Taking a holiday?

Richard Lishman of money4dentists discusses the current issues concerning furnished holiday lettings for businesses

Businesses have to meet both commercial conditions and letting conditions. This means the property must be let on a commercial basis in order to acquire profits and obtain tax reliefs. This is an important consideration when taking loss relief into account because, for example, if losses arise over three years, it may prove challenging to validate that the property is being let commercially.

In addition to this, the Budget 2009 announced that the previous tax reliefs would be discontinued from 6 April 2010 (1 April 2010 for companies) and in order to benefit from the previous tax reliefs, businesses operating as FHLLs will need to prove that they are functioning trades. Ironically, this was the situation that existed before Finance Act 1984.

Conversely, the new coalition government has announced that the Budget 2009 will not now take place. Instead, the previous FHLL rules will apply during 2010/11. The government plans to consult over the summer on the change of the tax treatment of furnished holiday lettings from 6 April 2011.

The government has declared that the FHLL rules need to be changed to comply with EU law. They are seeking to change the rules in a way that is consistent with deficit reduction and without compromising UK businesses.

The FHLL rules granted the following tax conditions to lettings that qualify as a trade:

- Loss relief
- Capital allowances
- Landlords Energy Saving Allowance (LESA)
- Certain capital gains reliefs.
- Business asset roll-over relief
- Entrepreneurs’ relief
- Relief for gifts of business assets
- Relief for loans to traders and exemptions
- Disposals of shares by companies with a substantial shareholding
- Relevant UK earnings when calculating the maximum relief due for an individual’s pension contributions.

It is worth noting that, as a trade, any income received from the property will be taxed as earned income. But what defines a trade? There appears to be little in the way of a legal definition, aside from section 988 ITA 2007 which defines trade as including any venture in the nature of trade. This is rather limited as definition and although judgements in various court cases can provide some guidance, the crux of the matter will be whether a person’s income is being obtained through trading or if they are a mere landowner who is exploiting the property for income.

For example, a hotel would amount to a trade due to the services that are provided, whereas a person letting a self-catering apartment without providing any services, would most likely be regarded as undertaking an investment business.

With regards to National insurance, FHLL has been regarded as land and property income for NIC purposes. There has been no need to justify that an FHLL is a trade due to the statutory provisions that are in place. In addition, in the context of FHLL, inheritance tax business property relief does not rely on a business satisfying the statutory definition within section 525(2) ITTOIA 2005. However, the FHLL must be a business that is not an investment business, ie: it should not deal in or hold investments, in this case land.

As they did previously, these FHLL rules will continue to apply to holiday lettings situated in the UK during the tax year 2010/11. Furthermore, HMRC will continue to apply the FHLL rules to properties situated elsewhere in the European Economic Area (EEA) during the tax year 2010-11. However, holiday lettings located outside the EEA do not qualify under the FHLL rules and are instead taxed under the normal property income laws.

The Government is looking to reintroduce the FHLL rules from 6 April 2011 (1 April 2011 for companies) for effect from tax year 2011/12. These will not only ensure the FHLL rules apply equally to properties in the EEA but will also change the way in which FHLL loss relief is given. Furthermore, it will increase the number of days FHLL businesses have to be available to let as commercial holiday letting.

Full details about the proposed changes will be discussed over the summer, and the legislation will be drafted in the autumn. With the finer details unclear at this point, property owners should seek out professional tax advice in advance of 6 April 2011 to make sure that their business profile gives them maximum scope for tax reliefs.

### About the author

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