AUDIT • TAX • ADVISORY

Agriculture & Rural Business **Newsletter**

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April 2021 Newsletter

Welcome to our April edition of Agriculture & Rural Business Newsletter

With lambs in the fields, the yellow of the OSR beginning to show and the longer, lighter evenings, Spring has certainly arrived. As lockdown measures start to ease there is still a way to go but at least there is a light at the end of the tunnel – and for those with campsites and holiday accommodation, and the uncertainty of holidaying abroad, it looks like “staycations” will be the norm for 2021.

In this edition we consider the recent Budget and the Tax Day and ask what’s in it for agriculture? We also review the preliminary details released regarding ELMS pilot schemes plus discuss a potentially unwelcome tax implication COVID may have brought for Furnished Holiday Lets. There is information relating to the changes brought in by DEFRA for selling firewood, an article on whether or not to claim a Super Capital Allowance and all you ever needed to know about Compulsory Purchase Orders.

So - Something for everyone!

MHA Agricultural Team

Budget 2021

what's in it for agriculture?

Rishi Sunak's second Budget, and the first one to reflect the full impact of the pandemic was described by one journalist as "spend big today, tax big tomorrow".

At first sight he has largely ignored the copious advice (including that from the Treasury Committee on taxation published earlier in the week), and simply offered a range of measures to limit the damage caused by the pandemic, whilst not materially increasing the tax burden. Indeed, the immediate tax increases will not even cover the annual interest which the government will be paying on the costs incurred over the last twelve months.

Whilst most of the new initiatives will benefit the high street rather the the agricultural sector, some will be of wider value. Those whose diversifications take them into tourism and leisure will welcome the business rate and VAT breaks and Corporate entities will particularly like the enhanced capital allowances which will give 130% tax reliefs. Sadly, this will not help the majority of family farms, which tend to be sole traders or partnerships, but for those who do trade as limited companies, there are real opportunities to undertake major capital investments over the next two years in a very tax effective way. They just need to be aware that where they are buying machinery which may be traded in later, the tax relief will come at 130% in a 19% corporation tax regime, but 130% of the trade-in may fall into a 25% tax charge.

Unlike the 130% relief, both corporate and non-corporate businesses will be able to utilise the three year carry back of loss relief, even where the losses have been created by capital allowance claims. Taken in conjunction with the earlier announcement that the Annual Investment Allowance would remain at £1m until December 2021, this gives a real window of opportunity to recover some of the tax which may have been paid over the last few years, rather than simply carrying losses forward to be used in the future.

However, there may be a sting in the tail. It was announced last month that in addition to the budget, there will shortly be a "Tax Day". Accordingto HMRC, this will…

allow for more transparency and scrutiny, documents and consultations that would traditionally be published at a Budget will be published on 23 March" although "None of the announcements will require legislation in the next Finance Bill or have an impact on the Government's finances."

Given the state of the country's long term finances, money for debt repayment will eventually have to be found somewhere, even if not this year. There must be some concern that we may see proposals in March based on some of the suggestions for tax reform which have been circulating.

Tax Day 2021

the shape of things to come?

In the past, annual Budgets have included both details of proposed legislative changes for the short term, normally covering 2-3 years, and outlined policies for discussion prior to implementation in the longer term.

That mould was broken in 2021. The recent Budget only included the shorter term plans, with discussion drafts being carried forward to a "Tax Day" some 13 days later. These new initiatives, which will not take place until the next Parliament, are fundamental and will affect almost all taxpayers.

The key changes are set out within three documents. A 16 page statement on "Tax Policies and Consultations" firstly outlines the intention to modernise tax administration by a combination of investing within HMRC through:

- Making Tax Digital (MTD) for taxpayers
- further digitisation for HMRC
- raising the standard of the tax advice market.

The second chapter of the statement looks at tackling non-compliance by, inter alia, clamping down on avoidance - although this rather looks like inaccurate terminology and confuses the terms "avoidance" and "evasion". Finally, there are 23 relatively minor policy announcements covering matters as diverse as aviation tax, business rates, the council tax liabilities of second homes and a review of landfill tax. Buried within this section is an announcement that there are now no plans to reform the tax treatment of trusts.

The devil, however, is in the detail of two further papers referenced within the documents as "calls for evidence". The first of these (running to some 38 pages) looks at establishing a framework for a 21st century tax system, and covers reforms to the administration framework (much of which is piecemeal and based on legislation some 50 years old).

Among many other issues it looks at pre population of tax returns from external data, and the possibility of effectively making all businesses produce accounts on a fiscal year basis.

The second major consultation is entitled "timely payment". Notwithstanding that HMRC has long denied that MTD was intended to accelerate payment of tax by the self-employed, this paper considers how taxpayers would find it so much easier to pay their tax liabilities regularly as their income arises. There is, of course, already a mechanism to do this under the "Budget Payment Plan" but HMRC concede that "uptake is low", and attribute this to the fact that it "is not easy to find, set up or manage" (although Google will drill down to it with a single click!).
This paper identifies some 14 reasons why taxpayers might like to pay their tax on a monthly or quarterly basis, looks at other countries where such payment systems are in place, and considers how those outside MTD might make regular payments. It fails to address issues such as the impact of fluctuating Cashflow in an agricultural business, where quite commonly almost the entire turnover of the business can take place in a single quarter, and it is relatively silent on how a transition between systems might be handled beyond suggesting that the transitional liability might be settled over a period of years, possibly subject to means testing.

The hope that such a transition "would need to be simple ...so that taxpayers are clear on what they are paying and why" seems a little hopeful.

Finally, it looks at case studies to see the impact a new system might have on them. The illustrations indicate more than anything where HMRC consider the self-employed sector to be: gig worker, tutor, landlord, small shopkeeper, personal service company director, business professional and pensioner.
Apart from the shopkeeper, these are small scale businesses on the fringes of employment/self-employment, probably with other sources of income. None of these will have substantial business expenses, huge fluctuations in turnover or the complexities of multi partner partnerships. It is hard to see how the paper could be more "out of touch" with the reality of the true self-employed market.

The paper concludes by asking 45 questions. Comments from the general public must be submitted by 13th July, so those of us wishing to express a view on the proposed changes have relatively little time to do so.

ELMS Schemes -
further details released

Preliminary details on the pilot schemes for the “Sustainable Farm Initiative (SFI)” were released on 10th March along with confirmation that qualifying farmers will be able to apply to take place in the pilot trials from later that month. The SFI is the first part of the Environmental Land Management Scheme (ELMS) which will ultimately replace the existing Basic Payment Scheme (BPS) subsidy, now in the process of being phased out.

It is intended that most farmers will be able to enter the SFI scheme. Roll out will begin in 2022 and initially all existing BPS claimants will be able to enter. In the meantime, those wishing to enter the pilot scheme (broadly BPS claimants who have land in England which is not in existing agri-environment schemes) will be able to volunteer from the end of March with agreements commencing in October.

Interestingly, the paper gives details of the payments which can be claimed under the pilot scheme in addition to an undisclosed “participation”” fee. Whilst it is stressed that the pilot payments will not be the same as the payments in the “live” scheme, and “updated payment rates for the launch of the SFI Scheme for 2022 are currently being developed”, it does give some idea of their possible magnitude.

Initially the standards which make up the scheme include separate criteria for horticultural and arable land and soils, similar standards for improved and low input grassland, and standards for hedgerows, woodland and waterbody buffering.

Although SFI payments cannot be claimed for land which is already receiving existing agri-environment payments, support can be claimed under different standards for the same parcel – so for example a field with hedges and a watercourse could be eligible under the hedgerow standard, watercourse standard and both the land and soil standards. Each standard has three different achievement levels each with its own payment rate. Further standards are likely to be added to the package in due course. It would appear that during the phasing out period both BPS and SFI could be claimed on the same land.

To take an example, a 10Ha field with 1500m of hedgerows and 550 m of buffer strips claiming at the highest rate for the four relevant packages might receive about £1900 made up from land and soil standards of £74 and £59/Ha and hedgerow and water payments of £24 and £34 per 100m. By comparison, under the BPS rates, and subject to satisfactory greening, the same field might have received a subsidy of about £2300.

Clearly it will not be possible to determine the exact financial impact until actual SFI rates (rather than pilot rates) have been determined, but in the meantime those who wish to participate in the pilot schemes need to express an interest, and those who want to know more about SFI can access the full 25 page document below

The full document can be found here

“It would have been helpful to see some more concrete payment data, but this paper makes interesting reading. We know that BPS payments are being phased out, and farmers will now be able to see exactly how they will need to make their operations greener in future to qualify for the optimal SFI income”

Compulsory Purchase Orders
what you need to know

Various geographical areas across England are seeing large infrastructure projects continue to build momentum, as the current government looks to make improvements, in particular to travel and the providing of better connections between thriving towns and cities.

We have seen a number of projects more recently in Cambridgeshire, as an example, with the widening of the A1 (into the A1M) and further the creation of the new A14 route.

A key feature with all these government projects is the Compulsory Purchase of land. Whilst there is little control for the landowner when a Compulsory Purchase Order (CPO) comes along, there are some important items to consider, particularly from a tax perspective.

The landowner will receive monies from the purchaser in exchange for the disposal of their land. Often, the disposal is unplanned from the landowner's point of view, and therefore there are some additional provisions available to the landowner.

Income or Capital

In most scenarios, the proceeds received from a CPO will include a mixture of income and capital proceeds. The devil, as usual, is in the detail (on the underlying contracts), but as a general rule there will likely be some compensation for the loss of income or disruption caused i.e. Loss of crop. This element will be taxed as income, so, for example, will form part of the farming business profit. It is important that the contract is read by the accountant / tax adviser so this element can be stripped out, and correctly reported.

The remaining proceeds, in most circumstances the lion's share, will be of a capital nature. Standard Capital Gains Tax (CGT) rules apply, in that you will need to calculate the amount of gain on the disposal. Large CGT liabilities can often be created due to CPO's, and a plan should be put in place as to the use of the proceeds and potential mitigation of the tax. Reinvestment is usually high on the list of the options due to the reliefs available, and thought should be given to exactly what you will/can reinvest into.

Rollover Relief is a popular route used, where you reinvest the proceeds, or an element of them, into qualifying assets. Should the recipient be looking to reinvest the proceeds into capital projects, then there are some differences and extensions to the usual rollover relief rules available.

Original rules:

1. Time frame for reinvestment extends to three years after unconditional exchange of contracts, and you can also rollover into acquisitions one year before.

2. Rollover must be into assets used for the trade. It is noted the construction of new buildings on land already owned can qualify for relief. Moveable plant and machinery are not qualifying assets.

3. The gain deferred rolls into the base cost of the new asset you are acquiring (reducing it). This will result in the gain crystalising on the disposal of the replacement asset.

4. Full relief (i.e. mitigation of the whole liability) is only obtained where the total proceeds figure is reinvested (not just the gain arising). This may mean finding some additional funds to account for costs of sale or other deductions made from the proceeds before you receive them. Where a lesser amount is reinvested, partial relief can be claimed, but tax will still arise on the disposal.

CPO rules:

1. Recipient proceeds must be reinvested into what is termed as 'new land'. This does not include the cost of buildings, or additions thereto, on land already owned. It can though extend to the purchase of a new property, for example, as long as this does not become the owner's main residence within the first 6 years.

2. The landowner must not have taken any steps to make any willingness to dispose of the land, known, i.e. it must be a disposal outside of the owner's control

3. There is no requirement that the new land is used in the trade. You could buy a buy-to-let property, for instance

It is also important to consider the time of a disposal in respect of a CPO. Normally, where a transfer is made under contract (a standard sale), the date of disposal is either the date of the contract or, if the contract is conditional, the date it becomes unconditional – usually on exchange of contracts. This is the 'tax point' and tax will be chargeable based on this date, regardless of when the money actually comes in.

However, a compulsory purchase may take place without a formal contract in place. In those cases, the date of disposal is the date the compensation is agreed. A first tranche of compensation may well be paid in advance of the final figure being agreed and it's therefore really important to know your tax liability (or as near an estimate as you can get) as early as possible, so you don't spend proceeds later required to settle a tax liability.

As you can see, the rules can be complex, and it is important to seek professional advice. Should reinvestment not occur within the requisite time period, HMRC have the right to remove the relief claimed and will also revert back to the usual time limits, which could cause a nasty cocktail of interest, and in the worst case, penalties to be added to the tax due.

Top Five Tips on CPO's

1. Get your professional network on board as soon as you can, and make sure important documents (like contracts) are shared.

2. Ensure the contract or agreement is reviewed for the split of income and capital proceeds and that this is clear. The date of agreement of these terms will usually be your tax point if all is finalised.

3. Understand the capital gain underlying on the CPO – seek advice from your accountant and tax advisor.

4. Plan for using the proceeds; whether you pay the tax or utilise rollover relief, you should identify the post-tax position. Partial rollover relief can be available, but remember it is the reinvestment of the proceeds, not the gain, that the relief is based on.

5. Don't rush if you don't need to. The time limits allow you to find suitable reinvestment assets. With the recent pandemic, it is likely you could argue an extension to the limits. A provisional claim can be made on your Tax Return whilst you're waiting for the right opportunity to present itself.

Covid and Furnished Holiday Lets

a sting in the tail?

Covid and its implications have had a rather mixed effect on diversified businesses. Some, such as farm shops have generally come out as winners, whereas others such as farmhouse B&B have seen income disappear, mitigated only, perhaps, by aspects of the support packages.

Furnished holiday lettings (FHLs) have probably come out as overall losers, although some will have experienced a windfall from the business rates grants, other owners may have picked up useful income in the summer from the "staycation boom", and others may have taken the opportunity to simply write the year off and catch up on maintenance and refurbishment. However, as is often the case, there may be a tax problem in the making.

Qualifying FHLs have a privileged tax position, and despite legally being a "property business" they are treated as a trading business if certain conditions are met. This not only means that the income is pensionable, but also that capital allowances can be claimed, and there is no higher rate restriction on a claim for mortgage interest suffered. Moreover, capital gains on the disposal of a FHL asset can usually be reduced or deferred by rollover relief, holdover relief or Business Asset disposal relief.

The FHL qualification tests are well known, and relate to location, occupancy and availability. The two key tests which usually need to be considered are occupancy of 105 days for short term lets and availability for letting of 210 days. Clearly these are quite likely to be problematic for 2020/21.

Fortunately there are some reliefs within the existing legislation. Unless this is the first or last year of letting, a business can elect for a "period of grace" which will obviate the occupation test where a commercial business satisfied the conditions in the previous one or two years. A further relief is given where "exceptional circumstances" led to periods of occupation exceeding a 31 day period which would have precluded them from being included within the 105 days.

Neither of these reliefs is helpful in achieving the 210 day "availability" requirement. There is perhaps a fine point for debate on whether a property can be available, if a customer is legally forbidden to occupy it. One could perhaps reasonably argue that the prohibition applies to the tenant, not the property owner, or perhaps that the case law on illegal trades might be usefully invoked. What is really needed is clarity from HMRC to redress a situation which is far from that envisaged when the legislation was passed. The HMRC blog on FHLs and Covid simply says "There is no COVID relaxation in relation to the availability condition for furnished holiday lets. So, if the property is not available for the 210 days, then the FHL status is immediately lost".

If the property fails to qualify, consequences will flow in two directions. From an income tax viewpoint, any income will be treated as normal rent, with the higher rate disallowance on mortgage interest and a potentially awkward position regarding losses, since brought forward FHL losses cannot be set against current rental income, and any rental losses arising in 2020/21 will not be able to relieve future FHL income. Potentially there is even the complication of cessation provisions being brought into play although there is some solace within the HMRC business tax manual which, no doubt with Covid, in mind, now states that: "Temporary breaks in trading activity do not amount to a permanent cessation of the trade for tax purposes. For example, if a business closed its doors to customers, or otherwise ceased trading during the coronavirus lockdown period, but intended to continue trading after restrictions were lifted, then the trade should not be treated as having ceased. Any income and expenses relating to the gap in trading will be taken account of in calculation of trade profits or losses, subject to the usual tax rules and case law.

This is dependent on the resumption of activities following the break being the same, or similar, to those prior to the break " A period of lost FHL status may also have longer term implications. Since most of the CGT reliefs must be time apportioned where an asset is only partially entitled to them, there will potentially be a year of ownership where no business reliefs are due. One wonders whether this will be picked up years into the future, when 2020/21 is just an awful memory.

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As we come into the start of the 2020/21 tax return season, FHL owners should perhaps be thinking what evidence they can produce to show that their properties were indeed available for let for 210 days – or better still, HMRC could give some thought to what the tests were intended to achieve – but it is definitely not a case of just "ticking the same boxes as last year"

Firewood supply rule changes –

Will it encourage the black economy?

New rules announced by DEFRA on 16th February will, with effect from 1st May, regulate the sale and supply of firewood for domestic use.

The rules, which have been introduced in order to reduce the emissions from the burning of damp wood, will require firewood suppliers to register with "Woodsure Ltd" and certify that wood sold in small volumes is properly labelled and has moisture content of below 20%. The rules will apply to the supply of firewood or wood briquettes in single retail bags or in loose volumes of less than 2 cubic meters.

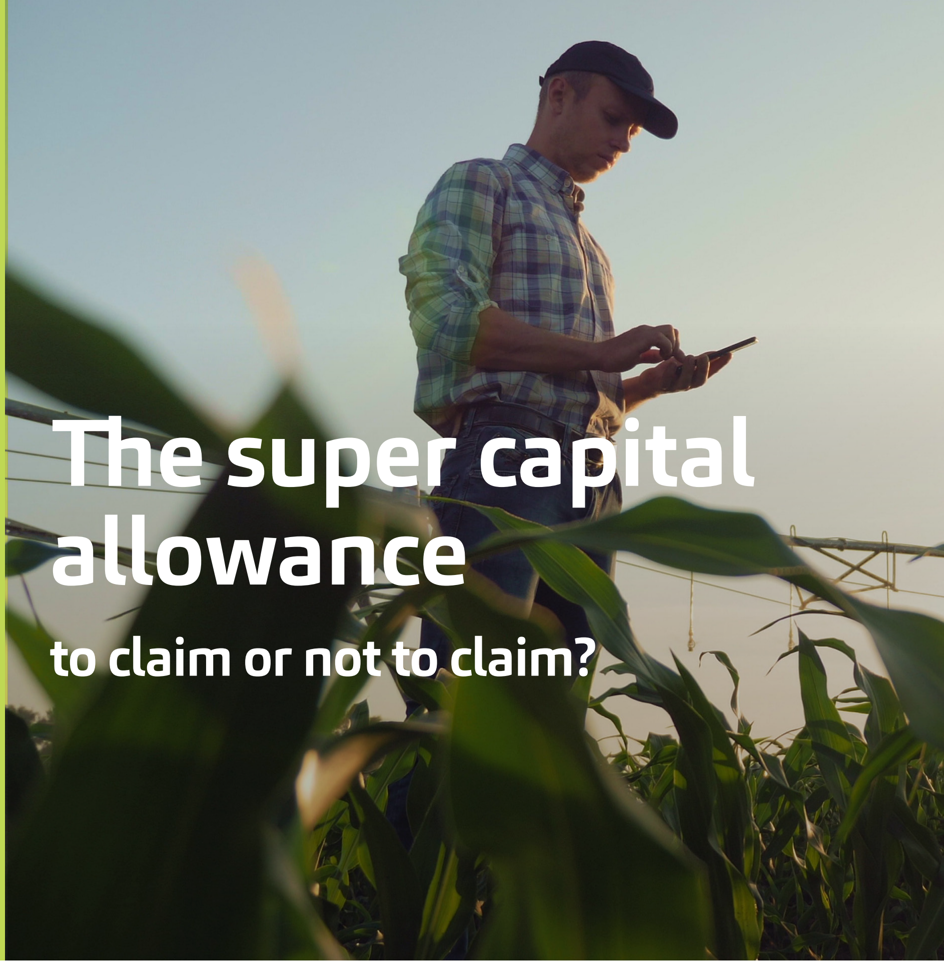
Registration will require details of how wood is sourced and dried, together with lists of retail outlets supplied, websites, storage depots and turnover. There will be a range of costs, with an initial registration fee of £122.40, an annual fee of £385.20 and further annual audit fees of between £134.40 and £2448, depending on volume. The rules will be enforced by local authorities, and fines for non-compliance can start at £300.

Businesses which supplied less than 600 cubic metres of fuel in the year ending 30th April 2021 do not need to comply until 1st May 2022, and those supplying fuel in loads of over 2 cubic meters only need provide customers with appropriate burning advice (in a prescribed wording).

Whilst the new rules will be irritating to those who sell a few logs or kindling to passing traffic at the farm gate, it is hard to see how it will have any material effect on emissions. Those who buy their dry wood at the garage or garden centre will continue to do so. Those who use wood burners regularly will continue to buy their logs, wet or dry, by the tipper load and those who cannot now find any legitimate local firewood will continue to steal it when they are out walking!

It should be noted that the rules include both sales and supply of fuel, and presumably will also include those who include fuel within the cost of a holiday letting rent – so buying fuel in bulk and then supplying small quantities to holidaymakers free of charge will also be caught by the new conditions.

These changes may be viewed by some as a further helpful measure in contributing to the reduction of emissions. However, others may view this as a pointless exercise which encourages future sales to be cash only, to regular customers, neighbours and friends and not to show it in the farm books thereby pushing this income into the black economy. If this happens - only time will tell.



130%

The super capital allowance

to claim or not to claim?

Whilst the "super allowance" of 130% enhanced tax relief announced in the 2021 Budget might seem attractive, claiming it should be given some consideration before doing so.

The new relief , which is only available to corporate businesses, becomes available from 1st April, and gives an uplift to the amount which can be claimed, so a piece of plant costing, say, £100,000 is treated as if it had cost £130,000 and the tax relief at 19% will be £24,700 instead of £19,000. This will be good for cash flow, but there is a sting in the tail.

The 130% allowance expires in April 2023 at exactly the same point as the corporation tax rate goes up to 25%, and when a "super allowance" asset is sold before that date, the proceeds don't go back into the machinery pool, but are treated as if the monies received were 30% greater. This means that if the plant were traded in before April 2023 for say, £80,000, the tax payable would be £80,000 x 130% x 19% = £19,760 – so the tax saved will always be limited to 24.7% (19% x 130%) of the depreciation suffered on that particular asset.

Even aside from the balancing charge issue, timing of capital purchases and sales will be absolutely critical over the next few years for smaller companies.

There will be a marginal rate of 27% for companies with profits between the small company and mainstream tax limits, (£50,000-£250,000) so it will be important to avoid keeping asset sales outside that band if at all possible –using the above example, if the sale transaction fell into the marginal rate, the tax relief would have been given at 24.7% but the clawback would fall into a 27% band. Similarly, although the enhanced loss reliefs also announced in the Budget could generate repayments of tax previously suffered at 19% it may be better to carry the enhanced losses forward to reduce tax in later years at 25% or 27%. Finally, the existing 100% annual investment allowance on investment of up to £1,000,000 is also only guaranteed until December 2021, so if it then reverts to £200,000 the options for managing optimum CT exposure will become slightly more difficult after that date.

Taking all these factors together, planning machinery transactions for best tax effect over the next few years seems likely to become far more challenging that it has been and detailed professional advice will be more important than ever.

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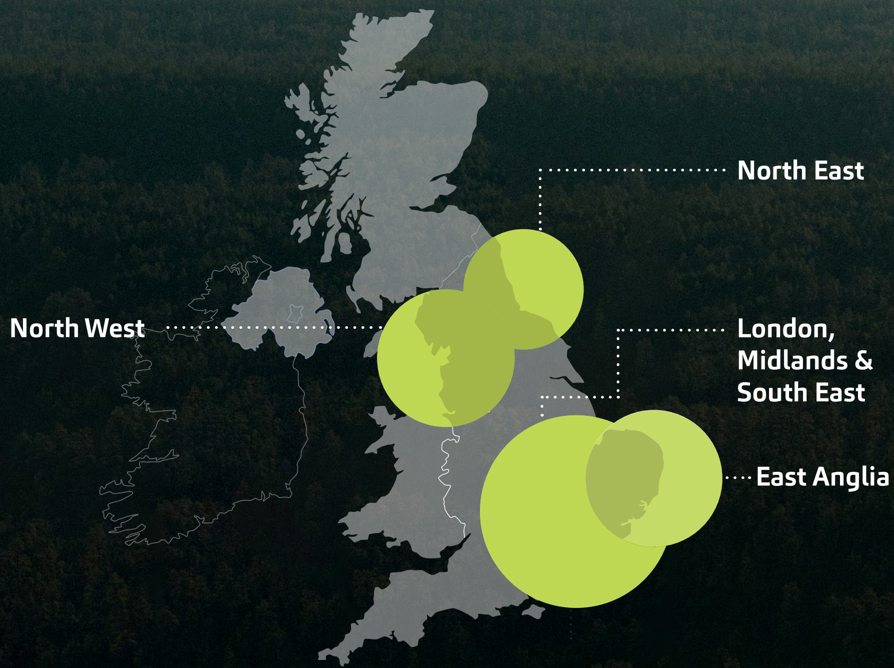

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