
The Personal Tax Planning Review

INVESTMENT BUSINESS RELIEF

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The purpose of this article is to explain how business property relief (BPR) from inheritance tax (IHT) can be obtained for an investment business.

Section 104 of the IHT Act 1984 gives business property relief where the value transferred by a transfer of value is attributable to "relevant business property". This is defined by section 105(1) to include property consisting of a business and shares in a company. After 5th April 1996, 100% BPR will be available for all holdings of unquoted shares. However, section 105(3) provides:

"A business.... or shares in.... a company are not relevant business property if the business or, as the case may be, the business carried on by the company consists wholly or mainly of... making or holding investments."

On the face of it, therefore, BPR is not available for an investment business. More precisely, BPR is not available if the business consists wholly or mainly of making or holding investments. Therefore, BPR is available if the business consists mainly² of carrying on a trade, even if the business also consists of making or holding investments. In fact, however, it is difficult to conceive of a single business which consists both of trading and investing; those activities will usually comprise separate businesses (see on this *River Estates v D-G of Inland Revenue* [1984] STC 60 at 63-4). If, then, an individual or partnership carries on trading and investment activities, BPR will be available for the trade but not for the investment business. The fact that the two businesses are carried on by the same person(s) does not mean that BPR is available for both.

But if a trade and an investment business are carried on by a company or by members of a group of companies, the position is quite different. Take first the case of a single company carrying on the two businesses. As we have seen, BPR is available for shares in a company, unless "the business carried on by the

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² Or equally.

company consists wholly or mainly of..... making or holding investments". The legislation appears to assume that a company carries on only one business, consisting of all its activities. Alternatively, the singular includes the plural, so that in effect BPR is lost if the businesses carried on by the company when taken together consist wholly or mainly of investing. Whichever is the correct interpretation, the result is the same, namely that BPR is available for shares if the company is mainly a trading company even if it also has investments. (The CGT legislation uses the same idea: for example, a company is a "trading company" for retirement relief purposes if its "business consists wholly or mainly of the carrying on of a trade or trades".) The IHT position is the same in a group situation. Take the case of a holding company (H) with a wholly-owned trading subsidiary (T). The shares in H would appear to be disqualified by section 105(3) because H's business consists wholly of holding investments, namely its shares in T. However, section 105(4)(b) provides that subsection (3)

"does not apply to shares in a company if the business of the company consists wholly or mainly in being a holding company of one or more companies whose business does not fall within that subsection."

Thus, the H shares qualify because H's business consists **wholly** in being a holding company of T, whose business is itself outside section 105(3). But the H shares would still qualify even if H also owns shares in an investment company (I), provided that the value of and amount of income from the T shares as compared with the I shares are such that H's business consists **mainly** in being a holding company of T rather than I. Section 111 provides:

"Where a company is a member of a group and the business of any other company which is a member of the group falls within section 105(3) above, then.... the value of the shares in the company shall be taken [for the purposes of BPR] to be what it would be if that other company were not a member of the group."

Thus, section 111 denies BPR for so much of the value of the H shares as derives from the I shares, if I is a member of the group. The presence of section 111 confirms my point that the H shares otherwise qualify in full under section 105 provided only that H's business consists **mainly** in being a holding company of T, even if H also holds the I shares. Section 111 itself is easily side-stepped, by ensuring that I is not a member of H's group. Section 103(2) provides that:

"a company and all its subsidiaries are members of a group, and 'holding company' and 'subsidiary' have the meanings given by section 736 of the Companies Act 1985."

Thus I will not be H's 'subsidiary' for section 111 purposes if H does not have voting control of I. For example, the individual owning the H shares could own

a single share in I which carries 50% of the votes but has virtually no other rights. Then section 111 will not apply to H's holding of I shares.

A simpler way to obtain full relief for the H shares would be to do away with I altogether, the investments being held directly by H or by T. Indeed, it would seem that investments can be held by H **and** by T. Suppose, for example, that the "value" of T's trade is 100; T could have a separate investment business worth up to 99; its business would not thereby fall within section 105(3) because it would consist **mainly** of the trade. Thus, H's shares in T are worth 199. H could itself own other investments worth up to 198; its business would not thereby fall within section 105(3) because it would consist **mainly** of being a holding company of T. The result is that full BPR is available for shares in H worth 397, even though the trade is worth only 100 and the investments are worth 297!

This is surprising, but there is nothing in the IHT legislation which prevents it. In particular, section 112 (exclusion of value of excepted assets) does not do so. An asset is an "excepted asset" in relation to shares in a company if it was neither used wholly or mainly for the purposes of the business concerned throughout the whole or the last two years of the period preceding the transfer of value during which the asset was owned by the company, nor required at the time of the transfer of value for future use for those purposes. The reference to "the business concerned" must be to the businesses of H and T, and the reference to assets which are "used" for the purposes of the business must include investment assets, otherwise shares in a trading subsidiary would always be "excepted assets". The other investments owned by H, and those owned by T, are therefore not "excepted assets" because they are used for the purposes of their respective investment businesses.

BPR is not available unless the shares have been continuously owned for at least two years before the transfer of value. Suppose that the taxpayer is old and sick and will not live that long. It may still be worthwhile continuing a trade and an investment business in a company or a group of companies before his death, so that the inheritance tax payable on death can be paid by instalments, interest free; see section 234(3)(a) and (b) of the 1984 Act.