INVESTING IN PROPERTY – PERSONAL OR COMPANY OWNERSHIP

2020/2021

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PROPERTY

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‘Investing In Property – Personal Or Company Ownership 2020/2021’ – First published November 2020.

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About Jennifer Adams

Jennifer Adams FCG TEP ATT (Fellow) has been a professional business author for over 15 years, specialising in corporate governance and taxation. She is also the proprietor of her own accountancy firm and as such, she is well placed to advise on tax problems that companies and their directors may face.

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- Tax Tips for Company Directors Guide
- How to use Trusts to Reduce Property Taxes Guide
- Dividend Tax Savings Strategies Explained Guide
- How to Maximise Landlord Expenses Guide

About This Guide

Being a landlord is not for the faint-hearted. The past five years have been difficult for many buy-to-let investors as successive governments have introduced measures that have arguably made this form of investing less appealing for some - particularly residential landlords. Indeed, in the current Covid-19 pandemic environment many tenants have taken advantage of the governments' ruling and deferred payment of rent. We may find that the government goes further seeing tenants being given greater rights and capital gains tax rates on the sale of non-main residence properties increasing. However, in an era where interest rates on bank accounts and other investments are either very low or unsecure and returns on pensions being squeezed then property investment produces the benefit of rental income and capital growth. Even with the challenge of the coronavirus and the potential impact of Brexit, the UK property market remains a suitable alternative for many investors.

Whether you decide to invest in property as an individual or via another medium be that a limited company, partnership or Limited Liability Partnership, or whether the property is commercial or residential, there are tax issues to consider. This guide sets out the tax implications for each method of ownership highlighting the tax traps in property investment.

1 Property Investment Options

Direct investment in property can be undertaken within a variety of structures, the most common being as an individual (or partnership) or as an investment company limited by shares. Other options include the use of a Limited Liability Partnership (LLP), a trading company or a pension scheme.

Although recent years have seen several changes to the taxation of property, those changes have been in respect of residential property rather than commercial; the exception being the extension of the Capital Gains Tax regime to include non-resident landlords owning UK commercial property as from 6 April 2019. The following section compares the differences between investing as an individual purchaser or partnership (including LLP's) as opposed to investing as a shareholder in a company that buys the property (an investment company).

1.1. Companies

There are many reasons why a property investor might use a limited company rather than purchase property in his/her own name (or in partnership). One of the main reasons relates to the differences in taxation. There are differences between the taxation of residential property and commercial property when considering VAT, Stamp Duty Land Tax (SDLT) but these taxes are the same whether the property is owned by an individual (or partnership including an LLP) or a company although the tax rates may differ. Otherwise the main difference is evident when the time comes to take monies out of the business.

There are other reasons for incorporation not least that a company has its own legal identity such that third parties contract with the 'company' and not the individual directors or shareholders. This means that companies can survive the death of the owners and there is the added flexibility for directors and/or shareholders to change. A company's existence will only cease when it is formally dissolved.

Another important reason for using a company is that companies have limited liability for the debts of the business, the extent of the liability being the amount paid for the shares plus, the unpaid amount on any nil or partly paid shares (if any). In practice the liability is usually restricted to the amount paid for the shares unless personal guarantees have been given. However, in certain cases, a company director can be held personally responsible for debts of the company when the company continues trading whilst insolvent. This limit on the shareholders' liability contrasts with sole traders or partnerships where there is the potential for unlimited personal liability (e.g. the private residence is at risk).

1.2. Partnerships

The rental profit or loss incurred on a property held jointly (or held within a partnership proper) need not be allocated in the same proportion as the underlying ownership. Where a genuine partnership exists the profits and losses from that business can be allocated between the partners in any ratio that the partners agree on and that ratio may be varied from year to year. Usually joint property ownership between spouses are allocated 50:50 unless the underlying ownership of the property is different.

As mentioned above the liability of an individual or partnership can be unlimited however, partnerships can be created with limited liability. This allows for a partnership structure but where each partner's liabilities are limited to the amount they put into the business.

Limited Liability Partnerships (LLP's) are a popular vehicle for holding a property portfolio. They are not partnerships as such but corporate entities sharing most features in common with companies (i.e. separate legal personality, limited liability protection, etc.) except that the individual owners are taxed on their share of the LLP's income or gains. The tax rate applied is therefore at each partner's marginal rate of tax, which could be as high as 45% plus there will be National Insurance implications irrespective of whether those profits are extracted by the partners or retained and reinvested in the business. The planning comes with allocating the profit to the partner(s) with the lowest marginal tax rate.

Being a partner or owning assets used in a partnership business will generally mean that such individuals will be able to take advantage of more exemptions or deferment claims on the disposal of assets or of part or all of the partnership share (provided all the other conditions associated with the particular relief apply) than are available to companies.

The table below shows the differences between each vehicle in relation to tax followed by explanatory details under each heading:

	Individual or partnership owner	Company owner
Tax Rates: (see section 2)	Profits taxed at owner's marginal rate. 20%, 40% or 45%	Profits taxed at corporation tax rate – 19 per cent
(section 2.1)	Property Tax Allowance available	
Payment date of tax	Payments on account due 31 Jan in tax year; 31 July after. If any balance is due then it is payable 31 Jan after tax year	Nine months and one day after the accounting year end
Loan interest: (section 3)	Relief given as basic rate reduction – fully allowable if FHL	Amount paid restricted to 30 per cent of profit subject to a 'de minimus' threshold of £2 million, otherwise allowable in full.
Losses (section 4)	No sideways loss against other income or gains – can only be offset against other rental income or carried forward unless FHL. There may be restrictions if the property is not let on a commercial basis. Loss 'cap' = the greater of £50,000 and 25 per cent of total profits on trading and property for the tax year relating to capital allowances	Offset against total profits of current year and then carried forward. Total profits include chargeable gains. Loss 'cap' = the greater of £5 million and 50 per cent of the next accounting period's profits

	Individual or partnership owner	Company owner
Extraction of funds: (see section 5)	Profits available after income tax and/ or capital gains tax has been levied.	Different methods of withdrawal. Individual must be either a director or a shareholder or both. May be tax deductible for company depending on method. Tax liability for individual will depend on method and available personal allowances.
Capital gains tax (see section 6)	Annual exempt amount of £12,300. Balance taxed at 18% if basic rate taxpayer; 28% otherwise. 20% on commercial property - Business Asset Disposal Relief may be available. Incorporation is capital disposal for CGT purposes. Incorporation relief, Gift relief/'hold over' relief and 'Roll over' reliefs may be available.	No allowances – taxed at 19% corporation tax rate (from 1 April 2020). Indexation allowance available albeit frozen at December 2017. 'Roll over' relief may be available.
Additional taxes: (see section 6.3)	VAT -none on residential.	Annual Tax on Enveloped Dwellings (ATED) – applies to high value residential properties held within a company that are not let on a commercial basis. VAT - none on residential.
Inheritance tax: (see section 11)	Properties form part of an individual's estate. Business Property Relief (BPR) does not apply.	Company itself not liable. Shares form part of the individual shareholders' estate - due on value of shareholding. BPR may be claimable.

Note: Furnished Holiday Lettings

One of the main benefits of a property being a Furnished Holiday Let (FHL) is that such properties are treated as if they are a trade for income tax purposes and therefore the restriction of loan interest on residential property does not apply (see section 3). In order to qualify as a FHL the property must be furnished, commercially let and pass the three ‘occupancy’ conditions – these conditions determine how many days the property must be available to let and how many days it is let.

There is no special provision applicable to IHT and owners of FHL have, in the past, not been able to persuade HMRC that Business Property Relief (BPR) applies on either property owned by an individual or on a share of a company that owns such a property (for further detail see section 10.1).

Tax Rates

In the tax calculation for a landlord who owns investment property personally (or jointly or in a partnership) their share of the rental profit is added to any other income received during the tax year and the balance over the personal allowance (£12,500 for 2020/21) is taxed at these rates:

Band	Taxable income	Tax rate
Basic rate	£12,501 to £50,000	20%
Higher rate	£50,001 to £150,000	40%
Additional rate	over £150,000	45%

Being investment income no National insurance contributions are payable on rental profits for either an individual or corporate landlord although it is potentially chargeable on a landlord who owns a FHL depending upon the amount of profit. In comparison, corporation tax is charged on profit made at a straight 19%.

2.1 The Property Allowance

This allowance applies to all types of lettings owned by an individual (or jointly) or by a partnership whether the property is in the UK or overseas including commercial property but excluding FHL. It is, in effect, two reliefs - being both an exemption from tax and a minimum deduction in calculating letting profit. It is not available to companies.

Under the allowance, where an individual’s total gross income from the property business is less than £1,000 in any one tax year then no income tax is payable neither is there a need to file a tax return. However, landlords who qualify for the allowance need to monitor the figure every year as should this amount exceed the limit then a self-assessment tax return will be required.

In addition, where the income of the property business exceeds £1,000 the landlord may elect to deduct a minimum of £1,000 from the income rather than deduct the expenditure incurred. As such, businesses with low outgoings (e.g. a single property with no mortgage and low repairs) would be advised to claim the property allowance instead of using the ‘income less expenses’ calculation. However, if a business pays a large expense during a year (e.g. a ‘one off’ repair bill) then it might be better to claim expenses using the normal rules; this would also be relevant should the business make a loss.