



AAT

Tax issues for farmers

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Is it farming?

The question is important

- The best tax breaks are for farmers farming their land!
- Good IHT and CGT breaks!
- So you need to know if you are “farming”
- Grazing horses?
- One cow, a pig and some hens?
- Huge country des-res in 2 acres?

Is it farming?

- What about:
- Contract farming?
- Share farming?
- Fish farming?
- Market gardening?
- Garden centres?

- Farm Business Tenancies (FBTs)?

A quote from ITA 2007, S996

- ‘In this Act “farming” means the occupation of land wholly or mainly for the purposes of **husbandry**, but does not include market gardening (the occupation of land as a garden or nursery for the purposes of growing produce for sale)
- Husbandry includes:
 - Hop growing;
And the breeding and rearing of horses and the grazing of horses in connection with those activities;
Short rotation coppice.
- All of the above words dripping with meaning – see BIM55051 - Farming in tax law: definition of farming

BIM55105 - Farming in tax law: Intensive livestock enterprise/fish farms

- To fall within the statutory definition of `farming', an activity must depend at least to some extent on the produce of the land occupied by the person carrying on the activity;
- Thus, an intensive enterprise, in which livestock are kept entirely separate from the land (for example entirely indoors or, in the case of fish, in tanks), and fed entirely on purchased feed, is not farming;
- (See *Lean & Dickson v Ball* [1925] 10TC341, *Jones v Nuttall* [1926] 10TC346, and *Peter Reid v CIR* [1947] 28TC451).

BIM55105 - Farming in tax law: Intensive livestock enterprise/fish farms

However, for the purposes of the averaging provisions of ITTOIA/Chapter 16, the definition of 'farming' is extended by to include the intensive rearing of livestock or fish on a commercial basis for the production of food for human consumption;

What about receipt of the Single Payment?

- The Single Payment System (SPS) is the main agricultural subsidy scheme in the EU;
- To be eligible for SPS payments, you must:
 - Be a farmer, as defined by the EU;
 - Have eligible land at your disposal on the prescribed date in May of the scheme year - this land must be eligible for SPS for the entire calendar year;
 - Hold payment entitlements;
 - Meet the minimum claim size (1 ha).

Are you a farmer?

- For **SP** purposes this is defined in Regulation (EC) No 1782/03 as someone who exercises an agricultural activity and this covers a wide range of farming activities (including growers of fruit and vegetables);
- Also keeping the land in good agricultural and environmental condition (GAEC);
- **So, definitions for tax and SP are different.**

Non-farmers can still receive the SPS

- Receipt of SP is not evidence that a person is carrying on a trade of farming for tax purposes;
- On the other hand there may be cases where the absence of a SP income will be unhelpful to a landowner who asserts they were farming;
- The difference between the way entitlement to SP is defined and the way farming is defined for tax purposes needs to be appreciated.

Non-farmers can still receive the SPS

- For example, land that is used for grazing horses or ponies kept for the leisure purposes of the SP recipient is eligible for SP provided all the other conditions are satisfied;
- If the occupier keeps the land in GAEC then SP may be received. But that does not mean a trade is being carried on;
- In these cases the charge to tax will arise under the miscellaneous income provisions of ITTOIA or CTA 2009 for companies.

Buying, selling and leasing of quotas

- Capital in nature, so a balance sheet rather than a P&L item;
- Capital tax treatment;
- If leased, leasing costs allowable for the lessee; and
- Normal trading receipt for the lessor;
- Milk quota supposed to be going from 2015.

Incidentally.....

- SP payments for traditional farmers are taxable in the normal way – IT or CT;
- Receipt of SP without production - GAEC – miscellaneous income;
- Receipt of SP for non-farmers – miscellaneous income.

So, the conclusion is.....

- You broadly need to be farming as defined, to get the capital tax reliefs (especially APR);
- But there are the odd wrinkles – as we will see.

Coping with the herd basis

The herd basis - basics

- As a normal rule, farm animals are dealt with as trading stock
- However some farm animals - those which are kept by farmers not primarily for resale but for the sake of the products (eg: milk or eggs) or offspring (eg: lambs or piglets) which they produce - are in many ways more like capital assets of the farmer's business;
- Tax law recognises this by giving farmers the option of dealing with such 'production animals' under the herd basis.

The herd basis - basics

- The herd basis provides a set of rules whereby a herd or flock of production animals is excluded from trading stock and treated like a capital asset;
- From the farmer's point of view, the main benefits are likely to be:
- The cost of maintaining the herd can be charged against tax, and
- Any profit on its eventual disposal will be tax-free (because there was no tax allowance under the original purchase costs).

The herd basis - basics

- A farmer must elect for the herd basis; otherwise the animals are treated as trading stock;
- The election, which is irrevocable, must specify the class of animals concerned;
- Normally it has to be made soon after the farmer first starts keeping animals of that class (the 12 month rule) and then the herd basis applies to those animals from the outset.
- (see BIM55595 - BIM55605).

Basic tax rules

- The initial cost of the herd is not an allowable deduction, nor is the cost of any subsequent increase in herd size;
- The net cost of replacing animals in the herd is an allowable deduction;
- Where the odd animal, or just a few animals, are sold from the herd and not replaced, the resulting profit or loss is taken into account in arriving at the farming profits.
- Where the whole herd, or a substantial part of the herd, is sold and not replaced, the resulting profit or loss is not taken into account.

The herd basis - items for consideration

- The greater the difference between the cost of animals in the herd and their ultimate market value, the greater the advantage of the herd basis;
- The difference will be greatest for pedigree animals.
- There will usually be a useful difference in the case of a home-bred, good-quality herd;

The herd basis - items for consideration

- The larger the herd, the more important the question of the election may be.
- Also need to consider age of farmer, retirement, or giving up say, dairy farming within the foreseeable future (possibility of tax-free receipts);
- In a period of inflation, the herd basis is additionally valuable in keeping unrealised profit out of the tax computation.

The herd basis - items for consideration

- On the herd basis, more detailed records need to be kept, and HMRC will tend to become involved in livestock numbers and values;
- The herd basis offers potential for tax-free profits, but carries risks;
- For example, a farmer forced to retire because of a slump in the livestock market might find losses in this department unrelieved against other farming profits.

Compulsory slaughter

- Compensation for compulsory slaughter is normally treated as sale proceeds whether or not the animal concerned is part of a production herd accounted for on the herd basis;
- Where the animals slaughtered are not on the herd basis and could not be (even with the fresh opportunity to elect for herd basis following compulsory slaughter of more than 20% of a herd), you can use ESC B11 to remove the profit arising from the year of slaughter and bring it in equal instalments over the next three years.

Capital Allowances

Normal rules apply.....

- So P&M allowances on P&M!
- But not on fixed structures; or
- Premises/setting;
- New R&C Brief: 32/12 – good on greenhouses/polytunnels;
- Centres on polytunnels:

Various uses of polytunnels.....

- Growing fruit;
- Raspberries (OK) v blackberries (not OK);
- Depends on how grown and how long before polytunnel is moved;
- Polytunnels can also be used to shelter livestock and store machinery – much more likely to be setting/fixed structure.

CAA 2001

- As well as disallowing CAs on “fixed structures”, CAA2001 also disallows certain structures such as:
- Dams and reservoirs;
- So a farmer building a reservoir as a water store for his farm will not be able to have P&M allowances on it!

Using the AIA

- Normal rules apply to farming;
- Good for items like wind turbines – that don't qualify for the ECA.

VAT issues

Basic VAT issues for farmers

- If VAT registered:
- Zero-rating for most basic farm products;
- Standard rated for most other activities: eg:
 - Camping;
 - Shooting;
 - Holiday accommodation;
- So, need to be careful with diversification activities;
- Compliance issues as well as recovery to consider.

If not VAT registered...

- Could use the Flat Rate Farmers' Scheme (FRF);
- No VAT recovery, but add a flat rate of 4% on invoices, (only) to VAT registered customers;
- Keep this – taxed to direct tax (IT or CT), but not VAT.
- Used as a VAT planning tools for small garden centres that grow a lot of their own products.

Passing the farm on – making the most of CGT and IHT reliefs

CGT reliefs

- Gift relief under S165, TCGA 1992;
- Holdover relief under S260, 1992;
- Entrepreneurs' relief.

S165, TCGA 1992

- Classic gifts relief provisions;
- Or sale at an undervalue;
- But only for business assets – not for investment assets;
- Allows base costs to be passed on to the recipient of the gift.
- Both parties need to claim.

S260, TCGA 1992

- Sometimes used when the asset being passed is not a business asset;
- Needs an immediate charge to IHT;
- Uses a discretionary trust.

Entrepreneurs' Relief (ER)

- 10% rate for CGT if the conditions are met:
- “Material disposal” - ie NOT piecemeal disposal of assets;
- Also “associated disposals”;
- Normally property.

Examples- a material disposal?

- Farmer sells 50 acres of land for housing but keeps 800 acres
- Unlikely to be a disposal for ER – see *McGregor v Adcock* (Retirement Relief Case)
- Would it be different if 50 acres was used for grazing and farmer ceases his livestock operation?
- Would it be different if at the time of selling the 50 acres of land he transferred the remaining 800 acres to a limited company?

IHT reliefs - APR and BPR

- Two important reliefs;
- Separate, but often come together in farming;
- APR is generally considered first – **only applies to the agricultural value;**
- Often the market value is well above the agricultural value;
- BPR may be available to top-up APR

APR

- A valuable and important relief for farmers;
- Virtually no other IHT relief for residences, so highly prized;
- Have I got a farmhouse?
- Or is it merely a “des-res” in 2 acres in the countryside?

APR –what qualifies?

- For agricultural property to qualify for APR, it must be in the UK, the Channel Islands, the Isle of Man or the European Economic Area, and it must be part of a working farm;
- You must have also owned it for two years;
- If you have let the property out you must have owned it for seven years before your death.

What rate is the relief?

- Normally 100%;
- But, it is 50% if the land is let on an “old” (pre September 1995) tenancy;

APR –what qualifies?

- Agricultural land or pasture;
- Farmhouses, cottages or buildings that are used for agricultural purposes and are proportionate in size to the nature and size of the farming activity
- Woodland;
- Buildings used for intensive rearing of livestock or fish;

APR –what qualifies?

- Growing crops transferred with the land;
- Stud farms that are breeding and rearing horses, and the land that the horses graze on;
- Short-rotation coppice - trees that are planted and harvested at least every ten years;

APR –what qualifies?

- Land that is actively not being farmed to help preserve the countryside and habitat for wild animals and birds under the Habitat Scheme;
- The value of land where the value includes the benefit of a milk quota;
- Some agricultural shares and securities.

So, what doesn't qualify?

- The following items also don't qualify for Agricultural Relief:
- Farm equipment and machinery such as tractors;
- Derelict buildings;
- Harvested crops;
- Livestock.

So, what about BPR?

- Generally used as a top-up for APR;
- It is designed for “business property”
- Like APR, it has a 2 year ownership rule;

What qualifies for BPR?

- A business or an interest in a business;
- Unlisted shares in trading companies;
- A holding of shares or securities that you own which give you control of a company, that are fully listed on a recognised stock exchange
- Land, buildings, plant or machinery you own, used wholly or mainly in the business.

RTI and casual labour

Latest HMRC guidance

- **Employed for a day or less:**
- Paid at the end of the day;
- No contract for further employment;
- No tax deducted, but need full details (DOB, NINO etc);
- Only report under RTI if you are already reporting (ie one or more employees/directors above LEL (ie normal rules);
- If none above LEL, then no reporting required.

Latest HMRC guidance

- **More than one day, but less than two weeks:**
- The same as the one day rules;
- **More than two weeks:**
- Usual PAYE reporting.
- <http://www.hmrc.gov.uk/payerti/employee-starting/special-situations/temps/harvest-casuals.htm>

The farmhouse – some tax angles

The dual role of the farmhouse

- A farmhouse normally fulfils a dual role being primarily the private residence of the farmer and his or her family and secondarily the centre of business operations on the farm.
- Only the proportion of the expenses such as heating and lighting, repairs, maintenance and insurance and, in the case of a tenant farmer, rent ,which is attributable to the business use of a farmhouse should be allowed as a deduction in computing farming profits.
- **(See S34 ITTOIA and BIM55250)**

VAT and farmhouse repairs

- Principle of apportionment applies (business v private);
- Tribunals have consistently rejected the area measurement approach to apportionment;
- Instead they have applied a more subjective test, assessing the “dominant purpose” for why the expenditure was incurred.

VAT and farmhouse repairs

- In the light of these decisions and in cases where:
 - The building is a typical working farmhouse;
 - The business is a full time farming activity; and
 - The work done is in the nature of repair and maintenance of the farmhouse, then:
- The business should treat 70% of the VAT incurred on the work done as input tax.

VAT and farmhouse repairs

- In all other cases, such as where:
- Farming is only a part-time activity and the farmhouse is primarily the family home; or
- The work done is an extension or alteration of the farmhouse,
- Then HMRC will think about each case on its merits;
- Unlikely to be more than 40% business use (per HMRC policy).

The farmhouse and PPR

- PPR available for residences;
- Farmhouses typically have dual use – private and business;
- The issue is whether parts of the farmhouse are exclusively business use as opposed to dual use;
- If parts have exclusive business use, then apportionment of the gain is required.

The farmhouse and PPR

- Whether any part of a farmhouse is used exclusively for business purposes is a question of fact;
- Normally parts have a dual purpose –principally the kitchen;
- So each of these rooms should be treated as part of the residence regardless of the fact that the farmer receives an allowance for his or her business use of the premises in the computation of the trading profits.
- If there is exclusive use, for example, of an office or dairy, then an apportionment is necessary.