The twist in the tale

Julie Butler on cleansing of potential development land using holdover reliefs

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With more development potential now presenting itself for agricultural land, serious tax planning will be needed and the GBP5 million limit for entrepreneurs' relief will be looked to.

The restrictions on entrepreneurs' relief are fairly onerous with regard to the fact that it cannot be let property, it cannot be a mere asset disposal, it must be the whole or part of the business and therefore it is likely that the owners of the land will turn to rollover relief as an alternative to entrepreneurs' relief. However, rollover relief has equal problems in many cases in that it is restricted via the mixed use or partial use where there has been non-business use for a while, e.g. the let property, the private use, etc, and this can be restrictive. It can also be difficult to find enough property to meet these criteria. However, perhaps the twist in the tax planning tale relates to the availability of capital gains tax (CGT) holdover relief.

Holdover relief

In order to qualify for holdover relief it is limited to a transfer at undervalue, normally to a family member. In looking at whether it is agricultural property that is being transferred, guidance is given in section 115(2) – 'agricultural land or pasture includes woodland and any building used in conjunction with the intensive rearing of livestock or fish. If the woodland or building is occupied with agricultural land or pasture and the occupation is ancillary to that of the agricultural land or pasture and also includes cottages, farm buildings and farmhouses together with land occupied with them as are of a character appropriate to the property'.

Therefore, in order for potential development land that has been used for agriculture to be passed down to the next generation it simply has to comply with the holdover relief provision of being agricultural property and being used for an agricultural purpose and being occupied in the correct way. However, it does not have to meet the stringent requirements of, say, rollover relief where there are restrictions for, as already mentioned, partial business use of development land, i.e. where the land that is part of the rollover relief claim contains areas that qualify for business use and areas not used for the purpose of the trade. Guidance in relation to rollover relief is found in the *Taxation of Chargeable Gains Act (TCGA) 1992* s152(6) where, for the period of ownership, or any substantial part of the period, part of a building structure or area is not used for the purpose of the trade. Where there is mixed business and non-business use of development land for rollover relief, there is restriction and this is covered in *TCGA 1992* s152(7). This deals with the situation where at some stage within the ownership period there is no qualifying use whatsoever.

The period of ownership cannot commence earlier than 31 March 1982. It is generally accepted that the apportionment of costs and disposal proceeds will be undertaken on a just and reasonable basis for this mixed business use, i.e. between business use and non-business use.

With the onerous provisions of rollover relief and entrepreneurs' relief there is a temptation with the potential development land to pass it down to the next generation using the holdover provisions for agricultural property and then wiping this land clean of those problems, i.e. periods when the land was let, periods when it was used for private use. Then in the hands of the next generation one can ensure that there is the required period which is only one year of business use; then the entrepreneurs' relief and the attractive 10 per cent rate of capital gains tax can be available. When this is compared

to the much more onerous 28 per cent of capital gains tax this is very attractive.

This could, for example, apply where some land has become available for development that was part of a main farm. It can be transferred to the next generation at a time when it would not qualify for entrepreneurs' relief, for example it is let up to the time of transfer. Under, say, a farm business tenancy the tenant could be given notice so that the property was clear, transferred at the end of the tenancy, move into new ownership so that it qualifies for entrepreneurs' relief as the entirety of their business conducted on the land and then be disposed of after the one year qualifying period.

Obviously transactions of such a large value could cause problems. The inheritance tax considerations must be thought of as must any anti-avoidance procedures that HMRC would be likely to put in the way to challenge such a disposal. The transfer to the next generation when dealing with the disposal afterwards might be picked upon by HMRC as trading in land and/or a transaction caught under *ITA 2007* s756 which will tax the capital profit as income. The terms of this section encompass a transaction where land is developed with the sole or main object of realising a gain from disposing of the land when developed, and where land is acquired with the main object of realising a gain from disposing of it. Clearly the motives for passing the property down to the next generation must be thought through. Arguably one defence to both a charge under s756 and a suggestion that the land is acquired as trading stock is that the transferees are passive recipients of a gift. As such most of the badges of trading are absent, and equally, a s756 motive to sell quickly at a gain cannot be automatically imputed to them. In theory, it might be more reasonable to apply s759(6) by which the gain can be taxed on a person providing the opportunity for it to be realised (the transferor) but the transferor never acquired the land to realise a gain from it and so that would seem unduly harsh.

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Inheritance tax

The next criteria is that of inheritance tax. Obviously this would qualify as a transfer for agricultural property relief, but consideration must also be given that a District Valuer would probably try and value this property at a high value for the hope value, i.e. when it is transferred as agricultural property from one generation to the next using holdover relief this would be a lifetime gift for inheritance tax purposes. However, it would have to be capable of achieving agricultural property relief (APR) and business property relief (BPR), to cover for the possibility of the transferor not surviving the gift for seven years. If it is let property, there would be problems under the BPR provisions. However, this could be where the 'Nelson Dance' case would come into play, depending on the full facts, and the provisions of such a transfer being tested by reference to the transferor's estate. Note also the recapture of BPR and APR on the decease of the transferor after the land has been sold by the transferee.

There would obviously be a loss in the uplift of value in that the base costs that would have to be used by the next generation disposing of the land would be the original base costs for the family but then that would be no different than as if the transferors had disposed of it. If they were elderly I suppose it could be argued that there would not be the capital gains tax uplift on death. However, there would be various concerns as to whether the land would qualify for full inheritance tax relief and what HMRC would do with the hope value.

So that then really rests on the second disposal when entrepreneurs' relief is claimed. Would there, in actual fact, be an attempt to use section 756 by HMRC? In this regard it is the advantage of life's realities that the development project would probably take a long time and therefore it would be difficult to argue that there were any quick fix advantages to such a transaction.

Action plan

Where there is development land which is tainted with criteria that would make it difficult to claim entrepreneurs' relief and difficult to claim rollover relief there are distinct considerations in using holdover relief to pass to the next generation. There is then a clean product that can then be sold, being able to use rollover relief and entrepreneurs' relief and the advantage of the 10 per cent without problems.