[2013] UKUT 050 (TCC)

Appeal number: FTC/36/2012

Inheritance tax – business property relief – holiday letting business of a bungalow carried on for profit – whether the business consisted mainly of holding an investment – whether the FTT erred in law in concluding that it did so consist – appeal allowed

UPPER TRIBUNAL (TAX AND CHANCERY CHAMBER)

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Appellants

- and -

(1) FRANCESCA LOUISE THORESBY LOCKYER
(2) CAROLINE VANESSA THORESBY ROBERTSON
(as the Personal Representatives of NICOLETTE VIVIAN PAWSON, Deceased)

Respondents

TRIBUNAL: MR JUSTICE HENDERSON

Sitting in public at the Rolls Building, London EC4A 1NL on 18 December 2012

Dr Christopher McNall, instructed by the General Counsel and Solicitor to HMRC, for the Appellants

Mr Keith Gordon and Miss Ximena Montes Manzano instructed by Pawson & Co for the Respondents

DECISION

Introduction

1. "Fairhaven" is a large bungalow overlooking the sea on the Suffolk coast near Aldeburgh. At the date of her death on 20 June 2006 Mrs Nicolette Vivian Pawson ("Mrs Pawson") owned a 25% beneficial interest in the property. The remaining 75% was owned equally by her three children: Mrs Francesca Lockyer and Mrs Caroline Robertson (who were also her executors), and her son Mr Nicholas Pawson.

2. Mrs Pawson's share in the property formed part of her estate for inheritance tax ("IHT") purposes, and in due course her executors claimed that it qualified for 100% relief as "relevant business property" within the meaning of Chapter 1 of Part V of the Inheritance Tax Act 1984 ("IHTA 1984") as amended (sections 103 to 114). The basis of the claim, briefly stated, was that Fairhaven had been used for the two years preceding Mrs Pawson's death for the purposes of a holiday letting business carried on for gain, with the result that her share in the property consisted of "a business or interest in a business" within section 105(1)(a) of IHTA 1984; and that her share was not disqualified from being relevant business property by section 105(3), which provides so far as material that:

> "A business or interest in a business … are not relevant business property if the business … consists wholly or mainly of … making or holding investments."

3. The claim was debated in correspondence but was ultimately rejected by the Commissioners for Her Majesty's Revenue and Customs ("HMRC"), who issued a notice of determination on 1 October 2008 saying that "none of the value transferred in respect of the deceased's share in "Fairhaven" … was attributable to the value of relevant business property". The executors appealed against the notice, and the determination was also reviewed by a senior officer of HMRC's Trusts and Estates office in Nottingham, Mr Robert Brown, who wrote to Mrs Lockyer on 26 July 2010 explaining why in his view the notice of determination should be upheld. In his letter Mr Brown made it clear that HMRC would wish to argue that there was no qualifying business at all, as well as that the business (assuming there to be one) was mainly a business of holding investments.

4. The executors' appeal was heard by the Tax Chamber of the First-tier Tribunal (Judge Richard Barlow and Ms Susan Stott FCA, "the FTT") sitting in Leeds on 7 and 8 November 2011. The executors had no legal representation, but were represented by their brother, Mr Nicholas Pawson, who is an actuary.

The FTT said of him that he is "clearly a very intelligent person as his presentation of the case demonstrated". HMRC were represented, as they have been on the present appeal to the Upper Tribunal, by Dr Christopher McNall of counsel. By their written decision released on 14 December 2011 ("the Decision"), the FTT allowed the appeal, finding that the exploitation of Fairhaven by the Pawson family in the two years before Mrs Pawson's death had constituted the operation of a business with a view to gain, and that the business was not one which consisted wholly or mainly of the holding of an investment.

5. No challenge is now made by HMRC to the finding of the FTT, after hearing the evidence, that there was a holiday letting business of the property carried on for gain. It is therefore now common ground that Mrs Pawson's share in the property was relevant business property, and entitled to relief accordingly at the rate of 100%, unless it was disqualified by section 105(3) on the ground that the business was "mainly" one of holding the property as an investment. Realistically, HMRC have never contended that the business was "wholly" one of holding an investment.

6. In relation to the "investment" issue, the FTT reviewed the law in paragraphs 16 to 21 of the Decision, citing extensively from what is now the leading English authority on the subject, namely the decision of a two judge Court of Appeal (Hale and Carnwath LJJ, as they then were) in IRC v George [2003] EWCA Civ 1763, [2004] STC 147 ("George"). The FTT also referred (in paragraph 17 of the Decision) to the subsequent judgment of Girvan LJ, giving the leading judgment in the Court of Appeal of Northern Ireland, in McCall v Revenue & Customs Commissioners [2009] NICA 12, [2009] STC 990 ("McCall"), as authority for two propositions. The first proposition, derived from paragraph [11] of Girvan LJ's judgment, was that the statutory test of holding an investment is not a term of art, and (as the FTT put it, echoing the language of Girvan LJ) "it should be given the meaning that would be given by an intelligent businessman and … just because the person holding it has to take active steps that does not prevent it being an investment". The second proposition, derived from paragraph [14] of Girvan LJ's judgment, was that (again in the words of the FTT):

> "where a landowner derives income from land he will be treated as having a business of holding an investment notwithstanding that in order to obtain the income he carries out incidental maintenance and management work, finds tenants and grants leases."

7. I record at this point that no criticism is made by HMRC of the terms in which the FTT directed themselves about the law relating to the investment issue.

8. The FTT then set out their findings of fact in paragraphs 22 to 35 of the Decision, which I will quote in full later in this judgment, and stated their conclusions on the investment issue in paragraphs 44 to 50. The core of their reasoning is contained in paragraphs 45 and 50, as follows:

> "45. On the facts of this case there are clearly significant services provided to the occupiers of the property. Those services are a significant part of the reason why the occupiers are prepared to pay what they do pay for the package of benefits they receive when they book to use the property as a holiday destination. The fact, even if it is a fact, that the appellants can provide those services at a relatively low cost to themselves compared with the amount they can charge for the package appears to us to be irrelevant.
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> …
>
> 50. We have no doubt that an intelligent businessman would not regard the ownership of a holiday letting property as an investment as such and would regard it as involving far too active an operation for it to come under that heading. The need constantly to find new occupants and to provide services unconnected with and over and above those needed for the bare upkeep of the property as a property lead us to conclude that no postulated intelligent businessman would consider such a property as Fairhaven to be correctly characterised as an investment. He would consider it to be a business asset to be exploited as part of the provision of services going well beyond an investment as such."

9. In short, the FTT appear to have taken the view that the services provided by the Pawsons to holidaymakers who rented the property went well beyond those which an intelligent businessman would regard as falling on the investment side of the line. Furthermore, although the FTT do not say this explicitly in paragraph 50, they must in my judgment have considered that the non-investment services were of such a nature and extent that the business was not even "mainly" one of holding Fairhaven as an investment. It is not plausible to suppose that the FTT had lost sight of the alternative nature of the statutory test, given their careful review of the relevant law and their express statement in paragraph 44 that "the question whether the business consisted of one which consisted wholly *or mainly* of the holding of an investment does require to be examined" (my emphasis).

10. HMRC now appeal to the Upper Tribunal, but only with the benefit of the limited permission to appeal granted by Judge Barlow on 13 March 2012. An appeal to the Upper Tribunal lies only on points of law: see section 11(1) and

(2) of the Tribunals, Courts and Enforcement Act 2007. HMRC sought permission to appeal on four grounds, alleging that the FTT had erred in law in that:

> "A. It formulated and applied the wrong test in assessing whether the Property was held wholly or mainly as an investment;
>
> B. It was wrong in its finding and treatment of the facts, and especially in relation to the level of services provided;
>
> C. Its overall analysis of those facts and the law was wrong;
>
> D. It applied the wrong burden."

Judge Barlow granted permission to appeal in respect of ground A, saying that it raised an arguable point of law, but refused permission in respect of grounds B, C and D. In relation to ground B, he said that it "clearly attempts to raise or re-argue questions of fact about which the Tribunal has made its findings and in so far as and if at all the words "and treatment" might be said to raise a point of law that is already encompassed in Ground A". Similarly, he said of ground C that it "also appears to be an attempt [to] raise or re-argue questions of fact or adds nothing to Ground A".

11. I cite these comments made by Judge Barlow when refusing permission to appeal on grounds B and C, because they show, to my mind, that he did not regard the grant of permission under ground A as being necessarily confined to the reasoning contained in paragraph 50 of the Decision, but as also potentially extending to a challenge to the FTT's conclusion on the investment issue in accordance with the well-known principles expounded by the House of Lords in Edwards v Bairstow [1956] AC 14: see in particular the speeches of Viscount Simonds at 29-30 and Lord Radcliffe at 33- 36.

12. On the appeal to this Tribunal the executors have been represented by counsel, Mr Keith Gordon and Miss Ximena Montes Manzano. They submit that HMRC's appeal should be strictly confined to ground A as originally conceived by HMRC, because (a) in their notice of appeal HMRC expressly stated that they did not seek to renew their application for permission to appeal in relation to the other grounds, and (b) the notice of appeal dealt with ground A in terms more or less identical to those set out in the original application for permission. In my judgment, however, that would be to take an unduly narrow view of the scope of the permission granted by Judge Barlow, although I agree with the submission to the extent that I do not consider it open to HMRC to seek to go behind individual findings of fact made by the FTT. HMRC are, however, in my view entitled to argue that, on the basis of the findings of fact

which they made, it was not open to the FTT to reach the conclusion which they did. As Lord Radcliffe said in Edwards v Bairstow at 36:

> "When the case comes before the court it is its duty to examine the determination having regard to its knowledge of the relevant law. If the case contains anything ex facie which is bad law and which bears upon the determination, it is, obviously, erroneous in point of law. But, without any such misconception appearing ex facie, it may be that the facts found are such that no person acting judicially and properly instructed as to the relevant law could have come to the determination under appeal. In those circumstances, too, the court must intervene. It has no option but to assume that there has been some misconception of the law and that this has been responsible for the determination. So there, too, there has been error in point of law. I do not think that it much matters whether this state of affairs is described as one in which there is no evidence to support the determination or as one in which the evidence is inconsistent with and contradictory of the determination, or as one in which the true and only reasonable conclusion contradicts the determination. Rightly understood, each phrase propounds the same test. For my part, I prefer the last of the three, since I think that it is rather misleading to speak of there being no evidence to support the conclusion when in cases such as these many of the facts are likely to be neutral in themselves, and only to take their colour from the combination of circumstances in which they are found to occur."

Statutory provisions

13. The relevant statutory provisions in IHTA 1984 are straightforward, and it is enough to cite the following:

> "103.
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> …
>
> (3) In this Chapter "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.
>
> 104. **The relief**
>
> (1) Where the whole or part of the value transferred by a transfer of value is attributable to the value of any relevant

business property, the whole or that part of the value transferred shall be treated as reduced –

(a) in the case of property falling within section 105(1)(a) … below by 100 per cent;

…

but subject to the following provisions of this Chapter.

…

105. **Relevant business property**

(1) Subject to the following provisions of this section … in this Chapter "relevant business property" means, in relation to any transfer of value, -

(a) property consisting of a business or interest in a business;

…

(3) A business or interest in a business … are not relevant business property if the business … consists wholly or mainly of one or more of the following, that is to say … making or holding investments.

…

106. **Minimum period of ownership**

(1) Property is not relevant business property in relation to a transfer of value unless it was owned by the transferor throughout the two years immediately preceding the transfer."

The facts

14. The FTT heard oral evidence from Mrs Lockyer, Mrs Robertson and Mr Pawson, each of whom had produced a written witness statement, and each of whom was cross-examined by Dr McNall on behalf of HMRC. As I have already said, the FTT's findings of fact are contained in paragraphs 22 to 35 of the Decision, which I now reproduce:

> "22. Fairhaven is situated on the Suffolk Heritage Coast near Aldeburgh, Snape and the Suffolk Heaths Area of Outstanding Natural Beauty. It is therefore in a holiday area. The property, which is a large bungalow, overlooks the sea and has direct access onto the beach. The business contended for by the

appellants is that of letting as a holiday cottage. Letting is the normal term used in such cases though the visitors have contractual licences to occupy rather than leases. Typically the lettings are for two weeks at most and many are for less than a week for example long weekends. The bungalow can accommodate up to eleven people. It is set in its own grounds of about .4 of an acre.

23. The property has been owned by members of the Pawson family for some time including Mrs Pawson's husband who died in 2002. Mrs Pawson died on 20 June 2006 at the age of 81 and she had been in ill health for about 18 months before her death, suffering from cancer.

24. The income from the property in the last three financial years before Mrs Pawson's death had been 2003/04 £4,342.99, 2004/05 £6,072.51 and 2005/06 £8,120.00. That income generated profits of £680.27 in the year 2003/04, £802.32 in 2004/05 and a loss of £2,071.61 in 2005/06. The income in 2006/07, during which year Mrs Pawson died was £16,589.67 with a profit of £4,449.66.

25. In each of those years family members had occupied the property for three weeks during the holiday season. In their Statement of Case [HMRC] alleged that without the family's payments for those three weeks there would have been a loss in each of the three years before Mrs Pawson's death but that was based on an assumption that the family members who occupied the property would pay the same amount as a holidaymaker would have paid. That was not the case as stated in evidence by Mrs Lockyer, Mrs Robertson and Mr Pawson which evidence was not challenged on this point. The family members who occupied the property were Mrs Pawson's two daughters and they paid amounts which they had calculated, or which had been calculated for them, from HMRC's literature for payments for private use by way of adjustments in accordance with the Notes on Land and Property. It was not contended that they had calculated that amount incorrectly.

26. The evidence of the witnesses, which we accept was truthful and accurate in this respect, was that the loss in 2005/06 was caused by a large expenditure on redecorating and improving the property. We note that in that year the income was higher than in the two previous years in which profits had been made and so we are satisfied and find that had it not been for the expenditure on redecorating and improvement a profit would have been achieved in 2005/06. The evidence was that the extra expenditure was decided upon to improve the

attractiveness of the property and therefore to increase the income.

27. A good deal of oral evidence was given about the operation of the property as a holiday home and it is the case that Mrs Lockyer and Mrs Robertson had an imperfect recollection of when events occurred which we find unsurprising after the lapse of time. Subject to that, we found them to be accurate and truthful witnesses as was Mr Pawson. Some of the items of expenditure were not individually shown in the accounts but we are satisfied that the figures for profits and the loss are accurately reflected in the totals.

28. Mrs Robertson's evidence was that over the years the expectations of holidaymakers have increased so that, for example, it is expected that clean bedclothes will be provided and that they will not need to bring their own. Clean bedclothes are now arranged through a laundry service and by the person who is employed as the cleaner and caretaker. However, it turned out when the documents were examined again that the laundry service only started after Mrs Pawson died.

29. Television and telephone have been provided at the property for a number of years as the accounts confirm from at least 2003/04. Until June 2005 Mrs Pawson had done most of the running of the holiday letting and things like advertising had not kept up with modern developments such as advertising on the internet. At about that time Mrs Robertson became more involved and the family had discussed how things could be improved and that led to the redecorating.

30. The cleaner cleans the property between each letting and the garden is attended to and that has been the case for all the relevant times for this appeal.

31. Mrs Robertson said that some repair or replenishment of supplies such as cleaning materials is needed after about one in three lettings and the cleaner/caretaker inspects the property regularly.

32. The property is fully furnished, heated by night storage heaters, hot water is turned on before visitors arrive, the kitchen is fully equipped and these services were provided at all material times.

33. There was some doubt raised by the respondents as to whether the insurance on the property covered letting but we

> are satisfied that it did, at least for some time before Mrs Pawson's death because the policy is called a "household – commercial" policy.
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> 34. It was put to Mr Pawson that Mrs Pawson had only allowed people she knew to rent the cottage and he denied that. We believed him.
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> 35. Mr Pawson produced evidence from an estate agent giving it as her opinion that the property could be let at about £1,000 per month on a long let. He contrasted that with the amount potentially available as a holiday let and indeed with the amount achieved in the year 2006/07. He argued that the difference reflected the value of the services provided with the right of occupation."

15. The next section of the Decision, running from paragraphs 36 to 43, sets out the FTT's findings on the question whether the exploitation of Fairhaven amounted to the running of a business for gain. As I have explained, that question is no longer in issue; but I need to set out the FTT's findings on it, because they form part of the overall picture in the light of which their conclusion on the investment issue has to be considered. The paragraphs read as follows:

> "36. We find that the exploitation of Fairhaven has amounted to the operation of a business during the years we have examined and therefore for more than two years before Mrs Pawson's death. We have taken into account all the evidence given by the witnesses and we have had regard to the documents in making that finding.
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> 37. The operation of the property as a holiday cottage for letting to holidaymakers was a serious undertaking earnestly pursued. Mrs Robertson explained to us the inconvenience she had suffered as a result of needing to travel to the cottage from time to time when an emergency occurred and the dealings she had to have with various people and we also regard the efforts to advertise for lettings [as] important in this respect.
>
> 38. Clearly there is and has been reasonable continuity in the operation. There has been no year in recent years when it was not used for letting and although inevitably the main period of occupation is during the summer months that is only to be expected given the location.
>
> 39. The annual outputs are certainly not de minimis and are an activity having a measure of substance.

40. Some criticisms of the effectiveness of the operation are no doubt possible, albeit understandable given Mrs Pawson's age at the time she was running the operation, but the basic principles on which the activity is run are regular and sound. The property is not being allowed to go to ruin, there are no debts and the owners are intending to achieve what they can by advertising and by keeping the property clean and up to a reasonable standard. Clearly the use of the property by family members for three weeks a year reduces the level of activity and the profit but in our view that is not enough to prevent the property being run on sound principles. In this context we would ask whether a property in a prime location, say in Central London, lettable at a very large fee as holiday accommodation would cease to be run as a business and would, for example, escape VAT registration accordingly; just because the owner occupied it occasionally.

41. The activity is clearly intended to amount to making supplies to consumers. That is all it does except for the three weeks a year use by family members.

42. The supplies are clearly of a type that are commonly made by those seeking to profit. In fact the operation had made a profit in two of the three years before Mrs Pawson's death and was apparently running profitably in the part-year in which she died.

43. The business was being conducted with a view to gain and we hold that that satisfies the "for gain" requirement in section 103(3) of the Act. In the year when the loss was made it was only made because the owners wanted to ensure the continued profitability of the business."

The law

16. As the author of McCutcheon on Inheritance Tax, 5th edition, observes at paragraph 26-34, the "investment business" exception in section 105(3) of IHTA 1984 involves an all or nothing test: either the property in question is relevant business property, and qualifies for relief in full, or it is not. It is therefore "not surprising that the question of whether a business is wholly or mainly an investment business has led to more case law than any other single IHT issue": *ibid*. paragraph 26-35. Since, however, the scope and nature of the exception has now been considered at Court of Appeal level both in England and Wales and in Northern Ireland (in the cases of George and McCall, referred to above), it is no longer necessary to make extensive reference to the earlier case law. Many of the cases, including George itself,

involved caravan parks, but (as McCutcheon notes at paragraph 26-36) "with significantly varying fact patterns".

17. In Martin v IRC [1995] STC (SCD) 5 ("Martin") the Special Commissioner, Stephen Oliver QC, had to consider whether an actively managed business of owning and letting industrial units on three-year leases at fixed rents fell within the investment business exception in section 105(3). He held that it did. For present purposes, the decision is significant for two reasons. First, the Special Commissioner rejected the submission that the exception should be confined to passive investment, and that it did not apply to a business which was actively managed on sound business principles. As he said in paragraph 20 of the decision:

> "I cannot accept the distinction drawn by Mr Prosser between the active and the passive property investment business. There is no necessary implication in the words of s105(3) that the expression "business of holding investments" is to be confined to the passive investment of property such as long leases managed by managing agents. To imply that is to narrow the scope of the words of exclusion to a point that is not in line with their ordinary meaning."

18. Secondly, the Special Commissioner adopted a three-fold classification of the deceased's activities which is echoed in several of the later cases: see paragraph 22 of the decision. The first category comprised those activities which were directed at "making" the investments, such as the finding of tenants, the negotiations over rent, the grant of leases and the taking of decisions such as whether to accept a surrender or allow an assignment. The second category comprised "compliance activities" which the property owner had to carry out as landlord in accordance with the terms of the leases. The third category covered "management activities", such as organising repairs and maintenance of the exterior of the buildings and the common paths, ensuring compliance by tenants with the terms of their leases, and dealing with tenants' complaints. The Special Commissioner said of the activities in this third category:

> "The purpose of these was to keep the property tidy, secure and in good repair and generally to keep up the standards of the whole investment property. But they were in no way productive of any income other than rent, nor were they designed to produce any separate income. This third category of activities covers, in my view, activities that were incidents of the business of holding investments."

19. The next case which I would mention is the decision of Lawrence Collins J, as he then was, in Weston v IRC [2000] STC 1064 ("Weston"). This was the

only case before George to reach the High Court. It was one of the caravan park cases, involving a mixed business carried on by a company which included the purchase and sale of caravans as well as the grant of the right to pitch caravans on the residential caravan park run by the company in return for "pitch fees", the maintenance and administration of the park, and the supply of electricity and bottled gas used by the residents at the park. The taxpayer accepted that the letting of pitches was a business consisting of holding investments, but argued that the principal business of the company was caravan sales to which the receipt of pitch fees was ancillary. This contention was rejected by the Special Commissioner, and Lawrence Collins J held on appeal that his approach and conclusion could not be faulted on Edwards v Bairstow grounds. For present purposes, the interest of the case lies in the review of the relevant legal principles by the judge in paragraphs 11 to 24 of the judgment.

20. In the first place, the judge held (in paragraph 12) that:

> "whether a property right is to be regarded as an "investment" is to be considered in its context and to be given the same meaning as a businessman would give it."

21. The judge derived this proposition from two decisions (of the Court of Appeal and House of Lords respectively) concerning the question whether patent royalties were "income received from investments", as the taxpayers contended, or profits of their trade or business, as the Revenue contended, and therefore liable to excess profits tax under the relevant war time legislation. In the first of those cases, IRC v Desoutter Bros Ltd (1945) 29 TC 155, Lord Greene MR had said that the word "investment" was not a term of art but had to be interpreted in a popular way. In the second case, Tootal Broadhurst Lee Co Ltd v IRC (1946) 29 TC 352, the House of Lords approved the decision in Desoutter. As Lawrence Collins J explained:

> "16. … Lord Simonds ((1946) 29 TC 352 at 371) emphasised that the meaning depended on the context, and applied the test for the purposes of the distinction between income from investments and profits of a trade or business of whether the asset had been acquired and was held for the purpose of earning profits, in which case it was not an investment. Lord Normand said (at 373):
>
> > "The meaning of investment is not its meaning in the vernacular of the man in the street but in the vernacular of the business man. It is a form of income-yielding property which the business man looking at the total assets of the company would single out as an investment."

> 17. Lord Morton of Henryton (at 375) spoke of the standpoint of the intelligent man of business and Lord MacDermott (at 376) also spoke of the viewpoint of the business man.
>
> 18. Despite the references to passivity by Lord Greene MR (see (1945) 29 TC 155 at 162) it is clear that a property may be held as an investment even if the person who holds the investment has to take active steps in connection with it, eg a landlord who has to keep property in repair. In *Cook (Inspector of Taxes) v Medway Housing Society Ltd* [1997] STC 90 … Lightman J said (at 98) that the term "investment" means "the laying out of monies in anticipation of a profitable capital or income return".
>
> 19. Thus land is generally held as an investment where gain is derived from payment to the owner for use of the property, and so a landlord will normally hold his property as an investment, even if the landlord has to engage in activities of maintenance and management which are required by the lease or are incidental to the letting."

22. Secondly, Lawrence Collins J held (in paragraph 20) that the question:

> "whether the business consists wholly or mainly of making or holding investments is a question of fact, and it is necessary to have regard to the quality, purpose and nature of the taxpayer and its activities."

23. I now come to the decision of the Court of Appeal in George. This was another caravan site case, where the business carried on by the relevant company was admittedly of a "hybrid" nature. The business included some activities (holding land for the purpose of receiving licence fees for stationing mobile homes and for caravan storage) which were agreed to constitute "holding investments"; but there were also other activities carried on for profit, such as the sale of caravans, and running a club for residents and non-residents, which clearly fell on the other side of the line. Having considered all the evidence, and looked at the business of the company in the round, the Special Commissioner (Dr John Avery Jones CBE) had concluded that the business did not consist "wholly or mainly of … making or holding investments". This conclusion was overturned on appeal by Laddie J, but the Court of Appeal restored the decision of the Special Commissioner.

24. The leading judgment was delivered by Carnwath LJ, who commented at paragraph [3] that the variety of conclusions reached in the earlier cases was:

> "… perhaps not surprising. One consequence of the relative imprecision of the statutory test is that the right to business

> property relief may depend on fine distinctions between businesses, which, to their owners, and for most practical and economic purposes, are virtually identical."

25. After setting out the relevant statutory provisions, Carnwath LJ said at paragraph [10] that the area of dispute was very narrow, given that the business admittedly included both investment and non-investment activities. He continued:

> "11. The question, therefore, is whether the business was "mainly" that of holding investments. For this purpose, the principal areas of debate have been: first, the correct allocation between "investment" and "non-investment" of the various activities involved in operating the site, including, in particular, the services provided for the residential part; and, secondly, in the light of that allocation, whether the "investment" element of the business was dominant."

26. Having thus stated the issue, Carnwath LJ then proceeded to review the authorities. He began his review as follows:

> "12. Although it is common ground that the exploitation of a proprietary interest in land for profit is in principle an "investment" activity, I would agree respectfully with the Commissioner's comment as to the wide "spectrum" involved; and with his view that cases relating to different taxes and different subject matter are unlikely to be helpful."

Carnwath LJ then quoted what Dr Avery Jones had said in his decision (reported as Stedman's Executors v IRC [2002] STC (SCD) 358) at paragraph 12:

> "It is not in dispute that the company carries on a business; the question is whether it is a business consisting mainly of holding or making investments. There is a spectrum at one end of which is the exploitation of land by granting a tenancy coupled with sufficient activity to make it a business, which may be activity in granting tenancies rather than activity in relation to the tenancy once granted. At the other end of the spectrum, while land is still being exploited, the element of services means that there is a trade, such as running a hotel, or a shop from premises owned by the trader. Normally for income tax, leaving aside services for which a separate charge is made, the income must be either income from land or trading profits. Here the concept of trade is irrelevant and one is required to determine whether the business of the company consists mainly

> of making or holding investments or some other business. Although I was referred to a number of income tax cases, I do not find these helpful on this issue."

27. In paragraph [13], Carnwath LJ emphasised the need to look at the business "in the round". He then considered Weston, describing the basis of Lawrence Collins J's decision (that the issue was one of fact for the Commissioner) as "unremarkable". He pointed out that the status of the relevant services in that case had not been raised before the Commissioner, and was not permitted to be raised in the High Court. In relation to paragraph 19 of the judgment of Lawrence Collins J, quoted in paragraph 21 above, he observed at [15]:

> "That is entirely fair as a statement related to the facts and arguments in that case. However, I will need to consider in more detail the question as to what is meant by "management", and the relevance to that question of the requirements of the lease."

Commenting on the decision of Lightman J in Cook v Medway Housing Society Ltd, Carnwath LJ said that the holding of investments may be neither "merely incidental", nor "the very business" carried on by the taxpayer, but "simply one of a number of principal components of a composite business".

28. Under the sub-heading "Management and services", Carnwath LJ discussed in some detail the decision of the Special Commissioner in Martin, and in paragraph [18] he endorsed the Special Commissioner's rejection of the submission that the exception in section 105(3) was confined to purely "passive" property investment:

> "Mr Oliver rejected that contention. That conclusion is unimpeachable. On any view, the business was at least "mainly" that of holding property for letting, and thus for investment."

It seems to me to be implicit in this endorsement that, had Mr Oliver found that the deceased's business of owning and letting industrial units was not mainly one of holding property for investment, he would have erred in law.

29. Carnwath LJ then discussed Mr Oliver's tripartite categorisation of the owner's business activities, and Mr Oliver's reliance in making that analysis on certain observations made by Slesser LJ in the Court of Appeal in Salisbury House Estate Ltd v Fry (Inspector of Taxes) [1931] 1 KB 304 at 331-2. He continued:

> "26. As I have said, I have no doubt as to the correctness of the *Martin* decision on its own facts …
>
> 27. However, I would make two comments of relevance to the present case. First, I agree in general terms that property "management" is part of the business of "holding" property as an investment (cf *Webb (Inspector of Taxes) v Conelee Properties Ltd* [1982] STC 913 at 921, 56 TC 149 at 157). In the case of a building held for letting, management no doubt includes the activity of finding tenants and arranging leases or licences, and that of maintaining the property as an investment. But I would not extend that term to additional services or facilities provided to the occupants (such as those referred to by Slesser LJ), whether or not they are included in the lease and covered by the rent. In the case of a building for letting, it is unlikely to be material. They will not be enough to prevent the business remaining "mainly" that of holding the property as an investment.
>
> 28. Where it does matter, in my view, the characterisation of such services depends on the nature and purpose of the activity, not on the terms of the lease (or, where relevant, a site licence). It is true that, in *Fry*, Slesser LJ noted the fact that the particular services mentioned (cleaning, heating and lighting) were optional under the lease, and that a separate charge was made. That was treated as a reason for not regarding them as "mere incidents" of the tenancy. However, the converse does not follow. There is nothing in that judgment to support the view that, merely because services or facilities are required by the lease, and their cost is included in the rent, they lose their character as services, and become part of the "holding" of the investment."

30. This passage in Carnwath LJ's judgment is in my view important for at least three reasons. First, he endorses the general proposition that property management forms part of the business of holding property as an investment, and he includes under that heading maintenance of the property as an investment as well as the activity of finding tenants and arranging leases or licences. Secondly, however, Carnwath LJ draws a distinction between such management activities on the one hand, and the provision of additional services or facilities to the tenants or occupants, whether they are separately charged for or included in the lease and covered by the rent, on the other hand. The characterisation of such services depends on the nature and purpose of the activity, and not on the terms of the lease or site licence. Nevertheless, and this is the third point, where the business is one of letting a building, the provision of additional services or facilities to the occupants is "unlikely to be material" because they will not be enough to prevent the business remaining "mainly" one of holding the property as an investment. The implication is in my judgment clear. In any normal property letting business, the provision of

additional services or facilities of a non-investment nature will either be incidental to the business of holding the property as an investment, or at least will not predominate to such an extent that the business ceases to be mainly one of holding the property as an investment.

31. Nevertheless, I accept that caution is needed before interfering with any decision of the fact-finding tribunal, and the imprecision of the statutory test is such that no test can be applied in a mechanical fashion. This emerges in particular from Carnwath LJ's subsequent discussion of the judgment of Laddie J in the High Court, and of the submissions advanced in the Court of Appeal by Mr McKay for the Revenue. Carnwath LJ stated his conclusions in the following terms:

> "58. For the reasons already given, I am unable to accept Mr McKay's reliance on the terms of the lease or licence as definitive in the case of a caravan park. On the other hand, I think, with respect to the judge, that he placed too much reliance on the particular formulations used in *Cook* and *Weston*, instead of concentrating on the language of the statute. As I have said, the most important point about each of those decisions is that the Court was upholding the decision of the fact-finding tribunal.
>
> 59. In the present case the judge was being asked by the Revenue to find some error of law in the approach of the Commissioner. The error identified by Mr McKay, as accepted by the judge … was, in Mr McKay's words, that instead of following the sequence based on *Weston*, he "jumped straight to *Cook v Medway*". As I understand it, the judge intended that as another way of putting his point that the first step was to decide what activities were in "the investment bag"; or, in Mr McKay's terms "recognising that the land was held as an investment", and then assessing which of the other activities were "incidental to the investment business".
>
> 60. For the reasons I have given, I think that was the wrong approach. The section does not require the opening of an investment "bag" into which are placed all the activities linked to the caravan park, including even the supply of water, electricity, and gas, simply on the basis that they are "ancillary" to that investment business. Nor is it necessary to determine whether or not investment is "the very business" of the company. The statutory language does not require such a definitive categorisation. In the present context, it gives insufficient weight to the hybrid nature of a caravan site business, as I have explained. The holding of property as investment was only one component of the business, and on the

> findings of the commissioner it was not the main component. In my view, the commissioner's overall approach was correct in law, and he reached a view which was open to him on the facts.
>
> 61. I would add that I am happy to be able to arrive at this conclusion. I find it difficult to see any reason why an active family business of this kind should be excluded from business property relief, merely because a necessary component of its profit-making activity is the use of land."

32. In a short concurring judgment, Hale LJ added this:

> "63. I agree. This was essentially a question of fact for the Special Commissioner who asked himself the questions which the statute requires him to ask. It is usually unfortunate to try to gloss clear statutory language with additional judicial tests. The Special Commissioners are the experts here, and any appeal to the High Court is on a point of law only. The court should resist any attempt to dress up a question of fact as if it involved a question of law."

33. I come finally to the decision of the Court of Appeal in Northern Ireland in McCall. The case concerned agricultural land which was let under seasonal grazing arrangements between April and November each year. The land was owned by the deceased, whose son-in-law spent about 100 hours per year looking after the fields. His work involved such matters as inspection of the perimeter fencing and walls, gates and water supply; the removal of rubbish, unblocking of drains, carrying out emergency repairs to vandalised or damaged fencing and tending the drinking troughs; and informing the graziers of any problems he observed in their animals. The land had been zoned for development use before the deceased's death, with the consequence that its market value for IHT purposes (£5.8 million) greatly exceeded its purely agricultural value of £165,000. It was common ground that the agricultural value of the land qualified for agricultural relief from IHT, but the remainder of the value would have fallen into charge unless it qualified for business relief.

34. The Special Commissioner (Mr Charles Hellier) heard a good deal of evidence and his key conclusions are helpfully summarised in paragraph [4] of the judgment of Girvan LJ. He concluded that the activities of the deceased's son-in-law on the land, coupled with the annual letting of the land to graziers, was just enough to constitute a business, but he also concluded that the business was one which consisted wholly or mainly of the holding of investments. The claim to business relief accordingly failed. The Court of Appeal (Girvan and Coghlin LJJ and Deeny J) dismissed the personal representatives' appeal, holding that the Special Commissioner had been fully entitled to come to the

conclusion which he did on the investment issue. There was no appeal against his conclusions that the activities in question had constituted a business, and that the deceased fell to be treated as the owner of that business.

35. In paragraph [11] Girvan LJ said that the Commissioner had:

> "concluded correctly that the test to be applied is that of an intelligent businessman who would be concerned with the use to which the asset was being put and the way it was being turned to account."

Girvan LJ then considered the assistance to be derived from Weston, Tootal, Desoutter and George, before stating at paragraph [14]:

> "What is clear from the authorities is that a landowner who derives income from land or a building will be treated as having a business of holding an investment notwithstanding that in order to obtain the income he carries out incidental maintenance and management work, finds tenants and grants leases …"

The authorities which he cited for this proposition included Martin and Weston at paragraph 19.

36. Like Carnwath LJ in George, Girvan LJ found assistance in the concept of a spectrum, and after quoting from paragraph [12] of George Girvan LJ continued at [18]:

> "This helpful reference to a spectrum shows that it is necessary to decide where a particular business falls within the spectrum. This necessarily involves a question of fact and degree. It requires a judgment to be made in the light of established facts. Having analysed the evidence and made his findings the Special Commissioner concluded that the arrangement fell towards the lease end of the spectrum not at the hotel or shop premises end. He was fully entitled to do so on the evidence.
>
> 19. While the appellants valiantly attempted to argue that the deceased's business was akin to that of a grass disposal business, a hotel, a dog kennelling business or a pick-your-own-fruit business such analogies were not apt. As found by the Special Commissioner on the evidence the land was not cultivated. The grass was not sown or grown in the manner of a crop. The activities of the deceased were considered by the Special Commissioner to be in the nature of maintenance work

> necessary to enable the deceased to successfully let the grazing in the growing season. This was a view that he was entitled to form in the light of the evidence. Before letting the lands the deceased did the necessary maintenance work of preparing and maintaining fences, water courses and so forth. She could alternatively have employed a third party to do so (thereby effectively reducing her net return from the land) or indeed she could have attempted to let the grazing of the lands as they stood (in which case the grazier would be likely to have demanded a reduction in rent to take account of work that he would have to carry out to secure the grazing area). Whichever approach was adopted affected the return from the land. But the work done was aimed at maximising the return from the grazing which represented income of the deceased by way of a return from the land … The deceased's business consisted of earning a return from grassland whose real and effective value lay in its grazing potential. The activities which were regarded as just sufficient to lead to the lettings of the land being regarded as a business were all related to enabling that potential value to be released."

The parties' submissions

37. Against this background, the submissions of the parties were briefly as follows.

38. Counsel for HMRC submitted that the appropriate starting point is that the business of owning land with a view to obtaining income from it is in itself an investment activity, and thus caught by section 105(3). He relied on the three-fold categorisation of property-related activities in Martin, submitting that the first two categories are referable to the business of investment, while the provision of additional services or facilities to the occupants (such as heating, lighting or cleaning) are unlikely to be material, and thus unlikely to take the business outside the statutory exception. Save in exceptional cases, at one end of the George spectrum, such services should be regarded as inherent in, or incidental to, property ownership, and they would only take a business out of the "investment" category if the business, in reality, and looked at in the round, was not a letting business at all, but rather consisted of the provision of services coupled with incidental occupation of the relevant land.

39. Applying these principles, counsel submitted that the essence of Mrs Pawson's business at Fairhaven was one of the provision of self-catering accommodation in an attractive seaside bungalow with some ancillary services, and not *vice versa*. As such, her business was firmly at the Martin or McCall end of the spectrum, especially bearing in mind that her own family

occupied the property for at least three weeks of the high season. The very nature of a furnished letting business is likely to include the provision of heating and lighting and some services; and the services provided in the present case were incapable, as a matter of law, of carrying the business outside the "investment" category. In reaching the contrary conclusion the FTT had therefore erred in law, and the test in Edwards v Bairstow for interfering with their conclusion was satisfied.

40. On behalf of the respondents, Mr Gordon submitted that the FTT had been entitled to conclude that, looked at in the round, the business carried on by the Pawsons at Fairhaven was not mainly one of holding an investment. He emphasised that the question was one of fact for the FTT, to be determined in the light of all the evidence before them. They had approached their task in a clear and systematic manner, and no criticism could be made of their exposition of the law. The test which they applied in paragraph 50, of how an intelligent businessman would regard the arrangements, was mandated by the authorities; and on any view a substantial part of the business consisted of the provision of services to customers which were not of an investment nature. The facts of the case were therefore more akin to those of George than those of McCall, and they occupied a position on the spectrum where the conclusion reached by the FTT was a tenable one which could not be said to be erroneous in point of law. The fact that the relevant services were paid for as part of the rent charged to holidaymakers was immaterial: see George at paragraphs [28] to [29].

41. In relation to the "mainly" criterion, Mr Gordon submitted that the FTT must have had it well in mind in paragraph 50 of the decision, although they did not expressly refer to it. As I have already indicated, I agree with that submission. Mr Gordon accepted that the test of holding an asset mainly as an investment will normally be satisfied if over 50% of the relevant factors fall on the investment side of the line, but he submitted that the nature of the test is a qualitative and not a quantitative one. He further submitted that the FTT's reference in paragraph 50 to the provision of "services unconnected with and over and above those needed for the bare upkeep of the property as a property" was not intended to introduce a new test, but simply to provide a convenient paraphrase or description of the types of activity which fell on the investment side of the line. Similarly, when the FTT referred (in the same paragraph) to "the provision of services going well beyond an investment as such", they were not intending to narrow the concept of an investment in any way that went beyond the guidance in the authorities.

Discussion

42. In considering these rival submissions, I take as my starting point the proposition that the owning and holding of land in order to obtain an income

from it is generally to be characterised as an investment activity. Further, it is clear from the authorities that such an investment may be actively managed without losing its essential character as an investment: see Martin, Weston at paragraphs 18 to 19 and George at paragraphs [18] and [27]. Accordingly, the fact that the Pawsons carried on an active business of letting Fairhaven to holidaymakers does not detract from the point that, to this extent at least, the business was basically one of an investment nature.

43. The business activities carried on in relation to Fairhaven which would naturally fall on the investment side of the line included the taking of active steps to find occupants, making the necessary arrangements with them, collecting payment of the rent, the incurring of expenditure on repairs, redecoration and improvement of the property, maintenance of the garden and grounds in a tidy condition, and keeping the property insured. All of these activities were directed at maintaining or enhancing the capital value of the property, and obtaining a regular income from its letting. Furthermore, in relation to the substantial expenditure on redecoration and improvement which took place in 2005/06, shortly before Mrs Pawson's death, the FTT expressly found (in paragraph 26 of the Decision) that "the extra expenditure was decided upon to improve the attractiveness of the property and therefore to increase the income". In my view this amounts to a clear finding that the purpose of the expenditure was to enhance the value of Fairhaven as an income-producing asset.

44. As part of the holiday letting business, certain services were provided to occupants. These are dealt with, quite briefly, in paragraphs 28 to 32 of the Decision. They consisted of (a) provision of the services of a cleaner/caretaker, who cleaned the property between each letting and carried out regular inspections of the property; (b) the provision of space heating and hot water; (c) the provision of television and telephone at the property from at least 2003/04; (d) being on call to deal with queries and emergencies; and (e) more minor matters such as the replenishment of cleaning materials as and when necessary, and the provision of an up-to-date welcome pack. Laundry services were also provided, but only after Mrs Pawson's death: see paragraph 28 of the Decision. As Mrs Robertson put it in paragraph 7 of her witness statement:

> "The fact that the place was clean, able to be at the right temperature, well equipped and that everything worked (and had clear user instructions) was key. In addition, the beds had to be made with clean sheets, the garden tidy (and equipped), there needed to be a good welcome/information pack and a number to ring and a local person to come round if there were queries. The holiday had to be hassle free."

45. It is clear from George that the provision of these additional services and facilities is not to be regarded as part of the maintenance of the property as an investment, and that their characterisation as services is unaffected by the fact that no separate charge was made for them. The critical question, however, is whether these services were of such a nature and extent that they prevented the business from being mainly one of holding Fairhaven as an investment. Carnwath LJ made it clear in paragraph [27] of his judgment in George that, in the case of a business of letting a building, the provision of such services is "unlikely to be material" because they will not be enough to prevent the business remaining mainly one of property investment. The implication is that in any normal case an actively managed property letting business will fall within the exception in section 105(3) because the "mainly" condition will still be satisfied.

46. With every respect to the FTT, it appears to me that, on the basis of their findings of primary fact, the only conclusion which it was reasonably open to them to draw was that the business carried on at Fairhaven did indeed remain one which was mainly that of holding the property as an investment. The services provided were all of a relatively standard nature, and they were all aimed at maximising the income which the family could obtain from the short term holiday letting of the property. Looking at the business in the round, there was in my view nothing to distinguish it from any other actively managed furnished letting business of a holiday property, and certainly no basis for concluding that the services comprised in the total package preponderated to such an extent that the business ceased to be one which was mainly of an investment nature. I am unable to accept Mr Gordon's submission that a holiday letting business is inherently of such a nature that it falls outside the scope of a "normal" property letting business, of the kind envisaged by Carnwath LJ in George at paragraph [27]. On the contrary, I consider such a business to be a typical example of a property letting business, albeit one of a fairly specialist nature.

47. The FTT reached their conclusion by seeking to apply the test of how an intelligent businessman would regard the business. They do not explain, however, how an intelligent businessman, who must be assumed to be fully instructed in the relevant law, could conclude that the services elements outweighed the investment elements to such an extent that the "mainly" test was no longer satisfied. Further, it is not clear to me what they meant by the concept of "an investment as such" in paragraph 50 of the Decision, and the comments which they make in relation to it strongly suggest to me that they must have misunderstood in some important respects the guidance to be found in the authorities.

48. Thus, the first reason which the FTT give for saying that an intelligent businessman would not regard the ownership of a holiday letting property "as

an investment as such" is that he "would regard it as involving far too active an operation for it to come under that heading". But it is well established that an investment business may be actively managed. The relevant test is not the degree or level of activity, but rather the nature of the activities which are carried out.

49. The FTT then referred to two matters which in their view would have prevented any intelligent businessman from characterising the business as one of holding an investment, namely "[t]he need constantly to find new occupants and to provide services unconnected with and over and above those needed for the bare upkeep of the property as a property". In my judgment, however, this is open to two serious objections. First, the need to find new occupants is on any view an activity which falls on the investment side of the line. Secondly, "bare upkeep" is far too narrow a criterion to identify the property management activities which are properly to be regarded as forming part of the business of holding property as an investment. These were in my view significant errors of law, and they must have contributed to the FTT's conclusion.

50. In all the circumstances, I consider that if the FTT had not misdirected themselves the only conclusion reasonably open to them on the facts was that Fairhaven was held mainly as an investment. It follows that HMRC's appeal must be allowed, and the original refusal of business relief for Mrs Pawson's 25% share in Fairhaven must be reinstated. Despite Mr Gordon's clear and skilful submissions, this is in my judgment one of those cases where "the true and only reasonable conclusion contradicts the determination" made by the FTT, that being the preferred formulation of Lord Radcliffe's in Edwards v Bairstow [1956] AC 14, at 36 (quoted in paragraph 12 above).

51. I have well in mind the cautionary admonitions of Hale LJ in George, but in the present case I would respectfully counter them with the concluding observations of Lord Radcliffe in Edwards v Bairstow at 38-39:

> "The court is not a second opinion, where there is reasonable ground for the first. But there is no reason to make a mystery about the subjects that commissioners [*now the FTT*] deal with or to invite the courts to impose any exceptional restraints upon themselves because they are dealing with cases that arise out of facts found by commissioners. Their duty is no more than to examine those facts with a decent respect for the tribunal appealed from and if they think that the only reasonable conclusion on the facts found is inconsistent with the determination come to, to say so without more ado."

TRIBUNAL JUDGE: MR JUSTICE HENDERSON
RELEASE DATE: 28 January 2012