

**Final
Business and Regulatory Impact Assessment**

**The Agricultural Holdings
(Scotland) Act 1991 (Variation
of Schedule 5) Order 2018**

October 2018

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Title of Proposal

The Agricultural Holdings (Scotland) Act 1991 (Variation of Schedule 5) Order 2018

Purpose and intended effect

- **Background**

When an agricultural tenancy ends, the tenant may be entitled to waygo compensation - compensation for improvements they carried out as tenant to the agricultural holding. The landlord and tenant should come to an agreement about what compensation is due.

The general principles behind waygo compensation claims are:

- (a) to allow both a tenant farmer and their landlord a fair measure of compensation for improvements made to the farm land or the holdings fixed equipment or for that matter their deterioration as the case may be; and
- (b) to provide for costs incurred by the tenant farmer associated with quitting the farm land, and for re-organisation where termination of the tenancy arrangement is for non-agricultural purposes.¹

Schedule 5 of the Agricultural Holdings (Scotland) Act 1991 (the 1991 Act) sets out a list of improvements to agricultural holdings which may be eligible for compensation when the tenant leaves the holding.

The list was originally created for the Agriculture (Scotland) Act 1948 (the 1948 Act), and has not been updated since, meaning that some items which are readily accepted now as being legitimate improvements are not listed. The Agricultural Holdings Legislation Review Group (AHLRG) in their Final Report published in 2015, called for the list to be updated, to reflect modern farming practice and for the avoidance of doubt and confusion.

Consequently, the Land Reform (Scotland) Act 2016 (the 2016 Act) required the Tenant Farming Commissioner to make recommendations to modernise the list. This was part of the overall modernisation of agricultural holdings delivered by the Act. The Tenant Farming Commissioner delivered his recommendations to Scottish Ministers in December 2017. The Scottish Government is now seeking to implement those recommendations through this Order.

- **Objective**

This Order falls under one of the objectives identified for the 2016 Act - to take forward much needed reforms to Agricultural Holdings legislation, identified by the AHLRG, to improve relationships, redress imbalances, and to provide tools to help the industry begin to move forward.

¹ SM Notley, *Scottish Agricultural Law Handbook*, p.197

The objective of this legislative change is to update list of improvements for which a tenant may be entitled to compensation. In doing so, the Scottish Government seeks to ensure compliance with modern farming practice and to provide legal clarity for existing practice, reducing the need for agreements to be made outside the legislative framework.

- **Rationale for Government intervention**

The underlying rationale of current provisions for waygo contained within the 1991 Act is to encourage tenant farmers to invest in the agricultural holding and keep the holding in good condition, knowing that they will be adequately compensated. Updating of schedule 5 to reflect modern farming practice ensures that this remains the case.

The AHLRG Final Report considered recent moves in the sector away from the traditional partnership model between landlord and tenant. Traditionally the partnership was one where the former contributes the fixed capital and the latter provides the working capital, management and labour. The development of capital intensity of farming over many decades has increased the proportion of working capital in the overall capital employed (excluding land value), and in addition a trend among landlords to limit their investment in fixed equipment, often as a response to low rents.

As a result many 1991 Act tenants now provide a significant fixed capital element. If a tenant carries out certain improvements during the course of his tenancy then they should be able to do so in the knowledge that the landlord must compensate them for such improvements on termination of the tenancy (compensation at waygo).

Aligned to this rationale is the Scottish Government's vision for a Scottish tenant farming sector that is dynamic, getting the best from the land and the people farming it, and provides opportunities for new entrants, forming part of a sustainable future for Scottish farming. 21% of agricultural land in Scotland is tenanted (this does not include crofts), and tenant farmers and landlords play an important part in the wider rural community. It is important that the legislative framework governing these arrangements reflects modern farming practice where possible, to ensure that these businesses can continue to contribute to the rural economy.

The Scottish Government's overarching purpose is "to focus government and public services on creating a more successful country, with opportunities for all of Scotland to flourish, through increasing sustainable economic growth".

This Order is part of the aims of the 2016 Act, which identified as contributing to the following National Outcomes :

- We have tackled the significant inequalities in Scottish society.
- We have strong, resilient and supportive communities where people take responsibility for their own actions and how they affect others.

- We value and enjoy our built and natural environment and protect it and enhance it for future generations.

Consultation

The updating of schedule 5 was an issue raised during the extensive consultation conducted by the AHLRG, which informed the policy provisions for the Agricultural Holdings provisions in the 2016 Act. The AHLRG consultation consisted of:

- first stage of work during Spring 2014 where the AHLRG members met with the key stakeholder organisations (National Farmers Union of Scotland, Scottish Tenant Farming Association, Scottish Land and Estates, Scottish Agricultural Auctioneers and Valuers Association and Royal Institute of Chartered Surveyors) and conducted over 50 meetings and private sessions with tenant farmers, their landlords and professional intermediaries in Islay, Oban, St Boswells, Dumfries, Turriff, Perth, Inverness, Stranraer, Ayr and Isle of Bute;

- in June 2014, launch of the AHLRG's Interim Report at the Royal Highland Show, where the AHLRG held a further 16 private meetings with tenant farmers, their landlords and land agents;

- second stage of work, during Summer/ Autumn 2014, where the AHLRG sense tested their emerging proposals (which includes the update of schedule 5) in 12 meetings held with the main stakeholder organisations, and again, well attended public meetings in Kelso, Inverurie, Bridge of Allan and Dumfries.

In addition to the above meetings, the AHLRG received 100 written submissions. 27 of these came from the main stakeholder organisations, and 73 came from individual tenant farmers, landowners and land agents.

The detailed notes of the AHLRG confirm that the main industry bodies, the Scottish Tenant Farming Association, Scottish Land & Estates and National Farmers Union Scotland, all suggest that the list of improvements in schedule 5 is revised to reflect modern agricultural practice.

They also note that this seems uncontroversial but any revision would need to be done with the benefit of expert opinion as to current agricultural practice and possible future developments.

In order to ensure that this is the case, in drafting his recommendations in 2017/18 the Tenant Farming Commissioner once again consulted with:

- The Scottish Tenant Farmers Association
- Scottish Land & Estates
- National Farmers Union Scotland
- Royal Institute of Chartered Surveyors

- Scottish Agricultural Auctioneers and Valuers Association
- The Central Association of Agricultural Valuers
- Agricultural Law Association

In addition, in drafting the Order, Scottish Government has discussed the draft with all of these parties.

In recognition of the extensive consultation work already undertaken in 2014, the further consultation work undertaken in 2017 and the widespread support for this industry-led amendment (there is no evidence of any objection to this proposal on any side), and in line with the approach taken for the BRIA for the 2016 Act, further interviews with firms have not been carried out as part of this BRIA. Scottish Government will continue to keep schedule 5 under review as farming practice continues to evolve, and will consider further updates to the schedule in future years if the sector advise that this is required.

Options

Sectors and groups affected

Tenant farming is a private arrangement between landlords and their tenant farmers not covered by the provisions of crofting law. Therefore, those primarily affected by this Order are landlords and tenant farmers of agricultural holdings.

Of the 52,000 farms in Scotland, there are over 6,700 with agricultural holding tenancy agreements. Figures obtained from the Central Association of Agricultural Valuers² suggest that in Scotland in 2017 49 tenancies ended, and therefore waygo compensation may be due. This compares to 51 in 2016, 50 in 2015 and 25 in 2014. This change is not retrospective, so is unlikely to affect waygo payments for several years.

Other secondary groups will also be affected, such as land agents, agricultural valuers and surveyors, where the landlord or tenant chooses to engage their services as part of the waygo process.

Option 1 – do nothing

If the schedule is not updated, waygo compensation will continue as it is. In some cases this will not be problematic, as landlords and tenants come to separate agreements about compensation payable for improvements not covered by the schedule. A recent review by the Tenant Farming Commissioner of the conduct of agents of agricultural tenants and landlords found that 82% of tenant farmers and 88% of landlords would describe their relationship with the other as either very good or good. Only 6% of tenants and 1% of landlords reported that the relationship was poor or very poor³. This indicates that, in general, amicable agreements should be

² The Central Association of Agricultural Valuers, *The Annual Agricultural Land Occupation Surveys for Great Britain 2017*, p.37

³ Scottish Land Commission, *A Review of the Conduct of Agents of Agricultural Landlords and Tenants*, April 2018, p.8

able to be reached. However, in some cases, particularly where the landlord-tenant relationship is difficult, then tenants will have no incentive to improve or modernise the holding if they do not anticipate being compensated for it, and thus maintain or improve productivity. This drives inequity across the sector, as compensation for some modern improvements remains outside the legislative provisions and therefore not uniform.

Benefits: - The current system allows for some way-go compensation and is understood by current parties, even if seen as unfair or not working properly.

Costs: - Under this option there would be no change to the costs to landlord or tenant. However, there would be a potential cost to the rural economy if, as noted above, tenants have no incentive to invest in the modernisation of holdings.

Option 2 – adopt the recommendations of the Tenant Farming Commissioner to update schedule 5

The Tenant Farming Commissioner has proposed a number of changes to schedule 5 which will modernise it in line with modern farming practice. Under this option all these recommendations would be adopted wherever possible, from the date that the Order comes into force.

Only one aspect of the Tenant Farming Commissioner's recommendations is not adopted - he recommends the addition of 'permissions, consents, contracts, authorisations and restrictions' to cover intangible benefits that have been obtained by the tenant and have a value to an incoming tenant. However, we do not have the legal power to include these items in the schedule.

Benefits: - Updating schedule 5 would bring it into line with modern farming practice and would provide legal clarity for existing practice. There would be uniformity across the sector, leading to greater certainty and therefore greater likelihood of investment in the holding, and therefore potentially an increase in the value of their property for the landlord.

Costs: - For landlords who are already happy to come to arrangements with their tenants on compensation for items not on the schedule but which add value to the holding, the change will have minimal cost as it will simply confirm existing practice. For other landlords, there could be a cost at waygo if their tenant makes an improvement which is added to the schedule but this should be offset by the increase in value of their asset as a result of the improvement. However, the Order is not retrospective and will only apply going forward – that means that costs should not be unexpected and can be planned for.

The compensation for an asset is calculated on the basis of the value to the incoming tenant. This is done by assessing the cost to install that asset at the point of waygo and adjusting for the remaining utilisable life of the asset.

For example, if a tenant erects a shed with a 35 year life span and leaves the tenancy after 25 years the shed is likely to have a remaining utilisable life of 10 years. If the cost to build an equivalent shed new at the point of waygo was

£100k then approximately £2,860 (£100k divided by 35 years) would be due for each year of remaining utilisable life, in this example £28,600. The actual cost of building the shed 25-years ago is not a factor in the calculations, only the value to an incoming tenant. Other factors are considered at waygo, such as appropriateness of the installation to the farm and, for assets such as wind turbines, any income streams.

Given the number of variables involved, which will depend on individual circumstances and actions, it is not possible to estimate an overall cost. However, the cost to the landlord should be balanced by the increase in value of their asset as a result of the improvement and this may also be reflected in the level of rent that can be charged to a new tenant.

There may be some costs associated with increased paperwork, but these are likely to be negligible as this will be adding items to the existing waygo process, rather than creating a new process of its own.

Scottish Firms Impact Test

Agricultural and landholding businesses were key contributors to the AHLRG report which informed this policy proposal and others in the 2016 Act. This measure was uncontroversial, with no evidence of any objection – it is logical that schedule 5 should be updated to reflect modern farming practice.

As each circumstance will be unique to that tenancy, it is not possible to estimate the future cost to parties. However, the Order aims to reduce uncertainty and therefore lead to a greater likelihood of investment in the holding.

Competition Assessment

Agricultural tenancies are private arrangements between landlords and tenants. This Order is concerned with eligibility for compensation at waygo, after an improvement has been made, so will not directly or indirectly limit the number or range of suppliers of that improvement, will not limit the ability or incentive of suppliers to compete vigorously and will not limit choices or information available to consumers.

Test run of business forms

No new forms will be required.

Legal Aid Impact Test

The Order should clarify matters around what is eligible for compensation at waygo. The provisions of the 2016 Act were assessed by the legal aid team as having minimal impact on the legal aid fund. This Order does not change that.

Enforcement, sanctions and monitoring

The Order is concerned with private leasing arrangements between agricultural landlords and tenants. These arrangements are enforceable contractually between the parties. The Tenant Farming Commissioner can provide advice on the resolution

of any issues and parties have recourse to the Scottish Land Court in event of dispute.

Implementation and delivery plan

The Order will be laid in Parliament and come into force by the end of 2018.

Post-implementation review

It is anticipated that the Scottish Government will ask the Tenant Farming Commissioner to reconsider schedule 5 on a regular basis, potentially every 5-10 years, to ensure it is still in line with modern farming practice.

Summary and recommendation

Option 2 is recommended. This is an industry-led change, which will ensure that schedule 5 reflects modern farming practice. This will encourage tenants to invest in the holding and keep the holding in good condition, knowing that they will be adequately compensated for improvements.

Declaration and publication

The Cabinet Secretary or Minister responsible for the policy (or the Chief Executive of non departmental public bodies and other agencies if appropriate) is required to sign off all BRIAs prior to publication. Use appropriate text from choices below:

- Sign-off for Partial BRIAs:

I have read the Business and Regulatory Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options. I am satisfied that business impact has been assessed with the support of businesses in Scotland.

- Sign-off for Final BRIAs:

I have read the Business and Regulatory Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs. I am satisfied that business impact has been assessed with the support of businesses in Scotland.

Signed:



Date: Thursday 4th October 2018

**Fergus Ewing
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Any enquiries regarding this publication should be sent to us at
The Scottish Government
St Andrew's House
Edinburgh
EH1 3DG

ISBN: 978-1-78781-303-8 (web only)

Published by The Scottish Government, October 2018

Produced for The Scottish Government by APS Group Scotland, 21 Tennant Street, Edinburgh EH6 5NA
PPDAS483266 (10/18)

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