By Beatons Group

So you are thinking of buying a property to rent?

With the rate of interest available on bank deposits struggling to beat the rate of inflation, there is a significant number of people considering purchasing a property for a potentially higher rate of return.

The first stage is how to purchase the property. Do you set up a limited company? Own it jointly with your spouse? Do you use a mortgage or savings to fund the purchase? There isn't a fixed answer to each of these questions but the manner in which you purchase the property and how it is financed will have implications on the tax position throughout the period of ownership. You can potentially save significant sums in tax if you get it right.

Your tax

When you start letting your property, you should, within 6 months of the end of the tax year that the renting commenced, report to HM Revenue & Customs the new source of income. They will bring you within the scope of filing annual self-assessment tax returns to enable them to collect the taxes due on any rental income. HM Revenue & Customs now have increasingly sophisticated computer trawling systems to identify those who have not reported rental income and will now be pursuing these taxpayers with some vigour.

What costs can be offset

Once the property is purchased it is worth considering what expenditure can be offset against the rental income before tax. Start from the basis that all expenses in connection with the property may be allowed, then consider whether the expenses are in connection with the letting business or with the physical fabric of the property and its capital value.

For example the capital repayment element of the mortgage is in connection with the capital value and therefore not deductible against rents, but any interest charged is allowable. This is often one of the largest allowable expenses and therefore structuring your mortgage correctly can be a significant saving. Repairs generally incurred on the property are allowed, but those incurred prior to letting are often disallowed by HM Revenue & Customs on the basis they are capital expenditure to bring the property up to the standard necessary for letting.

Eventually selling

When you eventually sell the property you may potentially be liable to capital gains tax on the excess of sale proceeds over original cost. It is however worth noting that properties which have at any time been your main or only residence benefit from additional exemptions from capital gains tax. This is also a situation where how you have structured the property purchase is important.

If you have any questions regarding investing in property please do not hesitate to contact us.

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