STARTING A PRIVATE PRACTICE

The taxman homes in on lettings

When the money starts coming in from your new private practice, then you need to find a good home for it. But, warns **Ian Tongue** (pictured below), the furnished holiday let option is no longer so attractive

WHEN DOCTORS start taking stock of the new wealth being generated from setting up in private practice, they often decide to shelter money by buying a second property.

Historically, furnished holiday lettings have been popular due to the desire to own a holiday home and the favourable tax relief available on it.

However, new taxation rules in relation to furnished holiday lettings are in force that, together with other future changes, may affect your decision to purchase a property of this type or continue to enjoy the favourable tax relief experienced of the past.

In last April's Budget, the Chancellor confirmed that proposed changes to the rules in consultation documents would be made from 6 April 2012 and these will apply to properties in the UK and the European Economic Area (EEA).

This is on top of the changes made from 6 April 2011 in relation to offsetting trading losses against other income sources.

What is a furnished holiday letting?

Under both the old and new tax rules, in order for a property to be classified as a furnished holiday letting it must meet strict criteria. It is not sufficient to buy what is essentially a family holiday home, rent the property out now and again and expect it to qualify.

In summary the main criteria is as follows:

- The property must be available for letting to the public for 210 days (30 weeks) a year. This is up from 140 days under the old rules;
- The property must be actually let to the public for 105 or more days (15 weeks). This is up from 70 days under the old rules;
- The property cannot be let to the same person for more than 31 days.

Businesses meeting the 'actually let' threshold in one year may elect to be treated as having met it in the two following years 'period of grace', providing certain criteria are met which have yet to be announced. This will apply from 2010-11.

What is downside?

In the past, those individuals with property meeting the criteria were able to offset losses made on such properties against other sources of income. For many, this was a significant help towards funding the furnished holiday letting.

But the bad news is that, from 6 April 2011, losses from qualifying furnished holiday lettings will no longer be allowable against other income.

Any losses generated will only be available to be set off against profits of the same furnished holiday letting business.

As the losses can only be used against this specific holiday letting business, if you have an investment property(s) – i.e. 'Buy to let' – then you cannot offset these losses if the investment property is making a profit.

> "If you have been making a £10,000 loss a year, which has been offset against your private practice profit, you could see your tax liability increasing by £5,000 a year if you are a 50% taxpayer"

Impact

As many have 'enjoyed' the loss relief against their other income, they will find their taxable profits/income increasing.

For example, if you have been making a £10,000 loss a year which has been offset against your private practice profit, you could see your tax liability increasing by £5,000 a year if you are a 50% taxpayer.

Additionally, due to the mechanism of payment under self-assessment, in the first January when the effect of the increase is felt, your payment on account is likely to increase and therefore the cash impact would be £7,500.

One benefit of the new rules is that it covers properties in the EEA as well as UK furnished holiday lettings. There has been a move towards this over the last couple of years, but no doubt there are individuals with foreign property meeting the criteria that will benefit from the changes.

It is important to understand that the country where the property is situated usually has primary taxing rights and therefore you may pay tax in a foreign country as well as the UK. Credit is usually given on your UK tax return for tax suffered abroad up to the UK tax due.

■ **Next issue: Strength in numbers – chambers and groups**

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WHAT CAN WE DO?

It is vital that you understand your individual position. If you have furnished holiday lettings, you must discuss your position with your accountant to assess the impact on you. As illustrated in this article, the impact could be significant if you have historically offset losses on your property.

If you have a loss-making furnished holiday letting but profit-making investment properties, it may be worth considering changing the classification of the property by reference to the criteria.

But a full consideration of your circumstances is essential, as other taxes such as capital gains tax and inheritance tax are affected by the different classification. This is an area to discuss with your accountant.

If you have a property in the UK or European Economic Area (EEA) that has made losses in the last four tax years and may have qualified as a holiday furnished let, then you should review previous years' claims for losses to see if they may be offset against your other income.

The changes to the taxation of furnished holiday lettings are significant and are likely to have a sizeable impact on those consultants owning property of this type.

Discuss your situation and intentions fully with your accountant who will be able to advise you further.