

Furnished holiday lettings (FHL)

Key points

- *To be a furnished holiday let, the property has to be properly furnished with guests being entitled to use the furniture.*
- *It must be let for a specified number of days each tax year.*
- *A period of grace election may be available for owners who failed to meet the 105-day test.*
- *Profits from holiday accommodation must be calculated separately from other rental business.*
- *Owners may wish to review their Covid-related grant claims.*

Income from the letting of property has to be reported on a self-assessment return. That includes any income which is below market rates, for example because the letting was at 'mates' rates' to 'friends and family'. Taxable income is not restricted to cash, and holiday let owners should consider whether they have entered into a barter transaction when they offer reduced rates, ie provision of accommodation for a discount on fees that would otherwise have been charged on services, or where holiday let owners swap holiday let houses.

There are nevertheless many tax advantages of owning a furnished holiday letting (FHL). Note that although this article considers only FHLs in the UK which are owned by individuals it is possible to have a qualifying FHL in the European Economic Area.

When will a property be deemed to be an FHL?

To be an FHL (for income tax purposes), the property has first to be properly furnished with guests being entitled to use the furniture. Second, it must be let commercially – the property owner must intend to make a profit. Letting the accommodation off-season, for example a property in Cornwall during the winter months, to help cover costs is still considered to be commercial. Third, it must pass the three occupancy conditions:

- ***pattern of occupation condition;***
- ***availability condition; and***
- ***letting condition.***

For each of these conditions a year typically means a tax year 6 April through to 5 April, but different rules may apply for new or ceasing FHLs.

- *The pattern of occupation condition requires the owner to monitor the number of days where the property is let to the same person for more than 31 continuous days and to ensure that all such lettings do not exceed 155 days during the year. Often, the simple solution is never to let the property for more than 28 continuous days to the same person.*
- *The property must be available for letting for at least 210 days in the year; this period does not extend to when the owner or their friends and family are using the property.*
- *The property must be let out commercially to the public for at least 105 days a year. While income from friends and family is taxable, if those guests are not paying a commercial rate, their days of use will not count towards this 105-day test. Lettings for more than 31 continuous days to the same person do not count either, unless this is due to unforeseen circumstances; sickness, accident or delayed flights are the examples given in the HMRC's Property Income Manual PIM4110, but arguably, Covid travel restrictions should also be considered sympathetically.*

If the 105-day test is not met, all is not necessarily lost. Owners of more than one FHL may look to an alternative averaging basis and all owners could consider whether a period of grace election (POGE) may be appropriate. A key condition of a POGE (there are others), is that the property was available to let for 210 days in the relevant year and the owner had a genuine intention to meet the letting condition but circumstances beyond their control intervened. There were concerns that during the various lockdowns, properties were, arguably, not available for 210 days as being so available would have been in breach of the Covid restrictions but this point has now been clarified (tinyurl.com/czc4xxmc):

‘HMRC’s current policy position in terms of Covid relaxation is in relation to the period of grace election (POGE). The availability condition is satisfied if the person has made the property available for letting as furnished holiday accommodation for at least 210 days in the year. We have taken the view that as long as the person had made it available for 210 days, even if the Covid restrictions meant that the property could not be used, the person has satisfied the test.

‘For example, if you had a holiday let and had it advertised on a booking platform for 210+ days and Covid restrictions/travel bans etc meant that in reality people could only book it for 190 days, and actuality (sic) you only managed to let it out for 70 days, then as long as you were an FHL or period of grace election) (sic) the previous year, then you would still qualify as an FHL. But if you took the opportunity of cancelled bookings to renovate the property such that you could not advertise it as available for 210+ days then you wouldn’t then qualify.’

Detailed advice may well be needed because another condition for a successful POGE is that it can only be made following a qualifying year, or following a POGE, with a maximum of two consecutive POGEs permitted. As a result, some owners (especially new owners) when filing their 2020-21 tax return, may not qualify.

What are the tax benefits of owing an FHL?

A qualifying FHL attracts a number of significant tax advantages as HMRC states in its *Guidance HS253* which was updated 6 April 2021 ([tinyurl.com/hmrchs253](https://www.tinyurl.com/hmrchs253)):

'If you let properties that qualify as FHLs:

- *you can claim capital gains tax reliefs for traders (business asset rollover relief, entrepreneurs' relief, relief for gifts of business assets and relief for loans to traders);*
- *you're entitled to plant and machinery capital allowances for items such as furniture, equipment and fixtures;*
- *the profits count as earnings for pension purposes.*

To benefit from these rules, you need to work out the profit or loss from your FHLs separately from any other rental business.

But there are at least three other tax and finance related advantages that this guidance does not mention, namely:

- *Small business rates relief (SBRR) often means that no business rates are paid. (The test here is different and less stringent than the income tax FHL test.)*
- *Many holiday home owners were entitled to Covid support grants and as Robert Hayton, UK president of Altus Group, said: 'The grants for second homeowners will have been far more lucrative than 'business as usual' for many, especially in the off-seasons, while there is a pivot towards holiday lets as rental prices boom in hotspots.' (Again, a different set of criteria needed to be satisfied.)*
- *Interest relief. Buy-to-let property owners will be familiar with the fact that from tax year 2017-18 there have been restrictions on the extent to which interest and other finance costs payable on a loan to buy residential let property may be taken into account when calculating the profits subject to income tax. Indeed from 2020-21 onwards, no deduction is allowed for these expenses when calculating the profits. Instead, the current rules are that, in effect, interest and finance costs are relievable at the basic rate rather than at the taxpayer's highest rate.'*

Let's look at each of these points in more detail.

Small business rate relief

Regarding SBRR, on 23 March 2021 the government noted that owners of holiday lets currently pay business rates rather than council tax if the owner declares that they intend to make the property available to let for 140 days in the coming year. According to the government, around 96% of holiday homes currently qualify for SBRR and as result, pay no business rates at all.

New criteria will be set out to ensure that SBRR is properly claimed and the Treasury confirmed that the Ministry of Housing, Communities and Local Government would be issuing a response 'shortly', but in the meantime confirmed that: 'The government will legislate to change the criteria determining whether a holiday let is valued for business rates to account for actual days the property was rented.'

Grants

For some, the release of some Covid-related grants gave the impression that the government was taking the 'pay now and check later' approach. Now that the dust has settled a little, FHL property owners may well be nudged by HMRC to revisit their claims and consider if, with the benefit of hindsight, the claim for the grant was indeed appropriate.

Interest

Currently there is a differential in the deductibility of interest as between buy to let and buy to holiday let, with holiday lets enjoying a more advantageous tax position

Being classified as an FHL is not, however, a panacea against all taxes and the value of the property will typically be subject to inheritance tax: 'HMRC's view is that furnished holiday lets will in general not qualify for business property relief. The income derived from such businesses will largely consist of rent in return for the occupation of property.

There may however be cases where the level of additional services provided is so high that the activity can be considered as non-investment, and each case needs to be treated on its own facts' (HMRC's *Inheritance Tax Manual* IHTM25278 'Business relief: Investment businesses: Holiday lettings').

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