PAY LESS TAX ON YOUR PROPERTY INVESTMENTS

HOW TO SAVE PROPERTY TAX

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Carl Bayley BSc FCA

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How to Save Property Tax

By Carl Bayley BSc FCA

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About the Author

Carl Bayley is the author of a series of 'Plain English' tax guides designed specifically for the layperson and the non-specialist. His aim is to help landlords, other business owners, and families understand the taxes they face and make savings through sensible planning and by having the confidence to know what they can claim. Carl's speciality is his ability to take the weird, complex world of taxation and set it out in the kind of clear, straightforward language taxpayers can understand. As he often says, "My job is to translate 'tax' into English."

Carl enjoys his role as a tax author, as he explains, "Writing these guides gives me the opportunity to use the skills and knowledge learned over almost forty years in the tax profession for the benefit of a wider audience. The most satisfying part of my success as an author is the chance to give the average person the same standard of information as the 'big guys' at a price everyone can afford."

He takes the same approach when speaking on taxation, a role he undertakes with great enthusiasm, including his highly acclaimed annual 'Budget Breakfast' for the Institute of Chartered Accountants. In addition to being a recognised author and speaker, Carl has spoken on taxation on radio and television, including the BBC's 'It's Your Money' programme and BBC Radio 2's Jeremy Vine Show.

Beginning his career as a Chartered Accountant in 1983 with one of the 'Big 4' accountancy firms, Carl qualified as a double prize-winner then began specialising in taxation. He worked for several major international firms until beginning the new millennium by launching his own practice, through which he provided advice on a wide variety of taxation issues; especially property taxation, inheritance tax, and tax planning for small and medium-sized businesses, for twenty years, before deciding to focus exclusively on his favourite role as author and presenter.

Carl is a past Chairman of the Tax Faculty of the Institute of Chartered Accountants in England and Wales; President of ICAEW Scotland; and member of the ICAEW Board. In June 2023, he stepped down after almost twenty years on the Institute's governing Council. He co-organised the annual Practical Tax Conference from 2002 to 2019.

Aside from his tax books, Carl is an avid creative writer and has just published his first novel, *Trinity of Souls*. When he isn't working, he takes on the equally taxing challenges of hill walking and horse riding: his Munro tally is now 106 and, while he remains a novice rider, his progress is cantering along nicely. Carl lives in the Scottish Borders, where he enjoys spending time with his partner, Linda. He has three children and his first grandchild arrived in April 2021.

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Introduction

Welcome to this thirtieth edition of *'How to Save Property Tax'*, fully updated for all the changes in property taxation that have taken place since our last edition.

Thirty editions on, it is astonishing to think it is more than twenty years since we first published this guide, and it is immensely satisfying to see the demand for good quality information on property taxation, coupled with sensible, practical, guidance on simple tax saving measures, continues unabated.

People in the UK have invested in property for centuries, but recent decades have seen property investment become a hugely important area of personal financial planning. The first few years of this century, in particular, saw phenomenal growth in the property sector, not just in the amount of property investment activity but also in the sheer numbers of people entering the property investment market. While the big flotations of the 1980s acted to spread investment in stocks and shares into all sectors of society; the early years of this century witnessed a similar spreading of property investment.

'Property investment' is a very wide term. At its simplest, buying your own home is usually most people's first property investment. Even this is not free from tax, as there will generally be Stamp Duty Land Tax (or its Scottish/Welsh equivalents) on the purchase and, of course, Council Tax to pay thereafter. Furthermore, any use of the property as anything other than your main residence may have Income Tax and/or Capital Gains Tax consequences.

Many people then go on to buy second homes, or invest in other property as a long-term asset. While some property investments are simply held for long-term capital growth, most such additional properties are rented out, with the investor thus becoming a landlord, and this, of course, is one of the main focuses of this guide.

As the property sector has grown more sophisticated, some investors have diversified beyond 'buy-to-let' and into other activities, such as 'buy-to-sell', 'let-to-buy' and, of course, a great deal of renovation, conversion, and development. Beyond these, there also lie the fields of property trading and management.

When increasing property prices raised the barrier to entry, people found other ways to invest in property, such as investing abroad, or clubbing together to invest through joint ventures, syndicates, or special purpose vehicles (SPVs).

All these different types of activity are subject to different tax regimes, and establishing the correct classification for each property investment can be quite difficult. One of my first tasks in this guide is therefore to help you understand how your property investments will be treated for tax purposes and this is something we will consider in depth in Chapter 2.

There are many reasons for becoming a property investor. Some fall into it by accident, finding themselves with a second property through marriage, inheritance, or other changes in personal circumstances. Others move into the property sector quite deliberately, seeing it as a safe haven providing long-term security and perhaps an income in retirement. Still others see the property market as a means to generate a second income during their working life.

Many landlords choose to enter the property business as a professional career. In fact, given the ever-increasing volume of rules and regulations the private rented sector has to contend with, a professional approach to property investment has now become essential: whatever your reasons for entering the property market in the first place. This is no bad thing: a professional approach has always been desirable. Those who are prepared to devote substantial time and resources to their business are generally rewarded with better results: including those who plan their tax affairs carefully.

The last twenty years have seen enormous changes in the property market. The 2008/9 banking crisis and its aftermath challenged previously held views on the certainty of capital growth and the philosophy of 'you can't lose'. But, while the economic difficulties instigated by the crisis were disastrous for some, they created opportunities for others. The lower interest rates enjoyed by investors for many years after the crisis brought healthy rental profits to many.

That 'golden age' has drawn to a close, as interest rates have risen again, and doomsayers begin to claim we stand on the brink of another crisis. Some might say it is the doomsayers who cause such crises, and each of us must form our own view of what the future is likely to hold. In the end, only time will tell but, whatever happens, periods of economic difficulty can be seen as part of an evolutionary process: the fittest property businesses will weather the storm and survive to become part of a stronger property sector.

As if economic uncertainty were not enough, for many years, the property sector has faced an unprecedented level of attack from a Government that appears to be hell-bent on its destruction. Quite where the Government expects to house all the former tenants now losing their homes as a result is a mystery to me!

Sadly, the numerous changes in personnel at 10 and 11 Downing Street we have seen over the last year or so have failed to put a stop to this unwarranted assault. Indeed, current Chancellor, Jeremy Hunt, has launched a further attack that will soon see many property owners suffering more than £5,000 in extra tax on property disposals compared with the position in the recent past.

With the Government continuing to take between 40% and 60% of many landlords' profits, PLUS what is effectively an additional penalty of between 20% and 40% on their mortgage interest; as well as 28% of their capital gains (a large proportion of which is usually down to inflation); and an extra 3% charge on their purchases; planning your tax affairs carefully is one of the best ways to ensure ***your*** property business is fit enough to survive.

There is no doubt these are hard times in the private rented sector. Nonetheless, despite the difficulties it faces, I believe the property sector as we know it, with its myriad range of investors of all types and sizes, is here to stay. Naturally, it will have its ups and downs, as any business sector does, but the idea of property investment as a career, or a pension plan, is now so well entrenched, it is impossible to imagine it ever disappearing.

Changes in both the economy and in tax legislation have always had a dramatic impact on the tax planning landscape, and will continue to do so. Tax and tax planning are a vital part of every business's strategy. Property businesses are no exception!

So, whatever your reasons for entering the property investment market, and whatever type of property business you have, my aim in this guide is to give you a better understanding of how the UK tax system affects you, and show you how to minimise or eliminate your potential tax liabilities. In other words, as it says on the cover: How to Save Property Tax!

In the first two chapters, I will set the scene by looking at the different taxes you will meet as a property investor and how they apply to the various types of property investments and property businesses.

Chapter 3 examines how annual income and profits from all types of property business is dealt with under the UK tax system. In Chapter 4, I focus on property letting businesses and the taxation of rental and other income derived from property investment. Chapter 5 looks at profits from property development and other property-based trading activities. These chapters include a detailed examination of the deductions, reliefs, and allowances available to every type of property business.

In Chapter 6, we move onto Capital Gains Tax, and explore the rules, the tax rates, the reliefs and allowances available, and the reporting and payment obligations relating to this vitally important tax for all landlords, property investors, and second home owners.

Chapter 7 covers Stamp Duty Land Tax and its devolved equivalents in Scotland and Wales: information vital to anyone purchasing property anywhere in the UK. Chapter 8 then looks at VAT, critically important to anyone renting out commercial property, holiday accommodation, or providing significant additional services to tenants; as well as property developers, agents, those carrying out renovations and conversions, and many others with property-based businesses.

Throughout the first eight chapters, there is an emphasis on simple, practical steps to minimise your tax burden, and to make meeting your tax obligations easier: so there is plenty of helpful tax planning guidance to get your teeth into. However, in Chapter 9, we step it up a notch, by looking at some more specialised areas, and pulling everything together with more advanced tax planning strategies that could help reduce your tax burden even further.

Along the way, you'll find plenty of **'Tax Tips'** to help you minimise or delay your bills; **'Wealth Warnings'** to keep you away from treacherous pitfalls; and **'Practical Pointers'** to make your obligations as painless as possible.

I believe this guide is comprehensive enough to meet the needs of almost every individual property investor based in the UK and I hope, with its help, you will be able to enjoy a much larger proportion of the fruits of your endeavours.

Finally, I would like to thank you for buying this guide, and wish you every success with your property investments.

Chapter 1

What is Property Tax?

1.1 KNOWING YOUR ENEMY

You cannot begin to consider how to save property tax until you understand what property tax is. In other words, you must know your enemy in order to combat it effectively.

There is no single 'property tax', but rather a whole range of taxes that apply to property. There is no point saving one of these only to find yourself paying even more of another!

Horror stories of this nature happen all too frequently, such as the taxpayer who managed to avoid 1% Stamp Duty on part of his new house, only to find he was stuck with a 17.5% VAT bill instead. Worse still was the taxpayer who undertook some Inheritance Tax (IHT) planning on the advice of his lawyer only to find himself with a £20,000 Capital Gains Tax (CGT) bill, with no sale proceeds from which to pay it. If only they'd spoken to a ***real*** tax expert first!

In this introductory chapter we will therefore take a brief look at the taxes that affect the property investor and give some consideration to the relative importance of each. Later, when we begin to consider tax-planning strategies, it is vital to bear in mind it is the overall outcome that matters, not simply saving or deferring any single tax. In fact, I would go even further …

> ***Bayley's Law***
> *The truly wise investor does not seek merely to minimise the amount of tax payable, but rather to maximise the amount of wealth remaining after all taxes have been accounted for.*

If this seems like no more than plain common sense to you, then all well and good. However, in practice, I am amazed how often people lose sight of this simple fact and, in trying to save tax at any price, actually end up making themselves worse off!

1.2 WHAT TAXES FACE A PROPERTY INVESTOR?

The only UK taxes specific to property that can apply to individuals are Council Tax (residential property); Business Rates (commercial property); and Stamp Duty Land Tax (SDLT) or its equivalents (Section 1.4).

However, as much as these taxes can be a painful thorn in the side, they are rarely as important as some of the other taxes that apply.

Property investment is exposed to a huge range of UK taxes. Tax is levied when property is purchased (SDLT), rented out (Income Tax), and sold (CGT); even when it is given away (CGT again). Property investors have to pay tax when they buy goods or services (VAT), when they make their investments through a company (Corporation Tax), and even when they die (IHT).

Those who are classed as developers or traders pay Income Tax and National Insurance (NI) on profits from property sales. Property developers must also operate and account for tax under the Construction Industry Scheme (CIS) when using sub-contractors for even the most routine building work.

Most property business owners will be paying Insurance Premium Tax, and those who employ help will have PAYE and employer's NI to pay too. Many will pay Road Tax (Vehicle Excise Duty) and duty on fuel as they travel in their business. They may even be paying Air Passenger Duty if their business takes them far.

Faced with this horrifying list, investors might be excused for turning to drink: only to find themselves paying yet more tax!

1.3 WHICH TAXES ARE MOST IMPORTANT?

For most individual property investors, two taxes comprise the majority of the tax burden they will face during their lifetime. These are Income Tax and CGT, and they are covered in detail in Chapters 3 to 6. The way these taxes will apply to ***your*** property investments depends on what type of property investor you are.

For tax purposes, there are a number of different categories into which a property investment, or property business, might fall, and it is crucial to understand how your investments or business will be classified before you can plan your tax affairs. I will return to this question in more detail in Chapter 2.

For some classes of investor, NI will form what is effectively an additional layer of Income Tax and we will examine this extra tax burden in Chapter 5. Other taxes that may also have a significant impact include VAT and the various forms of Stamp Duty. These are covered in Chapters 7 and 8.

For those investors using a company, Corporation Tax will become of equal, if not greater, importance to the two main taxes and IHT is likely to be a major concern for most property investors.

These two important taxes are covered in the Taxcafe guides *Using a Property Company to Save Tax* and *How to Save Inheritance Tax*.

1.4 PROPERTY STAMP TAXES

There are different forms of Stamp Duty on purchases and transfers of UK property, depending on which nation the property is located in:

England:	Stamp Duty Land Tax
Scotland:	Land and Buildings Transaction Tax
Wales:	Land Transaction Tax
Northern Ireland:	Stamp Duty Land Tax

The rules applying under each form of duty are broadly similar and are explained in detail in Chapter 7. For the sake of simplicity, I will refer only to Stamp Duty Land Tax, or SDLT, throughout the rest of this guide, but readers should bear in mind a different tax will apply to purchases of property in Scotland or Wales.