TAXATION

Agricultural Productivity, Land Occupation and Use After Brexit

A CAAV Discussion Paper:
Invitation and Summary

Central Association of Agricultural Valuers

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INVITATION TO DISCUSSION

This paper, concerned with the occupation and use of land and so the business of agriculture and the management of land, offers a review of potential tax measures that could aid agricultural and environmental productivity by assisting:

- entry, progression and exit from farming
- innovation and its adoption through investment
- the management of risk and resilience

seeking "game changing" measures for the sector to face the future.

It does so as taxation policy is seen as an important influence on behaviour which can have positive or perverse effects on real businesses and the economy. The positive effects can where its structures, rates and incentives accommodate change and enable or encourage businesses to thrive. The perverse effects can be where they hinder growth, lead to tax-driven gamesmanship or are just too complex to be effective or certain.

In this, we can look with interest at the agri-taxation review of 2014 in the Republic of Ireland and the resulting measures, now with some evidence of their effects. As a common law, English speaking market economy with similar land law and other commonalities there is much that can have relevance.

With this opportunity for the discussion and the benefit of this paper, we offer

- How could the taxation system be changed to support improving productivity?
- Where does the taxation system now act against agricultural productivity?
- How might taxation best enable flexibility in land occupation with entry, progression and retirement?
    - in the owner-occupied sector?
    - in the tenanted sector?
    - opening more opportunities for lettings and other business arrangements?
- How much larger might the tenanted sector be as a result?
- How can the taxation system most effectively support innovation and investment?
- How to achieve equal treatment for businesses whether under Income Tax/Capital Gains Tax under Corporation Tax?
- How might taxation help with risk management and resilience?
- What changes might help businesses make and sustain environmental improvements?
- What measures would have the greatest practical effect?
- What might they replace?

some questions to start the process, looking for practical effective answers.

As well as seeking views now, the CAAV is proposing to convene an event later in the autumn for all those interested to review these questions and others put forward.

SECTION 1 – SUMMARY AND OVERVIEW

1.1 Introduction

1.1.1 This paper considers taxation measures with the aim of enabling and supporting a continuing and sustained improvement in the productivity of agriculture that will also bear on the rural economy and the wider food sector. Taxation is an important factor as one component of a larger suite of policies to promote improving productivity in this sector of an economy that faces this as a larger issue.

The requirements for greater productivity are seen to be:
- skills
- investment
- confidence
- removing barriers to change and innovation
- removing barriers to markets.

1.1.2 With some review of recent similar endeavours in Ireland (close enough to the UK to be particularly relevant) and observations of some other experience abroad, this package focusses most on measures to support:
- access to land, particularly for those who are trained – the study for the Irish agri-taxation review showed a 12 per cent increase in output (taken at this point as a proxy for productivity (see 2.1.2) from such a move
- new investment in necessary fixed equipment, technology and business development to support the growth of productivity and innovation as well as substituting for labour.

1.1.3 For access to land, this paper is concerned with the occupation and use of land, not directly its ownership although recognising that only landowners can let farmland. The ownership of rural land in the densely populated and affluent UK is seen to be driven by other factors than the business of farming. While owning farmland give security and can be valuable collateral for a business, a model of purely owner occupied agriculture would not offer the flexibility or entry needed for the challenges we face and would be a distortion of investment not expected of any other sector of commercial life. Thera are good reasons why the last 35 years have seen a steady separation of ownership from farming use.

1.1.4 While there is a range of measures that would be beneficial, many might only offer marginal or incremental easing, not decisive change. This review seeks to focus discussion on those that could effect a significant change in behaviour ("game changing") and open new doors for the sector, although noting other proposals.

1.1.5 Such a taxation review is though only seen as part of a package of legislative and other policy measures, including the reform of support in each UK territory, that, taken together, set a new course.

1.2 Access to Land for Trained Farmers

1.2.1 The reform of agricultural tenancy legislation for England and Wales in 1995 was a "game changing" moment, usefully supported for the private landowners and potentially retiring farmers who are the potential providers of land by the equalisation of the rates of Agricultural Property Relief from Inheritance Tax for different tenures. The aim would be to build on that with these three goals:

- to attract more land into the tenanted sector with its flexibility for farming use
- to move land into the hands of the trained
- to encourage longer lettings

creating the conditions for improving productivity. As will be seen they can come into conflict.

1.2.2 While there are still issues with capital taxation, no changes that have been discussed seem either sufficient to effect the change needed or to do so without perverse consequences.

1.2.3 In the Irish Republic, the recent enhancement of relief from Income Tax for rental income from agricultural land, with the cap graduated by the length of letting, appears to be delivering substantive change. What is currently known is reviewed below and is encouraging. It is noted that this relief had been available at smaller scales from 1985 but the 2015 changes seem to have been at a level that is now changing behaviour. It could be seen as analogous to the Rent-a-Room relief for Income Tax for householders letting lodgings. With allowances for some differences in circumstances (save in Northern Ireland where the position is very close to the Republic), it is proposed that close consideration be given **to rent relief from Income Tax for letting farmland, geared to length of letting.**

1.2.4 We suggest that, with the benefit of the review in this paper of the Irish experience such a relief might be along these lines:

- a relief from Income Tax, not Corporation Tax
- for lettings of agricultural land made in writing
- to tenants who are not connected to the owner
- that are let for at least 5 years
- increasing with the length of the tenancy, perhaps sharply at 10 or 15 years
- for new tenancies, excluding ordinary surrender and regrants of pre-existing tenancies, and successions to secure tenancies

with consideration as to if and how training might be recognised response to the Irish evidence of the benefit of land going to the trained.

1.2.5 Specific levels for the caps for the relief are not proposed though a model with possible levels is discussed. In judging this, the Irish evidence is that the new higher levels are delivering the intended change in the attitudes of current occupying landowners while the previous lower rates were ineffective.

1.2.6 Such a relief can be presented as a positive aid to retirement for farmers in conjunction with the newly introduced Residential Nil Rate Band Amount with its potential in many, but not all, situations as a more secure alternative to Agricultural Property Relief from Inheritance Tax.

1.2.7 Intra-Family Transfer – The form of that proposal does not tackle the important issue of encouraging greater succession within family businesses which merits further discussion and does appear susceptible to intervention by taxation whether by defining the circumstances in which a current owner can have the benefit of tax relief on rent to a following generation, provisions in capital taxation or otherwise.

1.3 Equal Tax Treatment for Unincorporated Businesses

1.3.1 One significant feature of the rural economy, and notably of agriculture, is that businesses are conventionally sole traders or partnerships, rather that companies. As such, the differences between the Corporation Tax regime for companies and the Income Tax/Capital Gains Tax regime for unincorporated businesses pose a substantial problem as they are not neutral between the sectors. We have seen business incentives focussed on incorporated businesses rather than the self-employed, so excluding many rural businesses. These are highlighted by the next sections on encouragement for innovation, diversification and investment. One example is that when capital allowances for both agricultural and industrial buildings were removed under the Finance Act 2008, it was explained that the loss of relief was balanced by the accompanying reduced rates of Corporation Tax. However, sole traders and partnerships simply lost that relief with nothing to balance it. That raised problems for a sector like agriculture with its need to reinvest in buildings. More of the issues are developed in this paper.

1.3.2 Many concerns relevant to this paper would be eased by greater neutrality between Corporation Tax and Income Tax in their approaches to business taxation. We see that some of the concerns in this area have attracted the interest of the Office of Tax Simplification. The simple point is that businesses should not be discriminated against because of their structure so that reliefs designed to encourage the innovation and business development we need should be equally available to the self-employed and companies.

1.4 Encouragement for Investment and Innovation

1.4.1 The measures proposed seek to create a benign environment for businesses to invest, develop, adapt and innovate successfully.

1.4.2 A revised approach to diversified but unified composite businesses would be of great assistance. One model is that offered by the recent Office of Tax Simplification report on simplifying Corporation Tax which seems readily capable of being applied to the Income Tax that is relevant to most farmers and estates.

1.4.3 Two developments to the structure of capital allowances are proposed:

- **Agricultural Buildings Allowances** should be reinstituted with a rate of 5 per cent as buildings are now more akin to machinery and more vulnerable to technical and regulatory obsolescence.
- **a specific capital allowance of £2.5m to be available on a floating basis over a five year period for automation and digital technologies.** The sector faces a major need to embrace automation using new technologies, including the developing opportunities offered by digital, optical and other research, substituting for labour and improving competitiveness. Such a flexible allowance would be available at any point in that period as the need to invest arises and so optimise the effectiveness of this relief as technology develops - for investment in such specified technologies.

Buildings could also be brought within the scope of the Annual Investment Allowance.

1.4.4 **Research and Development relief should be extended to Income Tax.** At present it is only available under Corporation Tax (another example of how tax policy overlooks unincorporated businesses), it is suggested that it be extended to Income Tax for sole traders and partnerships and so available to all classes of business, not just those in corporate form.

1.4.5 Allied to supporting much needed new building, **any new system of CIL/LIT contributions should exempt agricultural buildings,** so removing that counter-productive burden on business development.

1.5 Diversification and Innovation

In seeking to stimulate the necessary exploration of new business and initiatives, three measures are proposed:

- raising the **limitations on sideways loss relief** as new lines of business frequently do not make money when they start, representing a drain on their parent business.
- a review of **treatment of composite interdependent trades**
- giving some relief for the **treatment of the costs of abortive proposals**, as where a project fails to secure planning permission. Where a purchase or project does not come to fruition, there is no tax relief for the costs involved in pursuing it as there is no project for them to capitalised with and they cannot ordinarily be set against the main accounts. At a time when encouragement for innovation and broadening the base of the rural economy is important, it is suggested that an innovation relief or allowance be considered for such abortive costs, perhaps subject, if necessary, to:
    - a cap and/or
    - 50% recognition of relevant costs

  to ease the financial risk for individuals and businesses pursuing new options.

1.6 Risk Management and Resilience

Once outside the EU with the constraints of its State Aid rules, a UK version of the Australian Farm Management Deposit Scheme should be established so that farmers can put aside money tax free when they can and draw it down when they need it, taxed at that time.

1.7 Environmental Policy

1.7.1 Aspects of other proposals already reviewed can also have environmental and other benefits. One example would be buildings allowances where larger buildings may be needed on welfare grounds or improved arrangements for slurry handling can reduce pollution risk or greenhouse gas issues. The adoption of new technology will also assist these larger ends.

1.7.2 While recognising that, beyond these points, this may be a more difficult area for effective intervention by taxation measures, some measures taken in the USA are reviewed briefly, the Green Alliance's concept of Natural Capital Allowances is set out and the potential raised for a form of stock relief on soil improvement.

Summary of Proposals for Discussion:

- **Rent relief from Income Tax for letting farmland, geared to length of letting**
- **Agricultural Buildings Allowances reinstated with a rate of 5 per cent**
- **Introduction of a specific capital allowance of £2.5m to be available on a floating basis over a five year period for automation, digital and other new technologies**
- **Neutrality between Corporation Tax and Income Tax for businesses**
- **Review treatment of composite interdependent trades**
- **Research and Development relief extended to Income Tax**
- **Raise the limitations on sideways loss relief**
- **Give some relief for the treatment of the costs of abortive proposals**
- **An Australian type deposit scheme to manage money between years and so support resilience at farm level**
- **Review tax treatment of environmental expenditure**

About the CAAV

The Central Association of Agricultural Valuers (CAAV) represents, briefs and qualifies some 2,800 professionals who advise and act on the very varied matters affecting rural and agricultural businesses and property in all four countries of the United Kingdom. Instructed by a wide range of clients, including farmers, landowners, lenders, public authorities, conservation bodies, utility providers, government agencies and others, this work requires an understanding of practical issues.

The CAAV does not exist to lobby on behalf of any particular interest but rather, knowing its members will be called on to act or advise both Government and private interests under developing policies, aims to ensure that they are designed in as practical a way as possible, taking account of circumstances.

Following its work and publications on agricultural tenancies, taxation, agricultural policies, support schemes and other The CAAV is widely engaged in and contributes to discussions with governments and other bodies about Brexit and post-Brexit issues across the United Kingdom. It is a member of many bodies involved in these discussions including the Tenancy Reform Industry Group, the Agri-Brexit Coalition and the UK Livestock Brexit Group.

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