This document relates to the Agricultural Holdings (Amendment) (Scotland) Bill (SP Bill 3) as introduced in the Scottish Parliament on 31 October 2011

AGRICULTURAL HOLDINGS (AMENDMENT) (SCOTLAND) BILL

POLICY MEMORANDUM

INTRODUCTION

1. This document relates to the Agricultural Holdings (Amendment) (Scotland) Bill introduced in the Scottish Parliament on 31 October 2011. It has been prepared by the Scottish Government to satisfy Rule 9.3.3(c) of the Parliament’s Standing Orders. The contents are entirely the responsibility of the Scottish Government and have not been endorsed by the Parliament. Explanatory Notes and other accompanying documents are published separately as SP Bill 3–EN.

POLICY OBJECTIVES OF THE BILL

2. The policy objective of this Bill is to amend legislative provisions relating to succession and rent review in order to create a better environment for the letting of farmland to the tenant farming sector of the agricultural industry and to encourage new entrants into tenant farming.

3. There are two principal statutes which regulate agricultural tenancies in Scotland, namely, the Agricultural Holdings (Scotland) Act 1991 and the Agricultural Holdings (Scotland) Act 2003 (“the 1991 Act” and “the 2003 Act” respectively). The Public Services Reform (Agricultural Holdings) Scotland Order 2011 (“the Order”) which came into force on 22 March 2011, made a number of amendments to those Acts.

4. Those amendments were designed to give effect to a set of recommendations made by the Tenant Farming Forum (“TFF”) which the Scottish Ministers agreed to implement by revising the legislation governing agricultural holdings. It had originally been the intention to include provisions in the Order prohibiting the inclusion of upward only or landlord only initiated rent reviews under the 2003 Act and extending the definition of “near relative” in Schedule 2 to the 1991 Act to include a grandchild of a deceased tenant of an agricultural holding. However, those provisions were omitted from the Order on the basis that they fell outwith the vires conferred by section 17 of the Public Services Reform (Scotland) Act 2010.

5. In response to the consultation on the Order, some industry stakeholders expressed disappointment that these two measures which had formed part of a “package” of reforms could not be included in the Order. Disappointment was also expressed that the opportunity had not been taken to correct an anomaly arising from the English High Court case of Mason v
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Boscawen\(^1\) regarding the incorporation of VAT in agricultural rents under the Agricultural Holdings Act 1986, in so far as it casts doubt over the equivalent provision in Scottish legislation. An amendment was included in the Finance Act 2009 to rectify the anomaly arising from that case in England.

6. The Bill implements the two provisions which were omitted from the Order and makes an amendment similar to that made in England regarding the VAT issue.

7. The Bill makes provision as follows—

- it contains an amendment to Schedule 2, Part III of the 1991 Act to extend the definition of “near relative” (section 1);
- it amends section 9 of the 2003 Act to nullify lease terms in Limited Duration Tenancies which provide for upward only and landlord only initiated rent reviews (section 2); and
- it contains an amendment to section 13 of the 1991 Act that provides that changes in rent resulting from the exercise or revocation of the option to tax by a landlord, or a change in the rate of VAT where such an option has effect, do not qualify as a “variation of rent” such as would prevent parties from seeking a determination from the Scottish Land Court on the rent for a period of three years.

Section 1 - Succession by near relatives

8. The first of these measures relates to succession. Where a tenant farmer dies and the tenancy passes by succession, a landlord is entitled to serve a notice to quit on the successor tenant farmer. A landlord can serve an incontestable notice to quit on any successor as tenant if they are not a “near relative” of the deceased tenant farmer. Where the successor tenant is a “near relative” of the deceased tenant farmer, that person is entitled to give the landlord a counter notice requiring that the Scottish Land Court consents to operation of the notice to quit. In other words, “near relatives” enjoy a degree of protection that other successors do not.

9. The definition of “near relative” currently includes a surviving spouse, surviving civil partner and a natural or adopted child of the deceased tenant farmer. Grandchildren are not included and the practical effect is that where there are three generations of a tenant farming family and the second generation dies before the first (i.e. where a parent who would otherwise succeed dies before the grandparent tenant), a grandchild may be prevented from succeeding to the tenancy if the landlord serves a notice to quit as he or she will be unable to contest that notice by way of serving a counter notice. The Scottish Government considers that the class of persons entitled to this degree of statutory protection should be widened to include a grandchild. It is considered that making it easier for grandchildren to inherit farm tenancies will help new and younger entrants get a start in tenant farming, which will be beneficial to the wider agricultural industry.

\(^1\)(2009 1 W.L.R 2139)
10. It is therefore proposed to extend the definition of “near relative” to include “grandchild” within the list of relatives of a deceased tenant farmer who are entitled to give a landlord counter notice requiring that the Scottish Land Court consents to the operation of the notice to quit.

Section 2 - Prohibition of upward only rent reviews etc.

11. The second measure relates to rent reviews. The Scottish Government considers that there are public policy grounds for nullifying the inclusion of rent review clauses in Limited Duration Tenancies (LDTs) that allow for upward only or landlord only initiated reviews. Where they do appear, the policy is that any such terms should be struck out.

12. In an LDT under the 2003 Act, parties enjoy freedom to contract - they are not restricted in any way when agreeing the contractual provisions which will appear in the lease for a review of rent. It is therefore possible at present for parties to agree to upward only rent reviews, or provision whereby the landlord only, not the tenant farmer, can instigate a review of rent.

13. There is evidence that some LDTs contain review of rent clauses that allow for upward only or landlord only initiated reviews. The nature of these provisions is such that they could result in tenants being burdened by uneconomically high rents, thus undermining their security of tenure.

14. As such, it is considered that there are strong public policy grounds in favour of them being nullified. Section 9 of the 2003 Act provides an implied lease term covering rent review arrangements for LDTs where the lease contains no such provision. It is proposed to insert a provision which would effectively nullify upward only and landlord only initiated review of rent clauses in this section. Where they do appear, the policy is that any such terms should be struck out and the provisions of section 9 would apply.

15. This provision is to apply only to review of rent provisions in LDTs entered into after the law is changed so as not to interfere with the contractual position of parties who have already entered into leases containing such provisions. Agreements between landlords and their tenant farmers that are already in place will continue unaffected by this provision until their expiry.

Section 3 - Effect of VAT changes on determination of rent

16. The Bill also includes a further provision relating to VAT and rent reviews, which has also been agreed by the TFF and mirrors a recent amendment to English agricultural holdings legislation. The judgement in the Mason v Boscawen case has cast doubt over the provisions in the 1991 Act regarding the three year rent review cycle. The case concerned the definition of rent and the Court held that VAT charged on rent is part of the rent for the purposes of the Agricultural Holdings Act 1986.

17. Reaching this conclusion gave rise to an unintended consequence; it followed that a change in the rate of VAT chargeable constituted a change of rent which prevents the parties to a lease under the Agricultural Holdings Act 1986 from referring the rent to arbitration for a period of three years from the date of the rate change. The exercise or revocation of the option to tax by a landlord would have the same effect.
18. In view of the unintended consequences of that judgment, the opportunity was taken to include an “emergency” amendment to the 1986 Act in the Finance Act 2009, Section 79 of which provides that changes in the VAT chargeable on rents is to be disregarded for the purposes of the rent arbitration provisions of the 1986 Act.

19. The equivalent Scottish legislation, Section 13 of the 1991 Act, is cast in almost identical terms to the English legislation that was the subject of the case and there is concern that if the judgement were to be followed by the Scottish Courts, the same problem would arise under the 1991 Act.

20. Although there has been no case law in Scotland on this point as yet, it is considered that the judgement in Mason v Boscawen has the potential to cause confusion in Scotland, although only in the limited number of cases where the option to tax has been taken and as such it is in the interest of the Scottish agricultural tenancy industry to clarify the position in Scotland.

21. Section 13 of the 1991 Act sets out circumstances under which the landlord or tenant farmer of an agricultural holding may seek to have the rent payable in respect of the holding determined by the Scottish Land Court. Subsection (8) states that a reference to the Scottish Land Court may not be demanded within three years of the commencement of the tenancy, the last variation of the rent or the last time a previous direction was given that the rent should remain unchanged. Subsection (9) sets out certain circumstances where subsection (8) may be disregarded and this does not currently include changes in rent resulting from the exercise of an option to tax, the revocation of such an option or a change in the rate of tax.

22. Therefore, a provision has been included in the Bill that would amend the law to clarify that any variation of rent in consequence of the addition of VAT (or election to waive exemption) or, where VAT applies, any variation in the rate, would not prevent a reference to the Scottish Land Court to determine the rent.

23. It is considered that implementing the outstanding two recommendations made by the TFF will help to facilitate new entrants to the tenant farming sector by making it easier for grandchildren to inherit agricultural tenancies and increase confidence in the sector by prohibiting upward only or landlord only rent reviews. Providing clarity on the effect of changes in rent arising from changes in VAT, or by the exercise by a landlord of an option to tax, will also help to reduce uncertainty.

ALTERNATIVE APPROACHES

24. Since “near relative” is defined in statute there are no alternatives other than to amend the primary legislation through a Bill. In relation to the proposal to prohibit upward only or landlord only initiated reviews of rent, it is possible to encourage landlords and their tenant farmers not to include such provisions within leases but this provides no guarantee that such arrangements will not be entered into. Therefore, primary legislation is considered to be the only way of achieving these aims. Similarly, in the absence of any definitive case law on the VAT issue, primary legislation provides the only means of clarifying the effect of changes in VAT on rent.
CONSULTATION

25. The package of measures agreed by the TFF was submitted to Scottish Ministers after extensive consultation with the constituent members of the TFF. In relation to the proposals contained within the Bill, the Scottish Government conducted a consultation exercise on a draft Bill between 22 March 2011 and 30 June 2011\(^2\). The analysis of the consultation response\(^3\) indicated that the measures in the Bill command broad support from a number of different stakeholders. Of the 16 responses received, 4 were from individuals and 12 were from stakeholder organisations. The consultation identified a few areas that required further consideration. In particular, the transitional arrangements for section 1 of the Bill relating to the changes in the definition of a “near relative” required further consideration.

26. The Scottish Government has adjusted the draft Bill to reflect the majority of these comments.

EFFECTS ON EQUAL OPPORTUNITIES, HUMAN RIGHTS, ISLAND COMMUNITIES, LOCAL GOVERNMENT, SUSTAINABLE DEVELOPMENT ETC.

27. The Bill deals with the terms of agricultural leases between private individuals and their landlords. The Bill is intended to create a better environment to encourage the letting of farm land to tenant farmers and encourage new entrants into tenant farming, supporting activity and sustainable development within rural communities. The only impact the Bill has on local government is, where local authorities are landlords of agricultural holdings, they will be affected by the proposed changes to the legislation prohibiting upward only or landlord only initiated rent reviews, in the same way that any other landlord will be affected. Both male and female grandchildren will be provided equal opportunity by having the potential to succeed a tenancy. It is considered that the Bill has no effect on human rights and island communities the majority of which have a combination of crofting, tenant farming and farming on them.

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\(^2\) [http://www.scotland.gov.uk/Publications/2011/03/18095404/0](http://www.scotland.gov.uk/Publications/2011/03/18095404/0)

\(^3\) All the consultation responses, where permission was given to publish them, can be found on the Scottish Government’s website at [http://www.scotland.gov.uk/Publications/2011/08/08143730/0](http://www.scotland.gov.uk/Publications/2011/08/08143730/0).
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