

Diversification of farmland (Lecture B1397 – 12.48 minutes)

With challenges like reducing subsidies and rising costs, farmers in many parts of the UK are increasingly looking at other potential sources of revenue beyond the traditional income from their farm.

Environmental and ecological diversification of agricultural land is one option, but it should be borne in mind that a move away from mainstream farming may well be at the cost of the landowner's IHT reliefs.

Farmland usually qualifies for 100% agricultural relief, saving a 40% IHT charge on, e.g., death. This enables the business to be passed onto younger members of the family and to continue operating without part of it having to be sold or to be burdened with debt to pay a tax bill.

Depending on the type of diversification being considered, there are knock-on impacts which need to be considered. For example, if the farmer diversifies into renewables, the land may no longer attract agricultural relief, unless this becomes an integral part of the agricultural business such as providing power for the principal farming activities. Of course, the farmland may still qualify for business relief, but it would not do so where the land is leased to someone else so that they can build wind turbines.

A joint venture could be the appropriate solution in these circumstances.

With woodlands, agricultural relief is only available if they are an integral part of the farm such as shelter belts, game coverts or coppices grown for fencing materials on the farm. The relief is lost if the farmer goes into commercial forestry and grows timber to sell, given that this counts as a non-agricultural activity. On the other hand, business relief may apply.

As far as the farmhouse is concerned, agricultural relief is available, but only if that property is at the centre of the farming business and is appropriate in size and nature to the relevant operations. Moving the running of the business to an office in an outbuilding might make sense from a practical perspective but be warned that relief on the farmhouse will be lost.

Where the farmhouse remains the hub of the farming business, there is still a risk of losing agricultural relief on the property if the farmer has diversified his business to the extent that most of the activities carried out are essentially non-agricultural. In such situations, farmers are generally advised that separate business vehicles will be the right option: one for the farm and the house and one for the other business activities. This is subject to the proviso that the farmhouse is not then out of proportion to the agricultural operations. As one well-known commentator has pointed out:

'By recognising the risks, the entitlement to relief can . . . be managed by the landowner so that the relief is fully preserved and not lost altogether on the whole business – or at worst (the projects are structured) so that the main business continues to qualify, even if the environmental projects cannot.'

Of course, if contractors or other personnel are brought in to help with the running of the farm, agricultural relief may be lost on the farmhouse unless the owner is still the farmer and decision-maker. It will be important to be able to provide evidence of this. Even if relief is not available on the farmhouse, the owner would still expect his land to qualify.

If a farmer does miss out on agricultural relief as a result of diversifying away from farming into other activities, business relief – as has already been mentioned – can be helpful.

However, relief for relevant business property is not available where the business is wholly or mainly an investment in land. This means that, if the diversification tips the balance from mainly farming to mainly letting (such as holiday or residential lets or letting land out to others), business relief will not be available and the farmer will not benefit from any IHT reliefs.

Diversification can cause farmers to lose relief for their original activities, but there are ways to mitigate this. One approach is that the diversified elements of the business (which attract no IHT reliefs) can be structured separately in order to protect the core relieved activities.

All the elements of a farming business need to be examined before diversification happens. Commercial opportunities should be uppermost in the farmer's mind, but IHT is always going to be an important factor. Careful planning and structuring can go a long way to protecting the availability of key IHT reliefs.

Contributed by Robert Jamieson