Income Tax

Income Tax is payable each year based on the profit from rental property.

Tax treatment of expenditure

Some expenses incurred when letting a property are allowable for tax purposes, but others are disallowable; common examples are:

Allowable

- Advertising the property for let
- Repairs to the property and general maintenance costs
- Cost of services provided to tenants, such as utilities
- Managing agents fees
- Insuring the building and contents
- Interest paid on any mortgage taken out to buy the property (but see below details of restrictions)

Disallowable

- Renovation work and improvements made to the property, for instance replacing an item with one of a higher specification or carrying out any work which was accounted for by a reduced purchased price for the property
- Capital repaid on any loan taken out to buy the property
- Costs incurred whilst the property is not available for letting
- Costs of purchasing/selling the property

These lists are not exhaustive, and we recommend that advice is sought regarding any expenditure incurred to ensure that the available tax relief is maximised.

Where an expense is not allowable for income tax it may be possible to obtain tax relief for these expenses when the property is subsequently sold: see "Capital Gains Tax" below.

There are additional rules regarding furnished holiday lettings, which may result in a claim for further deductions. Please see our separate brief guide for furnished holiday lettings.

Mortgage interest

Over the last few tax years, income tax relief on finance costs on residential properties has been gradually restricted.

The effect of the changes was to remove finance costs as an expense in calculating taxable rental profit.

For 2020/21 onwards, no deduction of finance costs as an expense is allowed, however a tax reduction of 20% of the finance costs is instead given against the taxpayer's income tax liability.

For example, if a taxpayers liability for 2020/21 was £15,432 and they had paid £5,000 in mortgage interest, the tax liability would be reduced by £5,000 x 20% - £1,000, the new tax liability then becoming £14,432.

Taxpayers should be aware that the non-deducibility of interest costs may cause adjusted net income to exceed various thresholds. For example, if net income exceeds £50,000 then child benefit would be progressively withdrawn.

Capital Gains Tax (CGT)

CGT may be payable when a property is sold.

In simple terms the gain is calculated as proceeds less the price originally paid for the property (or other appropriate base value in some cases). Additional relief is available for:

- Legal expenses
- Estate agents fees
- Stamp Duty Land Tax (SDLT)
- Any improvements to the property, including renovation work (assuming these costs have not qualified for relief under the income tax rules previously)

The amount of CGT payable will depend upon the length of time that the property is owned and whether the owner has lived in the property at any time during this period.

CGT – 60 day reporting on residential properties

A new 60 day (30 days for disposals prior to 27 October 2021) reporting and payment window has come into effect for sales of residential property where CGT is due. Where an individual is not UK resident, a return is required even where no tax arises.

A standalone return will have to be submitted to HMRC within 60 days of completion, along with a payment on account of CGT based on an estimated calculation of the gain.

Stamp Duty Land Tax (SDLT)

Purchases of additional residential properties completed on or after 1 April 2016 may be liable to higher rates of SDLT. The rates are 3% higher than the current SDLT percentages.

There are also further surcharges for non-UK residents purchasing residential property from 1 April 2021.

Administration

A Self-Assessment tax return will be required, including the supplementary pages for property letting and, if relevant, capital gains (note that if you filed a CGT return following disposal of a property earlier in the year, you will still need to report it again on your tax return). Any tax liability arising is payable by the 31 January following the end of each tax year.

It is necessary to register for Self-Assessment by 5 October following the tax year of commencement of the letting business. Penalties apply for late notification. HMRC also charge penalties where the tax return is submitted late and additional interest where the tax is paid late.

Find out more

In addition to the above, our specialist property investors group can also assist you with other property related matters, including:

- The furnished holiday letting regime
- Landlords resident overseas
- Non Resident CGT
- Private Residence Relief calculations
- Whether to hold your properties personally, or through a company

For further information, advice and guidance please contact one of our specialists in the property investors group:

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