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Answer-to-Question- _1_

Report

To: John and Margaret Austin

From: Nicola Askbridge

Date: 08 May 2025

Subject: Future planning of the farm

Introduction

Following on from our meeting on 1 May 2025, please see the report with considers the the future planning of Low Beck Farm ("LBF").

The report will cover the following areas:

1. Inclusion of Fred in the partnership
2. John selling the field
3. Gifting the outbuilding to Fred
4. Inheritance tax implications
5. Conversion of the outbuilding

The report has been prepared solely for the use of John and Margaret Austin. No responsibility will be taken from the use of the report by any other party.

The report has been written based on the figures and facts which were provided in our meeting.

Executive Summary

Inclusion of Fred

Where made is made an employee and given a salary of £25,000 for only working eight hours a week, HMRC could challenge this and state it is way of you both no being subject to income tax on these profits as they would be covered by Fred's losses.

If Fred was a made a partner, you both would be disposing of a 12.5% interest in LBF. This will be a chargeable disposal for capital gains and will result in capital gains tax of £16,373 each.

Business asset disposal relief is available on the disposal and would reduce your capital gains tax to 9,075 each. Fred will have a base cost of 487,500.

An election for gift relief can be made on the disposal and will result in no capital gains tax. However, this will means Fred has a base cost of £300,000 and your gains will be deferred until Fred sells his shares in the partnership.

I recommend that Fred is made a partner and a gift relief is claimed. This is because HMRC will not be able to challenge the salary paid to fred and by claiming gift relief, no capital gains tax will be due for you both.

Sale of John's Field

Where the field is sold before Fred is made a partner, the disposal will be liable to capital gains tax at 10% and 20%. Majority of the gain will be subject to capital gains tax at 20%. The capital gains tax payable will be £28,333.

If the field was to be sold soon after Fred is made a partner, it will qualify for business asset disposal relief and taxed at 10%. This will result in a tax payable of £15,000.

I recommend the field is sold soon after Fred is made a partner because it will save you around £13,000 in tax.

Gifting of outbuilding to Fred

The gift to Fred immediately or after the conversion would result in a CGT liability for each of you. This will be subject to tax at 20% given your other planned disposals.

Where the gift is made after Fred becomes a partner, this should qualify for BADR as an associated disposal and therefore, CGT payable at 10%.

As the asset is a business asset, it will qualify for GR and this will result in no immediate CGT liability. Fred will inherit your base cost of the outbuilding.

Where the outbuilding is left to Fred in your wills, there will be no CGT payable when the outbuilding is transferred to him and he will receive a tax free uplift on the cost of the market value when you pass away.

I recommend that the outbuilding is left to Fred in your wills. This is because no CGT will be due and he will receive a tax free uplift for his base cost.

Inheritance tax

A gift made in your lifetime will be a potentially exempt transfer and only liable to inheritance tax should you not survive seven years. If you were to survive seven years, no inheritance tax would be due.

Agricultural property relief is available on farmland and farmbuildings used for the purpose of farming which has been owned for at least two years. Therefore, all the land and building within the partnership qualify for APR at 100%.

Business property relief is available on business assets which includes interest in a trading partnership that has been owned for at least two years. Each of your partnership interest will qualify for 100% BPR.

Where the gift of the outbuilding is made immediately or after conversion, it will be a potentially exempt transfer. Therefore, if you were to pass away within seven years, there would be IHT payable as no APR and BPR will be available.

No agricultural property relief and business property relief will be available as it would not be used for the purpose of farmings and it would not be used for business purposes.

Where the outbuilding is left in your wills, it will still not qualify for APR as it will not be used for farmings purposes. However, as it will be a business asset, it will qualify for 100% BPR and no IHT will be due

I recommend that the outbuilding is left in your wills. This is because it will qualify for 100% BPR and no IHT will be due. This is in addition to the CGT free up lift on the business mentioned in the above section.

Conversion of the outbuilding

Each of you, the patners, will be liable to income tax on the rental profits.

No agricultural property relief will be available due it not being used for the purpose of farming. However business property relief will be available as its a bsi

Inclusion of Fred

Employing Fred

Where Fred is made an employee, LBF will be liable to secondary class 1 National Insurance Contributions ("NIC") on the salary paid to him. This is similar to how you will account for NIC for Georage.

The profits for the year ended 31 March 2026 will be reduced by Fred's salary and the class 1 NIC payable. As a result, the partnership will have a profit of the year ended March 2026 of £60,000 (Appendix 1).

The profits will be subject to income tax and class 4 NIC for each of you as usual. Therefore, for the 2025/26, you both will be basic rate taxpayers and paying tax at 20%.

Each of your income tax liability, after deducting your personal allowance will be £3,486 (£17,430 x 20%).

Class 4 NIC payable will be £1,046 (£17,430 x 6%).

Given that George is employee on a full-time basis and earning a salary of £24,000 per annum, it could be seen an unreasonable for Fred to be earnings a salary of £25,000 whilst only working eight hours per week.

HMRC could challenge this, especially as his employment income could be covered by

his trading losses, by stating the salary is unreasonable. In addition to this, HMRC may state that it is a way of John and Margaret diverting their income to Fred and not paying tax.

Making Fred a partner

Capital Gains Tax

Where Fred is made a partner, this will be a disposal for Capital Gains Tax ("CGT") purposes. You both will be disposing of a 12.5% share each in the partnership.

As Fred is a connected person to you, the disposal proceeds will be the market value of the partnership which is currently £1,950,000. As each of you will be disposing of a 12.5% interest in LBF.

Due to you disposing of a 12.5% interest in LBF, the proceeds will be 12.5% of the market value. You both will have a chargeable gain of £90,750.

The gain will be taxed at 10% and 20%. Part of the gain which falls into both of your basic rate bands, will be taxed at 10% and the remainder at 20%. Based on the Fred being made a partner on 1 July 2025, you both will have a CGT liability of £16,373 (Appendix 2).

Fred will have a base cost of £487,500.

Where there is a material disposal of a business and certain conditions are met, Business Asset Disposal Relief ("BADR") will be able.

A material disposal if at least a 5% interest in the patnership. As you both will be disposing of a 12.5% interest, this condition will be met.

In addition to the above, the other condition will are required to be met are:

1. The partnership must be a trading partnership - which the patnership is;
2. The partnership must be each of your personal partnership i.e. you have at least 5% interest in the partnership - you both have a 50% interest so this condition is met; and
3. You work in the partnership either full-time or part time - which you both do.

As you both meet all the conditions, BADR can be claimed on the disposal. As a result, all the taxable gain will be subject to tax at 10%. Therefore, you both will have CGT payable of £9,075 (£90,570 x 10%). This will reduce your CGT by £7,298 each.

CGT will be payable by 31 January 2027. BADR will need to be claimed on your tax returns by 31 January 2028 but I will claim this on your 2025/26 tax returns.

Another form of relief will can be claimed is Gift Relief ("GR"). GR can be claimed on business assets which includes the interest in a trading partnership. As LBF is a trading partnership, this qualifies as for GR.

As you both are expected Fred not to contribute anything to the partnership, 100% GR is available. The effect of GR is that it will reduce each of your gains to nil and reduce Fred's base cost by the chargeable gains. In effect, Fred will acquire each of your base costs of £150,000 giving him a total base cost of £300,000.

GR effectively defers the gain until Fred will sell his partnership asset.

A claim for GR is a joint election and will be required to be made between Fred and John and Fred and Margaret. The election must be made by 5 April 2030.

I recommend that Fred is made a partner and GR is claimed. This is because HMRC will not be able to challenge the unreasonable salary paid to Fred if he was made an employee and his partnership profits will be covered by his losses so no tax will be payable.

In addition to the above, GR will allow you both to have no CGT payable on the disposal of your partnership interest.

The implications of making Fred a partner on inheritance tax are discussed below.

The rest of my report will be based on my recommendation of Fred being made a partner on 1 July 2025.

Sale of Field owned by John

The sale of the field by John will be a chargeable disposal for capital gains tax.

The gain will be calculated using the consideration received, assuming it is not disposed to a connected person, less the cost of the field. The cost of the field is £100,000 (the probate value on the death of his mother).

The disposal would give rise to a chargeable gain of £150,000 (£250,000 - £100,000).

Where the disposal takes place before Fred is made a partner, the CGT payable will be at 10% and 20%. This will result in CGT payable of £28,223 $[(17,770 \times 10\%) + (£132,230 \times 20\%)]$.

On the other hand, where the disposal takes place after Fred is made a partner, BADR may be available because it could be an associated disposal.

As associated disposal is where the following conditions are met:

1. There has been a material disposal of a business asset; and at the same time;
2. An asset used in the business for at least 2 years before the disposal; and
3. Has been owned by the individual for 3 years before disposal

The same time will mean either 1 year after the disposal of your partnership interest of within 3 years of the disposal if it is not used for any other purposes. However, given you

need to raise funds to renovate the outbuilding, I assume the disposal will happen immediately.

As these conditions will be met, this will be an associated disposal and BADR will be available.

When the field is sold, it will qualify for BADR. Therefore, the CGT payable will be £15,000 ($£150,000 \times 10\%$). A tax saving of £13,223 compared to disposing of it before Fred is made a partner.

This is another reason as to why Fred should be made a partner as it will reduce your CGT payable on the disposal of the field.

I recommend that the field is disposed of soon after Fred is made a partner. This is because the field will qualify as an associated disposed and will be taxed at 10%.

Gifting of outbuilding to Fred

The gift of the outbuilding to Fred will be a disposal for CGT purposes. Due to Fred being a connected person, the market value at the time of the transfer will be taken as the consideration for the outbuilding.

If the gift was made immediately, the consideration would be £50,000 and if gifted after the building has been converted, the consideration deemed to be received would be

£500,000.

As a result of the above, where the building is held on to, the higher the CGT will be due.

However, GR can also be claimed on the outbuilding which will means the gain is reduced to nil and Fred will acquire the base cost of the outbuilding.

If the building was transfered to Fred after the he was made a partner and within either 1-3 years, the disposal should qualify as an assooiated disposal and qualify for BADR.

Where the property is left in your wills to Fred, there will be no CGT due and Fred's base cost will be the market value at the time of your death. Therefore, Fred will recieve a tax free uplift.

I recommend that the outbuilding is not transfered to Fred and is left to Fred in your wills. This is because there will be no CGT due and Fred will recieve a tax free uplift in value. In addition to this, if he was made a partner, he would acquire interest in the outbuilding.

Inheritance Tax

Where a gift is made during your lifetime, this will be subject to inheritance tax ("IHT"). IHT is charged on the reduction of each of your estate before and after the gift.

The value of the estate before and after will not be taken on a stand alone basis for IHT. As you both are married, both of your estates will be taken together and any decrease in value will be subject to IHT.

Where a gift is made during your lifetime, this will be a Potentially Exempt Transfer ("PET"). A PET will only be subject to IHT where either of you pass away within seven years of making the gift.

Where the gift is made during your life, it will be subject to taper relief once you have survived three years. After the three years, each year 20% of the PET will not subject to IHT.

If you were to pass away within seven years of making the gift, IHT will be payable by Fred after the consideration of IHT reliefs (see below)

Agricultural Property Relief

Agricultural Property Relief ("APR") is available on the agricultural value of agricultural property. This does not include any development value of the property but this could be covered by Business Property Relief ("BPR") (see below).

Agricultural property includes farmland and farmbuildings situated in the UK which was used for the purpose of farming.

Farmland is land or produce used for the purpose of growing crops.

Farm building include any buildings which are used for the purpose of farming activities and includes a farmhouse where the day-day-day operations of the farm are conducted from.

APR is available where the agricultural property has been owned for at least 2 years.

As you both have owned the agricultural property for more than two years, the farm and buildings have been owned since 1999, 100% APR will be available on them.

In order for APR to be available on a lifetime gift, the donee (Fred) will need to still own the property at the date of your death and use it within the business for agricultral purposes or have replaced it with another qualifying property within three years.

Business Property Relief

BPR is available of buisness assets which includes the interest in a trading partnership.

In order to qualify for BPR, the interest in the partnership must be owned for at least two years. As you both have owned interest in the partnership for many years, BPR will be available at 100%.

If the partnership was to own any excepted assets, assets which have not been used for business purposes for two years or assets not required for future use, the BPR will be

restricted. However, no excepted assets are within the partnership, 100% BPR will still be available.

In order for BPR to be available on a lifetime gift, Fred will need to still own the property at the date of your death and use it within the business or have replaced it with another qualifying asset within three years.

Gift of outbuilding to Fred immediately or after conversion

Where the gift is made to Fred either now or after its conversion, this will be a PET and will only be chargeable to IHT once you pass away.

The value of the PET will be £25,000 if gifted now or £250,000 if gifted after conversion for each of you. This is because the market value at the time the transfer is made will be shared equally amongst you both.

If you were to survive seven years from the date of the gift, no IHT would be due. However, if you do not survive seven years, there could potentially be IHT due. The IHT would be payable by Fred

If you were to pass away within seven years, as the building will not be used for the purpose of farming, no APR will be available. In addition to this, as Fred will own the outbuilding personally, it will not be a qualifying asset for BPR purposes and no BPR will be available.

This will enable Fred to take ownership of the building straightaway.

Leave outbuilding in your wills to Fred

The outbuilding will be included in your estate based on the market value and your share in the partnership.

Due to the outbuilding being converted into residential building and then rented out, it will not be used for the purpose of farming so no APR will be available.

As mentioned earlier, BPR will be restricted where the partnership have excepted assts. However, as the outbuilding will remain in the partnership and used for business purposes i.e. generating rental income for the partnership, it will qualify for 100% BPR.

The downside to this is that Fred will have to wait until both of you pass away in order to own the outbuilding. However, as he will be made a partner of the partnership, he will still own a share in it.

I recommend the outbuilding is not yet transferred to Fred and is left in your wills for Fred. This is because it will be used for business purposes and qualify for 100% BPR. This is in contrast to gifting him the outbuilding not and potentially being liable to IHT due to no APR and BPR being available.

Partnership interest

The disposal of your partnership interest will be a PET as Fred will not be making a contribution and will be a gift.

If Fred was to own the partnership interest if you were to pass away within seven years, no IHT will be payable as it will be covered by 100% BPR.

If you were to survive seven years, no IHT would be payable too.

Conversion of the outbuilding

The conversion of the outbuilding will make the outbuilding not qualifying for APR due to its purpose.

The partnership will be liable to income tax on the profits made from the renting out the building. Each partner will have their share of the profits similar to how the trading profits are allocated.

Appendices

1.Fred being an employee (profits for year ended 31 March 2026)

	£		
Profit	80,000		
Less: salary £25,000 x 9/12	(18,750)		
Less: ER NIC (£18,750 - £9,100)x 13.8%	(1,332)		
Profit	59,918		

2.Disposal of 12.5% share each

	John	Margaret	
	£	£	
Proceeds £1,950,000 x 12.5%	243,750	243,750	
Less: cost £1,200,000 x 12.5%	(150,000)	(150,000)	
Gain	93,750	93,750	
Less: AE	(3,000)	(3,000)	

Taxable gain	90,750	90,750	
Tax at 10% [£37,700 - (£32,500 - £12,570)] = £17,770 x 10%	1,777	1,777	
Tax at 20% £90,750 - £17,700 = £72,980 x 20%	<u>14,596</u>	<u>14,956</u>	
Total CGT payable	16,373	16,373	

3. Partnership income

	Total	John	Margaret	Fred
	£	£	£	£
1 April - 30 June 2025				
Profit £80,000 x 3/12	20,000			
	<u>(20,000)</u>	10,000	10,000	
	-			
1 July 2025 - 31 March 2026				
£80,000 x 9/12	60,000			
	<u>(60,000)</u>	22,500	22,500	15,000
	-			
Total		32,500	32,500	15,000
