FARM STOCK VALUATION

This Help Sheet explains the methods of farm stock valuation that are acceptable to HM Revenue & Customs. It will help you fill in the Self-employment Pages of your Tax Return and the Trading Pages of the Partnership Tax Return.

It was originally published in 1993 as Business Economic Note 19 and is sometimes referred to as 'BEN19'.

INTRODUCTION

This Help Sheet explains the basis of farm stock valuation at the end of periods of account acceptable to us. It has been prepared to assist farmers and their professional advisers. It has been prepared after consultation between us, the Central Association of Agricultural Valuers, the Institute of Chartered Accountants in England and Wales, the Chartered Institute of Taxation, the Royal Institution of Chartered Surveyors, the Country Landowners Association and the National Farmers Union (NFU). It supersedes all previous arrangements made by us and the NFU. It does not affect rights of appeal in individual cases.

Other methods of valuation may also be acceptable to us in particular cases, provided they are recognised by the accountancy profession as giving a true and fair view of the results for the period concerned and do not violate the taxing statutes as interpreted by the Courts.

A valuation that pays insufficient attention to the facts, although in form it is made on a recognised basis, will not be acceptable.

GENERAL PRINCIPLES

The reason for valuing stock at the end of an accounting period is to identify and carry forward those costs incurred before that date but which will not give rise to income until a later period. By carrying forward those costs they can be matched with the income when it arises. Profit will be understated if stock is not brought in.

However, if there is no reasonable expectation that the proceeds from the sale of the stock in a future period will be enough to cover the costs, then relief for the expected loss may be obtained in the period for which the accounts are being prepared by valuing the stock at what it is expected to realise when sold in the normal course of trade.

For tax purposes we are looking for a figure (commonly referred to as a valuation) which represents the cost, or, if lower, the net realisable value of the stock.

In some circumstances there may be more than one acceptable method of calculating the value of stock but the basis of valuation in a particular case should be consistent. If it is decided to change the basis of valuation, tell us. Our practice on changes of basis in valuation is explained in BEN19.

Occasionally, we discover that the stock figure in the accounts is net of a provision (reserve), such as for dilapidations. If the creation of such a provision is considered appropriate, we should be made fully aware of it. Provisions are only allowable for tax purposes if profits would not be properly stated in their absence and the amount referable to the year can be quantified with reasonable accuracy. Even if these conditions are met, tax law provides that some provisions are not allowable for tax purposes (for example, for repairs to premises which are not allowable unless expended).

Valuation problems can be complex and farmers normally seek the assistance of accountants and agricultural valuers and surveyors. But this is not compulsory and some farmers prepare their own valuations.

Although livestock should be valued on an animal-by-animal basis, it is acceptable for farmers to value animals of a similar type and quality together on a global or average basis, classified according to age. If deemed cost is used (see page 3) home-bred animals should be distinguished from animals which have been bought in.

If tax is lost or delayed as a result of incorrect valuation of stock then interest and penalties may be due in addition to the tax.

LIVESTOCK, GROWING AND HARVESTED CROPS

Production cost

Production cost is the actual cost of getting the stock into its condition and location at the balance sheet date. Farm stock valuations should include the costs directly attributable to producing or rearing the stock in question. From an accountancy point of view it is preferable, but not mandatory, except in the case of certain limited companies, also to include a reasonable proportion of the costs only indirectly attributable to the production of the stock to the extent that those costs relate to the period of production. This will result in a more accurate matching of costs with related sales income. Either method, if applied consistently, is acceptable to us.

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Direct costs

Costs which are directly attributable to buying, producing and growing the livestock or crops should be included. Such costs will consist not only of the expenses of acquiring the 'raw materials', such as seeds, but also of any expenses which directly relate to producing or rearing the stock in question. There can be no definitive list, but the following are examples of direct costs:

— Livestock

- purchase costs, **or**
- insemination costs plus additional maternal feed costs in excess of maintenance, **plus**

  costs of rearing to the valuation date, or maturity if earlier, including:
  - feed costs including forage
  - vets' fees including drugs
  - drenches and other medicines
  - ringing, cutting and dehorning
  - supervisory employee or contract labour costs.

— Growing and harvested crops

- seeds
- fertilisers
- beneficial sprays ('beneficial sprays' includes preventive sprays and means any sprays which are not applied to remedy a particular infestation or crop deficiency)
- seasonal licence payments (for example, short-term hire of land to grow a particular crop) but not normal farm rents
- drying
- storage
- employee (including director) or contract labour and direct machinery costs (for example, fuel, servicing, rental, spares and the reduction in value due to wear and tear caused by actual usage for the activity concerned) incurred on:
  - cultivations
  - crop working
  - harvesting.

Indirect costs

Examples of such costs:

- depreciation and maintenance of farm buildings
- rent and rates (excluding licence payments added - see above)
- general employee (including director) or contract labour and machinery costs.

Costs to be based on expenditure incurred

Except where the deemed cost method is used, cost **must** represent the actual costs incurred by the particular farmer on producing the stock, as established from the farmer's own personal records. Larger and specialised businesses, such as intensive pig-rearing units, will usually have adequate records to calculate the cost. The current Guide to Costings, as issued by the Central Association of Agricultural Valuers, together with figures produced by other independent institutions, provide useful models to help farmers establish their own costs.

Labour costs should not include anything for the notional cost of own labour for sole proprietors or partners.

Deemed cost acceptable in some circumstances

If it is not possible to ascertain actual costs from the farmer's records, Inspectors will accept deemed cost valuations (see page 3).

Net realisable value

If there is no reasonable expectation that the net realisable value of stock will cover costs incurred, then the stock should be stated at net realisable value.

Net realisable value consists of:

- the sale proceeds that it is anticipated will be received from the eventual disposal of the stock in the condition in which, at the balance sheet date, the farmer intended subsequently to market it. It is important that the valuation should be made on a normal commercial basis. For instance, it is not acceptable to value stock on the basis that it would have been sold in a forced sale on the balance sheet date in its then, possibly immature, state

plus

- grants and subsidies intended to augment the sale prices of stocks (see page 3)
- for breeding/production animals, the ancillary stream of income from the sale of their progeny and produce

minus

- the further costs to be incurred in getting the stock into marketable condition and then marketing, selling and distributing that stock. Where the proceeds from the sale of progeny/produce are brought in, then the costs relating to their production and marketing should also be deducted.

It is not acceptable to treat cull value as the only future revenue from production animals as this does not recognise the value of the future income stream from the produce and/or progeny.

We recognise, however, that farmers may not have the extensive records necessary to calculate net realisable value with reasonable accuracy, therefore:

- for production animals, such as laying hens and breeding sows, that are not usually sold except for slaughter at the end of their productive lives, we will accept that, at the balance sheet date, a reasonable approximation of the net realisable value is the value arrived at by consistently writing off the cost, down to anticipated cull value, on a straight line or other appropriate basis over the animal's expected productive life
- for other production animals, we will accept the use of the open market value of animals of the same kind, quality and condition, based on the assumption that, at the balance sheet date, there is a willing buyer and a willing seller of the particular animal as a production animal.

Where net realisable value is used as being less than the cost, the Inspector may want to establish the basis of valuation.

CO-OPERATIVES

In the same way as any other stock held by a farmer, stock marketed through co-operatives acting as agent for the farmer must be included in the valuation unless it has been sold.

Stock held off the farm which is identifiable as belonging to the farmer must also be included.

Where stock held off the farm has been pooled and cannot be identified as belonging to a particular farmer, the unsold proportion must be included. This may be computed by taking

$A \times \frac{B}{C}$

where A is the amount in the pool that came from the farmer, B is the amount in the pool not sold at the valuation date and C is the amount in the pool not sold at the valuation date plus the amount sold from it up to that date.

Where a co-operative acts as agent for the farmer but the relevant stock can be identified as not being part of a pool, no apportionment is necessary. It should be included in the valuation.

Stock which has been sold to a co-operative that does not act as agent should not be included in the valuation.

GRANTS AND SUBSIDIES - EFFECT ON STOCK VALUATIONS

Grants and subsidies towards specific expenses should be regarded as reducing those expenses. If those expenses are included in the cost for stock valuation, then the figure used should be the net cost after deducting the related grants.

Grants and subsidies intended to augment the sale prices of stocks should be taken into account in calculating their net realisable values.

CONSUMABLES

Consumables include spares for plant and equipment, oil, diesel, sprays, fertilisers, feedstuffs and bags. For any stock of unused but usable consumables held at the balance sheet date, the valuation should normally be made at cost.

If, however, the consumables have deteriorated or become obsolete, then use their net realisable value if it is lower than cost.

DEEMED COST VALUATION

When deemed cost is acceptable

Valuations should only be based on deemed cost where it is not possible to ascertain actual costs from the farmer's records. Deemed cost should not be used for purchased animals if it is less than the original purchase price plus (if the animal was immature when purchased) the costs of rearing from the date of purchase to the valuation date or, if earlier, to maturity.

In such situations, we will accept that a reasonable estimate of 'deemed cost' is given by a specific percentage of open market value. It may be necessary, from time to time, to review the percentages if the relationship between costs and market value changes. Current percentages are set out below.

For production animals, open market value should be based on the assumption that there is a willing buyer and a willing seller of the animal as a production animal free from, for example, movement restrictions. It is not acceptable to treat cull value as the open market value of production animals because this does not recognise the value of the future income stream from produce and/or progeny.

Livestock

The percentages in the case of livestock are:

- cattle - 60% of open market value
- sheep and pigs - 75% of open market value.

Note:
Deemed cost valuations are only valid for home-bred or home-reared stock or stock acquired some time before maturity and matured on the farm. (See above for stock other than home-bred stock.)

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It is preferable for deemed cost to be fixed at maturity but we will accept valuations at deemed costs based on open market value at the balance sheet date if that method has been used consistently. Farmers should be aware that using deemed cost at each balance sheet date may result in profits coming into tax earlier.

The valuation of immature and unweaned animals using deemed cost methods based on the open market value of animals of a similar age and type is acceptable to us except in the situation described in the next paragraph. If it is appropriate to value mother and progeny together because that is the market unit, this should be done.

The method described in the previous paragraph is not appropriate where the mother is on the herd basis and where there is no market or a very limited market in unweaned progeny (for example, unweaned lambs at foot). In this situation, failure to recognise the young stock at all in the valuation is not acceptable. The costs of producing the progeny (see page 2) should be carried forward to be set against the eventual sale price.

Deadstock (harvested crops)

Deemed cost based on 75% (85% for valuations at dates before 31 March 1993) of open market value at the balance sheet date will be accepted by us.

These notes are for guidance only, and reflect the position at the time of writing. They do not affect any rights of appeal.

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