

Renewable Energy Enterprises and Inheritance Tax

All landowners should be considering the potential additional income and profitability from renewable technology.

And whilst there has always been the potential for good profit for landowners from renewable energy, various changes from the government over the last year or so have increased the potential earnings from power generation.

Alternatives

From wind turbines to solar panels, with consideration for rainwater harvesting to breaking down organic waste, the potential is endless for the landowning and farming community to consider commercial return.

But with so many options out there, what are some of the alternative types of renewable energy schemes?

1. Wind

The much debated turbine, which has been very profitable for many landowners.

2. Solar photovoltaic

Basically a field of solar panels. These were very expensive to buy and install, but with costs coming down they are becoming a better investment.

3. Hydro

The power of water. A very traditional power source, but one that modern turbine technology has made much more efficient.

4. Anaerobic digestion

Producing energy from the vital process of recycling and breaking down organic waste

Government help

The opportunity to be profitably green with regard to renewable technology was boosted in April 2010, with the introduction of the nationwide Feed-in Tariff (FIT). This offers a guaranteed price for electricity generated from renewable sources, allowing you to plan ahead and get a stable return on your investment.

And the profit potential was further encouraged on 10 March 2011 when the RHI (Renewable Heat Incentive) was announced to use heat from renewable energy.

Tax planning

There are lots of factors to think of before starting a renewables project, but one that is often forgotten is tax.

And this is not just the tax on your hoped-for profits. There is a danger that going green could affect the whole long-term tax planning for your land holdings.

It can be argued that when looking at a renewable heat initiative (RHI) project, the same tax principles have to be considered as with any diversification project.

Incorporation

One opportunity where important decisions have to be made is whether there should be a separate limited company for the renewable energy enterprise to seek shelter under.

With the drop in the corporation tax rate from April 2011, and the increase in Class 4 National Insurance Contribution rates from the same date for unincorporated business activities, forming a limited company to be used as the trad-

ing vehicle for the renewable energy project becomes very attractive.

Inheritance Tax

But while we are concentrating on reducing the tax on the profits from the energy generation, it is easy to forget is that it is also vitally important to consider how the new business activity will affect the wider tax treatment of your land, and all the various tax reliefs that are hopefully linked to it.

One very important one is Inheritance Tax, where an active involvement will be required to maximise the use of Business Property Relief, or active husbandry will be important to claim Agricultural Property Relief.

Clearly a renewable scheme with active involvement on the farm/estate helps towards Business Property Relief, as there should be the badges of trade to help promote the Business Property Relief argument. But what about just renting out land to a renewables company?

Inheritance tax - active involvement or letting

The question to be asked is should the operation be a share in a joint venture, where you are sharing in the profits and losses of the venture, or simply a lease of the site to an operator.

As a landowner you have probably put significant effort into ensuring that the land qualifies for one of the exemptions from Inheritance Tax, and you will not want your renewable energy activity to endanger that,

And if you do not have much active involvement in the business, will the *Farmer* and *Balfour* cases

(*Balfour (RCC v Brander (as Executor of the Will of the Late Fourth Earl of Balfour))* [2010] UK UT 300 (TCC)) help extend the Inheritance Tax protection given on the rest of your land to the relatively small renewable energy part?

Alternatives

The choices are basically:

1. *Passive let*

Under this method you simply receive rental income or some similar fixed payment from the alternative energy operation.

2. *A share in the business*

Alternatively you can be a partner or shareholder in the renewable energy business, sharing in the profits and losses.

Clearly if you are a genuine partner in the renewable energy business, sharing in the profit and losses, then it is much easier to argue that you have a business for Business Property Relief purposes, and therefore to protect the land from possible future Inheritance Tax under Business Property Relief.

However even without that, the cases of *Farmer and Balfour* (examined in previous issues of *Tax Confidential*) can give an opportunity to claim Business Property Relief even on what might appear to be a simple investment activity.

Plus do not forget about the possibilities of joint use of land. If the decision is to have a letting operation, it is important that the site integrates into overall farm and landed estate, so in the same way it is important to have sheep grazing on the grouse moor, so must they graze around the turbines and solar panels or the arable surrounding the turbines.

Tax Tip

If your renewable energy activity is structured as a letting, with the farming operation letting the land to a separate renewable energy company, the Business Property Relief argument for Inheritance Tax exemption can be endorsed if the renewable energy operation is integrated into the predominant activity of farming.

To achieve this, there must be a review of the criteria established in *Balfour* and *Farmer* to see if the income etc from the Renewable Heat Incentive activity “tips the balance” of the investment activity, i.e. whether there is greater investment activity or farming activity on the criteria of turnover, profit, asset values and staff employed.

Carry out a “business” audit to review the chances of achieving Business Property Relief on the whole farm enterprise, and highlight the weak areas, including the Renewable Heat Incentive letting, that could be caught under s105(3) of the Inheritance Tax Act 1984.

This could help in the final decision-making as to which structure and trading vehicle to use for the Renewable Heat Incentive operation.

Enterprise Investment Scheme

One other possibility may be to take tax advantage of the Enterprise Investment Scheme (EIS), under which tax reliefs are given for investment in new business schemes.

Farming does not qualify for Enterprise Investment Scheme, but a renewable energy project can meet the criteria.

This would require a separate company in which there are other investors, with the land let to that

company. Land let for non-agricultural purposes would normally cause problems for Inheritance Tax, with a risk of losing Agricultural Property Relief, but if the activities can be sufficiently integrated (as shown above), then *Farmer* and *Balfour* could give the confidence to allow another let investment activity and so maybe take tax advantage of Enterprise Investment Scheme relief.

Care would have to be taken to ensure that the company, its shareholders and its operations met all the complex Enterprise Investment Scheme requirements.

Tailor made planning

The commercial decisions to be taken with regard to the use of the renewables will vary from enterprise to enterprise, and every review will have to be tailor made to the landowner.

No two situations will be the same as there will be such a variance of commercial energy potential on the land, and a wide variety of tax drivers and business opportunities to be taken into account. □

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