

By 15 September 2024



Abolition of furnished holiday lettings regime

Response from ICAS

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About ICAS

1. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants. We represent over 24,000 members working across the UK and internationally. Our members work in the public and not for profit sectors, business and private practice.
2. The following submission has been prepared by the ICAS Tax Board. The Tax Board, with its five technical Committees, is responsible for putting forward the views of the ICAS tax community; it does this with the active input and support of over 60 committee members.
3. ICAS has a public interest remit, a duty to act not solely for its members but for the wider good. From a public interest perspective, our role is to share insights from ICAS members into the many complex issues and decisions involved in tax and regulatory system design, and to point out operational practicalities.

General comments

4. We welcome the opportunity to comment on the policy paper and draft legislation on the abolition of the furnished holiday lettings rules from April 2025.
5. We have received a significant level of contact from our members since the Spring Budget announcement of the proposed abolition of the furnished holiday lettings rules, raising concerns about the impact of the changes and the absence of any transitional rules. This was particularly the case on the application of the anti-forestalling rule for capital gains tax, which will take effect from 6 March 2024.
6. Our members have shared feedback on practical aspects of the draft legislation and our response summarises the feedback we have received, along with other aspects to be considered. We would be very pleased to provide further details on any point on request.
7. Whilst there is a clear policy intention to remove the tax distinction between the treatment of residential properties used for furnished holiday lettings compared to longer term lettings, from April 2025, there remains an apparent inconsistency between furnished holiday lettings and the treatment of income from hotels and guest houses (which is treated as trading income). Our members have drawn attention to the fact that many hotel businesses have little or no interaction with their customers and question how this differs from furnished holiday lettings businesses, whose landlords may similarly not necessarily interact with their customers.
8. The Office of Tax Simplification's 2022 Review of residential property income considered a "brightline test" for determining whether a business should be considered a rental business or a trading business for tax purposes. We would support further exploration of this point and would be willing to participate in any stakeholder engagement in this area.
9. Our members have told us that they would appreciate more details on the treatment of furnished holiday letting businesses which commence during the 2024/25 tax year.
10. Additional clarity over the treatment of ancillary services and whether they are significant enough to be treated as a trade in their own right following the abolition of the furnished holiday letting rules would be useful.

Capital gains changes

11. This is the area where our members have reported the greatest level of uncertainty, particularly given the lack of clarity in the Spring Budget about how the anti-forestalling rule would apply despite taking effect from 6 March 2024. We welcome the confirmation that genuine commercial transactions during the 2024/25 tax year should be unaffected by the anti-forestalling rule, particularly where these are between unconnected third parties.
12. HMRC needs to publish more details about how the mechanics of making a claim that the anti-forestalling rule does not apply will operate in practice, in particular the evidence that will be required to satisfy HMRC that “no purpose of entering into the contract was to avoid the amendments made by Part 4 having effect in relation to the disposal” as stated by paragraph 14 (2) of the draft legislation.
13. There also needs to be clear guidance on what constitutes a genuine commercial reason. Our members have flagged a situation where a furnished holiday lettings business may no longer be commercially viable due to the proposed changes (for instance, due to the change in tax relief available for finance costs). It is unclear whether such a scenario would be caught by the anti-forestalling rule for transactions, i.e. where the taxpayer has decided to sell a property that is no longer commercially viable as a furnished holiday letting but would have continued as a furnished holiday letting if the tax rules had not changed.
14. We welcome the confirmation that furnished holiday letting businesses which cease before 5 April 2025 should still qualify for Business Asset Disposal Relief for the usual three years post cessation, subject to meeting the qualifying criteria and the taxpayer not having already used their lifetime limit. However, the legislation needs to make clear whether the abolition of the furnished holiday lettings rules will itself be treated as a deemed cessation of a trade for the purpose of Business Asset Disposal Relief.
15. In the event that changes to the scope or application of Business Asset Disposal Relief are announced in the forthcoming Budget, our members would appreciate clarity on the availability of Business Asset Disposal Relief where a furnished holiday lettings business has ceased or will cease before 30 October 2024. It would be helpful to confirm whether Business Asset Disposal Relief would still be available for the current three year period post cessation.
16. Whilst the draft legislation mentions that provisional Rollover Relief claims are within the scope of the anti-forestalling rule, it is silent on the treatment of existing provisional claims to Rollover Relief. For example, a taxpayer may have sold a furnished holiday letting property in a previous tax year and made a claim for provisional Rollover Relief in anticipation of purchasing a further property to be used in a furnished holiday lettings business. Some transitional provisions on such provisional claims, including details of any potential claw back of relief, would be helpful.
17. Our members would similarly appreciate confirmation that gains previously held over on furnished holiday lettings properties gifted or transferred at under value will not be subject to a claw back of relief received before the rules are changed.

Class 2 National Insurance contributions

18. We are aware of instances where a taxpayer has been able to pay Class 2 National Insurance contributions when they run a furnished holiday lettings business but do not have any other sources of employment or self-employment income. If individuals who operate their furnished holiday lettings business as a full-time occupation are unable to continue to make Class 2 National Insurance contributions, this may impact on their ability to maintain their National Insurance contributions record in a cost-effective manner.

Pension contributions

19. Our members have raised concerns about the proposed changes to the definition of relevant earnings for pension purposes under Section 189 Finance Act 2004. The feedback we have received gives the example of clients who operate a furnished holiday lettings portfolio as a full-time occupation, in comparison with the less onerous daily time commitment associated with a portfolio of properties let out for longer-term rental. Being limited to the £3,600 'basic amount' under Section 190 Finance Act 2004 will significantly impact on the ability of such individuals to make personal pension contributions in future tax years.
20. The legislation, as currently drafted, creates an undesirable distinction in the level of personal pension contributions an individual could make depending on whether they operate their furnished holiday lettings business as an individual or through a company. A director/shareholder of a company carrying out a furnished holiday lettings business would have relevant earnings from any employment income they receive from the company. A company could also make employer pension contributions without any net relevant earnings being necessary to match against the pension contributions being made. Whereas that same individual could run the furnished holiday lettings business as an individual and their income from that business would no longer be relevant earnings and this creates an inequity between the different business structures.
21. Our members are concerned about the long term impact on individuals whose full-time occupation is managing a furnished holiday lettings portfolio because their ability to make future pension contributions will be significantly restricted. In this context, we note that the £3,600 'basic amount' has not altered since the legislation was introduced, so perhaps this should be revisited by HM Treasury in any case, given the proposed changes to the furnished holiday lettings rules.

Capital Allowances

22. We welcome the confirmation of the Capital Allowances treatment of qualifying expenditure pre April 2025. The absence of a balancing adjustment for Capital Allowances in April 2025 and the ability to continue to claim Writing Down Allowances in future years on pre 1/6 April 2025 expenditure has been positively received by our members.
23. We have received feedback about the impact of the loss of sideways loss relief for excess capital allowances, which can be beneficial for new furnished holiday lettings businesses. The introduction of a 'brightline test' or similar test could perhaps result in furnished holiday lettings being able to continue with this much valued tax relief, especially where the upfront cost of furniture are significant.
24. The draft legislation is silent on the ability to make an election under Section 198 CAA 2001 on the disposal of a property which currently qualifies as a furnished holiday letting. Updated guidance on this point would be helpful.

Deductibility of finance costs

25. We note the proposed removal of the exception for furnished holiday lettings from the rules in Section 272B ITTOIA 2005 restricting the tax deductibility of finance costs on dwelling-related loans to the UK basic rate and that this will take immediate effect from 6 April 2025. Our members have drawn attention to the fact that the special rules for dwelling-related loans were originally phased in over four tax years.
26. Our members have made us aware that the inability to claim tax relief for finance costs in full will, in some cases, mean that an otherwise profitable furnished holiday lettings business may no longer be viable. They note that decisions to proceed with the purchase of a property may have been based on the expectation of tax relief being available as per the current tax rules. We suggest that the possibility of phasing in the restriction to the UK basic rate be considered, to help avoid a perceived 'cliff edge' scenario whereby the tax relief on finance costs will be restricted within a relatively short period of time. This would ensure an element of consistency with the introduction of the original special rules for dwelling-related loans.

VAT

27. There was no reference in either the policy document or draft legislation to any changes to Schedule 9 VATA 1994 in respect of the VAT treatment of holiday accommodation. Whilst we note that the VAT position on holiday accommodation applies regardless of whether a property meets the furnished holiday letting criteria for income tax or corporation tax purposes, feedback from members indicates an inconsistency and perceived unfairness that furnished holiday lettings will cease to receive the benefits of being treated as a trade, whilst rental income will still be subject to VAT at standard rate.

Loss relief

28. The proposals for losses brought forward being integrated with losses of any existing UK or overseas property business has been positively received by our members. This appears to be an entirely logical manner in which to treat losses once the furnished holiday lettings regime has been abolished.

Impact on Form 17

29. The removal of the exception for furnished holiday lettings in Section 836 ITA 2007 will have an impact on jointly owned property owned by couples who are married or in a civil partnership. Anecdotal feedback from our members suggests that couples who own furnished holiday lettings are more likely to allocate the profits from that business in a ratio other than 50:50, compared with longer term lettings.
30. Removal of the exception will withdraw the current flexibility of furnished holiday lettings owners to split profits unequally, regardless of the ownership. Our members tell us this flexibility is often used at present, taking the time spent by the owners individually in running the furnished holiday lettings business into account. Treating furnished holiday lettings in the same way as other property income does not reflect the additional time commitment involved with running a short term property rental business – for instance, one spouse or civil partner may give up their full time employment to run the business but would be unable to receive a greater proportion of the profits in future tax years despite devoting a more significant time commitment than the other spouse or civil partner.
31. Given the proximity of the proposed changes taking effect, consideration should be given to extending the time period under which an election can be made under Section 837 ITA 2007 in the context of those taxpayers who will be required to complete Form 17 as a result of the proposed changes to the furnished holiday lettings rules. We are particularly mindful of unrepresented taxpayers who may be unaware of the need to complete and submit Form 17 following the removal of the furnished holiday lettings exception.
32. We would specifically draw your attention to the application of the term 'beneficial interest' throughout the different UK jurisdictions. It is our understanding that under Scottish law this is a term not applicable in Scotland in the same way as elsewhere in the UK. Our members have made us aware of some practical challenges that this has already presented for longer term rented properties where Form 17 is appropriate. The abolition of the furnished holiday lettings rules is likely to increase the number of taxpayers owning property who are married or in a civil partnership, and who may need to consider completing Form 17.
33. A simpler solution may be to remove the requirement to complete Form 17 for couples who are married and in a civil partnership but wish to allocate their property rental profits in a ratio other than 50:50. This would align the treatment with unmarried couples owning rental properties in similar circumstances.



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