

OFFSHORE TRUSTS AND NON-DOMS

An opportunity for advisers and trustees

STAMP DUTY LAND TAX

Things people do wrong

BUSINESS/NON-BUSINESS USE OF PROPERTY

Avoiding a splitting headache

SERIAL TAX AVOIDANCE

Why advisers may consider notifying all clients

TAILPIECE

Intangible assets

MEMORY JOGGER

ABOUT TAX SUPPORT FOR PROFESSIONALS

As well as publishing Tax Insight, BDO offers a range of tax support services designed to give professional firms the benefit of another tax partner without the cost. Find out more by visiting our website, www.bdo.co.uk/tsp.

TAXLINE/VATLINE

OUR PAY-AS-YOU-GO SERVICE.

You can contact any of our advisers at any time. If it is possible to provide you with an immediate answer to your query over the telephone we would charge at a special discounted rate of £60 (plus VAT) per 12 minute unit or part thereof.

You can use our dedicated advice lines to obtain fast telephone advice:

Taxline 0845 356 0006
VATline 0845 356 0007

Short queries relating directly to an article may be answered with our compliments. For administrative queries, please call 020 7893 3627

**BUSINESS/NON-BUSINESS USE OF PROPERTY
AVOIDING A SPLITTING HEADACHE**



CHRIS HOLMES

chris.holmes@bdo.co.uk

BY CHRIS HOLMES

A Senior Manager with BDO LLP and a consultant on BDO's Tax Support for Professionals Taxline.

There are several areas where it is necessary to consider how items of property-related income and expenditure should be split between business and non-business use, and whether mixed use properties qualify for certain reliefs, for the purposes of both direct and indirect taxes. This article highlights some of the issues that arise, and looks at recent developments and case law.

INCOME TAX/CORPORATION TAX

HOMES USED PARTLY FOR BUSINESS PURPOSES

A proportion of household costs can be claimed as a deduction for business purposes.

Option 1: The simplest method, available to unincorporated businesses with less than 25 hours per month business use of the home, and which involves no record-keeping or apportionment calculations, is the HMRC-approved flat rate deduction.

The flat rates, depending on the amount of business use, are:

Hours of business use per month	Flat rate per month
25-50	£10
51-100	£18
101 and more	£26



OFFSHORE TRUSTS AND NON-DOMS

An opportunity for advisers and trustees

STAMP DUTY LAND TAX

Things people do wrong

BUSINESS/NON-BUSINESS USE OF PROPERTY

Avoiding a splitting headache

SERIAL TAX AVOIDANCE

Why advisers may consider notifying all clients

TAILPIECE

Intangible assets

MEMORY JOGGER

ABOUT TAX SUPPORT FOR PROFESSIONALS

As well as publishing Tax Insight, BDO offers a range of tax support services designed to give professional firms the benefit of another tax partner without the cost. Find out more by visiting our website, www.bdo.co.uk/tsp.

TAXLINE/VATLINE

OUR PAY-AS-YOU-GO SERVICE.

You can contact any of our advisers at any time. If it is possible to provide you with an immediate answer to your query over the telephone we would charge at a special discounted rate of £60 (plus VAT) per 12 minute unit or part thereof.

You can use our dedicated advice lines to obtain fast telephone advice:

Taxline 0845 356 0006
VATline 0845 356 0007

Short queries relating directly to an article may be answered with our compliments. For administrative queries, please call 020 7893 3627

This will be a convenient and acceptable method for many small businesses, including those where there is only a modest use of the home as an office. In addition to the flat rate, the business proportion of telephone and internet costs can be claimed.

Option 2: If there is only minor business use of the home, HMRC will accept a reasonable estimate of the business proportion consistent with the underlying facts.

Option 3: Where the business proportion of actual household costs is higher than the flat rate amounts, the business proportion can be calculated in a reasonable manner.

The main principles to bear in mind are:

- Would the expenditure have been incurred if no business was carried on at the property (wholly and exclusively)?
- Business expenditure does not have to be separately billed
- Part of the home need not be used solely for business purposes.

Generally, when considering the allowability of an expense a distinction is made between fixed costs and running costs:

Fixed costs are not generally allowable unless they are in respect of part of the property used exclusively for the business. There would be a strong case to claim a proportion of fixed costs where a larger property is specifically occupied due to the needs of the business.

Note: principal private residence relief for capital gains tax purposes (see below) may be lost if fixed costs are claimed.

Running costs are generally allowable to the extent that the expense is greater than it would have been if the business was carried on elsewhere; eg if no-one had been present in the property, it need not have been heated.

The factors that HMRC accepts can be taken into account in apportioning expenses include area, usage and time. The following table sets out when each might be appropriate:

Factor	Comments	When appropriate
Area	The proportion in terms of area of the home that is used for business purposes. Apportionment can be done by reference to the number of rooms or the floor area.	Apportioning fixed costs - where part of home used <u>exclusively</u> for the business
Usage	The amount of metered or measureable services such as electricity, gas or water that is consumed.	Apportioning running costs
Time	The length of time the expense is incurred for business purposes. <ul style="list-style-type: none"> • Business proportion of running costs: <i>Time room used for business each day</i> 	Apportioning fixed costs – where part of home used exclusively for the business for only part of the time
	<ul style="list-style-type: none"> • Business proportion of fixed costs: <i>Hours used for business each day</i> 24 	

OFFSHORE TRUSTS AND NON-DOMS

An opportunity for advisers and trustees

STAMP DUTY LAND TAX

Things people do wrong

BUSINESS/NON-BUSINESS USE OF PROPERTY

Avoiding a splitting headache

SERIAL TAX AVOIDANCE

Why advisers may consider notifying all clients

TAILPIECE

Intangible assets

MEMORY JOGGER

ABOUT TAX SUPPORT FOR PROFESSIONALS

As well as publishing Tax Insight, BDO offers a range of tax support services designed to give professional firms the benefit of another tax partner without the cost. Find out more by visiting our website, www.bdo.co.uk/tsp.

TAXLINE/VATLINE

OUR PAY-AS-YOU-GO SERVICE.

You can contact any of our advisers at any time. If it is possible to provide you with an immediate answer to your query over the telephone we would charge at a special discounted rate of £60 (plus VAT) per 12 minute unit or part thereof.

You can use our dedicated advice lines to obtain fast telephone advice:

Taxline 0845 356 0006
VATline 0845 356 0007

Short queries relating directly to an article may be answered with our compliments. For administrative queries, please call 020 7893 3627

In its Business Income Manual, at **BIM47820**, HMRC comments as follows with regard to specific items of fixed and running costs:

FIXED COSTS

Allowable cost	Comments
Insurance	If the business use is covered by a separate policy, then the cost of that policy is allowed in full, with no part of the household policy being allowed. Otherwise, an appropriate part of the premium can be allowed.
Council Tax	In principle, appropriate proportion allowable where other property-based expenses are deductible.
Mortgage interest	An appropriate part of the mortgage interest (but not, of course, capital) is an allowable deduction for part of the property solely used by the business
Rent	Part of the rent is an allowable expense when the home is rented and part is used solely for business purposes.
Repairs and maintenance	A proportion of the cost of general household repairs and maintenance is allowable in line with the proportion that the house is used solely for the business. Examples include the general redecoration of the exterior or repairs to the roof. Repairs that relate solely to part of the house that is not used for the business, such as decorating a room not used for the business, are not allowable. Equally if a room is used solely for business purposes then the cost of redecoration that room is wholly allowable.

RUNNING COSTS

Allowable cost	Comments
Cleaning	Depending on the facts, a higher proportion of costs may be attributable to either business or domestic use.
Heat, light and power	The allowable proportion should reflect the facts of usage, taking into account the number and nature of any power consuming items involved.
Telephone	The cost of business calls, plus a proportion of the line rental (based on the ratio of business use to total use) is allowable. Where private use is not significant, the full cost can be claimed as a business expense.
Broadband	Expenditure is allowable to the extent that the connection is used for trade purposes, with the same approach as for telephone rentals where there is 'mixed' (trade/non-trade) use. Where private use is not significant, the full cost can be claimed as a business expense.

There can be practical issues in identifying the running costs to apportion where different services are combined under a single contract, eg a telephone, broadband and television package.

OFFSHORE TRUSTS AND NON-DOMS

An opportunity for advisers and trustees

STAMP DUTY LAND TAX

Things people do wrong

BUSINESS/NON-BUSINESS USE OF PROPERTY

Avoiding a splitting headache

SERIAL TAX AVOIDANCE

Why advisers may consider notifying all clients

TAILPIECE

Intangible assets

MEMORY JOGGER

ABOUT TAX SUPPORT FOR PROFESSIONALS

As well as publishing Tax Insight, BDO offers a range of tax support services designed to give professional firms the benefit of another tax partner without the cost. Find out more by visiting our website, www.bdo.co.uk/tsp.

TAXLINE/VATLINE

OUR PAY-AS-YOU-GO SERVICE.

You can contact any of our advisers at any time. If it is possible to provide you with an immediate answer to your query over the telephone we would charge at a special discounted rate of £60 (plus VAT) per 12 minute unit or part thereof.

You can use our dedicated advice lines to obtain fast telephone advice:

Taxline 0845 356 0006

VATline 0845 356 0007

Short queries relating directly to an article may be answered with our compliments.

For administrative queries, please call

020 7893 3627

CAPITAL GAINS TAX

HOMES USED PARTLY FOR BUSINESS PURPOSES

Principal private residence (PPR) relief is not available for part of a private residence that is used exclusively for business purposes (S 224(1) TCGA 1992), the gain being apportioned in a just and reasonable manner (and not necessarily in the same way for income tax or corporation tax purposes).

As HMRC considers that income tax relief for fixed costs is only available if part of the house is used exclusively for the business, generally where fixed costs have been claimed, HMRC considers that PPR relief should be restricted on disposal of the property.

An apportionment based on the number of rooms and, if applicable, the length of time during the period of ownership that they were used for business purposes, will generally be acceptable. If the rooms used for business purposes are smaller than others, it will be beneficial to weigh the apportionment accordingly.

Relief is not restricted where a room is used partly for business purposes, eg the use of a kitchen for business purposes in a bed and breakfast business. In its Capital Gains Manual at [CG64663](#), HMRC also confirms that "occasional and very minor residential use" of a room used for business purposes, eg to keep private possessions, will be disregarded.

PARTICULAR CASES:

Farmhouses: In its Capital Gains Manual at [CG64680](#), HMRC states: "Whether any part of a farmhouse is used exclusively for business purposes is a question of fact. In what is probably the normal case, parts of the house, for example, the farm kitchen and dining room are used for business but are also used domestically. So each of these rooms should be treated as part of the residence regardless of the fact that the farmer receives an allowance for his or her business use of the premises in the computation of the trading profits.

If there is exclusive use, for example, of an office or dairy, then an apportionment is necessary and the relief should be regarded as extending only to that part of the farmhouse which was occupied partly or wholly as a residence."

Guest houses: In the Owen v Elliott case ([1990] STC 469), the Court of Appeal decided that if part of a main residence is commercially let on a bed and breakfast basis, that letting qualifies for relief under the lettings exemption in S 223(4) TCGA 1992 – the part of the property that is let does not have to be the home of the person occupying it.

Outbuildings: the general principles outlined above apply where an outbuilding is used exclusively for business purposes, eg a garage, workshop or temporary structure. A just and reasonable apportionment of the disposal proceeds, and any relevant capital costs, must be attributed to the outbuilding.

INHERITANCE TAX

BUSINESS PROPERTY RELIEF

Business property relief (BPR) tends to be the main inheritance tax (IHT) issue for which it is necessary to consider the split or balance between business and non-business use.

BPR is available in respect of "relevant business property", which includes:

- property consisting of a business or interest in a business
- shares or securities of quoted or unquoted companies, subject to detailed conditions
- land or buildings used wholly or mainly for the purposes of a business carried on by a company of which the transferor then had control or by a partnership of which he then was a partner.

In each of the above cases, BPR is not available if the business or interest in the business in question consists wholly or mainly of dealing in securities, stocks or shares, land or buildings or making or holding investments. For BPR purposes it is therefore an 'all or nothing' matter whether a business can overcome the "wholly or mainly" exclusion, depending on the facts and circumstance.

OFFSHORE TRUSTS AND NON-DOMS

An opportunity for advisers and trustees

STAMP DUTY LAND TAX

Things people do wrong

BUSINESS/NON-BUSINESS USE OF PROPERTY

Avoiding a splitting headache

SERIAL TAX AVOIDANCE

Why advisers may consider notifying all clients

TAILPIECE

Intangible assets

MEMORY JOGGER

ABOUT TAX SUPPORT FOR PROFESSIONALS

As well as publishing Tax Insight, BDO offers a range of tax support services designed to give professional firms the benefit of another tax partner without the cost. Find out more by visiting our website, www.bdo.co.uk/tsp.

TAXLINE/VATLINE

OUR PAY-AS-YOU-GO SERVICE.

You can contact any of our advisers at any time. If it is possible to provide you with an immediate answer to your query over the telephone we would charge at a special discounted rate of £60 (plus VAT) per 12 minute unit or part thereof.

You can use our dedicated advice lines to obtain fast telephone advice:

Taxline 0845 356 0006

VATline 0845 356 0007

Short queries relating directly to an article may be answered with our compliments.

For administrative queries, please call

020 7893 3627

Some of the most contentious cases involving land and buildings have been those concerning:

- **Caravan parks:** Several cases have come before the Tribunals and Courts, with decisions in favour of both the taxpayers and HMRC, depending on the facts and circumstances.

- The leading case in favour of the taxpayer is *George & Loochin (Stedman's Executors) v CIR* [2003] EWCA Civ 1763, in which the Court of Appeal decided that the holding of property as an investment was only one component of the business, and the Special Commissioner was entitled to find, on the facts, that it was not the main component. The Special Commissioner decided that the main pointer was the fact that "...72% of the site fees goes in overheads (excluding the director's fees) most of which relate to the provision of upkeep of the common parts. In my view the services element predominates. On this aspect the very business of the company is the provision of services and not the business of holding investments."

As the investment activities of caravan storage and rental income represented minority percentages of turnover, gross profit and net profit, the Special Commissioner did not find it necessary to consider the business 'in the round', in contrast to other cases

The Court of Appeal agreed with that approach, and found it difficult to see any reason why an active family business should be excluded from BPR merely because a necessary component of its profit-making activity is the use of land.

- One of the leading cases in favour of HMRC is *Weston (exor of Weston, decd) v IRC* [2000] STC 1064, which involved a wholly residential caravan park, with an income deriving mainly from pitch fees and caravan sales. The High Court considered that the Special Commissioner had been correct to look at the matter in the round, finding that caravan sales were ancillary to pitch fees, and that the business of the company consisted mainly in making or holding investments.

- **Furnished holiday lettings:** HMRC maintains that "In most cases the level of services provided will not be sufficient to weigh the balance away from 'investment'" ([IHTM 25276](#)). The leading case is [HMRC v Personal Representatives of Nicolette Vivian Pawson](#), in which the Upper Tribunal ruled in favour of HMRC, stating that:

- the starting point was the proposition that the owning and holding of land in order to obtain an income from it is generally to be characterised as an investment activity
- the relevant test was not the degree or level of activity, but rather the nature of the activities which are carried out.

On the above basis, the provision of additional services including a cleaner/ caretaker, space heating and hot water, a television and telephone, being on call to deal with queries and emergencies, and more minor matters such as the replenishment of cleaning materials, and the provision of a welcome pack, were not sufficient to prevent the business from being treated as wholly or mainly one of making or holding investments.

- **Commercial property letting:** Similar considerations to those in relation to furnished holiday lettings apply. In the [Trustees of David Zetland Settlement v HMRC case](#), where additional services included the cleaning of common parts, post sorting and delivery, reception, free food and drink at socials, and gift vouchers, the First Tier Tribunal followed the Pawson decision and decided in favour of HMRC. For further information, see [Tax Insight, June 2013](#).

DEDUCTIBILITY OF LOANS

Following the introduction of the FA 2013 restrictions on deductibility for IHT purposes of new loans taken out from 6 April 2013, HMRC confirmed that where a liability has been incurred to acquire a property of which only part qualifies for relief, HMRC's view is that for practical reasons the liability should be split in proportion to the values at the date of acquisition (see paragraph 7.8 of [HMRC's response to comments on Sch 36 FA 2013](#)).

OFFSHORE TRUSTS AND NON-DOMS

An opportunity for advisers and trustees

STAMP DUTY LAND TAX

Things people do wrong

BUSINESS/NON-BUSINESS USE OF PROPERTY

Avoiding a splitting headache

SERIAL TAX AVOIDANCE

Why advisers may consider notifying all clients

TAILPIECE

Intangible assets

MEMORY JOGGER

ABOUT TAX SUPPORT FOR PROFESSIONALS

As well as publishing Tax Insight, BDO offers a range of tax support services designed to give professional firms the benefit of another tax partner without the cost. Find out more by visiting our website, www.bdo.co.uk/tsp.

TAXLINE/VATLINE OUR PAY-AS-YOU-GO SERVICE.

You can contact any of our advisers at any time. If it is possible to provide you with an immediate answer to your query over the telephone we would charge at a special discounted rate of £60 (plus VAT) per 12 minute unit or part thereof.

You can use our dedicated advice lines to obtain fast telephone advice:

Taxline 0845 356 0006
VATline 0845 356 0007

Short queries relating directly to an article may be answered with our compliments. For administrative queries, please call 020 7893 3627

VAT

1. General principles: claiming input tax on expenditure on acquiring or constructing mixed use land or buildings

a) Expenditure of at least £250,000

Expenditure of at least £250,000 is dealt with under the capital goods scheme. In such cases, where the land or buildings are used to make both taxable and exempt supplies, a proportion of the input tax on the expenditure can be claimed under the partial exemption scheme rules. The use of the property and the VAT recovery position must be revisited annually for the first ten years of ownership, and an annual adjustment calculation must be completed in the VAT return. If there has been an increase or decrease in the taxable use during the year, there will be VAT to be claimed from, or repaid to, HMRC respectively. If the property is used for entirely taxable purposes in the first ten years of ownership, there would be no VAT adjustment required to the original VAT recovery position.

b) Expenditure of under £250,000

The expenditure must be apportioned using a fair and reasonable method. Common examples of acceptable methods are:

- Percentage of premises used for business purposes
- Percentage of income attributable to business supplies
- Percentage of total expenditure attributable to business supplies
- Percentage of time spent by staff on business activities
- Percentage of floor space attributable to business activities

2. Special cases

Supplies made by pubs with let residential accommodation

For many years, HMRC's policy with regard to supplies made by tenanted pubs with let residential accommodation has been to apportion the mixed supply 90:10 to the commercial and domestic elements respectively. This is based on a suggested split by the Brewers Society which HMRC neither formally agreed nor dissented from.

In the recent [David John Matthews and Pamela Ella Matthews v HMRC case](#), the taxpayers argued that the 90:10 split was inappropriate because the pub was sold shortly after it was purchased, without any commercial sales having been made, due to the tenant having failed to make the rental payments.

The taxpayers therefore suggested that the split of the sale proceeds should be 100:0 in favour of the residential element, in which case no output tax would be due. HMRC maintained that the split should be 90:10 in favour of the commercial element, in accordance with its established approach.

The First-tier Tax Tribunal (FTT) reviewed the relevant legislation and case law and decided that in the circumstances the appropriate basis for apportionment should be the floor space of the respective areas, which it found to be two thirds to one third in favour of the commercial element.

This confirms that a fair apportionment should always be sought where the 90:10 approach is inappropriate for any reason and, as this case shows, it is possible to effect a substantial VAT output tax saving.

Property developers purchasing pubs for redevelopment

We are seeing many instances of developers buying pubs for conversion into dwellings. In situations where the buyer is not able to disapply the vendor's option to tax prior to exchange, in many cases the VAT incurred is wholly or partly irrecoverable in the hands of the developer, and any reduction in the output tax chargeable by the seller will provide a welcome relief to the buyer who is going to make VAT exempt supplies, or VAT exempt use, of the property. In recent VAT tribunal cases such as [Languard New Homes v HMRC](#) and [Alexandra Countryside Investments Ltd v HMRC](#), there has been some taxpayer success in securing zero-rating for certain converted commercial areas that also incorporate part of the former pub residential area, where such conversion works result in a changed number of new residential dwellings. It should be noted that these case outcomes have not yet been incorporated into HMRC's published guidance, and HMRC has appealed the Languard New Homes decision, to be heard by the Upper Tribunal in June 2017.

Considering the VAT consequences of the intended new configuration of a converted property from the outset is recommended.

HOW WE CAN HELP YOU

For more information about how we can help you and your clients please contact:

JEFF WEBBER

jeff.webber@bdo.co.uk
+44 (0)207 893 3578

MALCOLM PENGELLY

malcolm.pengelly@bdo.co.uk
+44 (0)207 893 2936

ABOUT BDO

BDO is the world's fifth largest accounting network with over 68,000 partners and staff with more than 1,400 offices in over 158 countries (including exclusive alliances of BDO Member Firms).

BDO LLP

55 Baker Street
London W1U 7EU

t: +44 (0)20 7486 5888
f: +44 (0)20 7487 3686
w: www.bdo.co.uk

This publication has been carefully prepared, but it has been written in general terms and should be seen as containing broad statements only. This publication should not be used or relied upon to cover specific situations and you should not act, or refrain from acting, upon the information contained in this publication without obtaining specific professional advice. Please contact BDO LLP to discuss these matters in the context of your particular circumstances. BDO LLP, its partners, employees and agents do not accept or assume any responsibility or duty of care in respect of any use of or reliance on this publication, and will deny any liability for any loss arising from any action taken or not taken or decision made by anyone in reliance on this publication or any part of it. Any use of this publication or reliance on it for any purpose or in any context is therefore at your own risk, without any right of recourse against BDO LLP or any of its partners, employees or agents.

BDO LLP, a UK limited liability partnership registered in England and Wales under number OC305127, is a member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms. A list of members' names is open to inspection at our registered office, 55 Baker Street, London W1U 7EU. BDO LLP is authorised and regulated by the Financial Conduct Authority to conduct investment business.

BDO is the brand name of the BDO network and for each of the BDO member firms.

BDO Northern Ireland, a partnership formed in and under the laws of Northern Ireland, is licensed to operate within the international BDO network of independent member firms.

Copyright © 2020 BDO LLP. All rights reserved. Published in the UK.

ISSN 2056-7332

www.bdo.co.uk