

Annual Investment Allowance (AIA) will revert to £200,000 on 1 January 2021

Key Point

Businesses planning large capital purchases in the period up to and around 31 December 2020 should consider accelerating their plans to make the acquisition prior to 31 December 2020 to maximize tax relief.



Annual Investment Allowance

The annual investment allowance (AIA) gives 100% tax relief for qualifying plant and machinery expenditure incurred in an accounting period up to a specified annual amount each year.

AIA was capped at £200,000 per annum up to 31 December 2018 but was temporarily increased to £1m per annum for each of the two years ended 31 December 2020. It reverts to £200,000 on 1 January 2021.

There are transitional rules to deal with the reduction in AIA which can result in allowances being lost where businesses have an accounting period that straddles 31 December 2020. The timing of expenditure is therefore important.



Transitional Rules

To calculate the AIA that is due for a company with an accounting period straddling 1 December 2020, the following calculation is used:

$$(A/12 \times \text{£1m}) + (B/12 \times \text{£200,000})$$

Where:

A = number of months in the accounting period that arise before 31 December 2020.

B = number of months in the accounting period that arise after 31 December 2020.

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For an accounting period 1 April 2020 – 31 March 2021 the maximum AIA for the year is:

$$(9/12 \times £1m) + (3/12 \times £200,000) = £800,000$$

It is not as straightforward as the company claiming £800,000 though, as it depends on when the expenditure is incurred in a transitional year.



Transitional Rules – Example

Say a business with a 31 March 2021 year end purchases two items of plant costing £400,000 each.

One is purchased on 31 October 2020 and one on 31 January 2021. The total expenditure is £800,000 and so you would be forgiven for assuming that the full amount qualifies for AIA at 100%.

However, as the second item of plant was purchased in the period after 31 December 2020, the claim for that period is restricted to the AIA limit applying to 1 January 2021 to 31 March 2021 period – and so is restricted to £50,000.

So, the AIA claim for the period is £400,000 for the first machine plus £50,000 for the second, so a total of £450,000.

The remaining £350,000 of expenditure will qualify only for writing down allowance (18%).
If both machines had been purchased before 31 December 2020, the maximum £800,000 AIA could have been claimed.

The timing of expenditure is key. Be aware, the closer your year end is to the 31 December 2020 transition date, the greater potential there is for allowances to be lost.

Should you wish to discuss this in more detail then please get in contact with us.