BUY TO LET TAX GUIDE

Expert advice

FROM START TO FINISH

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Contents

Do you pay Stamp Duty Land Tax on a buy to let property?

Yes, the amount varies depending on the price of the property and where in the UK it is.

In England and Northern Ireland you'll pay Stamp Duty Land Tax, and the current rates of stamp duty are;

- 3% tax on the first £125,000
- 5% on the portion up to £250,000
- 8% on the portion up to £925,000
- 13% on the portion up to £1.5 million
- 15% on everything over that.

In Scotland you'll pay Land and Buildings Transaction Tax, and the current rates are;

- 3% tax on the first £145,000
- 5% on the portion up to £250,000
- 8% on the portion up to £325,000
- 13% on the portion up to £750,000
- 15% on everything over that.

In Wales you'll pay Land Transaction Tax, and the current rates are;

- 3% tax on the first £180,000
- 6.5% on the portion up to £250,000
- 8% on the portion up to £400,000
- 10.5% on the portion up to £750,000
- 13% on the portion up to £1,500,000
- 15% on everything over that.

Anyone buying a second property that isn't their main residence will be charged these new rates. This will include holiday lets and buying a property for children if the parents leave their name on the title deeds. Stamp duty has to be paid within 30 days of completion of the property purchase although this is usually paid by the solicitor on completion. The amount of Stamp Duty paid is deductible from any capital gains you might make when the property is sold.

Do you pay Capital Gains Tax (CGT) on buy to let property?

Yes, if you sell the property for more than you paid for it after deducting costs such as stamp duty and estate agent/solicitors fees.

By making a profit, you are essentially 'gaining capital', and so the tax applies. However, as an individual you get an annual allowance to set against any gain.

In the 2018/19 tax year, this allowance is £11,700. This is a special allowance purely for capital items and is separate from the annual personal income tax allowance.

If the gain is greater than the £11,700 allowance, you will pay tax at a rate of either 18% or 28% on any profit over £11,700 depending on the amount of income and capital gains you have.

Note that the lower CGT rates of 10% and 20% announced in the March 2016 budget don't apply to buy to let and second properties.

What you can do to reduce your CGT liability

There are legitimate ways to reduce the amount of Capital Gains Tax (CGT) payable

- A loss made on the sale of a buy to let property in previous tax years
- Solicitor fees
- Estate agent fees
- Costs of advertising the property for sale
- Stamp duty
- Any expenditure on ‘capital’ items

These expenses can be deducted from your capital gain.

There are also certain tax reliefs available. For example if the property was previously your main residence, the gain may be reduced.

Like income tax, any gain is declared on your Self Assessment tax return. The tax is therefore payable by the 31st January in the year after the tax year in which the property was sold.

(E.g. if a property was sold on 4th May 2018 it is in the tax year to 5th April 2019 so the tax is payable by 31st January 2020.)

However, the Government are proposing that, from April 2020, any tax payable on the profit of the sale of the property will be payable within 30 days of the date the property is sold.

Do you pay tax on buy to let property income?

Yes. The income you receive as rent is taxable.

You need to declare any rent you receive as part of your Self Assessment tax return. The tax on your income is then charged in accordance with your income tax banding (20% for basic rate taxpayers, 40% for higher rate, and 45% for additional rate). However, you can minimise the tax you have to pay by deducting certain "allowable expenses" from your taxable rental income.

Allowable expenses include:

- Interest on buy to let mortgages and other finance charges (but see below)
- Council tax, insurance, ground rents etc
- Property repairs and maintenance – however large improvements such as extensions etc will not be income tax deductible. They will be added to the cost of the property when it is sold and be deductible against any capital gain.
- Legal, management and other professional fees such as letting agency fees.
- Other property expenses including buildings insurance premiums

New rules came into force from April 2017 which restrict the tax relief given on interest payments. The restriction is being phased in over 4 years with the aim to only give basic rate tax relief from April 2020. See our examples overleaf for basic and higher rate tax payers.

An example of how the new rules could affect you

- House is bought for £300,000
- 80% mortgage is taken for £240,000
- Mortgage interest assumed at 4.5% annual mortgage interest is £10,800
- Rental yield is assumed at 5%, annual rent is £15,000

Basic rate taxpayer

	2017-18	2018-19	2019-20	2020+
Annual rental income	15,000	15,000	15,000	15,000
Mortgage interest payable	(10,800)	(10,800)	(10,800)	(10,800)
Reduction in mortgage interest allowance*	2,700	5,400	8,100	10,800
Total rental income on which tax is payable	6,900	9,600	12,300	15,000
Tax at 20%	1,380	1,920	2,460	3,000
Tax deduction which is 20% of the reduction in mortgage interest allowance	(540)	(1,080)	(1,620)	(2,160)
Total tax payable	840	840	840	840

*The reduction in mortgage interest allowance is 25% in 2017-18, 50% in 2018-19, 75% in 2019-20, 100% in 2020 and beyond

A basic rate tax payer on the face of it will not pay any more tax under the new rules, but that's not the whole story.

The new rules change the way income is calculated. Income is now before deduction of any mortgage interest and other allowable expenses.

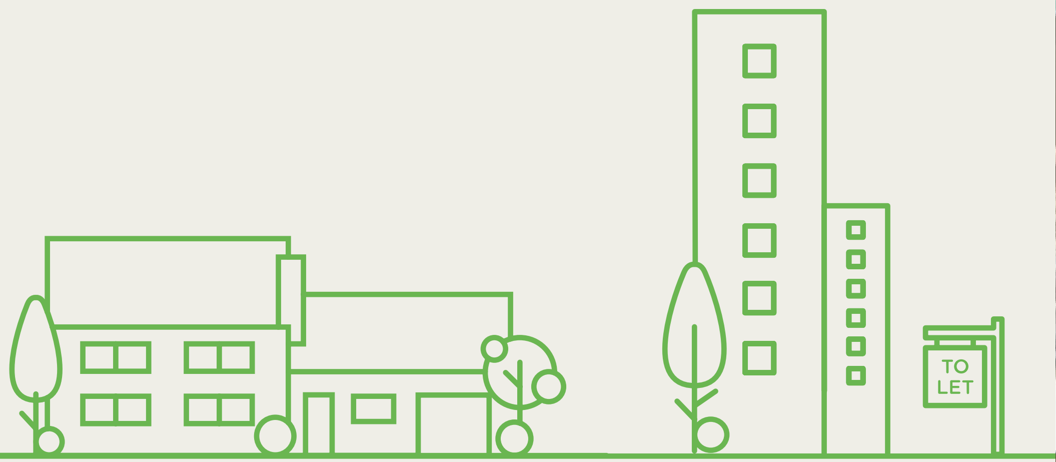
This increase in income could affect claims for Child Benefit and Income Tax Credits.

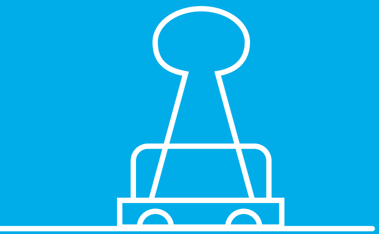
Higher rate taxpayer

	2017-18	2018-19	2019-20	2020+
Annual rental income	15,000	15,000	15,000	15,000
Mortgage interest payable	(10,800)	(10,800)	(10,800)	(10,800)
Reduction in mortgage interest allowance*	2,700	5,400	8,100	10,800
Total rental income on which tax is payable	6,900	9,600	12,300	15,000
Tax at 40%	2,760	3,840	4,920	6,000
Tax deduction which is 20% of the reduction in mortgage interest allowance	(540)	(1,080)	(1,620)	(2,160)
Total tax payable	2,200	2,760	3,300	3,840

*The reduction in mortgage interest allowance is 25% in 2017-18, 50% in 2018-19, 75% in 2019-20, 100% in 2020 and beyond

The tax impact of the new interest deduction rules will be a significant increase to the tax bill for higher and additional rate taxpayers.





Is using a limited company better for tax?

There is no simple answer. It depends on a number of factors such as how many properties you hold, whether you need the income quickly and how long you want to hold the properties for and your individual circumstances.

Limited companies are not affected by the new mortgage interest relief restriction which came into effect from April 2017. Interest for limited companies is classed as a business expense and fully deductible against income.

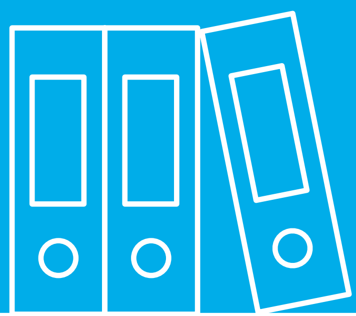
Companies pay corporation tax at a fixed rate irrespective of the size of the profits. The Corporation Tax rate is currently at 19% reducing to 18% in 2020.

This makes the tax rate very attractive compared to 40% for higher rate tax payers and 45% for additional higher rate taxpayers.

The question is how the money in the company is passed to the individual.

If the money is taken out of the company as a dividend, then from April 2018 only the first £2,000 of dividend income is tax free. Any dividends taken out in excess of this will either be charged at 7.5% for a basic rate taxpayer 32.5% for a higher rate taxpayer or 38.1% for an additional higher rate taxpayer. This tax is after the corporation tax at 19% has been paid.

The money could be taken as a salary, however the company would have to operate PAYE and pay Employers National Insurance contributions on any salaries paid. This usually (in most circumstances) works out more expensive than paying dividends.



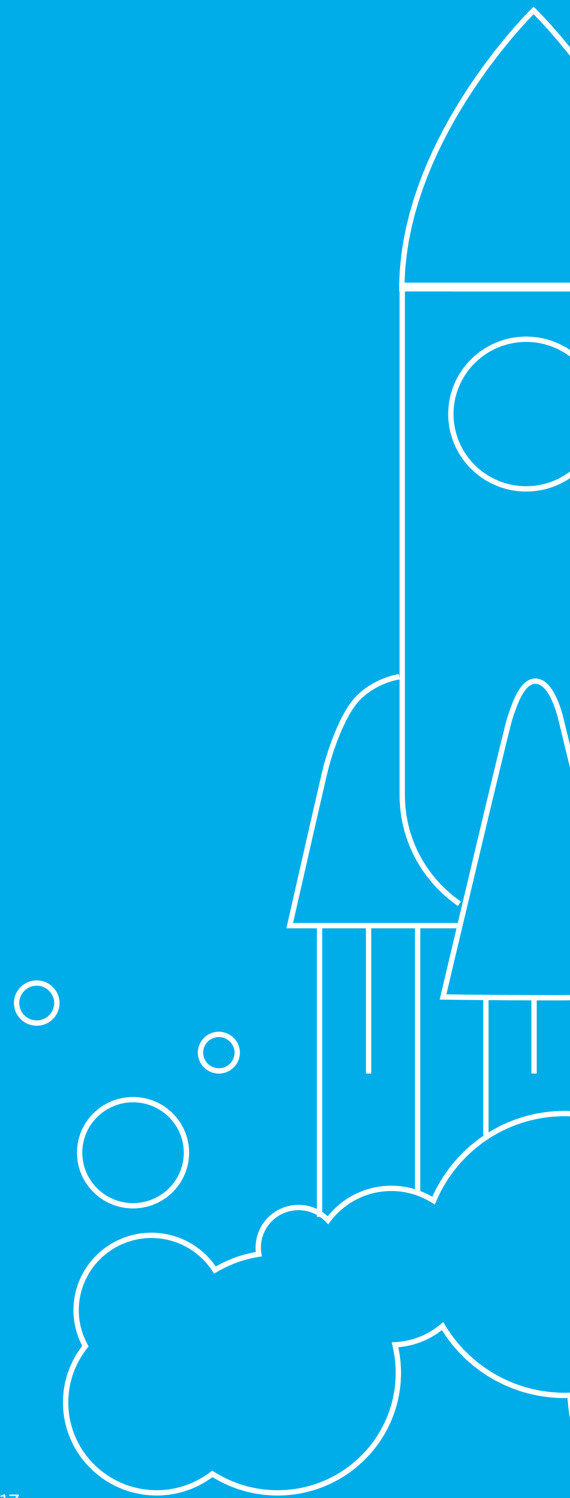
Companies also do not benefit from the annual allowance of £11,700 against capital gains. So extracting the money from a sold buy to let property could be less tax efficient than holding the property as an individual. As you have to pay the 19% corporation tax on any gain, no annual allowance is given and you have to pay tax on extracting the money from the company, whereas even a higher rate taxpayer only pays 28% on any gain from the sale of a buy to let as an individual.

Companies also have to prepare accounts to be filed with company's house, and prepare and file corporation tax returns which can be more onerous than self-assessment returns.

Interest rates charged on mortgages to companies have historically been higher than to individuals so further investigation of the comparison of the rates charged should be considered alongside the tax implications.

Transferring a current buy to let property into a limited company can trigger stamp duty and capital gains tax charges at the time of transfer so advice should be sought before undertaking such a transaction.

Due to the complexities of this area it is essential that you seek proper professional tax advice.



Do you pay inheritance tax on a buy to let property?

Yes, Inheritance Tax is payable on buy to let properties but the amount changes depending on your circumstances.

A buy to let property that you own will form part of your estate for Inheritance Tax purposes.

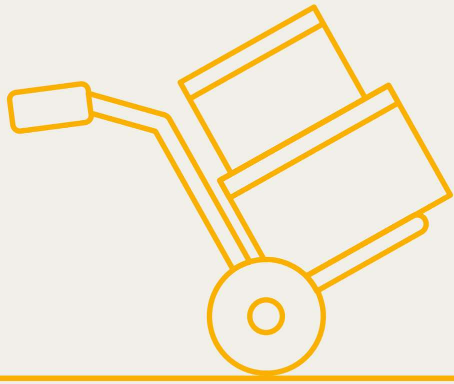
It works like this:

If you're operating as a sole landlord – with the buy to let mortgage in your name as an individual and your estate entirely owned by you alone – then you're liable to inheritance tax if your property value less any outstanding mortgage (or combined value of your estate) exceeds £325,000.

If you're in this with a married or civil partner, then you each have a threshold of £325,000 so the inheritance tax kicks in at £650,000.

Anything above these amounts is taxed at 40%.

Inheritance tax planning is complex and definitely something that should be discussed with an expert tax or financial adviser.



Disclaimer

The information provided in this booklet is of a general nature. It is not a substitute for specific advice on your own circumstances. You are recommended to obtain specific professional advice from a tax and legal adviser before you take or refrain from any action. Whilst we endeavour to use reasonable efforts to provide accurate, complete, reliable, error free and up-to-date information, we do not warrant that it is such.

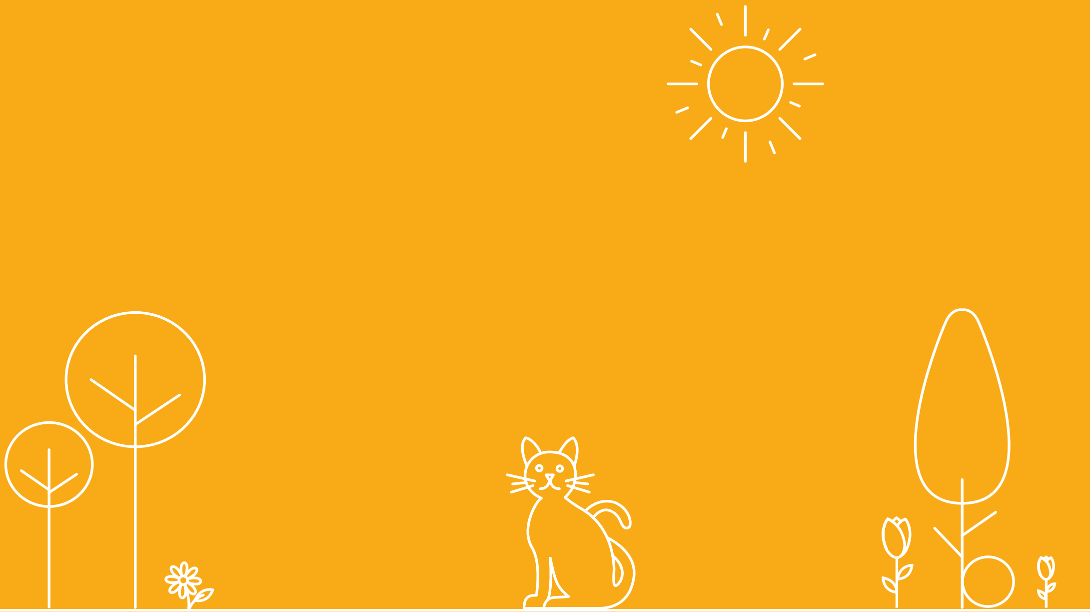
The information can only provide an overview of the regulations in force at the date of publication, and no action should be taken without consulting the detailed legislation or seeking professional advice.

The information, tax rates and allowances are correct as at the 1st September 2018.

Get in touch and we'd be happy to help with expert buy to let mortgage advice.

Call us free from your mobile or landline

0800 923 2055



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