Agri Matters

Winter 2018

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News -

FARMING IS OUR FIELD

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Accountants, Business & Financial Advisers

Welcome

Andrew Robinson
Head of Agriculture

Welcome to this edition of Agrimatters. Whilst I sit writing my editor's page it is fair to say that UK Agriculture is facing unprecedented uncertainty and change ahead. Whilst the Agriculture Bill is going through its second reading, and gives a modicum of insight into the future of farming and support policy, we are no further forward with what the outcome of Brexit and most importantly what the trade agreements will or won't be.

I personally think that the outcome of the trade deals is the single most important factor in how UK Agriculture will prosper. With regards to the Agriculture Bill I still don't understand how the production of high quality, sustainable and value for money food is not for the Public good?

We are very busy at present helping our clients prepare for Making Tax Digital and this is something everyone should be thinking about. There is no choice in this matter but there are positives - every farm business will have their records up to date on software at least once a quarter. The benefit of this is that good tax planning, budgeting and monitoring can be carried on using this info to stay ahead of the game.

We have a guest article from Joanne Metcalfe of YoungsRPS setting out the land agent's views of Brexit and the Agricultural Bill.

The use of pension funds as part of day-to-day planning has increased since the introduction of pension freedoms in 2015. We have an article which sets out some of the ways that these changes can help farming businesses.

We have mentioned the abolition of Tax Credits and introduction of Universal Credit on a regular basis on these pages in recent years. Full implementation has again been deferred but these changes will adversely affect many farming families and we explain the current position.

Rollover Relief for Capital Gains Tax should be one of the simpler pieces of tax legislation but there are several traps for the unwary to fall into. We therefore set out the issues to watch out for when selling and buying farming assets.

On our news page we cover a range of current topics – the recent announcement that Class 2 National Insurance is no longer to be scrapped, another tax tribunal case concerning furnished holiday letting, a few words about HMRC tax enquiries, and the increasing use of pre-nuptial agreements.

Our tax director, Keith Johnston, considers tax payable on selling development land, and warns that changes may be on the horizon which will enable local authorities to take a greater share of the increase in value when planning permission is granted.

And finally, whilst we are in times of unprecedented uncertainty, this will undoubtedly create opportunities as well as challenges. It is up to us all to work together to secure the best outcome so that we continue to be proud of being part of the UK Agricultural industry.

I hope winter is kind and short for you all, and helps those with low feed stocks.

Andrew Robinson.

Guest Article

The Agriculture Bill...
A land agent's perspective

Joanne Metcalfe - YoungsRPS

Michael Gove's long awaited Agriculture Bill was released on 12th September 2018 and sets out the Government's proposals for farming and land management policies following the UK's exit from the European Union. The Bill is a proposal for a new law and may be amended as it is debated in parliament, or changed by an incoming government after a general election, but it does provide us with an intended framework and direction for agricultural policy. The main points of the Bill are as follows:

Direct Payments - Basic Payment Scheme income has been guaranteed until 2021 - provided the current government remains in power. This will be followed by a seven year transition period when payments will gradually reduce to nil. During this period payments will be delinked from the requirement to farm the land and there may also be the opportunity to take annual payments as a one off capital lump sum.

Exceptional Market Conditions - Financial assistance will be made available to farmers following severe disturbance or threats in agricultural markets. This will include extreme weather conditions or outbreaks of disease. Other Matters - There is an intention to strengthen transparency in the food chain, provide support for investment in new technologies which boost productivity, and to ensure a fair playing field for agricultural markets by giving the government the ability to regulate contract terms with producers.

Environmental Land Management Systems (ELMS) - The Health and Harmony Consultation Paper introduced new Environmental Land Management System's (ELMS) to pay farmers and landowners for providing environmental benefits. From 2021 ELMs would offer multi annual agreements where payments are made in return for "public goods" such as improved air, water and soil quality, climate change mitigation, public access to the countryside and animal welfare.

It is clear that the government are willing to continue to provide funding to farmers but also that public perception of this funding is becoming increasingly important. The current support budget for UK agriculture is around £3.2bn and is set on a seven year cycle. It is unknown what budget will be available once the UK leaves the EU or how often this budget will be set. There will, undoubtedly, be more pressures on the budget with other sectors such as health and education all fighting for money from the same pot.

Taking all of this into account, our best advice for businesses is to start to prepare forward budgets taking into account likely diminishing direct subsidy income. This will allow consideration of ways in which productivity can be maintained going forward, with investment made now if required to strengthen businesses. Our team at YoungsRPS are on hand to help farmers and landowners with business planning or other specific concerns about the possible effect of changing agricultural policy.

Joanne Metcalfe – BSc (Hons) Real Estate, Reading University, MRICS, FAAV, RICS Registered Valuer, AMC Agent.

Joanne is a qualified surveyor in our Sedgefield office undertaking a wide range of general professional work. Joanne was born and brought up on the family farm near Darlington where she still helps out on evenings and weekends.

YoungsRPS is a leading firm of chartered surveyors and property consultants in the North of England, specialising in four key business disciplines - Land Agency, Planning and Development, Estate Agency and Commercial.

Joanne Metcalfe
Rural Chartered Surveyor

News

Changes to Class 2 National Insurance

We have written recently in these pages about the proposed changes to Class 2 National Insurance Contributions (NIC's), the government having previously announced in the 2015 Budget that these were to be abolished.

Class 2 NIC's are payable as flat-rate weekly contributions (£2.95 per week in 2018/19) if a person's profits for that tax year equal or exceed the Small Profits Threshold (currently £6,205). They are collected annually as part of the Self Assessment system.

Abolition was due to take place on 6 April 2019 at which point Class 4 NIC's were expected to rise as a consequence. Following an announcement in early September, the government has now confirmed that Class 2 NIC's will not be abolished during the lifetime of the current parliament, citing their main concern as being the impact the change would have on self-employed people with low profits.

Once Class 2 was abolished, it would still be possible to pay NICs voluntarily in order to maintain your NIC record, (and therefore entitlement to certain benefits, principally state pension) but this would have to be at the higher Class 3 rate (currently £14.65 per week). For completeness, Class 4 NIC's are payable at a rate of 9% on profits in excess of £8,424 but these do not entitle the payer to any state benefits.

So, in conclusion, it's as you were and Class 2 NIC's will, for now at least, continue to be payable annually and administered through your tax return as part of the Self Assessment System. We would always recommend obtaining a state pension forecast to ensure that you are on track to receive a full state pension.

Furnished Holiday Lets and Inheritance Tax Relief

We have covered the issue of Furnished Holiday Letting (FHL) and Inheritance Tax in these pages on several occasions. HMRC regularly argue that FHL is an investment activity and does not qualify for Business Property Relief (BPR).

Until recently HMRC had a 100% record in denying BPR in tax tribunal cases concerning FHL. At long last, we now have a victory for a taxpayer.

The deceased, Mrs Graham, ran the business from her home in the Isles of Scilly. The property was originally a farmhouse which had subsequently been renovated and operated firstly as a B&B, then a hotel and finally as holiday Self Catering Accommodation.

The property comprised four self-contained flats or cottages each with its own kitchen & dining/living area. There was a croquet lawn at the back of the house; prize winning gardens with barbeque area and a swimming pool with sauna. There was a games room and laundry at one end of the pool. Extensive services were provided, particularly by Mrs Graham's daughter, which were described by the judge as "exceptional".

The tribunal determined that overall, because of the extensive level of service and personal involvement by Mrs Graham, the activity here was more akin to the operation of a trading business rather than wholly or mainly collecting rents and therefore concluded that Business Property Relief was due.

So, a glimmer of hope? Crucial though is the extensive level of service and personal involvement. Simply letting out a holiday property through an agent is still very unlikely to qualify.

This however is not the end of the story. At the time of writing HMRC has just announced that they are appealing the decision.

Pre Nuptial Agreements

What are they and when might such an agreement be appropriate?

A Pre Nuptial Agreement or "Pre Nup" is an agreement between you and your future spouse that allows you to agree what will happen to your financial assets in the event that your relationship breaks down.

Essentially, each party will need to disclose of all their assets and determine who should receive what in the event of a Divorce. Once seen as the preserve of the super wealthy, with the rise in land and property values Pre Nups are becoming increasingly important and can be particularly relevant in respect of family farming businesses. Consider for instance the position where you have as yet unmarried adult children farming in partnership with parents. Should your children marry, in the event of a subsequent breakdown, the family farm might be at risk. A Pre Nup could help protect your position.

Although not legally binding, they will be taken into consideration when looking at financial settlements on divorce. The Courts have shown increasing willingness to enforce such agreements where it can be shown that each party had taken independent legal advice. Additionally, any provision must be seen to be fair and reasonable and neither party was put under undue pressure to consent to the agreement.

In the case of Radmacher v Granatino in The Supreme Court for example, it was held that "the court should give effect to a nuptial agreement that is freely entered into by each party with a full appreciation of its implications, unless in the circumstances prevailing it would not be fair to hold the parties to their agreement."

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HMRC Tax Enquiries

We are often asked how often HMRC enquire into farm accounts and tax returns, and how long it takes to resolve these issues? The answer is that we still receive a large number of queries but these are different in nature than in the past.

In years gone by tax inspectors were based in local tax offices and exclusively dealt with businesses in that area. These local tax offices have now closed and tax inspectors now deal with cases across the country. This means that tax inspectors have become more specialised, dealing with a particular type of business or technical area.

A second change is HMRC's use of technology. A key part of this is their computer system known as Connect which ties up information from a number of different sources such as the Land Registry, Companies House, Department of Work and Pension, Passport Office, Banks (both on and Offshore) and other online information, to name just some of the sources. It then seeks to check an individual's tax return by looking for instances where the information held on its system is not consistent with the tax return. This can then lead to an enquiry into the tax return to resolve the difference.

We are also seeing HMRC exchanging more data with overseas tax authorities. A recent campaign has seen UK taxpayers who own overseas property being asked to "consider" if they have undeclared foreign income.

To give you peace of mind, Armstrong Watson offers a tax enquiry fee protection service, which provides you with cover for any professional fees incurred should HMRC raise an enquiry into your affairs.

Rollover Relief

Beware some pitfalls

Rollover Relief sounds straightforward enough. You sell an asset, make a capital gain. Instead of paying tax, elect to defer it by purchasing a new asset. However, it's not always that simple.

Has the old asset been used for business purposes?

If part of the property sold has always been rented out, e.g. a cottage let under a shorthold tenancy, that part of the gain does not qualify for rollover relief. Tax will be payable at up to 28% on residential properties and 20% on other assets.

Has the old asset always been used for business purposes?

There is a restriction on relief if part of the property sold was only used for business purposes for part of the period of ownership. An example would be if a block of land was rented out under an FBT for a five year period.

Does the entire new asset qualify?

To rollover the whole capital gain, all of the proceeds have to be reinvested in qualifying assets. Where only part of the proceeds is reinvested, the taxable capital gain is the amount not reinvested. For example; a farmer sells an asset for £1 million and makes a gain of £400,000 and only reinvests £900,000. His chargeable capital gain is the £100,000 not reinvested.

Has new asset been purchased by the correct person?

Capital gains are charged on individuals not businesses. Replacement assets must be purchased by exactly the same person that sold the old asset. If the old asset is sold by husband and the new one bought jointly by husband and wife, only half of the proceeds have been rolled over and a large tax bill remains.

Has new asset been used for business purposes immediately?

The new asset must be "immediately taken into use for the purpose of the business". If part of the new farm is subject to a short-term tenancy when bought, this part does not qualify. If part of the asset needs repairing or renovating, it can still qualify as long as the work is done as soon as practicably possible.

Has new asset been purchased within the time limits?

The new asset must be purchased within specified time limits – no more than twelve months before the old asset was sold, no longer than three years after. Time limits run from the date of exchange of contracts, not completion. You can request that HMRC extend these limits if transactions are delayed by circumstances outside your control or if you are unable to find suitable assets to purchase. Provisional claims are possible if you have not purchased the new asset at the time the tax is due for payment. Interest will be payable if you change your mind and do not purchase new assets.

Watch out for grazing licences

You must be taking commercial risk rather than just renting to a third party. Essential is the landowner being involved in the husbandry of the land – applying fertiliser and controlling weeds – and not receiving a fixed income. HMRC will disallow the claim and charge the tax in full otherwise.

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Universal Credit

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We have written previously about the abolition of Tax Credits and its replacement with Universal Credit. If everything had gone according to plan, the transition would already be complete, but implementation has been far from smooth. In this article we will explain that whilst tax credits are due to continue for a while yet, many self employed claimants will either not be eligible or will receive a greatly reduced amount.

The office of Budget Responsibility recently stated that there are 3.6 million people currently claiming tax credits with an average claim of £7,170 per year, making a total cost of £25.8 billion. Back in 2015 a government minister stated that "the welfare system is not there to prop up unproductive or loss-making businesses." We have seen over the last couple of years an increasing number of challenges by the Tax Credit Office asking if clients' are genuinely self employed. These are certain to continue, and perhaps increase, under Universal Credit.

The key factors of the new system are as follows:

- Income for Universal Credit is not based on taxable profits, but "actual receipts minus permitted expenses".
- Information needs to be submitted to HMRC on a monthly basis.
- Apart from the first year of claim, all claimants will be deemed to have received income equal to the national minimum wage each month – known as the Minimum Income Floor.
- Self employed claimants with fluctuating incomes are disadvantaged. This will clearly be the case for many farmers where livestock sales and subsidy receipts are concentrated in a few months.
- Universal Credit is means-tested and anyone with more than £16,000 of capital is excluded from the system.
- Self employed claimants have to show they are in gainful self employment, which will be determined by DWP work coaches and will require attendance at meetings in their local job centre.
- Income and expenses are recognised on a receipts/payment basis, rather than when they are earned or incurred.
- No account is taken of stock. Thus income can be high in months when stock is sold and low in months when stock is purchased.
- Unlike normal accounts, a deduction is allowed for income tax, national insurance and pension contributions.
- Expenditure on machinery and equipment (but not cars) can be deducted but this is only for amounts actually paid, not for the part put on hire purchase.
- Interest on loans taken out for business use can be deducted, but only up to a maximum amount of £41 per month.
- Car running expenses must be calculated on a mileage basis. This will require a record of business journeys to be kept.
- In the case of a partnership, the amount of receipts and payments to be taken into account is the "amount attributable to their share in the partnership". This is simple where a partner receives a fixed percentage of profit, but less clear where profit allocation is not decided until the end of the year.

As a result of the increased complexity there may well be some current tax credit claimants who will decide that claiming Universal Credit is not worthwhile.

Make the most of your pension funds

Before 2015 the perception of pension schemes for farmers was that they were inflexible and didn't offer great value for money. Reason being that at some time before the age of 75 a person's pension pot had to be used to purchase an annuity.

The reforms in 2015 – known as pension freedoms – have made pensions much more attractive.

It's now possible from age 55 to draw any amount from your pension. However, firstly most of the income is taxable so taking a large withdrawal in a single tax year can result in a large income tax bill – and secondly if you have drawn most of the fund before you are 60, what will you use to live on in future years? A person can still purchase an annuity, but a consequence of low interest rates is that annuity rates are quite low.

Some of the benefits of these freedoms can be illustrated as follows:

Example 1: A 57 year old farmer has £200,000 in a pension fund. He requires funds to pay for a new building. One way of achieving this is to draw £50,000 from his pension by way of the 25% tax-free lump sum. No tax is payable on the £50,000 and the remaining £150,000 can be left within the pension until he needs to draw a pension income.

Example 2: A 50 year old farmer has £100,000 in a pension fund and is similarly in need of capital for their business. A possible solution would be to sell a block of land for £50,000 to the pension fund. There may be a small capital gains tax liability, and the business will have to pay rent to the pension fund, but again this could be an effective way of obtaining the funds for the business.

Example 3: A 53 year old farmer has £200,000 in a pension fund and has got the opportunity to purchase an adjoining block of land for £1 million. A distinct part of the land could be purchased in the name of the pension scheme. The land purchased by the pension could be at least £200,000. This amount could be increased if the farmer is able to make further contributions into the fund, which will be boosted by tax relief, and it is also possible to borrow money in the pension scheme to increase the amount further.

Some key actions to undertake with regard to pension funds:

- Don't forget about the State Pension – make sure you have got sufficient qualifying years to receive a full state pension.
- Get to know how much tax free lump sum you can draw from your pension.
- Confirm if your pension fund can be left Inheritance Tax free to your family.
- Update your 'expression of wishes' form.
- Ensure you keep a record of historic and current pension providers.
- Be aware of how the treatment of your pension plans would be treated in the event of your passing - older policies pay out as cash while more up to date policies provide wider options.
- Ensure that the firm and adviser you are dealing with are listed on the FCA Register.

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Keith's briefing

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Keith Johnston
Agricultural Tax Director

In this article I will be looking at the different ways that Government – both national and local – can collect tax and in particular consider the sale of development land and diversification projects. I will show that it is necessary to look beyond the traditional sources of government revenue – Capital Gains Tax (CGT), VAT, Stamp Duty Land Tax and Corporation Tax to name a few – to understand the full position.

The headline rate of CGT is 20%, although this increases to 28% where residential properties are sold. Interestingly, the sale of land with planning permission for residential property to be built on it pays the lower rate of CGT. It is also possible with careful planning to pay an even lower rate of 10% if the disposal qualifies for Entrepreneurs' Relief. This compares favourably with historic rates of 30% or even 40% when CGT was paid at the same rate as income tax.

Over the years there have been several attempts to charge additional tax on the sale of development land. For example, back in the 1970's, the standard rate of CGT was 30% but there was a 60% charge on development land gains. There was also an attempt just over 10 years ago to introduce a Planning Gain Supplement. This was to have charged a levy on the uplift in value when planning permission was granted, but was shelved before it was implemented. This was a relief to farmers planning diversification projects as it would have been charged on barn conversions and other on-farm projects where no cash was being generated from a disposal.

Turning to local government, there are two ways that they can charge money on development projects:

- Section 106 Agreements – these are conditions of planning permission, e.g. for a housing developer to pay for the construction of a new road or school. These are not paid by the landowner, but the developer will obviously take them into account and pay less for the land as a result.
- Community Infrastructure Levy (CIL) was introduced in 2010 and is a flat rate charge (e.g. £50 per square foot of floor space) charged on the granting of planning permission. The funds raised can be used for any infrastructure spending within the local authority area. Not all local authorities have introduced a CIL scheme, and the rates charged vary greatly. CIL is levied on planning permissions granted so can be paid on diversification projects as well as housing developments.

A recent report by a government committee – the Housing, Communities and Local Government Committee – looked at the question of how the increase in land value from planning permission should be shared between the landowner, central government and local government. The report quite bluntly stated that "our view is that central and local government should claim a greater proportion of land value increases." This is not government policy and there are no specific proposals on the table at present. At a time when local councils in particular are short of funds it seems inevitable that measures will be introduced in the near future.

Keith Johnston

People News

Susannah French has joined the Agriculture team in our Penrith Office as an accounting senior manager. Susannah relocated to Cumbria from the New Forest in 2016, where she worked at Saffery Champness in their Bournemouth office in the Landed Estates and Rural businesses sector, plus also maintaining several corporate audits. Previous to this, Susannah worked for Ernst & Young in Southampton.

Susannah will be responsible for looking after a large proportion of Steve Pinguey's agricultural clients' affairs after his retirement at the end of March 2019. She will be aiming to build a good working relationship with theses clients, so that she can properly understand their needs, and bring her knowledge and experience to the table to assist them. She will also be growing her own portfolio of agricultural clients, both landed estates and farming, in north and central Cumbria.

Susannah is a keen horse woman and has five Arabian horses. She competes in endurance riding with two of them at a national level, with the aim of doing her first international level ride in Scotland in the 2019 season. When not training or competing her endurance horses, Susannah can be found up on the Lakeland fells with her dog.

Susannah French
Accounting Senior Manager

Making Tax Digital

Fail to prepare, prepare to fail

When it comes to increasing productivity, enhancing biodiversity and getting a fair return for what they produce, farmers look to embrace technology. However, the same cannot always be said when it comes to their accounting records with many still using manual cashbooks to record the transactions of the farm.

With the introduction of Making Tax Digital (MTD) for VAT from April 2019, manual records are simply not an option for those farms over the VAT registration threshold of £85,000.

Although there will be pain involved in transitioning to a cloud-based accounting system, the huge benefit will be that farmers will be able to keep an eye on their business far more easily, thereby saving time.

We would urge those farmers who will be affected by the above change, who are not yet ready, to start to put plans in place to ensure compliance. The options open to farmers are:-

Invest in accounts software from a digitally compatible provider such as Xero;

Convert the manual records to a spreadsheet. This spreadsheet needs to be able to calculate the VAT repayment / liability and be able to be uploaded to HMRC via an Application Programme Interface. This is essentially a link between your computer and HMRC.

Ask your professional advisor to prepare and submit the VAT returns on your behalf.

In conclusion, digitalisation for VAT is coming and the sooner you can be prepared, the easier the transition will be. Please contact us to discuss the best option for your business.

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Summer Shows

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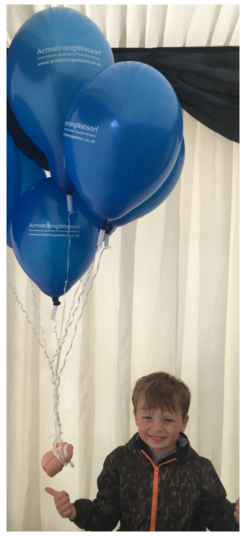
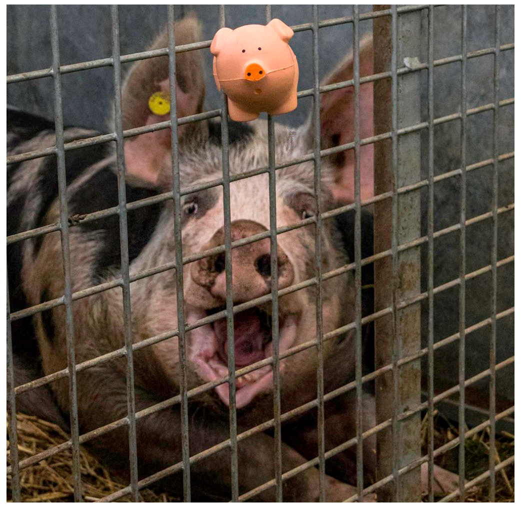
AGRICULTURAL SHOWS 2018





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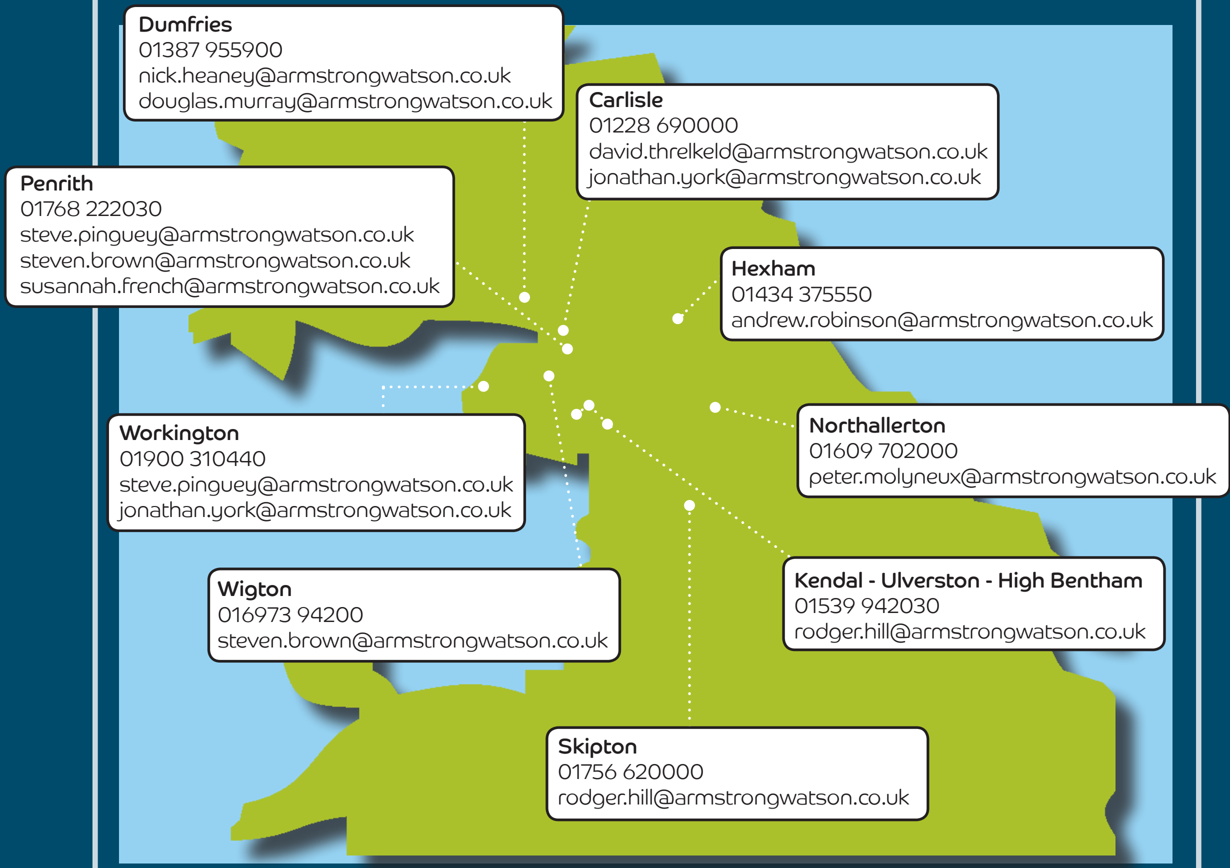

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We hope you've enjoyed this edition of our newsletter for rural businesses. Please don't hesitate to get in touch with us if you have any questions about any of the issues covered in this newsletter, or if there are any subjects you'd like us to cover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

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