



## CAPITAL GAINS TAX: PRIVATE RESIDENCE RELIEF: CHANGES TO ANCILLARY RELIEFS

Issued 21 May 2019

ICAEW welcomes the opportunity to comment on the consultation **Capital Gains Tax: Private Residence Relief: changes to the ancillary reliefs** published by HMRC on 1 April 2019.

This response of 21 May 2019 has been prepared by the ICAEW Tax Faculty. Internationally recognised as a source of expertise, the Tax Faculty is a leading authority on taxation and is the voice of tax for ICAEW. It is responsible for making all submissions to the tax authorities on behalf of ICAEW, drawing upon the knowledge and experience of ICAEW's membership. The Tax Faculty's work is directly supported by over 130 active members, many of them well-known names in the tax world, who work across the complete spectrum of tax, both in practice and in business.

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## EXECUTIVE SUMMARY

1. We are concerned that the proposed legislation is retroactive with no provisions included to grandfather the change in legislation.
2. The consultation period at just over eight weeks is shorter than the government recommended 12 week consultation period.
3. We have no objections in principle to the reduction in the final exempt period to 9 months but there is a problem for people with homes which will not sell and this reduced final period will be exacerbated by the restrictions on lettings relief.
4. Although we like the simplicity of allocating the gain pro-rata over the period of ownership when the final period is shortened to nine months we think there should be an option to elect to use the actual valuation at the end of the nine month exemption to compare to the original base cost for the first calculation and to compare to the selling price for the second calculation.
5. We understand lettings relief was introduced to help alleviate a housing shortage and encourage letting of space in a main residence not required for the owner's occupation. This appears to be a need at present as much as when the relief was introduced, the increased limit for rent a room relief seems to confirm this. Having a lodger in the main home does not preclude private residence relief (PRR) SP14/80 so changing the lettings relief such that it only applies if there is shared accommodation is duplicating the statement of practice. The change will deter the accidental landlord and is likely to result in a reduction in the number of rental properties.
6. The stated policy aim could be better achieved by limiting lettings relief to a lower amount or for a limited time period, say two years, rather than shared occupation.
7. Many individuals own houses which were bona fide sole and main residences which they have been unable to sell due to the financial crisis and its legacy over the last ten years or so. The owners may have rented the property out when they could not sell it expecting to receive lettings relief so to impose an unforeseen and unexpected capital gains tax bill when a sale is eventually achieved is inappropriate.

## DETAILED RESPONSES

### ***Question 1: Do you have any comments about the reduction of the final period exemption?***

8. We are concerned that yet again retroactive legislation is being introduced. A house owner who vacated their home in October 2018 selling it in March 2020 will have no chargeable gain but if the sale is just a few days later in the new tax year there is potentially a chargeable gain attributable to the last nine months of ownership.
9. The final period relief is intended to allow a leeway reflecting that it is not always possible to sell one home simultaneously with the acquisition of a new one and the period has varied between 12 and 36 months since introduction.
10. We understand from the meeting that we attended with HMRC and HMT representatives that this is based on data from RICS which shows that the average time to sell a house is 19 weeks or four and a half months. We have not seen this data or the assumptions on which it is based.
11. However, averages can very obviously be deceptive. This may well be the mean average, but the median average may be very different. In addition, different types of houses will have different patterns for average sale time. As a general observation we feel that four and a half months does not reflect the average time to sell on transactions that we see as advisers.
12. Anecdotally we are aware that in some areas the period between going to market and selling is in excess of 18 months and in addition the value of the property has fallen considerably in this period. Under the current proposal that could result in a charge to capital gains tax for that final period despite the property actually falling in value.

13. Although we like the simplicity of allocating the gain pro-rata over the period of ownership when the final period is shortened to nine months we think there should be an option to elect to use the actual valuation at the end of the nine month exemption to compare to the original base cost for the first calculation and to compare to the selling price for the second calculation.
14. Given the uncertainties around Brexit and the impact on the property market, it seems an odd time to be reducing the final period exemption.
15. It would be possible to link the actual period of residence to the final period exemption such that the exemption could not exceed the period of residence, which would introduce a further safeguard against abuse, if this was perceived to be an issue.
16. We are pleased the 36 months exemption remains in place for those people going direct to a care/nursing home from their own home but we would like to see the 36 months extended to also include those people who move in with relatives as they are no longer able to live independently. This would also support the policy of care in the community rather than in care/nursing homes. Currently those who go from their own home to a care home via a relative/friend's home only get relief for the shorter period.

**QUESTION 2: Do you have any comments about the reform of lettings relief?**

17. The preamble to section 4 of the consultation document states that ‘Lettings relief was introduced in 1980 to ensure that people could let out spare rooms within their property on a casual basis without losing the benefit of PRR’, and goes on to add ‘however, in practice lettings relief extends much further than the original policy intention and also benefits those who let out a whole dwelling...’
18. This is a somewhat disingenuous explanation such that the position as stated in the preamble to the consultation is a change of policy and the revised legislation is to encapsulate that change.
19. Lettings relief is legislated in s223 (4) TCGA 1992 which refers to property which has at some point been the main residence of the owner and at some point “wholly or partly let”. This was inserted by s80 Finance Act 1980 which included the word “wholly” and is clearly not there accidentally. It is plainly within the existing framework that a property can be let completely at some point.
20. SP14/80 which was contemporaneous with the 1980 provision is clear that this applied at that time to people who let the whole of their homes as well as part. The original policy intention was clear in 1980 – that it was to also benefit those who let the whole of their homes. This attempt to reframe a statutorily given relief and its interpretation by the then Inland Revenue almost 40 years ago as a relief which is in some way being abused or ‘extend[ed] much further’ by taxpayers seems to be a starting point in bad faith.
21. The proposal is that lettings relief will only apply where there is shared occupation of the principal residence but SP14/80 and CG64311 already confirms that PRR is not lost when there is a lodger. As such we question that this measure is in accordance with “keeping people’s homes out of CGT”. It is our view that there is once again a conflation of revenue raising and mixed policy measures and that the restriction of the lettings relief does not adequately protect the so-called accidental landlords of whom there are still many.
22. The three legs limiting the relief with an absolute maximum relief of £40,000 prevents long term landlords from benefitting disproportionately. At present rates of tax the maximum tax saving is £11,200 per home owner.
23. We suggest that the stated policy aim would be better achieved by limiting lettings relief to a lower amount or for a limited time period, say two years, rather than shared occupation. If the maximum part of the period of ownership which could be covered by lettings relief was say two years, this allows there to be a meaningful relief where it is needed with only a low possibility of misuse. The shared occupation requirement will, in our view, reduce the relief to meaningless.

24. Many individuals own houses which were bona fide sole and main residences which they have been unable to sell due to the financial crisis and its legacy over the last ten years or so. To impose an unforeseen and unexpected capital gains tax bill when a sale is eventually achieved seems inappropriate.
25. We are concerned that example 4 suggests that a retroactive effect is anticipated. Although Eric's sale takes place in December 2020, if it has been let for three years prior to the sale, that is December 2017 i.e. well before this announcement was in contemplation. Taxpayers in Eric's situation, with a choice, may have taken a different decision had they realised there would be capital gains tax consequences. We object to retroactive effects of legislation where there is no anti abuse in point.
26. If the relief is to be so severely curtailed then, at the very least, the period qualifying for relief under existing rules which has already accrued, in the period up until 6 April 2020, if not protected by one of the remaining s223 permitted absences, should continue to be regarded as an exempt period to avoid the retroactive effect of the provisions. Over time the proportion will shrink so the cost should not be an undue one to the Exchequer and the advantage is fair and proper legislation.
27. As part of the changes the opportunity should be taken to tidy the provisions regarding permitted absences to bring them up to date and align them with other legislation such as the statutory residence test as regards when an individual is considered to be working abroad and what time is allowed working in the UK.
28. The requirement to have to return to live in the house after a permitted absence should be removed.

**QUESTION 3: Do you believe there is a case for legislating to ensure that the benefits of job related accommodation will continue to apply to personnel who organise accommodation through the Future Accommodation Model?**

29. If there is doubt that the benefits of job related accommodation will apply to personnel who organise accommodation through the Future Accommodation Model then legislation should be introduced. The protection should be extended to other sectors such as ministers of religion, police, oil rig workers, farmers etc and not just Ministry of Defence personnel.

**QUESTION 4: Do you have any comments on legislating these ESCs in their present form?**

30. ESC D21 is needed if an individual lives in a property in which they have no significant economic interest but owns another property and were unaware that the election was needed to exempt the property, the concession allows an election outside the two year window. Rather than legislate for the concession it may be simpler to exclude properties in which the individual has no significant economic interest from the scope of the PRR legislation. The law would then reflect what most people expect it be, there seems no sense in including a property within the scope for capital gains tax when the occupier has no significant economic interest and so cannot have a capital gain arising on it.
31. Non-residents liable to non-resident capital gains tax can make an election as to which property is their PRR outside the two year window; the two year time limit for making an election should be removed for UK residents.
32. ESC D49 is still required and so should be legislated but the outcome of the *HMRC v D Higgins [2018] UKUT 280 (TCC)* appeal may have a bearing on this. In particular, the outcome of the case notwithstanding the new legislation should deal with the less extreme, but virtually universal situation where there is a short gap of days or weeks between exchange and completion. At present there appears to be an unwritten concession not to restrict relief in these circumstances, but that is not correct in law.
33. ESC D49 covers the acquisition of land which could include purchase, gift or inheritance but just the purchase of a house; we suggest that on legislating the ESC that it should be extended to apply to acquired properties.

34. Care needs to be taken in translating ESC into legislation as the ESC are not interpreted in such a strict manner as legislation so the legislation will need to include all the nuances that are put into the ESC.

***QUESTION 5: Should the receiving spouse always inherit the ownership period and the use to which the property had been put in the past regardless of whether it is a main residence at the time of transfer?***

35. We support the suggested change as this should eliminate the anomalies of the present legislation. The relief should operate to reflect the reality of the use of the property by either spouse/civil partner through the entire ownership period.
36. It would be equitable to always transfer the history of ownership as well as the ownership when transferring property between spouses/civil partners and this is probably what most people would expect the outcome to be. We do not think that use of PRR as in example 6 in the consultation was an intended use of PRR.

## APPENDIX 1

### ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory:** tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. **Certain:** in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. **Simple:** the tax rules should aim to be simple, understandable and clear in their objectives.
4. **Easy to collect and to calculate:** a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. **Properly targeted:** when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. **Constant:** Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. **Subject to proper consultation:** other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. **Regularly reviewed:** the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. **Fair and reasonable:** the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. **Competitive:** tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see <https://goo.gl/x6UjJ5>).