

# Issue focus

## Investment

Trusts and emotive assets • Privacy, security and property • Luxembourg limited partnerships

### KEY POINTS

#### What is the issue?

Practitioners should seek to understand the trading spectrum of the use of property, from passive receipt of rent to a trading operation, and why the business has to be pushed along to the 'trading' end.

#### What does it mean for me?

Successful business property relief claims need a file of qualitative and quantitative evidence proving the trading tests.

#### What can I take away?

Practitioners should advise clients with a business that involves holding property and a trading business to ensure that the trade is well documented and evidenced going forward.



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# Worlds apart

## JULIE BUTLER AND FRED BUTLER ASK WHERE THE APART-HOTEL SITS ON THE TRADING SPECTRUM IN ENGLAND AND WALES

There have been a number of tribunals that have looked at the definition of a trading business for inheritance tax (IHT) purposes, focusing on the evidence of services provided and not just the passive receipt of rent being an investment business. In *Mr Bruce Firth & Mrs Rita Firth as Trustees of the L Bately 1984 Settlement v HMRC*,<sup>1</sup> the First-tier Tribunal (the Tribunal) dismissed a claim for IHT business property relief (BPR). The services provided by the 'apart-hotels' concerned were considered insufficient to prevent the business from being classified as an investment business by the Tribunal. This case follows the successful cases of *Vigne (The Commissioners for HMRC v The Personal Representatives of the Estate of Maureen Vigne (Deceased))*<sup>2</sup> and, in particular, *Graham (The Personal Representatives of Grace Joyce Graham (Deceased)) v HMRC*,<sup>3</sup> as this related to holiday accommodation. Both *Vigne* and *Graham* showed the importance of a portfolio of evidence.

### TEN-YEAR CHARGE

In *Firth*, the facts were that the mentioned trust was subject to a ten-year charge

in relation to shares held in a company, The Lawrance (Hotel Living) Ltd (the Lawrance). The trustees claimed that the potential IHT liability was reduced to zero because of the availability of BPR. His Majesty's Revenue and Customs (HMRC) issued a determination denying BPR and the trustees appealed. The L Bately 1984 Settlement (the trust, in this instance) held 31 per cent of the shares in a company, the Lawrance. It had originally been a shareholder in the group holding company but in 2012, as part of a demerger, exchanged its holding for shares in the Lawrance, which became a separate company.

The Lawrance operated an 'apart-hotel' business; such activity is generally a 'hybrid' of a hotel and furnished apartments. At a glance, it can be seen that this is a mix of trade that should and could attract BPR, where the hotel does and the furnished let does not, but there is a problem. The Lawrance operated from premises in York and Harrogate in England. The question for the Tribunal was whether the combined business was wholly or mainly one of making or holding investments under s.105(3) of the *Inheritance Tax Act 1984*. ➔➔



### ACTIVITY AND SERVICES AT ISSUE

The Lawrance describes its apart-hotels as offering accommodation with the quality of a boutique hotel together with the freedom and privacy of apartment living. It might be argued that there is conflict between 'freedom of living and privacy' with the place on the trading spectrum that BPR qualification demands. The facts were as follows:

- The majority of guests were corporate customers staying for up to three nights.
- All apartments were available to let on a night-by-night basis but were not serviced for stays of less than a week other than on request.
- They provided welcome packs with tea, coffee, milk, etc., as well as Wi-Fi, bedding and towels.
- Guests could request additional packs for a fee, including items such as flowers, cakes, Prosecco, etc.
- One property comprised nine serviced apartments with a reception, communal kitchen and conference room but no parking.
- One of the properties included a café on the ground floor due to a planning requirement for there to be a retail unit. The café was operated by the hotel and could provide breakfast to the apart-hotel guests for an additional cost. On the other floors, it had 13 serviced apartments and a reception area but no parking.
- The other two properties comprised nine serviced apartments and a coach house with some private parking but no reception or other communal areas, other than a garden.
- The evidence showed that the café was not profitable, the receptions were closed two-thirds of the time, the conference room was rarely used and guests were actively deterred from using the out-of-hours service.

There is no doubt that there was potential to claim BPR on this interesting activity. It would seem that the services could have reached the trading standard required.

### THE NEGATIVE FOR BPR

The Tribunal was of the view that there was no debate that the hotel was a business, but looking at that business and all factors in the round, and applying a qualitative not quantitative test as set out in the case of *Executors of The Estate of*

*Marjorie Ross (Deceased) v HMRC*,<sup>4</sup> the hotel did not qualify for BPR.

The negatives for the BPR claim were the underlying facts:

- The hotel was originally acquired as investment properties.
- The property reception seemed to act more as the administrative hub of the investment business rather than as a service for guests, dealing with complaints and requests, maintenance, repairs, insurance and business rates.
- Food and extras were peripheral to the business at less than 5 per cent of turnover.
- There was a lack of clear evidence to substantiate claims made by the appellants that additional services were regularly provided to guests: this is a must for future claims.
- Although some apart-hotels would be categorised as providing services with the ancillary occupation of the accommodation, taken as a whole, the non-investment activities of the hotel outweighed the ability to do this.

### A BUSINESS, BUT HOW FAR ON THE TRADING SPECTRUM?

It was found that the hotel's activities did not take the business over the line away from the investment side of the spectrum and BPR did not apply. However, it could be argued that the investment line is marginal and with better evidence and trading activity there might be a possibility of relief being achieved. Moving forward, that should be reviewed by the owners of such marginal property.

The Tribunal accepted that the business had some features that pointed away from investment but those did not outweigh the many factors that pointed to this being an investment business. It could be argued that the activity overall was not greatly different from that of some national hotel chains, which provide little more than a room and a reception desk, and those must surely be trading businesses. There is often a presumption that the provision of meals takes a business over the line from investment to non-investment but that is complex in the context of modern hotel trading. Many commentators saw this as a negative for the apart-hotel. The authors see it as a timely reminder for a comprehensive provision of services and evidence pack.

### BE PREPARED

The case was hampered by a lack of financial information to support the hotel's

arguments. There were also no detailed descriptions of how the staff spend their time and no timesheets, as in *Vigne*. The Tribunal also found that the general manager had 'over-egged the pudding' when it came to giving evidence and had hyped up her account of what services were provided. The 'hype versus financial fact' element was clearly of importance to the Tribunal and worthy to note in the future. The case also gives guidance to all those with marginal BPR cases to act now. Those owners of businesses that are on the investment/trading spectrum should review their strategies to ensure that there is real activity and evidence to move the business on the spectrum from investment to trading and therefore qualify for BPR.

Tax advisors planning to submit any claim for agricultural property relief and BPR must have a pack of evidence ready. Some would say that *Firth* does not change the view on the understanding of the application of BPR relief on a property-based business. However, it does emphasise the need to be prepared for a challenge, to warn the clients and to start to prepare to defend the five tests of *George*,<sup>5</sup> followed through in *Balfour*<sup>6</sup> with the so-called 'Balfour Principle':

- the time spent on each aspect of the business;
- the capital employed in the business;
- the income of the business;
- the profit made by the business; and
- the overall context of the business.

These should be analysed in financial terms, as well as information surrounding the operation, e.g., staff job descriptions in employment contracts together with itemised invoices, websites, reviews and advertising brochures.

The Tribunal found that the actual operation of the business, where guests rarely spoke to staff, with little evidence on how many requests guests made, was more akin to a self-catering apartment with a complaints line. The principal business was investment, so no BPR was available. It can be argued that the best evidence of requests by guests and the service associated therewith is the staff timesheet, as shown in *Vigne*.

### #LAND AND PROPERTY #TAXATION #TRUSTS

<sup>1</sup> [2022] TC8542 <sup>2</sup> [2018] UKUT 0357 (TCC)

<sup>3</sup> [2018] UKFTT 0306 (TC) <sup>4</sup> [2017] TC05959

<sup>5</sup> *George and Loochin (as executors of the Will of Elsie Fanny Stedman, Deceased) v The Inland Revenue* [2003] EWCA Civ 1763 <sup>6</sup> *Brander (Earl of Balfour) v HMRC* [2010] UKUT 300 (TCC)