Landlords and Buy-To-Let Taxation

In recent years, owning one or more properties has become more commonplace within the UK. This has been either to hold properties for their capital growth, or as a Buy-To-Let (BTL) property. Not only this, but due to the attractiveness of the UK property market, this has also led to a significant increase in interest from individuals from abroad. This has had a knock-on effect as first time buyers are finding it increasingly difficult to acquire their first property due to a supply shortage and sky-high prices.

As such, the UK government has been implementing new tax rules and policies to make the Buy-To-Let (BTL) less attractive with the aim of freeing up more properties for first time buyers. This guide runs through the most recent changes to the taxation on the BTL market.

Additional 3% Stamp Duty Land Tax (SDLT) on a second property.

A recent change is the introduction of a 3% SDLT surcharge for those individuals who acquire an additional property (although the 3% surcharge will apply to residential properties where the consideration is greater than £40,000). The additional charge will only apply if you own more than property at midnight on the day that the 2nd property is acquired.

The aim of this measure was to make it less attractive for individuals to acquire a second property and in particular, to discourage those wanting to invest in a BTL by increasing the initial cost required to acquire a property.

The only exception to the above is that if you are replacing your main residence, you will typically own two properties at the same time as it there is often overlap when it comes to disposing of properties. The exemption HMRC provide is that you will not be required to pay the 3% surcharge on the acquisition of your new main residence (so long as the previous main residence is disposed of within 36 months).

Capital Gains Tax (CGT) for non-residents

Up until April 2015, non-UK residents paid no capital gains on UK based assets which included properties. Therefore non-residents could buy and sell UK assets without suffering UK tax on their disposals (of course, they may suffer a similar Capital Gains charge in their country of residence).

However, from 6 April 2015, any UK residential properties would now be subject to UK CGT at a maximum rate of 28%. The amounts which would be chargeable to UK CGT would only be the gains arising from 6 April 2015 with prior gains still being exempt.

Wear and Tear – No More!

When you let out a property that is furnished (i.e. a tenant could live in it from day 1 without the need to buy furniture and utensils), the UK government used to allow landlords to claim a further deduction to reduce their taxable BTL profits. This was broadly 10% of the gross rents.

Effectively, as a landlord, you were being given a 'free' deduction to further reduce the amount of tax payable.

However, from 6 April 2016, the UK government abolished this and instead, replaced this with a reformed replacements basis. In essence, rather than obtaining a 10% of gross rents deduction, landlords will now be able to claim relief for the cost of replacement. This will only apply if the newly acquired asset is like-for-like or a nearest modern equivalent. If there is an enhancement, then the cost will not be deductible / allowed as a deduction.

Cap on Mortgage interest tax relief

One of the largest expenses for any landlord is typically the monthly mortgage interest payments. As such, HMRC and the UK government have introduced a cap to the tax relief available on this expense which is likely to have the largest impact on BTL owners.

The current 2016/17 tax year will be the final year in which landlords can deduct their mortgage interest payments in full against their rental profits. The aim of the measure is to cap the relief available on any interest payments to the basic rate of tax, currently 20%.

As such, many landlords will start to see a slow increase in their tax liabilities in relation to their rental properties as the relief is scheduled to be phased in gradually over the next 4 years with 2020/2021 being the first year where the relief is fully capped at 20%.

In essence, if you are a higher rate taxpayer (40%), and we assumed all tax rates and bands remained the same, your tax liability would increase by 20% of the total mortgage interest you pay which may cause some landlords with cash flow issues. An example of this is below

Pre Basic Rate Restriction

Rental Income - £20,000
Mortgage Interest - £8,000
Other Allowable Expenses - £2,000
Net Rental Profit - £10,000

Personal Tax at 40% - £4,000

Pre Basic Rate Restriction

Post Basic Rate Restriction
(As Above)

Personal Tax at 40% - £5,600

Difference - £1,600 (I.e. 20% of £8,000)

All in all, it is quite evident that the current UK government are implementing policies to make the BTL and property market less attractive for investors in the bid to increase supply for the first time buyers. Although we have seen a minimal effect of this to date, it is likely that further measures may be implemented in the years to come.

If you would like to discuss your property tax issues in more detail, please feel free to contact Wisteria's dedicated property tax team on 020 8429 9245 or email info@wisteria.co.uk for more information.

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