



Trading places

A number of recent cases point to a worrying new trend by HM Revenue & Customs, whereby it assesses farms as investment rather than trading businesses – which do not therefore qualify for business property relief. Julie Butler explains what action farmers need to take

Lifetime inheritance tax (IHT) and capital gains tax obviously have to be planned for in detail by business owners, but such succession planning has not generally been embraced within the farming and rural industries. It has been argued that this needs to change, to bring farming in line with other industries, but as farmland values increase, and worries over loss of control, loss of income and loss of the farm through divorce become more common, action is frequently prevented.

One potential impetus for change is the recent trend by HM Revenue & Customs (HMRC) Capital Taxes Office (CTO) to try to classify businesses with a large asset base as an investment, although they have previously been treated as a trade for income tax purposes. As a result of this change, it tries to deny business property relief (BPR). Despite the fact that the trading results have been recorded on the trading pages of the appropriate tax returns, and class 4 National Insurance has been applied when the owner of that business dies, there have been problems with HMRC denying BPR where there is substantial freehold property. This approach has been evident in two 2013 tribunal cases: *Nicolette Vivian Pawson (Deceased) v HMRC* [2013] UKUT 050 (TC) and *Trustees of David Zetland Settlement v HMRC* [2013] UKFTT 284 (TC).

WHY THE APPROACH IS FLAWED

This approach of denying BPR seems flawed, in that it appears to look at what is being provided by the farmer / landowner in the context of the provision of land, and possibly buildings, as the main supply, plus some minor services. The services can never match the value of the land, so if the CTO considers the level of services in terms of a much larger supply of property, it is very easy to argue that a business is not a trading entity and never can be. The supply of land and property pushes the activity to the wrong side of the 'investment line'.

Examples of such activities are liveryes and holiday lettings. There is a lot more management involved in these than many realise, and an 'intelligent businessman' would view them as a trading operation, and something that was always intended to achieve BPR from the original drafting of the legislation. However, HMRC is pushing back the boundary, and its prize would appear to be a very large potential tax take from farmers and landowners who operate such activities. All such activities must consequently review their operations as a matter of some urgency.

THE WIDER CONTEXT

This approach would seem to be part of a wider attack by HMRC on many different areas of agricultural property relief (APR) and BPR. Examples of potential problems for HMRC to focus on are:

- a mixed estate that has too many investment properties which have greater income and value than the farming operation – no BPR (section 105(3) of the Inheritance Tax Act 1984);
- occupation for the purposes of agriculture of the farmhouse for the last few years where the farmer has 'semi-retired' due to ill health while still owning the farming business;
- redundant farm buildings and structures full of 'junk' that are not used

in the trade – no BPR or APR;

- a farmhouse surrounded by let land so it is not actually occupied for agricultural purposes – no APR; and
- pushing a trade over the 'investment line' into an 'investment' category in the eyes of HMRC – no BPR.



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HOW TO RESPOND

There is no doubt that the taxpayer will need to present a strong portfolio of evidence, so that an intelligent businessman can decide what side of the 'investment line' the business falls on. Thought must also be given to how to beat HMRC in its consistent and seemingly determined attack on genuine rural businesses that are trading and operating well into the proprietor's old age. It is essential that the collection of evidence is obtained now for all potential BPR and APR claims.

Such evidence should include the notes of the hours worked by the proprietor of every business that comes close to the 'investment line'. The taxpayer will end up with some bulging permanent files supporting IHT claims in the future, but if they do not take this step, HMRC could deny IHT relief where genuine claims exist, and that appears to be HMRC's current approach. Professionals must be ready to protect genuine arguments for the availability of IHT reliefs.