Correction Of Farm Accounts To Protect Tax Reliefs

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In [Tax]

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Many probate professionals complain about the quality of farm accounts. They mention how assumptions have been made over the years and the forensic analysis of activity and ownership have not been fully understood and reflected in the farm accounts. Often in order to achieve full capital taxes relief, it could be necessary to rectify the accounts when going through the probate process. Obviously, it is better to adjust whilst the farmers are still alive.

Well-drafted partnership agreements are needed for all farming families for accounts, tax and legal protection. For Business Property Relief (BPR) purposes, business assets (including land) achieve 100% BPR as partnership property and only 50% BPR as non-partnership property. This can be a very key point for development land.

It has been said that many farmers, and even some advisers, do not know the difference between farm partnership property and farm property that is owned jointly. When “hope value” exists on property, there could be a significant loss of BPR if there is an error of understanding. For example, if the deceased owns farmland used in the partnership, but this is not in the partnership accounts and there was no partnership agreement to clarify both the legal and tax position.

The importance of quality partnership agreements

If the drafting of the partnership agreement and the forensic work that goes into examining the exact legal ownership of the property highlights a discrepancy with the farm accounts, then the accounts should be adjusted to reflect the correct position. A strong example of the importance of correct farm partnership accounts is Ham v Bell and others [2016] EWHC 1791 (Ch) in the context of farm ownership.

In Ham v Bell, the accounts by mistake had continued to show the farm as an asset of the new partnership but it should not have been. That was an error because, on the evidence, there had been no agreement between the parties that this would be the case.

Rectification of farm accounts

Where the farm accounts show a misunderstanding as to ownership, ie the farm is put “in or out of the balance sheet” in error, they should be rectified as was actioned in Ham v Bell. Continuing with the analysis of the case there was no evidence that any discussion had taken place between the accountants and the claimant, John Ham, or between the accountants and the defendants, his parents Mr and Mrs Ham, about whether the farm had become a partnership asset. When producing farm accounts, the accountants must discuss ownership with the partners and not make assumptions.

The case of Foster (Foster v Revenue and Customs Commissioners [2019] BTC 523) has shown just how high "hope value" can be valued and what the risk can be. It is fair to say that there are potentially a lot of farm accounts for a variety of reasons that do not reflect the correct legal position with regard to ownership of the farm and these should be rectified.

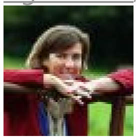
Partners meetings to approve accounts

A robust well-drafted and researched partnership agreement helps the farm partnership with understanding legal ownership. The agreement also assists accountants to produce accurate accounts. With strong legal clarity, the accountants can be sure that the accounts correctly reflect the legal position, and the farming community are protected with accurate accounts. Likewise, the accountants are protected from negligence claims by reflecting the correct position.

It is important that farm accounts meetings are held with all farm partners so everyone is aware of the correct accounts position and the balance sheet and trading position are explained to the partners as to the freehold property and the land capital account. Such meetings have been more difficult with the Covid lockdowns and Zoom meetings have helped. Ideally, any ownership misunderstandings should be embraced at this meeting stage and not in the courts.

With all the changes facing the farming world, particularly the Agriculture Act and capital taxes reforms, forensic understanding of the accounts will be even more important.

Agriculture, Farm, Tax



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