

## Why Improving And Repairing Property Can Have Inheritance Tax Advantages

Julie Butler looks at property repairs and inheritance tax efficiency, and highlights a worrying potential legal issue involving wills and inheritances.

Further to last month's article on tax relief for property repairs, we now focus on the impact on inheritance tax (IHT) and wills.

The recent tax tribunal cases on repairs of Pratt (TCO1269), Hopegear (TCO2734) and Cairnsmill (TCO2580), have made repairing property very attractive in terms of income tax relief and overall tax efficiency for the ageing property owner.

Where any property is eligible for IHT relief, spending money on it can prove to be IHT efficient as well. The principle is simple. If one asset (e.g. property) is eligible for IHT relief, any repairs or improvements can increase value and therefore overall IHT relief, whilst possibly achieving income tax relief at the same time. 'Reducing cash' for the taxpayer can also be IHT efficient.

The question is: what sort of property will qualify for IHT relief, e.g. business property relief (BPR) and agricultural property relief (APR)? Examples are as follows:

- freehold property used in a business, e.g. factory, shop, office or farm;
- let cottages ancillary to a farm, e.g. the Balfour (TC69) case; and
- bed and breakfast properties, hotels and furnished holiday lets as part of a holiday complex.

There is no doubt that repair and improvement strategy planning (to incorporate the maximisation of capital allowances) is currently proving very beneficial for property owners. Each case must obviously be looked at on its own merits.

### Repairs and improvements

Whether expenditure qualifies as repairs or capital can be a very grey area. In general terms, any money spent on repairs, new buildings and generally improving property will currently fall into one of the following categories of

expenditure:

1. repairs (see Pratt, Cairnsmill and Hopegear);
2. capital allowances (n.b. the current limit on annual investment allowance (AIA) of £500,000 ceases on 31 December 2015); or
3. improvements.

### Plans for cash expenditure

Cash left in an estate will be subject to IHT. Therefore, if the cash is used on the property portfolio there can be tax relief. The principle of repair now, save income tax and IHT, is a valued tax planning point which has to be considered as an overall tax planning strategy. An example may be an elderly farmer planning to build a new barn, or to repair an existing structure. There has to be consideration as to the complexities of what does qualify for capital allowances, and what is classified as a repair to achieve income tax reliefs. The Wetherspoons case (SPC657) provides useful guidance as to the function of the trade understanding what plant qualifies for capital allowances. The repaired farm property will qualify for IHT relief and the money spent for income tax relief.

### Capital allowance control

With the current beneficial ability to claim capital allowances on plant and machinery that is 'integral' to the property (e.g. farms and furnished holiday lets), there are going to be more problems for the probate valuation of property and increased need for accountants and probate valuers to work together. The current AIA ends on 31 December 2015, so time is of the essence.

When very beneficial tax planning exists for elderly property owners, care must be taken to consider the potential for will disputes and any 'undue influence' on decisions made. For example, if one 'child' is due to inherit property and another child cash and investments, the children can 'influence' the value of what they will achieve under their parents' will.

### IHT efficient repairs

One problem that can arise from spending money on property is the correct consideration of the elderly property owner's will. For example, with regard to farming, the will

could read that one son – perhaps the one who doesn't remain working on the farm – is due to inherit the outside investments, while the son who works on the farm is due to inherit the farming business. Perhaps the farming son has in good faith persuaded his father to move the investments into farm repairs and machinery - the son who doesn't stay on the farm then has nothing left to inherit.

It could be that everything has been dealt with in good faith and for the good of the farming business. The matter could be dealt with by a claim for 'presumed undue influence' by the child who is left nothing in the will, as a direct result of the actions of the son who remains farming.

### Presumed undue influence

The recent case of Hart and Samways v Burbidge [2013] EWHC 1628(Ch) provides a good illustration of how 'presumed undue influence' can impact on many wills involving property.

The question has to be asked, when the property owner is being encouraged to spend more on the property by the sibling who is in line to inherit, is legal advice being obtained? The case of Burbidge shows it is necessary for the court to be satisfied that the advice and explanation by a solicitor was effective to free the donor from the impairment of influence on his 'free will'. The sibling who has nothing or a considerably reduced sum left to inherit after the changes, needs protection.

### 'No deliberate wrongdoing'

The Hart and Samways v Burbidge case is a good illustration of the factors that will lead the court to determine that undue influence has taken place, even where there has been no deliberate wrongdoing.

- The case involved two brothers claiming their sister Susan had exerted undue influence over their mother, causing them to lose out on the property they were due to inherit under her will.
- The court held it was the daughter's duty to prove there was no undue influence and she failed to do so.
- While there was no evidence of actual undue influence, there was a relationship of trust and confidence between mother and daughter, which gave rise to presumed undue influence.

The judge absolved Susan of any deliberate wrongdoing,

but emphasised that undue influence can still exist in those circumstances, and relief can still be granted to undo the transactions procured by it. The problem was that when selling property the mother did not obtain independent legal advice.

### The inheritance problem and possible solution

How can property owners and their advisers protect against future situations such as shown in the Burbidge case?

- Wills with high property values are being challenged. 'Estoppel' cases are becoming common place and with the high value of property such disputes could be something that will be more frequently dealt with in future.
- When a property owner who is perhaps elderly is being 'persuaded' by one child to change property ownership then legal help should be considered. In the Burbidge case, Susan Burbidge could not identify any independent advice received by her mother before mother undertook the transactions in her daughter's favour.
- Many accountants and tax advisers will find that often they are the only advice sought in transactions, with no legal help being taken. What appears positive for income tax and IHT planning might not be positive for will protection. Another problem is that for the partnership accountant, there is perhaps a conflict of interest, and ideally this should be identified where appropriate. Independent legal advice must be obtained.



### Practical Tip:

Whilst a property repair strategy can be very tax-efficient, property values, including farms, have increased dramatically in the last decade, and this has not been matched by an increase in other investment values.

If it is a long time since legal advice has been sought, then significant tax planning advice should be matched with legal protection. It could well be that the elderly property owners refuses legal assistance. In this case, the accountant/tax adviser should set out the disadvantages of failing to do so. Many property owners do not have up-to-date partnership agreements, wills or a legal overview of all matters; and this is something that should be considered by all tax advisers.