May 2013

Business - Louise Hosking, Ellacotts LLP

Income tax

Income arising from the sale of electricity generated by systems installed at or near domestic premises, where the individual receiving the income occupies those premises and the intention is to generate electricity mainly for use in those premises, is exempt from income tax. Otherwise the income that is received for the energy or heat generated will be taxable as trading income.

In the first year a tax loss may be expected as the capital allowances available are likely to be greater than the income received. This loss could be offset against other income and potentially reduce personal tax bills and generate a cash flow benefit. The loss could create a tax saving of up to 62% depending on the rate of tax that the individual is liable to.

In subsequent years, the income received from the generation of energy or heat will be taxed at the relevant rate depending on the individual's other income. As a trade, the income will also attract class 4 national insurance at 9% on self-employed profits between £7,755 and £41,450 and 2% on profits over £41,450.

If the renewable project is undertaken by a limited company, the rate of tax will be 20% if it is a small company. It is sensible to review the most appropriate business structure for your renewable project, as corporate structures provide a number of benefits, not least a lower rate of tax on the income generated.

Capital allowances

Renewable energy equipment is generally eligible for capital allowances and the majority of the costs of installing such a system may qualify for integral features allowances (Annual investment Allowance (AIA) at 100% for the first £250,000 from 1 January 2013 – pro-rated for non 31 December year ends or 8% Writing Down Allowance) or plant and machinery capital allowances (AIA or 18% WDA for all renewable equipment other than Solar Panels which will fall into the special rate pool of 8% once the AIA has been utilised). However, to the extent that the renewable energy equipment will generate energy or heat for private use, these allowances should be restricted.

There is also an Enhanced Capital Allowances (ECAs) scheme which allows 100% of the direct costs of installation in the first year to be written off, however, this is dependent on the exact type of technology that is installed and can not be claimed when electricity or heat is generated where tariff payments under either Feed in Tariffs (FiTs) or Renewable Heat Incentives (RHI) are made. This is not in addition to the AIA above.

Capital allowances are generally only available if the installation is part of a trade – an installation for private domestic purposes will not qualify for capital allowances. However, if a trade involving the generation of electricity is created and the power generated is sold to third parties, back to the grid or used within an existing trade then capital allowances will generally be available.

VAT

Provided the eventual supply produced by the installation is of a taxable nature from a VAT point of view, the VAT on the proportion of the costs relating to the intended business use of the project can be reclaimed. However, VAT will have to be charged on the income received at the rate appropriate to the supply - standard rate (currently 20%) on supplies for non-domestic use and wholesale and reduced rate (currently 5%) for domestic use. If the energy or heat generated is used within let properties, the energy or heat must be invoiced separately from the rent and be metered to qualify as a taxable supply. Providing energy or heat to tenants along with the property and not invoicing it in this way will mean that the supply is exempt and the VAT on the installation will not be reclaimable in full.

The income receivable under the Feed in Tariff (FIT) Scheme is split into two components:

- The Generation Tariff which is paid for the amount of electricity generated. This income is outside the scope for VAT.
- The Export Tariff which is paid for any excess electricity generated and sold back to the grid. This income is standard rated for VAT.

Although the income and expenses for this project can be run through an existing business, (to avoid the need for a separate VAT registration and other onerous administration), the profits from the energy or heat generation trade should strictly be calculated separately to that of the existing business. This is especially important where there is a need to be able to demonstrate that a farm is being run with a view to a profit without the need for the profits from an energy trade, for tax purposes.

Capital taxes

Capital taxes (Capital Gains Tax and Inheritance Tax) should also be considered at the planning stage of the project. Correctly setting up the business could mean the difference between paying Capital Gains Tax at 10%, by obtaining Entrepreneurs' Relief on the disposal of the installation and any property it is connected with, and 28%.

Another point worthy of consideration prior to embarking on such a project is to consider how the installation, and any land or buildings it sits upon/within, would be chargeable to Inheritance Tax. This may be especially important if you are considering letting space for someone else to use to put solar panels or wind turbines on. Consider a field that is currently used to graze livestock. If this field is taken out of production and another business pays the landowner a rent to put solar panels or wind turbines on the land, the land has become investment property and is no longer agricultural property. This could have significant consequences on death as Agricultural Property Relief (APR) from Inheritance Tax is only available on agricultural property. There is another relief, Business Property Relief (BPR) that could be available if the overall business is structured correctly.

About the author

Louise Hosking from Ellacotts LLP, a Banbury based firm providing specialist advice to the agricultural and land owning community. Ellacotts LLP are also members of the UK200Agricultural Group. For further information contact John Thame, Agricultural partner on 01295 250401 or e-mail Louise LHosking@ellacotts.co.uk or John jthame@ellacotts.co.uk

---

Legal - Paul Rice, Wright Hassall LLP - Solicitors

The death knell sounds for overriding interests…

The first major land reform since 1925 was instigated in 2002 by the passing of the Land Registration Act. As part of the reform, the Act gave third parties with an overriding interest in land they do not own ten years to register that interest. This deadline ends at midnight on 12 October 2013. The vast majority of overriding interests not registered with the Land Registry by this date will be lost for good. This is part of a drive by the Registry to ensure that the register of title to all land (and the various interests in it) is as up to date and as comprehensive as possible. The Registry's objective is to simplify the process of buying and selling land by minimising the number of searches that prospective purchasers need to carry out and by eliminating any future possibility that a, hitherto, undisclosed interest (an 'overriding interest') in the property emerges from the woodwork.

Overriding interests are difficult to discover on an inspection of the land and most of them are, in fact, rather esoteric, historic relics that should have little bearing on modern property ownership. There are two overriding interests that are of particular interest to landowners: manorial rights, in particular those relating to mines and mineral rights, and chancel repair liability. The latter provoked considerable concern when a landmark case, Wallbank v Aston Cantlow, highlighted the considerable sums of money that could be at stake if a landowner found themselves at the wrong end of an overriding interest.

The background to this case starts hundreds of years ago. Rectors of parish churches have traditionally been responsible for the repair of the chancel (the area housing the choir stalls and altar) with parish members bearing responsibility for the remainder of the building. In mediaeval times many parish churches came into the possession of monasteries along with the liability for the repair of the chancel. After the dissolution of the monasteries in 1536, much of the monastic land sold off included the glebe land of their parish churches which carried the chancel repair liability, an anachronism which remains today. To make matters worse for the modern landowner, the liability attaches to the land as a whole so that when land is sold off into smaller plots, the owner of each plot carries an equal liability. This means that only one owner has to be found to fund the repairs, leaving him to extract payment from the other liable landowners.

In Wallbank v Aston Cantelow, the Wallbanks (who lived in Wales) had inherited a house in Aston Cantlow, Warwickshire, and were presented with a large bill for the repair of the church chancel. After protracted litigation, the Court of Appeal recommended scrapping the 'archaic and capricious' law. Unfortunately for the Wallbanks, the House of Lords disagreed and they lost the case. However, the Lords did recommend that the law was changed. This case has caused a good deal of concern among landowners and developers looking to purchase potential development plots as there is evidence that some Parish Councils are researching whether or not they have an overriding interest in the form of chancel repair in order to register it before the October deadline.

It should be acknowledged that Parish Councils, as charitable bodies, are legally obliged to protect the assets of the charity and thus must enforce such a repair liability if it exists. However, by the same token, few Parish Councils will relish the prospect of alienating their parishioners by demanding large sums for chancel repair. Many will be relieved by the outcome of a case in Broadway, Worcestershire in July 2012, when the PCC of St Eadburgha registered the Chancel repair liability against 30 residents. The Heritage Lottery Fund which took over funding for repairs to listed places of worship on 1 April 2013, agreed to step in *"…we……will ensure we do not encourage the PCC to pursue Chancel Repair Liability where it is evidently unreasonable for them to do so".* The Charity Commission also agreed that it was not necessary for the PCC to pursue the residents for the costs of repair.

The good news is that if you acquire a property for its full value on or after 13 October 2013 and chancel repair liability is not registered on its title that is an end of the matter. The bad news, for those owning property on 13 October 2013, is that the PCC can still register chancel repair liability (for a fee) even after the deadline has passed until the affected property is next sold on the open market whereby the new owner of the land will be free of the liability. However, the recent experience by the residents of Broadway and the assurances given by the Heritage Lottery Fund should give landowners a little more comfort.

Existing owners concerned about a chancel repair liability risk to their property should check with their lawyer (if they have not already done so) and consider obtaining insurance against any potential liability now. However, once the church's rights have been registered, or an application has been made for registration, it is unlikely that the risk will be capable of being insured on the basis of the relatively cheap standard polices currently available in the market.

About the author

Paul Rice is Agricultural Partner and Head of Farming and Rural Business at Wright Hassall LLP - Solicitors, and a member of UK200Agricultural Group paul.rice@wrighthassall.co.uk 01926 886688.

About UK200Agricultural Group

UK200Agricultural Group, a national grouping of independent chartered accountants and lawyers who understands the challenges facing farming and rural businesses, widely acknowledged as an authority within the UK rural economy and International Markets. Members help with strategic business planning, accounting, profitable uses of land, investment and diversification, inheritance, complex tax planning and legal issues. Farmers, landowners and rural business can expect trustworthy business support in this rapidly changing market, including expert help in sourcing grant aid funding for new enterprises jimy@uk200group.co.uk www.uk200roup.co.uk