



OFFICE OF TAX SIMPLIFICATION

INHERITANCE TAX REVIEW: CALL FOR EVIDENCE

RESPONSE BY THE AGRICULTURAL LAW ASSOCIATION 8 JUNE 2018

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1.0 The Agricultural Law Association

1.1 Background

The Agricultural Law Association ('the ALA') was formed in 1976 and is the UK's largest inter-professional organisation devoted to the law and business of the countryside.

We focus on the law in a non-partisan, apolitical way in order to promote its knowledge, understanding and development among those who advise rural businesses.

The ALA has over 1370 members across the legal, surveying, accountancy and farm business consultancy professions together with academics and members with specific expertise in international trade and investment; with all principal professional firms and, uniquely, all other principal member organisations within the agricultural sector represented within the membership.

We are a member of the following current sector cross organisation groups in the UK:

Tenancy Reform Industry Group
Agricultural Representatives Bodies Group (Taxation)
Scottish Land Commission – Tenant Farming Advisory Forum
Land Partnerships Service – National Advisory Group

We are also the largest member association of the European Council of Rural Law.

1.2 Consultation Work with Members

As part of our response to this Call for Evidence, we have consulted with a range of members within the legal, accountancy and surveying sectors.

This response is submitted on behalf of the ALA and its members and we look forward to working with the Office of Tax Simplification and Government on any proposed measures to simplify the current Inheritance Tax ('IHT') regime.



2.0 IHT FORMS, ADMINISTRATION AND GUIDANCE

2.1 Payment and forms

- 2.1.1 Consistency in the approach regarding time limits for submission of the relevant IHT form and payment of IHT after death would be welcomed by our members.
- 2.1.2 Our members report that on occasion, there are often cashflow issues arising where access to cash funds in a deceased's estate is not either readily available or in some instances, very limited cash resources are available to pay IHT.
- 2.1.3 Where property has been sold subject to overage / clawback conditions it is necessary to value these chose in action in the estate. Two problems commonly arise. Where prospects for development are remote, valuation costs can often be disproportionate to the value and utility of those chose in action, which are difficult to value. Where development is nearer to hand executors can face acute cash flow difficulties as the inheritance tax can be payable far in advance of any cash being received from a development.
- 2.1.4 For example, one of our members had a case where a farmer had sold land and had reserved a claw back on the land in case it ever came for development, which is not an unusual situation. Unfortunately, some ten years later, the farmer developed cancer and died leaving two daughters as heirs and no wife. The land in question had by the time he died been zoned for development. This meant that the clawback had a real value, but the cash would not be received until planning permission had been granted. Probably some three years away. Clearly there was no relief applicable to the chose in action and it was fully taxable. The tax due on the clawback exceeded the value of the remaining estate. The daughters had to cash in the clawback early by asking the purchaser to buy out the interest which involved a considerable discount because they had no way of raising the cash to pay the tax.
- 2.1.5 Furthermore, and perhaps of more importance, payment of IHT within 6 months after death before final submission of the relevant form relies on estimates of IHT liability where complex estates and the valuations thereof, are still being prepared. A change in the rules whereby the time-limit for payment and submission of the form are the same would greatly assist in this regard.
- 2.1.6 We therefore propose that the time limits for submission of the relevant form and payment of IHT should be 12 months after the date of death.



2.2 Probate

- 2.2.1 Subject to our proposal under 2.1.5 above and issues where no cash is available or where there is limited cash in a deceased's estate, our members do not experience any significant issues arising from the procedure covering the submission of the relevant IHT form and payment of IHT before probate is granted and the estate distributed.
- 2.2.2 In this respect, we support the continuation of the instalment payment option as currently in place.

2.3 Estates that do not have to pay IHT

- 2.3.1 We do not consider that there are significant administrative or compliance burdens in respect of estates that fall within the Nil Rate Band ('NRB').
- 2.3.2 However, to simplify the procedure in these cases, we propose that the relevant IHT form (IHT 205) should allow for a single 'tick box' option that has the effect of confirming that the value of the deceased's estate falls below the Nil Rate Band threshold and/or where a spouse exemption applies.

2.4 Administering an estate, record keeping and valuations

- 2.4.1 The administration of a deceased's estate often and, arguably, should in all cases, require the executors to obtain an appropriate level of professional advice. Where executors do not feel able to take up their appointment as an executor, they can refuse to be appointed.
- 2.4.2 In the majority of cases, the administration of an estate and the role of executors can be properly managed with sound advice from relevant professionals.
- 2.4.3 The requirement for Executors to disclose any gifts made in the seven years before the date of death is often burdensome with a lack of accurate information available to them. This is particularly difficult for professionals acting as executors where a potential PI issue arises if they do not have sufficient records available to them at the time of the submission. We would propose a shorter reference period of 2 to 3 years before the date of death.



- 2.4.4 To assist with the issues raised in 2.4.3 above, the current Income Tax return does not require submission of details relating to capital purchases in the relevant year. In order to provide further assistance to executors in collating accurate records of capital assets, we would suggest that Income Tax returns should provide a section that requires capital purchases to be recorded over and above a de-minimis threshold.
- 2.4.5 With further reference to obtaining financial records, there should be a simplified mechanism for executors to obtain copies of the deceased's tax returns. The mechanism could also provide for a standard disclosure by HMRC to the executors (on request) of the completed tax return for each of the preceding 12 years prior to the date of death.

3.0 LIFETIME GIFTS TO INDIVIDUALS

- 3.1 With reference to our previous comments regarding obtaining an appropriate level of professional advice, the rules in respect of lifetime gifts and reservation of benefit are well understood.
- 3.2 However, there remains some confusion in relation to the rules relating to lifetime gifts of agricultural property. Often it is misunderstood that so long as the property continues to be used as agricultural property after the gift, there is no additional requirement for the transferor to survive 7 years in order for it to qualify for the full agricultural property relief on death. Clearer guidance on this should be considered in HMRC guidance; particularly for those who are not taking specialist advice.
- 3.3 The rules around the calculation of the cumulative total where there have been PETs (Potentially Exempt Transfers) and lifetime trusts are understood by professionals but are particularly complex and arguably beyond the understanding of even an educated and interested lay person.
- 3.4 As part of our review of the Call for Evidence, it is apparent that little consideration has been given to the thresholds for annual exempt gifts (£3,000 per individual). Some allowances do not appear to have been revised in line with inflation for over 30 years.
- 3.5 We therefore propose that as part of any review of wider IHT provisions in addition to the principal objective of simplification, that the annual exempt threshold should be reviewed. We recommend a two-step approach; first that the annual exemption of £3,000 is increased in line with equivalent value today



and secondly, a provision is introduced whereby the annual exemption is then increased annually in line with the appropriate index. This should also apply to the other annual fixed exemptions.

- 3.6 We also wish to highlight a further area of review in relation to exemptions for gifts made out of income, which are generally poorly understood outside the professional adviser sector. Also, we consider that the exemption rules should be extended to include withdrawals from investment bonds. This widening of exemption rules should also include the provision for averaging, where, for example, income fluctuates widely.

4.0 BUSINESSES

- 4.1 As a general comment, businesses are well advised by professionals in this area and would be advised to take tax advice by ancillary professions where tax implications form part of a wider holistic approach to business strategy.
- 4.2 We acknowledge that there are inevitable complexities in applying reliefs for businesses where the reliefs are dependant on trading activity. However, we question the need for further simplification, where businesses are, in the main, advised.
- 4.3 It is our members' experience that whilst IHT planning is an important consideration in business planning and does (and should) feature in decision making, the principal drivers are commercial rather than tax focussed.
- 4.4 With specific reference to the availability of BPR not generally being dependant on the size of a person's interest, we do not consider that this adds complexity and would suggest it reduces it. It promotes decision making based on commercial drivers rather than tax drivers. A threshold for BPR availability would inevitably lead to an unnecessary influence on business structure and decisions.
- 4.5 The reliefs under BPR are important but diversification decisions in the main, are driven by the need for income. If the diversification project yields a sufficient income, it is unlikely given the current IHT regime, that IHT considerations will affect the decision to progress such a project; other than in the tenanted sector, where diversification by the Tenant could result in loss of APR for the Landlord. If the Landlord's consent is then not forthcoming for the



Tenant to diversify, as a consequence of the Landlord's IHT position, this is a potentially adverse impact on the Tenant's business.

5 FARMING BUSINESSES

- 5.1 We refer you to our comments under 4.0 above where the general principles of reliefs are well understood in the farming sector.
- 5.2 However, it is the quality of advice being obtained that can be the issue. Whilst our members who advise on IHT in the context of agricultural property are suitably qualified to do so, advice obtained from non-specialists can lead to incorrect submissions to HMRC; where the correct reliefs have not been properly claimed/applied to the estate. This can often be the case with APR claims for land subject to tenancies under the Agricultural Holdings Act 1986 which commenced pre-1 September 1995 and those which commenced post-1 September 1995 where the rates are different (50% and 100% respectively). With this in mind, the policy objective of providing a viable and sound market for letting agricultural land as an objective of the changes in 1995 remains the same today as it did then. We would suggest a single rate of relief at 100% would greatly simplify this area; also providing an equal treatment of all agricultural land whether let or owner-occupied and thereby minimising tax policy as a driver for business decisions.
- 5.3 We do not consider that there is any merit in merging APR and BPR as we consider this would have adverse effects on the tenanted sector. We consider there would be a significant loss of land available for rent (for example, an estate which is predominately or wholly formed of let agricultural holdings and for which APR reliefs apply, could potentially reconsider their approach where APR was no longer available, and the estate was then relying solely on BPR and the associated rules on trading activity which could result in a switch away from letting).
- 5.4 There remain clearly distinct policy objectives for the retention of APR and BPR as they exist for different reasons. One is to keep the agricultural estate intact for multi-generational occupation, the other protects and secures longevity of the business. APR plays a role distinct from BPR in allowing rural businesses that do not qualify as 'trading' under BPR to be transferred on death in a manner that preserves their integrity and is least disruptive of the businesses and individuals who depend upon them, for example, tenants (commercial agricultural or residential), contractors and employees.



- 5.5 The availability of both APR/BPR prevents fragmentation of an agricultural estate where these important reliefs ensure that an estate can be maintained intact and its viability protected for the next generation. Removal of APR would undoubtedly lead to sales to fund IHT liabilities and inevitable breakup of farming businesses and the potential consequences for future viability and productivity (key policy objectives in the context of other Government policy areas for the sector).
- 5.6 The current mix of APR/BPR reliefs provide stability to tenants of landlords where transfers of ownership arising from a need to fund IHT on the death of one generation of owner by the next are prevented thereby providing security to the tenant farmer where ownership by the same landlord family (often multi-generational in their ownership) continues.
- 5.7 It also assists in maintaining cash resources (often limited resources) within the agricultural enterprise in order to protect availability of cash and assets against which monies can be borrowed for reinvestment.
- 5.8 In the context of the valuation of farmhouses and the application of APR, this remains an area of significant discord between the approach by HMRC/District Valuers and those advising/valuing agricultural estates.
- 5.9 The practice by valuers on behalf of HMRC adopting an initial approach of discounting farmhouse market values by 30%, before any detailed assessment of farmhouses by a case by case basis, to arrive at an assumed agricultural value which qualifies for APR with the balance receiving no relief, does not recognise that in most cases, the character, situation and use of the farmhouse should give rise to APR on the full market value. Furthermore, there are many instances where the size, character and situation of a farm means there is more than one dwelling which should qualify for APR.
- 5.10 This is an area that requires significant improvement in the approach to valuation by HMRC/District Valuers which should be based on the individual facts of each case and not an assumed general discount which is applied in all cases. The valuation of farmhouses must be on the approach that the dwelling is a farmhouse and the specific facts of the case will determine if there is any valuation reason for departing from that principle in arriving at the market value; not an approach that pre-determines that every farmhouse should have



a discount applied to its market value that subjectively represents an 'agricultural value'.

- 5.11 If APR were extended to include the houses of retired farmers, this would remove an incentive to continue farming, sometimes unproductively in ill health or later life in order to qualify for the relief. This may have the effect of making more land available to new entrants, including the tenanted sector.

6 CHARITABLE GIVING

- 6.1 As we have previously commented, whilst the rules for charitable giving may prove difficult to understand for the lay person, where advice is sought, the rules are generally understood.

7 OTHER AREAS OF COMPLEXITY

- 7.1 The introduction and application of the Residential Nil Rate Band ('RNRB') has added unnecessary complexity to the understanding of this relief.
- 7.2 We consider that the RNRB should be abolished conditional on a consequent increase in the NRB threshold for an individual to £500,000 which would be a significant step towards simplification in all circumstances.
- 7.3 In respect of woodland, the assessment of what constitutes woodland that is "ancillary" to agricultural property is subjective and therefore already difficult. This difficulty will be compounded by a change in impetus from DEFRA towards the promotion environmental public goods over an area-based payment system. We would welcome a simplification to the effect that land under a statutory land management scheme that is not a commercially managed woodland be considered as part of the agricultural holding.

8.0 WIDER IHT SYSTEM

- 8.1 In respect of the reference to a higher NRB, see our comments in 7 above.
- 8.2 In respect of the reference to a graduated rate, in our view this would add complexity and would not achieve any form of simplification. This is evidenced by the operation of the RNRB, as an example.



- 8.3 In the context of the UK's exit from the European Union, taxation policy and any forms of proposed simplification must pay due regard to the wider agricultural policy in the UK. An absence of co-ordination in this respect may have unintended consequences for the agricultural sector.
- 8.4 Furthermore, we are concerned over the future implications for the ownership of agricultural assets by UK residents outside the UK and specifically in the case of the island of Ireland, where for example agricultural property either side of the border is owned by the same person and used in their overall agricultural enterprise. It is important that where IHT reliefs currently apply to the agricultural property owned outside the UK that this should continue following the UK's exit from the EU. A further example are circumstances where land is owned in both the UK and EU and is used for vegetable production. The land owned in the EU ensures continuity of supply and economic viability of the owner's whole agricultural enterprise and the reliefs should be maintained to protect that future viability.

9.0 CONCLUSION

We have welcomed the opportunity to discuss this Call for Evidence with the Office of Tax Simplification and with other stakeholders in the agricultural sector. We look forward to continual engagement with the OTS once it has completed its review of the submissions to the Call for Evidence.