

Spring 2013

Agricultural Focus

Sowing the seeds for future prosperity

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Introduction to Agricultural Focus

The period in the run up to 5 April is a good time to review the financial health of your business, both to identify the likely impact of trading over the next 12 months on the cashflows of the business and to ensure that activities are structured as tax efficiently as possible.

A good understanding of likely cashflows will be particularly important this year with many arable farmers having failed to establish anywhere near their normal amount of winter cropping; dairy farmers seeing their cows rapidly eating through reduced forage stocks; and potato growers considering the risk versus return profile of both contract and free market potatoes. Planning cashflows over the next 12-18 months will be harder this year than most, but that just makes identifying pressure points well in advance even more important.

Structuring your farming business as tax efficiently as possible just makes good sense. There are the normal planning points to consider in the run

up to 5 April 2013 such as looking at the timing of equipment purchases and the timing of realising profit through crop or livestock sales and for those with companies it is important to consider the timing of dividends. However, it may also be a good time to review the structure of your farming activities. Structural changes may involve introducing a new partner; separating part of the activities into a different entity, or transferring assets between family members.

Now that better accounting records are kept on most farms, producing a reasonably accurate profit forecast and calculating the tax liabilities based on these profits, has become a cost effective exercise for many. Even in the current climate of uncertainty it should be possible to predict tax cashflows through to July 2014 with a reasonable degree of accuracy.

If your current accountants just tell you what has happened in the past then please feel free to contact us so we can discuss what will happen in the future.



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Increased Annual Investment Allowance available

Ensure the tax benefit is maximised

The Annual Investment Allowance (AIA) available for capital allowances increased from £25,000 to £250,000 from 1 January 2013, for a period of two years. This will mean that the amount spent on new machinery that will obtain a 100% tax deduction in the year of expenditure has potentially increased.

However, when planning the timing of expenditure, a farming business needs to consider their accounting year end date and what other expenditure they have incurred in their financial year; as the manner in which the increased AIA will become available will mean that it is not available to all businesses that spend £250,000 on new machinery in early 2013. The full £250,000 allowance will initially be available in the first 12 month accounting period that commences after 1 January 2013.

How much of the increased allowance will be available?

If a business has a December year end, and incurs £250,000 of eligible expenditure in early 2013, a 100% tax deduction can be claimed for this expenditure in the year ended 31 December 2013.



However, a business with a March year end that incurs £250,000 of eligible expenditure before 31 March 2013 will only be eligible for a maximum AIA of £81,250, even if they have incurred no other eligible expenditure during the year ended 31 March 2013. This is because for nine months of the year the AIA was only available at a rate of £25,000. Therefore, the AIA available will be $9/12 \times £25,000$ plus $3/12 \times £250,000$.

A business with a year end in the early part of 2013 that is planning significant expenditure on machinery in the early part of the year should consider delaying the expenditure until the start of their new financial year in order to obtain the full £250,000 AIA. For example, a business with a March year end that incurred £250,000 of eligible expenditure in April 2013 would be eligible for AIA on the full amount. This is a significant increase on the £81,250 that would

have been available on expenditure incurred in January 2013. It may be possible to change the accounting year end of a business in order to accelerate the increased AIA available.

Relevant date of purchase of equipment for capital allowances

If an asset is being purchased outright, with no finance, the acquisition date for tax purposes is the date that the invoice is issued. However, extended payment terms cannot be available. If there is a gap of more than four months between the invoice date and the date on which payment is required to be made, the

expenditure is not incurred until the date on which payment is required to be made.

If an asset is being acquired with hire purchase, the acquisition date for tax purposes is the date that the asset is brought into use. Therefore, for agricultural machinery, the machinery must have been delivered before the year end for a tax deduction to be obtained. Additionally, the hire purchase must be on "normal" payment terms.

What entities do not qualify for AIA?

AIA is not available to a partnership where non-individuals are members. Therefore, a

partnership that has a corporate partner or includes a trust as a partner will not qualify for AIA. Such partnerships are not uncommon, as corporate partners have been used for income tax planning and trustees included as partners in order to maximise Inheritance Tax reliefs under Balfour type principles.

However, if capital expenditure is incurred in a corporate partner or a trust that is a partner, these entities may qualify for AIA.

Shooting syndicates

Is VAT an issue?

Many farmers and landowners are involved in shooting syndicates. Such syndicates may shoot over land farmed by individuals involved in the syndicate, or over land farmed by unconnected parties.

VAT considerations

There is no general rule that all shooting syndicates are VAT free. The VAT treatment of each syndicate will be decided on its own facts. Where a group of individuals get together to form a shooting syndicate, and contribute to cover the costs of that syndicate, this should not result in any unintended VAT liabilities being incurred. This will be the case whether the syndicate shoots over land owned by one or more of the syndicate members, or owned by unconnected parties.

Where a syndicate provides "let" days then this could be seen by HM Revenue & Customs as converting the entire syndicate activity into a "business", including the supplies made to its members. Therefore, where let days are provided, the level of income from all supplies made should be monitored carefully to ensure that this does not exceed the VAT threshold of (currently) £77,000 during any "rolling" 12 month period. This should include an imputed value for days supplied to members of the syndicate.

Where a landowner grants shooting rights to a syndicate in return for the provision of a number of days shooting, this should not be regarded as let days by the syndicate, but should be regarded as consideration given by the syndicate. If

registered for VAT, the landowner must account for VAT on the open market value of the rights.

Going forward

The way that a syndicate is structured may result in an unintended VAT liability being incurred. Therefore, all syndicates should regularly review their structure, and the number of let days provided, to ensure that it does not result in unintended VAT liabilities. Now is an appropriate time to do that, as syndicates begin to prepare for the next season.

If you would like to discuss potential VAT issues please contact Adam Lloyd or Julian Millinchamp on 01242 237661.



Proposed changes to loss relief available

Will you be caught ?

HM Revenue & Customs are proposing to introduce legislation with effect from 6 April 2013, which will restrict the ability of individuals to set off farming losses. This could have a significant impact for farming businesses that operate as partnerships or sole traders.

The timing of the new legislation will mean that tax losses resulting from the rain affected 2012 harvest, or as a result of increased expenditure on machinery to take account of the increased Annual Investment Allowance, may not receive tax relief as early as expected.

Current position

Currently, when an individual (sole trader or partner in a partnership) suffers a trading loss, this can be set against total income in the tax year of the loss, or the previous tax year. This means that "immediate" tax relief is available against business profits made in the previous year and also against non farming income such as rental income, or income from diversified businesses that have been developed.

For example, if a loss is suffered in the year ended 30 April 2012, this can be set against total income for the tax year ended 5 April 2013 or year ended 5 April 2012. Even the most successful farming businesses can suffer a loss as a result of circumstances such as the weather, and the current loss relief available can offer a significant cash flow advantage. The relief is extremely useful for businesses such as fruit growers and potato growers who tend to suffer a "yo-yo" pattern of profits and losses.

Future position

The proposed change in the legislation will restrict the ability to set a trading loss against total income, to an amount of the greater of £50,000 or 25% of total income in any tax year. Therefore, if a profit of £200,000 is made in the year ended 30 April 2012 by a sole trader or a partner in a partnership, and a loss of £150,000 is made in the year ended 30 April 2013, if the individual does not have any other sources of income such as rental income to set the loss against in the year ended 5 April 2013 or 2014, only £50,000 of the April 2013 loss can be set against the 2013 total income.

The remaining loss of £100,000 should be available to set against future trading profits. Currently, all of the £150,000 loss would be available to set against total income in the year ended 5 April 2013. This restriction will mean that loss relief will be received up to a minimum of two tax years later, which will affect cash flow.

This example has ignored the effect of farmers averaging of profits to illustrate how the change in legislation will work. Farmers averaging is likely to reduce the impact of the change, but this will depend on taxable profits and marginal rates of tax for earlier and later years.

Possible planning

The first accounting period to be affected is the first period ending after 5 April 2013. Therefore,

there is likely to be an opportunity to plan to reduce the impact of the proposed change.

Possible planning could include introducing a spouse as a partner; or additional partner in a partnership, in order to qualify for an additional £50,000 of loss relief in a tax year. Alternatively, there could be tax benefits from transferring a business to a company, particularly where the business has a "yo-yo" pattern of profits.

Where changes are planned to the structure of a farming business, the effect on the entitlement to Single Farm Payments should be considered, to ensure that the planned changes do not have an adverse effect on the entitlement.



Renewables

When embarking on a large-scale project ensure the right ownership structure is adopted

With large scale renewable projects becoming more common it is important to ensure that the right ownership structure is in place to minimise tax exposure. The most tax efficient approach may well depend first of all on whether the land owner is operating the site as a business themselves, or merely leasing the site to a third party, in which case the land involved is likely to become an investment asset.

If the landowner is operating such a project as a business then trading as a separate entity from an existing farming business may offer tax savings.

1. A second Annual Investment Allowance may be available

The majority of the capital cost of purchasing equipment will qualify for Annual Investment Allowance (AIA) and so in order to maximise the tax relief it may be advantageous to use a different entity to purchase the equipment. This would be particularly beneficial where the existing farming business already makes use of its AIA (currently £250k per year) and where the new entity may also claim the maximum allowances available on qualifying capital expenditure in its business.

2. A company may be a tax efficient vehicle for a profitable business

As the renewable project is likely to be profitable then undertaking the project through a company will probably mean that profits will suffer tax at a rate of 20%, instead of 40%, 50% or even 60%, leaving more profits to repay borrowings taken on in the company to fund the project.

The company could be completely separate from an existing partnership. However, a company could also be introduced as a new partner in a partnership and this new partner could undertake the project.

Plans for succession - availability of capital tax reliefs

Ensuring the business structure is correct from the outset is critical to avoid significant capital gains tax (CGT) or Inheritance tax (IHT) charges when passing assets on to the next



generation, particularly if the site is to be leased to a third party.

Generally bare farm land qualifies for Agricultural Property Relief (APR) from IHT, after the required qualifying period, and hence it is possible to leave land on death to the next generation without an IHT charge. Land that is eligible for APR also qualifies for Gift Relief from CGT and so it is equally possible to make a lifetime transfer of farmland without crystallising a charge to CGT.

However, where land becomes an investment asset, such as in the case of land rented to a third party as a solar park, then APR is unlikely to be available and one would need to rely on the Balfour case to secure Business Property Relief (BPR) from IHT.

Where the new enterprise is not wrapped up within an existing farming business, or traditional

farming activities are insignificant in comparison to the renewable project, then BPR may be lost.

The lifetime transfer of a leased site to the younger generation may crystallise a significant CGT liability as the site is unlikely to qualify for Gift Relief.

The best IHT planning approach may well be to try and ensure that the ownership of any largescale renewable site is transferred to the younger generation before there is a significant increase in value and before it stops being bare agricultural land. However, this may not be appropriate if the older generation needs access to the income or if there are concerns about the younger generation owning assets with a significant value.

The most sensible and tax efficient approach requires careful thought and may require action even before planning permission is granted.

Year end planning

Ensure full use is made of annual tax allowances and reliefs

There is still an opportunity to review matters and ensure full use is made of annual tax allowances and reliefs for the year to 5 April 2013.

1 Married couples should use both personal allowance and basic rate tax bands

For the year ended 5 April 2013, each individual has a tax free personal allowance of at least £8,105 and a 20% tax band of £34,370. Income between £42,475 and £150,000 is charged to tax at 40%. Where an individual has taxable income over £100,000 they will lose some or all of the personal allowance giving an effective tax rate of 60% on income between £100,000 and £116,210. Income tax is charged at 50% on income exceeding £150,000. Possible planning could include varying profit shares in a partnership or ensuring that

dividends paid from a company are paid to the spouse with the lowest tax rate.

2 Child benefit

Child benefit will be restricted where one individual in a household has an income over £50,000. Where possible, income should be equalised between husband and wife and "partners" to ensure that the child benefit restriction is minimised.

3 Pension contributions should be considered particularly where tax relief at 40%, 50% or even 60% is available

The rules relating to tax relief on pension contributions now allow an individual to contribute up to 100% of earned income (for example salary, or partnership profit) subject to an annual limit of £50,000. However, any unused

relief can be carried forward for up to three years. Therefore, pension contributions can be a useful tool in reducing the amount of income suffering higher rates of tax. Individuals should be aware that the annual limit is due to be reduced to £40,000 from 6 April 2014.

4 Capital Gains Tax annual exemption

Each individual currently has an annual exemption of £10,600, which means that the first £10,600 of capital gains are tax free. Therefore spouses should consider transferring assets to each other before disposal to ensure the annual exemption is utilised, which could save tax at 28%. It may also be more tax efficient to crystallise a capital loss in the year before making a capital gain, than in the same year as the gain, as a loss brought forward is only set against gains after the annual exemption has been utilised.

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