Ellacotts

AGRICULTURAL NEWSLETTER
January 2018 edition

In this edition...

Inheritance Tax - the importance of regular reviews

Part of our role as trusted family, business and tax advisers is to regularly review with our clients their potential Inheritance Tax (IHT) positions. These reviews need to be regular because circumstances change - there can be changes to the client's "basket" of assets, or their use of assets, a change to marital status, health, a change in tax law, etc.

Meeting your own needs in life must come before worrying about tax, and looking after your potential beneficiaries. However, with a potential IHT charge of 40% on your estate, tax cannot be ignored.

It may be appropriate to consider giving an asset away to save IHT. However, gifts made within seven years of death can also accumulate back into the estate charged to IHT, so consider:

- Once gifted, you've lost control - divorce and other family issues are always a concern.
- The recipient could inadvertently increase the IHT liability by changing the tax nature of an asset - for example converting a farm barn into a home (and thus losing Agricultural Property Relief on the value gifted) or diversifying the business so far that H M Revenue & Customs will no longer consider it a trade (typically if rents in the business increase and farming activity reduces).
- Can you forego the income generated from the asset?
- For a gift to be effective for IHT, the donor cannot "enjoy" the gifted asset.
- There may be a Capital Gains Tax (CGT) cost to making the gift, unless the gift qualifies for any CGT relief.
- Gifts to Trusts can trigger lifetime IHT at 20%, depending on what reliefs may be available.

Insurance can be useful to cover the risk and IHT cost of a donor dying within seven years of a significant gift.

As a starting point, you may find it interesting to list out the market value of all your assets, deduct £325,000 (the Nil Rate Band available to everyone) and calculate your approximate IHT position at 40%. This is only a very simple approximation, but a useful place to begin.

We would then look with you at assets that either do qualify for Agricultural Property Relief or Business Property Relief, or could potentially qualify. Developing a strategy to "move" assets into the scope of these reliefs would be our next step.

Do ask us for advice before you consider buying or selling significant assets - typically property, or an investment in a business - so we can work with you to optimise your IHT position.

IHT can be saved by various planning tools, notably by making gifts, possibly using trusts, charitable giving, and by appropriate Will clauses.

There are several useful factsheets on the Ellacotts website www.ellacotts.co.uk. Your regular Ellacotts contact would be pleased to discuss your potential IHT position with you, and to work with your solicitor to review your Will and any associated business documents (typically Partnership Agreement, Shareholders' Agreement and perhaps Tenancy Agreements) to identify required actions, or perhaps just to give you peace of mind.

The 2017 Autumn Budget

Philip Hammond's first Autumn Budget proposals were generally taken as "dull but solid". Certainly, he seems to have avoided treading on any banana skins, such as the failed proposal in March to increase the rate of self-employed National Insurance contributions. Here are some key points that farmers and landowners may need to bear in mind as they plan for the coming year.

- Tax relief ("capital allowances") at 100% continues for equipment purchases up to £200,000pa. This is an important benefit for capital-intensive businesses such as farmers but timing of the expenditure is crucial to ensure tax relief falls into a tax year maximising relief.
- Entrepreneurs' Relief continues to reduce the Capital Gains Tax (CGT) rate from 20% to 10% for qualifying gains up to £10 million on trading asset disposals. The Chancellor has not changed the rules for this important tax relief and so it may still be possible to reduce tax on farmland sales if planning is done in advance. However, business owners should check carefully whether they qualify for Entrepreneurs' Relief, as this could be worth up to £1,000,000 in tax savings per individual.
- Stamp Duty Land Tax has been abolished on house purchases by first-time buyers who pay up to £300,000 and reduced for house purchases up to £500,000. This should provide some help for the next generation who want to live near the farm without relying quite so much on "The Bank of Mum & Dad"!
- The Inheritance Tax "nil rate band" increased by £100,000 from £325,000 on the value of family homes in April 2017. This may allow more wealth to be passed down to the next generation without tax being payable at 40%. The relief will also increase again by £25,000 in April 2018. However, the increase is restricted for estates valued at more than £2 million. This seems a generous figure but it is calculated before deducting agricultural and business property reliefs and so will rule out the benefit for many estates that include farmland.
- Until now, any company making gains on selling capital assets has been able to reduce the taxable amount by adding to the original cost an allowance based upon the Retail Price Index (RPI) between the dates of purchase and sale. This "indexation allowance" is changed for disposals of assets from 1 January 2018, so that the RPI increase will be frozen to the period up to December 2017.
- There is also a cloud looming for non-resident landowners who want to sell-up in the future. The Chancellor announced a consultation on CGT for disposals of immovable UK property from April 2019. There is already a CGT charge for non-residents who sell residential property and this looks like it will be extended to catch all UK land from 2019. The CGT charge will only apply to capital gains arising from April 2019 and it may be possible to claim Entrepreneurs' Relief or rollover relief for disposals of farmland. However, it will be important for non-residents with long-term UK land investment to review their tax position.

Pensions update

Since 2012, employers have had a legal obligation to enrol their employees into a workplace pension. Everyone should ensure they are maximising their own pension allowances and that their pensions are working hard enough for them.

At present, every person in the UK can pay £3,600 into a pension whether or not they are working. Workers can contribute up to 100% of earnings or £40,000, whichever is lower. This automatically triggers an immediate 20% tax relief on the contribution, regardless of tax position: a payment of £2,880 into your pension fund turns into £3,600. For a higher rate taxpayer, further tax relief is available via the tax return.

What could this mean for you?

- If you have missed a number of years' contributions, it is possible to 'mop' these allowances up, providing you have sufficient earnings to do so in the year of contribution. For example, if you have unused allowances from previous years of £50,000 and funds available:
  - First maximise your contribution for the current year. This requires a contribution of £40,000, demanding earnings of at least £40,000.
  - To maximise the use of previous years' allowances, current year earnings must be at least £90,000.
- Pensions remain one of the most tax efficient investments you can make:
  - the tax relief creates an immediate 20% 'growth';
  - funds are protected from Inheritance Tax until age 75 regardless of whether or not benefits have been taken.
- If you have a number of pensions with different providers, remember to keep track of how your funds are performing.
- If your family claims Child Benefit, you should also read the following article.

For a number of years, we have been reviewing clients' pension provisions and making recommendations with the aim of reducing charges and enhancing performance. Consolidating investment into one plan prior to retirement can also be beneficial: drawing benefits is simpler as there is only one provider to deal with.

If you would like to review your existing provision, please speak to your Ellacotts contact who will be able to help.

Dividends and Child Benefit - tax return implications

Due to two changes to H M Revenue & Customs' (HMRC) Self Assessment criteria, many individuals now need to complete tax returns if they receive dividends or Child Benefit.

Dividends

Due to the abolition of the 10% tax credit on dividends and the introduction of the dividends allowance by HMRC from 5 April 2016, many basic rate taxpayers are now required to register for Self Assessment and to complete a tax return for the first time.

If the amount of dividends received by an individual in the tax year exceeds the dividend allowance of £5,000 (for 2016/17), tax is payable on these dividends. Dividends are taxed as the top slice of income, after earnings and savings income. Tax rates depend on income, and will be 7.5% basic rate, 32.5% higher rate and 38.1% additional rate.

Child Benefit

If you receive Child Benefit, you may now need to complete a tax return due to the High Income Child Benefit Charge introduced by HMRC.

If you or your partner earn between £50,000 and £60,000 per year, the partner with the higher earnings is required to complete a tax return. At this income level Child Benefit is restricted and a proportion is repayable as Income Tax on the Self Assessment tax return.

If you or your partner earn above £60,000 per year, again a tax return will be required by the partner with the higher earnings. However, all of the Child Benefit will now be repayable as Income Tax.

These thresholds are after deducting pension contributions: as well as the Income Tax benefits mentioned above, making pension contributions could help you to retain your Child Benefit.

If you would like more information, or believe you may fall into either of these categories and would like to check, please contact us today.

Keeping the family silver - National Heritage property

HMRC are keen for the public to "retain and care for our heritage". Provided certain conditions are met, gifts of property that are important to the National Heritage, such as works of art, stately homes and land of public interest can be exempt from Inheritance Tax (IHT) and Capital Gains Tax (CGT).

National Heritage property includes:

- Pictures, prints, books, manuscripts, works of art, scientific objects or other non income-producing assets which appear to HMRC to be preeminent for national, scientific or artistic interest.
- Land of outstanding scenic, historic or scientific interest.
- Any buildings where special steps should be taken to ensure preservation, because of outstanding historic and architectural interest, together with any area of land that is essential to protect the character and amenities of such a building and any object associated with it.

There will be no IHT liability when a qualifying asset is passed down a generation on the death of the owner, provided the new owner agrees to meet the conditions set out by HMRC such as:

- Keeping the property in the UK, e.g. for works for art.
- Preservation of the property.
- Reasonable public access, e.g. display of works of art in a private house, long term loans to exhibitions in museums and galleries, access to stately homes and land. This cannot be confined to access where a prior appointment has been made.

The tax exemptions are conditional and, if the owner fails to deliver on the conditions imposed, the exemptions are withdrawn and the tax previously exempted becomes payable.

Where it is not possible for heritage assets to be kept within the family, there is an "Offer in Lieu" system; i.e. the asset is offered to the nation in lieu of the tax that would otherwise be due. This could leave the owner with a better net cash result than a "normal" sale at auction as no CGT is payable when an asset is disposed of.

The heritage property reliefs are potentially useful ways of enabling assets to remain in the family, when a significant IHT charge might otherwise prevent it. If you think it could apply to a family heirloom, please contact us to discuss your options.

Benchmarking the 2016 harvest

We recently held an event attended by over sixty farmers discussing the results of the 2016 harvest for our arable clients. We summarise below our findings and comments:

	Wheat (per acre)		Oilseed (per acre)	
	2016	2015	2016	2015
Yield				
Average	3.41t	3.9t	1.23t	1.6t
Range	2.64t - 4.11t	2.85t – 4.6t	0.8t – 1.75t	1.2t – 1.9t
Gross output				
Average	£445	£442	£404	£450
Range	£340/£567	£335/£615	£235/£660	£345/£590

Taking a typical arable client's overheads:

Key trends

- Higher yielding clients no longer necessarily generate greater management profit. Only about a third of our top management profit performers are also our higher yielding clients.
- The majority of our top yielding clients grow spring and winter wheat with oilseed rape as a third crop.
- Other income is increasingly significant and where opportunities exist, Ellacotts' clients utilise their assets well.
- Power and machinery costs continue to rise despite a drop in machinery reinvestment, as depreciation is replaced by repairs to older kit.
- Farmers are still experiencing cash flow issues and timely payment of the 2017 Basic Payment will be key for many farmers.
- The 2017 harvest, we believe, will show even wider variation between our clients with significant early crop sales and the improved prices currently on offer.

	2016 £/acre	2015 £/acre
Gross output	£392	£424
Variable costs	£213	£220
Gross margin	**£179**	**£204**
Fixed costs		
Labour	£38	£33
Power and machinery	£125	£150
Property	£31	£37
Administration	£30	£32
Total fixed costs excluding rent and finance	**£224**	**£252**
Management loss before rent and finance	(£45)	(£48)
Rent	£29	£32
Finance	£15	£19
Total rent and finance	**£44**	**£51**
Other income including Basic Payment	£182	£224
Profit before drawings, tax and capital repayments etc	**£93**	**£125**