

# Rural Update

## June 2017



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The IRD have recently announced this year's livestock herd scheme values and we think this is a great opportunity to update you on the latest movements. The herd scheme values are the national average market values as determined by a process involving a review of the livestock market as at 30 April.

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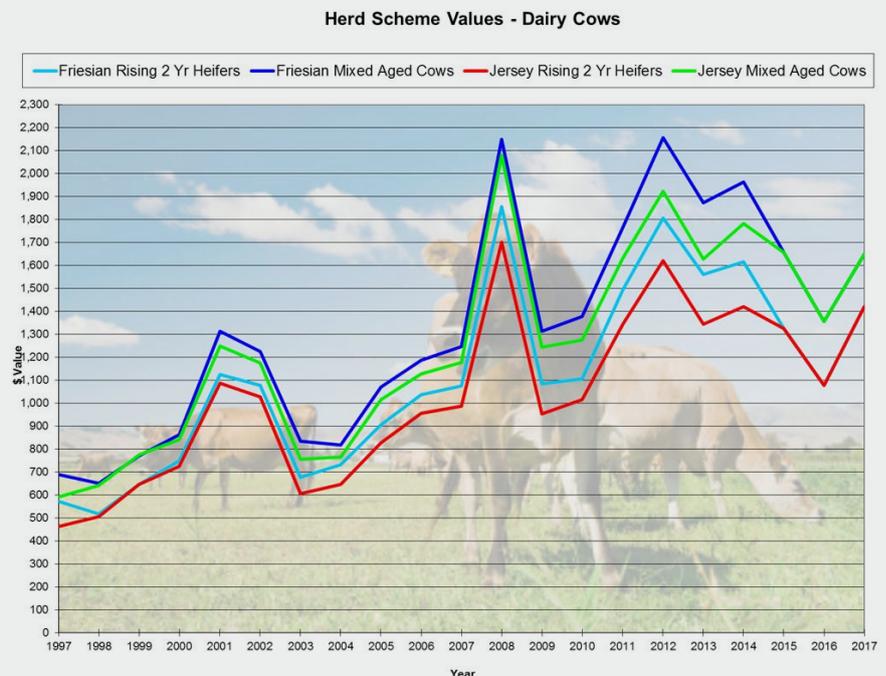
## Dairy Cattle

Late last year we saw some large increases in dairy cattle prices - however this eased back in the last few months so the resulting values for Rising two-year heifers and Mixed Age Cows were lower than what we were seeing late last year. The herd scheme value for a mixed age dairy cow has increased from the low in 2016 to \$1,649 - a definite rise (21.6%) from the \$1,356 in 2016. Rising two-year heifers are now valued at \$1,421 - up (31.9%) from \$1,077 last year.

The biggest rise is however in Rising one-year heifers - these have increased from a low of \$530 to \$819 - an increase of 54.5%. In talking to clients, this should come as no surprise as there seems to be a high demand for this age group of livestock.

Dairy bulls and steers have seen modest increases from last year with breeding bulls now valued at \$1,887.

There was an opportunity last year to move some clients from the National Standard Cost scheme to the Herd Scheme. This was because the 2016 values were at historic lows and were the closest to National Standard



Cost values than they had been for quite a long time. The rise in values in the 2017 year and the recently announced dairy pay-out increases for the 2017/2018 year mean that the decision to move was the correct one.

There may be an opportunity for clients who signed up to buy herds late last year at reasonably high prices to move into the

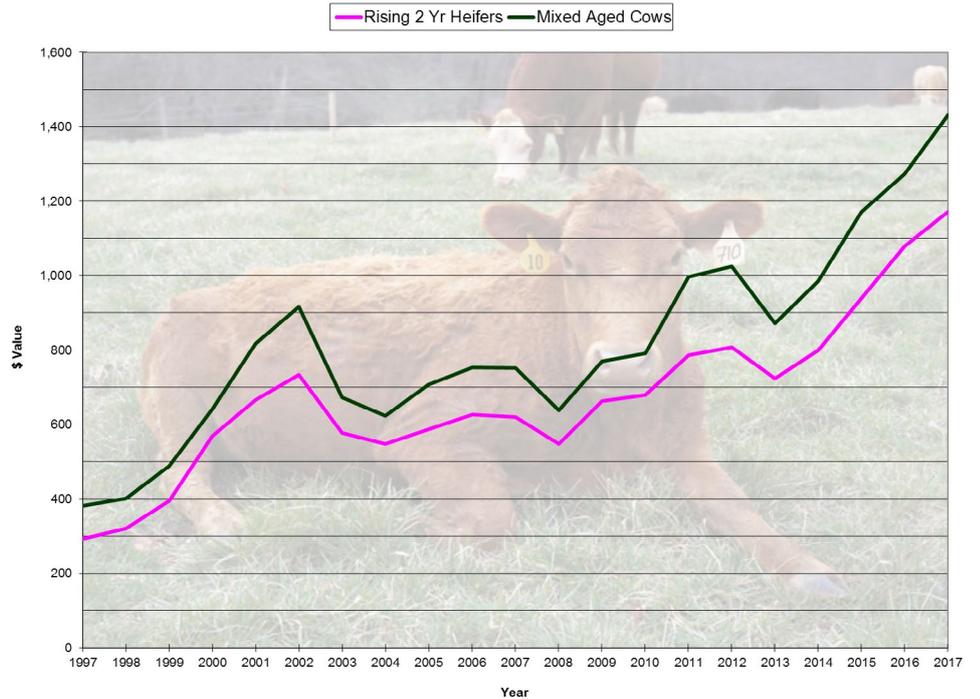
Herd scheme this year - assuming a 31 May settlement. This is something that can be considered at the time of completing your 2017 annual accounts. Each case will depend on the facts and of course we have to consider the long term implications as we will then be in the Herd scheme for the foreseeable future.

# Beef Cattle

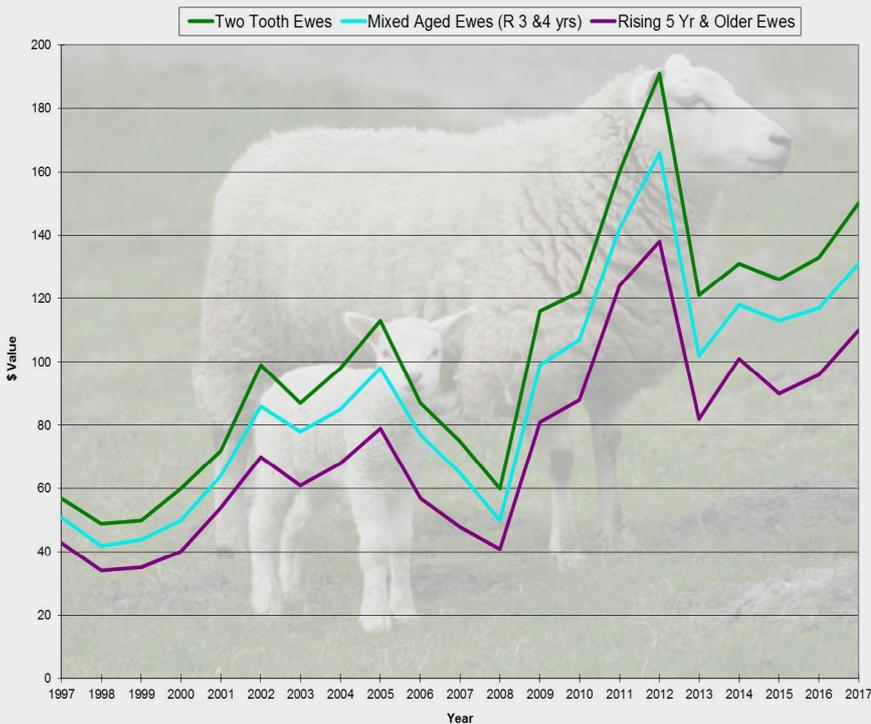
Beef values have once again increased markedly - Mixed Age Beef cows are now valued at \$1,431 - up (12.4%) from \$1,273 last year. Breeding Bulls increased to \$3,095 - up (20.4%) from \$2,571 last year. Commodity prices for beef products are at an all-time high. This has been strongly reflected in the beef market and in the prices farmers are receiving for their animals.

Beef prices have been steadily increasing since the lows of 2013 when a Mixed Age Cow was valued at \$872. The question is of course - how much longer will this upward trend continue. We have now seen four years of successive increases and as we all know this is a commodity market which inevitably has lows as well as highs. Food for thought!

Herd Scheme Values - Beef Cows



Herd Scheme Values - Ewes

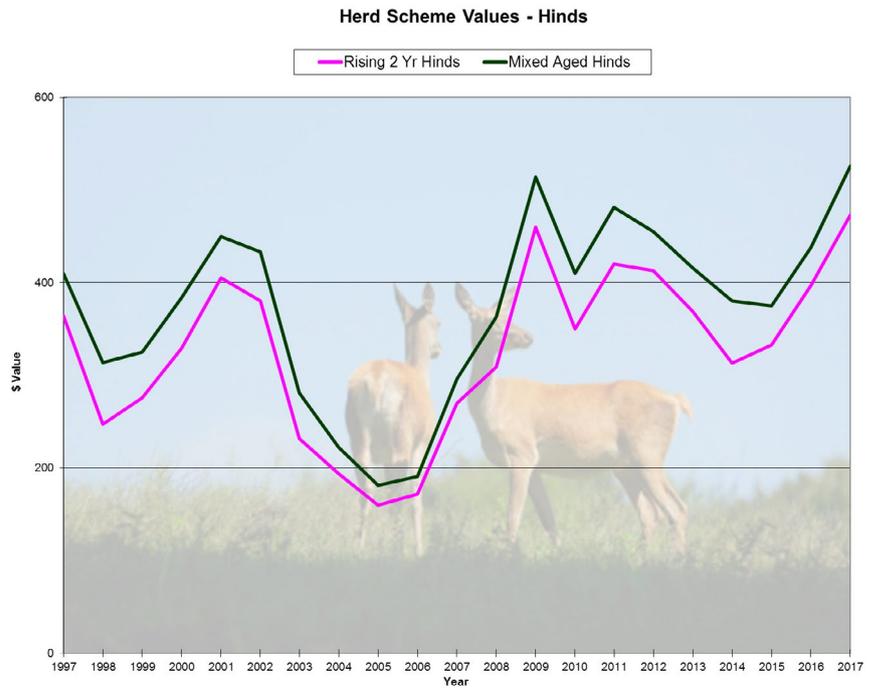


# Sheep

Sheep values have seen an overall average increase of 17.4% with two-tooth ewes now valued at \$150 - this compares to \$133 last year. Still some way to go to catch the most recent highs in 2012 when two-tooth ewes were valued at \$191!

# Deer

Deer values are continuing their upward movement with Mixed Age Hinds increasing by 20.1% from \$438 to \$526 per head. We understand that the deer market is a little erratic at times but hopefully these values are reflecting more maturity in the market and the demand for a quality product.



## General Summary

Careful consideration needs to be given to your livestock election choices. Even though changes were made to the Herd scheme in recent years, there is still flexibility around how to value increases in numbers - if you increase your numbers during the year you are able to choose an alternative valuation option to value that increase.

Whether you take that option or you elect to value the increase using herd values will depend on a number of factors - such as:

- where we are in the cycle of livestock values (e.g. at the bottom, or at the top)
- if the increase is a permanent or a temporary one

- your longer term intentions

As the decision is clearly one that should be made on a case by case basis, we will naturally discuss your valuation options with you on review of your 2017 Financial Statements and Taxation Returns.

## Fonterra Co-operative Support Loan Update

In 2015 when milk prices were low, Fonterra offered its shareholders a support loan to provide assistance through what was a tough period. Although it wasn't compulsory to take up the loan, the loan provided 50 cents for every kgMS produced from 1 June - 31 December 2015 for any share-backed Fonterra supplier as at 30 September 2015

Up until 31 May 2017, the Fonterra Co-Operative support loan was interest-free. Interest will now start being charged from 1 June 2017, and this rate will be reviewed and reset every three months. The Interest rate to be charged from 1 June - 31 August 2017 is 2.47%, and this is calculated as being Fonterra's cost of borrowings.

These interest payments will be deducted from the monthly milk cheque, and a Co-operative loan statement will be sent out each month to show the interest charges.

**It is important to remember when preparing your GST return that there is NO GST component on interest payments. For those of you who just return the net milk cheque deposit as income you will need to add back the interest deduction first so as not to under-return your income.**

The other major loan condition is that the loan principal is only repayable once the total advance payment rate (base advance rate + capacity adjustment) in a season is more than \$6 kgMS. The amount above \$6 is multiplied by the season-to-date production to determine the monthly payment amount until the loan is fully repaid. This total advance rate threshold of \$6 has now been reached and as such \$0.15 will be deducted from the final milk payment for the 2016/17 season in the October retro payment, paid on 20 October 2017.

**Again, please note there is NO GST component on the loan repayments so they will need to be added back to the net milk cheque deposited so you are correctly accounting for your income received.**

Here is an example of how this will be calculated for your GST return:

Fonterra milk cheque received in bank:	\$74,000.00
Interest charged for month:	\$19.50
Loan repayment made:	\$2,500.00
Actual milk income to return for GST:	\$76,519.50

If you have any queries please contact our office.

# Changes to Deductibility of Farmhouse Expenses

A recently released Farmhouse Expenditure Interpretation Statement from IRD considers the deductibility of expenditure relating to a farmhouse that forms part of a farming business. With farmers spending an increasing amount of time in the office, or at the kitchen table, as the case is for many farmers across New Zealand, the changes may come as a surprise.

## The position until the 2018 income year

The concession allowed a flat 25% deduction for farmhouse expenses without any evidence. It also allowed a 100% deduction for interest and rates.

## The position for the 2018 income year onward

The previous interpretation/position has been withdrawn. This change in policy will apply from the start of 2017-18 financial year.

The new policy distinguishes between two types of farmers, referred to as Type 1 and Type 2.

### Type 1 Farmers

A Type 1 farmer includes sole traders and partnerships operating a farm where the value of the farmhouse is 20% or less than the total value of the farm.

It is important to note that if farmers fail the Type 1 test based on cost, they can apply for a market valuation to ensure they pass the test. This would be relevant, for example, when a farm has been owned for a significant period of time, but a new farm house has been recently built.

Type 1 farmers are able to claim an automatic 20% deduction for farmhouse expenses (without evidence) and a 100% deduction for interest and rates.

For claims in excess of this, supporting evidence will be required.

### Type 2 Farmers

A Type 2 farmer includes farming operators where the farmhouse value is more than 20% of the value of the farm.

The IRD will not accept a minimum percentage deduction for Type 2 farmers.

These farmers may only claim deductions for interest, rates and expenses relating to the actual use of the farmhouse.

Type 2 farmers will need to undertake a "home office" type calculation based on the actual use (time and space) of the farmhouse to determine the percentage of expenses that may be claimed for business purposes.

Those who fall into the Type 2 category could find the new interpretation has a reasonable impact on their "bottom line".

## What does this mean?

It is important farmers are prepared for potential changes to their deductibility, including that they may need evidentiary proof to support higher farmhouse deductions.

The below table summarises the income tax treatment of dwelling and phone expenditure for each type of farm. If you have any questions please contact our office.

Farm Type	Interest & Rates Charges	General Dwelling Expenses	Fixed Line Phone Charges
Type 1 Farms (Large)	100% deduction for rates & interest expenses	Dissection where possible, then 20% deduction unless a larger claim can be sustained.	50% of telephone rental charges used for both business & private purposes unless a higher claim can be substantiated.
Type 2 Farms (small)	Dissection where possible, then apportion between farm & dwelling on a fair & reasonable basis. Deduct amounts attributable to actual business use of the dwelling.		Same as above.

