FARM OWNERSHIP AND SUCCESSION

by Jonathan Hayes, Partner at Simpkins Edwards LLP

It's no secret that the average age of farmers is significantly above the average age of active traders in virtually any other industry in the UK. The oft-accepted wisdom is that a farmer farms until death.

However, farm partnerships often have very high asset values (the value of the land and buildings itself) and can have complicated successions with multiple potential beneficiaries, some interested in continuing the farm and some not. Not planning for the succession of the farming business can be tax inefficient and give rise to unnecessary dispute.

A fear of solicitor fees means that many family farming partnerships are run without a written partnership agreement. Whilst not required by law, a well-drafted agreement aids understanding between the partners, protects their investments and can help ensure that the farm is structured and run tax efficiently.

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The partnership agreement and partners' wills need to be considered together. A common error is to rely on a will to gift particular parcels of land that belong to a partnership. Such land will pass as part of the partnership interest, and not in accordance with what the will says about the land. Relying on an informal understanding risks future dispute that could incur legal fees disproportionate to the initial saving from not having had a partnership agreement prepared – and could ultimately result in assets passing to the wrong beneficiary.

In the absence of contrary agreement, the law dictates that partners have equal profit shares, equal interests in all partnership assets and that property bought with partnership money belongs to the partnership. Even where accounts show differently, a party in dispute might argue that the accounts were incorrect. Where profit shares or interests in assets are unequal, it is important that a partnership agreement provides for this. Even more so when children are admitted into partnership but not intended to acquire interests in capital assets.

Families have different views on whether their farmland should be owned by the family partnership business (in which case incoming partners are likely to acquire an interest), or personally by individual partners.

Land ownership by individual partners has the advantages that:

- Older family members owning the land have security and the knowledge that the land is protected from a son or daughter's divorce or wayward behaviour.
- With detailed planning and sufficient lead time, it is sometimes possible to achieve Business Asset Disposal relief on a sale of part of the farm.
- Leaving selected property to non-farming children is accomplished more easily and with less risk of dispute.

On the other hand, land ownership by the partnership has the advantages that:

- The rate of Inheritance Tax Business Property Relief (BPR) is 100% instead of 50%.
- On a new land purchase, any borrowing within the partnership is matched by the addition of the land to the business balance sheet.
- There is less risk of dispute following improvement works (eg new buildings) paid for by the partnership.

There are pros and cons on either side, and it may depend on the intentions for succession as to whether an obvious path for land ownership arises. However, some recent developments mean that land ownership within the partnership may be a better route in more situations in future:

- The designation of land capital accounts in partnership agreements has become established as a means of enabling land to be owned by a partnership, while still retaining its value in the hands of particular (usually older) partners.
- The Business Asset Disposal relief (previously Entrepreneurs' relief) limit has been reduced to £1m of lifetime gains per person.
- Over the last 2 years, there has been much speculation about possible future Inheritance Tax (IHT) and Capital Gains Tax (CGT) changes. Arguably, land owned by a partnership might be less impacted by possible IHT changes.

We do not advise clients to plan on the basis of tax changes that might never happen. However, recent reports by both the Office of Tax Simplification (OTS) and the All-Party Parliamentary Group on Inheritance and Intergenerational Fairness (APG) include recommendations that, if implemented, would effectively result in a tightening of inheritance tax reliefs and a possible lessening of the traditional tax advantage of farming until death.

In due course, the government will need more revenue to pay for its Covid-19 economic support and political pressures may encourage it to adopt some of the OTS's recommendations. Moreover, governments have often implemented OTS recommendations in the past and the OTS's recent IHT and CGT reports were commissioned by the current and the previous Chancellors of the Exchequer. However, we cannot know what changes will be made and when, and do not recommend any immediate planning on the back of the OTS report.

It may seem to involve a lot of upfront time, cost and liaison with professional advisors to implement or even plan for succession, but the benefits of doing so are many. The process aids proper understanding of the family's assets and the wishes of family members. Appropriate documentation will help those objectives to be achieved tax-efficiently and will reduce the opportunity for dispute and bad feeling down the line.

We would be happy to discuss succession or assist you with an IHT review. These are important considerations, prior to commissioning a partnership agreement. We would also be glad to support you and your solicitor in preparing the partnership agreement, to help ensure that the final document is both tax-efficient and suitable for the business.

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