

FHLs and Business Asset Disposal Relief

(Lecture P1223 – 20.34 minutes)

Although the letting of property is not tantamount to the carrying on of a trade, for 36 years HMRC have allowed the owners of furnished holiday accommodation situated in the UK to be treated for income tax and CGT purposes as though they were traders. Initially, overseas properties did not attract a similar relief. However, in 2009, it was decided that this distinction was not compliant with European law and so, in FA 2011, the Government announced that the rules were being extended to cover all qualifying properties situated anywhere in the EEA for 2011/12 onwards.

For many property owners, one of the biggest attractions of the FHL regime is the possibility of claiming business asset disposal relief on a sale. However, the position here is not as straightforward as it might be and the tax treatment can depend on whether the vendor owns a single holiday property or several.

It should be explained that two of the categories of a material disposal of business assets are:

- a disposal of all or part of an unincorporated trading business (S169I(2)(a) and (3) TCGA 1992); and
- a disposal of assets previously used for a trading business which has ceased (S169I(2)(b) and (4) TCGA 1992).

Illustration 1

Simon, aged 70, has owned a single holiday property in the UK for many years which has always satisfied the furnished holiday accommodation criteria.

On 1 September 2020 (towards the end of the 2020 holiday season), he sold the house to his son-in-law as he was increasingly finding that the requirements of some of his holidaymaker tenants were becoming too demanding.

It seems clear that this transaction represents a disposal of all of Simon's FHL business under S169I(2)(a) TCGA 1992, in respect of which he can claim business asset disposal relief.

Let us now vary the facts about Simon's disposal.

The holiday rental season winds up on 31 October 2020. Simon decides that, at his age, he has had enough of property letting and so he sells off the contents of the holiday house on eBay over the pre-Christmas period.

In early 2021, Simon decides to put the freehold property into the hands of a local estate agent, but, because of COVID-19, he does not receive an offer which comes close to his asking price. On 1 April 2021, Simon therefore lets the property on a six-month tenancy, following which it is finally sold in January 2022.

S169I(2)(a) TCGA 1992 clearly cannot apply, but Simon is still able to rely on S169I(2)(b) TCGA 1992 in order to obtain his 10% business asset disposal rate.

When the 2020 holiday season finished, Simon's property letting business came to an end and, because the house was eventually sold well within the three-year window following this cessation, he was still able to claim the relief. Two points should be noted:

1. HMRC do not have discretion to extend the three-year period under any circumstance – see Para CG64045 of the Capital Gains Manual;
2. There is no restriction on the use to which the former holiday property can be put during the period from the cessation of the FHL business up to the date of the sale. The fact that it was subsequently rented out on a non-holiday basis is irrelevant. Contrast this position with the rules for associated asset disposals.

Another commonly encountered scenario is where a client has owned, say, five holiday rental properties for several years but only sells one of them. It is prima facie unlikely that he can argue for a part disposal under S169I(2)(a) TCGA 1992. And there has obviously not been a cessation of the FHL business which is a prerequisite if S169I(2)(b) TCGA 1992 applies. As a result, business asset disposal relief may not be available. However, do not neglect the following lines of argument:

If two of the five properties were located in Cornwall, another two in Suffolk and the fifth one in the Lake District (which was the property sold), it may be possible to contend that, because of the different locations and types of holidaymaker, the vendor operated more than one business so that the sale of the Lake District building represented a distinct part of his FHL business. In that case, a business asset disposal relief claim should be competent.

Even if all five properties were in the Lake District, it might well be that the sale of the first property was followed by a sale of the remaining four properties to a different buyer shortly thereafter. In other words, the vendor has disposed of the entirety of his property letting business, leading to a relief claim. In this instance, timing would be crucial and it might be better planning to arrange for the business to close down first before any of the sales were made (which could then be staggered over the next three years).

UK FHL activities and overseas FHL activities are regarded as separate businesses. Thus the letting of a furnished holiday cottage in Cornwall and the letting of a very similar property on the other side of the English Channel in Brittany (owned by the same individual) will always be treated as two distinct businesses.

When dealing with the sale of furnished holiday accommodation which is jointly owned by, say, a married couple, it should be borne in mind that the rental profits from an FHL do not have to be divided between the spouses on a 50 : 50 basis (S836 ITA 2007). However, if the property was purchased by the couple as equal tenants in common, the resulting gain should be split between them in that proportion, even if the income has been shared in a different way for tax purposes. This should maximise the benefit of business asset disposal relief for the husband and wife. As a practical point, if the rental profits have in recent years been divided on, say, a 10 : 90 basis, it might be sensible to ensure that, for the two years prior to the sale, the profits were split on a more even footing.

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