Rural productivity: CIOT response

Inheritance Tax and trusts **OMB**

07 September 2021

CIOT was invited by the Country Landowners' Association to give evidence to the All Party Parliamentary Group for Rural Business and the Rural Powerhouse. The inquiry was to examine different aspects of the rural economy and assess barriers to productivity growth. Our submission addressed various aspects of the question: Does the tax system provide benefits or barriers to rural productivity?

Does the tax system actively encourage or discourage investment in a farming/diversified farming business?

The vast majority of farming businesses are operated as sole trades or partnerships but R&D tax relief is only available to limited companies. Structures and buildings allowances are not currently set at a sufficient level to encourage investment in buildings. The
'default level' £200k annual investment allowance (AIA) does not buy much in a reasonably sized modern farming business; the ability to carry forward/back unused AIA from earlier/later years would smooth out the years of heavy investment. Additionally, where a trust is one of the partners there is no AIA at all.

Farmers are discouraged from significant non-trading diversification (for example, letting redundant farm buildings for offices/storage or letting land for solar or battery storage schemes) because they risk the loss of inheritance tax (IHT) agricultural property relief (APR) on the part of the farmland affected.

A non-trading element can impact on the availability of other capital taxes reliefs: capital gains tax (CGT) reliefs rely on the whole being at least 80% trading; and IHT business property relief (BPR) requires over 50%. Furthermore, the Office of Tax Simplification
(OTS) suggestion that the BPR threshold might be increased to 80% would render many rural businesses ineligible for IHT relief on the entirety of their non-agricultural

value.

The limitations on assets available for CGT rollover relief also stifle innovative activity. A farm business that wishes to dispose of a surplus cottage and buy further agricultural land is dissuaded from doing so by the tax arising on the disposal of the cottage. A rollover relief based solely on the type of asset invested into – akin to an Enterprise Investment Scheme investment – would encourage investment in appropriate assets.

What aspects of the way that businesses must engage with the administration of the tax system, now or as contemplated by the digitalisation project, may hinder productivity?

The number of multiple returns required for a farm business even with only minor diversification is astonishing. Under Making Tax Digital (MTD), in addition to the various returns already required, there will be separate quarterly returns (plus the catch-up) needed for, say, rental income (as that has a 5 April basis period) and farming income (that will almost certainly have a different year end). (We note that this issue is intended to be addressed, at least in part, by the proposed changes to basis periods that was announced (with a consultation) on L-day (20 July), after our submission to this enquiry had been made.)

We said that not only is it frustrating that a farmer should have to file so many returns, but also the fact that some of those returns (for example, those relating to farm performance not taking into account crop valuations/contracting balances) are meaningless additions both to the discontent and the cost.

How can tax levers boost rural productivity?

It is likely that existing capital taxes reliefs encourage elderly farmers to ‘hang on until death’ rather than passing on to the next generation earlier when the younger person is more likely to be willing to take risks and innovate. Furthermore, there are many instances of the younger generation working for an inadequate reward in anticipation of inheriting the farm later. Passing on interests earlier would give security and avoid the growing number of ‘one day all this will be yours’ proprietary estoppel claims – a real issue, judging by the number of farming cases before the courts in recent years.

Diversification exacerbates that problem: there may be situations where the diversified assets do not qualify for CGT holdover relief and will only qualify for BPR if retained in the same ownership as all of the qualifying assets. Thus the elderly farmer may be driven by capital tax considerations to retain the whole business (and preferably non-diversified) until death. A real advantage in implementing the OTS recommendation to remove the CGT uplift on death, where the estate has 100% APR and/or BPR, would be to remove the major disincentive to lifetime succession planning.

Our full submission can be found at: www.tax.org.uk/ref810.