



PUTTING FARMLAND OUT TO PASTURE

Julie Butler highlights the key tax headaches of diversifying away from traditional farming with regard to the UK *Agriculture Bill 2017-19*

➤ KEY POINTS

WHAT IS THE ISSUE?

UK farms must diversify to survive in the years ahead. The tax pitfalls and advantages of such alternative land use must be considered.

WHAT DOES IT MEAN FOR ME?

The next few months and years will be difficult for the farming industry. Farmers will need help from STEP members with regard to tax protection and tax planning.

WHAT CAN I TAKE AWAY?

There is a large amount of potential work for the diversified farming industry. The lack of farmer awareness is a key issue, as is highlighting the need for tax protection around the potential pitfalls of diversification.

THE *AGRICULTURE BILL 2017-19*, published in September 2018, sets out to reform the UK's existing farming policy as part of a 'Green Brexit'. In the process, it heralds the biggest change to the agricultural economy in generations. Michael Gove, the minister initially sponsoring the Bill, has claimed that this constitutes a farming revolution. Under the terms of the Bill, public money could be spent on various 'public goods', including:

- improved access to the countryside;
- environmental enhancement, protection and enjoyment;
- better animal health and welfare;
- healthy crops, trees, plants and bees; and
- reserving rural resilience, traditional farming and upland landscapes.

However, many in the farming industry are lobbying for greater emphasis on food production.

The Bill, though, appears to indicate a move away from the traditional view that farming is all about food production. Many argue that the modern-day farmer needs to diversify to survive, but the problem with such a direction is the potential loss of valuable tax reliefs, particularly around inheritance tax (IHT). Tax advisors are certainly aware of Her Majesty's Revenue and Customs' (HMRC's) current appetite to attack various tax reliefs, and it is therefore crucial to be prepared for the tax pitfalls (as well as possible advantages) of any changes of direction ahead.

DIVERSE OPTIONS

For farmers, there are currently many alternative business structures through

which they can trade, and there are a multitude of points to consider when deciding on a diversification strategy. These range from the personal need to provide for family succession and reduce the workload of elderly farmers to the industry-wide problems of low profits, Brexit and HMRC's attack on diversification projects. Farmers also need to be aware of the strong development opportunities in the UK in the light of a continued demand for housing.

These factors can make decisions on business structure complicated, even before consideration is given to the tax-planning strategies that could help to navigate these problems and opportunities in the most efficient way.

Housing development opportunities will need the protection of capital gains tax (CGT) reliefs to avoid substantial tax bills at the end of such projects, while farmers and their advisors must plan for potential IHT liabilities and look towards mitigating these through the correct application of agricultural and business property reliefs (APR and BPR). Any leased land runs the risk of not qualifying for BPR, or only receiving 50 per cent of APR.

One direction for the landowner to take could be to try to reduce the number of tenancies. However, there is always the risk of family disputes when it comes to discussing future inheritance and diversification strategies. All such matters must be dealt with sensitively and transparently.



HOPE SPRINGS ETERNAL

Last year, the case of *Palliser v HMRC*¹ before the Lands Chamber of the Upper Tribunal highlighted the importance of the correct consideration and calculation of ‘hope value’ (the amount that is added to the valuation of land due to development potential). It was concluded that hope value should be included in the probate value and, as such, BPR is likely to play a greater role for the farming community in the years ahead.

The primary intention of BPR is to enable businesses to cope with a death in the family or another IHT event without causing the entity to have to be sold. It is meant to be a ‘relief’ and must be considered in addition to APR on the death of any farmer. APR only covers the agricultural value of land, whereas BPR covers the whole market value of the land, including the hope value.

If only APR (and not BPR) is claimed by the farming family, there may still be a significant IHT liability, but a BPR claim would eradicate this extra liability on areas not qualifying for APR. In general terms, providing the potential development land is part of a trade and meets the tests under s.105(3) of the *Inheritance Tax Act 1984*, BPR should be achieved. If there are too many investments (including let property) under s.105(3) to qualify for BPR,² a withdrawal of some of these investment assets must be considered, so as not to ‘swamp’ the trade with investments. Such a balance of investments and trading can be considered the ‘investment line’.

For example, a farm business tenancy will not achieve BPR, and if such a tenancy relates to development land, this could have even worse tax implications. A full analysis of land leases is therefore required, and the whole issue of the trading operation and the ‘investment line’ must be reviewed to ensure future IHT liabilities are minimised. Indeed, the interaction with all areas of tax needs to be taken into account.

There are many short-, medium- and long-term goals for the farming

community with regard to diversification and its interaction with IHT and CGT reliefs. While farmers must focus on financial survival and what suits their businesses best, it is imperative to involve their professional tax advisors in pulling together the various angles and to ensure that the planning is tailor-made for their farming operations. The worry is that if there is too much ‘public good’ as described by the Bill, and not enough food production, then there may be issues over future claims for IHT and CGT.

LETTING IT ALL GO

It is a common occurrence in the farming industry for a ‘traditional’ agricultural farmer to move towards letting agricultural buildings and livery yards or supplying hay, for example – particularly as they become less physically able to undertake other farming activities. Unfortunately, such a course of action carries the risk of missing out on IHT reliefs from all directions. Animals used in the food chain clearly come under husbandry, so livestock can provide excellent farming tax reliefs. However, moving away from pure husbandry towards horses and ‘public products’ could be punishing in tax terms for the farming community. The exact details of the Bill and ‘public products’ are still evolving, and this is a difficult time for the tax advisor to help their farming clients.

However, the recent success for the taxpayer in *HMRC v The Estate of Maureen M Vigne (Deceased)*³ on claiming BPR on an enhanced DIY livery yard is positive news for the diversifying farmer. Meanwhile, the furnished holiday accommodation case of *The Personal Representatives of Grace Joyce Graham (Deceased) v HMRC*⁴ showed the need for a high level of public services to qualify for the all-important BPR where farms have diversified. HMRC was appealing the *Graham* case, but this has since been withdrawn.

Evidence that an operation’s offering goes further than simply the letting of land is essential for the business to avoid

being considered as one that wholly or mainly holds investments. There is an interesting quote from *Vigne* that there is no clear ‘bright line’ between investment and trading activities, but that guidance has been given when it comes to delineating services. In the *Graham* case, the tribunal recognised that customers were ‘lavished’ with services.

NEXT STEPS

When undertaking IHT planning in advance of a death, and likewise when subsequently completing the IHT400 form, the question of how the diversified operations are conducted must be analysed forensically, regardless of whether these are liveries, furnished holiday accommodation or storage operations. Recent tribunals and HMRC probate enquiries have showed that HMRC is likely to give the matter serious consideration, so farmers and their advisors should do so too.

Certainly, the emphasis on environmental protection and the priority of stewardship over food production in the Bill calls for a farm’s overall tax position to be reviewed urgently in the context of all leases, licences and other diversification activities. Given HMRC’s history of (arguably) being unduly aggressive about all forms of diversification or letting being seen as an investment activity, strong, solid arguments must be presented and defended to prove there is a ‘bright line’ showing the emphasis of trading.

¹ [2018] UKUT 0071 (LC) ² See *Commissioners for HMRC v A M Brander (as executor of the Will of the late 4th Earl of Balfour)* [2010] UKUT 300 (TCC) ³ [2018] UKUT 0357 ⁴ [2018] UK FTT 0306 (TC)



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