

Contract Farming – getting it right

HM Revenue & Customs and Excise is increasingly reviewing arrangements which are presented as contract farming agreements but which may not be genuine. The landowner may be seeking a “rent” together with tax advantages and other benefits of being a farmer without taking risk. In other cases the relationship between farmer and contractor and the agreement may not have been considered or adhered to. Outsourcing is a common occurrence in many industries but in no other does it generate retention of the tax advantages of maintaining a trading status.

The following are key points which must be considered for any agreement to withstand scrutiny:-

- Farmer must be capable of being seen to be actively in business, for example the business has a bank account, is VAT registered, has a proper recordkeeping system, prepares full annual accounts showing sales and purchases, completes form SP5 and collects the Single Payment.
- Arable farming is a seasonal business, the cashflows attached to the contract farming arrangements must correlate with those of a working farmer – capital must be employed and be at risk to the farmer, cashflow cannot be positive before crops are harvested unless there is a legitimate commercial argument for this.
- Invoicing from contractor to farmer must be regular, at least quarterly, and invoices must be paid on the normal commercial terms operated by the contractors.
- Inputs should ideally be invoiced by the merchant direct to the farmer.
- The contractor carries out operations of husbandry as agent for the landowner. The farmer must make all key decisions about cropping and strategy, obviously the contractor can advise and be involved in this process. The farmer must be involved in the day to day management of the operation and must be able to evidence this by means of minutes of meetings, diaries etc.
- All regulatory documents must be completed by the farmer and retained by the farmer on his premises.
- The farmer cannot have a guaranteed return, he must take risk – the contractors bonus or penalty must be defensible. No risk equals rent.
- Any written agreement must be adhered to and the farmers and contractors accounts must reflect this.
- The harvested crop must be sold after due commercial consideration. The crop can be sold standing or “off the combine”, particularly if storage facilities are in short supply, but evidence should be available of the reasons behind any decision.
- Any arrangements with third parties such as agronomists, consultants etc. should be direct with the farmer.
- Does the arrangement look real, does it make commercial sense? If the answer is no then HMRC is likely to come to the same conclusion.