

The TRIG Reforms and Taxation

By Sarah Denney-Richards and Alan Neal



TRIG Reforms



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What is TRIG?

The Tenancy Reform Industry Group ("TRIG") was convened to advise the Government on issues relating to the tenanted sector of the agricultural industry in England and Wales. Its aim was to increase the overall and "general health" of the industry and concentrate on measures which would encourage diversification.

TRIG was a group of individuals drawn from all sectors of the agricultural industry; ranging from professional organisations, Government members and independent organisations.

TRIG's final report was published in May 2003. Many of its recommendations were implemented in the Regulatory Reform (Agricultural Tenancies) (England and Wales) Order 2006 SI 2006/2805 ("the Reform Order") which took effect from 19th October 2006.

TRIG and the Agricultural Holdings Act 1986 ("the 1986 Act")

One of TRIG's key recommendations was to encourage flexibility in tenancies protected under the 1986 Act ("AHA Tenancies") whilst ensuring that the tenant did not lose its protection under the 1986 Act.

In particular it sought to clarify the circumstances in which existing AHA Tenancies could be extended (e.g. by adding land and buildings or by granting to a nominated successor) whilst preserving their legal status.

Previously where land had been added to an AHA Tenancy, there was uncertainty as to whether a surrender and immediate regrant of the holding back to the landlord had taken place, thereby creating a new tenancy which had no protection under the 1986 Act. TRIG sought to remove this as well as other legislative uncertainties.

Amendments to the Agricultural Tenancies Act 1995 ("the 1995 Act")

The general rule is that all tenancies of agricultural holdings beginning on or after 1st September 1995 shall be governed by the 1995 Act rather than the 1986 Act. Tenancies created under the 1995 Act are known as farm business tenancies ("FBT").

There are a number of exceptions to this general rule which are set out in subsection 1(a) to (g) of section 4 of the 1995 Act.

If the tenancy is one which falls within one of these subsections, then it shall be a tenancy created on or after 1st September 1995 but which falls within the 1986 Act.

Following TRIG's recommendations the following amendments were made to section 4 of the 1995 Act by the Reform Order:-

Section 4(1)(d) – agreed succession

It had always been the case that agreed successions resulting in the grant of a new tenancy after 1st September 1995 would be protected under the 1986 Act. However difficulties interpreting this section led to parties seeking Agricultural Land Tribunal orders for such arrangements, through fear of creating an FBT. TRIG sought to remove this uncertainty.

Whilst the wording of section 4(1)(d) remains the same, section 4(2) seeks to clarify the circumstances in which section 4(1)(d) will apply by permitting agreed succession to a close relative provided procedural conditions are followed.

Section 4(1)(f) and (g)- surrender and regrant

It was acknowledged by TRIG that any minor variations to the area of a holding comprised in an AHA Holding were caught by the original section 4(1)(f). However it was not sufficiently clear what was a minor variation; if a building was added to a tenancy would it increase the holding to such an extent as to trigger an inadvertent surrender of the AHA Tenancy and regrant of an FBT? This was a risk many tenants were not willing to take. It was felt that such uncertainty was preventing the growth of the tenanted sector. TRIG sought to remove this uncertainty by amending section 4(1)(f) (which addresses inadvertent surrenders and regrants) and adding a new provision under section 4(1)(g) dealing with express agreements.

Section 4(1)(f) now permits additional parcels of land or buildings to be brought within an existing AHA Tenancy provided that the original holding formed the "whole or a substantial part" of the new holding.

Section 4(1)(g) goes further. Where there is a written contract of tenancy which states that the 1986 Act is to apply and the tenant previously held a AHA Tenancy of all or a "substantial part" of the holding comprised in the new tenancy, the new agreement shall be a tenancy created on or after 1st September 1995 but which falls within the 1986 Act. Provided the conditions are satisfied this will allow parties the liberty to consciously bring land and buildings into an existing AHA Tenancy without risking the 1986 Act protection.



By Alan Neal

The TRIG Reforms explained by Sarah Overleaf have opened the door to landlords to improve the level of Agricultural Property Relief ("APR") they receive on agricultural property that they own which is let on an AHA tenancy. Broadly speaking, relief on the freehold reversion property let on an AHA tenancy, provided that the other qualifying conditions are met, will receive APR at the rate of 50%. What this means is that

Inheritance Tax will be paid on the full market value of the property reduced by one half of the agricultural value of that property. If the agricultural value and market value equate then in simple terms the rate of IHT is reduced from 40% to 20%.

The rate of relief can be increased to 100% where a tenancy is granted after 1st September 1995 or in respect of an AHA tenancy granted before that date if a succession tenancy comes in to existence after that date. By utilising the new provisions, particularly those set out in sub clauses (d) (f) and (g), as explained by Sarah Overleaf, it is now much easier to negotiate a position where the tenancy will be treated for IHT purposes being granted after 1st September 1995 thereby giving the landlord 100% APR, whilst the tenant retains his security.

That is the easy part but there are other taxes that need to be considered if one is going to go down this particular route:

1. Capital Gains Tax

Whilst technically the termination of the old tenancy and the grant of the new successor tenancy under the TRIG Reforms will be treated as a disposal by the outgoing tenant of his tenancy, the view of leading Tax Counsel is that there will be no capital gains tax liability arising either on landlord or tenant by going through the process.

2. Stamp Duty Land Tax

The position here is quite technical and leading Tax Counsel takes the view that in most straightforward cases no SDLT liability should arise. However, care needs to be taken to analyse the details of the transaction very carefully and particularly to consider the technical valuation issues that arise under the legislation to ensure that this is the case.

3. Income Tax

There is, however, one area of potential difficulty which relates to the situation where a landowner, has let agricultural property on a AHA tenancy to a company of which he is a shareholder. There is provision within the income tax legislation that if a shareholder receives value from a company in respect of which full consideration is not given by him the difference between the amount received and the consideration given will be treated as a dividend and therefore be subject to income tax. The amount of the

distribution is deemed to carry a non refundable tax credit of 10%. If the landlord/shareholder is a basic rate taxpayer then no income tax will arise as the tax credit is deemed to cover the liability. If, however, the landlord/shareholder is a higher rate taxpayer then, effectively, under present rates of tax, an income tax charge equivalent to 25% of the value deemed to be received will have to be paid in tax. Please bear in mind that the amount of value deemed to be received by the company will be added on top of the landlord's/shareholder's income in order to work out whether or not higher rate tax applies. If the value is substantial this could take a landlord/shareholder who is normally a basic rate taxpayer into higher rates of tax in any event.

As a result of the proposals announced in the Budget, from 6th April 2010 Income Tax rates will rise to 50% (42.5% on dividend income) where total income is over £150,000, and Personal Allowances will be reduced where total income is over £100,000. The effect of the latter is to create a marginal rate of Income Tax for those with incomes between £100,000 and approximately £113,000 of 60%. A deemed Income Tax charge on the surrender of a company tenancy could therefore prove very expensive.

Whether or not the tax charge arises depends upon whether or not there is any value passing. This is not a straight forward valuation exercise since it requires valuing the tenancy being surrendered on the one hand and the value of the tenancy being granted on the other. I am aware of a situation where unfortunately the valuers got the figures very wrong which resulted in the landlord/taxpayer being faced with a very large income tax bill which was quite unexpected.

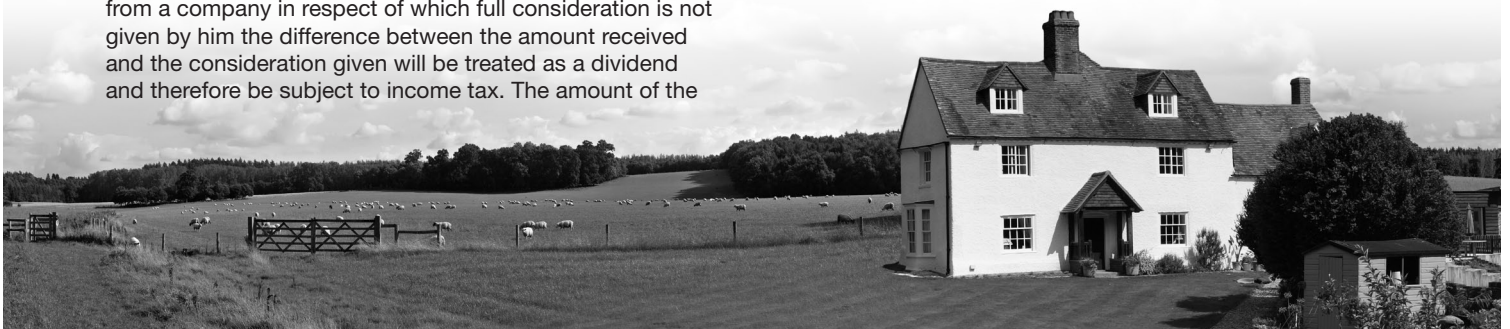
This situation will not arise in the event that the landlord is not a shareholder of the company/tenant.

The conclusion therefore is that unless you are in a situation where you have let land to a company of which you are a shareholder, where considerable care needs to be exercised, there are considerable advantages for landlords in using the TRIG Reforms to enhance the level of their agricultural property relief thereby reducing their ultimate liability to inheritance tax.

In all cases, however, it is essential to obtain good, expert professional advice in advance to ensure that the transactions are carried through properly and taxation pitfalls avoided.

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mfg Solicitors on:**

0845 55 55 321



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