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ABOLITION OF THE FURNISHED HOLIDAY LETTINGS TAX REGIME

Response by the Association of Taxation Technicians

1 Introduction

1.1 The Association of Taxation Technicians (ATT) is pleased to have the opportunity to provide comments on the policy paper[1] outlining the *Abolition of the furnished holiday lettings tax regime* and the accompanying draft legislation[2].

1.2 The primary charitable objective of the ATT is to promote education and the study of tax administration and practice. We place a strong emphasis on the practicalities of the tax system. Our work in this area draws heavily on the experience of our members who assist thousands of businesses and individuals to comply with their taxation obligations. This response is written with that background.

1.3 We would have liked to see broader consultation of the proposed changes in advance of draft legislation being published. This would have offered the opportunity to consult more widely with stakeholders, and for the points we raise below to have been considered at an earlier stage.

A longer consultation period would also have allowed affected landlords more time to consider the impact of the proposals, and would have reduced the risk of shocks to the property market and local economies if landlords of Furnished Holiday Lettings (FHLs) make snap decisions as a result of the abolition of the FHL regime.

1.4 Our response below is divided into a brief summary of likely positive and negative outcomes of abolishing the FHL regime, followed by areas where clarification is needed along with guidance on the impact of the changes.

1.5 For ease of reading, we refer to 6 April 2025 only as the commencement date for the proposed changes, but this should be read as 1 April 2025 for Corporation Tax purposes where relevant.

1.6 Whilst the ATT's focus and expertise is in tax, members have brought wider issues to our attention, primarily socioeconomic concerns, based on the likely impact abolishing the FHL regime will have on their

[1] https://www.gov.uk/government/publications/furnished-holiday-lettings-tax-regime-abolition/abolition-of-the-furnished-holiday-lettings-tax-regime
[2] https://assets.publishing.service.gov.uk/media/66a221cdfc8e12ac3edb0489/Draft_Leg_-_FHL.pdf

FHL landlord clients, and on the regions in which they operate. Some of these have been included as an Appendix.

2 Positive outcomes

2.1 Simplification

The FHL regime creates complexity within the tax system – subject to the relevant tests, a rental property might currently be classified for tax purposes as: a UK property business, an overseas property business, a UK FHL or an EEA FHL. Combining the FHL classifications with other UK/overseas lets, and removing the need for 'relevant tests' reduces this complexity, as well as aligning the tax treatment of FHLs with properties treated as 'ordinary' letting businesses.

3 Negative outcomes

3.1 The former Office of Tax Simplification (OTS) recommended in its 2022 Property income review[3] that the FHL regime should be reviewed, noting that it "adds a complex layer to the tax rules which apply to property income" and "may distort behaviour". Whilst it is encouraging to see the Government engage with these issues, the abolition of the FHL regime as proposed is not without drawbacks.

3.2 Primarily, balanced against the apparent simplification in paragraph 2.1 above is the fact that abolishing the FHL regime will blur the lines between a trading business and an investment business for tax purposes, particularly in respect of larger scale short-term lettings. In the absence of a separate tax regime for such businesses, comprehensive guidance will be needed to make clear when or whether they can be treated as trades for tax purposes. This is explored further in paragraph 4.1 below, where we suggest some differentiating factors which may be relevant.

3.3 The proposed reforms will take effect immediately on 6 April 2025. This risks creating a shock to the current FHL market, local and regional economies and potentially the wider housing market if FHL landlords decide to sell up as a result of the withdrawal of current beneficial tax treatments.

3.4 One result of abolishing the FHL regime will be an immediate and full restriction in tax relief for mortgage interest to the basic rate of tax.

Precedents exist for the changes affecting FHL landlords with mortgages to be phased in – for instance, the restriction to basic rate relief only for 'ordinary' let properties was introduced progressively between 2017/18 and 2020/21. Consideration should be given as to whether a phased introduction of some or all of the proposed changes would be appropriate.

[3] https://www.gov.uk/government/publications/ots-review-of-residential-property-income/ots-property-income-review-simplifying-income-tax-for-residential-landlords

4 Clarification & guidance required

4.1 Can property letting constitute a trade?

The OTS's 2022 report noted that:

"The furnished holiday lettings regime rules were introduced in 1982-83 to provide clarity over whether operating a short-term holiday rental business should be treated as a trade for tax purposes, following a number of cases on that subject and the resulting uncertainty for those involved in these businesses. The new legislation did not treat the activity as a trade, but provided that income from it was to be taxed as trading income rather than income from investments."

Abolishing FHL status reintroduces uncertainty over the dividing line between property letting as a passive investment activity and when it can amount to a trade.

The OTS recommended a "brightline test" for trading status. Since the Government has not taken up this recommendation, we would welcome guidance, ideally preceded by stakeholder engagement, to clarify when/whether property letting can be taxed as a trade. Relevant factors to consider might include: the number of properties operated, the level of additional services (catering, leisure facilities, on-site staff etc) and the amount of time owners spend running the businesses day-to-day.

4.2 What is the "relevant period" for new lets in 2024/25?

ITTOIA 2005 s324 defines the "relevant period" over which the "availability, letting and pattern of occupation conditions" need to be met in order for a property to qualify as an FHL.

In respect of newly-let properties, the relevant period is "12 months beginning with the first day in the tax year on which it is let by the person as furnished accommodation" (ITTOIA 2005 s324(2)).

If a landlord begins a short term letting business during 2024/25, it is not clear what the relevant period would be for these purposes following enactment of the draft legislation.

For instance, if a landlord first lets a property on 1 September 2024, absent the draft legislation, the relevant period would be 1 September 2024 to 31 August 2025. If FHLs are to be abolished with effect from 6 April 2025, would the relevant period be restricted to 1 September 2024 to 5 April 2025, or would the FHL conditions still be assessed based over the 'standard' first 12 months of letting? The former allows a much shorter period in which to achieve the required 105 days of commercial letting, so would this (and the other day count tests in ITTOIA s325) also be reduced pro-rata?

The principle significance is likely to be the landlord's ability to claim Capital Allowances during the first letting period, and to carry forward any capital allowance pool balances to later years. Both would depend on whether or not their property qualifies as an FHL in 2024/25.

4.3 Is there a deemed cessation of existing FHL businesses for CGT?

Would the abolition of the FHL regime result in a deemed cessation of an existing FHL business for CGT purposes? Repealing s241 of the Taxation of Chargeable Gains Act 1992 appears to result in a former-FHL business no longer being classed as a "trade" for CGT purposes, which could lead to claims for Business Asset Disposal Relief under the TCGA 1992 s169S(1).

Clarification of the Government's intention in terms of creating a deemed cessation of FHL businesses for CGT purposes, and the resulting impact on availability of BADR would be helpful.

4.4 Treatment of FHL losses within a partnership

Losses arising in respect of FHLs within a partnership are carried forward within the partnership, rather than being allocated to individual partners (as is the case with 'ordinary' partnership property losses). This is dealt with by forms SA801[4] and SA800(PS)[5] as follows:

- Partnership FHL losses are recorded in box 1.17 of SA801
- There is no carry-over of partnership FHL losses from box 1.17 of SA801 onto SA800(PS) – only partnership FHL *profits* are reported on SA800(PS) in Box 20, and divided between the partners accordingly
- Partnership FHL losses are carried forward to the following year, and entered in box 1.15B of SA801 to be offset against partnership FHL income

By contrast:

- Non-FHL partnership property losses are recorded in box 1.39 of SA801
- They are then carried over into box 19 of SA800(PS) and divided between the partners accordingly
- There is no non-FHL partnership property equivalent of box 1.15B on SA801 as any losses from the previous year are allocated between the partners in the year they arise, rather than being carried forward in the partnership.

In respect of FHLs operated outside a partnership, the policy paper states:

"persons may have losses to carry forward from their FHL business after repeal — losses generated from this FHL business will be permitted to be carried forward and be available for set off against future years' profits of either the UK or overseas property business as appropriate"

Clarification is needed as to how losses carried forward at 5 April 2025 from FHLs operated within partnerships will be relieved. For instance, will SA800(PS) be updated for 2024/25 to allow partnership FHL losses as at 5 April 2025 to be allocated between partners, so that they can be offset against property profits arising in later years? If so, presumably such losses would need to be ring-fenced to be offset only against future profits relating to properties operated by the partnership?

4.5 Increased importance of Form 17

Paragraph 3(7) of Part 1 of the draft legislation removes the exception for FHLs from the joint property rules contained in ITA 2007 s836-837.

Many spouses/civil partners who currently own FHLs in unequal shares will be accustomed to having the option to split profits/losses in accordance with their underlying beneficial ownership. In the absence of any action by the owners, the removal of the FHL exceptions from ITA 2007 s836 with effect from 6 April 2025 will result in profits/losses from former FHLs being split 50:50 for tax purposes between co-owning spouses/civil partners from that date onwards.

[4] https://assets.publishing.service.gov.uk/media/6602b52365ca2fa78e7da878/sa801-2024.pdf
[5] https://assets.publishing.service.gov.uk/media/66013a9865ca2f67417da739/sa800ps_2024.pdf

This change will need to be publicised and highlighted in guidance in advance of 6 April 2025, to allow affected joint owners an opportunity to make a Form 17 declaration effective from the beginning of the 2025/26 tax year, since such claims cannot be backdated.

Guidance may need to make clear any difference in treatment relevant to affected Scottish taxpayers, as we understand the treatment of beneficial and legal ownership differs under Scots law.

4.6 The ATT has previously recommended[6] that the deemed 50:50 split of income between spouses/civil partners should be removed, with the income tax treatment of assets owned in unequal splits instead aligned with that applying to unmarried joint owners, and with the capital gains tax treatment of such assets.

4.7 **Rollover relief – qualifying reinvestment after 6 April 2025**

We are not clear on the purpose of Paragraph 13 (2(a)) of Part 4 of the draft legislation. Does this mean that reinvesting sale proceeds after 6 April 2025 in a property which would previously have met the FHL conditions will no longer enable a claim to rollover relief to be made?

If this interpretation is correct, this provision seems redundant since FHLs will not exist after 6 April 2025 (assuming the legislation is enacted as drafted).

4.8 The inability to claim rollover relief in respect of reinvesting in a property which would previously have met the FHL conditions will adversely affect those who have made provisional claims for rollover relief under TCGA 1992 s153A in anticipation of reinvesting sale proceeds in an FHL after 6 April 2025, but within the three year period permitted under TCGA 1992 s152(3).

As a result of the proposed legislative changes, those affected who cannot (or do not wish to) invest in other assets which continue to qualify for rollover relief will need to withdraw their provisional claims, and will therefore face late payment interest and penalties. This seems unfair given the abolition of the FHL regime from 6 April 2025 was not expected at the time of their provisional claim.

4.9 **Draft legislation: Anti-forestalling rule in Part 4, Paragraph 14 (2)(a)**

Paragraph 14 (2) permits a "relevant claim" (as defined in Part 4, Paragraph 14 (3)) to be made in respect of a disposal arising under an unconditional contract made between 6 March 2024 and 6 April 2025 where completion occurs after 6 April 2025.

The condition in Paragraph 14 (2)(a) allowing such a claim to be made is that "no purpose of entering into the contract was to avoid the amendments made by Part 4 having effect in relation to the disposal". We question the value of this condition in some situations, given it relies on proving intention – how will it be enforced, how will taxpayers prove what their intention was, and how would HMRC disprove that taxpayer's claim? Tests of intention apply elsewhere in legislation (for instance in Private Residence Relief claims), but have been found to create uncertainty and require legal challenge before an agreed position can be established. Guidance on what would constitute proof of intention (or, equally, absence of intention) would be helpful.

We also question the fairness of this condition in respect of affected disposals where unconditional contracts were made between 6 March 2024 and 29 July 2024 (the date the draft legislation was published).

[6] https://www.att.org.uk/sites/default/files/2023-10/ATT%20autumn%20statement%20representation%20form%2017.pdf and https://www.att.org.uk/technical/submissions/att-budget-representation-income-tax-simplification

During that time, taxpayers had no indication of what the "anti-forestalling rule"[7] announced at the Spring Budget would be.

4.10 **Draft legislation: Template statement for Part 4, Paragraph 14 (2)(c)**

The requirements of Paragraph 14 (2) of Part 4 of the draft legislation must be highlighted in guidance to enable complete claims for rollover relief, gift relief and business asset disposal relief to be made in respect of eligible disposals between 6 March 2024 and 5 April 2025.

Guidance will need to make clear the need to include the statement specified in Paragraph 14 (2)(c). We would welcome publication of a template statement which HMRC will accept.

5 Contact details

5.1 Should you wish to discuss any aspect of this response, please contact atttechnical@att.org.uk.

The Association of Taxation Technicians

10 September 2024

6 Notes

6.1 The Association is a charity and the leading professional body for those providing UK tax compliance services. Our primary charitable objective is to promote education and the study of tax administration and practice. One of our key aims is to provide an appropriate qualification for individuals who undertake tax compliance work. Drawing on our members' practical experience and knowledge, we contribute to consultations on the development of the UK tax system and seek to ensure that, for the general public, it is workable and as fair as possible.

6.2 Our members are qualified by examination and practical experience. They commit to the highest standards of professional conduct and ensure that their tax knowledge is constantly kept up to date. Members may be found in private practice, commerce and industry, government, and academia.

6.3 The Association has more than 10,000 members and Fellows together with over 7,000 students. Members and Fellows use the practising title of 'Taxation Technician' or 'Taxation Technician (Fellow)' and the designatory letters 'ATT' and 'ATT (Fellow)' respectively.

[7] https://www.gov.uk/government/publications/spring-budget-2024-overview-of-tax-legislation-and-rates-ootlar/spring-budget-2024-overview-of-tax-legislation-and-rates-ootlar#chapter2:~:text=come%20into%20force.-,2.7,-Abolition%20of%20the

APPENDIX

Wider concerns raised by members

Impact on local economies

The policy paper does not seem to consider the potential variation in regional impact of abolishing the FHL regime. For instance, according to figures from Visit Britain[8], Cornwall and the Isles of Scilly have more short term rental properties than any other ITL3 area[9] in the UK. The impact of abolishing FHLs on local economies and small business which rely on tourism should be assessed, particularly in relation to the relative prosperity and other industries in those areas.

A counterargument is noted in the OTS 2022 report, that "[The FHL regime] has a detrimental effect on the stock of housing in coastal and other holiday regions".

The policy paper does not go into detail on either perspective, but both should be considered before the draft legislation is enacted.

Consultation with housing market experts would help understand whether local housing supply is likely to be freed up by landlords exiting the FHL market, and over what time period any impact might be seen on the ability of local people to afford those properties.

Wider economy and green agenda

If FHL landlords exit the UK holiday letting market, there will be a reduced supply of UK holiday accommodation, which could result in fewer international tourists spending money in the UK.

[8] https://www.visitbritain.org/integrated-report/short-term-rentals-dashboard
[9] https://www.ons.gov.uk/methodology/geography/ukgeographies/eurostat