Landed Estates Update

DRIVING LIFELONG PROSPERITY

Spring 2019

Welcome to the current edition of Landed Estates Update, our publication for landowners and those advising on Landed Estates. With house building a priority, we consider some of the issues around selling land for development.

OWNERSHIP

The grant of planning will add value to land, giving rise to a substantial gain on sale and the potential loss of inheritance tax reliefs. The current owner will need to consider the impact of the various taxes as well as their plans for the funds once they are received.

If the money is going to be reinvested in the business there is probably no benefit in changing ownership before sale. If, however, the funds are being earmarked for particular members of the next generation, possibly children who will not inherit the estate, passing the land on before sale may be beneficial. A gift could be outright or to trustees depending on the age of the recipient.

CAPITAL GAINS TAX (CGT)

Gift pre-sale

Gifting the land prior to sale will be a disposal at market value. However, providing the land qualifies for agricultural property relief (APR) or is a gift into trust, the gain can be held over. In this scenario the recipient of the gift takes on the donor's base cost and will pay tax on the full gain on disposal.

Sale to developer

The sale of the land will give rise to a CGT charge. For bare land the tax will be at 20%, unless the sale qualifies for entrepreneurs' relief (ER) in which case tax is payable at 10%. If the sale includes residential property the gain on that will be taxed at 28%.

ENTREPRENEURS' RELIEF

ER applies in the main on the sale or cessation of a business. In order to qualify, the business must have been running for two years (one year for disposals before 5 April 2019). Typically with land sales, the business will cease and ER is then available on sales within three years.

Where the land is part of a wider estate business it is unlikely to be possible to cease the whole business. To qualify for ER it may be necessary to move the land into a separate business which can be ceased in due course.

An alternative, if the land is held off the balance sheet but used in the business, is to make an associated disposal. Providing the landowner makes a disposal of at least 5% of their share of the business at the same time, the land sale can qualify for ER. The disposal of part of the business may well be to the next generation as a way of bringing

them into the business. There are potential restrictions on the availability of ER, if say the land has been rented to the business, and care is needed in these circumstances as the relief may not be as generous as first thought.

Each individual has a lifetime limit of £10 million of gains that qualify for ER. For large sales it may be necessary to ensure that ownership is spread widely enough to allow the gain to qualify. Trustees do not have an entitlement to ER, although qualifying beneficiaries can surrender part of their lifetime allowance to the trustees.

ROLLOVER RELIEF

If the land has been used in the farming business, it may be possible to 'rollover' the gain by purchasing more land (or other qualifying assets). When the gain is rolled over, the purchase cost of the new land is reduced by the amount of the gain, so that the gain becomes taxable on a later sale. In order to qualify for the relief the new land must be purchased in the period one year before and three years after the date of the sale, although in certain circumstances HMRC may allow an extension to these time limits.

There may be restrictions on the amount of the gain that can be rolled over, particularly if the land being sold has not always been used in the business, or only part of the proceeds have been reinvested. If ER is available it may be better to bank the 10% CGT rate rather than rolling over and potentially paying tax at a higher rate in the future.

EQUALISATION PAYMENTS

For larger development sites there are often a number of landowners involved. Due to the requirements for green spaces etc. the developer is unlikely to pay the same for all the land. To counter this, the landowners may enter an equalisation agreement whereby they make payments to each other, ensuring that they each receive the same proceeds per acre sold. For CGT purposes the landowner making the payment cannot get a deduction for the amount paid away, whilst the recipient is taxed on it, giving rise to double taxation.

In order to avoid this problem the use of land pooling arrangements or cross options can be considered. Both need careful planning and the best alternative will depend on the circumstances of all the landowners.

INHERITANCE TAX (IHT)

Land qualifies for two main reliefs from IHT, agricultural property relief (APR) and business property relief (BPR) The crucial difference is that APR gives relief for the agricultural value of the land whereas BPR gives relief to the market value of the land. Even if planning has not been granted the land may have hope value and BPR is needed to protect the IHT position.

If land is gifted, the donor must survive seven years for the gift to be exempt for inheritance tax. If the donor dies within seven years it is the value of the gift at the point it is made, and not at the point of death, that comes into charge. Gifting before planning permission is granted ensures that the value of the gift is kept to a minimum.

As noted above, for CGT purposes it may be necessary for land to be held off the balance sheet. In this scenario BPR is only available at 50% compared to 100% when on the balance sheet.

VAT

Under a promotion agreement, while the promoter initially bears the cost of obtaining planning, they will invoice the landowner for their services once the land is sold. These fees will be subject to VAT and, if the landowner wishes to recover the VAT, they will need to be registered for VAT and 'opt to tax' the land.

Once the option to tax is in place VAT will be charged on the sale. Whilst the purchaser will be able to recover the VAT, it may cause a temporary cash flow issue for them, and will increase the stamp duty land tax (SDLT) payable. If the landowner registers for VAT they need to be aware that any business carried out in their name will be covered by the registration.

To avoid the need for the landowner to register for VAT it may be possible to structure the agreement so that, in effect, the purchaser pays the promoter's fees. This has the added benefit of reducing the SDLT on the land sale. Consideration needs to be given at the outset to ensure the correct agreement is put in place.

CONCLUSION

When considering the sale of land for development there are a number of issues, both tax and non-tax, such as the ages of those involved, what they want to achieve and the timescale before the sale might happen, to think about.

Every case is likely to be different and starting the planning early will ensure that the family can benefit from the best option for them.

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