

INHERITANCE TAX – Deceased Lloyds name – Provision by the deceased of security to Lloyds in the shape of a bank guarantee – Bank guarantee supported by the deceased by a mortgage of commercial property – Whether such commercial property charged to the bank formed "relevant business property" – Sections 104, 105, 110 and 112 Inheritance Tax Act 1984

THE SPECIAL COMMISSIONERS

MICHAEL ANTHONY BASIL MALLENDER

RICHARD BUTLER-ADAMS

JOSHUA CHRISTOPHER ROWLEY

(As Executors of the Will of

CAPTAIN PATRICK JOHN BOTELER DRURY-LOWE DECD)  
Appellants

- and -

THE COMMISSIONERS OF INLAND REVENUE Respondents

Special Commissioner: MR T H K EVERETT

Sitting in London on 4 October 2000

Mrs Shân Warnock-Smith of Counsel, instructed by Messrs Taylor Simpson & Mosley, Solicitors, for the Appellants

Mr Peter Twiddy, Assistant Director, Capital Taxes Office, for the Respondents

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DECISION

Mr Michael Anthony Basil Mallender, Mr Richard Butler-Adams and Mr Joshua Christopher Rowley (hereinafter called the "Executors") each appeal against a Notice of Determination dated 15 March 2000 served upon each one of them by the Commissioners of Inland Revenue. The three notices are in identical terms and state as follows:

"The Commissioners of Inland Revenue have determined –  
  
in relation to

(a) the deemed disposal for the purposes of inheritance tax on the death on 11 July 1993 of Captain Patrick John Boteler Drury-Lowe ("the Deceased");

(b) the Deceased's business as a Lloyds Underwriter ("the Business").

That, for the purposes of section 110 Inheritance Tax Act 1984, the net value of the assets used in the Business did not include the value of any part of the interest in land known as Denby Disposal Point, Derby Road, Denby, Derbyshire."

The Crown accepts that the Deceased's activities as a Lloyds "name" constituted a business for inheritance tax purposes but submits that the security which he gave to his bank in the shape of a mortgage over commercial property did not constitute "relevant business property" entitled to relief under the provisions of section 104 Inheritance Tax Act 1984. The only question before me in these appeals is whether the commercial property mortgaged by the Deceased to his bank constituted "relevant business property" for the purposes of the Inheritance Tax Act.

The evidence before me consisted of a brief statement of agreed facts supplemented by further facts agreed between the parties at the hearing.

In addition certain agreed documents were to be found in a bundle put in evidence at the hearing, supplemented by a copy of a counterpart lease dated 20 July 1990 and photographs of the relevant commercial property mortgaged by the Deceased to his bank.

The facts

From the evidence before me I find the following relevant facts:

1. The Deceased died on 11 July 1993, a grant of Probate having been made out of the Birmingham District Probate Registry to the Executors on 16 November 1993.
2. The Deceased had been a Lloyds underwriter for many years with an allocated capacity of £500,000 at the date of his death.
3. The Deceased's underwriting business was supported by a personal reserve of quoted shares worth £78,627.23 at his death and several guarantees provided by National

Westminster Bank Plc in the total sum of £100,000.

4. The guarantees were given by the bank in consideration of the Deceased indemnifying the bank against all liability that might incur, such indemnity being secured by a legal charge over freehold property owned by the Deceased.

5. From and after 18 May 1991 the property so charged as security to the bank was the Denby Disposal Point ("the Denby DP").

6. The Denby DP comprises 20.29 acres of land in Denby, Derbyshire which was the subject of a lease in favour of British Coal for a term of 10 years from 25 March 1990 at a rent of £170,000 per annum. The value of the asset was considered by the Deceased and his advisers to be a depreciating asset: the land was heavily contaminated and British Coal was the only realistic occupier. A failure by British Coal to renew its lease would have had a serious effect on the value of the land. As it was, the estimated value of the land in May 1991 was £1.2 million, but by the date of the Deceased's death its value was nearly £200,000 less at £1,020,000. Its value would reduce further as every quarterly rent payment was made.

7. The Denby DP was charged to the bank in substitution for an earlier property so charged, Little Hay Grange. The bank had always maintained the requirement that the value of the acceptable security must exceed the amount of the guarantee by at least 70%: hence the minimum value of the property to be charged had to be £142,858. The Deceased had only two possible candidates with individual value sufficient for mortgage purposes, one of which had development potential and would not have been available for more than a few years as security. The other was Denby DP which the Deceased was prepared to encumber for these purposes. Under the terms of the mortgage the Deceased:

(a) subjected himself to positive obligations to keep the property in a good state of repair and condition and to insure on terms approved by the bank and

(b) was prohibited from letting the property otherwise than with the consent of the bank.

Although in normal circumstance such obligations would be quite onerous, the obligations of British Coal in its lease mitigated the severity of those obligations to a considerable degree.

8. A statement provided to the Executors by R F Kershaw Ltd, the Deceased's agent at Lloyds, giving details of the investments and cash provided to Lloyds by the Deceased as at 20 July 1993 stated as follows:

"Nominal Deposit

holding

£100,000 National Westminster Bank Plc – bank guarantee

Personal reserve

£6,296 Grand Metropolitan Plc Ord. 25p

£700 Great Universal Stores "A" none V Ord 25p

£14,000 Hanson Trust Plc Ord 25p

£1,494 Vodafone Group Plc Ord 5p

£1,177.62 Treasury 2½% Index-linked stock 2001

Special reserve"

9. The guarantees provided by the bank at the request of the Deceased to Lloyds comprised four in number and were granted over a period of years between 1978 and 1986. They are in broadly similar terms, although the order of the clauses varies slightly between one guarantee and another.

10. The operative part of the guarantee granted on 21 November 1985 by the bank to secure a sum of £60,000 recites that the Deceased was about to enter into Security and Trust Deeds with Lloyds under which he agreed to procure that the bank would execute and maintain a guarantee in favour of Lloyds of the sum of £60,000 and it also recited that the Deceased had requested the bank to give the guarantee and that the bank had agreed to do so. The operative part of the Deed continued as follows:

"Now these presents witness and it is hereby agreed and declared as follows: -

1. The bank with intent to bind its successors and assigns and any company with which it may amalgamate hereby guarantee that at any time after [the Deceased] or [the Deceased's] personal representatives or estate shall be in default under the Trust Deed the bank will on demand in writing being made upon it pay to Lloyds such sum or sums as may from time to time be specified in any such demand not exceeding in the aggregate the said sum of £60,000.

2. Lloyds may without further consent from the bank and without affecting the bank's liability hereunder hold over renew or give up in whole or in part and from time to time any security received from the [Deceased] or from any other person or persons and this guarantee shall not be discharged nor shall the bank's liability under it be affected by anything which would not have discharged or affected

such liability if the bank had been principal debtors to Lloyds instead of guarantors.

3. In any demand proceeding or otherwise under this guarantee the fact of the [Deceased's] default under the Trust Deed shall be conclusively proved by a certificate signed by a duly authorised officer of Lloyds.

4. A demand shall be duly made upon the bank if it is signed by the Manager of the Deposits/Membership Department or one of his duly authorised deputies, addressed to the bank at its registered office and posted by first class mail and the bank shall be taken to have received such demand forty-eight hours after it is posted.

5. This is a continuing Guarantee and it shall remain in force until the fifth anniversary of the date hereof and thereafter unless the Bank shall give not less than four years notice in writing to determine the same expiring on such fifth anniversary or on any date subsequent thereto; such notice to be served on the Manager of the Deposit/Membership Department or one of his duly authorised deputies."

11. The Trust Deeds were not put in evidence.

The contentions of the parties

It was the contention of Mr Peter Twiddy for the Crown, that the relevant business asset was simply the guarantee. For the Executors Mrs Warnock-Smith contended that what had been referred to in correspondence as "the underlying assets", namely the Deceased's commercial property, could not be ignored. She provided a written skeleton argument which will be available to the Court should this appeal proceed further.

Conclusions

Mr Twiddy has referred me to a dictum of Lord Evershed MR in the case of *Imperial Chemical Industries Ltd v Caro* [1961] WLR 529, where he said at page 538:

"I think Mr Magnus is entitled to say in a case of this kind, where prima facie there is a clear tax liability on the subject, that if the subject is going to say: "I claim relief by virtue of certain statutory provisions or their equivalent," it is for the taxpayer to establish that he is entitled to that relief. We were referred, in support of that view, to a passage in the judgment of Cohen LJ sitting in this Court in

Littman v Barron."

Mr Twiddy's contention was that where a taxpayer is claiming a relief provided by a statute, the burden of proof falls upon the taxpayer. Mrs Warnock-Smith did not seek to contend otherwise.

Section 104(1) Inheritance Tax Act 1984 provides, where relevant:

"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;"

Section 105(1)(a) reads as follows:

"... 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".

Section 110 provides:

"For the purposes of this Chapter –

(a) the value of a business or of an interest in a business shall be taken to be its net value;

(b) the net value of a business is the value of the assets used in the business (including goodwill) reduced by the aggregate amount of any liabilities incurred for the purposes of the business;

(c) in ascertaining the net value of an interest in a business, no regard shall be had to assets or liabilities other than those by reference to which the net value of the entire business would fall to be ascertained."

It seems to me that the critical words in the statute for the purposes of these appeals are to be found in Section 110(b) namely "the net value of a business is the value of the assets used in the business." (My emphasis).

Mr Twiddy has highlighted the fact that Lloyds would have been unaware of the identity of the security provided to the bank by the Deceased and would also have been unaware of the change of security which took place in 1991, when Denby DP was substituted for Little Hay Grange. He also relies on the statement provided by R F Kershaw Ltd of investments and cash provided by the Deceased as at 20 July 1993, which refers only to the bank guarantee (and investments) with no mention of "the underlying assets".

However I take judicial notice of the fact that banks do not do anything for nothing and I am confident that Lloyds would have been alive to the fact that the Deceased's bank would have required some quid pro quo as the price for providing the requested guarantee.

To say that Denby DP was not one of the "assets used in the business" of the Deceased is to look at the Deceased's business using blinkers. The Deceased required a bank guarantee; he could only obtain such guarantee by providing security to the bank to a minimum value of £142,858; he in fact provided security to a value in excess of £1m. Had he not provided the bank with the security which it required, a guarantee to Lloyds would not have been forthcoming and the Deceased's business would have been seriously affected.

In my judgment Denby DP constituted one of the assets used in the Deceased's business and accordingly the net value of the assets used in the Deceased's business included the value of the interest in land known as Denby DP.

The appeals succeed and I quash each of the three notices served on the Executors.

T H K EVERETT

SPECIAL COMMISSIONER

Date of Release: 9<sup>th</sup> November 2000

SC 3034/2000