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**Spring Budget 2024: Abolition of the Furnished Holiday Lettings (FHL) tax regime**

**Proactive submission by the Chartered Institute of Taxation**

## 1 Introduction

1.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 20,000 members, and extensive volunteer network, in making this submission.

1.2 At Spring Budget 2024, the government announced it will abolish the Furnished Holiday Lettings tax regime with effect from April 2025.[1] The policy intention is to eliminate 'the tax advantage for landlords who let out short-term furnished holiday properties over those who let out residential properties to longer-term tenants'.

1.3 Draft legislation will be published in due course and include an anti-forestalling rule taking effect from 6 March 2024.

1.4 The purpose of our proactive submission is to raise current uncertainties for individuals and businesses following the announcement, to identify any potential unintended consequences and to suggest ways in which they might be addressed including through further consultation.

1.5 Our stated objectives for the tax system include the following aims that are relevant to this submission:

- A legislative process that translates policy intentions into statute accurately and effectively, without unintended consequences.
- Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
- Greater certainty, so businesses and individuals can plan ahead with confidence.
- A responsive and competent tax administration, with a minimum of bureaucracy.

[1] See Paragraph 2.7 Spring Budget 2024: Overview of tax legislation and rates (OOTLAR)

## 2 Uncertainty in relation to the boundary between investment and trading

2.1 In the 2022 Property Income report, the Office of Tax Simplification (OTS) concluded that the FHL regime can give valuable tax benefits but is not widely used and adds a complex layer to the tax rules which apply to property income. We recognise the benefits of simplification in removing the complexities of the FHL regime such as complying with the qualifying day tests[2]. However, the FHL regime currently acts as a bridge between the tax treatment of running a property business, such as a letting under a shorthold tenancy agreement, and the tax treatment of running a trade such as a hotel or guest house. It therefore provides certainty of tax treatment for short term holiday letting businesses that meet the FHL qualifying conditions. It does not afford trading status, but enables access to certain tax treatment that is available to trades[3].

Abolition of the FHL regime reopens the complexity of a dividing line between trading and an investment business, which turns on fine distinctions. This was demonstrated in a number of tax cases[4] and was one of the reasons for the introduction of the FHL regime in 1982/83. Many holiday businesses would be treated as a trade following the 'badges of trade' if ownership of the property were ignored, a difficulty acknowledged in the more recent *Julian Nott*[5] case.

2.2 The OTS recommended that if the FHL regime is abolished the government should consider a means of making the boundary more certain to avoid disputes about letting businesses with a high level of services[6]. In such cases arguments may be put forward that the activity constitutes a trade. The more favourable tax treatment for trades may lead therefore to potential disputes/litigation and consequential costs for HMRC and taxpayers. One means of addressing this issue, set out by the OTS, is the introduction of a statutory 'brightline' test that might involve factors such as those below in determining where the boundary lies.

- Minimum number of units,
- Short term lettings only;
- No private use; and
- Level of personal time devoted and/or provision of services.

We support the OTS suggestion that there should be a statutory test on the boundary between a trade and rental businesses on the basis that abolition of the regime may not only give rise to costly disputes but could lead to administrative complexity. For example, a large proportion of agricultural businesses have diversified in order to maintain their core trade, however apportionments will be required between trading (farm property) and non-trading activity (holiday lets) within a diversified farming business.

We note that HMRC's current practice is to treat hotels and bed and breakfasts as trades (see BIM22001). However even this distinction may not be easy to apply and was questioned in *Julian Nott* as being 'unduly

[2] Confusingly the qualifying day tests are not aligned with the tests for business rates.

[3] The favourable tax treatment for the FHL regime includes:

- Loan interest and finance costs are fully deductible;
- Capital allowances are available;
- Profits are relevant earnings for pension contribution purposes; and
- CGT reliefs including replacement roll-over relief, gift hold-over relief and business asset disposal relief.

[4] For example *Gittos v Barclay [1982] 55 TC 633* and *Griffith v Jackson [1985] 56 TC 83*.

[5] *Julian Nott v HMRC [2016] UKFTT 106 (TC)*

[6] Long term letting of residential properties in the UK is usually on an unfurnished basis. In contrast to long term lets, there is likely to be a greater degree of investment in furniture and furnishings required for a new holiday let . Following abolition of the FHL regime, relief will only be available for such expenditure on a replacement basis unless the activity constitutes a trade.

simplistic' (see para 89 of the decision). The comparison may also be somewhat outdated given that, in some hotels, services are largely automated.

If adopted we suggest final design and scope should be determined following consultation. In accordance with the government's simplification objectives, a further/wider consultation could consider whether definitions for inheritance tax[7], CGT and national insurance are aligned to income tax status.

## 3 Transitional issues

3.1 Removal of the FHL regime gives rise to the need for transitional measures on:

- **Capital allowances and treatment of balancing charges/allowances;**

*The default position*

Without transitional provisions, a notional balancing charge may arise on abolition of the FHL regime based on the difference between the market value of the assets on which allowances have been claimed and the tax written down value (typically nil due to the availability of the annual investment allowance). Any balancing charge will be a 'dry' tax charge (a tax liability without cash proceeds) for FHL businesses that incurred the expenditure in the expectation that the FHL regime would remain in place.

Where the assets on which capital allowances were originally claimed under the FHL regime include domestic items such as includes furniture, furnishings, household appliances and kitchenware and those items are subsequently replaced post abolition, we assume a deduction will be available to the property business for expenditure incurred on the replacement of those domestic items under ITTOIA 2005 section 311A (CTA 2009 section 225A).

Possible alternatives to the default position, depending upon the policy intent, might include:

*Option 1*

The OTS suggested consideration could be given to allowing individuals to elect for limited spreading of any notional balancing charge arising on cessation. As with the default we assume that the replacement of domestic items would be available for subsequent eligible replacements.

If this option is adopted, it may be necessary to provide the ability to elect out of spreading if to do so is more favourable for the taxpayer.

*Option 2*

An alternative approach might be to allow notional allowances to continue post abolition based on CAA 2001 section 13B. The notional pool would maintain a record of unrelieved FHL expenditure and any disposal receipts, with a balancing charge arising on the property business where disposal receipts exceed the balance

[7] There is a body of case law considering the availability of Business Property Relief for IHT purposes in a holiday lettings context including the Upper Tribunal case of HMRC v Pawson's Personal Representatives UKUT 050 (TCC) and The Personal Representatives of Grace Joyce Graham (deceased) v HMRC [2018] TC06536. However these cases concern the question of whether the holiday letting business was disqualified from BPR because the business of the company consisted wholly or mainly of making or holding investments.

in any year and a final balancing charge when the property business ceases. As with the default and option 1, we assume that the replacement of domestic items would be available for subsequent eligible replacements.

We suggest that whatever approach is adopted it would be helpful to publish proactive guidance on the transitional position for capital allowances in advance of abolition to address current uncertainty – see for example: HMRC Customer Forum: Capital Allowances on FHLs.

- **Treatment of un-used losses**;

*The default position*

The current position is that losses from an FHL business can only be carried forward against other FHL profits and cannot be set against general property income. Therefore, unless this point is addressed by transitional provisions, any accumulated FHL losses as at 5 April 2025 would be lost when the property loses its FHL status at that time.

Possible alternatives to the default position, depending upon the policy intent, might include:

*Option 1*

The OTS report suggested that to alleviate this situation it might be appropriate to merge FHL losses with other rental losses.

*Option 2*

FHL losses could be carried forward to be used only against future rental profits from the former FHL property. We note this option could give rise to administrative complexities for the taxpayer in keeping appropriate records. It would also require more complex changes in legislation and in the structure of the self assessment tax return to enable the losses to be streamed in this way.

## 4 Anti-forestalling rule

4.1 The anti-forestalling rule applies from 6 March 2024. The Budget statement is reproduced below:

*As announced at Spring Budget 2024, the government will abolish the Furnished Holiday Lettings tax regime, eliminating the tax advantage for landlords who let out short-term furnished holiday properties over those who let out residential properties to longer-term tenants. This will take effect from April 2025.*

*Draft legislation will be published in due course and include an anti-forestalling rule. This will prevent the obtaining of a tax advantage through the use of unconditional contracts to obtain capital gains relief under the current FHL rules. This rule will apply from 6 March 2024.*

4.2 Draft legislation for the anti-forestalling rule has not been published at the time of writing. As a general point it is obviously difficult for taxpayers to comply with provisions in force that have not been published and such an approach seems contrary to the Charter commitment to help taxpayers meet their tax responsibilities.

4.3 The anti-forestalling statement is also causing some uncertainty. It is not clear whether the intention is that

- business asset disposal relief will not be available from 6 March 2024; or

- the anti-forestalling rule is intended to prevent taxpayers seeking to take advantage of business asset disposal relief by resting on contracts that is, where a contract is exchanged after 6 March 2024 but not completed until after 5 April 2025;
- the anti-forestalling the rule also extends to claims for other CGT reliefs - for hold-over on succession or roll-over?

We think it is important to clarify the scope and intent of the anti-forestalling rule and publish draft legislation and guidance without delay because of the uncertainty.

## 5 Acknowledgement of submission and participation in consultative discussion

5.1 We would be grateful if you could acknowledge safe receipt of this submission. We would be pleased to be involved in any discussion or consultation on the consequences of abolition.

The Chartered Institute of Taxation

10 April 2024

The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.

The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries.

Our members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.