

NATIONAL TUTORIAL 2024

TAX ISSUES

MODEL ANSWER

This is an Outline Answer, covering the points raised in a very broad problem, covering more content than might be covered in an exam question tackled in 40 minutes.

This Outline Answer Sheet is intended to be read alongside the detailed Tax Notes provided to Delegates

We know that the Estate currently consists of a mixture of commercial, residential, and agricultural land. The split between in-hand operations and property let-out is roughly 50/50.

We are asked to set out the tax issues facing the Estate generally, and what the Estate could be doing to mitigate the issues.

We are told that Bruce and Holly own the Estate. Inheritance Tax is going to be a key driver when considering how to structure the Estate as part of their overall succession plan.

Accordingly, we should start by considering the availability of any potential reliefs from IHT for the composite parts of the Estate (750ha in total).

ASSET	DESCRIPTION	OCCUPANCY
Home Farm	400ha mixed farm of arable and livestock (includes potential development land?)	In hand – Lucy and Stuart Is this Partnership property? Lucy plans to diversify part of the bare land to sell produce and to run a glamping site
Argyle Farm	90ha dairy farm with grade II farmhouse and farm buildings	Let to Gruber family since 1978
Hillside	120ha tenanted farm, with a picturesque dwelling and range of traditional buildings	Let on periodic tenancy
Other let farms	Various	Let
Manor House	Is the Manor House the centre of the farming operation?	Entire family live there – the three children want to move out
An industrial estate	Let to 3 commercial tenants and 2 empty commercial sheds and yards not currently let or used	Let
Gennero Links Golf Course	Golf course business	Trading?

Accordingly, we need to start by considering the availability of any potential reliefs from IHT for the composite parts of the Estate.

1. Agricultural Property Relief

Where applicable, Agricultural Property Relief (**APR**) will provide 50% or 100% relief from IHT on the agricultural value of property / land occupied for the purposes of agriculture.

As per section 115 IHTA 1984, APR applies where the property / land has been used for agricultural purposes and either:

- (a) occupied and used for agricultural purposes **by the owner** for at least **two years** prior to the owner's death; or
- (b) occupied and used for agricultural purposes **by a third party** for at least **seven years** prior to the owner's death.

APR will only cover the agricultural value of the land (the value the agricultural property would have it was subject to a perpetual covenant prohibiting its use other than as agricultural property – section 115(3) IHTA 1984).

This may not be the same as the full market value of the land. If the land has a market value which is more than its agricultural value, then the excess value will not be covered by APR – this is important in relation to the potential development land, and we will come back to that.

Home Farm

We are told that Home Farm is farmed in-hand and is a mixed farm of arable and livestock.

It has been owned by Bruce and Holly for the required two years and is clearly farmed / used for the purposes of agriculture. Therefore, 100% APR should apply to the agricultural value of Home Farm.

Note however, that if any of the land has an excess market, or "hope" value (for example, if part of Home Farm neighboured Green Valley and has development potential), then that excess market value would not be covered by APR.

It might be possible for the excess market value to be covered by Business Relief, if the land formed part of a wider, composite, wholly or mainly trading business, for example in a partnership – please see further below.

The APR position becomes more complicated if Lucy and Stuart pursue their glamping enterprise. APR is only available on assets used for agricultural purposes; running a glamping business does not fall under the definition of agriculture. Therefore, Bruce and Holly would lose APR on the part of the bare land used for glamping / the farm shop. This is an important point to consider when taking land out of agricultural use, for example when looking to explore diversification projects on the Estate. The same issues apply for the farm shop.

Presumably the glamping business / farm shop are intended to be trading businesses carried out for profit, and so Business Relief could apply (see detailed notes).

Therefore, if Lucy and Stuart wish to pursue the glamping business, Bruce and Holly should consider this as part of their overall succession plan. It might be prudent for them to consider a gift of that part of the land to Lucy and Stuart whilst it still qualifies for APR, in the hope of surviving seven years after which the value of the gift would leave their estate for IHT purposes (even if the land is no longer being used for the purposes of agriculture). Bruce and Holly are 75 and 72 respectively, so there is an argument for doing this sooner rather than later.

The capital gains tax (**CGT**) position upon any proposed gift would need to be carefully considered, although on the face of it any gain triggered by Bruce and Holly would be able to be "heldover" under section 165 TCGA by virtue of the fact that the land is agricultural, and would qualify for APR. See below and the detailed notes for further information re CGT.

Argyle Farm

Argyle Farm is let to the Gruber family.

Agricultural land let before 1 September 1995 will, unless certain conditions relating to land owned pre-10 March 1981 are fulfilled, only qualify for 50% APR. This is compared with 100% APR that is available on land subject to a FBT entered into from 1 September 1995 onwards.

If this is an AHA 1986 tenancy, it therefore appears that Argyle Farm would only qualify for 50% APR. If possible, Bruce and Holly could look to replace the AHA tenancy with an FBT so that 100% APR would be available.

Hillside

This is let on a periodic tenancy. If the land is used for the purposes of agriculture, then APR should be available at 100% on the basis that Bruce and Holly satisfy the seven-year ownership requirement under section 115(3) IHTA 1984.

We must also consider the farmhouse, which we are told is a "picturesque dwelling". APR can apply to the agricultural value of a farmhouse if it is occupied with the agricultural land or pasture and is of "character appropriate" to the agricultural property. As the farmhouse would be occupied by another, Bruce and Holly would again need to satisfy the seven-year ownership requirement.

The availability of APR on a farmhouse is a complex area guided by caselaw. In simple terms, the farmhouse is the place from which the farmer (the person who farms the land on a day-to-day basis) conducts the farming operation. In practice, the position is almost always more complex where (for example) farmers let land to others, enter partnerships and ultimately retire / cease to carry out agricultural activities.

When assessing whether a farmhouse is of "character appropriate", HMRC base their approach on the Antrobus case which sets out the main factors to be considered, including its size, layout, and content, whether it is "proportionate" to the farming activities being carried out, and how long the farmhouse has been associated with agricultural production. HMRC also apply the "elephant" test – you know a farmhouse when you see one. Further information would be required to establish whether the farmhouse was of character appropriate to the overall farming operation – a significant country house would be far less likely to qualify for APR than a working farmhouse.

We are told that Hillside also includes a range of traditional buildings, although we are not told specifically what they are.

The agricultural value of buildings used for the purposes of agriculture (e.g. barns) can qualify for APR. In addition, the agricultural value of farm cottages can qualify for APR if the cottage is occupied by persons employed solely for agricultural purposes (supported by the case of HMRC v Atkinson) and provided that they are of "character appropriate". In Atkinson, it was said that there should be "some sort of connection between the residential use of the cottage and an agricultural purpose sufficient to make the use occupation for the purpose of agriculture".

Other let farms

Further information is required to advise in full, but we can apply a similar analysis as set out above in relation to Argyle Farm and Hillside.

The industrial estate

APR is only available on assets used for agricultural purposes. Therefore, the industrial estate will not qualify for APR. Please see below re Business Relief.

Gennero Links

The golf course is obviously not an agricultural use, and so no APR will be available on that land. Please see below re Business Relief.

The Manor House

As set out above, APR can apply to the agricultural value of a farmhouse if it is occupied with the agricultural land or pasture and is of "character appropriate" to the agricultural property.

However, the Manor House may not be of "character appropriate" to the wider farming operation. If Manor House is a significant country house (we are told that the entire family are living there, and so presumably it is fairly large!), then it would be far less likely to be of character appropriate to the overall farming operation.

Even if the agricultural value of Manor House qualified for APR, the position may change if Bruce and Holly were to step back from the day-to-day farming operation in their retirement. The retirement of farmers has the potential to impact the APR position, and so advice should be sought.

2. Business Relief

BR can provide 50% or 100% relief from IHT on the full market value of the land where it applies. Please see section 105 IHTA for the categories of relevant business property eligible for BR, and their respective rates of relief. The relevant property business needs to have been owned for two years.

It can be extremely valuable in relation to agricultural property that qualifies for APR but has an excess market value, as BR would cover any difference between the market value and agricultural value of the land.

Crucially, where land is owned by an individual and used by a partnership or business they control then it will only receive 50% relief for BR purposes.

Home Farm

Let's consider Home Farm. There was some discussion earlier about whether Home Farm was a partnership asset and being farmed for the purposes of a trade. For these purposes, let us assume that Home Farm is a partnership asset let's assume that the glamping business / farm shop have been carved out – the farming income generated by the farm trade, for profit, would indicate that the partnership was wholly or mainly trading, so that BR applies to the land at 100%.

This is particularly valuable for Bruce and Holly if there is any excess market value to the land (for example if some of it has development potential), which is not covered by APR. BR would cover the full market value of the land (including the excess above its agricultural value).

Argyle Farm, Hillside, let farms, commercial lets

Unfortunately, BR would not apply to Argyle Farm or Hillside in these circumstances. The fact that the land is let means that it will be deemed to be an "investment" asset in Bruce and Holly's hands – they are simply receiving rents, as opposed to actively "trading", as required for BR.

The same would apply to the other let farms and the commercial lets on the Estate – these would be deemed to be "investment" assets, simply generating an income as opposed to being used for a trade.

Gennero Links

We would need further information to consider the golf course business in detail.

We are told that Simon helps with the running of the golf course. We know that the golf is owned by Bruce and Holly, but we are not told that they are operating it as a trading business.

If Bruce and Holly own the land but use it in a business that they are a partner in or a business they control, then the land will only receive 50% relief for BR purposes.

Bruce and Holly could explore ways of introducing a corporate structure to run the golf club business, so that it qualifies for 100% BR in its own right. A corporate structure would enable income to be taxed at lower rates of corporation tax. However, the transfer of land into the corporate structure would need to be very carefully considered – CGT and SDLT issues would be in point.

The golf club business could also form part of a wider, composite, wholly or mainly trading business (please see further below) so that it qualifies for 100% BR in its own right.

Can the Estate be structured as a composite, trading business for BR purposes?

We are told that the split between in-hand operations (i.e. trading activities) and property let out (i.e. investment activities) is roughly 50/50.

We know that BR at 100% can apply to an interest in a wholly or mainly trading partnership. This might enable the overall estate to be structured as a single, composite, wholly or mainly trading business, which can qualify for BR, despite the assets of the business including what would ordinarily be deemed to be "investment" assets if considered on an individual basis (i.e. Argyle Farm, Hillside, let farms, commercial lets etc).

This potential planning strategy would be based on the principles laid out in the case of Brander (representative of James (deceased), Fourth Earl of Balfour) v Revenue and Customs Commissioners [2009] UKFTT 101 (TC), [2009] 374 9 (the so-called Balfour case - see notes) - if the majority of the business (i.e. more than 50%) is carrying on trading activities, then BR should be available on the business as a whole.

When judging whether this is the case one would need to consider the turnover, profitability, underlying market values and time spent in the trading and investment sides respectively of the business. For example, does the majority of the turnover come from the **trading** farming business, or from the let property (which would constitute **investment** income)?

Bruce and Holly would be well advised to consider the position in the round to ascertain whether it might be possible to structure the Estate in a way which qualifies for 100% BR. Hypothetically, this is possible given what we are told about the trading operations accounting for approximately 50% of the overall operation. The "trading" position could potentially be improved further if vacant possession was obtained on (for example, Argyle Farm and Hillside), and the land was farmed "in hand" by the Estate.

Manor House, assuming that it is a large country house, would not, on the face of it, attract BR (or indeed APR, as it is not used for the purposes of agriculture). If the property was "pre-eminent" for its historical, cultural, or artistic merits, it may potentially qualify for Heritage Relief and be conditionally exempt from an IHT charge. Further information would be required to advise in this respect.

It would also be important for Bruce and Holly to consider the country house in the context of their overall estate planning. It may be that the property can be gifted to the next generation in due course (benefitting from PPR for CGT, and in the hope of surviving seven years from the date of the gift for IHT purposes – please see notes), provided that they move out and do not retain a benefit in the property given away. They could also consider insuring against this potential IHT liability using life insurance.

For completeness, we should note that BR will usually be available for farming business property such as the business banking accounts, farm machinery / plant.

3. Capital Gains Tax

The other key capital tax for Bruce and Holly to consider is CGT when giving assets away.

CGT is charged on any growth in value of certain capital assets (over and above the value at which they were acquired) which are disposed of or deemed to be disposed of by individuals, personal representatives, or trustees.

Any assets held at death would be re-based for CGT purposes to the value as at the date of death (the probate value). There is no CGT payable on gifts between spouses.

However, giving assets away during lifetime is a disposal for CGT purposes, and CGT would be payable on any gain in value between the date of acquisition of the asset and the date of the disposal (less any allowable deductions). CGT is payable at 20

There are certain reliefs available, and Bruce and Holly would be well advised to consider whether any of the following apply when structuring lifetime gifting.

Business Asset Disposal Relief (BADR)

Depending on the nature and underlying structure of the landowner's farming business, BADR could apply to apply a CGT rate of 10% to qualifying gains up to a lifetime limit of £1 million.

Rollover relief on replacement of business assets

Where all conditions are satisfied, rollover relief under Sections 152-159 TCGA 1992 can be available if the landowner makes a disposal of certain business assets and uses those proceeds to acquire new business assets.

If the relief applies, the chargeable gain on the disposal is deferred until the landowner disposes of the new business assets.

Holdover relief

If assets used in a trade are disposed of at less than full market value, holdover relief under Section 165 TCGA 1992 may be available to be claimed by the landowner.

If the relief applies, the chargeable gain on the disposal is effectively deferred until the assets are subsequently disposed of by the transferee. See detailed notes for further details.

4. Environmental schemes / Solar development opportunities

We are told that Karl is an environmentalist and is keen for the Estate to explore new ventures.

Let's focus initially on the proposed solar farm. The land will likely be taken out of agricultural use, and so APR may not apply. Some solar farm agreements permit some agricultural use, but this is not normally enough to secure APR as the main use of the land is the solar farm.

The value of the land would likely increase due to the solar farm, and so even if APR were available, it would only cover its agricultural value.

The land would likely be let to the solar company, and so it would become an investment asset – ineligible for BR in its own right (an investment asset), and an "investment" asset if part of a wider composite, trading business.

Again, for tax planning purposes, Bruce and Holly would be well advised to consider a gift of the land before entering into the agreement, although solar schemes can provide a helpful income stream in retirement.

In relation to environmental schemes generally, the key point to remember is that it will be very important for Bruce and Holly to consider the underlying tax implications of any potential environmental before entering into it, as they have the potential to generate significant and longstanding tax implications for landowners. Depending on the nature and structure of the

deal, capital gains tax (**CGT**), Stamp Duty Land Tax (**SDLT**) and Value Added Tax (**VAT**) could all be in play.

Prior to the Spring Budget 2024, one of the main concerns for landowners exploring opportunities in the natural capital asset market was the potential loss of APR.

If land were to be taken out of agricultural use and instead entered into an environmental land management scheme, APR may cease to apply to the value of the land (as the land would no longer be used for the purposes of agriculture), and the landowner would potentially face a 40% IHT charge on its value upon their death.

In the Spring Budget 2024, the UK Government confirmed that they will extend the existing scope of APR to include environmental land management from 6 April 2025, although that did not make it to the Finance Bill which was rushed through before the July election, and so we await further details on whether the new government will stick to that, or indeed whether wider reform of IHT is on the cards.

There are interesting valuation issues to be considered too – for example, whether existing land has an excess "hope" value based on its potential environmental / Natural Capital uses. It would be prudent for Bruce and Holly to take this into account in relation to her future estate and succession planning, particularly from a tax perspective.

As the succession aspects are very much linked to the overall tax position, it would be prudent for Bruce and Holly to take advice as soon as possible so that any succession strategy can be implemented tax efficiently.