VAT TEAMS ARE SET TO KNOCK ON DOORS

* Be ready for the taxmen – they're coming, warns specialist **Julie Butler** of Butler & Co.

Are you prepared for the VAT hit team? Ten years ago, the preparation of the farm VAT return was a relatively easy affair. Generally, all income was agricultural and therefore zero rated and most of the VAT on expenses could be reclaimed.

Nowadays, more cottages are available for rent, barns have converted to residential and commercial accomodation and there is also a vast amount of alternative land use.

Where buildings have been converted for commercial use, there have been various "options to tax", so all the VAT paid in converting the building can be reclaimed. The result is an extremely complex VAT Return for many farmers.

Income from residential lettings is exempt from VAT. But generally, this means "partial exemption", which involves some interesting new terminology – "deminimus limits", "annual adjustments", "the standard method" and the "use-based method". If this vocabulary is alien to you, then worry.

HM Revenue and Customs has recently announced they intend to scrutinise VAT-free commercial shoots, and its Norwich-based Shooting Project team claims "an average extra tax take of £19,000 a visit".

But I believe there are more worries for the farming community through the VAT treatment of cottages and the alternative use of buildings than their involvement in shooting. Have you checked the VAT treatment of new ventures? HMRC has already said it would like to see the shooting project extended to cover farms' diversified enterprises.

Farming was historically deemed a low risk to the VAT inspectorate and in many cases it is 10 years or more since most farms had a VAT inspection. Is there a nightmare round the corner? And what can farmers do about it?

It would be a cost effective and sensible safeguard for farmers to have a VAT audit carried out by their accountant or adviser.

The review of VAT returns is often not included in the accountant's engagement letter and if the right VAT questions have not been asked, the answer may not have been given.

Historically, VAT has attracted a level of complacency. But the signals from HMRC are becoming clearer and clearer. So, make a New Year's resolution: Ask your tax adviser to visit before the VAT inspector does!

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* This year has seen changes, concessions and outright U-turns to the taxation regime for trusts.

Several changes were expected. But there was genuine surprise when changes to the inheritance tax treatment of trusts, which were not discussed during the consultation process, were included in the 2006 Budget.

The new rules have brought almost all trusts into the discretionary trust tax regime. This means that Accumulation & Maintenance trusts, commonly used to ensure that children are looked after financially, but are unable to control their inheritance until reaching a certain age of maturity, may be treated like all other trusts for tax purposes. The new rules mean that there is now a difficult choice facing trustees: They must either pay a tax charge or distribute assets to beneficiaries at 18 to avoid falling into the new discretionary trust regime.

The obvious risk here is of granting young people huge responsibilities – ownership of valuable property, for example – at an age when they may not be able to manage these assets responsibly.

There is now a 20% cost of transferring assets into almost all trusts during an individual's lifetime. In addition, almost all trusts will be subject to 10-yearly periodic charges at a maximum value of 6%, as well as "exit" charges when property leaves the trust.

However, a number of legitimate tax-planning opportunities still exist, provided planning takes place at an early stage. Farmers, landowners and other rural business owners should also review their wills, as many contain trust provisions, often for surviving spouses, which

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will be affected by the Finance Act 2006.

Accumulation & Maintenance Settlements can avoid the new IHT charges regime by appointing assets to beneficiaries before 5 April 2008. It is therefore important to seek advice well before this date as there is no hard and fast rule – each situation needs to be judged on its own merits.

In appropriate circumstances, for new trusts, families can still avoid almost 20 years of charges by distributing trust assets to beneficiaries at the age of 18. On the other hand, it may be felt that it is worth taking the tax hit as trusts allow families to protect assets, and a tax cost of 0.6% per annum may be a small price to pay for the security and peace of mind they provide. And many trust assets will hold farmland which will be subject to generous IHT reliefs such as Agricultural Property Relief and Business Property Relief.

Farmers and landowners should still consider the use of trusts to hold assets, particularly as agricultural land and assets can qualify for APR and will therefore not attract an inheritance tax charge. Trusts remain a useful method of passing an asset, intact, to an heir and providing the family with the benefit of asset protection.