Response from ICAS

Capital Gains Tax: Private Residence Relief: changes to the ancillary reliefs

31 May 2019

About ICAS

1. The following submission has been prepared by the ICAS Tax Board. The Board, with its five technical Committees, is responsible for putting forward the views of the ICAS tax community, which consists of Chartered Accountants and ICAS Tax Professionals working across the UK and beyond, and it does this with the active input and support of over 60 committee members. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants and we represent over 21,000 members working across the UK and internationally. Our members work in all fields, predominantly across the private and not for profit sectors.

General comments

2. ICAS welcomes the opportunity to contribute to the consultation Capital Gains Tax: Private Residence Relief: changes to the ancillary reliefs issued by HMRC and HM Treasury on 1 April 2019.

3. The length of time it takes to sell a house varies according to market conditions. It would therefore make sense to provide that the length of the final period exemption should be subject to periodic review – and that it could easily be amended by statutory instrument – to avoid it contributing to a problematic stagnation of the property market in future.

4. The shorter final period exemption could cause problems for couples divorcing or dissolving a civil partnership. Our response to Question 1 below suggests a possible solution.

5. Consideration should be given to allowing some relief in respect of the letting of a property before 6 April 2020 which would have qualified under the current rules. This is discussed in more detail in our response to Question 2 below.

6. In legislating ESC D49 we suggest that some amendments should be considered, to reflect the decision in a recent First Tier Tribunal case (Mr George McHugh & Mrs Mary McHugh v HMRC). and to address the problem illustrated by another recent Upper Tier Tribunal case (HMRC v Desmond Higgins). This is discussed in more detail in our response to Question 4 below.

Specific questions

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

7. We welcome the retention of the longer final period exemption (36 months) for those with a disability or moving into care.

8. The consultation recognises that the intention of the exemption is to provide a CGT free period in which to sell a dwelling after leaving it. The length of time it takes to sell a house varies according to the state of the property market and other factors. In normal circumstances 9 months would probably be sufficient in the majority of cases.

9. However, there could be periods when it takes longer to sell properties; we understand, for example, that Brexit uncertainty and increased stamp duty rates are currently causing a market slowdown. A shorter final period exemption (combined with the proposed changes to lettings relief) could therefore act as a disincentive to certain sellers, with adverse consequences for all property buyers.

10. We assume that the 6 April 2020 date for the introduction of the reduced period is fixed, regardless of the outcome of Brexit. However, it would make sense to provide that the length of the final period exemption should be subject to periodic review – and that it could easily be amended by statutory instrument, if evidence emerges that it is contributing towards a problematic stagnation of the property market in the medium to long term.

11. The shorter final period exemption could cause problems for couples who are divorcing or dissolving a civil partnership. In many of these cases a period of longer than 9 months is likely to be required. Section 225B TCGA 1992 already recognises that the existing period of 18 months may be insufficient in divorce/civil partnership cases - an election under s225B is potentially relevant where one spouse or civil partner is transferring an interest in the matrimonial/civil partnership home to the other spouse or partner.

12. It would be helpful to introduce a similar election which would be available to the spouse/civil partner who has moved out of the matrimonial/civil partnership home in cases where the property is ultimately sold, rather than where the interest is transferred – and the reduced final period of 9 months is insufficient to permit arrangements for the divorce and sale to be finalised.

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

13. Paragraph 4.1 of the consultation states that lettings relief was introduced in 1980 "to ensure people could let out spare rooms within their property on a casual basis without losing the benefit of PRR". Paragraph 4.2 goes on to say that in practice it 'extends much further than the original policy intention and also benefits those who let out a whole dwelling that has at some stage been their main residence."

14. If this was the original intention behind lettings relief it is difficult to see why the long-standing legislation did not reflect that intention – or why it has not been amended before now. Many property owners will have decided to let whole properties, which were at some time occupied as their private residence, on the basis that lettings relief would be available; the change is therefore likely to be regarded as unfair, unless the legislation allows for some relief to be given in respect of letting before 6 April 2020 which would have qualified under the current rules.

15. HMRC will need to ensure that this significant change is widely publicised ahead of April 2020 to enable those affected to make informed decisions. This change, together with the change to the final period exemption and the restriction of relief for finance costs (which is being phased in), may mean that some landlords decide to sell rather than continuing to let a property. Combined with Brexit, this could cause some disruption in the property market in the run up to April 2020. This effect could be mitigated, as outlined above, by allowing some relief for periods of letting before 6 April 2020 which would have qualified under the current rules.

16. In the longer term there will also need to be adequate guidance with self-assessment returns to highlight that the long-standing relief is no longer available in cases where the whole property has been let.

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?

17. Yes – this appears to be a sensible proposal.

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

18. We have no comments on the proposed approach to legislating ESC D21.

19. For ESC D49 we suggest that rather than legislating the concession in its present form, some amendments should be considered.

20. ESC D49 is relevant where there is a short delay in taking up residence in a property – in three specified scenarios. One of these relates to cases where an individual acquires land on which they have a house built - which is then used as their only or main residence.

21. The concession allows the individual to treat the property as their only or main residence in the period before they are able to move into the property, provided certain conditions are met. One of the conditions is that the period does not exceed one year – which can be extended to 2 years where there are good reasons for exceeding one year.

22. A maximum period of two years will sometimes be inadequate to allow self-builders to complete construction of the residence. This was illustrated by the recent First Tier Tribunal case (Mr George McHugh & Mrs Mary McHugh v HMRC). As outlined in the case HMRC's practice is not to allow any relief where the two year period is exceeded. The FTT decided that, taking into account the intention behind the concession, the relief should be available for two years ie only the pre-occupation period in excess of two years would not qualify for relief.

23. FTT decisions are not binding but as the concession is being legislated, we believe that it would make sense to adjust the relief to reflect the decision in McHugh and to allow relief for a maximum of two

years – with only any excess pre-occupation period over two years failing to qualify. This would reflect the intention of the concession which is presumably to encourage – or at least not to disadvantage – those who want to construct their own home. This appears to be in line with the wider government policy of facilitating home ownership.

24. In the interests of simplicity, we suggest that the same approach should apply to the other two scenarios in the concession – delay in selling the previous residence and delay in taking up residence due to alterations or redecorations. In view of the requirement for there to be good reasons for any delay over one year we do not see scope for abuse.

25. It would also be helpful in legislating the concession to address another scenario – delay in taking up residence where a property is reserved off-plan, but construction delays result in the property not being available for occupation for a significant period. This was illustrated by another recent case in the Upper Tier Tribunal (HMRC v Desmond Higgins). The delay in that case was probably unusually long but in principle we cannot see why this scenario should be treated differently to the one in McHugh. The Upper Tier Tribunal stated that ESC D49 would not assist the taxpayer in off-plan purchase cases (even if the delay in occupation had been shorter) because the delay was between exchange and completion.

26. We therefore suggest that when legislating ESC D49 the relief should be extended to cover off-plan purchases where completion/occupation is delayed by construction delays – applying the same conditions as outlined above (ie with a maximum pre-occupation period of two years qualifying for relief).

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?

27. This proposed change seems broadly sensible and would address the unfairness in Example 7. We wonder how often the issue in Example 6 would arise in practice, given the legal consequences of transferring the entire property, particularly if the marriage later broke down – but again the proposal seems to address the issue.

28. It may, however, be the case that whilst addressing some existing unfair outcomes, the proposed change could give rise to new ones.