

Capital Allowances

Everything you need to know about the changes to capital allowances for holiday lets

CAPITAL ALLOWANCES



From 6th April 2025 (1st April 2025 for Limited Companies), capital allowances will no longer be available to short-term lets that met the Furnished Holiday Let (FHL) tax legislation.

Zeal have put together this document to provide all the information owners need to be aware of prior to, and after, the rules change. We have included as many answers as possible to the questions that owners have asked our team over the past few months in an easy to understand format.

What are capital allowances?

Capital allowances provide tax relief against income or corporation tax for the cost of purchasing business assets (capital expenditure). The most common examples for short-term let owners are furniture, furnishings, cooking and refrigeration equipment and hot-tubs.

However, many owners are unaware that there is an extra level of capital allowances that can be claimed on 'Integral Features,' commonly referred to as 'Embedded Fixtures', that were purchased with or installed in the property. Qualifying fixtures include heating and electrical systems, fire & security alarms, kitchens, bathrooms, water and disposal pipework, carpets etc (more on these later).

What doesn't qualify for capital allowances?

Assets that are structural in nature and don't meet the definition of Plant & Machinery (P&M), such as hard landscaping, doors, windows, walls, roofs etc.

What are capital allowances pools?

Capital allowances are allocated to two different 'Pools'. Most assets go in the Main Pool, which provides an 18% deduction from the pool balance, each year.

The Special Rate Pool, is for Integral Features (see later section) and provides an annual deduction of 6% a year (reducing balance method).

Expenditure is only 'pooled' if you use the accruals basis of accounting and when the Annual Investment Allowance (AIA) is not available. The AIA gives a 100% tax deduction in the year you make a qualifying purchase. However, sometimes it is tax efficient not to claim a 100% tax deduction in one go. If you don't claim 100%, the unclaimed balance is 'pooled'. This is usually done to avoid wasting tax free personal allowances.

What if we use cash basis accounting? I heard we can't claim capital allowances?

Expenditure that qualifies for capital allowances CAN be deducted as a business expense for businesses that use the simplified cash basis of accounting. There are no capital allowances pools under the cash basis.

Most owners use the cash basis and HMRC actually encourage it. They have made cash basis more attractive for small businesses from April 2025. Read more about cash basis changes from the 2024/2025 tax year on the GOV.UK website [here](#).

When is the DEADLINE to claim capital allowances?

There is a key difference between the deadline to claim capital allowances, and the deadline to incur expenditure that qualifies for capital allowances.

The last date to incur expenditure (i.e. buy an asset qualifying for capital allowances) will be 5th April 2025 (31 March 2025 for limited companies).

For individuals or partnerships, the last time capital allowances can be claimed will be in your 2024/25 tax return. The 2024/25 tax return needs to be submitted by 31 January 2026. However, an amendment can be made to the 2024/25 tax return until 31 January 2027.

The deadline to claim expenditure that qualifies for capital allowances will be 31 January 2027.

Is the deadline the same for Companies?

For limited companies, if the expenditure is incurred before 1st April 2025, the claim can be made in the corporation tax return that covers this period.

A company can also amend a corporation tax return for up to 2 years after the end of the accounting period. For example, a company with a 31 December 2025 year end, will be able to make a claim for capital allowances **until 31 December 2027**. The key point is that the asset must be purchased before 1st April 2025.

What happens after April 2025?

Capital expenditure on replacing domestic goods, will still qualify for tax relief post April 2025.

Domestic goods are defined by HMRC as follows:

- ▲ Moveable furniture (sofas, tables, bed frames etc).
- ▲ Furnishings (curtains, rugs, carpets etc).
- ▲ Household appliances (fridges, freezers, washing machines etc).
- ▲ Kitchenware (utensils, crockery, cutlery etc).

This list is not intended to be exhaustive but gives an idea of the assets that are domestic items which would qualify for 'Replacement of Domestic Items Relief'. It is expected that a 'hot tub' would not be classed as a domestic good by HMRC.

Embedded Fixtures are not domestic items and do not qualify for 'Replacement of Domestic Items Relief'. You will not be able to claim capital allowances on Embedded Fixtures purchased after April 2025. However, you can claim them as a 'revenue deduction' in certain circumstances (see below).

Is the deadline the same for Companies?

Yes and No! If a company are replacing a domestic good that it already owns (for example a sofa), it will not matter when it is purchased. The company will get the tax relief whenever it makes the purchase. A hot tub or a domestic item that is **not** replacing an existing one, would need to be purchased before 1st April 2025. No tax relief would be available if the company purchased after 1st April 2025.

The same rules apply to companies for Embedded Fixtures. Whilst the company will not be able to claim capital allowances on Embedded Fixtures (such as a kitchen or bathroom) after 1st April 2025, they may still be able to claim tax relief as a 'Revenue Deduction' (business expense).

What is Revenue Expenditure?

Revenue expenditure is typically the day-to-day expenses incurred in the 'normal' course of running and maintaining a property to generate rental income. The expenses are normally recurring and don't have a lasting benefit for the business. Once incurred they are consumed and provide no further benefit to your business. Typical examples include utilities, cleaning costs, council tax, maintenance etc.

Will replacing Embedded Fixtures like kitchens and bathrooms qualify for a revenue deduction?

In most cases, replacing an existing bathroom, kitchen, carpet, alarm systems etc will qualify for a revenue deduction (a repairs and renewals expense). This is providing they are a like for like replacement with no 'significant' improvement.

There is lots of case law around what is a 'significant' improvement. There is also a concession for trivial improvements or advances in technology. For example, replacing wooden windows for UPVC double glazed.

Changing an old kitchen for a modern kitchen with more advanced materials will likely qualify as a revenue expense (repair). However, if the kitchen is extended and larger than the previous kitchen, it is more likely to be classed as capital expenditure and no tax relief available against income tax.

Do these rules apply to all Embedded Fixtures?

No. Embedded Fixtures that fall into the 'Integral Features' category have special rules. If the cost of replacing an Integral Feature is more than 50% of the original cost of the Integral Feature, the whole cost will

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be treated as capital expenditure. You won't be able to deduct it as a business expense.

Integral Features are:

- ▲ Electrical systems.
- ▲ Heating and ventilation systems.
- ▲ Water systems.
- ▲ Lifts and Conveyors.
- ▲ External Solar Shading.

Are the rules different for Limited Companies?

No. The same rules and case law applies to revenue and capital expenditure incurred by a company.

Will I not get any tax relief for the cost of Embedded Fixtures if they are classed as capital not revenue expenditure?

Although you will not get tax relief against income tax or corporation tax, you will get tax relief for the cost incurred against Capital Gains Tax (CGT) when you sell your property.

This is not the same for loose fixtures and fittings (chattels), like furniture and equipment. If they don't qualify as a replacement of a domestic goods, you will not get any tax relief.

Are the rules different if I replace an Embedded Fixture after I purchase the property?

Potentially yes! If you replace an Embedded Fixture after purchase, whether or not you can claim a revenue expense will depend on several factors. For example, was the property price reduced to reflect the condition of the property? If it was, then it will not be deductible as a revenue expense.

For example, if you purchased a property and decided to replace the kitchen as it was not to the standard or finish you desire, then replacing the kitchen is likely to be a revenue expense that is tax deductible against your rental income.

If you bought a dilapidated property with an old kitchen, the purchase price is likely to reflect the condition of the property. The new kitchen will likely be regarded as capital expenditure, not deductible against your rental income (but you can deduct against CGT when you sell).

Is there an advantage to claiming capital allowances rather than a business expense?

Yes. If an embedded fixture qualifies for capital allowances, you can claim a tax deduction against rental income AND also deduct it as capital expenditure when calculating CGT, if you sell your property for a gain.

Many accountants are unaware of this and incorrectly advise their clients that you have to make a choice between claiming now against income tax or against CGT when you sell.

Furthermore, it is common for an accountant to advise that any replacement of fixtures is capital expenditure. This not the case, as set out before.

So, is there a benefit to replacing a bathroom, kitchen or other Embedded Fixture before April 2025?

Yes. If you can claim capital allowances, you will get tax relief against your income and CGT in the future. After April 2025, you may need to decide if you claim the cost against income tax now or in the future against CGT.

Currently, CGT rates are lower than income tax rates. If you are profitable or will be before you sell, it is better to claim a revenue deduction, where possible.

Is it too late to claim capital allowances if I didn't claim when I purchased, built or refurbished my property?

No. If you have incurred costs to purchase a property that included embedded fixtures, or you installed new fixtures when you refurbished, built or converted a property, you have until 31 January 2027 to make a claim. **However, the sooner you claim the better.**

You can even go back to your 2023/24 tax return and make the claim until 31 January 2026. This could enable you to reclaim tax paid and generate losses that you can carry forward to future years.

Will I lose any remaining capital allowances or losses when the rules change in April?

NO! Fortunately, the new legislation will allow capital allowances or losses remaining to be carried forward until used up. The other major advantage is that they can also be used against profits from long term lets.

I am planning on changing my business to a LLP or Company structure. How does this affect capital allowances?

In short, you will not lose the capital allowances, they can transfer to the new entity.

If you are transferring your property to a company, you will need to identify and claim the capital allowances in your personal name **first**. They can then be transferred with the property. There is a 2 year time limit from transfer to a company to pass the capital allowances over.

Can I really claim part of my property purchase price as a capital allowance?

In most cases, YES! You can claim on part of the purchase price that related to the embedded fixtures you acquired with your property. Typically, this can be between 15% and 30% of the purchase price.

However, you will need a capital allowances specialist firm like Zeal to do this for you. It is **not a service an accountant can typically provide** as it requires the skills of quantity surveyors.

Does this affect CGT when I sell?

NO! Claiming capital allowances do not impact your CGT calculations if you sell the property for a gain.

Can I qualify for capital allowances if I start my FHL business before April 2025?

Yes. As long as your property is available for letting before April 2025, and you incur the costs of the loose or embedded fixtures before the relevant date, you can apply the letting days test to the 12 months from the date your business started.

If you are available for short-term letting for 210 days and achieve 105 days of actual letting in the 12-month period, you'll qualify in 2024/25 (subject to meeting all other qualifying criteria).

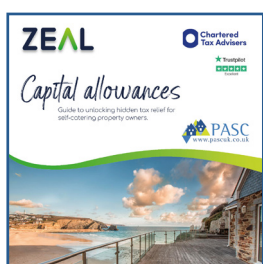
If you are new to short-term letting or are about to start a new business, make sure you incur the costs and make the property available for letting before 6th April 2025 (1st April 2025 for a company).

Capital allowances on embedded fixtures is a complex area of taxation, which is often overlooked and misunderstood by accountants. Many owners have missed claims on their property purchase, refurbishment, build or conversion costs. The new rules around revenue expenditure on replacing fixtures is also complex and will require advice from specialists like Zeal.

If you have missed a claim or would like to find out if you have any unclaimed capital allowances, you can contact the team at Zeal for a FREE consultation.

ARRANGE A CHAT

Further information:



DOWNLOAD

For more details on all the changes to the FHL tax regime, you can download Zeal's free eBook 'Tax Changes for Furnished Holiday Lets'.

You can read more about capital allowances on embedded fixtures in Zeal's free guide for short-term let owners.



DOWNLOAD