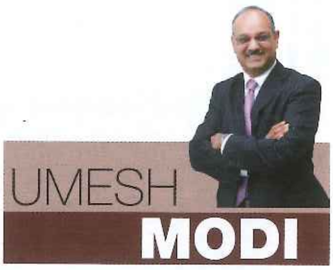
Umesh Modi

Property Investment - Buy to Let

Umesh Modi looks at why purchasing a buy-to-let property in the UK can be a good long-term investment



The UK property market, whilst cyclical, has proved over the long-term to be a very successful investment. This has resulted in a massive expansion in the buy to let sector.

Buy to let involves investing in property with the expectation of capital growth with the rental income from tenants covering the mortgage costs and any outgoings.

However, the gross return from buy to let properties – i.e. the rent received less costs such as letting fees, maintenance, service charges and insurance - is no longer as attractive as it once was. Investors need to take a view on the likelihood of capital appreciation exceeding inflation.

Factors to consider

Do

- think of your investment as medium to long-term
- research the local market
- do your sums carefully
- consider decorating to a high standard to attract tenants quickly.

Don't

- purchase anything with serious maintenance problems
- think that friends and relatives can look after the letting for you - you're probably better off with a full management service
- cut corners with tenancy agreements and other legal documentation.

Which property?

Investing in a buy to let property is not the same as buying your own home. You may wish to get an agent to advise you of the local market for rented property. Is there a demand for say, two bedroom flats or four bedroom houses or properties close to schools or transport links? An agent will also be able to advise you of the standard of decoration and furnishings which are expected to get a quick let.

Agents

Letting property can be very time consuming and inconvenient. Tenants will expect a quick solution if the central heating breaks down over the bank holiday weekend! Also do you want to advertise the property yourself and show around prospective tenants? An agent will be able to deal with all of this for you.

Tenancy agreements

This important document will ensure that the legal position is clear.

Taxation

When buying to let, taxation aspects must be considered.

Stamp Duty Land Tax (SDLT)

From 1 March 2019, buyers of property are required to file the SDLT return and pay the SDLT tax within 14 days of the date of acquisition. Previously the time limit was 30 days.

Tax on rental income

Income tax will be payable on the rents received after deducting allowable expenses. Allowable expenses include repairs, agent's letting fees, an allowance for furnishings and a proportion of the mortgage interest.

Restriction loan interest relief for 'buy to let' landlords

Rules have been introduced which restrict the amount of income tax relief landlords can get on residential property finance costs to the basic rate of income tax. Finance costs include mortgage interest, interest on loans to buy furnishings and fees incurred when taking out or repaying mortgages or loans. No relief is available for capital repayments of a mortgage or loan.

Landlords are no longer able to deduct all of their finance costs from their property income. They will instead receive a basic rate reduction from their income tax liability for their finance costs. To give landlords time to adjust, the change is being introduced gradually from April 2017, over four years. The restriction in the relief is being phased in as follows:

- in 2017/18, the deduction from property income is restricted to 75% of finance costs, with the remaining 25% being available as a basic rate tax reduction
- in 2018/19, 50% finance costs deduction and 50% given as a basic rate tax reduction
- in 2019/20, 25% finance costs deduction and 75% given as a basic rate tax reduction
- from 2020/21, all financing costs incurred by a landlord will be given as a basic rate tax reduction.

This restriction does not apply to landlords of furnished holiday lettings.

Replacement of furnishings

A relief enables all landlords of residential dwelling houses to deduct the costs they actually incur on replacing furnishings, appliances and kitchenware in the property. Relief is due on the cost of replacing furnishings to a wide range of property businesses.

Examples of eligible capital expenditure are:

- furniture
- furnishings
- appliances (including white goods)
- kitchenware

but excludes items which are fixtures.

However the relief is limited to the cost of an equivalent item if there is an improvement on the old item. The deduction is not available for furnished holiday lettings or where rent-a-room relief is claimed.

Tax on sale

Capital gains tax (CGT) will be payable on the eventual sale of the property. The tax will be charged on the disposal proceeds less the original cost of the property, certain legal costs and any capital improvements made to the property. This gain may be further reduced by any annual exemption available.

CGT is generally charged at 10%, within the basic rate and 20% for higher rates. However 18% and 28% rates apply to chargeable gains arising on the disposal of residential property that does not qualify for private residence relief.

From April 2019, non-UK residents will have to report and pay CGT on disposals within 30 days of the disposal. This will extend to UK residents from April 2020 but will not apply to gains on properties which are not chargeable to CGT, for example where the gains are covered by Private Residence Relief.

This article is based on current legislation and practice and is for guidance only. Specific professional advice should be taken before acting on matters mentioned here.

Umesh Modi BA ACA is a Chartered Accountant and Tax Advisor, and a partner at Silver Levene LLP. He can be contacted on 020 7383 3200 or umesh.modi@silverlevene.co.uk