also be a flock; however, it should be borne in mind that the election would apply to the same species irrespective of the breed. The cattle or sheep must be kept for the products that they produce i.e., progeny or any other product except one that could be obtained through slaughter so this is principally milk, eggs, or honey. So a beekeeper could elect for the herd basis although one would not want to deal with the stock reconciliation.

Generally speaking the election applies to mature animals i.e., a female that has produced a calf or a lamb and for male animals when they have been first used for breeding. That said some immature stock can be included if they are hefted. This means that owing to the nature of the land, only stock reared on that land can be used as replacements to maintain the numbers in the flock. It is important to note that this does not apply to closed herds and flocks for health reasons as this is unlikely to relate to the land.

In practical terms the cost of any replacement animal brought in is allowed for tax purposes but where the stock numbers are increasing the value of the animals bought would be added to the capital value of the herd or flock. In addition, if the replacement animal is of much better quality then a view needs to be taken so that the improvement value is added to the capital sum of the herd or flock.

The benefits of the election are that the maintenance cost is always allowed for tax purposes and if there is any disposal of the herd or a substantial part thereof then the profit is not taxed however if there is a deficit then no tax relief would be available. It is important to realise that if the herd is then built up in part or in full within five years then the profit would actually come back into charge for tax. The election is irrevocable and so great care must be taken when making that decision and it is not available to businesses that have had flocks and herds for many years unless there is a partnership change as there are tight time limits for making the election.

It is a very interesting and complicated area for livestock breeders and worth consideration even if no election is ultimately made.

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