



HM Revenue
& Customs

Reform to the Wear and Tear Allowance

Summary of responses
9 December 2015

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1. Introduction

Background to the consultation

- 1.1 Landlords (including company landlords) of fully furnished residential properties can elect to claim a tax relief for wear and tear on furnishings of 10 per cent of the net rent received in the property business.
- 1.2 The Wear and Tear Allowance is not available to those property businesses that rent part furnished or unfurnished property.
- 1.3 The Wear and Tear Allowance gives relief even where expenditure is not incurred or where less expenditure is incurred than the relief given. The allowance is also limited to 10 per cent, even where the landlord incurs higher costs in that year.
- 1.4 The Wear and Tear Allowance is dependent on the amount of rental income received. This has the consequence that where rental income is higher the allowance is higher so that similar properties in different parts of the country will attract different levels of Allowance despite potentially having incurred the same expenditure.
- 1.5 The Government announced that from April 2016 the Wear and Tear Allowance will be replaced with a relief that enables all landlords of residential dwelling houses to deduct the costs they actually incur on replacing furnishings in the property. This change aims to give relief for expenditure on replacing furnishings to a wider range of property businesses and to provide a more consistent and fairer way of calculating taxable profits that is based on landlords' economic costs.
- 1.6 HMRC published a consultation that invited comments on the scope of the new relief, the amount of the relief and whether there were any additional impacts that had not been considered in the impact assessment. The consultation ran for 12 weeks and closed on 9 October.

The responses

- 1.7 The Government has received 170 formal responses to the consultation, including 137 from individuals.
- 1.8 During the consultation period, HMRC and HMT officials also met with a range of stakeholders, including accountants, lawyers and representative groups. A full list of representative bodies and professional advisors that responded to the consultation is included at Annexe A.
- 1.9 The Government would like to thank respondents for taking the time to submit helpful written responses, and for the input of advisors and representative bodies at meetings.

2. Responses

- 2.1 Although the question of whether to reform the Wear and Tear Allowance was not covered in the consultation, many respondents expressed support for maintaining a Wear and Tear Allowance, principally because they saw it as simple.
- 2.2 Equally, a significant number of stakeholders agreed with the Government that the Wear and Tear Allowance was not fair, both as it only applies to landlords of fully furnished properties and because it provides relief where no expenses have been incurred. The decision to provide some form of relief for landlords of unfurnished and part-furnished properties was particularly welcomed.
- 2.3 The Government has carefully considered the different ways in which a relief based on actual expenditure could be designed and implemented, so that all landlords can benefit from it and it relates closely to the landlord's economic position. Following the requests to retain the Wear and Tear Allowance, the design has also focused on minimising complexity.

Scope of the new replacement furniture relief

Initial costs

- 2.4 The consultation document explained that the new relief will only apply to the replacement of furnishings and that the initial cost of furnishing a property would not be included.
- 2.5 11% of respondents, including some representative groups, commented that the relief should be extended to the initial cost of furnishings. They argued that this would be more representative of landlords' economic costs and that it would give more consistency across property businesses because commercial property businesses obtain relief for the initial cost of furnishings by way of capital allowances.
- 2.6 Moreover, 6% of all respondents suggested that relief for initial costs would be best achieved by extending the capital allowances regime to residential property.

2.7 **Government response:** The Government has considered the issue of providing relief for initial costs. But this would require additional rules to prevent relief being given for personal use of the furniture, based on the market value of the furniture.

2.8 The Government has also considered whether the capital allowances regime should be extended to landlords. This would bring the requirement to make balancing adjustments based on the original cost of the asset once it stopped being used in the business, and to pool amounts once the annual investment allowance limit is reached.

2.9 On balance, the Government has decided that moving from the Wear and Tear Allowance to a system that requires adjustments for personal use or an understanding of the capital allowances regime would introduce unacceptable complexity and administrative burdens for these landlords. Therefore, the Government has decided to allow relief only for the costs of replacing furniture.

Transitional provisions

2.10 Some respondents argued that transitional arrangements should be provided for.

2.11 Some argued that because the Wear and Tear Allowance was generous in order to account for future replacements, claimants of the Wear and Tear Allowance should not receive such generous relief during a transitional period.

2.12 Others suggested that those incurring significant recent expenditure would not yet have been fully compensated by the Wear and Tear Allowance and should be able to claim more generous relief during a transitional period.

2.13 Landlords of part-furnished and unfurnished properties have been unable to claim any relief for replacing furnishings since April 2013, following the withdrawal of extra-statutory concession B47. Some respondents argued that these landlords should receive relief for the costs incurred in the interim period.

2.14 **Government response:** The Government has considered what transitional provisions could be introduced. Providing different transitional provisions based on different circumstances or levels of expenditure in previous years would introduce considerable complexity. More simplified provisions would also favour some taxpayers that had benefited from the generous Wear and Tear Allowance.

2.15 On this basis, the Government believes that the need to provide a simple relief without favouring those whose Wear and Tear Allowance received was greater than the expenses they had incurred outweighs the benefit of any transitional provisions. The Government has therefore decided not to introduce transitional provisions.

Amount of the relief

Improvements

2.16 The consultation document proposed that the cost of the replacement asset that represents an improvement on the old asset would be excluded from the new replacement relief, in line with the policy that relief for the initial costs of assets will not be given.

- 2.17 The cost of the nearest modern equivalent of the old asset would be deductible in full to accommodate changes in technology.
- 2.18 26% of respondents expressed concern that this creates uncertainty. It may not be clear what constitutes an improvement if the item has some minor new features or is of an improved quality.
- 2.19 The majority of stakeholders HMRC met with were of the view that although excluding improvements generated some uncertainty, it would be simpler for landlords to operate than a system that gives relief for initial costs, but requires them to make adjustments, based on the market value of assets, when they stop being used in the business.

2.20 **Government response:** Opinion was divided on the extent of the complexity excluding improvements brings. The Government remains of the view that this rule is necessary to make the relief fair, so that the initial cost of additional functionality is not available in the same way as the initial cost of assets.

2.21 To minimise uncertainty, HMRC will produce comprehensive guidance to enable taxpayers to apply this rule to their circumstances, particularly around what constitutes a modern equivalent.

Disposal proceeds

- 2.22 The consultation document proposed that the new rules would give relief for the cost of the replacement asset, less any proceeds received from the old asset that is being replaced.
- 2.23 21% of respondents viewed this as an unnecessary complexity in the new regime, on the basis that the majority of assets would have no second-hand value when replaced.
- 2.24 Respondents argued that in some cases, there was actually a cost in disposing of old assets and proposed that these disposal costs should be included in the new relief.

2.25 **Government response:** Having considered this issue the Government believes that this rule should not introduce undue complexity, particularly if no proceeds are received in the majority of cases. This marginal additional complexity is outweighed by the aim to mirror the landlord's economic expenditure as far as possible. The Government has therefore decided that this rule will form part of the design of the relief.

2.26 The Government appreciates that landlords may indeed incur disposal costs and agrees that it is right to extend the relief to include the cost of disposing of old assets.

Other impacts

2.27 16% of respondents argued that these changes would result in increased rents and that landlords would be less willing to offer furnished properties, because the relief would be less generous than the Wear and Tear Allowance and because there were greater administrative burdens associated with this new relief.

2.28 **Government response:** The level of rents is driven by the balance of supply and demand in the market, which is not expected to be affected significantly by these changes to the tax rules. Landlords of part-furnished and unfurnished properties operating in that market will now receive relief for the costs of replacing furnishings. The Government does not expect these changes to have a large impact on rent levels.

2.29 The Government recognises that tax is not the only consideration when deciding whether to offer furnishings in a property, and that this may be dictated by market demands.

3. Next Steps

3.1 The Government has decided to proceed with the introduction of the new relief, in place of the Wear and Tear Allowance, in Finance Bill 2016.

3.2 An updated impact assessment is included in the Tax Information and Impact Note that will be published alongside the draft legislation for this measure.

3.3 The Government has published draft legislation for technical consultation today. We would welcome any comments you have on the draft legislation. The consultation will run for 8 weeks.

3.4 If you have any comments on the draft legislation, please send them by email, if possible, to wearandtear.replacement@hmrc.gsi.gov.uk.

3.5 Alternatively, comments may be sent by post to: Megan Shaw, HM Revenue and Customs, CTIS, 3/64, 100 Parliament Street, London, SW1A 2BQ.

Annexe A: List of stakeholders consulted

The following representative bodies and professional advisors formally responded to the consultation:

1. Association of Accounting Technicians
2. Association of Residential Letting Agents
3. Association of Taxation Technicians
4. AW Tax Service Limited
5. British Property Federation
6. BKL Tax
7. C Phillip Rees & Associates Limited
8. Central Association of Agricultural Valuers
9. Chartered Institute of Taxation
10. Computershare (operator of the Deposit Protection Service)
11. Council of Letting Agents
12. Crisis
13. Deloitte
14. Institute of Chartered Accountants in England and Wales
15. KPMG
16. London Society of Chartered Accountants (Taxation Committee)
17. Mazars
18. Mishcon de Reya Solicitors
19. National Landlords Association
20. Purvis Stevens LLP
21. Residential Landlords Association
22. Reynolds & Co Chartered Accountants
23. Select Accountants Ltd
24. Scottish Association of Landlords
25. TaxAid
26. Thandi Nicholls Ltd