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Practical VAT Newsletter

# All change on the farm – VAT protection

**Now is the time to review all farm diversification activities as part of important VAT planning.**

There is one certainty with regard to the current 'alternative land use' and VAT, and that is beyond any question of doubt that the associated VAT compliance is complicated!

There are so many various ingredients to ensure complexity – to start the exotic mix of the supply of land and the supply service together with ongoing changes and ideas to support commerciality. This strong cocktail is mixed with a flurry of tribunal cases attempting to supply clarity.

## Metal storage containers

Many farmers have diversified into the activity of affixing metal storage containers to their land and letting out the space. There is a debate as to whether this is a trading activity or an investment activity for income tax and corporation tax purposes. A recent VAT tribunal has questioned the VAT treatment of such storage. For farmers the exempt supply treatment of this income means that there are partial exemption problems BUT where these storage containers are for private customers the VAT exemption can have advantages in marketing and profitability terms.

The renting of storage space within a warehouse complex is often treated as an exempt right over land rather than a taxable supply for VAT purposes. HMRC took a case against VAT exemption applying where the storage was provided in large metal containers. In the case of *David Finnamore trading as DA Hanbridge Storage Services* (TC 01081) the business model employed by this company was to place large metal containers on bare land, and then hire these out to the general public wanting to use them for storage.

HMRC's argument was largely based on the distinction between a metal container that is capable of being winched into a different location or being used to transport contents, and infrastructure that is affixed to the land. HMRC focused on the VAT Directive's reference to an exemption applying to 'the leasing or letting of immovable property'. The metal containers were 'movable'. Specific hirers were allocated specific containers, and hirers had general access to those containers as in a warehouse building. The only difference with the warehouse building concept is that the metal container is not, necessarily, a building.

The tribunal acknowledged that metal containers are more portable than buildings but suggested that this was an irrelevant distinction, since the VAT Directive was distinguishing between items that were readily portable (such as a chair) from items that were not. In the context of this case, the metal containers were not movable items; they were, by virtue of their own weight, affixed to land.

The container could not be readily moved, and the lease agreement did

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not allow them to be moved. On the basis of 'fiscal neutrality' the tribunal decided that it would be wrong to draw a distinction between a building infrastructure and such metal containers, and therefore the supply was decided to be exempt as a right over land.

As the supply is exempt for VAT purposes it is very easy for HMRC to argue that this is an investment activity for Inheritance Tax (IHT) purposes which many would consider a disadvantage. However, where the metal containers are part of a mixed farming estate with considerable trading activity the case of *Balfour (RCC v Brander (as Executor of the Will of the Late Fourth Earl of Balfour)* [2010] UK UT300 (TCC) indicated that Business Property Relief (BPR) could be achieved on the whole business enterprise so this would not necessarily be such a disadvantage.

## Bed and breakfast

Another recent VAT case involved bed and breakfast (B & B) carried on from a farmhouse by Mrs Forster. The farmhouse at Parsonage Farm was part of a farming partnership of which Mrs Forster was a partner. HMRC tried to argue artificial separation between the B & B and the farming business. However, the B & B had been trading since 1970, had separate books and records and none of the other partners were involved. The tribunal found in favour of the appellants and deemed the B & B trade to be separate from the farm *(AD and J Forster* TC 01319*)*.

All farmers should review all their diversified activities as the supply of land compared the supply of service or movable object together with the status of most diversified activities currently seems important to HMRC. Indeed, while there is so much concern in income tax and inheritance tax terms regarding the difference between investment and trading activity, so should there be concerning the supply of storage for VAT purposes.

It is certainly important for the farmer/landowner to review the VAT position and to consider business definition, commerciality and partial exemption status and calculation.

## Horse livery charges

There has been huge confusion as to the VAT treatment of livery services. A lot of the confusion arises because there is a mixed supply, ie partly the supply of feed via grazing (zero) and the supply of stabling (exempt land) and the supply of care and services (standard rated). This can be seen in the example in Box 1.

Services provided for horses are those that go beyond the right to occupy the stable.

The problem is the definition of service, so the question is asked:

## What are services and 'care'?

- feeding or turning the animal out to graze;
- mucking out, spreading straw or other bedding;
- worming and clipping;
- grooming and plaiting; or
- taking on any responsibility for the welfare of the animal, including arranging for veterinary services.

## Box 1

| Supply | VAT Treatment (and direction) |
|---|---|
| Grazing | Zero (V FOOD 3120) |
| Grazing with care/services (keep of animals) | Standard (V FOOD 3140) |
| Exclusive use of stabling (no option to tax) | Exempt (Notice 701/15) |
| Exclusive use of stabling (option to tax) | Standard (Notice 701/15) |
| DIY livery – grass (no services provided) | Zero (V FOOD 3120) |
| DIY livery – stable (no services provided) | Exempt (V FOOD 3120) |
| DIY livery – grass and stable (no services provided) | Apportion between exempt and zero (V FOOD 3120) |
| Part/Full livery with services | Standard (Notice 701/15) |
| Training, schooling and breaking | Standard (Notice 701/15) |
| Part/Full livery where there is exclusive use of stable (right over land) | Apportion between supply of stable exempt & the services standard |
| Grass keep when visiting a stallion | Standard (Scott) |

## The problems created by the *John Window* tribunal

The problems arose from the John Window Tribunal (LON/00/011) and Business Brief 21/01 published in December 2001 that followed it.

John Window owned stables. He received rent from owners of horses which were kept at the stables but did not account for VAT on the rent, treating it as exempt. Customs and Excise issued an assessment on the basis that, because the trader also supplied additional services such as feeding and watering, the charge was for the keep of animals and was standard-rated. The tribunal allowed the appeal, holding that the trader was making a single exempt supply, and that, by application of the Card Protection Plan principles, any additional services were ancillary to it.

The problem seems to be with the application of the Card Protection Plan principles and the fact that the care was ancillary. The *Window* case only applies if the horse owner is given exclusive use of the stables. So much depends on the contract for livery and it is essential for all livery providers to have a contract for their horse owners.

## Grass livery

The distinction between grass livery and 'keep' is set out in two cases – *Holt Manor Farm* and *Suzanne's Riding School*.

The case of *R W and J R Fidler trading as Holt Manor Farm* (LON/94/0798A) concerned the distinction between grass livery and keep. The appellants provided grass livery on a seen twice daily basis but, if they judged anything to be wrong with the animals seen, would arrange for a vet to visit on their own initiative. They also arranged for regular worming and shoeing, and charged the owners for these services (plus VAT). The tribunal found that, where these extra services

were provided, they did not constitute part of the supply by the appellants, who were acting rather as agents for the owners in this respect. It was not considered to be a supply of care.

A similar line was taken in the case of *Suzanne and Julian Marczak trading as Suzanne's Riding School* (LON/94/1682A), where similar occasional extra veterinary and farriery services were arranged for by the appellants in respect of horses for which they provided basic grass livery. However, in this case it was understood that such services were to be provided only in an emergency, not as a recognised part of the contract for livery. The tribunal found that, in the absence of any contractual obligation on the appellant's part to provide such services, they were correctly treated as separate from the basic supply of grass livery. The position on ancillary grass keep for horses follows the position on general animal grazing.

A supply of grazing rights is zero rated as animal feeding stuffs. If, however, care of animals is provided for in the relevant agreement other than merely incidental care, the entire supply is treated as liable to VAT at the standard rate. All other forms of 'keep' of customers' animals which are provided on a headage basis, including livery and agistment, are similarly regarded as liable. To avoid charge, separate agreements for grazing and service should be arranged.

In *Customs and Excise Comrs v Scott* (1978) STC 191 it was held that the supply of grazing was only part of a general supply of keeping mares at stud. It therefore followed that the supply should be standard rated as being a supply of animal care. On the other hand, in *Fidler (RW & JR) v Customs and Excise Comrs* (1995) VAT Decision 12892 the taxpayer provided a full livery service for owners, including monthly treatment, blacksmiths and veterinary services. It was held that the overall supply should not be treated as standard rated, but that the standard-rated services arranged as agent for the owners could be separated from the supply of grazing. The agency arrangements, an implied term of the contract, were thus an important element in separating out the standard-rated from zero-rated categories of services.

*Derrick Dennis Scott* (CAR/75/0206) operated a stud farm. Mares brought for covering by his stallion remained on his premises, normally at grass, until the service was effectual. For this, Mr Scott charged a one-off service fee plus a further weekly charge while the mare was on his premises. The service fee was standard rated, but he zero-rated the weekly keep charge as being for a supply of animal feed.

The tribunal, ruling that the total consideration (including the keep fee) was in respect of all the appellant's obligations under the contract, nevertheless allowed these various obligations to be treated in effect as separate supplies (including one of animal feed), and output tax apportioned between them. However, on appeal, the High Court held the transaction relating to each mare to be in substance and reality a single supply of the keep of animals and standard rated.

## Racehorse Owners Registration Scheme

Those who own racehorses and are registered under the Racehorse Owners Registration Scheme will have the ability to reclaim the input VAT provided the sponsorship criteria are met.

There are many racehorse owners who move on to the purchase of a stud farm. Care must be taken to notify the change to HMRC and ensure the correct treatment.

## Grazing rights

There has been much written about the VAT position on grazing rights, especially where it involves horses. Likewise, there has been a huge amount written about the IHT relief on grazing agreements following the *McCall* case. One of the points arising from *McCall* is that there must be clear service in order to achieve Business Property Relief (BPR). Ironically, William Massey QC tried to argue that the service provided with the grazing was similar to a 'hotel for cattle' and indeed similar to a boarding kennel.

In the case of Leander International, trading as Arden Grange (LON/02/0575), the appellant maintained that a supply by a kennels/cattery should be exempt. There argument applied the Card Protection Plan principle, whereby any additional services were ancillary to the main supply in this case land. Also the precedent set by the *John Window* case (LON/00/0011) whereby the supply of land was the principal element of the supply and should determine the liability of that supply. HMRC argued that the supply was one of care, of which the supply of land was a minor element in the wider package of care provided by the kennel/cattery. The tribunal decided in favour of HMRC.

The principle is explained in VFOOD3140 'Animal feeding stuffs: keep of animals'. The simple grant a grazing right is zero rated. However, the supply of the keep of animals is standard rated, this might include an element of care. For example if it is the landowner's actual responsibility to call in a vet for a sick or injured animal without reference to its owner to save time then this is care.

Similar to other cases, it is essential to ensure that a written agreement is in place which defines the position and degree of service. It will also be important to ensure that the facts tie up to the agreements and that there is evidence of these facts. If the grazing agreement is a zero rated supply, guidance is given in VFOOD3120 (Animal feeding stuffs: Grazing rights).

Grant of grazing rights (the right to allow someone else's animals to graze on your land – also known as grass keep lettings) is both the granting of a licence to occupy land and a supply of animal feeding stuffs (ie grass). In the grazing rights situation, the supply of animal feed takes precedence over the supply of a licence to occupy, and the supply is zero rated. It is possible to identify a grant of grazing rights by examining the contract, which will clearly limit the grantee's rights over the land to grazing only.

If the grazing agreement includes an element of shepherding or oversight and this extends to more than once or twice a day then the supply may

be the keep of animals as opposed to grazing (VFOOD3140). If the grazing arrangement is subject to zero-rated VAT it is difficult to see how a claim for BPR after IHT can be justified?

After the *McCall* case there was much written about the need to ensure a grazing agreement with full and robust service was in place and adhered to.

There were also strong suggestions that in order to achieve BPR on grazing agreements, the farming arrangement has to move to being 'in hand'. The clear advice is to make sure that there is clarity – there must be at the very least a marriage between VAT and tax – if BPR will be sought on the land then this will no doubt fail with a zero-rated arrangement.

## VAT registration – registration limit

As part of a campaign aimed at taxpayers who should be registered for VAT but are not, HMRC have sent out letters. For those who should have been registered there was a voluntary disclosure opportunity by 30 September.

The VAT registration limit is currently £73,000.

If some of the livery supplies are exempt this increases the registration limit for the livery yard as the taxable element is below the registration limit and the other part is exempt 'outside the scope' of VAT.

This again highlights the importance of the analysis of DIY grazing with no care (zero), DIY grazing with care (standard) and the DIY livery with stable and no grass or services provided. The latter could be a competitor who effectively 'rents identified stables' and the facilities. However, if the facilities include, for example, some small 'turn out' facility and, say, some use of the indoor school, this could change the exempt supply status.

## Practical Planning Points

All diversified activities must be reviewed for VAT compliance and planning – consideration must be given to the need to register and the possible attack by HMRC on artificial business splitting. All supplies must be reviewed to ensure the correct identification – zero, exempt, standard, and the impact on partial exemption and IHT planning.

All grazing and livery agreements should be reviewed to ensure that the arrangement is correct for what needs to be achieved with both VAT and other tax concerns. It is essential that the agreements and the facts meet the criteria in both compliance and planning terms. If potential development land or simply high value land seeks shelter from IHT reliefs then the risks of not protecting are high as is the reward for ensuring protection is achieved. **TPV**

**Julie Butler FCA**

*Julie Butler FCA, Butler & Co,*
*Tel: 01962 735544*
*Email: j.butler@butler-co.co.uk*
*Website: www.butler-co.co.uk*
*Julie Butler FCA is the author of* Tax Planning for Farm and Land Diversification *(Bloomsbury Professional),* Equine Tax Planning, *and the forthcoming* Stanley: Taxation of Farmers and Landowners *(LexisNexis)*