Vantage ACCOUNTING

A GUIDE TO buy-to-let

Introduction

Stagnant wages and rising living costs are driving people to find new ways to earn an additional income. Investing in a buy-to-let property can provide you with a steady stream of income, as well as offering you the chance to save and invest for the future.

Why is investing in buy-to-let properties a great idea? We think this quote from our literary wordsmith and Tax Manager, Sean Gregory, sums it up quite nicely;

"There are many ways to make money in this world... but none quite so satisfactory as a passive income."

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What is ‘passive income’?

If you’re not familiar with the term ‘passive income’, it refers to earning an income from something that you are not actively involved with. It is commonly associated with income that someone makes from a rental property.

Although we’re sure many landlords wouldn’t describe managing a rental property as being ‘passive’!

Whether you’re considering becoming a landlord for the first time, you’re on the cusp of purchasing a second property or are looking to become the next big property tycoon, we can help you achieve your goals. With 20 plus years’ experience working with individuals and small businesses, we are proud to class ourselves as experts in property Accountancy and Taxation.

We understand that being a landlord is becoming a more complicated proposition and we’re sure you have many questions.

So, we’ve put together this brief guide to look at the pros and cons of becoming a landlord and the options available for funding a buy-to-let property.

Am I ready to become a landlord?

There are many reasons to become a landlord. From conversations we've had with our clients over the years, the most common reasons are:

- To make use of an inherited property
- As a source of additional income
- For investment purposes/capital appreciation
- To gain an income from the family property whilst working overseas

Whatever the reason, here are some things to consider first:

Pros	Cons
Additional Income	The extra taxes that come with earning an additional income
Investment	Extra time and resources spent on managing the investment
The opportunity to build a portfolio of properties	Market volatility; property prices and demand for rental properties, can go up as well as down

How to purchase a buy-to-let property

There are two main ways to purchase a buy-to-let property, either through **personal ownership** or through a **limited company.**

Due to the recent changes in legislation which has arguably adversely affected landlords, many are considering the incorporation route; this is in part to avoid the changes in how mortgage interest (very often the biggest single expense a landlord has to face) and other finance charges are treated as expenses.

A company can still claim 100% relief on interest relating to the purchase of a property, whereas an individual cannot do the same. While this may sound like a big enough reason to incorporate, there are other considerations.

Should i purchase through a limited company?

The first major obstacle to incorporation is if you already own the property. You will effectively have to sell the property to your own limited company – which will give rise to a capital gain and stamp duty.

In broad terms, if you want to gain immediate access to any profit generated from your rental property, it is better to own the property personally. That way, you are only taxed on the profit you make at your relevant rate of tax.

A limited company will add an additional layer of tax on your profits. Firstly, your company will be taxed on its profits, via corporation tax (currently 19%). Then, you will be taxed on the drawings you make – these will normally be dividends and are taxable at 0% for the first £2,000, then 7.5%, 32.5% and 38.1% dependant on levels of other income.

Another consideration is that when you come to sell the property, you will as the personal owner have the benefit of a capital gains allowance to offset some of the taxable gain. This is doubled if you own the property with a partner. There is no such allowance if the company decides to sell up.

If, however you want to leave the profits in your company to build up capital and purchase more properties, then the incorporation route may be the way to go.

Lastly, obtaining a mortgage for a company is sometimes a trickier proposition than as an individual, again we can help with this process by referring you to our associated financial advisers, who are specialists in buy-to-let mortgages.

Responsibilities as a personal ownership landlord

If you take ownership personally, then it's your responsibility to keep accurate records of your income and expenses that relate to the buy-to-let property.

HMRC expect details of your income and expenses to be available to them on demand if they wish to see them. With this in mind, we can help you organise and keep track of your ingoings and out-goings by providing the tools necessary to keep a clear record of how your taxable rental income has been arrived at.

As with any income that has come about through self-employment, you are responsible for submitting details of this income to HMRC through your online self-assessment and for the payment of any tax liabilities.

Self-assessment tax returns need to be submitted and any tax liability paid in full by midnight on 31st January, following the tax year-end. There are fines and penalties for late submission and payment. Plus, interest will be applied to any outstanding amount. This can soon add-up so it's important to get it done on time.

How do i submit self-assessment tax returns?

This can be done via HMRC online services (if you have registered). It is also possible for a third party to do this for you. We offer this service as part of our specialist landlord accounting packages.

What to expect if you decide to incorporate

Purchasing a property through an incorporated company is sometimes referred to as a Special Purpose Vehicle or SPV.

The first thing to think about when looking at renting a property through a limited company is that the company will be a separate legal entity to yourself. This means that any profits, assets and liabilities all belongs to the limited company rather than you as an individual.

CORPORATION TAX	LIMITED LIABILITY
Tax is another big consideration, especially if you earn more than £50,000 from a job or another source of income. The new property company would pay corporation tax (currently 19%) on the profits, with the profit after tax being available to be distributed as a dividend to the shareholders. The tax advantage here is that you can choose whether to take the dividend or leave it in the company. This can vary year on year depending on your own personal circumstances.	One of the biggest reasons that many choose to "go limited" is for limited liability. This essentially means that you can only lose what you put into the company. The important consideration with a company used for letting is that the mortgage provider will sometimes ask that you as an individual personally guarantee the finance, effectively rendering the limited liability almost a void point.

How to fund a limited company

When the company is formed, it will be set up with an initial share capital, normally £100, to allow each share to represent 1% of the company. This will be the initial funding of the company. Sadly, you're not able to acquire your rental property with just your £100 investment!

Below are some ways in which you can fund your company and, ultimately, fund that property purchase:

Director's loan

You, as the owner/director, can lend the company money to fund the purchase. Any amounts introduced to the company are simply an unsecured loan and don't need to have any fixed terms for repayment or interest. Plus, the repayments of this loan are tax free. Sometimes it's tax-beneficial for a Director to charge interest on a loan to their company anyway and make use of their personal savings allowance.

Loan from family and friends

A loan from family or friends works in a similar way to that of a director's loan, but the repayment amounts would be due to the family member or friend rather than yourself as director.

Mortgage

This is the most common way to fund your company. Your company will obtain a mortgage directly and any interest on the mortgage will qualify as a business expense in full.

Business to business loan

If you already have another trading limited company, then you could look at lending the funds from one of your companies directly to another. The key advantage of this is that you wouldn’t pay income tax on the dividends you draw from your company in order to inject into the new company as a director’s loan.

We strongly recommend that you speak to us before doing this so as to ensure you don’t accidentally give yourself a personal tax bill.

Limited company director's responsibilities

As a director of a limited company, you must adhere to the rules set out by The Companies Act and tax legislation. These include legal and financial responsibilities, such as:

Annual accounts

These need to be submitted on an annual basis to Companies House. This is typically done within nine months of the year end date.

Confirmation Statement

The Confirmation Statement is submitted to Companies House on an annual basis. This provides them with up to date information on your limited company. This information includes details on directors, the shareholders, and the company's address.

Real time information

Information must be sent to HMRC about an employee's salary and associated deductions before, or at the same time as the payment is made.

Corporation tax returns

The Corporation Tax Return needs to be submitted to HMRC with a set of year end accounts.

Top tip: For simplicity, we advise our clients to submit this at the same time as sending documentation to Companies House.

ATED Returns

ATED Returns stands for Annual Tax on Enveloped Dwellings. This is an annual form that should be completed if your property has a value of £500,000. If your property is let on a commercial basis then there should not be any liability arising from this. If you can, it's important to ensure that your property is exempt, as tax liabilities can become significant. If you're unsure if your property can be exempt, we are happy to provide guidance on this.

Paying PAYE and NIC

If your payroll is run on a monthly basis, you need to inform HMRC via Real Time Information (RTI) of any PAYE and NIC payments due. Payment should be made by bank transfer. It may or may not be tax efficient for a salary to be run from your company.

Let’s talk about expenses

One of the questions we frequently get asked is, “How can I minimise my tax liability?”

To ensure that the tax liability on your rental profit is a small as possible, it’s vital that you keep accurate records of the expenses your rental property has incurred.

The rules are complex surrounding what can and can’t be claimed for as expenses for residential properties and furnished holiday lets. However, we’ve summarised it for you here:

In general, allowable expenses are things you to spend money on as part of the day-to-day running of the property.

This includes:

- Letting agents’ fees
- Legal fees for lets of a year or less, or for renewing a lease for less than 50 years
- Accountants’ fees
- Buildings and contents insurance
- Interest on property loans
- Maintenance and repairs to the property but not improvements
- Utility bills
- Rent, ground rent, service charges
- Council Tax
- Services you pay for
- Other direct costs of letting the property
- Replacement cost of furnishing, though not the initial purchase.

TAKE THE TEST:

Is buying through a limited company right for you?

We've put together a simple 10 second test to determine if purchasing a buy to let property through a limited company is the right option for you:

If you answer yes, to all five questions, becoming incorporated is something you should consider:

1. Are you looking for a long-term investment?
2. Are you a higher rate tax payer or looking at funding via your company?
3. Can you confirm you will never live in the property?
4. Can you confirm you will not let to a family member?
5. Are you happy to keep the funds in the company if more tax efficient?

Thanks for reading. Need more help?

We hope that our guide has been useful to you. Embarking on a buy-to-let property can be challenging but, ultimately, a very rewarding experience.

Careful planning of buy-to-lets is essential. We would be happy to discuss the options with you. Give us a call on 01962 820375 or send us a message through our website for further advice.

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