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Chartered Certified Accountants

Winter 2020

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THE INSIDE TRACK

Welcome to the Winter Edition of The Inside Track

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We have finished another tax return season and are already looking ahead, with Dan kicking everyone into gear with some worthwhile things to consider as the tax year ends and a new one begins.

Leaving the EU has preoccupied our Government to say the least and due to this, the potential Inheritance Tax changes are still only a proposal but Victoria has summarised what we could be expecting.

By the time you read this, Brexit should have happened but the effect on agriculture is still uncertain. We believe that despite the inevitable bumpy ride that is still to come, there will be opportunities for strong and adaptable businesses who plan well.

Share farming and joint ventures have become more popular recently and we expect this trend to continue when looking at the future. With this in mind, we have provided an insight into joint venture agreements.

All things considered, we are in for another interesting year.

We are of course here to help and advise you in any way we can.

JUST PAID TAX: TAKE A MOMENT TO PAUSE AND REFLECT

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Having paid tax at the end of January and now approaching the end of the 2019/20 tax year, many people will now be contemplating how they can reduce this year's tax liability. Before springing into action, however, it may be useful to pause and reflect on the long term objectives of the business and the family. Recapping where you are trying to get to can be very helpful in making confident decisions for the short term which are aligned with those longer term goals.

For example, parents may wish to step back from the business in the future to give greater freedom to the next generation. Being financially independent of the business will be key to allowing the parents to confidently make this step. A key objective may therefore be to accumulate wealth outside of the core business, whilst continuing to grow the business to pass on a successful and viable enterprise. There is therefore an important balance between how much of the profits should be invested in the business and how much outside of it.

When it comes to investing in the business, it is widely understood that spending money on qualifying plant and machinery can reduce taxable profits. The Annual Investment Allowance is currently £1million, although this is set to revert to £200,000 from 1 January 2021, so the timing of capital expenditure in accounting periods straddling that date should be carefully considered.

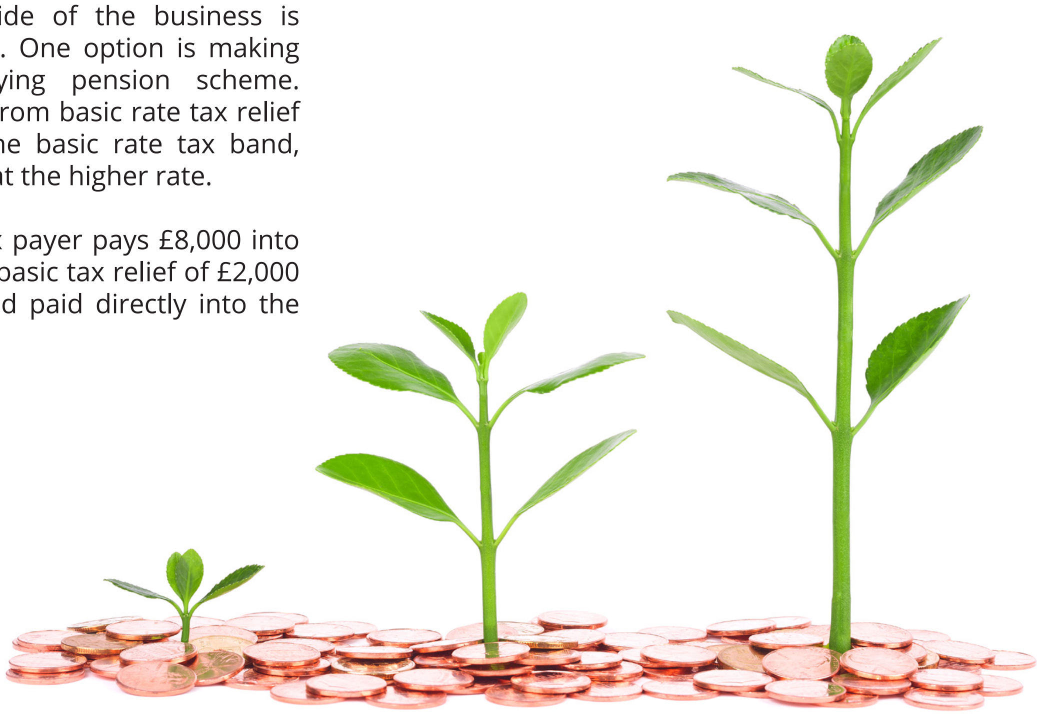
Investing tax efficiently outside of the business is perhaps less well understood. One option is making contributions into a qualifying pension scheme. Contributions usually benefit from basic rate tax relief at source and also extend the basic rate tax band, meaning less income is taxed at the higher rate.

For example, a higher rate tax payer pays £8,000 into a personal pension plan, with basic tax relief of £2,000 being claimed from HMRC and paid directly into the pension fund. The gross contribution of £10,000 extends the basic rate tax band, resulting in a £2,000 higher rate tax saving. Overall it has cost £6,000 to invest £10,000 in the pension fund.

In recent years the rules surrounding how benefits can be drawn from pension funds have altered, making them a more flexible and attractive investment vehicle. With sound advice from a financial advisor they can be used as an important part of wealth management and succession planning, as well as saving Income Tax in periods of strong profitability.

All investments, whether on or off-farm, of course consume cash. With the difficult planting season that has been experienced over recent months, consideration should be given to how this will impact upon business cash flows for the year (or two...) ahead. Be it reduced grain receipts next winter or higher feed prices, cash flow could be restricted. Whether tying up cash in machinery purchases or pensions, cash flow forecasts should be reviewed before making any significant commitments.

In summary, it is usually advantageous to think through the long term implications of any Income Tax planning that is undertaken, to ensure that it compliments, rather than detracts from, longer term objectives. If you would like to discuss the above, or any other pre-yearend tax planning points, please do not hesitate to contact us.



SIMPLIFYING INHERITANCE TAX (IHT)

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The Office of Tax Simplification (OTS) has recently reviewed several key aspects of IHT and put forward recommendations to HMRC. If adopted, these recommendations could have significant implications for farmers and landowners.

The OTS's report acknowledges that "there are many areas where IHT is either poorly understood, counter-intuitive, requires substantial record keeping, creates distortions, or where the application of the law is simply unclear". The key recommendations in resolving these issues which could affect famers and landowners include:

1. **Where assets pass on death and the assets benefit from IHT relief or exemption, the recipient should be treated as acquiring the assets at the historic base cost of the deceased.**

Currently it is possible that a farm, acquired many years ago at a fraction of the current value, could be inherited on death with no IHT being payable. The beneficiary could then sell the farm without incurring Capital Gains Tax (CGT), having acquired the farm at probate value.

If the farm were to be gifted during lifetime, rather than on death, it is likely that CGT could be deferred by a claim for Hold Over Relief. As a result, the beneficiary would acquire the farm at the historic low base cost. If the beneficiary were to then sell the farm, it is likely that they would suffer a substantial CGT liability.

Holding the farm until death can therefore provide a 'CGT uplift' and this often means that some farmers retain ownership of the farm and continue as partners until their death, purely for tax purposes. The OTS suggest that this is distorting decision making and business succession. They therefore recommend that the legislation is altered so that the tax implications of gifting assets such as a farm, are the same whether the gift is during lifetime or on death.

Whilst such a change may simplify decision making when considering the appropriate time to pass assets on to the next generation, it has the potential to significantly increase CGT liabilities on farm sales or reorganisations of asset ownership within the family.

2. **The level of trading activity of a business required for it to benefit from Business Property Relief (BPR) from IHT, should be increased to align it with the level of trading activity required for CGT purposes.**

Currently BPR can apply where a business is 'mainly trading'. Providing the investment activities constitute less than 50% of the overall business, BPR can apply to relieve the full value of the business from IHT. This can, for example, allow let cottages to benefit from IHT relief where they are held within a mainly farming business.

When considering the availability of CGT reliefs, however, HMRC consider that the investment activities cannot constitute more than 20% of the overall business. The OTS recommends that these thresholds are aligned for IHT and CGT. Whilst this would simplify matters, it could significantly worsen the IHT exposure for many farmers with rental properties and other non-trading assets that constitute more than 20% of their business.

3. **Treat Furnished Holiday Lets (FHLs) as a trading activity for IHT purposes.**

FHLs are currently treated as a trading activity for Income Tax and CGT purposes, but are generally considered to be an investment activity for IHT purposes and therefore do not generally benefit from BPR (unless they are held within an overall trading business). The OTS has suggested that the tax treatment is aligned such that FHLs are also treated as a trading activity for IHT purposes and therefore benefit from BPR. With many farmers having diversified into FHLs, this could be a very beneficial change if implemented and could reduce the impact of the potential increase in the level of trading activity required for BPR purposes set out above.

4. **To reduce the '7 year clock' to 5 years so that gifts to individuals made more than 5 years before death are exempt from IHT.** This would be a welcome change and could facilitate making further use of lifetime gifts, with individuals being able to make substantial gifts every 5 years to mitigate IHT.

These are just the OTS's suggestions at this stage. The Budget on 11 March 2020 may provide indications as to whether the government have chosen to implement any of the recommendations. With IHT reform on the horizon, with some positive changes but coupled with some punitive changes, it remains sensible to periodically review the overall tax position of the business and the family.

UPDATES

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SMALL BUSINESS RATES RELIEF

In recent months we have seen an increase in inspections from the Valuation Office Agency, looking into non-domestic business rates payable on equine facilities and renewable energy facilities. This can include farms with non-agricultural areas such as stabling, unless they are in close proximity to the house forming part of the domestic curtilage.

Don't forget that the small business rates relief is available to businesses with a rateable value of less than £12,000. You have to claim the exemption by logging in through your local council's website.

If you have a larger renewable energy facility and use some of the power yourself you may need to set up a special purpose vehicle so that the energy is produced by one entity and sold to another.

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PAYROLL YEAR END 2019/2020

The tax year end will soon be upon us and you will need to prepare for your payroll year end. Once you have submitted your final full payment submission (FPS) and employer payment summary (EPS) for the year, the deadline for which is the 5 April 2020, you will need to ensure that you are using the most up to date version of your software. You should then run your 'payroll year end' on your payroll software, this will trigger the population of P60's for each of your employees employed at the year end. You must ensure that each employee is sent a copy of their individual P60 prior to the 31 May 2020. Before proceeding with the first payroll run of the new tax year you must also ensure that you have updated all your employees tax codes for the new tax bands.

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SCAMS

The Year 2020

Usually when we write the date, most of us will chop off the first two digits and leave the last two to signify the year, e.g. 2019, is shortened to '19.

However, this year it is important that you write the year 2020 in full or you could be putting your documents at risk. Leaving the date in its shortened version could open yourself up to fraudsters, who could easily change it to many other years.

The general warning is to be cautious when writing the date on any documents, as well as accepting documents without the full date – it is better to be safe than sorry.

HMRC Scams

Just a little reminder that HMRC will never email, text or call you regarding a tax rebate or penalty, nor will they contact you this way asking for personal details. If you are unsure on any correspondence you receive from HMRC then please do not hesitate to ask us about it.

USEFUL DATES

31 January 2020 - Tax return filing deadline, deadline for paying tax bill for the year ending 5 April 2019 & 1st payment on account due for 2019/2020

11 March 2020 - Budget

5 April 2020 - End of 2019/2020 tax year

6 July 2020 - P11D Submission deadline

31 July 2020 - 2nd payment on account due for 2019/2020, tax credit renewal deadline

CONSIDERING A JOINT VENTURE

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Joint ventures are being considered more widely and can enable succession, improve efficiency or aid entry into farming.

New Zealand leads the way with their share farming opportunities. The attitude in the UK differs somewhat to that in New Zealand as farms here are held for many generations often being very effective planning tools for both Capital Gains Tax and Inheritance Tax reliefs. A joint venture may be a way for the landowner to retain reliefs yet do less work on a day to day basis and for a non-landowner to use their technical skills and others assets to their mutual benefit.

Joint ventures can be used to meet personal and business objectives and, if used well, playing to the strengths of all those involved can be a recipe for success. However, this is not a given and if they are not fair, meeting everyone's goals, however well worded the agreement may be, they are not likely to work.

The term joint venture means a business arrangement in which two or more parties agree to pool their resources for the purpose of accomplishing a specific task.

Both share farming and contract farming are joint ventures but it can also mean sharing equipment or land.

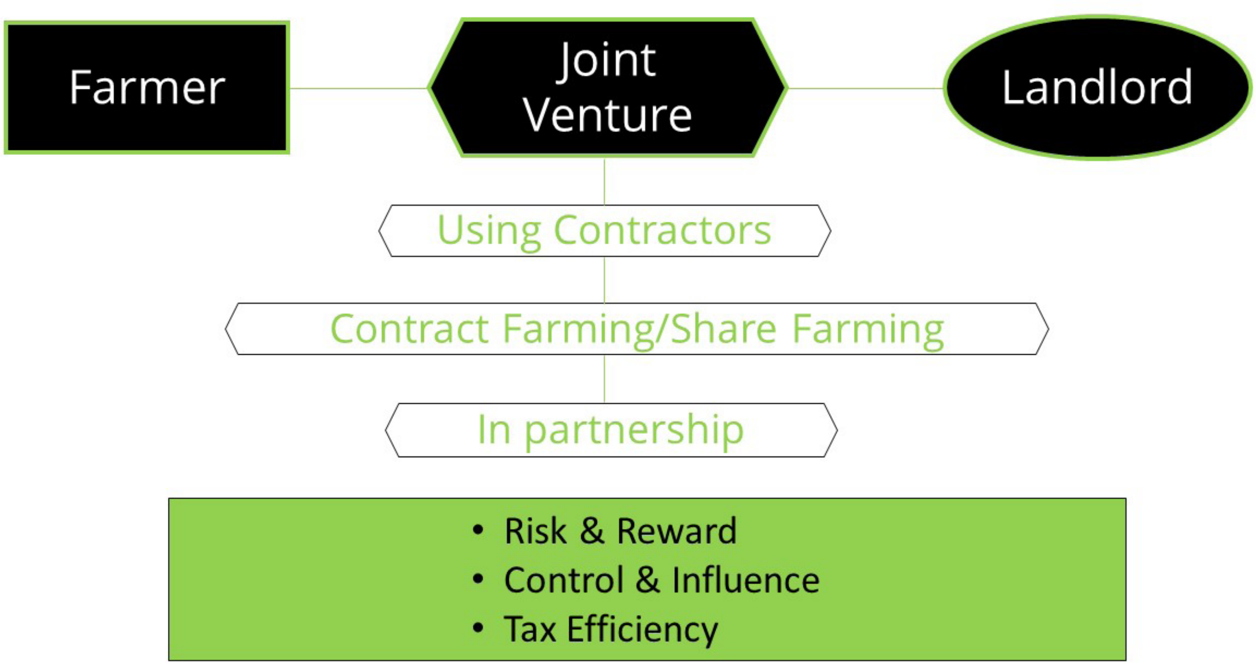
The key to all joint ventures is to collectively consider everyone's objectives and attitudes in respect of:

- Risk and rewards – seeking either a secure income or seeking a higher return, accepting increased risk
- Control and influence – retaining all control or relinquishing some control
- Administrative burden – reducing/sharing the red tape burden
- Decision making – operational vs strategic – dealing with the day to day team on the ground differs to taking a higher level approach to the long term aims of the business

Together with considering everyone's motivation, joint ventures are based on what each party is offering:

- Skills
- Labour & time
- Machinery
- Finance
- Land or access to tenanted land

A joint venture can take a number of forms:



On one hand, a farmer has complete control over the land, taking all of the risks, whilst receiving all of the rewards. Although it can be time consuming, with potentially large capital requirements, from a tax perspective a farmer has an agricultural trading status and should be eligible for all of the associated tax benefits and reliefs.

On the other hand, a landlord has little control over the land but their financial risk is minimised, assuming they have good tenants, receiving a safe, fixed return. Some of the landlord's time may have been released, but both the Income Tax and capital tax positions are less efficient. The right tenant with the skills and capital is required and a house may need to be provided for them.

A joint venture agreement sits somewhere in the middle, somewhere between having full control over the farm as the farmer, or little control over the farm as the landlord. There is no set formula and each agreement will be unique to the individuals involved. A joint venture can be as little as an agreement for a fixed fee with a contractor to undertake specific tasks, to a full equal partnership between all those involved. The key is that it has to work for both parties in order for it to be sustainable and most importantly there needs to be trust.

Joint ventures can:

- Enable landowners to continue farming whilst stepping back from the day to day work
- Create economies of scale - e.g. use of a contract farming agreement whereby a forager is utilised over the area it is capable of rather than just the acreage of one farm.
- Break down barriers for new entrants - whether that be capital requirement or the opportunity of economies of scale in order to make a business finically sound.
- Facilitate succession by granting the next generation control, but in a well-managed environment

It is also important to ensure that both parties are still in a position to achieve longer term goals and recognise those goals so that they can be met, for example, if the long term plan is to sell the farm rather than to pass it on to the next generation, the structure may differ.

The key is to ensure everything is considered, ranging from where each party's real passion lies, to what they want long term and the tax implications of the plan. Changing the potential trading status may impact the shorter term Income Tax and VAT position as well as impacting the longer term capital tax reliefs. Many forget that Income Tax could be up to 45% of taxable profits but Inheritance Tax can be 40% of net worth.

The future is bright but challenging and we would encourage everyone to consider the opportunities available and collaborative farming may be one of these.

GRAZING AGREEMENTS - THE CHARNLEY CASE

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Tax legislation is designed to support the economy and encourage, or discourage, certain behaviours. Generally speaking, reliefs are available for activities that help the economy whilst anti avoidance legislation discourages activities that could damage the economy.

Valuable Capital Gains Tax and Inheritance Tax reliefs are therefore available for trading businesses, and the assets used therein, which typically contribute to the economy. They are often restricted for investment activities, such as letting property.

A landowner with grazing agreements falls between a farmer carrying out his own farming trade and a landlord letting land to a farmer for use in their trade. It is therefore unclear whether certain tax reliefs should apply.

The recent Charnley case considered the availability of Agricultural Property Relief (APR) and Business Property Relief (BPR) from Inheritance Tax in respect of a farm subject to grazing agreements. The tribunal concluded that, in this case, the deceased's activities "were those of a farmer, working an active farm" rather than the activities of a landlord. APR was therefore allowed on the modest farmhouse and BPR, as well as APR, was allowed on the land and buildings on the basis that the business was of a mainly trading nature.

It would be dangerous to interpret this decision as grazing arrangements will allow entitlement to tax reliefs in all situations. It is extremely important to consider the facts and circumstances of each case as these will determine whether the reliefs should apply.

In the Charnley case the deceased, Mr Gill, had historically operated a larger scale commercial mixed farm. As he got older and found the administrative burden of livestock passports, for example, too cumbersome he ceased farming his own livestock and entered into grazing agreements with local farmers.

Despite the actual agreements suggesting that Mr Gill was more akin to a landlord, the tribunal considered what actually happened in practice. The primary grazier, Mr Blacklidge, gave evidence explaining the activities that Mr Gill carried out. These included fixing fences and hedges, digging out and clearing ditches, harrowing, rolling, topping, reseeding, checking stock daily and moving stock. Mr Blacklidge described Mr Gill as "farming his land using my stock", he was "the boots on the ground" and the "director of operations".

Mr Gill's activities were considered to amount to more than those of a landlord and relief was allowed. The outcome of this case is hugely positive for the farming community, particularly those looking to scale back farming in their later years, but what actually happens on the farm day-to-day is of paramount importance to maintain access to the reliefs available.

EVOLUTION NEWS

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Since our last newsletter, we have welcomed Mary Sparks to our team, Mary joins us as a Business Administrator and works 9.00am – 3.00pm Tuesday to Friday. We are also pleased to welcome manager Ellie Hammett back from maternity leave. Ellie will be in the office from Monday to Thursday.

Also, a huge congratulations to Dawn Radford who passed her ACCA finals in October 2019 – a fantastic achievement!

If you have any queries regarding any of our articles, or would like any further information, please do not hesitate to get in touch.

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