

IHT business property relief: the going gets tougher

A recent statement by HM Revenue & Customs Capital Taxes rather ominously announced that they are reviewing their approach in relation to claims for business property relief on furnished holiday lets. Although the announcement does not say, in terms, that HMRC will no longer allow claims for relief in respect of furnished holiday lets, it is almost certainly the case that in future the Capital Taxes Office will be very reluctant indeed to allow it in such cases.

This is the latest in a long downward trend with business property relief. Over the last ten years, the Capital Taxes Office has made efforts to draw in the boundaries of the relief and there has been a spate of cases before the Special Commissioners which have highlighted the more stringent approach which is currently being taken in relation to this relief.

Some 19 years ago, a case was reported in *Taxation* which concerned a four storey building in the medical area of London which was let out on licences to medical practitioners. The owner of the building used the top floor as a private residence but most of the rest of the building was used by medical practitioners. A receptionist was provided together with various other facilities, but what the owner received was rent under the licences. As a result, the Capital Taxes Office considered that, although there was undoubtedly a business carried on at the premises by the owner, that business was an investment business for the receipt of rent. Investment businesses are not eligible for business property relief. The case went to the Special Commissioners and was not reported at the time, but they upheld the taxpayer's case. The taxpayer was not simply holding an investment but was conducting a business which was eligible for business property relief.

More recent similar cases which have been before from the Special Commissioners mostly concerned caravan sites. Once again, the Revenue's approach to such cases is to regard the sites as investment activities by the owner, despite the substantial daily work which is normally required to keep the site running actively. In some of the cases, the Commissioners have endeavoured to identify on the one hand the work carried out by the site owner which can be categorised as a service provided to the caravaners, as well as any other trading activity, and on the other hand the activities of the owner which relate simply to maintenance of the land as a holding of property. If the services and trading element is more than 50 per cent of the total activity, or the total income received, then business property relief is allowed, but if it is less than 50 per cent it may be denied.

This is an extremely harsh approach and it may seem surprising that the Revenue has been successful with it in some cases. Caravan sites would not normally be considered as investment activities and most of them are probably returned for income tax purposes as trading activities. Some staff will be required to run the site; there will often be a shop, there may be a club for evening entertainment, there will be sales of gas cylinders and sometimes sales of caravans. All in all, the site owner will be running it as a full-time daily

occupation with the assistance of staff and it is hard to imagine anything less like an investment. Investment has the connotation of passive activity, such as holding quoted shares in order to collect the dividends from them and one day to sell them at a profit. It is hard to imagine any other investment activity which constitutes the daily work of the owner.

Fortunately one caravan case was decided in favour of the taxpayers, this being the *Stedman* case reported at 75 TC 735. This went as far as the Court of Appeal which held that although the income from the site may be described as rent, this does not prevent part of the return being attributable to the services provided by the site owner. In that case, the services were sufficient to allow the claim for business property relief.

No doubt the Revenue's successes in various other caravan site cases has brought about the change of view in relation to furnished holiday lets. The Revenue feels that it can argue that the main activity is simply the renting out of the property, and although services may be provided, they are likely to be relatively minor compared to the pure rental activity. One can now see how the trend has moved in the Revenue's favour since the 1990 case concerning the four storey tenanted building. This is partly the result of the Special Commissioners being increasingly receptive to the views of HM Revenue & Customs (in fact I have heard that one of the Special Commissioners has never ever found for the taxpayer in any case to date).

Anyone who wishes to challenge the Revenue's latest announcement on the topic is therefore likely to face an uphill struggle, even if the appeal is taken to the Special Commissioners (it cannot go to the General Commissioners because this is not permitted under the inheritance tax legislation). Of course, if the furnished holiday lets are part of a larger business, such as a farm business, then the taxpayer is on much better ground and relief should be available in such cases.

Where the holiday lets are not part of a larger business, we can advise on methods of strengthening the claim to business property relief.

The announcement concerning holiday lets is not the only recent development in relation to business property relief. A recent case before the High Court held that the relief is due where an asset of a business is given away, without any transfer of part of the business itself. In the case concerned, the asset was a field which had been used for the purposes of a farming activity. This case offers a number of tax planning opportunities, particularly as a method of transferring land or properties into a discretionary trust without any inheritance tax or capital gains tax being payable and without any danger of a clawback of business property relief should the donor not survive for seven years from the time of the gift. It remains to be seen whether the Revenue will amend the business property relief legislation to reverse this decision but, in the meantime, there is a small window of opportunity for the well advised.

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