Ellacotts

AGRICULTURAL NEWSLETTER
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Incorporation?

As more farms and rural businesses diversify, we frequently discuss with clients the merits of holding the new activity in a company. Typical motivators are:

- Limiting shareholder liability - although directors can risk criminal or civil penalties if things go wrong.
- Minimising tax liabilities - rates of Corporation Tax (19%) being well below Income Tax rates of 40-45% plus National Insurance Contributions.

There are, however, many other factors to consider:

- Whether or not premises transfer into the company needs careful consideration. If premises remain outside, take tax advice regarding any rent paid. If transferred in, will Stamp Duty Land Tax be due?
- The bank must be consulted early on and, if there are borrowings, a formal tenancy over personally owned property may be required to reassure the bank, and perhaps charges and personal guarantees.
- Careful cashflow and tax planning is needed to ensure cash is available in the desired/intended hands at the right time, without suffering excessive rates of tax.
- Advice may be needed regarding the VAT position of any property.
- Transferring assets into a company with the same ownership does not usually trigger an Inheritance Tax liability.
- As an employee/director of the company, it should be possible for the company to make pension contributions (subject to limits) to a registered fund irrespective of the salary level. In contrast, pension contributions are a private expense for sole traders or partners with relief claimed on personal tax returns. Where income is from non-trade sources (e.g. property rental), a company can offer greater scope for pension contributions.
- A business owner may move funds to and from an unincorporated business without tax implications. When a company is involved there may be tax implications of these transactions, particularly if the company lends to the director. If the director lends to the company, interest can be charged.
- The share structure of the company offers various tax planning opportunities to ensure tax efficiency now and in the longer term.

If an existing trade will cease, to be carried on by the new company, more factors come in to play:

- Can tax efficient payment of mixed business/ private costs be made without having to report cars and other costs as Benefits in Kind? This would trigger Class 1A National Insurance Contributions and Income Tax on the employer and employee respectively.
- Future profits and losses are within Corporation Tax rules, not personal Income Tax, restricting offset. Unused personal losses cannot be carried forward to offset against future company results.
- There is some flexibility surrounding the value at which plant and machinery transfers into the company for tax purposes, and similarly trading stock.
- Will the transfer of trade trigger a Capital Gains Tax liability? If so, there are reliefs potentially available which defer the Capital Gains Tax.
- The date the old business ceases could have significant impact on personal Income Tax positions, due to Overlap Relief.
- The company will survive the death of any particular director or shareholder, enabling long term planning and greater commercial credibility.
- Effective ownership of the business may be more readily transferred, and shared across the wider family, perhaps using different classes of shares and a formal shareholder agreement to optimise the tax position and also ensure clarity and fairness.

There may be a number of good reasons for considering using of a company as part of a tax planning strategy. However, as you can see there are many factors to consider. We would welcome the opportunity to talk to you about your own specific circumstances. Please speak to your usual Ellacotts contact.

When grain storage qualifies for tax relief

In our last edition, we explored the increase in the Annual Investment Allowance and how, with careful planning, businesses can maximise the benefits of the allowances available. This planning requires not only attentive timing but also consideration as to what assets the business requires, ensuring the assets chosen qualify as expected. Do consider tax early on as an important part of your project planning.

An area that causes confusion, where capital allowances are concerned, is grain storage. In May 2019, the First-Tier Tribunal (FTT) decided that a horizontal grain silo qualified for plant and machinery allowances. Whilst decisions of the FTT do not generally create a binding legal precedent, the areas examined in this case are useful in determining what extent other grain storage facilities qualify for plant and machinery allowances.

Most grain drying facilities, at first glance, appear to fall onto excluded lists whereby HMRC explicitly note the expenditure does not qualify as plant and machinery. Capital Allowances Act 2001 'Section 21 - List A' covers assets treated as buildings (floors, ceilings, stairs, etc.) and 'Section 22 - List B' covers excluded structures (a fixed structure of any kind, other than a building).

HMRC also provide a list of expenditure unaffected by sections 21 and 22. 'Section 23 – List C' covers various expenditure but most notably, the ones of interest to many of our clients are:

- Partition walls – where movable and intended to be moved in the course of the qualifying activity
- The provision of silos provided for temporary storage
- The provision of slurry pits or silage clamps

In all of these situations, the asset meets another test. It performs a function. HMRC accept that a grain silo is more than a structure. HMRC's manual CA22050 states 'treat a grain silo as plant where, together with its attendant machinery, it performs a function in distributing the grain so that it acts as a transit silo rather than a warehouse'.

The word 'silo' is not defined in HMRC legislation and so it is highly likely that HMRC will continue to challenge where the total cost of constructing a grain store is claimed as plant. Items such as driers, fans and pedestals are undeniably plant whilst other elements such as grain panels can fit within the 'partition wall' definition and be deemed plant. Only where the very structure of the building is integral to the success of the operations carried out, are HMRC likely to agree the building is plant.

Income Tax relief through capital allowances is one way grain stores can be tax efficient but all is not lost if the definition of plant is not met for capital allowance purposes. Grain stores also present a good Rollover Relief opportunity to minimise exposure to Capital Gains Tax where qualifying assets have been disposed of. Using a pension fund to construct a grain store can also be extremely tax efficient.

If you are considering investing in grain storage, our team will be happy to discuss the possible taxation benefits available to you and your business.

Farmers' Averaging – Are you taking full advantage of this relief?

You may have heard of Farmers' Averaging but not be aware of exactly what it is or what it can mean for you and your business. Averaging is a tax relief which can be applied to farming profits as long as certain conditions are met.

Farmers' Averaging works by allowing you to restate profits of either the last two or five years as the average for that time period. This allows you to flatten out the profits over the period and potentially reduce your tax liabilities. You can choose which averaging option to use each year depending on what gives the best tax saving.

If we take an example of a farm's profits over a five year period:

Tax Year	Profits (£)	Averaged Profits (£)
2018/19	50,000	37,400
2017/18	37,000	37,400
2016/17	37,000	37,400
2015/16	35,000	37,400
2014/15	28,000	37,400

The 2018 harvest has produced a gross output per acre higher than the last five years, generally resulting in overall higher profits. Without using Farmers' Averaging this additional profit could take the farmer into higher tax rates of 40% or 45%. By using Farmers' Averaging we can make use of the lower profits in previous years to potentially reduce the tax burden considerably.

This is obviously a simplified example. The rules around Farmers' Averaging are in fact very complex. In a partnership, each tax payer is considered separately. Companies cannot claim Farmers' Averaging Relief. When averaging, losses are taken as zero, with losses considered as a separate exercise.

Factors to consider include:

- The order in which to offset both trading losses and Class 4 National Insurance losses
- The impact on previous historic loss claims
- Different trades and capping of loss restrictions
- Ability to make pension contributions and tax relief thereon
- The impact on student loan repayments
- Child Benefit and the High Income Child Benefit Charge
- The impact on tax payable on account

There is uncertainty within the industry as to how to apply the calculations and the implications of making a claim. H M Revenue and Customs (HMRC) have released very little guidance and in general current tax software struggles to cope with the variations and interactions with other reliefs.

Ellacotts are very experienced in dealing with these issues and have recently undergone a detailed review with HMRC regarding Farmers' Averaging calculations. This dealt with many of the issues listed above. HMRC agreed all our calculations, resulting in our client receiving a very significant tax repayment.

Please contact us if you'd like to make sure you're taking full advantage of this relief.

Benchmarking – 2018 harvest

An early indication from clients' year end accounts

We are currently preparing 2018 harvest gross margin accounts for our arable clients. An early indication of how the 2018 harvest compares with 2017 harvest, drawn from clients' year end accounts, is summarised below:

	Barley (per acre)		**Wheat** (per acre)		**Oilseed** (per acre)	
Harvest	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**
Yield						
Average	2.15t	2.47t	3.4t	3.5t	1.4t	1.37t
Ellacotts "Best in Class"	3.58t	3.6t	4.1t	4.41t	1.7t	1.87t
Gross Output						
Average	£336	£323	£560	£502	£470	£461
Ellacotts "Best in Class"	£535	£487	£676	£657	£561	£714

Taking a typical predominantly arable client's figures:

	2018(£/acre)	**2017**(£/acre)
Gross output	£414	£359
Variable costs	£164	£173
Gross margin	£250	£186
Fixed costs		
Labour and contract	£34	£45
Machinery and power	£155	£133
Property	£42	£34
Administration	£40	£32
Total fixed costs	£271	£244
Management loss before rent and finance	(£21)	(£58)
Rent	£32	£35
Finance	£29	£18
	£61	£53
Other income incl Basic Payment	£232	£218
Profit before drawings, tax etc.	**£150**	**£107**

Key trends:

- Early indications across all farms show lower yields for barley and wheat. Oilseed rape yields show a slight improvement. However, our top 20% have seen increases in yields across all crops. Significant increases in prices, especially for early harvest sales, have resulted in gross output per acre across all farms increasing by £55 per acre.
- Savings are being achieved across variable costs, mainly a reduction in spray costs possibly due to more spring cropping.
- Average labour, power and machinery costs have increased by £11 per acre to £189 but our top 20% have achieved a small saving of £4 per acre bringing their total down to £181.
- Currently we are seeing a conflict: average machinery repairs have increased to £27 per acre suggesting kit is being kept longer, however depreciation has also risen by £12 per acre due to investment in new machinery.
- The £8 per acre increase in property costs is due to building repairs suggesting money can be found for essential work around the farm.
- Administration costs have increased by £8 to £40 per acre, the rise is in professional and management fees showing farmers are looking at possible new projects as they plan for the impact of lower BPS monies in the coming years.
- We have already seen a small reduction in rents to an average of £32 per acre. The £11 increase in finance costs to £29 per acre is down to bank loan interest, due equally to new advances and the restructuring of long term debt.
- Other income has on average increased by £14 per acre to £232. There is an increase in mid-tier monies being received but this looks more likely to be due to late payment on previous schemes rather than an increased uptake of new schemes. Forage sales for our arable farmers have seen an increase of £10 per acre. We have noted a drop in receipts for renewable energy projects.
- Cash generated by farmers through farming and other activities has increased by nearly 25% to £206 per acre. This coupled with lower drawings has resulted in a cash surplus of £66 per acre. In harvest 2017 there was a cash deficit of £15 per acre.
- We are seeing that funding for new projects, business restructures and retirement plans is increasingly difficult to find. Finance providers appear to be asking for greater reassurance.

Events round up

In the past few months we have enjoyed seeing lots of clients and contacts at the Bedfordshire Young Farmers Rally, Kenilworth Show and Cereals.

We're pleased to announce the joint winners of our competition at the Bedfordshire Young Farmers Rally were Ian Northern and Tom Church.

We look forward to seeing more of you at the following events in the coming months:

Blakesley Show | Saturday 3 August
Maidford, Northamptonshire

Bucks County Show | Thursday 29 August
Weedon Park, near Aylesbury

Moreton-in-Marsh Show | Saturday 7 September
Moreton-in-Marsh, Gloucestershire

Expansion of the team

Ellacotts is delighted to announce the promotion of Joanne Wright to Partner from 1 June 2019. Joanne has been fundamental in growing Ellacotts Kettering office and expanding the specialist tax services available to clients.

John Thame said: "The promotion is very well deserved and is a reflection of Joanne's significant efforts, resulting in excellent client service and growing both the Agriculture and Property team and the range of services we are able to offer our clients."

Joanne said: "I am very excited about the future of Ellacotts and it is a privilege to be invited to be a Partner of such a progressive firm. It is great to be part of a team where I can make a real difference working with clients to achieve their goals and I look forward to helping grow the Kettering office further".

In a further strengthening of the Ellacotts Agriculture and Property team, we are pleased to have been able to promote Pip Cusack to Manager and Patrick Gardner to Assistant Manager.

Meet some of our team

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