

## Capital allowances on Furnished Holiday Lets

### Introduction

Each year owners of holiday properties miss out on thousands of pounds in tax relief as a result of lost or under claimed Capital Allowances. Some owners are not aware that tax relief is available and in other situations they are not fully aware of the basis of the claim.

Tax relief in the form of Capital Allowances is available on the plant and machinery fixtures within a property. This includes heating systems, the electrical installation and kitchen and bathroom fittings.

The previous Government did announce that the rules would be repealed and for any expenditure after 1st April 2010 capital allowances would no longer be available. These changes were, however, dropped and Capital Allowances can still be claimed!

### The Valuation

The claiming of capital allowances on a purchased holiday property is not straight forward. The claim is not based on the original construction cost of the property even if it is newly built. Instead, a separate valuation known as a "just apportionment" is required. As this is based on the actual purchase price, a higher claim usually results!

The need for the "apportionment" is set out in CAA 2001, section 562. It must be based on the separate valuations of the land, buildings and plant and the aggregate value reconciled to the overall purchase price using a method as set out in the Valuation Office manual. Often an investor will also purchase items of loose fixtures and fittings such as beds, chairs, settees etc. These are sometimes called Chattels and should not form part of the just apportionment calculation.

### Possible Restrictions

In some cases there may have been previous claims made on the plant and machinery fixtures. If this is the case, the maximum allowable amount available to the purchaser will be restricted to the prior claimant's disposal value.

The disposal value is required to be equal the purchaser's apportionment of the purchase price, subject to a maximum of the amount of capital expenditure incurred by the prior claimant. In practice, the seller will want to minimise and the purchaser maximise, this value. Further complications will arise when there has been an intervening owner who had no interest in Capital Allowances.

In the absence of an election or contract provisions, it is open to the purchaser to challenge the sellers disposal value on the basis that is not equal to the purchasers apportionment, subject of course to knowing the limits that apply.

It is, therefore, essential that any capital allowances claim is fully researched and correctly computed in order to withstand the potential interrogation of HMRC's Inspectors of Taxes.

### Other Rules

In order to claim capital allowances on furnished holiday properties, there are a number of other tests which are included to ensure that the lettings are on a commercial basis. The criteria set out by CAA 2001, section 17 and ICTA section 504 are as follows;

- The property must be situated in the UK
- Be let furnished
- Be available for holiday letting to the public on a commercial basis for 140 or more days per year
- Actually be let commercially as a holiday property for 70 days or more per year
- Must not be occupied continuously for more than 31 days for at least seven months of the year

Where a taxpayer owns more than one holiday property the 70 day letting requirement can be averaged out over the other properties.

The "year" is usually treated as the tax year to 5<sup>th</sup> April although for the first year of trade a twelve month period from the start of the business applies.

## 4-thought

The “commerciality test” is important as there have been cases of taxpayers purchasing a property primarily for their own enjoyment and then trying to claim allowances and reliefs. There have been two reported cases where the commerciality of a holiday letting business was challenged.

In Walls (SpC4) (1995) the taxpayer was successful even though losses had been made. In Brown (SpC129) (1997) the taxpayer lost his claim as the initial intention was for the property to be used primarily for pleasure, rather than with a view to the realisation of commercial profits.

### **Improvements or conversion works**

As well as being able to make a claim on the purchase expenditure, if you have refurbished, extended or improved the building, additional tax allowances could be available.

Where works are “repairs”, the expenditure should be treated as a revenue cost. If, however, the works include improvements or extensions, these are capital items and capital allowances could be available.

### **What to do when you sell**

When a property is sold and a capital allowances claim has been made, it is essential that the taxpayer enters into a Capital Allowances Act 2001, Section 198 election with the purchaser. By doing so any repayment of the tax relief already claimed is avoided and it may even be possible to obtain the benefit of some additional tax relief even after the property has been sold.

A section 198 election will set out the amount attributable to plant and machinery fixtures and provided it is in the correct format and the election is submitted to HMRC within two years of completion, it will be accepted by HM Revenue & Customs in lieu of an apportionment based on the sale price. The amount cannot be more than the expenditure incurred by the seller on the fixtures, nor the price paid for the property, but can be as little as £1.

A £1 election value will allow the seller to retain the benefit of the capital allowances to the detriment of the purchaser. On the other hand many purchasers will want the value to be the maximum possible and certainly no less than tax written down value, so a degree of negotiation may be needed.

### **How can ca4 help?**

We will carry out a free initial report for you on your holiday property to let you know how much you could potentially save - nothing is too small or too big!

All we need is some background information on the property such as purchase price, address etc.

We can produce the formal valuation in accordance with the capital allowances rules for submission to HMRC. This report provides all of the information they will need to undertake the initial review.

Our fees are based on the tax savings - **no savings, no fee.**

**Any queries? Call 01905 619224**

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