LIFE ON THE FARM

Gifting of farm property

George is at the kitchen table, looking worried. Henry, Mary and David walk in chatting.

Meet the Barleymow family

Every issue we will be following the fortunes of the Barleymow family and the issues they face as a family farming business.

George
- Henry *m* Mary
  - David *m* Carolyn
    - Mark
    - Emma
- John *m* Sarah

David: *What's up, Grandad?*

George: *I was wondering about passing on more of the farm to you all …*

Henry: *Eh, why?*

They all sit down.

George: *I want to protect you from that bloomin' Inheritance Tax when I finally pop me clogs. (Pause) Not that I'm planning to anytime soon!*

Mary *(smiling): Well that's a relief! So, what's worrying you?*

George: *I just don't want you all to be burdened with huge tax bills when I'm gone. I mean, I still own quite a lot of the farm that was left to me by my parents. And the land that we bought before you became a partner, son, is in my name and*

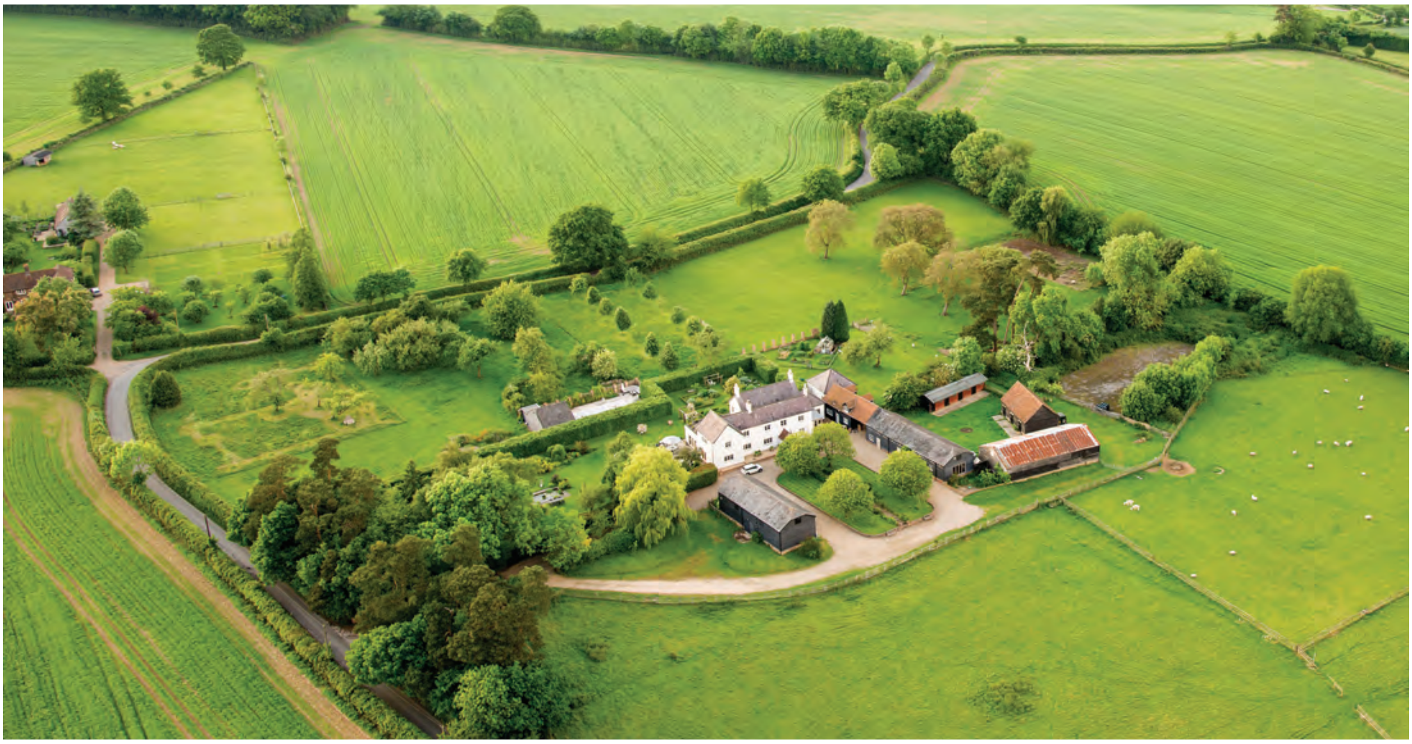
David: *Hang on Grandad! Ensors told us we're all pretty well protected from Inheritance Tax because the property is considered to be partnership property and used in partnership activities. Even the let cottages and the land with the development potential look to be covered …*

Henry: *That's right, they said not only would the property pass free of Inheritance Tax, but it also passes at the value at the date of your passing for Capital Gains Tax (CGT) purposes. This means that should we then sell any of it, we'd only pay CGT on the increase in value between what we sell it for and what it's worth at the time of your, ahem …demise.*

Continued overleaf

Ensors

Making you more than just a number



David *(smiling): See, nothing to worry about Grandad!*

George *(thinking): I know we're in a pretty good position right now but let's face it … this current government isn't exactly stable and a new one might change the policy in years to come. What would happen then, eh?*

Mary: *You may well be right George. But no one can predict what might happen. At the moment things are OK.*

George: *Maybe, but it would be a whole lot easier for you all if you knew when I was likely to pop off and*

David: *Stop grandad! Nothing's going to happen …*

George: *Well, I'm not going to live forever … so why don't we just look at me passing at least some of the property over?*

Henry: *We could, but wouldn't that just create another tax liability?*

David: *You are probably thinking about CGT, Dad. Ensors explained if property is given away that, for tax purposes, the person giving it away is considered to have sold the property for full value at the time of the gift. Even though no money has changed hands; this would give rise to a CGT charge.*

Henry: *Ah yes – I remember now – but there was a way around it.*

David: *Ensors said in certain cases it's possible to defer the CGT so no tax is payable on the gift. I think it's called Capital Gains Tax Holdover Relief.*

George: *Defer? For how long?*

David: *It is actually fully deferred until the property is sold on.*

Mary: *That's good because if you sold, you'd then have some cash from the sale to pay the tax!*

George *(scratching his head): So, if I give some land to Henry first and he then wants to give it to David … is tax payable at the time of that second gift?*

David: *No – providing the conditions are met at the time of the second gift, you should be able to use Holdover Relief on that as well, providing the rules haven't changed from where they are now.*

Mary: *So, what are the conditions to get this Holdover relief?*

David: *For us, the property that is being gifted must be either used in our farming trade, or qualify for Agricultural Property Relief. I'm sure there must be some more detail behind these requirements that Ensors would be able to help us with.*

George: *The farmland and buildings should be OK then, but what about the farm cottages?*

David: *The one that has been occupied by old Ned for years should be fine as it's housing a farm worker, so will qualify for Agricultural Property Relief. I'm not so sure about the two cottages that are let on Assured Shorthold Tenancies though. I think they might be a bit more complicated. We'll need to take some advice from Ensors, but I'm sure something could be done.*

Henry: *Any disadvantages to all this?*

David: *There will, of course, be some professional fees involved in the process. If the tax rules don't change between now and when Grandad passes, then we are probably at a bit of a disadvantage should we ever sell the properties that are passed on, although I can't see that happening.*

This is because if we use CGT Holdover Relief the property does not pass over for CGT purposes at the value of the gift but passes at Grandad's original cost, or at the value that he inherited the property at. So the CGT on an eventual sale would then be that much higher. It's only a problem if we ever sell … which is unlikely.

George: *But if you did sell, at least you'd have received some money to pay the tax. It's some protection against IHT should the rules change, which is what worries me.*

David: *One last thing to consider, Grandad – if you give property away for this to be effective for IHT purposes, you cannot be seen to continue to benefit from what you've given away. This means we'd probably have to reduce your profit share in the farm, so that you're not then retaining a benefit from land or other property that you've given away …*

George *(shrugging): That's the beauty of having quite a large pot in my Partners Account in the partnership of undrawn profits from previous years. I'm sure we can come to some arrangement where I can draw on that should it be needed …*

Henry: *Now you're talking, Dad! So let's get this meeting booked in with Ensors.*

Ensuring the family farm continues through the generations is often of utmost concern to families and will involve crucial decisions that require careful thought and planning. Gifting land and property to the younger generation will usually be high on the agenda, however, this does come with potential tax consequences.

SUCCESSION PLANNING
A matter of trust

People will be fairly familiar with the seven-year rule for Inheritance Tax (IHT), where the donor must survive seven years from the date of gift for it to be IHT free.

Less familiar are the Capital Gains Tax (CGT) rules on gifting. Where an asset is gifted, the donor is taxed on the market value of the asset at the date of the gift, even though no actual proceeds are received. In certain circumstances, holdover relief may be available to defer the capital gain, but this only applies to qualifying business assets, such as:

- Agricultural land and buildings used for the purposes of farming
- Shares in an unquoted trading company
- Assets used in a trading business

Even some of the above will not qualify for full holdover relief, such as shares in a farming company which also has rental or investment assets. This is where the use of trusts comes in.

A trust is a separate entity. When assets are placed into a trust, the legal owners, known as the trustees, will hold assets on trust for the ultimate beneficiaries.

TAX CONSEQUENCES OF GIFTING ASSETS INTO TRUST

The most common types of trust are 'discretionary' trusts and 'interest in possession' trusts. A gift to either of these is a chargeable lifetime transfer on which IHT is immediately payable.

Business property relief (BPR) and agricultural property relief (APR) should be available to reduce the value of any chargeable lifetime transfer of relevant business or agricultural property, so the gift of land, or shares in a farming company to a trust should be IHT free.

BPR and APR are not, however, available on the gift of a let cottage in isolation, or on other non-business assets. In these cases, IHT would be payable on the value of the gift over and above the donor's IHT nil rate band.

A gift into trust is a disposal for CGT purposes, however, the gift can be made without any immediate CGT being payable if holdover relief is available. This may sound familiar, but the use of holdover relief is a lot more wide ranging with regard to trusts. Providing the gift is a chargeable lifetime transfer for IHT purposes, then the gain on any asset can be held over, not just on qualifying ones. There are, however, restrictions where the trust is settlor interested. A settlor interested trust is one where either the settlor (the person introducing assets into a trust), their spouse, or their minor dependent children may benefit.

Taking the above into consideration, it is possible to gift a let cottage, or shares in a farming company with non-trading assets, to a trust without an immediate IHT charge and also holdover the capital gain so that no immediate tax liability arises on the transaction. If after a few years the trustees decided to break the trust and appoint the assets to the beneficiaries then provided the qualifying conditions are still met, this could be done without an immediate IHT charge and again holdover the capital gain.

OTHER BENEFITS OF GIFTING ASSETS INTO TRUST

Apart from the potential tax advantages, there are a variety of other reasons why a settlor may wish to transfer assets into trust, such as:

- **Guaranteeing succession of property** – by gifting assets to a trust, the settlor can make sure that the assets they are giving away remain within their family.

- **Flexibility** – if, for example, the potential beneficiaries are under 18, it can be difficult to know if they will want to take on the farm. Putting the farm into a trust means it is protected until a successor becomes apparent.

- **Protecting a vulnerable beneficiary** – to avoid an individual holding significant assets being targeted by someone wishing to take advantage of them.

The consequences of making any gift will always depend on the circumstances at the time. It is important to take comprehensive advice at an early stage when considering succession planning and Ensors are here to help.

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> ***“Ensors have an excellent understanding of how a rural agricultural estate operates and as such are able to work closely with clients and fellow professional advisors to ensure maximum benefit.”***
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