Farms: CGT and ascertained value for accounts

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With farmland values remaining high and some farmers looking to sell farmland, sometimes in small blocks, the base cost for capital gains tax (CGT) becomes a key consideration. Julie Butler, joint managing partner at Butler and Co, examines the accounting and tax planning priorities

The date of death or probate value automatically forms the base value on a subsequent disposal for capital gains tax (CGT) purposes but only if it has been 'ascertained' for inheritance tax (IHT) purposes within the meaning of TCGA 1992, section 274.

In a non-IHT paying estate the value will not normally be ascertained in the technical sense and it would be open for the taxpayer to argue a different base value. If a property is sold subsequently for a higher figure than that submitted it may be that the sale price reflects the market value at the date of death, or it may be that there has been an increase in the value since that date.

HMRC resists the use of the 'loss on sale' provisions in IHTA 1984, s190 et seq to substitute a higher value if no IHT is payable: see the HMRC Inheritance Tax Manual IHTM33026.

There has to be consideration about 'ascertained values' for IHT purposes in order to see if it is correct to be used for CGT purposes on a subsequent sale. There are detailed IHT Manuals on the subject to help with guidance.

Tips for accountants

On the basis that the farm property will have to be included in accounts post death and after the land has been gifted on death, accountants must look to disclosure and clarity.

For example, if the farm is left to the spouse and half was gifted to the farmer's son pre-death and the spouse and son are in partnership, this raises issues. If the spouse then chooses to make her share of the farm partnership property to achieve 100% business property relief (BPR) using a land capital account, many would argue that it is full disclosure to show the value used as 'unascertained'. The same would apply to the spouse trading as a sole proprietor.

Let us consider how the probate value per the formal probate valuation in fact does interact with the base cost for CGT. Currently under TCGA 1992, s274, if the value of a farm asset has been 'ascertained' for IHT purposes, then this forms the farm base cost for CGT purposes.

If the value of an asset has not been ascertained, the normal rules of TCGA 1992, s272 will apply to determine the CGT acquisition value to be used by the executors or beneficiaries in subsequent sales.

For a value to be ascertained for this purpose, there has to be some form of agreement by HMRC as to the value put forward by the executors. If the value proposed is merely accepted by HMRC because the IHT liability is not dependent upon the value, then the value has not been 'ascertained'. In particular, this will be the case if:

- the whole estate is clearly below the IHT threshold;
- the estate is transferred to the deceased's spouse or civil partner so that inheritance tax is not due; or
- assets are exempt from IHT.

Any question of valuation for CGT purposes then goes back to consideration of what indeed was the open market value at the date of death. In such cases the CG34 post-transaction valuation check procedure may be used to give certainty.

In practical terms this can be important when the farm passes to the spouse and the probate values are not ascertained for both accounts and tax. If there is development value and the spouse sells part of the farm for development, the base cost for CGT can be important in calculating the CGT liability and also in CGT planning, eg, rollover relief.

Therefore, the base cost for CGT planning on future disposals must be considered by accountants. Also, the accounts disclosure of the probate value has to be assessed in the accounts moving forward. 'Unascertained values' of the farmland, buildings, farmhouse and cottages are normally used as the historic cost of the beneficiary and their base cost for CGT. The reliability of the value should be reviewed by the tax planner and those producing the accounts.

Land capital accounts

If the land has been made an asset of the business and thus appears on the balance sheet then it is very important that specific land capital accounts are used rather than having all the assets in one general capital account.

By having the land and the ownership thereof clearly defined within land capital accounts removes issues of 'accidental' gifts/transfers of value of the underlying asset. This is known to happen when everything is lumped together, perhaps because of loss utilisation through adjustment of profit/loss shares.

Furthermore, adjusting freehold property to probate value is a lot simpler if the asset is held within its own land capital account.

Uncertain farm values and the interaction of farm beneficiaries

In *Stonor & Mills (Dickinson's Executors) v CIR* [2001] SSCD 199, it was held that a claim to substitute the proceeds of the sale of a property was not valid when there has been no IHT liability, so IHTA s191 cannot be used to increase the base cost for CGT purposes.

During the administration of an estate any CGT loss made on a disposal may be set against any other gains made by the executors or administrators in the same way as with individuals. However, the CGT loss of the estate cannot be transferred to the beneficiaries. This is in contrast with the rule that allows CGT losses arising to trustees to be transferred to beneficiaries.

In some circumstances it may be better for tax planning purposes to transfer a property to beneficiaries before sale if the loss can be used by the beneficiary as they will acquire the property at probate value for CGT purposes.

Any transfer should be made in good time before the sale and preferably before the property is put on the market. In practical terms with the volatile farm property market it has been very difficult for valuers to ascertain the s160 market value, which is the probate value of farms.

The starting point for the valuation of assets within a deceased's estate for CGT purposes is 'the price which…might reasonably be expected…on a sale in the open market' – see TCGA 1992, s272 as already mentioned.

The IHT requirement under IHTA 1984, s160 is substantially the same. Fluctuations can occur where 'rollover buyers' become interested and increase the sales value a potentially short time after the probate value has been agreed. In these cases, the executors can claim that the probate valuation was wrong and did not, for example, take account of 'special buyers'.

What value to choose

The IHT405 schedule for interests in land allows the personal representatives the option to have the sale price of a property sold within 12 months of death to be treated as the date of death value. This choice must be made when the IHT400 is submitted and the outcome of the sale may not be known at that stage.

For IHT purposes many argue that the executors should ensure that at least two independent valuations of the farm are obtained, some consider this disproportionate. Although if there is a debate with beneficiaries they too might obtain a valuation. In the case of properties, estate agents should be asked to give a realistic sale price rather than a suggested selling price in respect of which lower offers will be accepted.

Ironically Covid and farm subsidy uncertainty does not seem to have reduced farm values.

A clear message is that how probate values are reflected in the accounts must be given serious consideration.

For example, with regard to the beneficiary's historic cost probate value. Also, the impact of probate value on the whole of the partnership accounts figure used as the cost of the freehold farm. Another generic question must be asked with regard to the historic cost used: is this a good time to revalue the farm in the accounts instead of using historic cost?

Sales made by executors

Sales made by the executors which result in CGT payable by the executors during the administration of the estate are currently taxed at 28% on farm residential property or 20% on other farm assets, eg, farmland and buildings, subject to basic rate restrictions.

Any costs of sale, such as estate and land agents' fees and legal fees, are deductible in calculating any capital gain. This can result in some complex tax planning with the CGT rates of tax lower than the IHT rates but where BPR and APR apply, higher values are welcomed by the beneficiaries for future CGT values.

Executors can claim the full annual exempt amount for CGT for the period from the date of death to the following 5 April and in the following two tax years. From time-to-time executors have to sell assets for a number of reasons, eg, to pay off beneficiaries, to pay IHT bills, to repay loans and other costs of the estate.

If at a later date the personal representatives seek, without adequate justification, to revise their initial IHT figure by way of a corrective account they risk HMRC arguing that the initial figure was inaccurate, so the FA 2007, Sch 24 penalty regime applies. However, in the IHT context that regime will not bite unless there is an actual loss of tax, which would be the case if the adjusted value led to the estate becoming taxable.

Following the Budget 2021 and Tax Day with no real changes to IHT and CGT many tax planners consider that lifetime gifting will also be a strong consideration both now and after any reform of CGT at some point in the future.

These are uncertain times for the future of farming and the speculation of the impact of the future tax policy is rife. There are, however, a number of certainties – quality and accurate base costs for CGT will be essential and the importance of evidence of previous ascertained values together with improvements on non-ascertained values will be essential.

Many would argue that this base cost work should be part of full succession planning for farms. All values shown in farm accounts should be clearly identified with notes so that farmers, accountants and tax advisers fully understand.

It is incorrect for tax advisers to use unascertained values without warning their clients of the consequences of challenge by HMRC, indeed the full consequences of the probate value, ascertained and unascertained together with the base cost for CGT.

In these times of the 'minimum disclosure' trend when it comes to farm partnership accounts with the propensity for farmers to dispute, as well as not to understand the partnership/non-partnership distinction (100%-50% BPR) there are many arguments for full disclosure to try and prevent disputes, loss of BPR and value misunderstandings.

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