# Business relief

Synopsis: Conditions for business relief.

Date published: 17.08.2023

**Business relief– Section 104 IHTA 1984 and Section 105 IHTA 1984**

Relief is available for transfers of certain categories of businesses and business property. Where the relief applies the value attributable to the 'relevant business property' is reduced, according to the category in which it falls, by 100% or 50%.

Business relief used to be called ‘Business property relief (BPR)’ and this term still features in many textbooks and articles.

## Transfers to which the relief applies

The relief is available for transfers during lifetime and on death.

Subject to the other conditions outlined in this topic, the relief is available on transfers of the following categories of ‘relevant business property' at the rates shown below.

At 100% for...

1. A sole proprietor's business or an interest in a business (such as that of a partner);
2. A life tenant's business or interest in a business (including assets of which they were life tenant in possession under a settlement which were used in that business). Please see **Fetherstonhaugh v IRC [1984] BTC 8,046;**
3. A holding of unquoted securities which, by themselves or in conjunction with other such securities owned by the transferor and any unquoted shares owned by them, give the transferor control of a company; or
4. Unquoted shares.

At 50% for...

1. Shares or securities of a company which are quoted and which, either by themselves or in conjunction with other such shares or securities owned by the transferor, give the transferor control of the company.
2. Land, building, plant or machinery owned by a partner or controlling shareholder and used wholly or mainly in the business of the partnership or company immediately before the transfer, provided that the partnership interest or shareholding would itself, if it were transferred, qualify for business relief.
3. Any land, building, machinery or plant which, immediately before the transfer, was used wholly or mainly for the purposes of a business carried

on by the transferor, was settled property in which he or she was then beneficially entitled to an interest in possession and was transferred while the business itself was being retained.

A holding of shares or securities is treated as giving a person control of a company if they can control the majority of the voting powers on all questions affecting the company as a whole. Shares or securities which form related property are taken into account for this purpose. Where shares or securities are held in a settlement, the voting powers held by the trustees are, except in the case of a discretionary trust, treated for this purpose as held by the person beneficially entitled to the shares – Section 269 IHTA 1984.

For the purposes of the relief, 'business' includes a business carried on in the exercise of a profession or vocation but does not include a business carried on otherwise than for gain – Section 103(3) IHTA 1984.

However, in **Pawson (deceased) v HMRC** (2013) UKUT 050 (TCC) a holiday letting business was conducted with a view to gain and this satisfied the "for gain" requirement of S103(3) (though ultimately business relief was not given as the scale of the activities undertaken in conjunction with the running of the business were deemed to be more typical of the type undertaken by an investment business).

'Unquoted shares' include shares dealt in or on the Alternative Investment Market.

Relief is not available where the business or company is engaged ***wholly or mainly*** in dealing in securities, stocks or shares, land or buildings or in making or holding investments unless...

- The business is that of a market maker or discount house in the UK;

or

- The company is a holding company and the group as a whole is not wholly or mainly engaged in property or investment dealing or holding – Section 105(3) IHTA 1984 and Section 105(4) IHTA 1984.

HMRC's view on whether or not a business is regarded as *wholly or mainly* an investment business is in IHTM25265, namely that, in deciding the question, regard should be had to the main activities of the business, and to its assets and sources of income or gains, over a reasonable period preceding the transfer.

Problems can arise where there are several sides to the business, one or more of which appear to fall within the excluded categories. This has been the subject of a series of cases relating to caravan parks. In **Weston v IRC [2000] STC 1064**, the Commissioners outlined the factors that are to be taken into account, as cited in their previous decision in **Farmer v IRC** [1999] STC (SCD) 321 **SpC 216** as follows...

*"...the overall context of the business; the capital employed; the time spent by the employees; the turnover; and the profit. When these factors have been considered it*

*will then be necessary to stand back and consider in the round whether the business consisted mainly of making or holding investments."*

More recently, a "hybrid" business was considered in **HMRC v A.M. Brander (as executor of the Will of the late 4thEarl of Balfour)** [2010] STC 2666 UKUT 300 (TCC). The same principles as in Farmer were applied.

In practice, most of the Special Commissioners' decisions that a business is predominantly one of holding investments have been cases where the net profit from investment activity has exceeded 50% as a whole. However, the position regarding business relief is not always clear cut as the case law shows.

In **Stedman´s Executors -v- Inland Revenue Commissioners** [2002] STC 358, another case involving a caravan park (which was eventually decided in the Court of Appeal as **IRC v George** (2003) EWCA 1763), a company owned a caravan site and carried on various business activities and more than half of its net profits derived from caravan sales. The issue was whether the holding of land to produce profits was incidental to the carrying on of some other business (which was the provision of services to the residents) or was it the very business itself carried on by the company. In this case the Special Commissioner decided that business relief was due and, while this decision was reversed in the High Court, it was eventually restored by the Court of Appeal. The case shows that the 50% test is perhaps not justified.

Relief is applied automatically without a claim and is given before any available exemptions, but after any agricultural relief (previously referred to as agricultural property relief). To qualify, certain conditions have to be satisfied as to the type of business and as to the length of ownership.

Relief is denied if...

- The business is subject to a contract for sale, unless the sale is to a company which will carry on the business and is wholly or mainly in consideration of shares in the company;

or

- The shares are subject to a contract for sale, or the company is being wound up, unless the sale or winding up is part of a reconstruction or amalgamation to enable the business of the company to be carried on – Section 105(5) IHTA 1984 and Section 113 IHTA 1984. Thus, where there is a binding "buy and sell" clause in the partnership deed or a shareholders' agreement (or company Articles) which binds the continuing partners/shareholders to buy the deceased partner's/shareholder's share(s) from their personal representatives, and vice versa, the relief will not be available. However, an option to buy or sell the shares in a company or interest in a partnership is not considered by HMRC as a contract for sale - Statement of Practice SP12/80.

According to the case of **Beckman v IRC (2000) SpC 226,** relief is also denied to the value of the interest in a partnership owed by the partnership to a retired partner (even where that interest qualified for relief before the partner retired).

### Nature of the relief

The relief takes the form of a percentage reduction in any value transferred which is attributable to relevant business property – Section 104 IHTA 1984. Any exemptions or any reliefs relating to transfers of value are given after business relief has been given.

### Example

The amount chargeable to tax on a chargeable lifetime transfer of relevant business property valued at £400,000 attracting 50% relief, and assuming that the donee pays the tax and the only exemption available is the annual exemption for the year in question, is as follows...

| | £ |
|---|---|
| Value of business | 400,000 |
| Business relief at 50% | (200,000) |
| | |
| Reduced value transferred | 200,000 |
| Annual exemption | (3,000) |
| | |
| Chargeable transfer | 197,000 |

It is important to note that even though business property may qualify for 100% relief from inheritance tax, the value of the business property must nonetheless be included in the estate total for the purposes of determining eligibility for the Residence Nil Rate Band (RNRB).

If the total estate value, including the value of any business property, exceeds £2 million, the RNRB will be restricted.

### Minimum period of ownership – Section 106 and 107 IHTA 1984

Property is not relevant business property unless it was owned by the donor throughout the two years immediately preceding the transfer. This rule is  extended to cover replacement property – Section 107 IHTA 1984.

### Death transfers and lifetime transfers chargeable when made

Relief is given if...

- The donor owned the business property for two years immediately before the transfer.
- It replaced other relevant business property and one or other property has been held for a combined period of at least two years out of the five years immediately prior to the transfer.

In the latter case, the relief on the transfer of the replacement property cannot exceed what would have been due on a transfer of the property it replaced, unless the change of property was made solely in the course of changes in a partnership, or of the takeover of a business by a company controlled by its proprietor – Section 107(2) IHTA 1984 and Section 107(3) IHTA 1984.

Where the donor acquired the property on a person's death, they are assumed for this purpose to have owned the property since the death (the fact that they do not own it until the personal representatives distribute it is ignored). Where the donor acquired the property on the death of a spouse or civil partner, they are treated as having owned it since the spouse or civil partner acquired it – Section 108 IHTA 1984.

The condition that there must have been a two-year period of ownership may be set aside where a donor or spouse/civil partner acquired the relevant business property as a result of a transfer of value if…

- The earlier transfer was itself eligible for business relief;

and

- One or both of the transfers in question took place on death.

If, in such a case, the property replaced other property acquired as a result of a transfer of value, the business relief cannot exceed that which would have been due if the replacement had not been made. And, if the earlier transfer was the occasion of the purchase of the property for less than full consideration, the two-year condition is set aside for a proportionate part of the value transferred, that is the part attributable to the gift element in the earlier transfer – Section 109 IHTA 1984.

**Business relief clawback if donor dies within seven years and donee no longer owns property – section 113A IHTA 1984**

Where potentially exempt transfers become chargeable or further tax becomes payable on a lifetime transfer, chargeable when made, as a result of the donor's death within seven years, relief, at the rate appropriate to the property at the time the gift was made, is only given if…

- The original property has been owned by the donee throughout the period between the gift and the death of the donor – Section 113A(3)(a) IHTA 1984;

and

- The original property qualified for relief at the time of the gift and, immediately before the donor's death, remained property capable of qualifying for relief as relevant business property (i.e. was the original or replacement business property) – Section 113A(3)(b) IHTA 1984.

**Example**

Andy gives Barbara a holding of unquoted shares worth £1 million, which qualify for business relief at the date of gift. Andy dies within seven years. If Barbara has sold the shares before Andy's death, the relief will not be available. Similarly, the relief will be denied where, although Barbara has retained the shares, they have acquired a full Stock Exchange listing before Andy dies, or the donee (Barbara) has entered into a binding contract to sell the shares.

For transfers on or after 17 March 1987, the second condition above is removed for shares which were quoted at the time of the gift, or shares which were unquoted and gave the donor control at the time of the gift and remained unquoted throughout the period until death (Section 113A (3A) IHTA 1984).

If, at the date of the donor's death, the conditions are satisfied for only a part of the gifted property, a proportionate part of the value transferred is reduced – Section 113A(5) IHTA 1984. If the donee dies before the donor, the conditions for relief have to be satisfied at both the date of gift and at the time of the donee's death – Section 113A(4) IHTA 1984.

If the donee is given shares and, as a result of a reorganisation of share capital or a takeover bid, receives other shares, those other shares are treated as the original property – Section 113A(6)(a) IHTA 1984.

If, after the gift but before the donor's death, the donee receives shares in a company in consideration for the sale to the company of the property given, the shares are treated as the original property – Section 113A(6)(b) IHTA 1984.

The 'donee' is the person whose property the original property became as a result of the transfer and includes a life tenant of an interest in possession trust and the trustees of a settlement where no interest in possession subsists – Section 113A(8) IHTA 1984. As a result, dealings with business property comprised in a trust, whether by way of appointment or otherwise, may result in relief not being available when any further tax due on the donor's death is calculated.

If further tax is payable because the donor dies within seven years of a lifetime transfer, chargeable when made, and business relief, though available at the time of the gift, is not available at the time of the donor's death, the additional tax payable is the difference between the tax at death rates on the unreduced value and the tax paid at half the death rates on the reduced value – Section 113A(2) IHTA 1984.

**Replacement property – Section 113B IHTA 1984**

Where the original relevant business property has been disposed of before the donor's death and the proceeds used to buy replacement property the relief is not necessarily lost. The relief will be preserved where the whole proceeds of sale of the original property have been used to purchase the replacement property provided both the sale and purchase were arm's length transactions taking place within three years, or such longer period as HMRC allows, of each other. Additionally, the replacement property must be of such a nature that, were it transferred by the donee immediately before the death of the donor, it would (apart from the minimum period of ownership requirement) itself rank as relevant business property qualifying for relief.

**Gifts with reservation - Paragraph 8 Schedule 20 FA 1986**

For relief to be given by reference to either the death of the donor or when the property ceases to be subject to the reservation, the requirements are that, at the time of the gift, the property was relevant business property which would then have qualified for business relief and that in relation to a notional transfer of value treated as made by the transferee immediately before the death, the property would qualify for relief. For the purpose of considering the notional transfer of value by the donee, ownership by the donor before the disposal by way of gift and occupation before and after, are treated as ownership and occupation respectively by the donee for the purposes of Section 106 IHTA 1984.

**Example**

Alex gives his business to Bill in 2020, reserving for himself an annuity of £10,000 a year. On Alex’s death in 2023, the business is treated as part of Alex’s estate and, for the purposes of business relief, Bill is treated as having made a transfer of value at that time. The two-year ownership test required by Section 106 IHTA 1984 is by reference to Bill's ownership. If, in this example, Alex had died in 2021 when Bill would only have owned the business for one year, Alex’s ownership prior to the gift would have been treated as part of Bill's ownership for the purposes of the test. The rate of relief is the rate applicable to the property at the date of the notional transfer by the donee - Paragraph 8(1) Schedule 20 FA 1986.

**Value of relevant business property and excepted assets**

The value of relevant business property for the purposes of the relief is worked out in the normal way. If the property is an unincorporated business, or an interest in such a business, its value for the purpose of the relief is the net value of the business. That is the value of the business assets, including goodwill, less the liabilities incurred for the purposes of the business - Section 110 IHTA 1984.

The amount of any relevant business property which qualifies for the relief is reduced insofar as it is attributable to 'excepted assets' – Section 112 IHTA 1984. An asset is excepted if it was not either used wholly or mainly for the purposes of the business throughout the two years immediately before the transfer (or since its acquisition by the concern if more recent) or required at the time of the transfer for future use for the purpose of the business. An asset is also excepted if it was used

wholly or mainly for the personal benefit of the donor or a person connected with the donor.

Relief is due on assets lent to a partnership or company by a partner or controlling shareholder only if, in addition to the 'minimum period of ownership' condition, the assets have been used by the business concern throughout the two years preceding the transfer or, where one asset replaced another asset if the assets together have been used by the concern for at least two years out of the preceding five. This period is limited to the actual period of ownership where the 'minimum period of ownership' condition is modified – Section 112(3) IHTA 1984.

Where any land or building is an excepted asset but part of it is used exclusively for the purposes of the business, that part is regarded as a separate asset and is taken into account, where the conditions are satisfied, in determining the value of relevant business property – Section 112(4) IHTA 1984.

The application of the "excepted assets" rule was examined in **Barclays Bank Trust Co Ltd v IRC (1998 SpC 158)**. Barclays Bank was the executor of the Will of a woman who died in 1990 owning 50% of ordinary shares in an unquoted company (the other 50% owned by her spouse.) The company sold bathroom and kitchen fittings. HMRC accepted that business relief was due on these shares. The annual turnover of the company was around £500,000. From 1986 to 1990, the relevant date for the purpose of this case, the company`s deposit account had risen from £188,000 to almost £460,000. Circumstances not unlike these may be relevant in many successful private businesses who do not spend, or who reinvest, some or all of their profits.

HMRC argued, and Special Commissioners accepted, that of the cash deposits only about £150,000 was needed for business purposes in 1990, the remaining £300,000 being "excepted assets" as defined in Section 112(2) Inheritance Tax Act 1984, i.e. those assets not used wholly or mainly for the purposes "of the business concerned" in the two years up to the relevant date, nor *required at that time for future use in the business*. The constantly upward trend of cash in the bank account would seem to bear this conclusion out.

The fact that the company had made unsuccessful enquiries as to the possibility of purchasing a competing company prior to 1990 and the fact that the company did, in fact , complete the purchase of another business in 1997, using up £355,000 of the then available cash, made no difference.

The Special Commissioner's opinion was that the term "*required for future use*" implies some imperative that the money will fall to be used upon a given project or for some palpable business purpose", not a possibility that it might happen.

Note that legislation was introduced in Finance Act 2013 to restrict the way in which a deduction for a liability owed by the deceased on death is allowed from the value of an estate.

**Interaction of agricultural relief and business relief**

Where the value of relevant business property is partly attributable to an asset which qualifies for agricultural relief, agricultural relief is given in priority and business relief is given on the value of the remainder (including any value of agricultural land in excess of its agricultural value). This means that in the case of a farm business, the value of land and buildings will be eligible for agricultural relief and the value of the remaining assets, such as the stock and plant and machinery, for business relief – Section 114(1) IHTA 1984.

**Business relief and woodlands**

Business relief is available on the land and other non-timber assets of a forestry business, and on the timber itself where tax is not deferred under Section 125(2) IHTA 1984. The relief is also available on disposals of timber following an election for deferment on the previous owner's death provided that business relief would have been available on that death if the election had not been made.

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