

Agricultural Focus

DRIVING LIFELONG PROSPERITY

Autumn 2021

SPOTLIGHT ON CAPITAL ALLOWANCES



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HAZLEWOODS

DRIVING LIFELONG PROSPERITY

Corporation tax: Capital allowance super-deduction

In the 2021 budget the Government announced the introduction of a temporary capital allowance super-deduction. This is a beneficial tax deduction in the year of purchase of qualifying equipment, aimed at encouraging businesses to make investments now, to help stimulate economic growth. Set out below are the main qualifying conditions and the potential tax savings available.

WHO IS ELIGIBLE TO CLAIM?

The deduction is only available to limited companies, not partnerships, LLPs or sole traders.

WHAT QUALIFIES?

Most new plant and machinery purchases such as tractors, cultivating and harvesting equipment will qualify for relief at 130% of the purchase price.

A first-year allowance of 50% is available on special rate qualifying assets; for example, solar panels, electrical and water systems integral to a building.

There is no cap on expenditure for the super-deduction, unlike the annual investment allowance (AIA) which is currently capped at £1 million, dropping to £200,000 from January 2022.

WHEN?

The relief covers expenditure between 1 April 2021 until 31 March 2023.

WHAT IS EXCLUDED?

There are a number of specific exclusions from the relief including:

- Cars
- Building and structures
- Second-hand equipment or equipment used for leasing



WHAT ARE THE TAX SAVINGS?

Plant and equipment	Rate	Tax saving per £1 spent	Type of expenditure
Super deduction	130%	24.7p	New
AIA (£1m cap)	100%	19p	New and second hand
Main pool	18%	3.42p	Second hand
Special Rate			
Super deduction	50%	9.5p	New
AIA (£1m cap)	100%	19p	New and second hand
Main pool	6%	1.14p	Second hand

WHAT SHOULD BE CONSIDERED?

- Should you buy new equipment rather than second hand?
- When should the acquisition be made?
- Is the planned capital expenditure likely to exceed the AIA limit?
- If the relief for capital expenditure leads to a tax loss, how should this be relieved?

IN SUMMARY

For limited companies, there is a two-year window of opportunity in which to benefit from the super-deduction which ends 31 March 2023. However, as one of the qualifying criteria for expenditure on plant and equipment is that it needs to be new, rather than second hand, you should establish if the increased cost and benefit of buying new is covered by the additional relief you will receive.

Plan the timing of capital expenditure to make the best use of the allowances available, including AIAs. There is the added complication of the reduction in AIAs from 1 January 2022 to add into the mix. The actual AIA relief available will depend on your accounting year end as well as the date of the expenditure. For example, if your year end is 31 March and all your capital expenditure takes place between 1 January 2022 and 31 March 2022, the maximum AIA available to you would be £50,000.

Where the super-deduction results in a tax loss, this can be carried back against profits of the last three years, subject to a £2 million cap giving a 19% tax deduction. Alternatively, the loss can be carried forward against future profits where there is potential for a corporation tax saving of 19, 25 or 26.5%, depending on the profit level of the company.



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ENSURE YOU MAXIMISE AVAILABLE CAPITAL ALLOWANCE CLAIMS ON BUILDINGS

When constructing an agricultural building, or making alterations to an existing building, capital allowances (CAs) can be available as 'plant machinery' under the integral features rules, and the remaining 'shell' of the building under structures and buildings allowances (SBAs).

Expenditure which qualifies as integral features, such as heating, electrics, ventilation and water systems, may obtain an immediate 100% tax deduction if they fall within the AIA limit set out in the article above. Any amount not qualifying for AIA will receive a tax deduction at 6% per annum on the reducing balance basis.

Expenditure qualifying for SBA does not qualify for AIA but can receive a straight line tax deduction over a period of 33 $\frac{1}{3}$ years.

When buying a 'used' building, the position regarding available CAs needs to be confirmed during the purchase process.

SECTION 198 ELECTION

In order for the purchaser to be able to claim CAs on items included in the building such as heating, electrics, ventilation and water systems, an amount allocated to these items must be agreed with the vendor and what is known as a Section 198 election made. If no amount is agreed, no CAs claim can be made on items included in the building by the purchaser.

SBA STATEMENT

Similarly, if SBAs have already been claimed on a used building, a statement will need to be provided by the vendor to the purchaser confirming the amount of expenditure available to be claimed by the purchaser going forward. Without such a statement, no SBA claim can be made on previous expenditure.

During the purchase process it may become clear that available CAs and SBAs on the building have not previously been claimed. In this instance, it may be possible for the purchaser and vendor to work together resulting in the vendor making a valid claim. This can then allow the purchaser to use the available CAs going forward.

FURNISHED HOLIDAY LETTINGS

Integral features CAs are available on expenditure on items included in the property such as plumbing, electrics and heating.

If a property is already used as a furnished holiday let at the time of purchase, a Section 198 election is required to confirm the amount the purchaser can claim CAs on going forward.

Where the property being acquired has previously only been used as a private residence, it may be possible for the purchaser to make a CA claim based on a proportion of the purchase price relating to such items as plumbing, electrics and heating.

AGRICULTURAL STRUCTURES ON WHICH PLANT MACHINERY CAPITAL ALLOWANCES MAY BE CLAIMED

Readers may remember our article 'Capital allowances: what is a silo?' in our Summer 2019 Focus. This article referred to the tax case of May and another (TC6929), where the taxpayer successfully argued that the entire cost of constructing a building qualified for CAs as plant and machinery.

Earlier this year there was another successful win for the taxpayer on a potato storage facility. JRO Griffiths Ltd v HMRC (TC8203). The company built a specialised storage facility which used external air at ambient temperature with no mechanical refrigeration and claimed CAs on the entire cost as plant and machinery. HMRC refused the claim, but the First Tier Tribunal decided the facility was 'plant' both as a silo and a coldstore.

Both cases are important wins for farming businesses and proves it is worth exploring the options when embarking on expenditure on new buildings for very specific purposes.

If you have any questions on capital allowances, please contact Peter Griffiths or your usual Hazlewoods contact.



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COMPULSORY PURCHASE ORDERS

In recent years, there has been an increasing number of compulsory purchase order cases involving agricultural businesses. After many years of public debate, the high-speed rail link from London to Birmingham, known as High Speed 2 (HS2), has become a reality. For landowners and tenant farmers on the route they will have, and may still be in the process of, securing compensation for the land that was taken. At the time of writing, many with land earmarked for the route between Crewe and Manchester/Leeds, still do not know the fate of their land. Many businesses will have been blighted by the threat of HS2 for many years and may be entitled to compensation for losses in this period.

The ability to take land, without the owner's consent, is granted to HS2, and other bodies (referred to as Acquiring Authorities) through the use of legal powers known as 'Compulsory Purchase'.

“ Compulsory purchase of property is an essential tool in a modern democratic society. It facilitates planned and orderly development... Hand in hand with the power to acquire land without the owner's consent, is an obligation to pay full and fair compensation.”

Lord Nicholls of Birkenhead

For businesses whose land is subject to compulsory acquisition the task of quantifying the impact of this on their business can be complex and often daunting for business owners.

It is vital that businesses give themselves sufficient time to consider relocation options, and to fully understand the impact that relocation may have on their business operations. The impact may be temporary, but this does not mean that quantification is straightforward. Some businesses that have relocated have suffered a permanent impact resulting in certain income streams no longer being viable. Unfortunately, the ability to relocate a farm, is often limited and the question then asked is how to quantify the value of a business which has been extinguished.

Businesses need to be prepared and take professional advice to ensure all options are adequately explored; this is vital to securing the right level of compensation. The rules of compulsory purchase and entitlement to compensation are complex. A business owner is entitled to compensation for certain losses, including loss of business profits, on the basis of 'Value to Owner'. This principle is unique to compulsory purchase.

As in any claim situation, the success of the claim will rely heavily on the quality of evidence. Evidence prepared and obtained at the time of the event is more likely to be considered credible than evidence recreated when compensation is disputed. Third party evidence is considered stronger than evidence generated internally. Taking appropriate expert advice from the outset can help business owners to create, seek and preserve key evidence including evidence to demonstrate they have mitigated their losses.

The claim will be scrutinised, it must stand up to challenge. The better a claim is constructed, in accordance with the compensation code and suitably evidenced, the more chance it has of achieving quicker resolution resulting in the payment of compensation. Whilst the costs of taking professional advice will need to be incurred, in the first instance, by the farmer or landowner, the Acquiring Authority is required to compensate for all reasonable costs incurred in taking professional advice. In recent years there has been an increase in such cases being funded by litigation funders but there is a price to such funding.

There is no doubt, the loss of land is a very difficult and emotional period for those affected and it is vital that full and fair compensation is received. If you would like any advice regarding compulsory purchase, please contact Hannah Griffin.



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Opting to tax land and buildings

The majority of farms and estates will be registered for VAT. As with any form of taxation, on the surface VAT can seem simple; however, it has many complexities in particular opting to tax land and buildings.

WHAT IS OPTING TO TAX (OTT) ON LAND AND BUILDINGS?

The supply of land and buildings, such as the sale, leasing or renting of freehold land and buildings, is normally exempt from VAT. This means that no VAT is charged, and the entity making the supply cannot normally recover any of the input VAT incurred on costs relating to the exempt supply.

Due to the nature of activities undertaken by many farms and estates, they are classed as partially exempt for VAT purpose. This means they generate both taxable (e.g. sale of crops and livestock) and exempt supplies (e.g. land and building rental). Under the partial exemption rules, a business can only recover the input VAT relating to exempt supplies provided that the amount of such input VAT does not exceed both £7,500 and 50% of the total input VAT incurred in VAT year (year ending March, April or May depending upon which of those dates is the end of a VAT period).

Once an OTT election has been made, VAT will be charged on the rent at the standard VAT rate. The landlord is then able to recover all the VAT that has been incurred in making the supply. However, even after an OTT has been granted, residential income will always be exempt from VAT.

LETTING OF COMMERCIAL BUILDINGS

The letting of a commercial building (if not solely for storage) is generally seen as an exempt supply for VAT. If the building costs or repair costs are likely to exceed the partial exemption threshold, businesses should consider opting to tax the property to allow for the full VAT on costs to be recovered.

When repairing an existing building which has previously been used for trading activities, but is now about to be let out, an OTT should be made prior to any subsequent supplies of the building being made. The option cannot be materially backdated, and HMRC should be notified within 30 days of the decision.

If the building is new, and no other activity has been operated from it, an OTT made at any point prior to its first use will ensure full input tax recovery. This can be particularly useful if building costs are higher than expected or exceed the partial exemption threshold in a particular year.

Once the land or building has been opted to tax, any future supplies will be subject to VAT. If the tenant is not VAT registered, they will have the added cost of covering the irrecoverable VAT.

If the building is sold within 20 years of the effective date of the option, VAT will need to be charged on a sale of the building (unless transfer of going concern rules apply). It is, therefore, important to consider the long-term plans for the building before making an OTT.

PROMOTION AGREEMENTS

A promotion agreement relies on a developer or land promoter gaining planning permission on land on behalf of a landowner, who then sells the land. As the sale of land is generally exempt for VAT purposes, no VAT can be recovered by the landowner on costs associated with the sale.

The promoter acts as a principal in his own right, securing planning permission for the landowner for which he charges a fee. This fee will be subject to VAT and will almost certainly exceed the partial exemption threshold. Therefore, the only way for the landowner to recover the input VAT is by making an OTT election on the land.

If the land is personally owned, rather than by a business, it will be necessary for the landowner to register for VAT and OTT the land to enable VAT on the promoter's fee and other costs to be recoverable.

COMMUNICATION

When letting or selling land or commercial buildings, it is essential for all parties and their professional advisors to understand the VAT treatment, this will enable any contract to include the appropriate VAT clauses. This is crucial to ensuring the ability to be able to charge VAT and to recover VAT on associated input costs.

The timing of the OTT should be carefully considered and made only when there is certainty of selling, letting or of considerable improvement or repair work taking place. This should avoid the landowner being left with land or buildings on which they will have to charge VAT for no actual benefit. As mentioned above, generally once made the OTT election lasts for at least 20 years, however, there is the possibility of revoking the option to tax within six months, subject to certain conditions being met.

SUMMARY

Careful consideration of if, and when an OTT should be made is key to ensuring the most beneficial VAT treatment. Opting can open the door to recovering VAT on costs that would otherwise be irrecoverable. However, by opting too early, you could be stuck with having to charge VAT on a sale or rent where the purchaser or tenant is not able in a position to reclaim. This could result in a lower rent, or sale proceeds being achieved.

If you would like to discuss options to tax, please contact one of our VAT team, or your usual Hazlewoods contact.



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Ten tips to avoid a partnership dispute

It is a sad fact that partnerships within farming families can end under acrimonious circumstances. Where valuable business assets are so tightly bound, family history tensions can run high. To help avoid a potential dispute, here are our 10 top tips:

- 1 Good communication.** Communication is key to a well-run partnership. Ensuring partners are open to discussion, debate and most importantly, listening, will help maintain the status quo.
- 2 Partnership agreement.** If you do not already have one, put in place a well written partnership agreement which all partners understand and buy into. The agreement should clearly outline the rights and obligations of the partners and set out steps for division of assets upon termination. If one is already in place, check that it is current and reflects the ongoing business activities.
- 3 Regular partners meetings.** Busy farmers may see each other frequently on the farm but it is important to make time to sit down and discuss the business and the future direction. These meetings should allow each partner to voice their opinion and ideas. This will highlight potential areas of disagreement early and with open conversation, hopefully an equitable solution can be found.
- 4 Plan ahead and budget.** Prepare for any significant capital expenditure, including the timing of purchase and the financing arrangements. This will ensure all partners are on board with major commitments made on behalf of the partnership.
- 5 Property capital account review.** The annual partnership accounts should include a property capital account. This allocates the land and property between individual partners based on the underlying ownership of assets. Reviewing this on an annual basis and approving the split by signing the accounts avoids any ambiguity and misunderstanding about asset ownership.
- 6 Ensure profit share reflects input.** Often the allocation of profits within a farm partnership is driven by the tax position. Provided the partners agree and understand why profits have been allocated in a certain way, this approach works well. However, if one or more partners feel they are contributing more than others, they may want this to be reflected in the profit share. A partnership agreement should build in flexibility when allocating income profits, perhaps by considering a prior share of profit in the form of a fixed salary.
- 7 Private use of assets.** This can become a bone of contention if there are material differences between the partners. For example, if one partner drives a new Porsche Cayenne and the other a 10-year-old farm truck and the partnership pays for the running of these assets, or a variance between living in a large farmhouse and a small estate cottage. Compensation can be made by way of a larger profit share and additional drawings to equalise the position on an annual basis.
- 8 Review of drawings and capital introduced.** A detailed breakdown of the amounts included in accounts can always be provided. These should be reviewed and discussed on an annual basis to ensure allocates are correct and fair. The result being the capital accounts reflect the true position.
- 9 Document final decisions.** This should avoid a decision being questioned later when the reasonings, although valid and agreed in the moment, are lost in the mists of time.
- 10 Agree roles and responsibilities.** Ensure each partner's role is a conscious decision, rather than a habit formed from a lifetime of working together. It is important to share the workload fairly and for each partner to feel valued for their input.

Hopefully these tips will help pave the way for a long and happy partnership. However, if communications break down and the partners no longer agree, it is worth considering mediation to help resolve a dispute and potentially avoid litigation.

The role of a mediator is not there to offer tax or legal advice, but to facilitate discussion and explore options. If partners have a divergence of opinions, mediation may be able to find an agreeable way forward.



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WHAT IS BOTHERING OUR FARMERS?

You may have taken part in and/or read our recent report on the 2021 survey undertaken by the Rural Agricultural Group (RAG) of accountants which we published in August. The overall sentiment of respondents being 'somewhat' optimistic about the future of farming; but what are the concerns, where are the links and how, if at all, can the concerns be alleviated?

The five top ranked concerns in order are:

1. Future of subsidies
2. Environment, climate change and weather
3. Cashflow
4. Price volatility
5. Tax

One of the main linking factors between 1, 2 and 4 is the impact they have on profitability. Profitability then impacts cashflow (3) and inevitably tax (5).

There is no golden bullet to resolve the issues facing UK farming - but things such as being prepared for change, being in a position where you understand your businesses strengths and weaknesses, knowing where your breakeven point is, will all help you make and implement sound, informed decisions.

As yet, there is no clear guidance on future subsidies and what will be required to qualify for these. We know it will not be 'money for nothing' and with the significant

emphasis on the environment and climate change there will be opportunities for some, but not all farmers.

By ensuring your bookkeeping records allow you to identify your costs of production for each enterprise you run, you can start to balance out your cashflow requirements against profitability and price volatility. Some of the areas to think about include:

- What is the minimum price required to make a profit?
- When do you need cash and how much?
- When do you have significant outgoings?
- Can/should you forward sell?
- Do you need a seasonal additional overdraft facility?
- Do you need new plant and machinery, if so, when should you buy?
- What are the tax implications?

Many farmers suffer from sleepless nights, not only due to calving and lambing! Having a clear strategy, backed up with a business plan and accurate accounting records will at least provide peace of mind that you know where your business is doing well and where there are challenges to be resolved.



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Meet our team

A Q&A with Manager in the Farms and Estates team, Daniel Webb.

WHAT IS IT LIKE BEING AN ACCOUNTANT IN THE AGRICULTURAL SECTOR RIGHT NOW?

The agricultural sector is renowned for trading ups and downs. In the last 12 months, except those businesses which have diversified into hospitality, farming hasn't been as dramatically impacted by COVID-19 as many sectors. The main concern for farmers is more often than not, the weather and 2020 was no exception! The poor weather throughout late 2019 and early 2020 severely affected both forage and arable yields, many clients saw their 2020 arable crops drop by 50%. To support our clients with this, we helped with forecasting profits or losses, and where possible, reducing tax payments on account for 2021.

WHAT DOES THE FUTURE LOOK LIKE IN THE AGRICULTURAL SECTOR?

Farming is always challenging. One of the longer-term issues farmers and landowners are grappling with, is how they are going to replace the income lost by the phasing out of the basic payment scheme. With the first reduction due December 2021, the scheme will be phased out entirely by 2027, and could dramatically reduce profit unless alternative income streams can be found.

The good news is that 2022 will see the introduction of the new environmental land management scheme (ELMS). This will focus on sustainable farming incentives, local nature recovery and landscape recovery.

It is difficult to know exactly what impact ELMS will have, there are likely to be some winners and losers. We expect to see new diversification projects, and perhaps a change in working practices. The younger generation of farmers and landowners that we speak to are definitely seeing the

opportunities ELMS could bring. There is a potential shift to some more traditional working practices, perhaps a reduction in fertilisers and sprays, and more consideration for the impact of farming on the land. It could be a really exciting time for farming and agriculture.

TELL US SOMETHING THAT WE MIGHT NOT KNOW ABOUT YOU?

I used to have my own pet cow called Boris. I have no idea why I called her Boris, I bottle reared her from two days old after her mother rejected her. Everyone who came to the farm knew her and she would come running when I called her!

WHY DO YOU WORK IN THE AGRICULTURAL SECTOR?

Farming really is in my blood; I grew up on a farm in the Cotswolds where my dad is a farm manager. I knew from a young age I had a love for numbers and being able to combine that with my passion for all things farming is the perfect scenario.

WHY HAZLEWOODS?

I love the people in our team and this has become more evident in the last 12 months. Work is far more interesting when you are in the office, sharing ideas and discussing challenges with like-minded people. Working with our clients is also great; I'm not sure I would be an accountant if I didn't work in the farming sector.

If you would like more information on BPS and ELMS or other business advice, please get in touch with Daniel Webb at daniel.webb@hazlewoods.co.uk or 01242 680000.



MEET THE TEAM



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