BUY TO LET HEALTHCHECK 2023

Marsland Nash Associates

Increases to Buy to Let Taxation in recent years

- April 2016 additional 3% stamp duty second home purchase
- 2017-2020 finance costs restricted to 20% relief for Landlords (Section 24)
- Capital Gains Tax PPR relief where rental was main home – the last 36 months deemed as PPR reduced to 18 months and then 9 months in 2018
- Lettings relief on CGT largely abolished in 2020
- Capital Gains Tax – the £12,300 annual allowance reduced to £6,000 2023/24 and then £3,000 2024/25.
- Basic rate band frozen at 2020/21 levels until 2027/28

Other factors affecting landlords

- Landlords have also seen steep house price inflation but now face a declining market
- Higher interest rates reduce returns (and possibly compounded by lack of higher rate interest relief)
- Savings rates available at 5-6% guaranteed may exceed returns on rentals
- MTD for landlords >£50k deferred to April 2026
- Renter’s reform bill – possibly Spring 2024, additional tenant rights and landlord responsibilities

Effect of increased interest rate

Landlord with one property solely owned, PAYE job and two children

Low Interest Landlord in 2021

- £150k interest only mortgage at 3% costs £4,500 p.a. (£50k equity)
- Rents received £1,050 p.m. : £12,600 p.a.
- Other costs £800 p.a.
- Earns £38K PAYE
- Rental profit 12,600 – (4500+800)= 7,300
- Tax at 20% is £1,460

- **Profit after tax £5,840**

- Nearly 12% R.O.I. after tax

Effect of increased interest rate

Landlord with one property solely owned, PAYE job and two children

Higher Interest Landlord in 2023

- £150k interest only mortgage at 6% costs £9,000 p.a. (50k equity)
- Rents received £1,200 p.m. : £14,400 p.a.
- Other costs £800 p.a.
- Earns £43K PAYE
- Rental profit 14,400 – (9,000+800)= 4,600
- Tax due on rental £3,555 (including £1,369 child benefit charge 2 children)

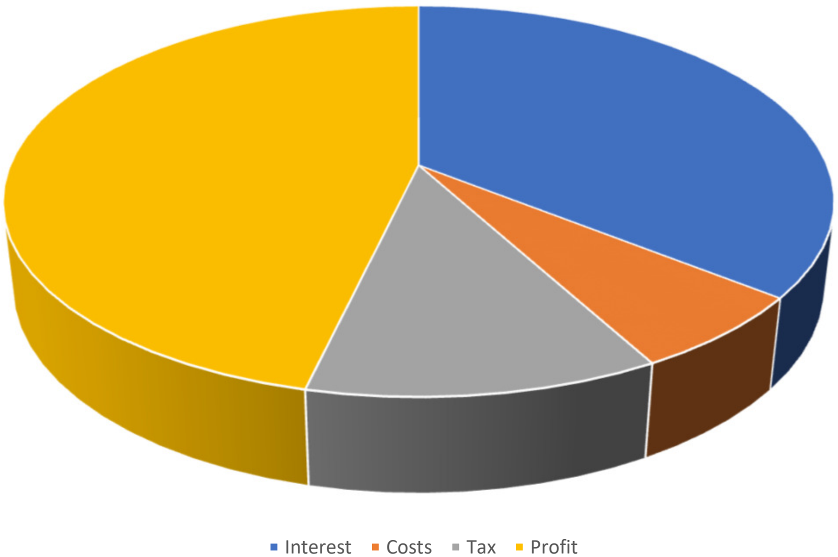
- **Profit after tax £1,045**

- 2% R.O.I. after tax

Effect of increased interest rate with small rent increase

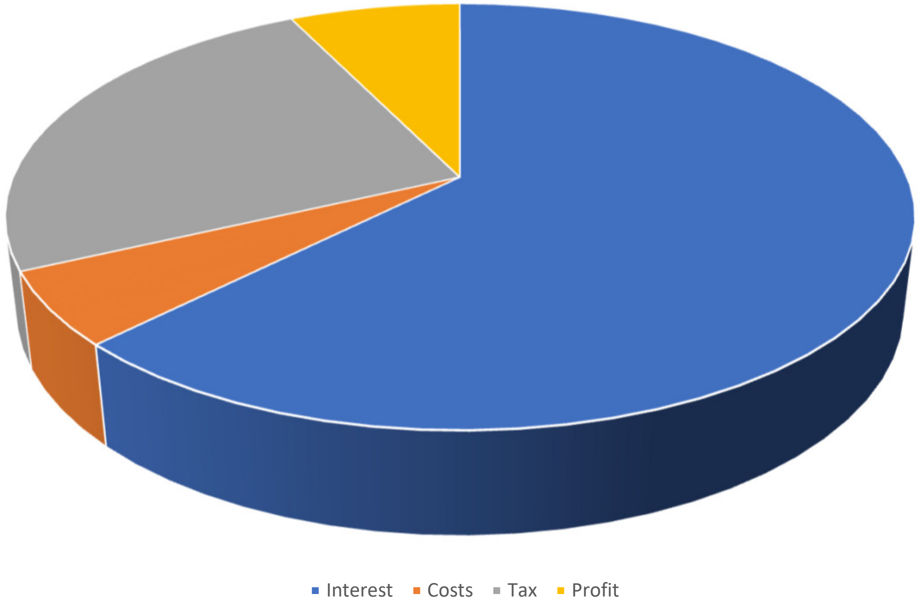
Low Interest Landlord in 2021

Rent	12600
Interest	4500
Costs	800
Tax	1460
Profit	5840



Higher Interest landlord in 2023

Rent	14400
Interest	9000
Costs	800
Tax	3555
Profit	1045



Why is there more tax on less profits?

Personal Tax Computation

				£	£
Income					
Employment				43,000	
Land and property				13,600	
					56,600
Deductions					
					NIL
					56,600
Allowances					
Personal allowance					(12,570)
					£44,030
Tax Borne					
Non-savings income (UK income tax rates)					
Basic rate	37,700	@	20%	7,540.00	
Higher rate	6,330	@	40%	2,532.00	
				10,072.00	
Rate restricted relief					
Relief for finance costs 9,000.00 @ 20%				(1,800.00)	
High Income Child Benefit charge				1,369.00	
Tax deducted at source				(6,086.00)	
Total liability					£3,555.00

What are the options if the interest/tax cost is too much?

1. Change to a Furnished Holiday Let (AIR BNB)

Furnished holiday lets have a special set of qualifying conditions and some tax advantages (ask for our factsheet)

Available 210 days, let 105 commercially.

The main advantages are :

- Interest relief – interest relief is not restricted as it is with long term lets
- Pension contributions , if your main income is FHL you can use these as qualifying income for pension contributions
- Capital allowances- kitchen /bathroom fittings and integral fixtures may be claimed as capital allowances which cannot be claimed on buy to lets.

What are the options if the interest/tax cost is too much?

Change to a Furnished Holiday Let (AIR BNB) advantages continued

- If owned for 2 years then BADR reduces the CGT rate on any sale from 18%/28% to just 10%- this could be a massive saving on disposal18% of gain

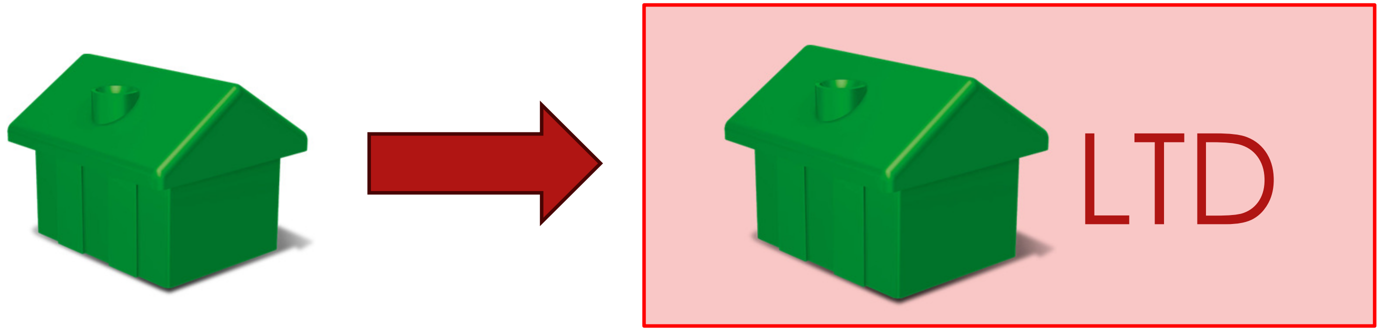
- Rollover of any gains into a further FHL is possible

But! Watch out for VAT if you are VAT registered in your own name, or rentals exceed £85k.

This can be worked around if jointly owned.

What are the options if the interest/tax cost is too much?

2. Incorporate



You can incorporate a company and move your rental properties into that company, there will be no restriction on interest relief in a company, but there are drawbacks:

- The mortgage will need to be changed to the company , this will have fees and likely a higher rate, this alone may outweigh the tax relief gained on the interest

- Stamp duty will likely be payable on the transfer , with a 3% surcharge, so an 8% effective rate on 250k-925k of property value

- There are schemes which try to avoid stamp duty by creating a partnership and then incorporating it to avoid SDLT but these must be very carefully considered and may not work

continued.....

What are the options if the interest/tax cost is too much?

Incorporation – continued

- Capital Gains tax may be avoided on the transfer of properties if there is incorporation relief on the property business, but a "business" must be accepted by HMRC

- The company deducts the full interest and any other costs and then pays corporation tax on its profits. If the money is sit in the company and then be invested again all is well, but as soon as the owners want to use the profits there is a second level of taxation, the owners could use salary, dividends, or interest on loans which all have varying levels of tax. Pension contributions may be used.

- If one day the property is sold and the business ceased then the company will make a capital gain on any rise in profits, and the full value of the company must then be distributed, probably via a formal liquidation and personal capital gains tax on the shareholders.

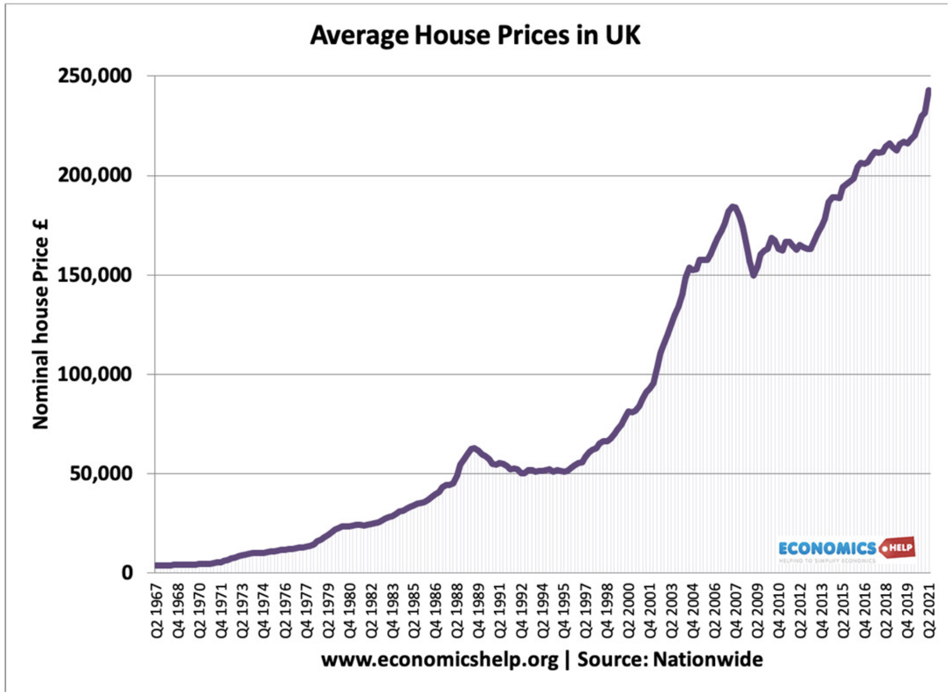
- Company rental set ups are costly to run each year and not easily undone once entered into.

What are the options if the interest/tax cost is too much?

3. Keep going

Continue as a buy to let landlord, possibly reduce borrowings, hope that after the higher rate period interest rates are lower, and long term property prices increase giving growth.

Rents are rising, don't allow rents to sit below market value. In the Autumn statement automatic planning for converting houses to two flats was announced, although may be some way off.



What are the options if the interest/tax cost is too much?

4. Sell the rental property

If making a gain, will give rise to a CGT charge payable and reportable within 60 days.

If owned jointly a gain on property will be split and have 2 x £6,000 CGT allowance to offset, dropping to £3k from 6 April 2024.

The CGT rate will be at 18%/28% so company owners may be able to plan other income to reduce the effective rate.

Reinvest cash into investment, pension, reduce other borrowings.

What are the options if the interest/tax cost is too much?

Property Tax Schemes

There are schemes marketed on social media such as property 118 that claim to work around the section 24 tax relief rules but these are being challenged by HMRC and should be very carefully considered.

Summary

Long term rentals that are not highly geared may still provide a good return, but there are options to change the nature of the rental or to cease being a landlord.

The company rental route can work in certain cases, but we have often seen clients come from other advisors with rental properties stuck in expensive companies with no real saving.

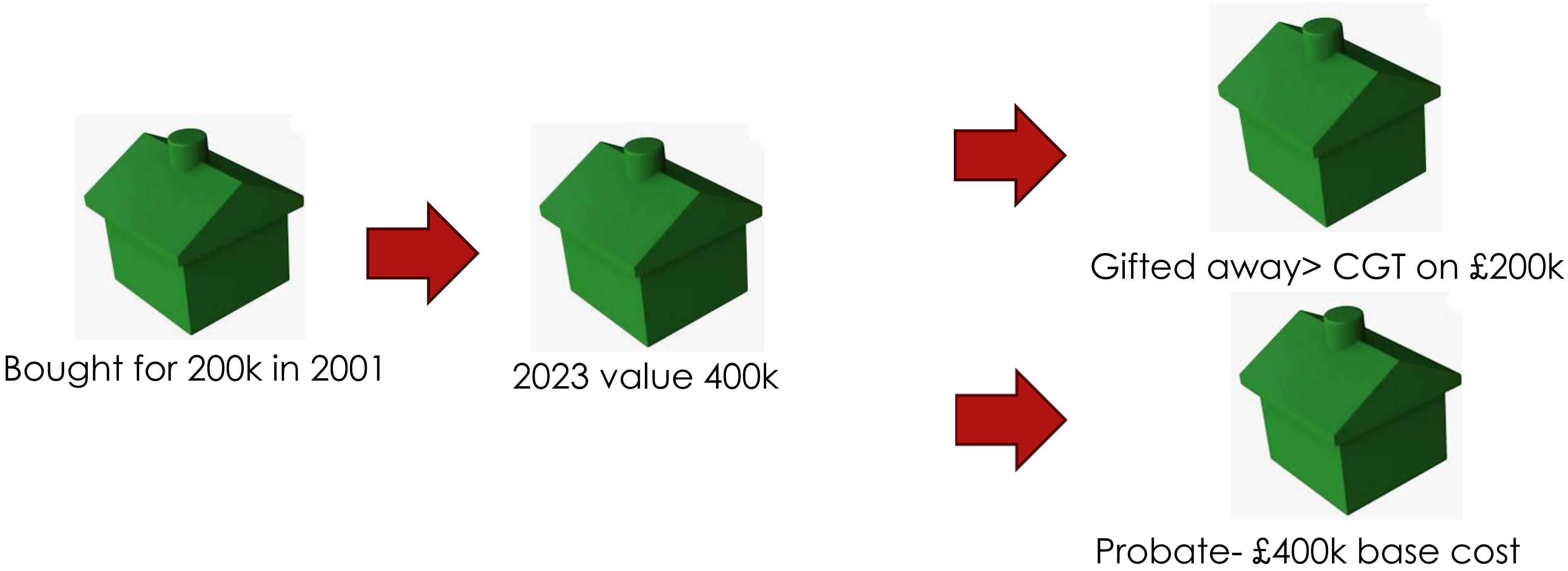
Review your return on capital invested and the tax on that return, get a market value from an estate agent or a lettings value from a holiday let agent.

Individuals who own a property and leave it to their descendants will likely have a £500k IHT allowance, doubling if they have a spouse and each leaves their estate to the other.

Rental properties will form part of any estate for IHT, so the value of properties (less any mortgages) together with other personal assets and liabilities should be considered to establish if any IHT will be payable upon death.

Transferring properties out of ownership can be part of estate planning but only if you are willing to give up the income. Any CGT gain sat in the property at market value would crystalise upon a gift even though no cash exchanges hands, so this must be weighed up against the beneficiary inheriting the property at market value after probate, with IHT paid.

It may be possible to holdover a capital gain on a property through use of a trust.



Inheritance Tax

Example

- Mr & Mrs A bought a buy to let for 200k it is worth 400k and their family home is worth 700k (no mortgage).
- Their son cannot afford a deposit for a property and they want to help.
- If they both pass away then the estate is 1.1m, IHT will be 100k @40%= £40k payable by the estate
- If they gift the buy to let to their son then a £200k gain (400k-200k) has been made, taxable at 18%/28%, likely a £45k tax bill !
- They decide instead to take a lifetime mortgage on their home of £100k, they gift the £100k to their son instead.
- If they survive the gift by 7 years and estate the same they now have no IHT exposure (but they do have an interest charge or will see the interest roll into the loan for their lifetime)

ANY QUESTIONS?