IFS: Inheritance tax and farms

Synopsis: The Institute for Fiscal Studies (IFS) has published an article commenting on the Autumn Budget 2024 changes to inheritance tax (IHT) reliefs for agricultural and business assets.

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The Autumn 2024 Budget introduced significant changes to IHT, particularly affecting agricultural and business properties. These reforms, aimed at raising additional revenue while addressing existing disparities in tax treatment, have elicited varied responses. Below is a detailed summary of the key outcomes and implications of these changes.

Scope and revenue impact: The reforms, effective from April 2026, include curtailments to IHT relief for agricultural and business assets, adjustments in pension inheritance rules, and freezes on tax-free allowances until 2029/30. Collectively, these measures are expected to generate £2.3 billion annually by 2029/30, with £520 million stemming from reductions in agricultural and business reliefs.

Specific adjustments: Estates will now receive 100% IHT relief on the first £1 million of combined agricultural and business assets but only 50% relief on values exceeding £1 million.

Shares listed on the markets of a stock exchange that is not a recognised stock exchange, such as AIM shares, will be capped at 50% relief in all scenarios.

Despite these changes, the nil-rate band (£325,000) and the residence nil-rate band (£175,000) remain, enabling substantial tax-free inheritance opportunities.

Illustrative example: A married couple/civil partners with a £3 million farm (including a £350,000 home) could transfer the entire estate tax-free to descendants, provided both use their £1 million allowances and inherited nil-rate bands (i.e. those assets don't pass to the surviving spouse/civil partner on first death, as any unused £1 million allowance will not be transferable between them).

Impact on farms and farmers

Number of affected farms: The Government estimates around 29% (approximately 500 out of 1,800 estates annually claiming agricultural relief) could face higher IHT liabilities. However, this figure may decline due to changes in behaviour, such as strategic splitting of asset transfers between spouses/civil partners or increased gifting of assets during the owners' lifetimes.

Contrasting perspectives: The National Farmers' Union suggests that up to two-thirds of farms, valued over £1 million, might be impacted.

Discrepancies arise from differing data sources and definitions of "farms," with some estates including low-output properties or partial farm ownerships.

Potential sales: Farms with insufficient income to meet IHT liabilities could face partial or complete sales. However, provisions such as spreading tax payments over ten years interest-free could alleviate immediate pressures. Moreover, the reforms may temper inflated farmland prices, facilitating market entry for new farmers and promoting efficient land use.

Policy implications and critiques

Equity and efficiency: The revised tax framework still favours agricultural and business assets over other forms of wealth, maintaining significant tax advantages.

Critics argue for a uniform application of IHT across asset classes unless compelling reasons, like environmental or food security concerns, justify preferential treatment.

Transition challenges: Current farm owners passing away within seven years of the policy's implementation (post-2026) lack sufficient time to mitigate tax burdens through lifetime gifts. Gradual transition policies, such as exempting early gifts, could address this disparity.

Allowing the unused portions of the £1 million allowance to be transferred to surviving spouses or civil partners (as with other allowances) could reduce complexities and enhance fairness.

Economic and social impacts: Potential reallocation of farmland for higher-value uses, such as development, could stimulate economic efficiency but might necessitate targeted government support to safeguard food security and biodiversity goals.

Conclusions

The 2024 Budget reforms mark a step towards reducing inequities in IHT treatment, aligning agricultural and business properties more closely with other asset classes. While significant tax planning opportunities remain, the measures target high-value estates, ensuring a progressive tax burden. However, the policy's success hinges on effective transition arrangements and the Government's commitment to addressing broader land-use and environmental objectives through direct, transparent support mechanisms.

Overall, these changes strike a balance between raising much-needed revenue and maintaining fairness within the IHT system. By refining transitional provisions and introducing portability for allowances, the Government could further enhance the policy's equity and acceptance among stakeholders.

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