Will I have to pay CGT on sale of shared house?

Q I have farmed our family farm all my working life, initially along with my father and then, for the last 30 years since his retirement, on my own. Since that time I've also occupied the farmhouse.

When our father died in 2008 I inherited the farm jointly with my brother and sister and we own it as "tenants in common". My siblings have no involvement in or income from the farm, on the understanding that when I retire in a couple of years' time we will sell the property and divide the income equally between us.

My query is simply when we do sell, will I qualify for 100% tax relief, as I am effectively selling the house I own, and have occupied for the last 30 years, or should we rearrange the ownership so that I own only the house and my brother and sister only own the buildings and land. We would still split all the proceeds equally between us.

Mark Chatterton
Director
Duncan & Toplis

A The first point to mention is that you, your brother, and your sister are all taxed independently from each other, despite jointly owning the farm. Your individual personal circumstances will affect your tax position.

The disposal of the farm as a whole will be liable to capital gains tax, and certain reliefs could apply.

As a reminder, capital gains tax is charged on the profit arising on the difference between the net sale proceeds, and the acquisition cost. In your circumstances, the acquisition cost will be the probate value when your father died in 2008.

The farmhouse will be taxed separately to the land and buildings, and as you have lived in the property, you will not be required to pay capital gains tax on the disposal. This is because the farmhouse has been your Principal Private Residence (PPR) throughout the period of ownership.

Your siblings will be taxed fully on the gain, as they have not lived in the property while they were joint owners. As farmhouses are residential property, the rates of tax will be 18%, while the gain falls within the basic income tax band, or 28% on any amount above this.

The farmland and any farm buildings are not treated as residential properties, and therefore are taxed at lower rates of capital gains tax. These are 10%, while the gain falls within the basic income tax band, or 20% on any amount above this.

As you have personally farmed the land, assuming the farm is sold in its entirety, Entrepreneurs' Relief (ER), may be claimed, making the tax rate 10% up to £10m of gains. Your siblings, having not been involved with the farming operations within the 12 months prior to disposal, will not be able to claim ER, thus the majority of their gain is taxable at 20%.

It is important for clients to sort out property and business ownership at an early stage to maximise potential reliefs. Ideally an individual should own 100% of the house they live in to secure full Principal Private Residence relief, so preferably you would have owned all of the farmhouse rather than just a one-third share.

Unfortunately this is difficult to achieve now since any transfer to you by your siblings would incur a charge to capital gains tax as if the property were sold at market value. This would accelerate their share of capital gains tax, and only protect any growth between now and the date of sale from the charge to tax. Therefore this may well not be tax efficient unless their gains could be covered by their annual exemptions.

Additionally, have you considered bringing your siblings into partnership for at least a year before a sale to maximise the availability of Entrepreneurs' Relief? Depending on the sums involved, this could near enough halve their share of the tax bill.

DO YOU HAVE A QUESTION FOR THE PANEL?

Outline the issue in no more than 350 words and *Farmers Weekly* will put your question to a member of the panel. Please give as much information as possible.

Send your enquiry to Business Clinic, *Farmers Weekly*, RBI, Quadrant House, The Quadrant, Sutton, Surrey SM2 5AS. You can also email your questions to fwbusinessclinic@rbi.co.uk

How can options help cut grain price risk?

Q I keep hearing about the use of options in grain marketing as a means of managing risk and protecting income for a business. How do they work and what are the level of costs involved?

Andrew Wraith
Director
Savills food and farming

A There are two types of option: a put option and a call option, which can be considered much like an insurance policy. A put option is effectively the buying of "insurance" against a fall in grain prices without removing the potential to sell your physical crops at a higher price in the future. In the same way as you take insurance out for a tractor or any piece of equipment, the hope is that it will not be necessary to make a claim, but should there be an incident you are covered for the value of the item at that period in time.

It is obviously far more agreeable to be able to sell the physical crop at a higher price but if the market should fall you are guaranteed a pre-determined price for the crop. In practice, a grain merchant offers to buy 300t of your wheat at £140/t for November 2018. You decide not to take it because there is some prospect of a market increase but the prospect of a significant market collapse isn't affordable.

Instead you are prepared to buy a put option through a broker based on November 2018 futures at £145/t. It costs £8/t so for 300t the cost is £2,400. If the market stays strong and goes up, whatever the grain is sold at, then the £8 premium is effectively lost but the upside is on the physical sale.

Those facing a large capital gains tax bill may be able to make use of Entrepreneurs' Relief

If prices fall back then once futures drop below £136/t you make money on the option after taking the cost of the option into account to add to the physical sale of any wheat, effectively locking out a minimum base price for the wheat.

A call option is "insurance" against upward price movements. If you have a lack of storage for grain or need to sell some crop to ease cashflow, a call option will enable you to still benefit from a rise in grain prices.

Because the physical crop has already been sold you are not at risk from falling prices and your risk is limited to the cost of the premium you have paid for the option. You buy a call option at £145/t for November 2018 for 300t priced at £8/t and this starts making money, allowing for the cost of the option, once the futures price goes above £153/t.

There are two ways of buying options. Either via a Financial Conduct Authority registered broker, through whom you set up an account, or over the counter via a merchant or grain trader. In both cases the option still needs to be monitored and managed to ensure it achieves what it sets out to do.

The costs of buying options are valued on three variables: the strike price at which the underlying futures price is set; time value – how long the contract has to run; and volatility in the market.

The strike price is the level at which you look to take protection against price volatility and is based upon the difference between the agreed level at which the call or put option is activated and the actual futures price at the same point in time.

As with any insurance policy, the longer the time period, the greater the premium. So a harvest option which expires in November may cost £3/t, whereas an option expiring in the following May might cost £7/t.

Market volatility is also factored into the price. During a period of bad weather when the market is more volatile, the cost of purchase will be higher than during a period of market stability.

Should we put our estate into a long-term trust?

Q My wife and I are in our reclining years with our younger generation managing the estate. On our deaths we are considering putting the farm into a single 125-year discretionary trust, managed by our offspring. We would like to know what does this involve? What are the drawbacks and advantages? What are the tax implications?

Carol Ward
Solicitor
Thrings

A On the face of it, there would be no difficulty in putting the farm into a discretionary trust on your deaths. This could be achieved by drafting your wills to ensure that, on the latter of either your death, or your wife's if she survives you, the estate passes to a discretionary trust that would be managed by your children as trustees.

One advantage of putting the farm into a discretionary trust is that there is some control over the ultimate devolution of the farm.

By placing it into trust, the estate can be kept in the family and can be passed down to the next generation by including future grandchildren and great-grandchildren within the class of beneficiaries. The younger generation would then be able to continue managing the estate.

Another advantage is that the farm would not fall into your children's estates for inheritance tax and it would also be separate from their personal assets in the event of a marriage breakdown.

A disadvantage of a discretionary trust is that the trust does need to be formally managed, with trustee meetings held and accounts prepared. There is an administrative burden that would not exist if you passed your estate to your children outright. Over recent years, there have also been numerous regulations brought in that impose a more onerous compliance burden on trustees.

Placing a farm into a discretionary trust will ensure it can be kept in the family

The trust will have its own nil-rate band and as a discretionary trust it will be subject to a specific tax regime, called the "relevant property regime".

As part of this regime, the trust that you create under your wills will be subject to inheritance tax every 10 years, with the first anniversary occurring 10 years after the latter of either your death or your wife's if she survives you.

There will potentially also be inheritance tax charges on distributions of capital from the trust. The rate and amount of tax would depend on various factors, such as the amount by which the value of the trust assets exceed the available nil-rate band, the length of time the assets have been in the trust and also whether any reliefs, such as agricultural property relief or business property relief, are available on the trust assets at the relevant time. The tax computations are complex but any tax charge would not exceed 6% of the value of the fund.

Trustees pay income tax at the higher rate of 45% (or 38.1% on dividend income) and would be subject to capital gains tax at 20% (or 28% for residential property). There are certain reliefs from capital gains tax that may be available and the trustees would also benefit from an annual exemption, although this is only half of the exemption available to individuals.

There are many factors that influence clients' decisions as to whether they wish to proceed with a discretionary trust or whether they ultimately decide to pass down their estate to their children outright. A detailed discussion with your solicitor about your assets, wishes and family circumstances will enable you to decide whether putting in place a discretionary trust would be the most appropriate course of action for you.