

CAPITAL ALLOWANCE CHANGES IN APRIL 2012

From 1 April 2011, the Government reduced the rates of corporation tax for all companies. However, in order to 'pay' for this reduction, the Government has changed the capital allowances system for **all** businesses, not just companies, to take effect from April 2012.

CHANGES TO THE ANNUAL INVESTMENT ALLOWANCE (AIA)

The main change is to reduce the maximum AIA from its current level of £100,000 to £25,000 for expenditure incurred on or after 6 April 2012 (1 April 2012 for companies).

As the accounting periods of many businesses will span these start dates, a pro rata calculation of their maximum entitlement will be required. Where a business has an accounting period that spans the 1 or 6 April 2012, the maximum allowance for that period is the sum of:

- the maximum AIA entitlement based on the previous £100,000 annual cap for the portion of the accounting period falling before the 1 or 6 April 2012; and
- the maximum AIA entitlement based on the new £25,000 cap for the portion of the accounting period falling on or after the 1 or 6 April 2012.

However, a restriction is set so that, for expenditure incurred in the part of the accounting period falling on or after 1 or 6 April 2012, the maximum entitlement is given only by reference to the second bullet point above.

This does not affect the business's maximum AIA for the accounting period as a whole but rather the amount of expenditure after the relevant start date that may be covered by the AIA.

Example 1

A business makes up its accounts to 30 September annually. For the year to 30 September 2012, the limit is calculated as follows:

October 2011 – March 2012	$6/12 \times £100,000$	=	£50,000
April – September 2012	$6/12 \times £25,000$	=	£12,500
Total			£62,500

If, in the six months to March 2012, the business spends £60,000 on purchases of machinery, it will all qualify for AIA as it is below the total available AIA of £62,500.

Example 2

For the six months to 30 September 2012, the limit on expenditure qualifying for the AIA is £12,500.

If the business spends £60,000 in the six months to September 2012, only £12,500 will qualify for AIA.

TIMING

Obviously, the timing of expenditure may be critical, particularly in light of the rather strange '£12,500 rule' in the example above. Consideration should be given to ensuring that expenditure is **incurred** before the 1 or 6 April 2012, as the date that expenditure is incurred usually triggers the entitlement to capital allowances.

TRAPS FOR THE UNWARY

Two points are worth noting in relation to the trigger point for capital allowances.

Firstly, the normal rule is that expenditure is incurred on the date on which the obligation to pay becomes unconditional. The contract for purchase will be evidence of when this arises. So if the contract specifies that payment is required within 30 days of delivery, the obligation to pay arises on the date of delivery.

However, if there is a gap of more than four months between the date on which the obligation to pay becomes unconditional (eg delivery) and the date on which payment is required to be made, the expenditure is not treated as incurred until the date on which payment is required to be made. This could, for example, apply to interest-free credit arrangements.

Secondly, a special rule applies to hire purchase agreements. Usually all of the capital expenditure incurred under a hire purchase contract is treated as incurred up front. However, if the asset is not brought into use by the end of the accounting period, any capital expenditure not incurred at the end of that period is deferred until the asset is actually brought into use.

CHANGES TO WRITING DOWN ALLOWANCES (WDAs)

For accounting periods commencing on or after 6 April 2012 (1 April 2012 for companies), the rates of WDAs per annum on expenditure not relieved by other allowances is reduced as follows:

- from 20% to 18% on expenditure allocated to the main pool; and
- from 10% to 8% on expenditure allocated to the special rate pool.

Transitional rules apply for accounting periods which span 1 or 6 April 2012. The broad effect of the rules is to give a rate for the transitional period between 20% and 18% (or 10% and 8%).

This change affects all the main rates which apply to plant and machinery, including cars.

WHAT TO DO

As you can see, the changes are not positive for businesses but, with a bit of careful planning, the rules for capital allowances can be maximised. If you would like to discuss these changes in more detail, please feel free to get in touch.