Amenity value, grazing agreements and conacre

All tax advisers are prepared for the concept of 'hope value' and the need to put tax protection in place. Hope value is the difference between Agricultural Value (AV) as defined by s115(3) Inheritance Tax (IHT) Act 1984 and market value for the purposes of probate or lifetime transfer (s160 IHT 1984). Essentially 'hope value' is the value of potential development opportunity.

Hope value

Professional advisers should be prepared to object to HMRC's attempts to include 'hope value' on farmland with full 100% Business Property Relief (BPR). In order to qualify for 100% relief the land must be partnership property. If the land is held outside the partnership, the rate of BPR is only 50%. The land must also be used in a trade and it must not be let through a tenancy, a licence or a very vulnerable grazing agreement which does not amount to trading activity. Post the Brexit vote the farming industry will have to restructure and reassess its markets, production methods and of course reliance on subsidies. Such considerations will be a great opportunity to ensure that updated legal agreements, licences and grazing arrangements are in place.

Valuations are on the basis that hope value is potential development value and the land is going to be developed and sold in the relatively near future. Therefore the probate value at market value will in fact be the base cost for CGT for the beneficiaries of the estate on death and, provided 100% BPR is achieved, the executors will generally be content and prepared to embrace a high hope value figure as this is the base cost on which the CGT computation will be prepared when they sell the land. Whilst many valuers fight the concept of 'hope value' as difficult to quantify and many have said that it is like 'taxing air', such a worry does not exist, provided there is 100% BPR for the landowners. Therefore, the tax planning point is that, provided 100% IHT relief can be achieved on the potential development value, this will in turn help the future CGT computation liability by providing a high base cost.

Amenity value

A problem then arises with 'amenity value' as often argued by the District Valuer (DV). Amenity value is generally considered to be where the property is located in a desirable area. The greater the desirability, the greater the value. Such a term is not the 'hope value' of the future development of the land, but just a high value arising from location. It is indeed a rather 'vague concept'. With hope value, the land that is under scrutiny must have the potential to be developed, the land must be an obvious candidate for planning permission or there must be planning permission already achieved. However, with amenity value the consideration for increased value can be just location. HMRC have realised the amenity value concept and are therefore challenging amenity value land with regard to the IHT relief. The Agricultural Property Relief (APR) is fixed to the AV (s115(3) IHTA 1984) and therefore not all the IHT relief on the land may be achieved. The arguments would be that market value is the AV on amenity value land as farmers are willing to pay the high price of the land.

Such a scenario does raise some very difficult problems for tax advisers and landowners. For example, just exactly what is AV? Statistics would show that over the last five years there are some very high values that have been achieved for agricultural land by farmers. Whilst land values might have reduced in the last year and post Brexit, there is still a worry

for advisers. Often farmland in more 'sought after' areas, eg with good rail and road links and in areas of outstanding beauty, might achieve high prices, but this does not stop the land being used for only agricultural purposes. Just because land looks like it could be cut up into 'pony paddocks' does not mean that it will be. So why should more IHT be paid? The amenity value argument must be fought to protect IHT relief. The AV is market value as this is the price farmers have to pay for farmland.

Land used in a trade and the farmhouse

The obvious answer is for BPR to be claimed on the land to avoid AV restriction on the difference between amenity value and AV. However, a large number of land agents advise clients to take on licences, such as Farm Business Tenancies (FBTs), which is a letting situation, especially when health is failing. The need to ensure that land is used in a trade becomes more and more important, although the amenity value point should be fought in its own right.

The protection of the trade status is key at a general level. Firstly, for IHT protection there is also the need to prove that the farmhouse is occupied for the purposes of agriculture under s117 IHTA 1984, and in that regard let land does not qualify unless there is some form of involvement in the trade which again is difficult to define. Secondly, there is the risk of the loss of BPR on the hope value on the land which, in view of the huge potential development projects in the UK, is very extensive and very valuable and has been on people's minds for a long time. Thirdly, there is the worry of the amenity value as set out above. If there is a restriction to AV, there could be some loss of IHT reliefs, but as said such arguments must be fought with the DV. Therefore the risks of not trading are hope value, amenity value and the farmhouse.

The risks of not trading the land

The HMRC guideline IHTM24073 states 'where land is let to a third party under a grazing licence or agreement the owner is unlikely to be in occupation for agricultural purposes of that land during the period of the licence. This may have an impact on whether agricultural relief is available on the farmhouse (IHTM24074). Where the grazier occupies land for agricultural purposes the ownership test under s117(b) IHTA 1984 will need to be satisfied'.

The risk of not trading in tax terms is if the owner of the farmhouse is unlikely to be in occupation for agricultural purposes, and it also does of course depend upon what the arrangement is with the grazing agreement. The case of *McCall (PN McCall & BJA Keenan (Personal Representatives of Mrs E McClean) v HMRC* [2009] STC 990) has looked in depth at grazing agreements and whether or not they qualify for a trade. From practical experience it is fair to say that HMRC appear to have sent various officers to a 'grazing agreement boot camp' so as to maximise the take of IHT from what some would consider an unfair position or even a 'sitting target', particularly where the farmers are fairly elderly and have farmed the land all their lives quite intensely for the majority of the time, such as a big milking operation that became a beef operation, that became a grazing agreement, which is very vulnerable especially where the owners of the land are still looking after livestock and they are being punished in tax terms. The ultimate tax protection is trading.

The importance of accounts

The professional advisers must help the farming community in respect of both the trading and the amenity value 'fight'. Possibly accountants are seeing nothing but Single Farm Payment (now the Basic Payment Scheme) and effectively rent received going through in the accounts and they must flag up the problem of the potential inheritance tax risk. Sadly, farmers are very mindful of costs and sometimes have their accounts and tax returns produced by unqualified advisers and it would not necessarily be highlighted to the landowner as a tax risk. There are examples where the grazing agreement income without any expenses has been posted straight onto the Tax Return without any accounts being prepared. HMRC take a very negative view of such treatment when reviewing the IHT400 and appear to have been trained to challenge such situations automatically and try to disallow IHT relief.

Many HMRC officers consider that in order for the farmhouse connected to the land that is subject to a grazing agreement to qualify for IHT relief, there must be accounts and expenses claimed. The IHT on farmhouse is at risk and this demonstrates the importance of tax compliance and tax advisers thinking ahead and providing complete advice to their clients. The importance of accounts and tax returns for inheritance tax is seen in practice time and time again.

Accounts and the farmer

Whether there is a grazing agreement, a contract farming arrangement or trading in hand, it is important to have strong accounts that correctly reflect the activity. Many of those producing these accounts and the associated tax returns possibly do not realise that due to the self-assessment system where HMRC do not actually see the accounts but just the translation thereof on the tax return, the most likely point for HMRC to scrutinise the farm accounts and inspect the accounts is when the executors use the accounts as a basis of determining APR and BPR, and when the accounts (or lack of accounts) are submitted with the IHT400.

In summary, as accounts do not have to be submitted to HMRC with the tax returns but have to be submitted with the IHT400, the accounts are more critical, it can be argued, in IHT terms rather than income tax terms.

Grazing agreements and correct expenses

All these examples highlight the very critical need for tax advisers to understand the importance of the grazing agreement, the claiming of expenses and the importance of accounts. Likewise, land agents must be very mindful of

the problems that are created by putting a licence or a lease or a weak grazing agreement, without much involvement by the landowner, in place. It is a key tax planning point to ensure that the grazing agreement is not in fact a tenancy. The landowner not the grazier should be responsible for growing the grass and actively performing some activity on the land and looking after the livestock. The statutory definition of farming for both income tax and corporation tax purposes requires that for the landowner of grasslands to be farming he must show that he is in occupation of the pasture and that this is for the purposes of husbandry. In deciding whether the land is occupied by the farmer, the approach to the courts has been to determine the paramount use of the land and then to ascertain the identity of the person who has that use.

Paramount use of the land

In the case of seasonal grazing of grasslands the courts have been prepared to accept that the landowner can be the person with paramount use of the land, hence as long as the landowner conducts some activities which are husbandry in connection with that use, the landowner can be regarded as farming the land. Thus in *CIR v Forsyth-Grant* (1943) 25 TC 369 it was noted by Lord Carmont (at page 379) that '...the laying down of grass in suitable parks, the manuring of the land so as to produce a good crop, and the arranging for the seasonal eating off the grass by cattle brought on to the land are operations of husbandry. The parks are being used for the purposes of husbandry by the proprietor who is occupying them.'

The impact of the *Allen* case (J C Allen TC 5100)

The very recent case of *J C Allen* and the tax interpretation of the 'conacre' arrangement highlights the need to challenge the very aggressive approach of HMRC and the need for the landowner to have the right legal agreement in place. In the *Allen* case the First-tier Tribunal (FTT) decided that Mr Allen had occupied the land for the purposes of husbandry. The FTT was 'strongly influenced' by the traditional understanding of conacre and that the grantor of the licence remained in occupation.

The *Allen* case concerned the eligibility of the conacre for business asset taper relief (BATR). The other farmer (the 'grazier') did not occupy the land for part of the year. Post the Brexit decision there will be many changes to farming and review of the English grazing agreement to reflect more closely the conacre plus additional services that could be considered to establish a trading position.

Action points

In practice towards the end of a farmer's life when ill health plays a critical part in the farm organisation, and when the landowner is possibly still very much involved in the farming operation and enjoying his farming involvement, the lure of a grazing agreement or a tenancy appears the only solution. All those surrounding the family – the beneficiaries, the children, the land agents advising on the use of the land, the tax advisers and those who have drawn up the Will – should be very mindful of ensuring that the trading activity continues on the land as it probably has done for several generations. It is really sad for somebody who has been an active farmer all his life to 'fall at the last hurdle' due to what amounts to be potentially bad advice. There are a considerable number of elderly farmers still owning land. There are large numbers of letting arrangements in place when they should be active and can be made active with help from family members, potential beneficiaries, etc. The awareness of the importance of the trading function just needs to be in place and the advisers and those who produce the accounts and tax returns need to be alert to a problem of too much letting activity by the landowning community and also the impact of the tax disadvantages.

Post the Brexit vote there will be considerable changes to farming at every level and one of these must be to replace the let activity with trading in hand in a structured way. This can offer protection against undue IHT being due on the farmhouse and being due on the 'amenity' and 'hope' value. The concept of amenity value at a general level and the punishing attempt by HMRC at tax collection must be considered.

Supplied by **Julie Butler** F.C.A. Butler & Co, Bennett House, The Dean, Alresford, Hampshire, SO24 9BH. Tel: 01962 735544. Email; j.butler@butler-co.co.uk, Website; www.butler-co.co.uk

***Julie Butler**, F.C.A., is the author of Tax Planning for Farm and Land Diversification (Bloomsbury Professional), Equine Tax Planning* ISBN: 0406966540, and *Stanley: Taxation of Farmers and Landowners* (LexisNexis).

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Client Services: Please contact Client Services on tel: +44 (0)20 7017 7701; +65 65082430 (APAC Singapore), or email clientservices@i-law.com

Editorial queries: Please contact Kate Clifton on tel: +44 (0)20 7377 3976, or email kate.clifton@informa.com

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