CHARTERED ACCOUNTANTS, TAX CONSULTANTS & FINANCIAL PLANNERS

ALBERT GOODMAN

AG RURAL INTELLIGENCE SUMMER 2016

WELCOME

The 23 June 2016 will be etched into our minds for many years as the date that the UK decided to leave the EU. The vote was close, however the great British public have spoken and our politicians will now be negotiating an orderly exit from the European club, if it is possible to leave in an orderly way.

For farming businesses, there are major changes looming on the horizon, with more questions than answers. My view is that, in the short term, there may be a devaluation of sterling. This will have the effect of increasing commodity prices for farmers. So, from a very low value, there may be some good news. How strong the pound gets in the long term, will of course depend upon the world view of the changes made to the UK economy as we exit the EU.

In 2015 we exported £14 billion of food and non-alcoholic drink. Four of our five biggest customers were in the EU, being Ireland, France, Netherlands and Germany. Now that we are on our way out of the EU club, we must work harder than ever at Government level to make sure that these exports are not diminished. I urge the farming lobby groups to speak loudly and make sure that we can continue to export goods without tariffs.

Farmers must also look at their export markets and make sure that we are producing the type of food that both UK and exporters can sell. Our world is getting more competitive and looking forward, it is the producers who continue to adapt to the market place that will succeed.

In this issue we have two articles about VAT. VAT is a European tax, and some of you may be forgiven for thinking that this will disappear. VAT accounts for about one-fifth of UK government income. Whilst we may see some changes, VAT in some form will be here to stay. Therefore the VAT points made in this newsletter remain important.

Finally, the politicians promised, that UK farmers will still be supported when we leave the EU. Watch this space to see what this means. This is an ideal opportunity for farmers and the Government to look at which parts of agriculture should be supported and how this is undertaken. Is it too much to ask for some radical reform, which will both help UK agriculture and the public perception of farmers? Whatever happens there are some interesting times ahead.

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MAXIMISING CASH FROM ASSET SALES

Now that Basic Payments have been received by most, harsh realities mean that for many farms cash flow will become increasingly difficult.

Many will be considering the sale of some off-lying or "non-core" assets such as cottages, land or old buildings to realise cash. The merits of such a decision can and should be very thoroughly debated and it is important that advice is taken about the consequent tax liability.

Capital gains tax (CGT) is the tax on the increase in value of an asset between the time it is acquired and the time it is disposed. With land price increases over the last ten years the capital gain on land sales is often substantial. Gains on commercial property are charged at 10% in the basic rate band and 20% within the higher rate band. Residential property gains are taxed at 18% and 28% respectively. Relief from CGT should be considered early on.

Entrepreneurs' relief

Where qualifying gains are chargeable to tax at 18% or more it is beneficial to make sure entrepreneurs' relief (ER) applies to reduce the tax rate to 10%.

Where only part of the farm is being sold qualifying for ER is more problematic. Planning for the sale to ensure crucial steps are put in place at the right time around exchange of contracts is vital.

Even if the whole farm is being sold, the timing of the sale of the property in relation to the cessation of the business is critical to ensure the sale qualifies for ER.

The savings with ER are usually substantial, typically halving the capital gains tax bill.

Brought forward losses

Where assets have been sold at a loss in previous years or where purchased milk quota was held prior to its abolition last year, these losses can be used to offset future capital gains.

Part disposals

Where part of the farm is sold and part is retained there are special rules for calculating the capital gain on the part disposed. This provides an opportunity to use one of two alternative methods to calculate the gain which may reduce the overall tax payable.

In addition, where the gain qualifies as a small part disposal the sum received is deducted from the allowable cost of the retained part going forward, effectively deferring the tax payable until the retained asset (remainder of farm) is sold.

Main residence & lettings relief

For those selling residential property, which has been their main residence during their period of ownership, relief will apply which can relieve all or part of the gain. In addition if all or part of the property has been let during the period then lettings relief can apply.

For tenant farmers who are required to live in the tenanted farmhouse under the terms of the tenancy, and for those employed and in job related accommodation, if they own a residential property and intend to live in the property in due course, main residence relief can exempt the gain on a future sale, even if they have never actually lived in the property. This relief is often overlooked and advice will be beneficial to ensure the relief applies and is claimed correctly.

Rollover relief

Finally, where land or buildings, which have been used in the business, are sold and there is an intention to reinvest the proceeds into new assets used in the business, the gain on the sale of the old asset can be deferred until the sale of the new asset. The new asset will need to be purchased within either a year before the sale of the old asset or three years afterwards. One often overlooked point with rollover relief is that it is the sale proceeds that have to be reinvested not the amount of the capital gain. Again timing and the amount reinvested is crucial so advice is required.

The difference between good planning and no planning can be substantial in relation to the sale of assets and the consequent CGT charge so take advice to minimise the tax liability.

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MAKING PENSIONS CONTRIBUTIONS IN LATER LIFE

Much of the focus in the media, since the passing into law of the Taxation Of Pension Act 2014, has been on the potential personal tax charges individuals can incur when they breach the Annual and/or Lifetime Allowances.

However, one of the most welcome reforms to pensions is ability to now preserve a pension fund for children and grand-children, as well as for spouses and financial dependants. In effect, an individual's pension fund can pass 'down the generations', entirely fee of Inheritance Tax (IHT).

Pension contributions still benefit from income tax relief at the individual's marginal rate, or a deduction for corporation tax, where paid by a company. With the gross pension contribution reducing the value of the individual's potentially 'taxable' estate', there are now a number of compelling arguments for making a £40,000 annual pension contribution, especially now that those aged 55 and above have 'unfettered' access to their pension fund, under so called flexi-access drawdown.

Many business owners and their professional advisers are aware that pension contributions at this level can be made right through to age 75 potentially, however very few realise that it is possible to carry on making pension contributions beyond age 75, potentially for life.

There are however some provisos, as follows:

- Not all Pension Trusts allow pension contributions to be received, post age 75.
- Pension contributions made at or after age 75 will not be tested against the Annual Allowance.
- Pension contributions made at or after age 75 will not be tested against the Lifetime Allowance.
- Pension contributions made at or after age 75 do not benefit from income tax relief.
- Those making pension contributions at or after age 75 will, we understand, need to live for 'at least' two years, from the date of the contribution being made, for it to be ignored for IHT purposes.

Unsurprisingly therefore, more and more older people are starting to view their pension fund as more of a family trust, building its value as much as possible during their retirement and only calling upon the funds as a last resort.

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FARMERS' AVERAGING - CHANGES

Following a period of consultation the Finance Bill 2016 has introduced changes to the farmers' averaging rules from the 2016/17 tax year, affecting all of those with year ends finishing after 6 April 2016.

The headlines and sentiment here were positive with the Chancellor apparently doing his bit to support the farming sector at a difficult time. As a result many believe that in giving farmers a choice to average over two tax years, as is the current position, or to average over five years, there would be significant tax savings and repayments of tax.

It is clear that no-one loses out from the changes as you can still use the previous rules and the changes are a significant extension to the previous arrangements. As a result of this we will be better placed to try to ensure that farmers are not penalised by paying tax at higher tax rates in the isolated very good year.

However, the expectation of a significant tax windfall or significant additional tax savings going forward should be tempered. Initial calculations indicate that for many there will need to be very large fluctuations in profits to offer real savings and we believe that for many of our farming clients the existing two year averaging already met their tax planning needs.

Furthermore it is clear that, from a practical perspective, five year averaging calculations will be complex and time consuming and could provide little or no additional benefit.

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VAT & OPTIONS TO TAX

VAT is one of the most complex taxes we have. Anthony Barber the Chancellor of the Exchequer said that VAT would be a "simple tax" when he oversaw its introduction in 1973. How the world has turned since then.

As part of the expansion of the tax, the Option to Tax land and properties was introduced in 1989.

VAT is a self-assessing tax applied to business transactions that take place (in the main) in the UK. The VAT rates that exist today are 0% zero rate, 5% reduced rate and 20% standard rate. These rates are called "taxable rates". If a business has net taxable income in any 12 month rolling period that exceeds £83,000, then it must register for VAT.

Provided that the business sells its goods or services at any of the taxable rates, it is entitled to reclaim VAT on all its business expenditure.

There are some sales which are not subject to VAT; these are exempt from VAT by law. These include finance, education, health and welfare, insurance, sport, charity fund raising, postage, burials and cremations etc. It also includes specific land and property transactions.

If a supply is exempt from VAT, no VAT is being charged to the customer and, therefore, nothing is paid over to HMRC. As HMRC get nothing on the sale, any VAT incurred on expenditure/costs related to the exempt sale is not recoverable. (If a business has both taxable and exempt supplies please see our Spring Newsletter on partial exemption).

The Option to Tax is a declaration mechanism that allows a business to add VAT to the supply of non-residential land or property. By adding VAT to the land or property, VAT is charged on any sale/lease of the land which is paid over to HMRC. As HMRC are receiving VAT on the sale, it is permissible to claim VAT on expenditure/costs on a VAT return.

An Option to Tax is a voluntary declaration – you do not have to add VAT to the land and property unless you really want to.

Why Opt to Tax?

Imagine you were considering selling a piece of bare land. You feel it would be beneficial to get planning permission to build houses on the land so you could sell it at a better price. If you sold the land exempt from VAT i.e. no VAT charged on the sale, HMRC would not allow the VAT on your costs to be recovered.

If you declared an Option to Tax, the sale would be made with 20% added to the price which is ultimately paid over to HMRC. Due to the Option to Tax being made, HMRC anticipate receiving the VAT so, in the meantime, you can claim VAT on expenditure/costs.

If you sold the land to a developer, you would charge him VAT which he should be able to recover from HMRC.

When might an Option to Tax not apply?

There are occasions when an Option to Tax can be "disapplied" or cancelled. These can cover sales to housing associations, leases to charities, sale of commercial properties destined to be converted to residential properties, sales between connected parties etc.

It is important to examine each case to ensure that, if an Option to Tax is made, it can stay in place to enable VAT recovery on costs.

How do I make an Option to Tax?

A particular form VAT 1614A is completed and submitted to HMRC. It may need additional material to accompany it such as proof of ownership, evidence of the owner's intention, VAT registration etc.

If an Option to Tax is something you would consider, get professional advice from a VAT expert.

Who makes the Option to Tax?

The freehold owner, the head lease holder, the sub lease holder, the beneficial owner etc – whoever has a legal "interest" in the land or property makes the Option.

How could this affect me?

If you are planning to sell a piece of land or a property, you need to weigh up whether you are going to incur significant VAT on costs. Are you going to apply for planning permission? Are you going to put in a new road access? Are you laying in new infrastructure?

Also who is the potential buyer? If you have a housing association interested, any Option to Tax you make may be cancelled out and you need to renegotiate the price to account for any VAT you cannot claim.

If you are considering selling your property rental business of small industrial units, you need to establish if VAT is due on the sale. Did you get charged VAT on the building of the units, have you Opted to Tax the units, are you charging VAT to your tenants, are the tenants to remain once you sell the entire site, is the buyer VAT registered – if the answer is yes to these questions, your sale could be entirely VAT free PROVIDED the buyer Opts to Tax the site.

Other scenarios that may be relevant surround the construction, renovation and refurbishment of rental properties which may incur significant input VAT. This may not be recoverable unless an Option is in place; but, if an option is made, any subsequent rental income will become VATable.

The Option to Tax is a complex beast and needs careful consideration if you are buying or selling property – VAT is no longer a "simple tax".

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CHANGES AHEAD FOR TAX RELIEFS FOR RESIDENTIAL LANDLORDS

The Summer Budget 2015 included three significant announcements of relevance to residential property landlords. These are likely to have far-reaching implications for many property investors, including farmers and estates with surplus farmworkers' cottages which are let out.

Relief for landlords' finance costs: loss of tax relief

The most significant change is the reduction in income tax relief residential landlords will be able to claim on finance costs. Most critically finance costs include interest on loans to purchase or carry out work to a let residential property, but the term also extends to mortgage arrangement fees, and interest on loans to buy furniture or fixtures.

The measures will apply to most residential landlords who are subject to income tax on their property income, including trusts and personal representatives, the exception being furnished holiday lets. The new rules will not apply to commercial property or to companies charged to corporation tax.

For the residential landlords affected, the new rules will restrict relief on finance costs to the basic rate of tax, and will be phased in over a four-year period from 6 April 2017 (the 2017/18 tax year) at the following rates:

Tax year	Finance costs - full relief	Finance costs - Finance costs -
2017/18	75%	25%
2018/19	50%	50%
2019/20	25%	75%
2020/21	0%	100%

For example, a higher rate taxpayer receiving rental income of £15,000 and incurring finance costs of £5,000 will receive tax relief of £1,750 in 2017/18. Before the changes, they would have received tax relief of £2,000, a cash reduction of £250.

The way in which the basic rate relief is given will create complexity where non-investment income and/or property income are low compared to financing costs, and will result in some finance costs not attracting relief in the year in which they are incurred. However, relief for any excess finance costs may be carried forward to the following years.

Rent-a-room relief in your own home

Rent-a-room relief has remained frozen at £4,250 since 1997. This relief has increased to £7,500 from 6 April 2016 onwards, and applies to income from letting out furnished accommodation in your home. The relief is halved if the property income is shared with a partner or someone else. You can let out a room or an entire floor. You can opt into the scheme at any time if you are a resident landlord, whether or not you own your home, including if you run a bed and breakfast or a guest house

Wear & tear allowance

This allowance was abolished from 6 April 2016. At present it is understood that a new relief will allow a deduction based on the actual costs of replacing furnishings, known as Replacement Furniture Relief, and will be available to all residential landlords whether the property is furnished, partly furnished or unfurnished. The cost to buy the original item is not expected to be allowable.

The type of items will be limited to those used by tenants. Certain items are deemed to be part of the fabric of the property itself (e.g. baths, toilets, boilers and fitted kitchens), and it is expected that replacement of these will continue to be treated as a repair to the property itself.

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STABLING & LIVERY ACTIVITIES - VAT

Whether your business activities are full time within the equine sector or you have buildings on your farm that are used to house horses, the VAT implications for the income you receive and the expenditure you incur in connection with these activities needs to be considered.

If you provide stabling only and the horse has its own allocated area for its exclusive use then the income received is exempt for VAT purposes. If there is no designated area or exclusive use then the income becomes liable to VAT at the standard rate.

It is commonplace for additional services to be provided alongside the stabling, for example mucking out, feeding and turning out the horse to graze. The VAT position of these services will generally follow the VAT

treatment of the stabling income; if it is exempt then the livery services will follow that treatment.

As with all taxes there are always exceptions, if you are a business that schools and breaks horses in, a racehorse trainer or a stud farm then the stabling and livery services provided to those horses will always be chargeable to VAT at standard rate.

There is also the option to change the treatment of the stabling and livery income so it becomes subject to VAT at the standard rate by choosing to 'opt to tax' the buildings where the horses are stabled. (See earlier article).

Most providers would prefer their stabling and livery income to be exempt but this does then impact on the business's recovery of input tax (VAT on costs) incurred on its purchases and expenses.

If you are already VAT registered any exempt income creates a partial exemption issue which could mean that the VAT incurred on costs relating directly to the stabling and livery cannot be claimed. In addition this could also lead to a restriction in the recovery of the VAT incurred on overheads depending on the values involved. The loss of input tax could be substantial if you were planning to upgrade or build more stables. (See Spring newsletter article).

If you are in the position to choose between having an exempt or standard rated source of income you will need to decide on the most VAT efficient course of action to take.

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ARE YOU MISSING OUT ON TAX CREDITS?

According to statistics, more than 1 million people in England, Scotland and Wales who are eligible for working or child tax credits don't currently claim their entitlement.

Tax credits have received some bad press over the past few years with some households having to pay back significant sums of overpaid credits. Largely this is due to fluctuating incomes within households as current years' claims are paid based on the previous year's income. When the current year income is finalised, the claim must be adjusted up or down accordingly. With careful management these overpayments can generally be avoided.

Broadly, you will be entitled to claim some form of tax credits if you fall in to one of the following groups:

- A parent/parents and your household income is up to £47,000 per annum (or up to £73,000 if you are paying for childcare).
- You are a couple who are both working with household income of under £18,000 per annum, even without children.
- You are single with no children and are working earning under £13,000 per annum.

Tax credits will soon be superseded by the new universal credit system. This is being rolled out in phases and is already in place for single, unemployed new claimants. The new system should be fully implemented for all claimants by June 2018.

If you are already claiming tax credits when the universal system comes in to force, and your claim under universal credits would result in a lower payment, transitional protections are in place to ensure you continue to receive the higher tax credit amount until you have a change of circumstances. If you are claiming tax credits and would receive a higher amount under the universal credits system you will be able to move to the new higher payment straight away. Providing you make a claim as soon as possible, this is a win win situation and everyone who thinks they are eligible should check now.

For those with fluctuating incomes year on year, making a protective claim is also important to ensure you do not miss out on credits when you have a year with particularly low income. This could be particularly relevant to farmers in the current market.

If you are unsure whether you are entitled to make a claim, or how to make a claim, please get in touch.

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GRAZING LAND QUALIFIES AS A BUSINESS ASSET

For those that read our newsletter regularly and come to our seminars you will have heard me discuss the risks associated with farming arrangements such as grazing licenses, share farming and contract farming agreements.

There has now been a case heard at the First Tier Tribunal which has found in favour of the taxpayer. In John Carlisle Allen v HMRC [2016] TC05100 it was found that the grazing land qualified as an asset used in the business of Mr Allen and as such qualified for business taper relief for capital gains tax purposes.

The land amounted to around 10 acres and was let to a neighbour for seasonal grazing and silage from March to November every year. However Mr Allen supplied the fertiliser and water as well as engaging contractors to control the weeds annually. Mr Allen also inspected the land and kept some animals for grazing in the winter.

A further feature of this case was that, throughout the year, other members of Mr Allen's family and a company in which Mr Allen was a minority shareholder used the land for temporary housing of animals which had been sold at the livestock market but which for various reasons could not be immediately removed by the buyers. The effect of this was that the neighbour did not have the land entirely to himself and shared occupation.

As a result of the above it was held that Mr Allen was in occupation of the land for the whole year and, due to his activities of husbandry, it was held that he was occupying the land for the purposes of husbandry by keeping the land in a good state of condition and fertility.

Whilst this case was in relation to business taper relief, a relief which has now gone, it is relevant for entrepreneurs' relief, inheritance tax business property relief and agricultural property relief on the farmhouse.

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WE ALSO DO THIS – CLOUD ACCOUNTING

What is Cloud Accounting?

Think about when you use internet banking. Every time you access this data, you're using the cloud. The cloud is a platform to make data and software accessible online anytime, anywhere, from any device.

You can use cloud-based software from any device with an internet connection.

Cloud accounting means you can stay connected to your data and with us.

Why move to Cloud Accounting?

The benefits of Cloud Accounting compared to traditional (desktop) accounting software include:

- It's quicker and easier to stay up to date with your bookkeeping - you don't need to wait for the bank statement to arrive in the post because you don't need to enter the bank transactions – they can be fed directly into the cloud system.
- No more expensive upgrades or down-time whilst the system installs updates - cloud software is updated live at no extra cost.
- Your data is automatically saved remotely, so you don't have to take back-ups.
- You can integrate and build your own solution by linking with customisable add-ons and additional modules and features
- No large annual payment for the licence – cloud software offers various packages on a monthly subscription.
- By 2020, most businesses, self-employed people and landlords will be required to keep track of their tax affairs digitally and update HMRC at least quarterly via their digital tax account. These changes will be introduced for some businesses from April 2018, and will be phased-in by 2020, giving businesses time to adapt. Cloud Accounting packages will link directly with the HMRC system making it easier to comply.

How can Albert Goodman help you and your business with Cloud Accounting?

We have staff who are certified using Xero, QuickBooks and Sage. We can get easier access to your systems making it easier for us to help and advise you.

At Albert Goodman we know about agriculture and we know about Cloud Accounting - talk to us to discover the best Cloud solution for you and your business…

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Contributing most to our clients' success

Our aim is to work closely with our clients. Our practical agricultural knowledge, accounting and tax expertise and enthusiasm mean that we are well placed to do this. We believe that we bring a proactive approach and fresh perspective to our clients' businesses. This means that we can give the best possible advice, enabling businesses to have the most suitable structure, pay the least amount of tax and effectively plan for the future.

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