Escape to the country

In the second of a two-part series, Julie and Fred Butler provide a beginner's guide for conveyancers to some of the key tax issues relating to agricultural property

Although there is a lack of supply of farmland and large demand for it, there are recent indications that low supply is beginning to ease and that agricultural property transactions could be on the increase in the forthcoming months and years. This will add to the many financial and tax challenges farmers are facing and will give landowners a more viable option to sell.

Changes to payments and subsidies

The Department for Environment, Food and Rural Affairs (Defra) has confirmed that farmers in England will be able to take a 'lump sum' exit payment in April 2022 instead of receiving their remaining area-based subsidy, the Basic Payment Scheme (BPS), on an annual basis. The BPS is the main rural grant to help the farming industry and since leaving the EU has been renamed by the Direct Payments to Farmers (Legislative Continuity) Bill 2020 (but is still known as BPS). The government's objective is to phase out BPS payments by 2028, but the exit payment is intended to accelerate the pace at which new entrants join the industry and adopt one of the three replacement environment land management schemes (ELMS). Farming will be going through a lot of changes as it moves towards 'farming for the environment', and it will be interesting to see the impact that the proposed exit payment will have on the market.

Bridging the payment gap

One clear action point for all farmers (and their advisers) is to understand the legal ownership of the farming business and property, as there can be complexities in the ownership structure that can lead to misunderstandings. Financial projections must also be prepared for the impact of the loss of BPS on farming finances in order to move towards possible solutions.

By 2024, the BPS payments will be halved, and by 2028 the government aims to have ended 'area-based subsidies' completely. The BPS will be replaced by subsidies under the 'Agricultural Transition Plan' to restore wilder landscapes and achieve enhanced beauty through ELMS. However, the full detail and impact of this is still emerging.

The Finance Act 2021 (FA 2021) leaves capital gains tax (CGT) rates unchanged and agricultural property relief (APR) and business property relief (BPR) are currently intact but future losses of subsidies could be funded by sales of buildings and small areas of land. There is an opportunity for farmers looking to diversify or sell to take advantage of the current high land values and demand. Owners of small fields delivering limited returns from agriculture could benefit from 'cashing in' on the general public's growing demand for land. Sensibly priced property is attracting interest from buyers, but most farmers need help and advice to enable them to make the right short-, medium- and long-term decisions.

More detail is still needed around ELMS, the Agriculture Act 2020 and farming for the environment to assist with decision-making. Against this background, farmers across the country are having to redesign their business models and contemplate future ELMS investment.

Will landowners sell?

Funding will be needed to cope with all of these changes and to do that, options include:

- selling unproductive or marginal fields away from the main farm
- getting professional advice on selling buildings that add value and/or have planning potential
- selling in-demand land with good access, a desirable location or unrivalled views
- using overage clauses to protect the original seller's interests in case of future changes in planning policy and development proceeds, and
- introducing controls over the site's future (such as restrictive covenants).

Development land

Another potential financial solution for farmers could be to realise some of the continuing high values of development land. To do this, CGT planning will have to be revisited due to the increases to CGT rates in the FA 2021.

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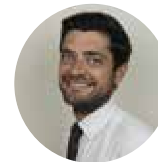

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Of particular interest in terms of tax planning will be the possible deferred consideration of farm development deals. For example, the deferred consideration could be the balance payable (provided planning permission is obtained) to develop land or buildings. For the vendor, negotiating maximum sale proceeds and the tax-efficient split between the deposit and the balancing payment has been a key point of negotiations over the last few years. Here, farm tax and legal teams must work together to ascertain how the terms of a legal contract affect the fundamental tax position.

The date of disposal (under a contract) is given by section 28 of the Taxation of Chargeable Gains Act 1992 (TCGA 1992). In the case of a standard conveyance, section 28(1) is clear that this is when the contract is made (at exchange of contracts, as long as the contract goes on to complete). However, section 28(2) then says that if a contract is conditional, the time of disposal is when the condition is satisfied. As a result, the time of achieving payment of the balance and payment of the deferred consideration may have increased tax implications, as suggested by the Office of Tax Simplification's (OTS) first report on CGT. With concerns over increasing CGT rates, each potential deal will need to be considered on a case-by-case basis as adjusted for the 'battle' between cashflow and tax mitigation. The benefits of rollover relief for CGT will also have to be considered.

The negotiations with the developer with particular reference to deferred consideration and the legal drafting thereon is extremely important to ensure the sale of the land is treated as a capital receipt, rather than an income receipt. Broadly, the landowner cannot be seen to be benefiting from the developer's 'profits' on the sales, as these can be seen as 'slice of the action' arrangements. Therefore, ensuring capital treatment is key. With capital receipts, then the reliefs follow, such as business asset disposal relief (BADAR, formally entrepreneurs relief) or rollover. Both these reliefs are complicated by deferred consideration. Furthermore, taking a property in payment is an extremely tax-inefficient way of receiving proceeds, so will require careful consideration and specialist advice.

VAT considerations on sales and rents

As part of the considerations coming out of 'Tax Day' 2021 on 23 March the VAT position on land (whether it be, a sale or letting) will need to be reviewed. There has been a general trend to narrow the exemption for 'letting land', for example, from self-storage and wedding-related supplies. It is generally expected that the parameters narrow further.

With the VAT status of the supply of land under review, it is a timely moment to consider all potential farmland sales and review both new and old applications for 'opt to tax'.

Guidance on opting to tax land and buildings can be found in VAT notice 742A (tinyurl.com/exdcye6z). Supplies of farmland and buildings, such as freehold sales, leasing or renting, are normally exempt from a VAT charge. This means that no VAT is payable on the sale but the person making the supply cannot recover any of the VAT that is incurred on their expenses. It is possible to opt to tax the land, for example, to charge standard rate VAT on the supply (such as on commercial letting) instead of the exempt supply in order to maximise the overall VAT position. For example, the landowner can claim back all the VAT on converting their farm buildings into commercial units but will have to charge VAT to the tenants (who are usually VAT-registered)

If the farm is a VAT-registered business intended for use as a commercial property entirely for the purposes of their own trade, the farmer / landowner can, subject to any partial exemption restrictions, recover input VAT on the relevant costs without the need of opting to tax the building. If the farmer subsequently decides to let out or sell the property, they should consider whether it is appropriate to opt to tax the property in advance of the letting or sale. Another solution to the 'subsidy gap' would be to let buildings commercially in anticipation of a subsequent sale for development.

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Selling with an opt to tax

This is a complex area of tax and it's worth considering and reviewing the following points:

1. A seller's option to tax does not transfer to a purchaser (they just have to charge standard rate VAT) and a landowner's option to tax does not transfer to a tenant. Each party in the chain of supply should consider whether it's appropriate for them to opt to tax their interest in the property. For example, a tenant of the farm building that is sub-letting part of a property should consider whether they should opt to tax the property.
2. Where a commercial building that would otherwise be subject to standard rate VAT is transferred in the context of a transfer of a going concern and the purchaser opts to tax it in advance of the purchase, a VAT charge can be avoided, providing certain detailed conditions are met.
3. It is essential for the farmer / landowner and their adviser to keep the opt to tax election certificates filed in a very safe place for future sales and to be very clear about what area of land and buildings is included.

The limited company

With the introduction of the 'super deduction' tax relief at 130% in the FA 2021 restricted to the limited company, incorporation has come under the spotlight. Similarly, the tax advantages of research and development are restricted to the limited company, and the farm adviser will have to consider this as part of the overall strategy for farm succession planning and to maximise tax relief in these areas. There will be much debate as to what qualifies as allowances, but the tax advantages are obvious and, in the case of the super deduction, they are limited by time until 31 March 2023.

Incorporation issues for farmers and landowners could impact on the legal occupation and even the ownership of farm property and it is anticipated that there will be legal considerations around the impact of the possible tax advantages in the months and years ahead.

Changes to come

All farming legal and tax advisers will have to be alert to the move to 'farming for the environment', possible farmland sales and possible lifetime gifting while the positive tax rates still exist. Claiming of input VAT on farm sales and letting, together with the output VAT on the sale via opt to tax should also be given due consideration. Similarly, all advisers need to be aware of the stamp duty land tax advantages of 'mixed rates' (where residential and commercial combine) but should be prepared for HM Revenue & Customs to challenge the criteria used. The need for limited company structures to maximise tax advantages too means legal and tax advisers will need a forensic understanding and a holistic approach to all transactions involving property.