MEREWOOD

Financial Services

RESIDENTIAL INVESTMENT PROPERTIES and TAX

Residential Investment Properties And Tax

Who’s This Guide For?

If you’re looking to make an investment and buying a property to rent out, it’s **definitely an opportunity that can have both personal and financial benefits.**

However, recent tax changes for Buy to Let properties have two major implications for landlords and this guide is designed to highlight these and allow you to make a fully informed decision when deciding to invest this way.

Firstly, landlords need to take the changes into account when completing their tax returns. Secondly, and possibly more importantly from the landlord’s point of view, their profit could be affected.

I should point out that this guide is correct at the time of publication and I’d always recommend landlords consult an accountant about their personal situation.

However, I really hope you find it useful and don’t hesitate to get in touch with any questions.

David Tarry MBA
Merewood Financial Services
01983 875151 or 0771 476 2597

Your Home (or property) may be repossessed if you do not keep up repayments on your mortgage.

Residential Investment Properties And Tax

Income Tax

Mortgage/loan interest

It's never been possible to claim the repayment element of your mortgage but, since 6 April 2017[1], there have been restrictions on how you can claim the interest on any loans *(and any other finance costs such as arrangement fees)*.

There are two changes rolled into one:

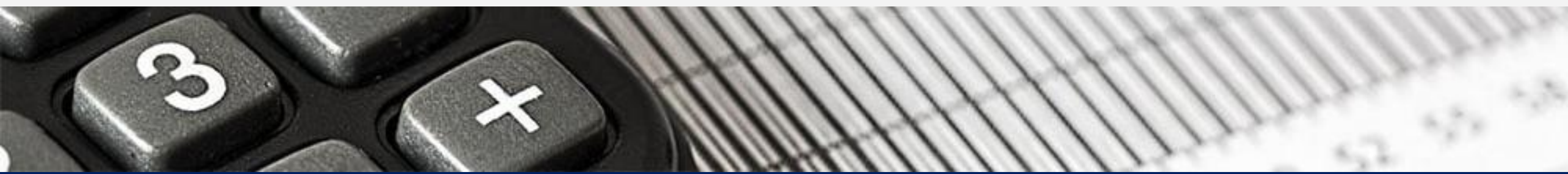
1. Instead of claiming finance costs as a letting expense you will only be able to **claim a deduction which will reduce the tax due on rental properties.**

This can be claimed in the appropriate section of your tax return. Fundamentally, *if you only pay tax at 20% then you will pay the same amount of tax*

2. Unfortunately, there will **no longer be additional relief for higher rate taxpayers.** The deduction will be limited to a maximum of 20% of finance costs.

In real terms, this means:

- **Your taxable profits could be higher so you may pay more tax**
- **You may pay tax even though you have no net cash after paying out loan interest and repayments**
- **You should review your BTL properties in the light of this increased taxation and the effect on your cash flow**



[1] https://www.gov.uk/government/publications/restricting-finance-cost-relief-for-individual-landlords/restricting-finance-cost-relief-for-individual-landlords

Residential Investment Properties And Tax

Other expenses

There are plenty of other expenses that you can claim from the list below:

Buildings insurance
(not contents unless it's a furnished property)
Light and heat
Cleaning
Gardening
Security
Rent and ground rent
Service charges
Council tax while vacant
Repairs and maintenance
Replacements

Redecorating
Small tools
Legal
e.g. preparation of rental contracts
Accountancy fees
Debt collection fees
Other insurances
Advertising
Letting agents' fees
Travel
Advertising for new tenants

Repairs or improvements?

Repairs and improvements are both allowable costs but it's an important distinction as tax relief is claimed in one of two ways depending whether building work is repairing or replacing pre-existing materials or whether it is an improvement.

Repairs and maintenance usually include:

Painting and decorating
Re-pointing existing brickwork
Damp or rot treatment
Repairs to existing equipment, windows, doors, etc.
Replacing a roof

Residential Investment Properties And Tax

Capital items are work which improves the property such as an extension. These costs can be claimed to reduce your capital gains tax when you come to sell the property.

Sometimes it is hard to tell if an item is a replacement or an improvement so, if you're unsure, do take advice.

Furniture and Fittings

Another recent change is the removal of the 10% wear and tear allowance to cover furnishings (beds, sofas etc.) or appliances. Since 6 April 2016[1], it is only possible to **claim the actual cost of repairing or replacing these items. This means that you now need to keep your receipts.**

Capital Gains Tax

When the time comes to sell, hopefully your property will have increased in value. **Unlike selling your main home, this increase in value is taxable as a capital gain.**

The good news is that you can claim the costs of purchasing, selling and improving the property.

If the property was your main residence at any time then there may be reliefs available. You can find more information on capital gains tax [here](#).

[1] https://www.gov.uk/hmrc-internal-manuals/property-income-manual/pim3210

Residential Investment Properties And Tax

Capital Gains Tax (continued)

There is **an annual capital gains allowance** for each individual owner to offset net gains/losses in the year of disposal. Everything above this allowance is currently taxed at 18% or 28% depending on your normal tax rate.

If you **are thinking of selling a property that has significantly increased in price then it may be worth taking individual tax advice early** in the process and definitely before the sale itself as there may be actions that can be taken in order to minimise your tax burden.

Furnished Holiday Lets (FHL)

Special rules apply when letting out a holiday property in the European Economic Area (EEA). These rules may well change following our exit from the EU and/or EEA.

To qualify as a FHL[1], the property must be:

Available to let commercially for at least 210 days in the year[1]

Actually let at a commercial rate for at least 105 days per year[1]

Any letting periods over 31 days long can't be included in the 105 days and the total of all such longer lets must be less than 155 days per year[1]

If you own a **FHL then these properties must be accounted for separately from your other properties**, however, there are additional reliefs available. The rental income is a useful way to part fund what may be your own holiday home.

[1] https://www.gov.uk/government/publications/furnished-holiday-lettings-hs253-self-assessment-helpsheet/hs253-furnished-holiday-lettings-2019

Residential Investment Properties And Tax

Stamp Duty

When you purchase a property you will **probably pay stamp duty land tax (SDLT)[1].** The rate you pay will depend on the price you pay for the property, excluding any carpets, curtains and free standing furniture etc. at the market value *(the amount that you would pay for these on the open market and not an artificially constructed value)*.

From 1 April 2016, **the rate of stamp duty was increased by 3% on second properties which may be a second home or a buy to let property.** Click **this link** for a great online calculator that'll help you work out how much SDLT may be due.

Companies also pay SDLT on all property purchases.

Differences For Companies

If you decide to use a limited company to hold your property portfolio, you will pay tax on profits **as corporation tax. This rate is currently 19% on all profits[2].**

You will potentially have to pay further tax when you want to take the profits out of the company as salary (PAYE/National Insurance) or dividends (dividend tax). There is no annual allowance for a company's capital gains on sale.

Using a limited company **may** give you opportunities for tax planning but **there will also be higher admin and accountancy costs.** There are also different inheritance tax rules when transferring shares in a property company rather than transferring the properties themselves.

[1] See https://www.gov.uk/stamp-duty-land-tax/residential-property-rates for details of current rates and the stamp duty holiday scheme due to expire on 31 March 2021
[2] https://www.gov.uk/topic/business-tax/corporation-tax

Residential Investment Properties And Tax

Differences For Trusts

There may be Inheritance Tax (IHT) advantages if your property is held in a trust[1].

If you are thinking of using a limited company or a trust then it is worth taking professional advice.

You can find out more information on IHT and Trusts here.

Next Steps

This guide is intended as a brief overview of the main ways that your residential property investment will be taxed and is correct at the time of publication. Next steps for landlords might include:

Ensure you understand the impact on your business and income now and in the future.

Take a look at the suggested sources throughout the guide.

Consider appointing an accountant if you don't already have one. The more complex your income and the larger your portfolio, the more likely this is to be beneficial. **ICAEW** or **ACCA** are great websites for searching for accountants near you.

Be aware that according to your situation, other taxes may apply and there are special rules for non-UK residents.

[1] Some forms of Buy to Let mortgages are not regulated by the FCA. IHT and Trusts are not regulated by the FCA

Residential Investment Properties And Tax

David Tarry

Merewood Financial Services

www.MerewoodFS.co.uk

01983 875151 or

0771 476 2597

david@merewoodfs.co.uk

Merewood Financial Services is a trading style of David Tarry, an Appointed Representative of The Right Mortgage Ltd, which is authorised and regulated by the Financial Conduct Authority.

David Tarry, t/a Merewood Financial Services is not authorised to give advice on Investment and Tax advice and this brochure should not be regarded as advice in any way. If you require advice on investments or tax, you should seek your own professional advice.

Published date: December 2020

The information in this guide is correct as at the date on the document. Merewood Financial Services does not accept any responsibility for how the guide is used. If we become aware that the advice is out of date, we will remove the guide from our site. It is the responsibility of the user to ensure the guide remains correct as and when it is used.