Carry on farming

The threats posed by the coronavirus epidemic may mean that tax planning minds should be focused on succession planning. This is particularly true in the farming sector, says Julie Butler.

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What happens to the trade of farming and indeed all the farm diversified operations when a farmer dies and what are the consequences? Tax practitioners will be well advised to consider such issues during normal reviews of any business and, in the context of future planning, there has also been much in the news recently on the problems for dairy and potato farmers with reduced demand from coffee shops and restaurants respectively and what this means for inheritance tax planning. However, if these questions have not been addressed they may now take on increased importance during the coronavirus pandemic given the reality of an elderly farming population. The answers lie in the nature of the legal entity, the quality of the legal agreements and the executor.

> “Farmers may be reluctant to take on a partner.”

Death of a sole trader

A sole trade operation, by definition, can be complex because when the owner dies the business dies with them. There can be less of a problem in industries other than farming because, often, the trader retires before death or has moved to incorporation with an easier succession strategy.

On the other hand, farmers may be reluctant to take on a partner. And if they do move to partnership, a strong legal agreement must be in place. After a farmer dies, responsibility rests with the executor and accounts must be produced to the date of death. The executor must then ensure that the trade continues effectively; for example, ensuring that livestock and employees are protected.

Key points

- The consequences of death on business operations.
- Is there a succession plan?
- Protecting livestock and employment security.
- Self-isolation may be the opportunity to sort paperwork in farming situations.
- Is farmland owned outside the business?
- The impact on inheritance tax business property relief.

If the matter has been discussed with the deceased and there is a well-drafted will and a clear beneficiary or when there are beneficiaries who wish to carry on the trade, the executor can grant them the right to take over the business on the executor’s behalf. Once probate is granted, they can carry on the trade. In practice, many beneficiaries simply take over the trade and the executor lets this happen.

Early identification of the will

The question of livestock is an example of why the will must be found at an early stage with the executor(s) taking a strong role. Many advise that a partnership should be formed before the owner’s death so that the business continues in accordance with the partnership agreement. However, the tax advantage with trading stock can be lost and the sole trader may be averse to any form of partnership. The current self-isolation period may present an opportunity to sort the paperwork around all farming situations.

Tax advantage of the sole trade

The tax advantage is that the new trade starts with ‘probate’ value of stocks, which in farming can be large in amount and value. However, in the accounts for the period to the date of death the stock is still valued at the lower of cost or net realisable value (*HS232: Farm stock valuation* at tinyurl.com/y95n9yxw). There is therefore a tax-free uplift in value. However, this can be a relatively small advantage and the whole position of sole trade versus partnership must be considered ‘in the round’, especially with the logistics of carrying on farming after death: livestock commitments, bank facility and the like.

Death in a partnership

The Partnership Act 1890, s 33 states that if a partner dies the partnership must cease. This can have various logistical problems. To avoid s 33, there must be a clause in the partnership agreement to say the trade will continue. Alternatively, and ideally, there must be a written partnership

minute stating that all parties agree to continuation and understand what this means. Everyone must think through the logistics of the 'new trade' post death and determine who stands in for the new partner in the trading operation; for example, the executor or beneficiary.

A key consideration will be if the deceased owned farmland outside the partnership or had a share of the farmland through a land capital account. These factors should be provided for in the partnership agreement. From an inheritance tax viewpoint, only partnership property qualifies for 100% business property relief. Farmland held outside the partnership has relief at only 50%, although fortunately agricultural relief has no such distinction.

The limited company

The death of any farming director or shareholder should not mean that the trade ceases. However, how the beneficiaries of the director or shareholder should proceed might be dealt with through the shareholders' agreement.

Again, if the deceased farmer owns land outside the limited company there should be protection for the trade through the tenancy arrangement for the limited company to use the land. Often, no such lease is in place because the grant would incur a charge to stamp duty land tax. Thus, not only does the farmer and landowner achieve only 50% business property relief, but the legal occupancy needs to be defined to protect all parties.

It could be that the limited company has an incorrect 'agricultural occupancy' or that the landowner's executor can simply take the land away from the limited company and destroy the trade that has been built up by the other directors. The key is always well-understood legal documents tied into tax and succession planning, to be prepared with the full facts and to plan ahead. ●

Planning point

If farmland is owned personally, does the farming business have security of tenure? Consider the stamp duty land tax and business property relief implications as well as the need to protect all parties.

Author details

Julie Butler FCA 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). She can be contacted by phone on 01962 735544 or email: j.butler@butler-co.co.uk.

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