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FARMING UPDATE

Self Invested pensions – take another look

KEY TO PROFITABILITY
Big may not be beautiful

CAPITAL ALLOWANCES v CASH FLOW

FARMHOUSE VICTORY

ENTREPRENEURS RELIEF
Can you qualify?

WOOD FUEL GRANT
and other developments

TURNOVER IS VANITY

A 3 year survey of farming clients who are advised by Charter Group* members reveals consistent results year on year – those in the top quartile for turnover are not the most profitable client group. This accolade, repeated over all the sectors covered by the survey, (dairy, beef & sheep, poultry and arable), is held by those in the second quartile. This finding reinforces the theory that using resources efficiently is the key to profitability. The consistently successful farms are those with a keen eye for detail and an analytic approach to farm management.

Risk

As farm businesses grow managing risk becomes an increasingly important part of business strategy as the numbers involved increase. Buying or selling ahead gives a stable platform for at least some of the outputs and inputs (e.g. obtaining forward prices for all or some of the 2012 harvest wheat sales, and agreeing fertiliser prices for the same crop). Against these certainties the other variable elements can be managed to try and obtain the best margin.

Managing Costs

Benchmarking is a useful tool to establish the difference in performance between enterprises, the results can be used to draw up a plan to improve results. Even an informal discussion of cost drivers can provide an opportunity to discuss changes in approach that may be adopted to increase profits e.g. Shifting to towards greater use of contactors with specialist machinery rather than carrying the costs of potentially under utilised machinery.

Subsidies

It is also revealing that on average the subsidy payments account for 14.5% of farm profit, this figure varies from 8.5% on dairy farms, 20.8% on livestock units and 16.8% on arable holdings while poultry units are those least dependent on support deriving only 5.4%. of their income from subsidy. In the next few months we will have a better idea of the impact of the CAP review will have on these figures.

Do discuss these issues with your accountant – we are specialists in accounts for farm businesses and can help you make your business more profitable.

*Charter Group is an alliance of high quality, independent firms of chartered accountants.

USE YOUR PENSION TO BUY FARMLAND

Front End Planning

A self invested pension plan (SIPP) is a flexible way to make your savings work for you as well as plan for your future. If you have a standard personal pension the balance held in this can be transferred to a SIPP. You can make pension contributions of up to the annual allowance of £40,000 per year net of basic rate tax. This can also mitigate higher rate tax. Within your pension this is topped up by £10,000 by HMRC.

If you want to purchase some farmland you could use the funds in your pension as follows:

1. The pension can borrow up to 50% of its asset value e.g a pension fund can borrow £50,000 to purchase land worth £150,000.
2. A market rent would be paid to the pension scheme – this covers the interest and the capital repayments incurred by the pension fund (and is tax deductible in the trade).
3. Additional contributions to the scheme can be used to build up funds for future purchases or make faster repayments. These benefit from the HMRC tax repayment into the scheme available to all pension contributions up to the annual allowance.

Wins

The money in your pension plan is now working for you and not lost to the business.

You get tax relief for the contributions you make and the rent paid to the pension fund.

There is no income tax or CGT within a pension scheme.

Effectively you are obtaining tax relief on the capital repayments, which is not achievable in other borrowing arrangements.

Back End Planning

Since April rules have changed to allow flexible draw down from a pension fund. The main conditions for this are:

- **a)** You can show other pension income (including state pension) of at least £20,000.
- **b)** You stop making pension contributions to any scheme

Assuming these are satisfied then you can draw 25% of the fund tax free (as before), and then take all or part of the remaining fund as a lump sum or a series of payments spread over a number of years to maximise the tax efficiency of the withdrawals which are subject to income tax.

If your fund still holds farmland at the date of retirement you may look to sell the land to a pension scheme held by your successor if you want to keep it in the family.

If the cash is excess to your spending requirements you can give it away to avoid inheritance tax at 40% on your estate. If the balance of the undrawn fund is left to your beneficiaries on death the tax rate is 55%.

Make your pension fund work for you – talk to us about the opportunities.

WHAT'S NEW?

VAT

If you have a VAT inspection let your accountant know beforehand even if you deal with it yourself. Often the inspector will want to see the accounts and may have questions about them. If you are using cash accounting tell the inspector as the outputs on your VAT returns will not equate to sales figures in the accounts.

Tax Return Penalties

In the past penalties on late tax returns were limited to the equivalent to the amount of tax due. This year if your personal tax return is not e-filed by 31 January 2012, even though you have no tax liability the penalty will be due and can rack up to £1300 very quickly.

HMRC Time to pay agreements

Warning – repeat requests from businesses are more likely to be rejected as HMRC say that these applications to them for funds indicate that the business is not viable. So if you have used these in the past consider alternative funding before the deadline.

Women and Work

www.lantra.co.uk/womenandwork - Check out this website for details of grants of up to £400 for funding training for women working in agriculture and environmental sectors.

NEW WOODFUEL GRANT

The grant offers 60% towards the cost of work to support the sustainable production of woodfuel. The main supported operations include: roads, tracks and other infrastructure to assist the extraction of timber from woodland. Also included is a woodland inventory and costs associated with managing harvesting contracts.

To be eligible a woodland management plan should be in place and owners can apply for a Woodland Planning Grant to help with the cost of preparing the document which will need to provide evidence of under management or of a barrier to sustainable harvesting.

For details apply to the Forestry Commission: www.forestry.gov.uk Guidance is available in the EWGS General Guide.

CAPITAL ALLOWANCES – CASHFLOW NIGHTMARE

As in most financial matters the critical issue is to PLAN AHEAD.

We have enjoyed / are enjoying a generous £100,000 100% first year allowance. From April 2012 this drops to £25,000. Apart from the timing issues associated with the purchase dates for new equipment referred to in previous editions there is a further costly trap.

Standard writing down allowances now at 18%, reduce farming profits for tax in lieu of the depreciation figure shown in the farm accounts. With 100% allowances the tax relief has come much quicker than the gradual depreciation shown in financial statements and could cause some nasty surprises.

	2011/12	2012/13
Accounting profits	£150,000	£150,000
Capital expenditure	£100,000	£100,000
Profit before depreciation	£190,000	£190,000
Max capital allowance claim	£100,000	£38,500 (for a 31 March accounting date)
Taxable profits	**£90,000**	**£151,500**

This is could be an additional £25,830 in tax due January 2014 plus a further additional £12,915 on account based on the same accounting profits for unincorporated businesses. It will be worth warning the bank manager in advance of the £38,745 liability arising due to changes in the legislation.

For farming companies the additional tax will be £10,210. In the meantime you will also be funding the capital purchase costs which could be denting your cashflow along with potentially higher interest rates by this time. (Sorry to be depressing but a reality check now will help long term planning).

Ultimately you will get full relief for the capital expenditure but it could now take over 12 years to claim 90% of the purchase cost and a further 10 years to nearly get to a complete reclaim.

To maximise AIA's see our "When to buy" calculator at www.simpkinsedwards.co.uk

SOLE TRADERS – DON'T TAKE 10% CGT FOR GRANTED

Capital Gains Tax (CGT) is calculated on the difference between sale proceeds (after selling costs), and the purchase cost. Improvement expenditure can be deducted to arrive at the taxable gain. If the asset was acquired or disposed of by way of a gift, a valuation at the date of the gift is used in place of the cost or proceeds. If the asset was acquired before March 1982 then a March 1982 valuation is used as the cost. Each taxpayer has an annual exemption for CGT of £10,600 (2011/12). Entrepreneurs Relief (ER) is now an important relief for business assets as it results in a tax rate of 10% rather than 18% or 28% if the asset does not qualify. However, obtaining the relief is not straightforward.

Sole Trade qualifying asset

To make a claim for ER on farmland "the sale needs to be structured as the sale of the whole or, an identifiable part of the business", or be "on or after a cessation of the trade". The sale of a single field will not qualify as the sale of part of a business. However if the disposal of land and buildings is tied in with retirement from dairying for example, and the herd and equipment are all sold, a claim for ER may be considered. The farming business could continue on the remaining land, but perhaps as a beef or sheep enterprise.

If farmland is held by a farmer and his spouse, where one of them is a sole trader farmer, the quickest way to ensure that ER for capital gains tax (CGT), can be claimed on the whole gain, is to transfer the non farming spouse's interest in the land to the farming (qualifying) spouse prior to sale. For partnerships, additional planning opportunities may be applicable.

Advance planning to maximise CGT reliefs is essential to minimise tax bills. Take advice in advance to ensure a tax efficient outcome.

IHT RELIEF ON FARMHOUSES – A VICTORY

In the recent Golding case the Tribunal decided that a particularly run down farm house with a relatively small area of land being farmed was "of a character appropriate" to the property having taken a broad, historical and largely objective approach to the test. The Tribunal was satisfied that the deceased was engaged in farming immediately prior to his death but they also took account of the extent of his farming earlier on in life, rather than the level he was capable of during his last years.

As in all cases the exact circumstances are not likely to be replicated, the farmhouse was described as "spartan at best" and there was no electricity in the upstairs bedrooms, not a property attractive to the "Lifestyle" who is the object of many of the cases. However it gives hope to the beneficiaries of genuine farmers whose farming activities have decreased in inverse proportion to their age, that the onslaught on the availability of Agricultural Property Relief on farmhouses is not a one way street.

As always – keep your tax adviser up to speed with changes in trading activities and family arrangements with regards to farm dwellings. The usual mantra applies - Plan Ahead!

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