# You do not qualify

**Julie Butler discusses the First-tier Tribunal's recent decision that a holiday cottage did not qualify for repayment under the DIY housebuilders scheme.**

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The current costs of house builds are incredibly high with building costs still rising. Pressure is therefore placed on the DIY housebuilders scheme which allows private individuals to claim back the VAT on the building materials used in constructing their own homes. With the staycation industry booming, some may think that using this scheme in constructing a holiday home would be a wise move. However, the recent case of *Philip Spani* (TC8916) has shown it cannot be applied to ventures such as furnished holiday lets (FHL).

## Analysis of planning permission

Mr Spani obtained planning permission to build a new house on two floors in Seaford in the South Downs Country Park. The planning consent approved the construction but clearly stated that it could only be used as holiday accommodation and must be available as such for at least 140 days each year – quite a serious restriction. The consent recognised the fact that the national park area looked more favourable on constructions used for holidays rather than purely residential purposes. The case also shows the need for all tax and VAT planning to be undertaken from the start of the project, eg at the planning permission application stage (see 'Starting well', *Taxation*, 16 March 2023).

Mr Spani submitted a DIY housebuilders refund claim to HMRC under guidance from VATA 1994, s 35 on the basis that the property would be his only UK home. Mr Spani explained that when the property was used as a holiday let, he and his partner would either live in Italy or stay with friends.

HMRC rejected the claim on the basis that the property would only be used 'in the course or furtherance of any business' rather than as a private residence of the claimant. Mr Spani claimed to HMRC and the First-tier Tribunal (FTT) that his letting through Airbnb fell short of a commercial business arrangement – the purpose of the project was for him and his partner to live in the property rather than to earn profits (a clear contradiction to the planning application).

The construction and use of holiday accommodation is a complex area which requires careful reading of VATA 1994, Sch 8 Group 5 and Sch 9 Group 1, as the definition of a dwelling for construction purposes and for letting and sale purposes has subtle but important differences. Indeed, the whole area of property and VAT is extremely complicated. Ironically, this especially applies to farmers who have a large amount of property and undertake an equally substantial amount of diversification. The tribunal found that Mr Spani was merely proposing the use of the building as holiday accommodation as a ploy to obtain planning permission to build a home in a national park, and the tribunal judge therefore refused the claim on the grounds that holiday accommodation designed for use as a holiday let does not qualify for the DIY housebuilders scheme specifically.

**Key points**

- The DIY housebuilders scheme cannot be applied to ventures such as furnished holiday lets.
- In *Philip Spani*, the First-tier Tribunal found that Mr Spani's cottage was built in furtherance of a business.
- There is a distinction between a person building a holiday home as a second home versus a holiday let.
- The intended use of a building is key, and the planning consent is strong evidence of this.

## Holiday lets cannot be used for the DIY scheme

The FTT agreed that the 'designed as a dwelling' condition had been met. However, the fact was that the property was built to be a holiday let, as stipulated by the planning consent. Even if the tribunal were to consider that the property was to be a second home, as claimed by the appellant, the judge was of the view that, 'the property remains one that was built first and foremost to be a holiday let and is therefore built in furtherance of a business'. Therefore, the claim for refund of VAT was denied for non-qualification.

## The facts confirmed business, not private use

The FTT found that Mr Spani's cottage was built in furtherance of a business for the following reasons:

- Use of the cottage as a 'dwelling house' by 'a single person or by people to be regarded as forming a single household' was prohibited by the planning consent and the property was specifically proposed as a holiday let in the planning consent application.
- The planning consent explicitly stipulated that the cottage 'shall only be used for holiday accommodation' and 'for no other purpose'. The FTT found that it was bound by this stipulation and restriction.
- Mr Spani's correspondence with HMRC stated in no uncertain terms his intention to carry on a FHL business. These intentions were evidenced by the fact that Mr Spani had advertised the property on Airbnb as mentioned.
- The home and contents insurance cover for the cottage specified that tenant's liability insurance was part of the cover.
- Although the impact of Covid together with Mr Spani's partner's ill health hindered Mr Spani's intention to let the property as holiday accommodation, these subsequent events did not detract from the planning consent which indicated the property was constructed in furtherance of a FHL business.

The FTT considered the distinction between a person building a holiday home as a second home (which would usually qualify under the DIY housebuilders scheme) and a building designated to be furnished holiday accommodation. It is this distinction that could be most useful to tax advisers and taxpayers alike; therefore forensic analysis of the plans and the actual activity is necessary.

## Registering for VAT on a voluntary basis

Perhaps we should look at alternative VAT treatments as holiday lets are charged at standard rate. Many would argue that it could have been more effective for Mr Spani to build a new dwelling in an area that allowed residential use and the planning agreement did not insist on holiday accommodation. However, the national parks are an attractive place to reside and it is difficult when that is the place where the taxpayer is determined to live. Another alternative would have been to register for VAT on a voluntary basis to claim input tax but that would have created an output tax liability on Mr Spani's revenue. The problem here is having to charge VAT on the income and having to prepare returns that are open to inspection. However, the answer is to carry out the calculations of VAT advantages and disadvantages.

## Lessons to be learnt

We cannot deny that in this case, Mr Spani built the residence for the purpose of letting as holiday accommodation. VAT law excludes DIY claims where there is a business and VAT advisers should be aware that holiday letting is a business purpose, even if operating below the VAT threshold, and therefore the claim was bound to fail. However, the tribunal took the trouble to set out the law, and its reasoning over ten pages, which is useful for those faced with the dilemma of understanding the correct VAT treatment in similar scenarios.

The whole area on VAT and the supply of land is incredibly complex – what is a dwelling for VAT purposes? What is VAT treatment for construction, conversion, sale, and letting of a dwelling? – together with the zero rate on new builds. It must always be remembered by tax advisers that the planning permission guidelines will be considered by the VAT authorities as standard procedure.

The new building met the conditions of a property that was 'designed as a dwelling' in accordance with VATA 1994, Sch 8 Group 5 item 2. In essence, it consisted of self-contained living accommodation; it had no internal or other access to any other building; its separate use or disposal was not prevented by the terms of any planning consent; the construction had been legal and carried out in accordance with the planning conditions. However, the problem was the intended business use.

## Impact of the case on farmers

Farmers are already registered for VAT, although sometimes they might keep any holiday accommodation business ringfenced in a separate trading entity such as a limited company and below the VAT registration limit.

The next step is considering whether registering for VAT on a voluntary basis would be beneficial. The clear advice for tax advisers and taxpayers is that in all instances the alternative VAT treatments of each option must be reviewed alongside the planning permission and understood in the context of the VAT rules. Financial forecasts should also be prepared to assess the alternatives fully. The case is a timely reminder of the need to understand the planning application and the intended use of the property and to ensure that the correct decisions are being made from the get-go as opposed to reviewing the position retrospectively.

Many would argue that with the current rising building costs cashflow forecasts are very difficult to undertake but they are needed as a guide for all tax planning. It is not just the immediate advantage of the VAT refund under the DIY housebuilders scheme but also the income tax on the holiday accommodation, as well as possible business property relief (BPR) for inheritance tax on the cottage through the business element of the property and capital gains tax on disposal. Ironically, the business element that disallowed the VAT claim might not have been enough to qualify for BPR. All tax planning must be looked at in the round.

This decision does highlight that the interpretation of business and trade needs careful understanding in the context of each tax regime that is being reviewed. 'Intent' and 'actual use' must be understood to fully decide on claims for tax relief. See 'Focus on trade', *Taxation*, 13 July 2023, for reference. ●

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