ESC 4 Depreciation Allowances on Farmhouses

People in business for themselves are taxed upon a level of profits based on their business accounts. Under normal accounting principles the profit and loss account does not include capital expenditure, which is therefore not deductible for income tax purposes. However, the Falkland Islands tax code includes a stand-alone system of Depreciation Allowances to give relief for the reduction in value of capital assets over time. Allowances due under the relevant rules as laid down in Chapter 2 of Part 5 of the Taxes Ordinance 1997 are treated as an expense of the business in arriving at the amount of assessable profits. The legislation stipulates that deductions may only be given in respect of expenditure incurred for the purposes of the business, and that if a building is used partly for non-business purposes no allowance will be given in respect of the non-business use. This rule is disregarded in respect of farmhouses occupied as the private residence of the farmer, where otherwise one would expect to have to calculate a business / private split. All capital expenditure on owner-occupied farmhouses will therefore qualify for Depreciation Allowances.

This concession only relates to capital expenditure, and does not extend to expenditure on the maintenance, upkeep and ongoing expenses of running the farmhouse, which will still require to be apportioned between those expenses pertaining to the running of the business, which are allowable deductions in computing the profits of that business, and those pertaining to the private occupation of the house, which are not.

Other capital expenditure on buildings used wholly for the purposes of the business (such as barns, sheds, workers accommodation etc) will qualify in full for Depreciation Allowances under the normal rules.

Explanation

Prior to the land reforms of the 1980s many farmhouses were provided to managers and as such the companies owning them correctly claimed depreciation allowances. The practice of allowing full depreciation allowances, with no private element excluded, continued after the land reforms even though the occupiers of the properties were now self-employed people in business. This is wrong in law and arguably inequitable as no one else in business can claim the personal costs of their private house against their business income. In practice, farmhouses which are also the farmer's residence will always have a considerable amount of private use, possibly even 100%. And certain items of capital expenditure on the farmhouse may easily be totally private, such as the building of an extension as a living room for example.

This issue was discussed during the Tax Policy Framework review in 2002/2003. As this has been a long held practice, and acknowledging the need to improve the quality of much of the housing in Camp, the review group did not propose stopping this practice at that time.