ON THE RIGHT TRACK

Summer 2022

- Taxation of solar energy
- Top tips for keeping the tax man at bay
- Taxation of woodland
- Promotion for Hayley

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CHARTERED ACCOUNTANTS

WELCOME

WELCOME TO THE 2022 SUMMER EDITION OF ON THE RIGHT TRACK. I AM GLAD THAT WE, I CANNOT SAY I, HAVE BEEN ABLE TO PULL TOGETHER ANOTHER ISSUE FOR OUR READERS.

Who would have thought two years ago we would still be talking about COVID, but hopefully we are winding ourselves out of the virus (I may have said something similar last year) but we all need to be careful and take care of each other.

What a year we have had, just when we thought COVID could do no more, we find ourselves in the midst of an energy crisis, war in Eastern Europe and a period of general inflation this country has not seen for many years.

The food crisis and the rising costs of inputs is unprecedented. We have seen significant increases in all inputs within the industry and this can only lead to a rise in outputs. The cost of grain is unlikely to fall within the next 2 years, the price of milk is being talked up to 50ppl and livestock prices must surely continue their upward trend.

All of this will start to put pressure on the finances of the business and it is very important that businesses monitor their current position and budgets ahead in order to identify those pinch points in the finances for the months ahead.

As a firm we are proud of our relationships with our clients and in these unsettling times, it is more important than ever that we maintain conversations and are available to support your business in the period ahead.

Kind Regards
Mark Griffiths

TAXATION OF SOLAR ENERGY

ALTHOUGH THE FEED IN TARIFF SCHEME CLOSED IN 2019 FOR NEW ENTRANTS, RECENT INCREASES IN ELECTRICITY COSTS, IMPROVEMENTS IN SYSTEM EFFICIENCY AND A WISH TO HELP THE ENVIRONMENT ARE INCREASING THE INTEREST IN SOLAR ELECTRICITY GENERATION, PARTICULARLY ON DAIRY FARMS, WITH THEIR HIGHER CONSUMPTION.

There are two different sets of tax rules, depending principally on whether the installation is domestic or commercial. The contract documentation will state the type of installation.

Domestic

A domestic installation is normally mounted on the farmhouse roof (occasionally in the garden) and provides electricity solely to the dwelling. The generation capacity must not 'significantly exceed' (HMRC interpret this as 20% more than) the home electricity consumption, so domestic installations are small scale.

- VAT is charged at 5% on domestic installations and this is not reclaimable.
- No capital allowances (or other income tax relief) can be claimed on the cost of the solar installation.
- Any income from a domestic installation at one's home is tax-free. This includes both sales of exported electricity and any Feed in Tariff.
- Any income from a domestic installation at a let dwelling is taxable (even though capital allowances are denied). The principal incentive for residential landlords is to improve the EPC rating (but your tenant will appreciate the lower energy costs).

Commercial

Installations on farm outbuildings (or in fields), which supply electricity to the farm (on its own or in conjunction with the house) or to multiple properties, are commercial.

Commercial installations are usually larger than domestic ones.

- VAT is charged at 20% on commercial installations and this is usually reclaimable (subject to similar considerations as for other business expenditure).
- Any income from a commercial installation is taxable.
- The cost of a commercial solar installation is eligible for capital allowances. HMRC regard solar installations as a long-life asset, which sometimes reduces relief. However, the installations do qualify for 100% Annual Investment Allowance (which is available for up to £1,000,000 of total qualifying expenditure by most standalone farming sole trades, partnerships or companies in the year ending 31 March 2023).

If you are considering investing in solar energy, we would be glad to further discuss the tax implications.

TOP TIPS FOR KEEPING THE TAX MAN AT BAY

OUR TOP TIP IS TO ENSURE THAT YOU HAVE THE MOST SUITABLE BUSINESS STRUCTURE AND THAT INCOME IS SHARED EFFICIENTLY; NOT ONLY BETWEEN SPOUSES, BUT ALSO WITH OTHER WORKING ADULT FAMILY MEMBERS WHERE APPROPRIATE.

Do's

Partnership structure can be very flexible:

- Profits can be shared across several family members to take advantage of each of their personal allowances and basic rate income tax bands.
- Losses can be set against non-farm income (e.g. employment or pensions).
- Younger partners can pay inexpensive Class 2 National Insurance Contributions to build future entitlement to state pension.
- Sharing profits across several family members can reduce or avoid higher marginal tax rates.

Farms are valuable, and farmers are understandably concerned about the financial risks (e.g. divorce) of bringing family members into partnership. Those risks can be managed by keeping the farm property outside the partnership business, or by putting in place a suitably tailored partnership agreement and land capital accounts where there is substantial value within the business.

We discourage farmers from spending money (e.g. on new machinery) just to save tax. However, there are occasions when investment is needed in the business, and some forms of investment can achieve generous tax relief.

- 100% Annual Investment Allowance is currently available on up to £1m of annual expenditure; not only on machinery, but also on functional fixed plant such as silos and slurry stores. Costs of (e.g.) concrete for those assets need to be clearly distinguished in the records from similar purchases for new buildings or for repairs.
- There is little tax relief on new farm out-buildings (Structures and Buildings Allowance is only 3% per annum), but costs of electrics, plumbing and other functional elements can qualify for 100% Annual Investment Allowance. These costs need to be identified separately from the building expenditure; we recommend having them separately identified in the invoicing and/or contract documentation.

To qualify for capital allowances, the legal liability to pay for an asset must have arisen by the year end – this usually means that the asset has to be on-farm (but it also has to be in use by the year end if purchased on HP). Having an order in with the dealer (even if invoiced) is not sufficient. Please beware also that any grant on the investment must be deducted from the cost eligible for capital allowances.

Occasionally, an individual might be entitled to a chargeable event gain on encashment of an insurance policy or, less commonly, a state pension lump sum. These have special income tax rules and it is sometimes advantageous to time them in a year when other income sources are lower. Please speak to us after you have found out your entitlement and before you commit to drawing it.

Although basic rate taxpayers usually do not see any reduction in their self-assessment tax liabilities, pension contributions have several income tax advantages:

- HMRC pay a tax rebate directly into the pension scheme, boosting your investment. This rebate amounts to one quarter of your pension payment.
- Higher rate taxpayers also benefit from a reduction in their self-assessment tax (usually another quarter).
- Making pension contributions reduces the income that is counted for both tax credit purposes and high income child benefit charge (HICBC). The effective tax relief on pension contributions can be very high in situations where there is a tax credit or HICBC advantage.

Please beware that an individual's payments into pensions in a tax year must be restricted to £2,880 or 80% of earned income, whichever is greater.

Don'ts

Tax legislation has mushroomed over the years and many anecdotal tax planning ideas no longer work; for example:

- Property income is defined in tax legislation, and it must be taxed on the person who has the legal right to it.
- For a different person to be taxed on (e.g.) holiday letting income, that different person must have a tenancy or a licence.
- To occupy the property.
- Be wary of agreeing to let out a property at an under-rent on condition that the tenant undertakes major improvements. In such cases, the landlord is taxable on the value of the improvement work.
- Special care is needed in considering whether a project is capital or repairs. Google Maps (which often provide clear satellite images at a selection of different dates) and on-line planning application records provide rich sources of information that are instantly available to HMRC if they choose to check them.

Retrospective planning

After the accounts have been prepared, there are still measures which will often help reduce tax liabilities or precipitate a larger repayment:

- Marriage allowance – If your spouse is not using their full personal allowance, they can transfer part of it to you, so long as you are a basic rate taxpayer.
- Farmer averaging - Often considerably reduces or delays tax.
- Where results have fluctuated over the years, we can sometimes manage taxable income at an optimal level with a combination of capital allowance restrictions, 5-year farmer averaging and optimal loss allocations. The interaction between these reliefs requires careful planning. It should also be noted that these reliefs are not available to taxpayers preparing accounts on the 'cash basis' (which we recommend that most farmers avoid).

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TAXATION OF WOODLANDS

WITH GROWING FOCUS ON ENVIRONMENTAL ASPECTS AND THE TRANSITION FROM BASIC PAYMENT TO ENVIRONMENTAL LAND MANAGEMENT SCHEMES, SOME FARMERS HAVE BEEN PLANTING FORESTRY, OR ARE CONSIDERING DOING SO. IT SHOULD BE NOTED THAT WOODLANDS HAVE A SPECIAL TAX REGIME.

Income tax

Proceeds from woodland timber sales are exempt from income tax. 'Woodland' means a sizeable area of land that is to a significant extent covered by growing trees of some maturity, height, and size.

The income tax exemption extends to forestry scheme grants, but not to farm woodland scheme grants (which HMRC regard as taxable compensation for lost farming income).

As new grants are introduced, it will be necessary to check whether they are tax exempt forestry or taxable farming income.

The income tax exemption does not cover:

- Property income from renting out a woodland.
- Trading income from ancillary activities, such as the processing of timber (e.g. planking or firewood), or the running of a shoot, motorsport or recreational activity in a wood.
- Short rotation coppice; i.e. the intensive cultivation of trees (such as willow or poplar), planted at high density, with the stems being harvested at intervals of less than 10 years. This is treated as a farming trade.
- Christmas trees grown specifically as a crop for sale.
- Timber income from farm trees or hedges, rather than a defined woodland area.

The woodlands income tax exemption is much less of an advantage than might be expected, because it also means that there is no income tax deduction for the costs incurred and, historically, many commercial woods have been loss-making; particularly when managed by paid contractors or employees. Capital allowances are not available on machinery for the tax exempt woodlands activity, nor income tax relief on the initial clearing and preparation of the land.

Capital taxes

For both capital gains tax (CGT) and inheritance tax (IHT), there is a crucial distinction between commercial and amenity woodland.

Commercial woodland is where the trees are grown to be sold as timber. This activity will incur regular operational costs and, on enquiry (e.g. in the event of a capital tax relief being claimed), HMRC would expect there to be records available of woodland management costs that were incurred over the years and not claimed for income tax deduction.

In the long term, there are major capital tax advantages in running woodland as a commercial activity.

VAT

Sales of timber (and Christmas trees) are standard rated (20%) for VAT.

Sales of timber for fuel are standard rated if sold to a merchant, but eligible for the reduced rate (5%) if marketed as firewood and sold directly to the end user.

The fact that timber sales are vatable has the advantage of supporting input VAT reclaim on the expenses of a commercial woodlands activity.

It is important that farmers consider the very different tax regime for woodlands at the outset. We would be glad to advise on the tax implications of your plans.

	Commercial woodland	Amenity
Capital gains tax	Capital gain on the timber is exempt Capital gain on the land is taxable, but may qualify for rollover, holdover or business asset disposal relief	Capital gains on the land and standing timber are taxable (but felled timber is usually exempt due to chattels relief) Business reliefs are not available
Inheritance tax	Land and standing timber qualify for Business Property Relief	Land and timber are IHT exposed (subject to any available Agricultural Property Relief), but the charge on the timber can be deferred until it is sold ('woodlands relief')

BPS LUMP SUM EXIT SCHEME

APPLICATIONS IN ENGLAND FOR THE LUMP SUM EXIT SCHEME HAVE NOW OPENED AND WILL RUN UNTIL 30 SEPTEMBER 2022. IT IS NOT EXPECTED THE SCHEME WILL REOPEN IN FUTURE YEARS. TO MAKE THE CLAIM YOU MUST SATISFY THE FOLLOWING RULES:

- Claimed or been eligible for BPS payments in the 2018 year, inherited agricultural land or succeeded to an Agricultural Holdings (AHA) Act 1986 tenancy after 15 May 2018.
- Transfer out land in England, which was agricultural land at your disposal on 17 May 2021 i.e. land claimed on the 2021 BPS application. This includes land you owned and farmed yourself or land farmed under a Farm Business Tenancy (FBT) or AHA. You can retain up to 5 hectares or any land entered into a woodland creation scheme.

You can transfer out land you own by selling it, gifting it or renting it out under a FBT with a minimum term or 5 years. The tenancy must not include a break clause within the first 5 years of the agreement.

For tenanted land you can transfer out by surrendering the tenancy to the landlord or being served a notice to quit, assigning the tenancy, succession under an AHA or expiry of the tenancy.

For sole traders you cannot transfer the land to your spouse/civil partner or someone you are cohabiting with. You may transfer the land to your son or daughter.

For partnerships or limited companies that have been making the BPS claims the partnership or company must also make the lump sum exit scheme claim. For partnerships a partner or partners with more than 50% individually or combined must leave the partnership. For companies a shareholder or shareholders who own more than 50% or the shares individually or combined must sell or gift their shares. The partners or shareholders must give up their interest in any agricultural land used in the business whether owned or on a tenancy. The land can be transferred to the remaining shareholders/partners in the business. The lump sum payment will be made to the partnership or company that must then decide how the money is allocated.

The lump sum will be calculated based on your average BPS claim for the years 2019 to 2021 (reference amount) multiplied by 2.35. The reference amount will be capped at £42,500, the maximum claim available is £99,875. Provided you are not affected by the cap the amount received under the lump sum should be equivalent to the amounts you could have received in direct payment from 2022 to 2027.

To receive the lump sum payment you have until 31 May 2024 to give up all of your English BPS entitlement and transfer out of the agricultural land. You can still claim BPS for 2022 and 2023 as protective claims in case you don't meet the rules for the lump sum exit scheme. You must meet the normal BPS rules in these years. If you are successful in claiming the lump sum payment any BPS payments for 2022 and 2023 will be deducted from the lump sum payment.

Subject to legislation being introduced it is intended the lump sum payment will be treated as capital in nature and subject to capital gains tax. For individuals this will be taxed at a rate of 10% or 20% (subject to circumstances and eligibility or Business Asset Disposal Relief) vs. 20% 40% for as income. The capital treatment will also apply to interim Direct Payments (2022 and 2023), which will be deducted from the lump sum payment amount once the scheme rules have been met.

LAST ORDERS

WE HAVE WRITTEN ABOUT THE MAKING TAX DIGITAL (MTD) REGIME IN ALMOST EVERY RECENT EDITION OF THIS NEWSLETTER, AND THE LAST ONE INCLUDED A 'FINAL REMINDER'!

Some VAT-registered farms have delayed acting because of low transaction volumes and values, and concern to avoid the ongoing extra cost of a cloud software subscription. According to HMRC, those businesses will be blocked from submitting VAT returns for periods commencing on/after 1 April 2022 if they do not become MTD compliant.

For most farming sole trades and partnerships, we recommend moving to cloud accounting software now.

Bridging software

For the smallest VAT-registered farms (e.g. where turnover is under £10,000 or likely to fall under that figure in the next few years), MTD compliance could instead be achieved by keeping the records on Excel spreadsheets and using special 'bridging software' to link each quarter's spreadsheet to HMRC's system.

Bridging software is lower cost than cloud accounting software (sometimes free) and there are many HMRC-approved providers (see **https://www.tax.service.gov.uk/making-tax-digital-software**). One example is Vital Tax (***https://vitaltax.uk/***), whose website has a useful demo that is worth viewing even if you subsequently choose a different solution.

Exemption

It is also possible to seek HMRC's permission to be exempted from the MTD VAT regime on grounds that it is 'not reasonable or practical for you to use computers, software or the internet to follow the rules for Making Tax Digital for VAT'. Details of how to opt out are available from **https://www.gov.uk/guidance/apply-for-an-exemption-from-making-tax-digital-for-vat**.

With most farmers already using computers for grant applications and/or livestock registrations, few VAT-registered farms are likely to qualify for exemption and we do not recommend applying if the MTD requirements can reasonably be met (e.g. with the assistance of a family member or bookkeeper). However, there are circumstances where exemption may be appropriate – e.g. elderly farmers who are not computer literate and who have neither internet access nor help available.

As ever, trying to beat the system by ignoring it is unlikely to succeed. Please speak to us now if you need help.

MOVING THE GOALPOSTS

IF, LIKE MOST LIVESTOCK FARMERS, YOU PREPARE YOUR ACCOUNTS TO 31 MARCH, PLEASE IGNORE THIS ARTICLE.

But, if your sole trade or partnership uses a different date (and 30 September is a popular choice for arable farms), please read on...

Existing position

Existing rules tax the profit of the accounts year that ends within the tax year. In other words, the profit of an accounts year to 30 September 2022 will be taxed in 2022/23.

Proposal

Government have indicated that, from 2024, the actual profit of the tax year (i.e. year to 31 March or 5 April) will be taxed. As a transitional measure, you will be taxed in 2023/24 on the profit of your traditional accounts period plus the profit between then and 31 March 2024. Thus, in the 2023/24 tax year:

- Farmers with a 30 September year end will be taxed on 18 months' profit (i.e. 1 October 2022 to 31 March 2024).
- Farmers with a 30 April year end will be taxed on 23 months' profit (i.e. 1 May 2022 to 31 March 2024).

For some farmers, this change could mean considerable extra taxable profit recognised in 2023/24, although any overlap relief will be deductible, and the Government envisage allowing some of the 2023/24 profit to be carried forward and the tax paid over several years. Implications for tax rate thresholds, tax credit, high income child benefit charge etc have yet to be determined.

There has been considerable opposition to this proposal and the Government have already postponed the transition date by one year. They are publicly committed to proceeding according to the timetable shown above, but this change is not yet certain.

Planning

Affected farmers might consider making extra pension contributions or timing major tax-allowable business expenditures in 2023/24 to keep down that year's taxable profit (assuming 2023/24 remains the transitional year).

From a practical perspective, most affected farmers will need to change their accounting date to 31 March (by 2024).

If you have a major dip in tax-adjusted profit before then (perhaps because of plant/machinery expenditure), we should consider moving sooner to a 31 March accounts date. Moving sooner would sacrifice the proposed spreading relief but, with heavier costs and no Basic Payment Scheme income to recognise over the winter, some beef/sheep farms might show less profit for 15 months to March than for 12 months to December, although this will depend on the timing of livestock sales.

Changing to a March year end will make it necessary to complete your accounts sooner after the year end.

Please speak to us if you would like to discuss the implications for your farm.

PROMOTION FOR HAYLEY

WE ARE DELIGHTED TO ANNOUNCE THE PROMOTION OF HAYLEY PRICE TO ASSOCIATE DIRECTOR.

Hayley initially joined DY for 12 months on a university placement as part of her studies at the University of Wolverhampton, before returning as an Accounts Clerk following the completion of her degree.

She currently works as a Client Manager in our Agricultural Department alongside Director Mark Griffiths and has been with DY for over ten years. During this time, Hayley has trained and qualified as a Chartered Accountant and then as a Chartered Tax Adviser.

"I'm absolutely delighted to have been named as an Associate Director and I couldn't be prouder of the recognition I've received," said Hayley.

"Dyke Yaxley is a great company to work for and I thoroughly enjoy my work meeting up with clients – I particularly enjoy the sense of accomplishment I feel knowing I've been able to help them with their accounts and tax compliance.

"I manage a portfolio of sole traders, partnerships and limited companies, and I'm committed to delivering the very highest level of support to every client.

HAYLEY PRICE WITH MARIE BRAMWELL AND MARK GRIFFITHS

"To have been promoted to my new senior position is a great honour, and I'm pleased that my work has led to such a great opportunity."

Dyke Yaxley Managing Director Marie Bramwell said: "Our company ethos has always been to encourage our team members to continuously develop their skills and Hayley is an excellent example of someone who has worked hard and shown great dedication.

"Thanks to her experience and wide-ranging knowledge, she plays a key role in our team, and we're looking forward to the contribution she will make to our future plans and strategies moving forward."

VAT ON STORAGE

SOME FARMERS WITH REDUNDANT FARM BUILDINGS NOW OFFER STORAGE FACILITIES TO INCREASE THEIR BUSINESS INCOME.

Although property letting is usually exempt from VAT, it is important to note that standard rate VAT (20%) is chargeable on a supply of space for the storage of goods in a fully enclosed container, building or structure.

For this purpose, 'storage of goods' does not include livestock; for which the VAT status depends on the level of service. For example, DIY horse livery (i.e., the provision of unserviced stabling only) is VAT-exempt, but full or part-serviced livery is standard-rated.

HMRC regard it as the farmer's responsibility to establish how the customer uses the space and to keep documentary evidence of that. Typically, this would be covered in the written contract with the customer.

Option to tax

Where a farmer cannot ascertain the customer's use, one way of resolving that uncertainty would be to opt to tax income from that (area of) the property. Opting to tax would make clear that standard-rated VAT must be charged on the income – and on all future rents and sales proceeds for at least 20 years. An option to tax may be commercially disadvantageous for the farmer if the property is let or sold at some future time to a person who is not VAT registered.

Recovery of input tax

Agricultural produce is zero-rated for VAT, and thus treated as a 'taxable' output (like standard rated sales), rather than exempt.

Therefore, most farmers are able to reclaim input VAT on nearly all business purchases (except where there is a private use element). However, where there are exempt sales (e.g. property letting), the partial exemption rules must be considered and, depending on the individual circumstances, there may be some restriction of the input VAT that can be reclaimed.

When you make standard-rated sales, you must charge output VAT and pay it across to HMRC. But it is a consolation if this avoids having to restrict input VAT recovery.

Please contact us if you require VAT advice.

MEET THE TEAM

We have welcomed some new faces into our Agriculture Team over the last two years and we thought it was time we introduced you to everyone again. Please say hello to the team ....

MARK GRIFFITHS
DIRECTOR

IAN WALSH
DIRECTOR

SEAN GORMAN
DIRECTOR

HAYLEY PRICE
ASSOCIATE DIRECTOR

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CLIENT MANAGER

ANDREW THOMAS
CLIENT MANAGER

CAROL WRIGHT
CLIENT MANAGER

JENNA WOOLLEY
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IAN THOMAS
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