Under pressure

Julie Butler and Andy Case discuss the 2023 Budget changes leading to pressures on farming arrangements and tenancies.

The 2023 Budget 'packed a surprising punch' for farmers. Not just a consultation on the taxation of ecosystems, but also consideration around farm tenancies as a large amount of UK farmland is let. The consultation called for views on restricting agricultural property relief (APR) at 100% to farm business tenancies (FBTs) that run for a minimum period of at least eight years. This is an area where there is a great deal of controversy following the Rock Review on agricultural tenancies (tinyurl.com/yc8h3bdd) and it is essential for all farm tax advisers and those advisers that act for landowners, and also recent investors in farmland, to be aware.

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The results of the consultation are still awaited, but the government has responded and accepted the majority of the Rock Review and has begun implementing this.

The government is exploring:

- the impact of restricting 100% APR for tenancies of at least eight years, whether any exclusions to this would be necessary, and how these could be defined if the government pursued this; and
- the issue of farming tenants' access to long-term environmental schemes.

Many organisations were opposed to the suggestion of FBTs that run for a longer period than the current short-term arrangements because they considered that it could lead to the loss of large areas of land from the let sector in England alone. There could be further losses of let land being available in Wales and Scotland and it would act as a deterrent to any tenancies in Northern Ireland. There could be an impact on contract farming arrangements (CFAs) and other farming arrangements.

Key points

- The government has accepted the majority of the Rock Review on agricultural tenancies and has begun implementing changes.
- Many organisations were opposed to the suggestion of FBTs that run for a longer period than the current short-term arrangements.
- It is considered that the move could permanently remove land from the tenanted market into 'contracting models' like CFAs.

Opposition to the eight year agricultural tenancies

The logic of the proposals seems to be that if the government restricts APR so that it can only be applied to tenancies of more than eight years, the market will move to eight-year tenancy periods. However, many consider that this is unlikely to be the case as this would be unattractive to landowners who enjoy short leases as a commercial approach to farming through the current FBT provisions.

It is considered that there is a very real risk that rather than encouraging longer-term letting, the proposals to limit APR to tenancies of eight years or more will drive those who would otherwise let for the short-term market to look for other business models such as CFAs. The move could permanently remove land from the tenanted market 'into the arms' of a contracting model. Again this has evoked different commercial and tax views.

The government's response to the Rock Review covers a lot of interesting angles and headlines:

- Increasing tenants' access to a wider range of environmental scheme options.
- Making environmental management scheme (ELMs) agreements transferable between tenant and landlord and other tenants.
- Implementing restrictions on landlords after taking land back in hand.
- New entrants.
- Strengthening landlord/tenant relationships.

- Diversification in the farm business tenancy (FBT) so they don't have to be restricted to agriculture and they can be for longer periods.
- The consideration of the regulation of land agents.

The Tenant Farmers Association

The Tenant Farmers Association (TFA) wholeheartedly agrees with the proposal as longer-term tenancies provide the best basis for tenant farmers with regard to funding investment, delivering productivity gains and securing environmental objectives.

However, in practice, this might not be achieved. The association's preference is for land to be let for an initial term of ten years, without fixed break clauses, before being eligible for 100% APR (as opposed to 50% APR), but that has problems. However, the TFA would be happy to accept an eight-year provision – as recommended as part of the Rock Review, as a major step in the right direction. It also rejects the argument that restricting APR in this way would be a restriction on freedom of contract for the landowners.

The TFA view is understood to be that landowners can continue to be free to let land on whatever terms they desire. However, landowners will only obtain the taxation relief if they let for longer terms. In reality, tax reliefs drive landowners in a greater way than has been considered and could be negative.

Impact on tax planning for CFAs

The TFA accepts that some landowners might be encouraged not to let land because of the changed tax position and, above all, the longer period for the FBT, but it is understood they believe there would be a marginal negative impact. The views on this matter vary considerably between the organisations.

Whatever happens in the wake of this, it will be essential that contract farming agreements (CFAs) are run tax efficiently, with the landowner assuming the risks of farming the land, rather than the contractor.

Alongside making the change to inheritance tax (IHT) relief, many consider that it will be important for the Treasury to ensure that the HMRC guidance to identify weak contract farming and other arrangements should be made stronger in tax terms. Currently it is considered that business property relief (BPR) can be achieved on CFAs provided they demonstrate that the landowner is trading.

Likewise, APR on the farmhouse – the relevant case here is *Arnander and others (executors of McKenna dec'd)* [2006] SpC 565 where the weak CFA prevented APR and BPR being claimed.

The risks of the CFA coming under even more scrutiny must be taken seriously by landowners and their advisers right now.

All CFAs will have to be updated for any ELMs work and the move away from BPS. With these reviews, as well as full succession planning with all the changes, working to make CFAs more robust to run alongside the eight-year FBT debate should be considered.

Risks of changes moving farmers to CFAs

Many are supportive of seeking ways to increase the average length of FBTs but are worried about the possible risks of moving landowners away from short-term tenancies and the flexibilities they give and encourage more CFAs which must be tax efficient.

Many consider that it is essential for the Department for Environment Food and Rural Affairs (Defra) to undertake a modelling exercise to evaluate the likely outcome of this eight-year tenancy proposal.

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Given that two-thirds of all active farmers rent some or all of their farmland, many could only support the proposal if the modelling strongly suggested it was likely to lead to longer-term FBTs without a significant contraction of the agricultural land available for active farmers to rent. Very complex dynamics for all those involved. In the meantime, the proposals emphasise that tax advisers must ensure that all farming arrangements are robust for tax purposes.

Things that are certain as a result of all the proposed changes is that all tenancies and farming arrangements will have to be reviewed in the months ahead and tax planning for tenancies and farming for the environment will have to be incorporated into full succession planning that has been carried out and needs to be carried out.

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