# Agri Matters

Summer 2019

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FARMING IS OUR FIELD

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# Welcome

Andrew Robinson
Head of Agriculture

Welcome to our summer 2019 issue of Agrimatters. As I sit writing this article after checking my pedigree calving cows, it feels like things haven't changed since the last issue of Agrimatters. We are still no further forward with the Brexit issue and whichever side of the fence you sit on, I think we can all agree that the continued uncertainty is bad for the UK Farming Industry. We need decisions sooner rather than later to allow businesses to plan and move forward.

Making Tax Digital (MTD) is now here and we are working with our clients to ensure they are compliant. While it may seem an extra level of bureaucracy, it is important to take the positives from it where possible. Having to keep up to date and have real time financial data allows far greater forward planning and monitoring for all farming businesses. This also allows valuable tax planning to be undertaken much easier - this is a real positive of the MTD regime. We include an article on how we are looking to lead as a firm by partnering with Figured a farm management and budgeting software provider. This uses your MTD data to generate management tools to help monitor your business.

Farming is coming under some very unjust criticism in terms of environmental and diet choice, in my opinion, from the media and social media. It is therefore important that all of us in the industry spread the strong and positive messages we have, but don't rise to the bait – the best way is to engage via proper conversation with all parties.

We have a guest article from Caroline Hawcroft of solicitors Lupton Fawcett in York on the subject of legal pitfalls arising on farm diversification projects.

We also have a guest article by Chris Clark which is a thought provoking discussion on whether increasing output on upland farms makes commercial sense. Chris will be writing a blog on our website with his insight on political and economic changes affecting agriculture.

Areas of woodland on farms are often overlooked, but can be a useful contributor to overall farm profitability. We have an article by Jonathan York looking at this area.

There have been further changes to capital allowances on farm machinery and buildings, and an article by Peter Molyneux explains the current position.

Our agricultural tax director, Keith Johnston, discusses problem areas for Inheritance Tax when a farming business diversifies away from traditional agricultural activities.

Our news page contains topical updates on Universal Credit, tax on sale of Dairy Crest shares, increases in probate fees, and a recent Scottish Land Commission report.

We will be attending our regular shows and we are heavily involved in the National Beef Expo this year held at J36 auction mart Kendal on 23rd May where I am speaking at one of the seminars on future proofing your farm.

I hope to see you around the events this summer.

Andrew Robinson

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# Guest article

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## Upland farming – A Dilemma!

Chris Clark

**In 2005 Chris and Fiona Clark bought Nethergill Farm – 175 hectares in the middle of the Yorkshire Dales. Since then land management at Nethergill has evolved to a point where the production of food, farming and nature are significantly better in balance.**

In 2018 I was contracted to investigate and analyse hill farms in Nidderdale AONB and to work with NGO's in North Yorkshire, Cumbria and Surrey. In order to complete the assignments, a bespoke 'Nethergill Model' was developed. This calculates the maximum level of financial sustainability on a farm, or alternatively the maximum sustainable stocking rate (MSSR).

Hill farming is driven by the quality and quantity of grass available to the farmer. This situation is affected principally by:

- **Geology, which is the pre-determinant factor in grass quality**
- **Latitude, which determines sunshine**
- **Elevation, which determines temperatures**
- **Precipitation, which is an essential pre-requisite**

Whilst much has been done to make farmland more productive over the centuries, for example through de-forestation or drainage, it has had little impact on the fundamental viability of hill farming.

Since 1945, one-off capital investment has largely been replaced by annual programmes of investment to try to correct the fundamental natural deficiencies of the uplands, such as poor soils, latitude and elevation. This includes the use of artificial fertilisers or purchase of proprietary feed-stocks. This has enabled hill farmers to increase the number of livestock to levels well above the natural carrying capacity of the land, and to generate significant additional income. It has not, however, enabled hill farmers to generate any additional profit.

Our direct experience of farming at Nethergill Farm and the experience of other hill farms in Wharfedale, Malhamdale and Nidderdale, and our detailed analysis work with over 25 hill farms so far in 2018, have developed this thesis for hill farming - "If there isn't enough natural grass, no amount of corrective economic action can make the farming any more profitable."

This has significant implications for current stocking rates, and it undermines (totally) the economies of scale theory that prevails in the rest of the industrial world. The world of hill farming is characterised by non-linear variable costs. This means that "Beyond the maximum sustainable stocking rates on a farm, its intrinsic profitability reverses and so, as many farms attempt to produce additional revenue, more money is lost."

Hence, the more stock that a farm attempts to produce, the more the actual profit decreases – to a point, which many hill farmers have now reached without realising it, that the core farm business is actually losing money. Contrary to the received wisdom and counter-intuitively, the economic reality is that reducing stocking rates (to the 'sweet-spot', naturally sustainable level) produces the maximum profit (i.e. the maximum positive differential between income and costs).

Not only does this improve farm business viability, by default it produces more resilient rural communities. It also naturally starts to generate significant environmental improvements; improvements that, with the current DEFRA thinking, would appear to be eligible for the highest level of any future 'payment for public benefits' policy currently being promoted by government.

Chris Clark
Nethergill Farm

# Capital allowances

## *and farm buildings*

**In these pages in the past we have explained the constant changes made to the level of tax relief on the purchase of machinery and equipment. The Chancellor of the Exchequer introduced the Annual Investment Allowance (AIA) in 2008 and at the same time announced that Agricultural Buildings Allowances (ABA), which had given a less than generous 4% tax relief per year, were to be phased out.**

Between 2008 and 2015 there were five changes to the AIA limit, then from January 2016 a "permanent" AIA of £200,000 was introduced, which for most farming businesses was sufficient to ensure that all machinery purchases obtained 100% tax relief.

The "permanent" AIA lasted less than two years before it was changed again, with a temporary increase to £1 million for two years, from January 2019 to December 2020. Unless a business draws up accounts to 31st December the increased AIA will have to be apportioned between accounts years, which will create complications. For example a business with a 31st March accounting date will have an allowance of £400,000 in the year to 31st March 2019. However, HMRC guidance says only £200,000 of the expenditure can occur before 31st December 2018.

The second announcement in the November 2018 Budget was the introduction of a Structures and Buildings Allowance (SBA), which has similarities to the old ABA system mentioned above:

- It applies to expenditure incurred on or after 29th October 2018.
- It gives tax relief at a flat rate of 2% per year over 50 years.
- Relief is only given when the building is brought into use.
- Relief is given on the cost of constructing or renovation of the building, but not on the cost of the land, and not on professional fees or planning fees.
- No relief is due on a dwelling house.
- Expenditure on items within a building which already qualify for tax relief, as either integral features or plant and machinery, are unaffected by these changes.
- Relief will be available on the purchase of a second hand building, but only where the expenditure has taken place after October 2018.
- When a building is sold, the SBA claimed is deducted from the cost of the building when calculating the capital gains tax (CGT) position.

In summary, the new SBA will provide a modest tax saving to farmers constructing a new building. However, it is unlikely to be of sufficient scale to tip the balance for anyone undecided as to whether to undertake a significant project. As always, all capital expenditure should be undertaken for the long-term benefit of the business, not merely for the tax advantage.

**Grain Stores –** there has been an interesting tax tribunal where an arable farmer from Devon claimed capital allowances on the entire cost of his new grain store. Prior to this case HMRC would only allow tax relief on minor parts of the building such as drying machinery and electrical fittings.

The Tribunal allowed the claim on the basis that the structure was a grain silo for temporary storage. HMRC are not appealing the decision but have apparently stated that in their view most grain stores still do not qualify for capital allowances.

*Peter Molyneux*
Accounting Partner

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# Guest article

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## Diversification - the legal pitfalls

*Caroline Hawcroft*

This is an extremely challenging time for the farming industry. With lower food prices, increasing energy costs, slashed subsidies, and increased competition; it is not surprising that many British farmers are finding it hard to make a living. Add in Brexit and the recent publication of the new Agricultural Bill we are likely to see the biggest shake up in the industry for decades.

With all the challenges facing our farming community it is no surprise that many farmers have to think laterally to make ends meet. As such diversification is likely to play an even greater role in creating a strong, robust and successful farming business than ever before. A diverse farming business with more than one income stream has a greater chance of succeeding in the future. Business diversification is a key strategic step to future proof farming businesses. However, it is essential that landowners are properly advised before embarking on such a project in order to avoid the legal consequences of the various pitfalls:

**Title**
It is important to check the title of the property to determine whether there are any restrictions which could prevent diversification. In addition, if the land is secured by a bank charge it is likely that bank's consent will be required to any change of use. If the property is leasehold then careful consideration of the terms of the lease need to be carried out to ensure the terms allow for a change of use. Landlord's consent is likely to be required before any diversification works can be started. Furthermore, if the land is tenanted, do the terms of the tenancy/licence allow for termination if the land is required for the project?

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**Planning**
Careful consideration must be given as to whether the diversification project requires planning consent. For example, renovating a farm building to be used for commercial or residential use is likely to require a change of use and, as such planning consent. However, consideration should be given as to whether the proposed development would be permitted under Permitted Development Rights, without a full application.

**Services**
Development of land or buildings may require connection to utilities such as water, drainage, electricity, etc. Are there express rights for services in the title? If connection to the services cannot be obtained direct from the land easements may need to be negotiated with neighbouring land owners. Consent to connect to public utilities may also be required from statutory undertakers.

**Finance**
Additional finance may be required to fund the diversification project with security being required over land/buildings. It is sensible to discuss the diversification project and any funding requirements with a lender at an early stage.

**Tax**
Obtaining tax advice before committing to a diversification scheme is essential as diversification can have tax consequences, in particular Inheritance Tax. As such, it is extremely important that tax advice is taken at the outset of the project.

*Caroline Hawcroft*
Head of Agriculture,
Lupton Fawcett
Solicitors, York

# News

## Capital Gains Tax on Dairy Crest shares

**A significant number of current and former dairy farmers owned shares in Dairy Crest PLC. The company has been taken over by a Canadian company called Saputo, and following the long drawn out legal process, shareholders received £6.20 per share at the end of April.**

This receipt will be taxed as a Capital Gain but there are a number of deductions and exemptions which can be claimed to reduce the amount of tax payable.

Dairy Crest was originally part of the Milk Marketing Board until it was disbanded in 1994. All farming businesses that produced milk in 1993 were given free shares, and had the opportunity to purchase additional shares at a cost of £1.55 per share. The cost of any purchased shares can be deducted from the capital gain. If shares have been inherited since 1994, then the value at the date of inheritance can also be deducted.

Where shares are owned by a partnership, the gains can be shared between the partners, who each have an exemption of £12,000. For example a partnership of four individuals who do not make any other capital gains this tax year will only have tax to pay if they receive more than £48,000 of proceeds. If an individual's gain is greater than £12,000 the rate of tax will be either 10% or 20% depending on their other income.

The position is more complicated for limited companies as they do not receive any capital gains tax exemption, and are likely to pay 19% Corporation Tax on their capital gain.

## Migration to Universal Credit

**We have covered the ending of Tax Credits and implementation of Universal Credit in several articles in these pages in recent years. This has not gone smoothly and under the current timetable it will be almost five years before the final tax Credits claimants are transferred over.**

There are two ways of switching over from Tax credits to Universal Credit – natural migration and managed migration – with an important difference between the two.

Natural migration will usually be where a person has voluntarily applied for Universal Credit, or had a change of circumstances, eg moving from being a single claimant to a joint claim or vice versa.

Managed migration by contrast is under the control of the Department of Work and Pensions (DWP) who will dictate when a person is switched across. The present timetable is that DWP will carry out a pilot scheme of 10,000 claimants between July 2019 and July 2020. Remaining Tax Credits claims will then be transferred across between November 2020 and December 2023.

Under the managed migration process, claimants will still have to make an application to Universal Credit, although not everyone currently claiming Tax Credits will be eligible for Universal Credit.

Those who transfer across under managed migration can claim transitional protection, which means at the point of transfer they cannot be worse off in cash terms.



## Scottish Land Commission Report

**A report published by the Scottish Land Commission in March 2019 considered the issues associated with "large scale and concentrated land ownership" and made recommendations to Scottish Ministers.**
**Whilst the report concentrated on issues caused by large estates, problems were identified with land owned by individuals, charities and communities.**

The recommendations are all lacking in detail so it is difficult to assess if there will be any impact on working farmers:

It is suggested for significant land transfers, that a "public interest test" be introduced.

For land holdings over a certain size, a management plan will need to be published.
To introduce "in the immediate future" a programme of land rights and responsibilities good practice.

Investigating policy options to encourage a more diverse pattern of private land ownership.

The report also states an intention to explore whether a land value tax can be introduced on development land, and also to consider "wider tax and fiscal policy". This is clearly highly political with Capital Gains Tax and Inheritance Tax both under the control of Westminster rather than Holyrood.

The Commission is continuing to consult on its findings and are holding a series of events and public meetings, culminating in a Land reform Conference in October 2019. There is therefore still time to influence the final outcome here.

## Increased probate fees

**The cost of applying for a Grant of Probate in England when a family member dies is due to increase dramatically. The increase for some farming families could increase from £155 to as much as £6,000.**

These increases were due to be introduced on 1st April 2019, but at the time of writing in mid-April the legislation has not been enacted. At present fees are £215 for a personal application and £155 if made by a solicitor.

Under the new system, fees will be based on the value of the estate rather than a flat fee. The fees rise in stages from £250 for an estate worth between £50,001 and £300,000, to £6,000 for estates of more than £2 million. The change has been heavily criticised as the amount of work for the Probate Registry does not materially change according to the value of a person's estate. The only benefit is that under the new rules, an estate valued at £50,000 or less will not pay anything.

These changes may encourage more farmers to pass assets to the next generation during their lifetime, or to hold assets in joint names in order to reduce the probate fees. Neither of these courses of action should be entered into lightly, as there are numerous tax and non-tax issues to consider. In particular, there could be greater Capital Gains Tax liabilities if land is gifted during lifetime.

# Seeing the wood for the trees

**Forestry has become profitable again. Increased demand for wood and paper products has seen demand rise significantly over the last few years. What was once worth little, now has the potential to provide a good return.**

With £40 - £50 per tonne achievable for good quality Sitka Spruce and other types of conifer, 250 tonnes of good quality timber might yield upwards of £10,000. All of a sudden a typical 2 hectare shelter belt planted 30 years ago might have the ability to produce an income of £20,000, maybe more.

There is more good news in that income from selling standing timber is generally exempt from Income Tax. The exception here is if you are growing short rotation coppice such as willow or poplar on a 2-5 year cycle. Complications also arise if your business uses any of the harvested timber, eg to generate energy in a biomass boiler.

Whilst a detailed analysis and commentary on grant funding is beyond the scope of this article, money is available to help support qualifying schemes:

The Woodland Creation Grant for example is a 2 year Capital Grant Scheme that is worth up to £6,800 per hectare for areas of 3 hectares or more. There must be 20% of open space and there is a focus on increased biodiversity and native species.

The Woodland Creation Planning Grant applies for larger scale schemes. This can be worth up to £150 per hectare and the minimum area is 10 hectares.

A 10 year Woodland Maintenance Grant is also available that will provide up to £200 per hectare.

Currently, Basic Payment Scheme can be claimed on new Woodland.

For now at least the only certainty is uncertainty. Is there money tied up that could be released over the next few years' tax free to help fund other projects? Would new planting be worth considering in order to lay down some insurance for the next generation? The current favourable attitude of policy makers towards forestry means that it is worthy of consideration, especially so when assessing the impact of the proposed changes to farm support payments from 2021 onwards.

Finally a few words about tax and forestry:
As mentioned above, sales of standing timber is tax free provided it can be shown that you are managing the woodland commercially.

No tax relief is available on associated costs such as replanting or maintenance of the trees. VAT does need to be charged on the income and can be reclaimed on expenses.

If an area of woodland is sold, Capital Gains Tax is only paid on the underlying land, and not on the value of growing trees.

Inheritance Tax and woodlands is not straightforward. Agricultural Property Relief is not due unless the woodland is classed as a shelter belt or is short-rotation coppice. Business Property Relief can be due but care needs to be taken with the structure of the business to ensure that 100% relief rather than 50% is obtained.

Jonathan York
Accounting Director

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# Figured

In these uncertain times the UK Agricultural Industry is currently experiencing it has never been more important to forward plan in terms of cash flows and budgets and then to monitor these on a ongoing basis.

It is inevitable change will happen and being able to robustly plan and measure change is something which is very important.

To help our clients with this and to make it more efficient to produce accurate management information we have partnered with Figured which is a powerful farm management software product which allows all of the following:

- Budgeting and planning
- Production tracking
- Mutual Farm/Enterprise management
- Powerful reporting at a glance
- Simple, easy to use software
- Planning ahead with confidence
- Works hand in hand with Xero
- Figured is the only farm accounting software that allows real time collaboration
- Adding value to the MTD requirements by using the live data.

The Figured product has been designed for farmers and accountants by farmers allowing better focus and easier decisions to me made on farm.

We at Armstrong Watson Agri strongly believe that in times of such change we need to help our clients through this and by partnering with products like Figured it gives us the best tools to do so.

We are currently in the pilot phase with the product but it is our aim to provide each farming client with a simple budget report each year with their annual accounts at no extra cost, to aid and assist discussions about their future strategy and direction.

We then are certain farming businesses will see the value and benefit in planning ahead and the information which can be gained from using this software; this should encourage and then lead onto more robust forward panning.

It is our opinion that the best businesses look forward all the time and this has never been more critical. Our partnership with Figured helps us advance with all this.

Figured

Andrew Robinson
Head of Agriculture

# Keith's briefing

Keith Johnston
Agricultural Tax Director

## Is it a business?

In previous editions of this newsletter we have regularly covered Inheritance Tax (IHT) and in particular Holiday Cottages and whether they are liable to Inheritance Tax. In this article I will look at why farm diversifications in general can cause a problem when planning to minimise IHT.

The starting point is to note the differences between Agricultural Property Relief (APR) and Business Property Relief (BPR):

APR can be due even though the land is not farmed by the landowner. To obtain BPR the property owner
must be involved in the trading business.

100% APR can be due regardless of whether the asset is owned by the business or is held outside by an individual partner or shareholder. To obtain 100% BPR the land must be owned by the business.

APR is only due on the agricultural value of an asset which means that land or buildings with a potential non-agricultural use may not get APR on its full value.
BPR is denied where a business consists wholly or mainly of holding investments.

It is the final point that has caused much uncertainty and has been the subject of dispute with HMRC in recent years:

**Caravan Parks**
If a caravan park consists mainly of annual pitch fees, rather than from touring caravans or campers, then it could be considered an investment business. To obtain BPR it is necessary to show that a considerable range of other services are offered to visitors.

**Diversified farming businesses**
When a business is receiving income from a range of non-farming activities, APR will not be available on the full value of the farm. If it can be shown that the business is predominantly a trading business then the whole property can qualify for BPR. This has been the subject of several tax tribunals and court cases, and involves analysing a number of different factors – turnover, profit, asset value, and management time.

**Holiday cottages**
HMRC has successfully denied BPR on most holiday cottages. There was a recent case involving a business on the Scilly Isles where BPR was granted, but despite being described by the judge as providing an exceptional level of service, it only just qualified for BPR.

**Horse livery**
In another recent case, a horse livery business successfully claimed BPR as it was able to show that it provided a range of services over and above the provision of a stable and grazing. However, other livery businesses, particularly those offering DIY livery, will find it difficult to convince HMRC that they are providing sufficient services to qualify for BPR.

**Grassletting**
To be a farmer, the landowner must be seen to be carrying out husbandry on the land. If the grazier fertilises the land and sprays weeds, then it is the grazier not the landowner who is the farmer for tax purposes. Similarly barter arrangements where the grazier pays for the fertiliser in exchange for a lower grazing rent should also be discouraged as it could result in loss of IHT reliefs.

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# Trusts -

## a brief introduction and when you might use them

**In this article we will attempt to dispel some of the mystery surrounding trusts and explain how and when they might be used. A trust can be created during a person's lifetime, usually as part of their Inheritance Tax (IHT) planning, or on death via a person's will.**

**There are 3 people involved in a trust:**

**Settlor** - This is the person who creates the trust.

**Trustees** - These are the people who control the trust, normally by following the terms of the Trust Deed which sets out who can receive income and capital from the trust.

**Beneficiaries** - The people who receive income from the trust assets or can occupy trust property.

For IHT planning, if a person puts an asset into a trust more than seven years before their death and gives up the right to any income from it, then the asset is not chargeable to IHT.

Creating a trust on death is often used to ensure a surviving spouse has sufficient income for their lifetime and specifying who ultimately owns the asset.

A beneficiary can either have an absolute right to income or a discretionary right. A discretionary trust can be used where some of the beneficiaries are young, or there is a worry about their ability to manage money.

Our team of trust specialists can advise on all areas of setting up or operating a trust.

# Summer Shows

**We'd love you to join us for hospitality at our upcoming summer agricultual shows**


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|---|---|
| Beef Expo | 23 May |
| Cumberland Show | 15 June |
| Penrith Show | 20 July |
| Cockermouth Show | 3 August |
| Dumfries Show | 3 August |
| Westmorland County Show | 12 September |

# Serving farmers across the country for over 150 years

We hope you've enjoyed this edition of our newsletter for rural businesses. Please don't hesitate to get in touch with us if you have any questions about any of the issues covered in this newsletter, or if there are any subjects you'd like us to cover in future editions. This map shows just some of the main points of contact for our agriculture team.

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