

Furnished holiday property and business relief?

(Lecture P1239 – 28.42 minutes)

The question for determination in the First-Tier Tribunal hearing of *Cox v HMRC* (2020) was whether furnished holiday accommodation known as Crail House, situated in Fife, was eligible for 100% business relief on the death of the owner of four of the five flats into which the property had been divided. The owner was Sheriff Principal Graham Cox QC (C).

C died on 27 December 2014 at the age of 81. Crail House was built in 1871, with a two-storey wing being added in 1937. The property contained five apartments:

- Flat 1 which had been purchased by C in 1989 and which then became his main residence;
- Flat 2 which C purchased in 1996;
- Flat 3 which C purchased in 1991;
- Flat 4 which C purchased as a second home in 1971 where he lived during the summer months until 1989 when, after his acquisition of Flat 1, he started his holiday letting business with Flat 4. Flats 2 and 3 were added to C's rental portfolio following their acquisition in the 1990s;
- Flat 5 was owned by a third party.

On C's death, Flats 2, 3 and 4 were valued at £562,040 and business relief of this amount was claimed by his personal representatives. The IHT saved by this claim – were it to be successful – was £224,816.

The situation of the flats within Crail House is as follows:

- Flat 1 is on the ground floor of the property, together with the basement of the original house;
- Flat 3 is immediately above Flat 1;
- Flats 2 and 4 are in the newer wing, on the ground and upper floors, respectively;
- Flat 2, being the ground floor flat, has its own garden area;
- Each flat has its own front door, but they share a communal main entrance through a glass porch which gives access to the four flats;
- Each flat has its own dedicated parking space within the grounds.

The gardens and grounds of Crail House extend to more than one acre (= 0.405 of a hectare) and are in an elevated position overlooking the harbour in the village of Crail, the Isle of May and the Firth of Forth.

As mentioned above, the furnished holiday letting business was started in 1989. C operated as a sole trader and employed his wife to assist him in the business. She had no stake in the rental properties.

The personal representatives' claim for business relief as part of C's death estate was refused by HMRC on the ground that the business consisted mainly of the making or holding of investments. They cited S105(3) IHTA 1984. Any additional services or facilities provided were insufficient, in HMRC's view, to change the nature of the business. As a result, the personal representatives appealed, and it was one of the deceased's three daughters (Mrs T) who represented the appellants before the First Tier Tribunal. Mrs T is a chartered accountant as well as being one of her late father's personal representatives.

The question of whether furnished holiday accommodation can be relevant business property for IHT purposes has been the subject of litigation in a number of recent cases:

- HMRC v Pawson (2013) where the Upper Tribunal overturned the First-Tier Tribunal's decision in favour of the taxpayer;
- Green v HMRC (2015) where the First Tier Tribunal rejected the taxpayer's contention that the difference in rent between a holiday letting and an assured shorthold tenancy represented the value of the services provided under the holiday letting arrangements;
- Ross v HMRC (2017) which was decided in the same way as the two earlier cases, despite the fact that the lady owner provided an impressive list of services for her holidaymaker tenants; and
- Graham v HMRC (2018) where the First-Tier Tribunal judges held that the provision of many of the facilities for the tenants distinguished it from other more mainstream actively managed holiday letting businesses and found for the Graham family.

To date, the Graham case has been the only one where the taxpayer was successful. HMRC appealed the First Tier Tribunal's verdict, but, in March 2019, they withdrew their appeal just before the planned Upper Tribunal hearing.

It should be emphasised that, when the special furnished holiday accommodation legislation was put in place in FA 1984, it only extended the 'deemed trading' regime for qualifying properties to income tax and capital gains tax.

IHT and its predecessor (CTT) were never included. Initially, that did not seem to be a problem.

If the owner of residential property which satisfied the furnished holiday letting requirements died, the tax authorities did not deny a claim for the IHT relief. It was only after the turn of the century that HMRC started to impose a stricter interpretation, with the Pawson dispute being the first case law victim.

C advertised his holiday letting business in a number of national newspapers and through entries on websites such as 'VisitScotland'. Annual mailshots were sent to guests who subscribed to the mailing list and, in 2008, C launched his own website.

The case report states that the judge saw archived website pages from periods in 2008, 2009 and 2011 which were printed out shortly before the hearing and which 'provide a good description of the business as advertised to the public'.

From Mrs T's evidence, the activities of the letting business were held by the judge to fall into the following three categories:

1. Investment activities that included:
 - the provision of accommodation;
 - the provision of parking spaces;
 - the provision of communal laundry facilities;
 - repairs and maintenance of the buildings, gardens and grounds; and
 - all the administration dealing with bookings and advertisements.
2. Incidental or ancillary activities that included:
 - the provision of electricity and other utilities;
 - the provision of appliances, furniture, kitchen utensils and crockery;
 - the provision of kitchen basics such as tea and coffee;
 - the provision of consumables such as washing up liquid and toilet paper;
 - cleaning the apartments and the laundry of bed linen and towels between lets;
 - welcoming guests on arrival.
3. Non-investment activities that included:
 - the provision of books, DVDs and information leaflets;
 - the use of tennis or badminton racquets; and
 - the use of buckets and spades, crab lines and frisbees.

With regard to this categorisation, the judge said:

‘The ancillary activities were an integral part of the provision of the accommodation and, as such, they are to be considered as part of the business of holding the property as an investment. The non-investment activities were so insignificant in scale as to be negligible.’

And there was no evidence that extra services such as dog sitting, child minding, transport, breakfast and supper were rendered to the guests with any degree of regularity. Indeed, they appeared to be ad hoc in nature.

While not taking issue with Mrs T's ‘credibility’, the judge said that her evidence was ‘strained, anecdotal and, at times, contrived in the way that the generality of a state of affairs was suggested by implication from the particulars’.

The judge went on:

‘(Her) description of staying in one of the apartments to be “the equivalent of having a suite in an exclusive country hotel with a concierge on site” is an overstatement.’

Another key quote is this:

‘I find that the business was run to a high standard for furnished holiday lettings, but there was nothing exceptional about the business to elevate it to the level of the business found in Graham which qualified for business relief. The non-investment activities in Graham were extensive: swimming pool, games room, sauna, fresh produce from the herb garden, greenhouse and fruit trees, three or four barbecues in each holiday season, receipt of grocery deliveries for guests, fresh seafood at cost price, event and party planning (three or four a year) and prize-winning gardens.’

The First Tier Tribunal’s conclusion was therefore that the Crail House letting business fell firmly on the investment side of the line. The business was mainly one of holding an investment. The appeal was dismissed.

Let the last comment be provided by the Editor-in-Chief of ‘Taxation’:

‘Yet again a decision shows that there is no substitute for contemporaneous evidence of how an activity was actually carried out. The taxpayer’s daughter did her best but could only make general assertions that could not be backed up. In these sorts of cases, where a dispute is likely to arise after death, it is essential that the best possible evidence is obtained and retained during the proprietor’s lifetime. Whether this would have made any difference here is not clear, but, in other cases, it could certainly tip the balance in the taxpayer’s favour and prevent a large IHT bill.’

Contributed by Robert Jamieson