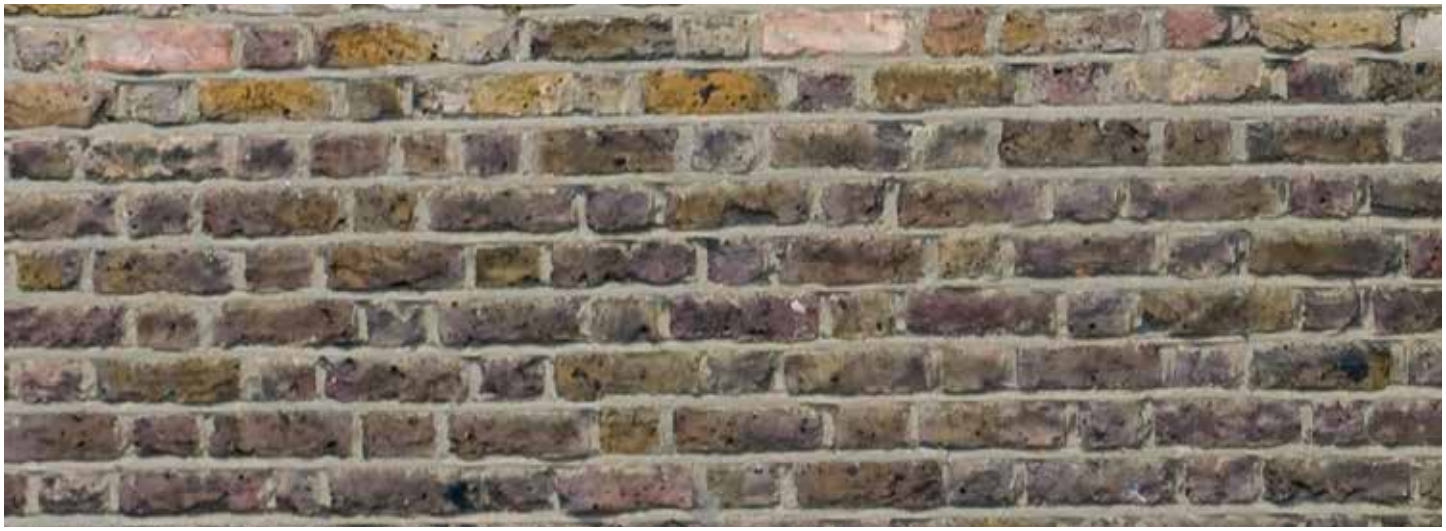
wmt

Incorporation of a property business

Briefing notes for landlords



Many landlords and property investors consider owning their property portfolios through a limited company rather than owning the properties personally.

The ideal way to own buy-to–let properties depends on a number of factors. These include long term exit or succession plans, taxation - especially in light of recent changes - and the bank's willingness to re-finance any borrowings.

This briefing sheet expands on these key elements, providing insight into the complexity of the decision and the points that need to be kept in mind.

Taxation implications

Properties can be held by individuals, by companies, or in a trust. How properties are held has an impact on:

- income tax
- corporation tax
- loan interest tax relief
- capital gains tax
- stamp duty land tax
- the annual tax on enveloped dwellings
- inheritance tax.

Comparison of income tax v corporation tax

Rental income from properties held by individuals is taxed at 40% once income levels reach over £50k. The tax rate rises to 45% once income is in excess of £150k. Corporation tax paid on company profits is currently 19% and is due to decrease to 17% by 2020/21.

The disparity in tax rates makes a company seem more tax efficient, but it is necessary to compare like with like. The taxation costs when withdrawing the available profits from the company need to be brought into the equation.

Profit can be withdrawn as income in the form of salary or dividends. A salary is taxed under PAYE and may also be subject to National Insurance. Dividends are taxed (subject to a £2,000 nil rate band) at 7.5% for a basic rate taxpayer, 32.5% rate for a higher rate taxpayer and 38.1% for an additional rate taxpayer (total income over £150k).

The cost of filing company accounts and an annual return at Companies House also needs to be borne in mind.

However, a company does not necessarily have to distribute it's profits once the corporation tax is paid. The profit can remain within the company and be paid out to the shareholders at a later date. Extracting profit when an individual's overall income levels have decreased (eg after retirement) could result in paying a lower rate of income tax.

Loan interest changes

From April 2020, it will no longer be possible to deduct loan interest from rental income. It will be replaced with a basic rate tax reduction from the overall income tax liability.

There are transitional rules in place that will restrict the loan interest deduction at an increasing rate of 25% for each year between April 2017 and 2020. There will be a corresponding increase in basic rate tax relief over the same period.

These restrictions to loan interest will have a considerable effect on those individuals with substantial borrowings on their property portfolios.

Capital gains tax on the sale of the properties

A higher rate taxpayer will suffer capital gains tax at 28% on the property gain. This is calculated on the difference between the proceeds and the original cost, minus any available annual exemption allowance (2019/20 - £12,000).

In contrast, a company will be able to claim indexation on the original cost up to December 2017 and pay lower corporation tax on the gain but does not receive an annual exemption allowance.

The loss of the annual exemption versus the lower corporation tax rates adds to the mix of uncertainty about the overall tax savings. These savings may be reduced further by the additional personal tax liability on any profits from a property sale that are withdrawn from the company.

Stamp duty land tax (SDLT)

Since 1 April 2016, a 3% higher rate of SDLT has applied to acquisitions of residential properties, unless it is a purchase or replacement of the main home. This rate applies whether the property is acquired by an individual or a company. There are some reliefs that may be available for investors with larger portfolios.

Annual tax on enveloped dwellings (ATED)

Companies that own UK property valued at more than £500,000 are subject to an annual tax on the value of the property if it is not used for trading or let comercially to unconnected parties.

Tax charges can arise if the property is occupied by an individual who is connected to the owner of the property. Normal property letting to unrelated third parties on a commercial basis will be covered by the reliefs, although annual filing obligations for an ATED return still remain.

Inheritance tax and succession planning

With a company, it is the value of the shares held that form part of an individual's estate for inheritance tax purposes. If properties are owned personally each is separately valued as part of the estate for inheritance tax purposes.

Owning the company rather than the properties means that the value of the shares can be transferred to the next generation, rather than the properties. This is likely to provide greater flexibility for inheritance tax planning.

There are other alternatives if an element of flexibility is required. Trusts can be used to pass the properties on to the next generation.

Tax planning

It can be costly to move a property portfolio from personal to corporate ownership. There is the risk of triggering capital gains tax and stamp duty land tax liabilities on the transfer. With careful tax planning it is often possible to transfer ownership of the properties into the corporate structure over time, to minimise excessive tax charges. There are also VAT issues to take into account on transfer.

How we can help

Whether you are just about to set-up your property business or are already well established, WMT can advise on the best way to hold your portfolio in your particular circumstances. Our advice is always based on an understanding of your current and long term goals, as well as your personal and commercial tax position.

Guideline pricing

We provide a no-obligation consultation on the taxation implications of incorporating your property business for £350 (plus VAT). The cost of the consultation will be offset against the cost of any subsequent work we undertake.

The table below shows the range of reports available with their associated prices. Fees will vary in line with the complexity of your situation, but you will always be advised of the final cost before we begin the report.

Report on setting up a company and comparison of income tax v corporation tax on net income.	£1,500 - £2,000 (plus VAT)
Report on the taxation implications of incorporating an existing property business and recommendations on how to structure it.	£2,000 - £3000 (plus VAT)
Full report on incorporating a property business with long term inheritance tax planning on the owner's whole estate.	from £3,000 (plus VAT)

Our reports contain both analysis and recommendations that will give you the information you need to make your decision. If you choose to incorporate your business, we can set up the company for you and meet your ongoing advice and compliance needs.

To arrange a no-obligation consultation, please contact:

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