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FOCUS ON

Tax changes to property income

There have been a number of recent changes to the legislation relating to the taxation of property income.

This summary is provided as an overview and further guidance from our Tax team should be sought

Interest Relief - Residential Buy to Let Properties
The new rules apply to individuals, partnerships and LLP's.

There are new rules on mortgage interest on residential Buy to Let properties which come into effect from April 2017. At the moment, mortgage interest is fully deductable from rental profits but over the tax years from 6 April 2017 to 5 April 2020, a restriction will apply as follows:

- 2017/18 – 75% interest full deduction: 25% interest relieved at basic rate of income tax;
- 2018/19 – 50% interest full deduction: 50% interest relieved at basic rate of income tax;
- 2019/20 – 25% interest full deduction: 75% interest relieved at basic rate of income tax;
- 2020/21 – 100% interest relieved at basic rate of income tax

The basic rate relief on interest will be given as a tax reduction in the individual's tax computation for the year, rather than as a deduction from the rental profit. The tax reduction will be 20% of the lower of the interest affected, the rental profits, and the individual's income (excluding savings and dividend income) for the year. Please see overleaf for an example of how the new rules will increase the tax liability for a higher rate taxpayer.

Where the loan interest exceeds the rental profits in a year the excess will be carried forward for potential relief in subsequent tax years.

The new rules apply to 'costs' of a dwelling related loan and therefore extend to other deductions including incidental costs of obtaining loan finance. A loan taken out to acquire a motor vehicle used in the management of a property business will also have a restriction to the allowable interest.

The rules do not apply to a property business being carried on by a company including a non-resident company subject to income tax nor a loan taken out for a furnished holiday letting business.

Example: Higher rate taxpayer (paying income tax at 40%). Annual rental profit is £30,000. The property has a mortgage of £450,000 suffering a 5% rate of interest therefore £22,500 of interest payments arise each year (assuming no capital repayments).

	2016/17	2017/18	2018/19	2019/20	2020/21
Rental profit before interest relief	£30,000	£30,000	£30,000	£30,000	£30,000
Mortgage interest					
100% allowable	(£22,500)				
75% allowable		(£16,875)			
50% allowable			(£11,250)		
25% allowable				(£5,625)	
0% allowable					-
Taxable rental income	£7,500	£13,125	£18,750	£24,375	£30,000

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Income as tax reducer					
(£22,500 - £22,500) @ 20%	-				
(£22,500 - £16,875) £5,625 @ 20%		(£1,125)			
(£22,500 - £11,250) £11,250 @ 20%			(£2,250)		
(£22,500 - £5,625) £16,875 @ 20%				(£3,375)	
(£22,500 - £0) £22,500 @ 20%					(£4,500)
Net tax due	£3,000	£4,125	£5,250	£6,375	£7,500
Net cash remaining[1]	£4,500	£3,375	£2,250	£1,125	-

[1] Net cash remaining = £30,000 - £22,500 - Net tax due for the year

Wear and tear allowance reform

The wear & tear allowance and the renewals allowance for property businesses will be repealed. Instead, with effect from 6 April 2016, a deduction can be made for capital expenditure incurred by a lessor on replacing furnishings and appliances including white goods and kitchenware in a dwelling house. No relief is available for fixtures.

If the new item is substantially the same as the old item, the deduction is equal to the expenditure incurred on the new item. If the expenditure incurred involves a substantial improvement to the replacement, the deduction must be restricted to the cost of a similar replacement.

The deduction is not available for furnished holiday lettings or where rent-a-room relief has been claimed.

Contact us

For advice on investing in or disposing of residential property or assistance with filing your ATED return, please contact your local office.

Alternatively, email your enquiry to us at info@mhllp.co.uk

Capital Gains Tax (CGT) for non-UK Resident Individuals

From 6 April 2015 non UK Resident individuals, personal representatives, trustees & partners are subject to capital gains tax on the disposal of a UK residential property. The capital gain is calculated by reference to the increase in value of the property between 6 April 2015 and the date of disposal.

In addition, there are now limited circumstances in which a non-resident can elect for the UK residential property to be their main residence and thereby claim Principal Private Residence (PPR) relief. In essence, the non-resident has to spend at least 90 nights in the property during the tax year in order to claim the relief (and not at the same time become UK Resident by spending too many days in the UK under the new Statutory Residence Test).

CGT: payment window

From April 2019, a payment on account of any CGT due on the disposal of residential property will be required to be made within 30 days of the completion of the disposal. This will not affect gains on properties which are not liable for CGT due to PPR Relief. The government will publish draft legislation for consultation in 2016.

Stamp Duty Land Tax

A new additional rate of 3% SDLT will apply to purchases of buy-to-let residential properties and second homes over and above the normal rate with effect from 1 April 2016.

Band (£)	Existing SDLT Rates	New SDLT rates
£0-£125k	0%	3%
£125k-£250k	2%	5%
£250k-£925k	5%	8%
£925k-£1.5mn	10%	13%
£1.5mn+	12%	15%

	Current SDLT	New SDLT (from 1/4/16)	Increase in Tax
£100k	£0	£3k	£3k
£150k	£500	£5k	£4.5k
£250k	£2.5k	£10k	£7.5k
£350k	£7.5k	£18k	£10.5k
£450k	£12.5k	£26k	£13.5k

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