Osborne Books Update

Business Tax Tutorial

FA2020

Postponement of Change in Annual Investment Allowance (AIA)

Introduction

In November 2020, the government announced that the planned change to maximum Annual Investment Allowance due to take place on 1st January 2021 would be postponed. This means that the change from a maximum AIA of £1,000,000 to £200,000 that was due to affect periods straddling, or starting after, 1st January 2021 will not now happen.

The AAT has announced that the Finance Act 2020 examinations that will be held during 2021 will take account of this postponement. Therefore, the maximum annual AIA of £1,000,000 will apply to all periods starting on, or after, 1st January 2019. This will have an impact on capital allowances under both Corporation Tax and Income Tax.

Since the Osborne Books Business Tax (Finance Act 2020) Tutorial, and other materials were created before this announcement, the following amendments now need to be made to the affected pages in our Tutorial.

Revisions and deletions are shown in RED in the text that follows.

We apologise for any problems that this will cause for both tutors and students.

Please note that the revised pages from the AAT guidance material are produced here for reference. Fully updated guidance is available from the AAT website.

Annual Investment Allowance (AIA)

This provides a very simple system for companies to claim capital allowances. The Annual Investment Allowance applies to virtually all plant and machinery **except cars**, and provides an allowance of the whole amount spent on this plant and machinery, up to a total amount of £200,000 for CAPs ending on or before 31/12/2018. The limit is £1,000,000 for CAPs starting on or after 1/1/2019. ~~and ending on or before 31/12/2020. For CAPs starting on or after 1/1/2021 the limit is £200,000~~. For CAPs that straddle 31/12/2018 ~~or 31/12/2020~~ there are special rules that we will examine shortly.

Any acquisitions in a year that exceed the relevant limit are dealt with through the pooled system that we will look at shortly, and will then be eligible for other capital allowances.

The key features of the scheme are:

- it applies to the acquisition in the Chargeable Accounting Period of virtually all plant and machinery except cars
- it is available for the first £200,000/£1,000,000 of qualifying expenditure per 12 month CAP
- the relevant limit is reduced proportionally if the CAP is less than 12 months (eg the limit is £750,000 for a nine month CAP starting on or after 1/1/2019)
- it gives a capital allowance equal to the whole of such expenditure, and this allowance can then be deducted in the calculation of adjusted trading profits

example

Suppose A Limited had adjusted trading profits (before capital allowances) of £1,900,000 for the CAP 1/1 /2020 to 31/12/2020.

If during the CAP it spent £120,000 on plant and machinery, it could set the whole £120,000 against trading profits, giving a trading income assessment of £1,780,000.

or

If during the CAP it spent £1,045,000 on plant and machinery, it could set £1,000,000 (the maximum) against trading profits, giving a trading income assessment of £900,000 before other capital allowances. The remaining £45,000 expenditure would be subject to capital allowance claims through the pooling system.

We will shortly look at how this works and what allowances can be claimed.

In some cases groups of companies may not be entitled to the normal annual limit for each company in the group, but may be required to share the limit between the companies. This could occur if the companies shared premises or had similar activities.

AIA in CAPs straddling 31 December 2018

As noted already, the AIA annual limit changed on 31 December 2018 from £200,000 per year to £1,000,000 per year. Where a CAP straddles 31 December 2018, the maximum AIA for the whole CAP will be based on calculating proportions of each limit based on the length of time of each part of the CAP and adding them together.

For example, the maximum AIA for a CAP for the 12 month period from 1 October 2018 to 30 September 2019 would be calculated as follows:

Period 1/10/2018 – 31/12/2018	£200,000 × 3/12	£50,000
Period 1/1/2019 – 30/9/2019	£1,000,000 × 9/12	£750,000
Maximum AIA for whole CAP		£800,000

AIA in CAPs straddling 31 December 2020

The AIA annual limit changed on 31 December 2020 from the temporary £1,000,000 per year that had been in place for two years to £200,000 per year. Where a CAP straddles 31 December 2020, the maximum AIA for the whole CAP will be based on calculating proportions of each limit based on the length of time of each part of the CAP and adding them together.

For example, the maximum AIA for a CAP for the 12 month period from 1 October 2020 to 30 September 2021 would be calculated as follows:

Period 1/10/2020 – 31/12/2020	£1,000,000 × 3/12	£250,000
Period 1/1/2021 – 30/9/2021	£200,000 × 9/12	£150,000
Maximum AIA for whole CAP		£400,000

pooled expenditure calculations

There are some situations that fall outside of the AIA. These are:

- balances of unrelieved capital expenditure brought forward from earlier periods
- expenditure during the period on cars
- expenditure on plant and machinery during an accounting period in excess of the AIA limit
- disposals during the period of plant and machinery

These situations require a working involving one or more expenditure ‘pools’. Each pool requires a separate calculation (shown in a separate column) in the capital allowance computation that will be used to calculate any capital allowances that are claimable. Separate pools are used for:

Case Study

SPENDER PLC: PLANT AND MACHINERY CAPITAL ALLOWANCES

Spender plc has a Chargeable Accounting Period running from 1 April 2020 to 31 March 2021. At the start of the period, the following balances were brought forward in its capital allowances computation from the previous year:

General (main) pool	£48,000
Single asset pools:	
Short-life asset	£20,000

During the Chargeable Accounting Period y/e 31/3/2021, Spender plc had the following transactions in plant and machinery:

Purchases (cost)	
Equipment	£32,000
Van	£17,000
Lorries	£850,000
New 'Low-Emission' Car	£28,000
Car with emissions of 200 g/km	£19,000
Disposals (proceeds)	
Short-life asset	£13,000
Plant (main pool)	£10,000

Spender plc had adjusted trading profits (before capital allowances) for the CAP y/e 31/3/2021 of £1,500,000.

required

(a) Calculate the total capital allowances claimable for the CAP.

(b) Calculate the assessable trading profits after deducting capital allowances.

solution

(a) Of the expenditure during the CAP, the following items are eligible for AIA, and are within the annual limit of £1,000,000.

	£
Equipment	32,000
Van	17,000
Lorries	850,000
	899,000

Note that the expenditure on the cars is not eligible for this allowance.

~~The expenditure in excess of the AIA allowance will be added to the main pool and be eligible for writing down allowances (WDA) at 18%~~.

The capital allowance computation using the pools can now be built up (see table on the next page). We will use one column for each pool, plus a further column on the right hand side to collect and total the allowances.

(b) Following the capital allowances computation shown on the next page, the assessable trading profit can now be calculated:

	£
Adjusted trading profits (before capital allowances)	1,500,000
less capital allowances	(941,980)
Assessable trading profit	558,020

The notes below explain some of the more complex issues in the capital allowances computation. Make sure that you can understand all the points so that you could build up a similar solution without any template.

(1) The new low-emission car had a 100% first year allowance (FYA). The balance after deducting the allowance from the cost (in this case zero) is notionally added to the main pool. When the car is ultimately sold the proceeds will be deducted from the main pool.

(2) The acquisitions qualifying for AIA are within the £1,000,000 limit. ~~The excess is added to the main pool~~.

(3) The writing down allowances are calculated as:

(a) main pool £38,000 × 18% = £6,840

(b) short-life asset – no WDA since asset has been disposed of

(c) special rate pool £19,000 × 6% = £1,140. The car was entered into this pool as it has emissions over 110 g/km.

(4) The balancing allowance on the short-life asset pool is claimed to close the pool with a zero balance.

(5) The written down values carried forward on the two remaining pools will be used to start the computation for the next period.

		Main pool	Short-life asset	Special rate pool	Capital allowances
		£	£	£	£
WDV bf add		48,000	20,000		
Acquisitions					
without FYA or AIA:					
Car (200 g/km)				19,000	
Acquisitions					
with 100% FYA:					
Low-emission					
car (1)	£28,000				
100% FYA	£(28,000)	0			28,000
Acquisitions qualifying for AIA (2)					
Equipment	£32,000				
Van	£17,000				
Lorries	£850,000				
	£899,000				
AIA	£(899,000)				899,000
~~Excess~~		~~99,000~~			
less					
Proceeds of disposals:		(10,000)	(13,000)		
		38,000	7,000	19,000	
18% WDA (3)		(6,840)			6,840
6% WDA (3)				(1,140)	1,140
Balancing Allowance (4)			(7,000)		7,000
WDV cf (5)		31,160	0	17,860	
Total Capital Allowances					941,980

The reference numbers shown above are linked to the explanation shown on the previous page.

CAPITAL ALLOWANCES FOR SHORT CAPS

So far in this chapter we have examined the way that capital allowances for plant and machinery are calculated for Chargeable Accounting Periods of twelve months.

It is, however, possible to have CAPs for less than twelve months, and this can arise either:

- if the accounts are prepared for a period of less than twelve months, or
- where accounts are prepared for a period exceeding twelve months, and are divided into two CAPs, one for the first twelve months, and another for the balance, which will be for less than twelve months

In each of these situations, the impact on capital allowances for plant and machinery in the short CAP is as follows:

- First Year Allowances, Balancing Allowances and Balancing Charges are unaffected and are calculated as normal.
- Writing Down Allowances are time-apportioned based on the short CAP (taking account of the change in special pool rate on 1 April 2019 if applicable).
- the Annual Investment Allowance maximum limit is time-apportioned based on the short CAP. This is also based on the limits that apply to the periods before and/or after 31 December 2018, ~~and before and/or after 31 December 2020~~.

DEALING WITH THE ACCOUNTS FOR A LONG PERIOD

As we saw in the last chapter, where we have accounts that are prepared for a long period, the procedure is:

- the accounting profits for the long period are adjusted in one computation, before deducting capital allowances
- this adjusted profits figure is then time-apportioned into the two CAPs
- capital allowances are calculated separately for each CAP
- each CAP's adjusted profit is then finalised by deducting the capital allowances that have been calculated for that CAP

We can now examine the issues involved in creating two capital allowance computations, one for each CAP within a long period for which accounts were prepared. The points to note are:

- each acquisition and disposal of assets needs to be allocated to the correct CAP, and incorporated in the appropriate computation

Chapter Summary

- Capital allowances are available on certain non-current (fixed) assets, and act for tax computation purposes as an alternative to depreciation, which is never allowable as tax-deductible (set off against tax).
- The main type of capital allowances is for 'plant and machinery'.
- Plant and machinery includes vehicles, computers, and various other assets.
- An annual investment allowance is available for the whole cost of virtually all plant and machinery, except cars, up to a maximum of £200,000 for 12-month periods ending before 1/1/2019 and £1,000,000 for 12-month periods after 1/1/2019 ~~and 31/12/2020, and £200,000 after that date~~.
- Allowances include 100% first year allowances for new low-emission cars, and zero emission goods vehicles. There are also writing down allowances at various rates depending on the circumstances.
- Most assets are merged together or 'pooled' in the capital allowance computation, but some need to be kept separately in 'single asset pools'. Single asset pools are used for short-life assets. Balancing allowances and charges occur in single asset pools when the asset has been disposed of, and also in the general pool and special rate pool when the business ceases.
- When capital allowances are calculated for a Chargeable Accounting Period of less than twelve months any writing down allowances are time-apportioned. The AIA limit is also time-apportioned.
- First year allowances and balancing allowances and charges are unaffected by short CAPs. Where the accounts for a company have been prepared for a period of over 12 months, the two CAPs that result will each require a separate capital allowance computation. Non-current asset acquisitions and disposals will need to be allocated to the correct CAP before these capital allowance computations are carried out.

solution

The capital allowance computation is shown below. The notes that follow provide explanations.

		Main pool	Car (BMW) 25% private	Car (Audi) 25% private	Capital allowances
		£	£	£	£
WDV bf		30,000	15,000		
add					
Acquisitions					
without FYA or AIA:					
Ford Car (105 g/km)		11,000			
Audi Car (100 g/km)					
(25% private use)				25,000	
Acquisitions qualifying for AIA:					
Computer	5,000				
AIA claimed	(5,000)	0			5,000
Pick up truck	20,000				
AIA claimed	(20,000) × 80%				16,000
less					
Proceeds of Disposals:					
Machine		(2,000)			
BMW			(14,000)		
		39,000	1,000	25,000	
WDA 18%		(7,020)		(4,500) × 75%	10,395
Balancing Allowance			(1,000) ×75%		750
WDV cf		31,980	0	20,500	
Total Capital Allowances					32,145

- The only additions that do not attract AIA or FYAs are the two cars. The Audi has 25% private use so is kept separate, while the Ford joins the main pool. Both cars have emission levels of 110 g/km or less and so are entitled to 18% writing down allowances.
- The limit of AIA on purchases is £1,000,000. The £5,000 cost of the computer can be claimed in full, and the whole £20,000 cost of the truck is eligible for AIA. The £20,000 is then restricted for the 20% private use.
- The disposal proceeds of the machine are deducted from the main pool.
- The WDA on the Audi is £4,500 × 75% business use. Note that the full £4,500 is used to calculate the WDV carried forward.

3.2

		Main pool	S/L asset	Capital allowances
		£	£	£
WDV bf		60,000	10,000	
add				
Acquisitions				
without FYA or AIA:				
Car (95 g/km)		24,000		
Acquisitions qualifying for AIA:				
FL Truck	30,000			
Computer	5,000			
	35,000			
AIA claimed	(35,000)*			35,000
		0		
less				
Proceeds of Disposals:		(3,000)	(4,000)	
		81,000	6,000	
WDA 18%		(14,580)		14,580
Balancing Allowance			(6,000)	6,000
WDV cf		66,420	0	
Total Capital Allowances				55,580

*The maximum AIA limit for the CAP is: £1,000,000

Trading Income for CAP year ended 31/3/2021:

	£
Adjusted trading profits	154,000
Plant & Machinery Capital Allowances	(55,580)
Trading Income	98,420

3.5 PLANT & MACHINERY CAPITAL ALLOWANCES COMPUTATION:

		Main pool	Special rate pool	Capital allowances
		£	£	£
WDV bf		90,000	13,000	
Additions				
without FYA or AIA:				
BMW Car			27,000	
Low-Emission Car	20,000			
100% FYA	(20,000)	0		20,000
Additions qualifying for AIA:				
Plant	790,834			
AIA	(790,834)			790,834
[limit of 10/12 x £1,000,000 = £833,333]		0		
Disposals				
Plant		(1,000)		
		89,000	40,000	
WDA 18% × 10/12		(13,350)		13,350
WDA 6% × 10/12			(2,000)	2,000
WDV cf		75,650	38,000	
Total Capital Allowances				826,184

	£
Adjusted trading profit for 10 month CAP to 31/1/2021	1,510,000
less capital allowances	(826,184)
Trading Income assessment	683,816

1. Taxation tables for business tax – 2020/21

1.1. Capital allowances

Annual investment allowance

Prior to 1 January 2019	£200,000
From 1 January 2019 ~~and 31 December 2020~~	£1,000,000
~~From 1 January 2021~~	~~£200,000~~

Plant and machinery writing down allowance	
Assets other than motor cars	18%
Motor cars	
CO_2 emissions up to 50 g/km	100%
CO_2 emissions between 51 and 110 g/km	18%
CO_2 emissions over 110 g/km -Prior to 1 April 2019/6 April 2019	8%
CO_2 emissions over 110 g/km -From 1 April 2019/6 April 2019	6%

1.2. Capital gains

Annual exempt amount	£12,300
Basic rate	10%
Higher rate	20%
Business asset disposal relief rate	10%
Investors' relief rate	10%
Business asset disposal relief lifetime allowance	£1,000,000
Investors' relief lifetime allowance	£10,000,000

1.3. National Insurance rates

Class 2 contributions:	£3.05 per week
Small profits threshold	£6,475p.a.
Class 4 contributions:	
Main rate	9%
Additional rate	2%
Lower profits limit	£9,500
Upper profits limit	£50,000

6.2. Example 2 – relevant period is greater than 12 months

Vaughan changes his accounting date as follows:

Accounts	Year	Period
Year to 31 December 2019	2019/20	1/1/19 to 31/12/19
15 months to 31 March 2021	2020/21	1/1/20 to 31/3/21
Year to 31 March 2022	2021/22	1/4/21 to 31/3/22

Year of change – 2020/21
Relevant period – 15 months to 31 March 2021
Basis period for 20/21 – 15 months to 31 March 2021

7. Capital allowances on plant and machinery

7.1. Layout of capital allowances on plant and machinery computation

(see taxation tables for rates)

	First Year Allowance (FYA)	Annual Investment Allowance (AIA)	General pool	Special rate pool	Short Life Asset	Total allowances
	£	£	£	£	£	£
WDV b/f			X	X	X	
Additions	X	X	X			
Disposals			(X)		(X)	
	X	X	X	X	X	
Balancing allowance/balancing charge (BA/BC)					X/(X)	X/(X)
					Nil	
AIA/FYA	(X)	(X)				X
Writing down allowance@ 18% pa			(X)			X
Writing down allowance@ X% pa				(X)		X
WDV c/f	Nil	Nil	X	X		
	===	===	===	===		
Total allowances						X
						===

- Plant – defined by 'function/setting' distinction and case law.
- AIA – 100% allowance for expenditure (other than cars) in 12-month period (pro rata). Expenditure in excess of AIA qualifies for writing down allowance (WDA). If the accounting period straddles 1 January 2019 ~~or 1 January 2021~~, the AIA must be pro-rated.