2025/26

PROPERTY COMPANY V PROPERTY TRUST

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Contents

‘**Property Company v Property Trust**’ first published October 2022, second edition October 2023, third edition October 2024, fourth edition October 2025.

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1 About this guide

This guide looks at two of the options for holding property – in a limited company or in a trust. In each case, consideration is given to the associated tax implications that may arise. Property may also be held by an individual (or a number of individuals) running an unincorporated property business or by a partnership or limited liability partnership. These are mentioned briefly but are not the focus of this guide.

When looking at property, there are a number of different taxes to consider and a number of scenarios which may give rise to a tax liability.

- On initial purchase of the property, a liability to stamp duty land tax (SDLT) (or land and buildings transaction tax (LBTT) in Scotland or land transaction tax (LTT) in Wales) may arise.
- Where a property which is already owned in a personal capacity is transferred into a limited company or a trust, there is a disposal for capital gains tax purposes which may trigger a capital gains tax charge.
- If the property is transferred into a discretionary trust, there may be a lifetime charge to inheritance tax.
- In the event that the property in question is let out, there will be rental income to consider, on which tax will be payable.
- If the property is eventually sold, a tax liability will arise if a gain is made on disposal. If the property is held by a company, the charge will be to corporation tax and if the property is held in trust, the charge will be to capital gains tax.
- Where a high-value residential property is held in a company, the annual tax on enveloped dwellings will also need to be considered. However, there are exemptions from the charge, including where the property is let out and certain conditions are met.

The liability and nature of the taxes and the rates that apply will depend on how the property is held. This report looks at the various 'tax events' that may arise where a property is held in a limited company and where a property is held in trust.

2 Holding an investment property

Property has historically been viewed as a good investment, and one which generally appreciates in value over time. Where the property is let out, whether as a residential or commercial let or as a holiday let, it will also generate a source of income. However, recent changes to the tax rules mean the climate is not as favourable as it once was.

There are various ways in which an investment property can be held. The way that a property is held will dictate what taxes are payable.

2.1 Unincorporated property business

The simplest way to hold an investment property is to hold it in a personal capacity. Under the property tax rules, all properties held in the same capacity by the same person or persons form part of the same rental business. Following the end of the special tax regime for furnished holiday lettings, since 6 April 2025, properties which are let out as furnished holiday accommodation are treated in the same way as other residential lets and the rental income and expenses from the holiday lets are taken into account with those for longer-term residential lets and commercial lets when calculating the profit or loss for the property rental business. A distinction is made between UK properties and overseas properties, and where a person owns both UK and overseas properties, they will have both a UK property business and an overseas property business.

On the initial purchase of the property, a liability to SDLT (or, as appropriate, LBTT or LTT) will arise if the consideration exceeds the relevant threshold. Where the landlord already owns one residential property, the purchase of second and subsequent residential properties will attract the SDLT, LBTT or LTT supplement.

The cash basis is the default basis of accounts preparation for unincorporated landlords with rental income of £150,000 or less. Where the rental income exceeds this, or if one of the other cash basis conditions is not met, the accounts must be prepared using the accruals basis. A landlord who is eligible for the cash basis can also elect to prepare accounts on the accruals basis if this is preferred or advantageous.

The profit or loss is computed separately for each property rental business. The calculation is at business level rather than for each individual property. In this way, a loss on one property is automatically relieved against a profit made on another property within the same property business. As noted above, the separate rules for furnished holiday lettings were abolished from 6 April 2025. Since that date, the profits and losses of holiday lets and other lets will be amalgamated within a single property business and profits calculated for the business as a whole.

The profits of an unincorporated property business are charged to income tax at the landlord's marginal rate.

If a gain is made on the disposal of the property, a liability to capital gains tax may arise. This will be the case if the landlord's net gains for the year, less any allowable losses set against the gain, exceed the annual exempt amount. Residential gains must be reported to HMRC within 60 days and a payment on account of the capital gains tax must be made within the same timescale.

Changes to the tax rules in recent years have reduced the attractiveness of holding investment property in a personal capacity. In particular, changes to the mechanism for relieving interest on finance costs, which moved from relief by deduction (allowing relief at the landlord's marginal rate) to relief at 20% of the interest and finance costs as a tax reduction, have prompted many landlords to consider other property holding structures.

Changes to lettings relief and the need to pay and report residential gains within 60 days have also decreased the attractiveness of holding property as an individual.

The abolition of the favourable tax regime for furnished holiday lets from 6 April 2025 decreased the attractiveness of holiday lets. As a result, unincorporated landlords may consider whether to run a holiday lets business other than in a personal capacity or, alternatively, leave the market.

2.2 Property partnerships

Property may also be held in a partnership. This can be advantageous where property is jointly owned as it provides greater flexibility for allocating profits and losses than where jointly owned property is held outside a partnership, particularly if the joint owners are spouses or civil partners.

A traditional partnership is transparent for tax purposes, and the individual partners are liable for income tax on their share of the profits. Where an individual partner also owns property outside the partnership in an individual capacity, they will have two separate property businesses – one for their share of the partnership profits and one for the rental properties owned in an individual capacity. If a gain arises when the property is sold, each partner is liable for capital gains tax (subject to the gain being sheltered by the annual exempt amount and any allowable losses) on their share of the gain.

Property can also be held in a limited liability partnership (LLP); in certain circumstances, this can generate tax advantages. An LLP is something of a hybrid between a company and a traditional partnership. Like a limited company, it offers the advantage of limited liability and, like a traditional partnership, it provides the flexibility to agree on how to share profits between the partners. As with a traditional partnership, an LLP is transparent for tax purposes, with each partner being taxed personally on their share of the profits and liable to capital gains tax on their share of any gain on disposal. However, unlike a traditional partnership, an LLP can hold property in its own right and properties transferred to the LLP are held on trust by it.

2.3 Property company

In recent years, holding a property in a limited company has become popular. This is due in part to the restriction for interest and finance costs that applies in relation to residential property held by an unincorporated property business (including furnished holiday lettings from 6 April 2025 onwards). The restriction does not apply where residential property is held in a limited company, and any associated interest and finance costs can be deducted in full when computing the taxable profit.

Under the favourable tax regime for furnished holiday lettings which came to an end on 5 April 2025, landlords with furnished holiday lets could deduct interest and finance costs in full in calculating their taxable profits. From 6 April 2025 onwards following the end of that regime, unincorporated landlords letting holiday lets receive relief for interest and finance costs as a basic-rate tax reduction. However, where holiday lets are held in a company, interest and finance costs can be deducted in full. This may lead to an increase in the incorporation of furnished holiday lettings businesses.

Since 1 April 2023, the rate at which a company pays corporation tax on its profits depends on the level of those profits. Where a company has profits below the lower profits limit (set at £50,000 for a company with no associates), the small profits rate applies. This is set at 19% for the financial year 2025 which runs from 1 April 2025 to 31 March 2026. At the other end of the scale, where a company has profits in excess of the upper limit (set at £250,000 for a company with no associates), corporation tax is charged at the main rate of 25%. If the profits of the company fall between the two limits, the effective rate will be between 19% and 25%; corporation tax is calculated at the main rate of 25%, as reduced by marginal relief.

The tax payable by a property company on the profits of the property business may be less than that payable by an unincorporated property business. The small profits rate of 19% is less than the basic rate of income tax, and the highest corporation tax rate at 25% is significantly lower than the higher and additional rates of income tax. However, unlike an individual, a company does not have the equivalent of a personal allowance, so tax is payable from the first £1 of profit. For 2025/26, the personal allowance is £12,570. However, it is gradually reduced once adjusted net income reaches £100,000, being lost entirely once adjusted net income reaches £125,140.

Companies also pay corporation tax on chargeable gains at the same rate at which they pay corporation tax. By contrast, the rate at which individuals pay capital gains tax on residential property depends on whether their income and gains exceed the basic-rate band (set at £37,700 for 2025/26). Where income and gains are within the basic-rate band, gains are taxed at 18%. This is less than the small profits rate of corporation tax, which is set at 19% for the financial year 2025. Where income and gains exceed the basic-rate band, gains are taxed at 24%. Whether this is higher or lower than the rate at which corporation tax would be payable on those gains will depend on the company's profits and the rate at which it pays corporation tax. Unlike an individual, a company does not have an annual exempt amount, which for 2025/26 is set at £3,000. The reduction in the annual exempt amount in recent years has reduced the advantage that this gives to unincorporated landlords in reducing or eliminating any capital gains tax liability on a property gain.

Residential property gains realised by individuals must be reported to HMRC and the associated tax paid within 60 days of completion. By contrast, any corporation tax on capital gains, including that on a residential property gain, is payable by the normal corporation tax due date of nine months and one day from the end of the accounting period in which the gain arose. This provides a much longer payment window and associated cash flow advantages. A company does not need to report the gain on a residential property within 60 days of completion.

For 2025/26, capital gains tax is charged at 18% where income and gains fall within the basic-rate band and at 24% otherwise. The same rates apply to residential property gains. Corporation tax on chargeable gains is payable at the company's effective rate, which will be between 19% and 25%.

It is important to note that the story does not end there. If the profits are to be used outside the company, they will need to be extracted, and this may give rise to additional tax and, potentially, National Insurance liabilities. When assessing whether it is beneficial to operate through a property company, this must be borne in mind.

The tax implications of holding an investment property in a limited company are discussed in detail in section 3.

2.4 Property trust

Putting a property into trust can be beneficial, particularly from an inheritance tax perspective as the property may fall outside the settlor's estate.

The tax consequences of putting a property in trust will depend on the type of trust that is used. There may also be tax implications when the property is put into the trust and when it is transferred to the beneficiaries.

Where the property is let, tax will be payable on any rental income received by the trust. When this is distributed to the beneficiaries, the beneficiaries will be taxed on the income that they receive but will receive credit for that already paid by the trust. This may give rise to a repayment.

A tax charge may also arise on the settlor when the property is settled as the settlor will be deemed to have disposed of the property at market value. This may trigger a chargeable gain. However, in certain circumstances, it may be possible to hold over the gain, delaying the point at which the tax must be paid.

Property trusts are considered in detail in section 4. While the main focus of this report is the use of a trust to hold an investment property, such as a buy-to-let or holiday let, a trust can also be used to hold a main residence or family home.

3 Property companies

3.1 Popularity of property companies

Tax changes adversely affecting unincorporated landlords in recent years led many to consider whether they could cut their tax bill by operating through a limited company.