Equine exemption

Julie Butler considers whether equestrian property qualifies for inheritance tax relief

ABOUT THE AUTHOR

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As part of inheritance tax (IHT) planning and compliance, the question has to be asked as to whether the equine property will qualify for Agricultural Property Relief (APR) and/or Business Property Relief (BPR)?

Stud farms

Stud farms have the advantage over other equestrian activities in that they do qualify for APR and are not just dependent on BPR for IHT. In order to qualify for BPR there must be evidence of a business, which can cause problems when trying to claim the IHT relief.

The Inspector's Manual at BIM55701 sets the overview as follows:

'Stud farming, which in these paragraphs is taken to mean the occupation of land for the purpose of breeding thoroughbred horses, is a very expensive and high-risk activity. In some cases it may be carried on by wealthy individuals essentially as an adjunct to their racing activities. Nevertheless, for tax purposes it is treated as farming and thus – by virtue of TA 1988 s 53(1) (ITA2007 s 9(1)) – as the carrying on of a trade regardless of its commercial viability.'

An important point here is that reference is made to the thoroughbred horse, but what of the sports horse? The principle should follow provided there is a genuine stud activity carried on with prospect of profit.

Horseracing, however, is not a taxable activity. Where, as is often the case, a stud farmer also races horses, considerable care is needed to ensure that the division between the two activities has been correctly made as one will be eligible for IHT relief and one will not.

Agricultural value

The claim for APR will of course be restricted to the agricultural value of the stud farm.

When reviewing APR claims, an understanding of the definition of agricultural value is vital. It is limited by *Inheritance Tax Act 1984* (*IHTA 1984*) s115(3): 'The value which would be the value of the property if the property was subject to a perpetual covenant prohibiting its use otherwise than as agricultural property'. Priority is given to APR under *IHTA 1984* s116(1) before BPR, ie when property qualifies for both reliefs, APR is given first.

District Valuers (DVs) have been known to argue for a discount of up to one-third (or more) from market value in determining the agricultural value of a farmhouse. DVs tend to apply the s115(3) definition by assuming that the property was subject to an agricultural tie; however, this is thought to be unduly restrictive, in that the statute refers to 'use' rather than to agricultural 'occupation'.

The important point that any tax planner would worry about (as indeed would their clients) is the fact that the market value of agricultural property might well exceed its agricultural value and there could, therefore, be a differential that would be chargeable to IHT over and above the APR claim. It is useful at this point to look at the scope of the claim for BPR as it may be that the relief could be claimed against the difference. In order to obtain BPR the property must be a business not just pure let equine property. Is there hope of development value?

Priority of APR

Under *IHTA 1984* s116(1) APR takes precedence over BPR. In the situation where both of these are available in respect of a single asset, APR is given first and BPR is given second. This can often happen in the case of a stud farm left in the estate of a deceased person. If the relevant conditions are fulfilled, APR will remove from charge the value of the land, valued for agricultural purposes, and the balance could form a claim for BPR provided the relevant conditions are satisfied. It is therefore essential to see how and when BPR can be claimed against part of the stud that does not qualify for APR. The essential ingredient for a claim for BPR is that there must be a business – simple but true!

Horse livery

Is the horse livery activity a business or is it a business excluded from relief as consisting mainly of making or holding investments s105(3) *IHTA 1984*?

There has been a recent case, *McCall and Anor* (*Personal Representatives of McClean Deceased*) v *R & C Commrs* (*2008*) *SpC 678 7 April 2008* that highlights the importance of providing additional services to just that of letting out the land and buildings. The Special Commissioners did not accept that the grass letting provided in this case was 'akin to hotel accommodation for cattle'.

Trading status will usually apply to a livery business where an element of care is provided by the stable owner, e.g. feeding, mucking-out, putting out to graze, arranging for veterinary and farriery services, etc. However, this may not be so sustainable where the stables are merely rented out for DIY livery and where the horse owner has exclusive use of the stable. There may be a mixture of DIY and non-DIY activities with trading status being secured on the basis that both activities will usually also involve a supply of feed to the stable owner (by the fact that the horse will be put out to graze

in any event). It will, therefore, be necessary to consider each case on its own facts. BPR should be available provided that the stable rent is not the main activity. The businesses of riding schools and horse trekking will be assessable as trading income and therefore should be eligible for BPR.

VAT advantage

Livery yards obtained a potential boost when VAT charged to clients with minimum service (Business Brief 21/2001) was deemed to be an exempt supply. However, such advantage comes with the downside of the 'exempt' supply – not being able to claim back input VAT and the possible complexities of partial exemption. Problems can arise in deciding whether schooling and 'breaking in' are provided. If the yard is mainly a specialist breaking yard, then any supply relating to breaking in will be standard-rated. On the other hand, if the main purpose of the yard is livery, with schooling or breaking as an add-on, then the entire supply will be exempt. Where a horse is sent to a yard that has the specific purpose of breaking in or schooling the horse, rather than as somewhere to keep the horse, then the supply will be standard-rated. Provision of grazing is zero rated (as food) – if there is a significant degree of care then VAT is standard rated. Horse liveries are not farming, and business should be separate from farming in the accounts and tax computation. The advantage of the complete horse livery service (as opposed to DIY) is that it is a business for tax purposes and full BPR should be achieved. It will be difficult to argue that BPR applies to business assets which are subject to exempt VAT registration.

Full livery is where the livery provider is responsible for the complete care of the horse. The owner will come and go and the livery provider should act in accordance with the owner's wishes, but will be fully responsible for the full care of the horse. Full livery will be a trade, and the trade will hopefully have the advantage of BPR. However, the provision of DIY livery is not always a trade.

Finding out that their DIY livery operation is not trading income can be a shock for many landowners and farmers. It can also be a shock if it contributes to the disallowance of BPR. The VAT complexities on the supply of land are a clear example of how all tax planning surrounding farms and lands has to be comprehensive and looked at in the round. Short-term VAT advantages should not be taken lightly by the taxpayer to the detriment of IHT planning.

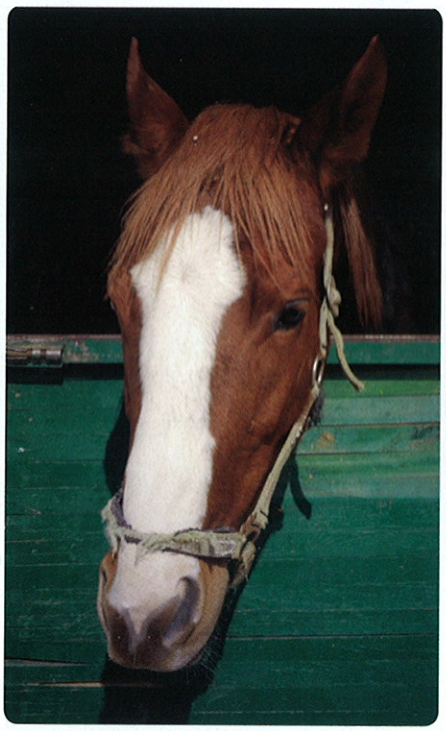
Polo

The sport of polo has recently been brought into the equine tax lime light through a VAT tribunal case (see below). The letting of sports facilities and sporting rights is normally standard-rated. An example of sporting rights is the right to take game which is standard-rated. However, there are debates over the element of land supplied with the facility and the split between exempt and standard-rated. There are special rules for the use of sports facilities where there are lets in excess of 24 hours or for the hire of facilities to the same user for a regular series of events (both then become eligible for exemption but can be opted). It is more difficult to claim BPR where there is an exempt supply.

Polo Farm VAT Tribunal

A recent VAT tribunal case, *Polo Farm Sports Club* VTD20105, has highlighted the fact that the whole area of VAT, the supply of land, the supply of sports facilities and horse liveries could benefit from clarification by HMRC. This could also impact on contemporaneous information to support a BPR claim.

It suited the Polo Farm Sports Club to make standard-rated supplies. It had not opted to tax the land in question. A dispute therefore arose with HMRC, which said the Club was making a series of lettings that should therefore be exempt. In this case the lettings were daily for several hours each day and there was never a whole day between



each letting. HMRC argued that this was nonetheless sufficient to fulfill the exemption criteria, since there was still 'a day' between each letting. But the tribunal preferred the appellant's view, which was that there had to be at least a clear day, or 24 hour period, in order for the rule to apply. The Polo Club won this case and achieved their standard-rated supply, this should also enhance the BPR claim on the polo property but a lot will depend on the activity surrounding the letting.

BPR – the importance of Arnander and the building

(*C J F Arnander, D T M Lloyd and M M Villiers Executors of David McKenna deceased* v *HMRC (2006) Spc 565*)

In practice, the stud outbuildings often have a high probate value and therefore a high potential IHT liability. There is often scope for planning permission and some form of development of the buildings when BPR will be needed as well as APR.

> "The key to the riding school and IHT planning is that it is by definition a vibrant business and eligible for Business Property Relief"

The *Arnander* case also placed focus on the outbuildings. For the Appellants, Mr Massey argued that all the outbuildings were occupied for the purposes of agriculture as they were used, or kept ready for use, predominantly for the purposes of the storage of farm machinery and utilities. His argument was that they were not used for any non-agricultural purposes.

In looking at any future APR/BPR claim on the equine property the use of the outbuildings will be important.

The riding school

Riding schools generally offer a wide range of equine-related activities and training, including lessons at all levels, trekking and hacking, show jumping tuition, dressage, etc. They may also offer ancillary facilities such as an all-weather or indoor sand school, full, part or DIY livery, holiday accommodation and tack and equine supplies. Some riding schools are small-scale and offer only basic facilities, whilst, at the other extreme, some may have a whole team of British Horse Society (BHS)-qualified instructors and quality horses/ponies. The key to the riding school and IHT planning is that it is by definition a vibrant business and eligible for BPR.

Horse tourism, trekking and riding holidays

This activity is not farming nor is it agriculture but it is a useful diversification activity for farming. The equestrian industry is now a major economic factor in many rural areas. Thus there are many opportunities to offer equine recreational facilities – both to those who do not own a horse of their own, and also to those who can provide their own mount.

The range of establishments offering riding holidays is large. Details are available from the British Horse Society. This can be an additional attraction of the 'Furnished Holiday Let' market, and a diversification activity.

Many farms offering bed and breakfast or cottage accommodation will also have suitable buildings to accommodate owner's horses. In locations with good riding facilities this can be a strong selling point and higher charges can be made. Customers will expect certain minimum standards in any horse accommodation. As a comparison to *McClean* they do provide 'hotel accommodation' for the horses and therefore the opportunity to claim BPR is robust.

Summary

Equine IHT planning is complex. No one equine property or the involvement of the proprietor(s) is the same. The definition of and difference between providing DIY liveries and providing 'hotel accommodation' for the horse is complex and the VAT legislation does not help in provision of guide to the difference between a trade and the supply of a space to keep a horse. Has the recent case of *McClean* given guidance? What this case has shown is that where the equine business involves letting, it is imperative to look to the degree of service provided in order to maximise the claim for BPR. ■