Guide To Buying Property Through A Limited Company

ESPER WEALTH
PROPERTY INVESTMENTS

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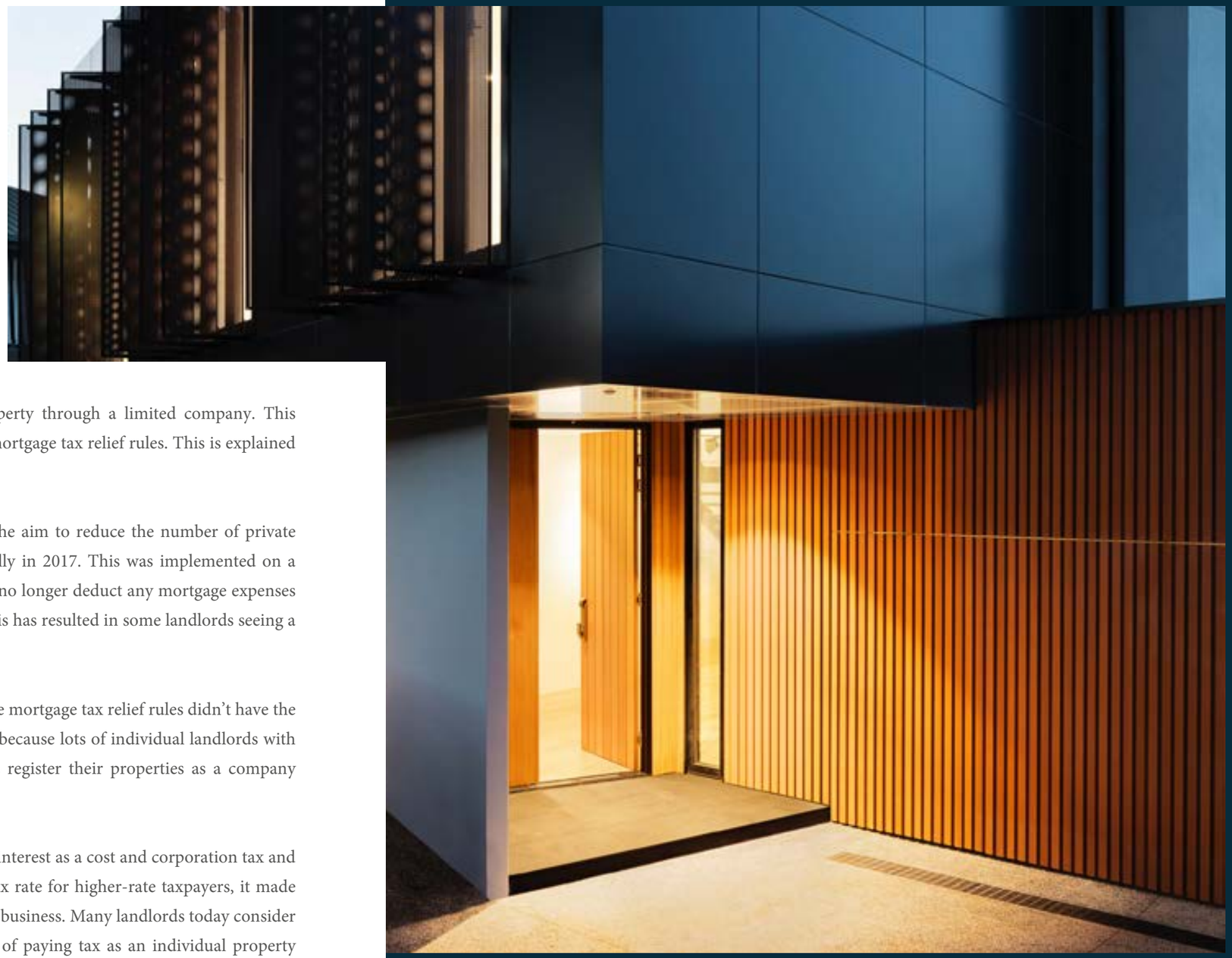
Introduction



There has been an upsurge of people buying property through a limited company. This increase in demand is a result of recent changes to mortgage tax relief rules. This is explained in greater later in the brochure.

These rule changes were introduced in 2015 with the aim to reduce the number of private landlords in the UK. They were introduced gradually in 2017. This was implemented on a sliding scale. By April 2020, private landlords could no longer deduct any mortgage expenses from their rental income to reduce their tax bills. This has resulted in some landlords seeing a considerable reduction in their after-tax profits.

Whilst some landlords moved out of the industry, the mortgage tax relief rules didn't have the intended effect Mr Osborne was aiming for. This is because lots of individual landlords with only a handful of buy-to-let properties changed to register their properties as a company instead of an individual.

And, because limited companies can treat mortgage interest as a cost and corporation tax and dividend tax rates are much less than the income tax rate for higher-rate taxpayers, it made sense for a lot of private landlords to restructure as a business. Many landlords today consider setting up a limited company at the outset instead of paying tax as an individual property investor.

However, nothing in life is clear-cut. There are both advantages and disadvantages to becoming a limited company when investing in buy-to let-property. This brochure explains to you the pros and cons of both structures.

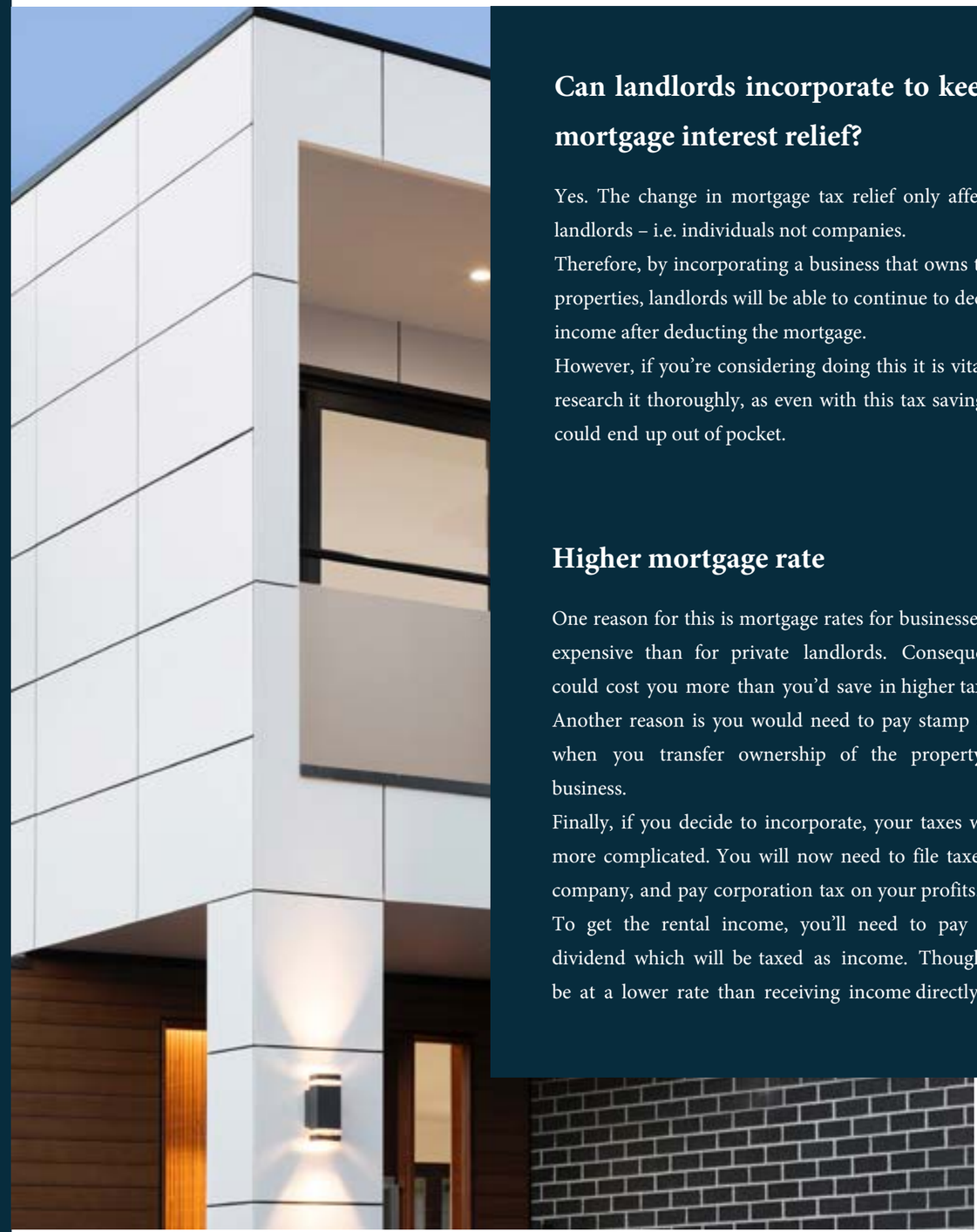
Mortgage Interest Tax Relief

The way landlords must declare their rental income has changed. This means higher tax bills for many.
Whilst borrowing money through a buy-to-let mortgage was once a major tax advantage, this is no longer the case.
Since April 2020, it is no longer possible to deduct any of your mortgage expenses from your rental income to reduce your tax bill.
Instead, you now receive a tax credit, based on 20% of your mortgage interest payments.
For higher-rate taxpayers, this is less generous than the previous system, which effectively enjoyed a 40% tax relief on mortgage payments
This new system means higher-rate taxpayers can no longer claim the tax back on their mortgage repayments, as the credit only refunds tax at the basic 20% rate, rather than the higher rate of tax paid.
Additionally, these new rules could force some landlords into a higher tax bracket, because they'll need to declare the income that was used to pay the mortgage on their tax return.

An example of a buy-to-let mortgage interest tax relief

The below example assumes that a landlord takes in £1,000 per month of rental income and makes mortgage interest payments of £650 per month.

- They'll pay tax on the full £12,000 rental income they earn
- They'll pay £7,800 in mortgage interest
- They'll get a tax credit of £1,560 (£7,800 x 20%)
- A basic-rate taxpayer will pay £840 – no increase compared to the old rules
- A higher-rate taxpayer will pay £3,240 – double the amount payable under the old system.



Can landlords incorporate to keep their mortgage interest relief?

Yes. The change in mortgage tax relief only affects private landlords – i.e. individuals not companies.
Therefore, by incorporating a business that owns their rental properties, landlords will be able to continue to declare rental income after deducting the mortgage.
However, if you're considering doing this it is vital to research it thoroughly, as even with this tax saving you could end up out of pocket.

Higher mortgage rate

One reason for this is mortgage rates for businesses are more expensive than for private landlords. Consequently, this could cost you more than you'd save in higher tax relief.
Another reason is you would need to pay stamp duty again when you transfer ownership of the property to your business.
Finally, if you decide to incorporate, your taxes will become more complicated. You will now need to file taxes for your company, and pay corporation tax on your profits.
To get the rental income, you'll need to pay yourself a dividend which will be taxed as income. Though this will be at a lower rate than receiving income directly.

Inheritance tax benefits

Landlords planning to pass their property portfolio down to children or family members could avoid large amounts of inheritance tax by buying the property through a limited company. That's because they can apply Business Property Relief to their income and assets.

Since 2013 property investors have been allowed to hold shares which qualify for Business Property Relief in a tax-efficient ISA account. Public companies can't access this BPR because their shares are listed on the stock exchange. At the same time, sole traders (ie self-employed property investors) are forbidden from accessing it if they plan on transferring fixed assets, such as land, premises and machinery. In other words, this is a form of tax relief specifically aimed at limited companies.

Advantages Of Buying Through A Limited Company

Tax treatment of mortgage interest

As discussed earlier, private landlords can no longer deduct any of their mortgage expenses from rental income to reduce their tax bill. Instead, they receive a tax credit, based on 20 per cent of their mortgage interest payments. If you are a higher rate taxpayer you won't get all the tax back on your mortgage payments as the credit only refunds tax at the basic rate and not the top rate you paid.

Additionally, you may also find yourself pushed into the next tax bracket because you will need to declare the income that was used to pay the mortgage on your tax return. This has been a common problem for many property investors and this is why it made more sense to become a limited company, instead of paying tax in a higher band.

Limited company status becomes much more attractive because, unlike property owned by an individual investor, mortgage interest is treated as a business expense for limited companies. This means it's possible to deduct the cost of mortgage interest before paying your corporation tax.

Tax treatment of profits

For private landlords, profits from rental income are taxed via income tax alongside their other earnings. That means adding the money made from rental income to the amount you receive from a salary, as well as any other money received from shares or dividends. Income above your personal allowance is taxed at the rates listed in the table below. Currently, the standard personal tax-free allowance is £12,571 (although this reduces if your income is over £100,000).

Tax Band	Income	Tax Rate
Basic Rate	£12,571 to £50,270	20%
Higher Rate	£50,271 to £150,000	40%
Additional Rate	over £150,000	45%

If you invest in property via a company with limited status, you will be liable for corporation tax on your profits. The rate of corporation tax is currently 19 per cent but is set to rise to 25 per cent by 2023. If you are a higher-rate taxpayer you stand to make a huge tax saving. You will still be taxed if you want to access your rental income, either via income tax on the salary you pay yourself or tax on dividend payments. However, there are ways a tax accountant can minimise the tax you pay.

Disadvantages Of Buying Through A Limited Company

Mortgage availability

The number of buy-to-let mortgage products on offer for limited companies is far lower than for individuals. Lenders also don't lend on the same LTVs as they consider lending to a business as a higher risk. As a result, you may find it much more difficult to arrange a mortgage. And if you can, the interest rates will probably be higher.

Tax when you take money out

To access your rental income, you can pay yourself a salary. This will be liable to income tax but will count as a cost when calculating your pre-tax profit for corporation tax purposes.
Rental profits taken as dividends are not considered a business expense. For the tax year 2022-2023, the tax-free allowance on dividends is £2,000. How much tax you pay on dividends above this amount depends on your tax band. The following dividend rates apply.

Tax Band	Tax rate on dividends above the allowance
Basic Rate	7.5%
Higher Rate	32.5%
Additional Rate	38.1%

If you plan to leave the rental profits in the company, this is not a problem. However, if you need to live off your rental income (which many small-scale landlords do), then you will need to do the maths to work out whether a limited company reduces your tax bill. Speak to a tax accountant as there are ways you can maximise your tax efficiency, such as splitting dividends with a spouse who is a basic rate taxpayer.

Transferring any properties you own in your own name is costly

In order to switch your properties over to a limited company, you have to go through a prescribed legal process. This involves paying taxes and conveyancer fees. Effectively, you have to 'sell' your properties to yourself. Naturally, there are costs involved in this. This includes:

- **Stamp Duty Land Tax** – This is a standard charge based on your property's worth. But in addition, because the investment property isn't your main residence, you will also be due to pay a further three per cent tax. That's because it comes under the 'second home' category.
- **Capital Gains Tax** – Any profit you make on your property investment will accrue tax. The amount of CGT you will pay is dependent on how much income tax you pay on an annual basis. That means if you're a basic rate taxpayer you'll pay 18 per cent CGT, whereas the higher tax rate is calculated at 28 per cent.
- **Conveyancing and solicitor fees** – Just as if you were selling to another individual, the standard procedure will apply ie a solicitor or conveyancer will be required to ensure the switch is legal.
- **Early redemption charges and increased mortgage costs –** Some lenders will charge a re-payment fee if you have only just started paying your mortgage off. This is typically between one per cent and five per cent.

For some landlords, these costs make moving to a limited company very prohibitive. For others, the long-term tax savings far outweigh these costs.

Extra cost and hassle

Limited companies have to file annual accounts, so you will need to pay an accountant. Running a limited company also requires more administration and paperwork.

Fequently Asked Questions

Many property investors wonder whether it is better to buy property in their own name, or to buy it via a limited company. Here are some commonly asked questions.

1. Is setting up a limited company difficult? And what does it involve?

Firstly, you will need to pick a company name and then register your company at Companies House.
To do this, you will need to:

- appoint at least one director
- choose who the shareholders are and issue shares
- prepare a Memorandum and Articles of Association to determine how you will run your company

Currently, it costs £12 to register a new company. This is easy to do and can be done online. The process is swift and you will usually established within 24 hours of submitting your application. You will receive a certificate of incorporation. This confirms the company legally exists and shows the company number and date of incorporation.

2. I'm buying my first investment property, should I do this through a limited company?

This is a great question, and it really depends on your future plans as a property investor. If you are only looking to rent out one or two properties, then setting up a limited company is probably not the best option. However, if you have more ambitious plans, then it can be cheaper and easier to create a limited company from the outset. Many larger investors use a limited company when purchasing property.

3. If you own property in your own name, is it worth transferring it to a company?

This will depend on how many properties you have. If, for example, you only have a couple of investment properties then it probably won't be worth switching. If however your portfolio is a large one then it's definitely worth looking into. Find a good tax accountant, especially one who specialises in property, and they should be able to advise you on what to do next.

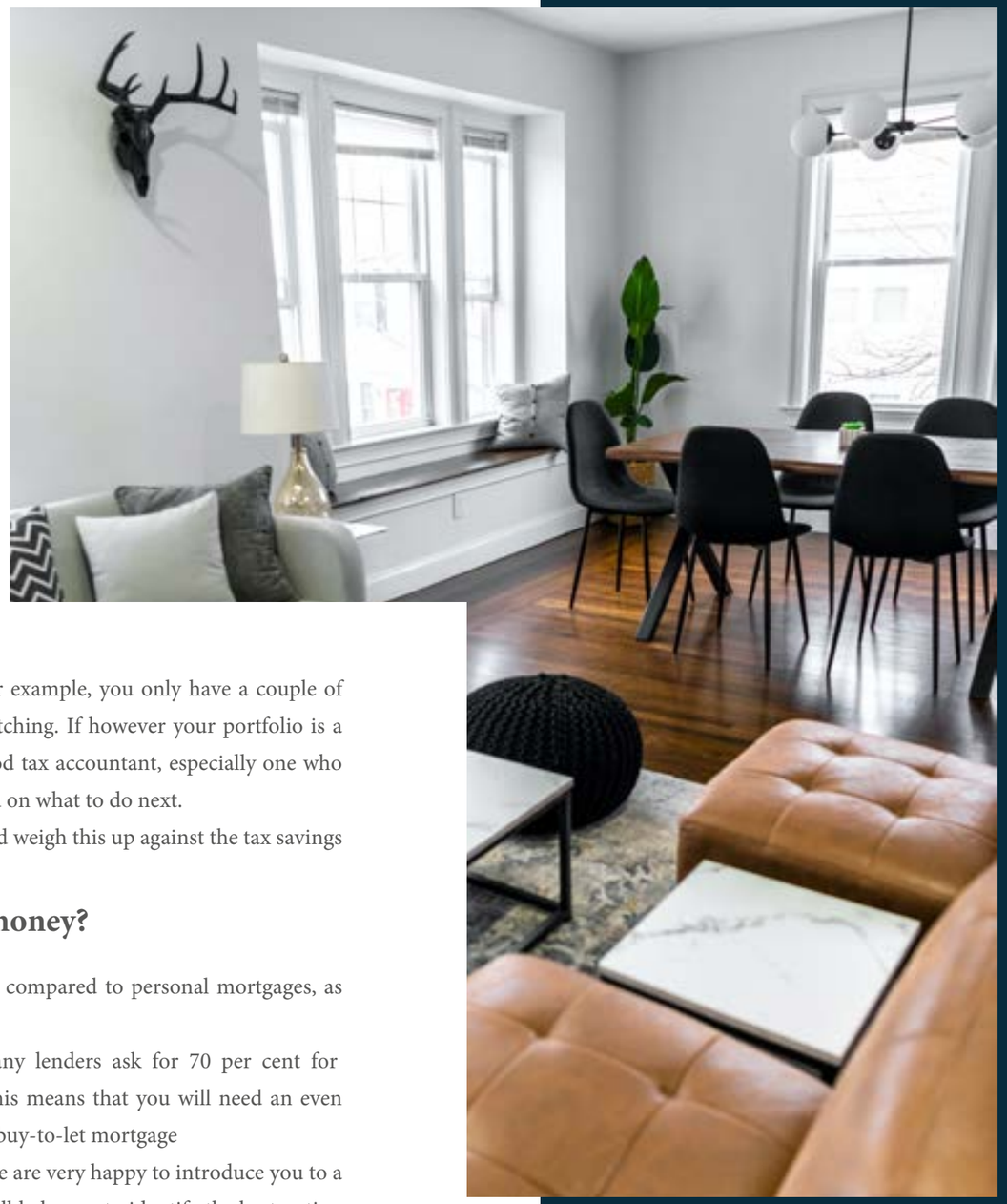
You will need to calculate all the costs, as outlined above, and weigh this up against the tax savings you could make.

4. Will my company be able to borrow money?

Yes, but you may find the interest rates are slightly higher compared to personal mortgages, as lenders perceive the risk to be higher.

Expect the loan-to-value percentage to be lower too. Many lenders ask for 70 per cent for repayment mortgages and 65 per cent for interest only. This means that you will need an even bigger deposit than you have paid in the past for a standard buy-to-let mortgage

At Esper Wealth work's very closely with tax consultants. We are very happy to introduce you to a tax specialist and an independent mortgage broker. They will help you to identify the best option for you. You can find out more on our Funding Solutions page.



The Esper Approach

At Esper Wealth we work for you. Our role is to listen to you and guide you to achieve your goals. As a client we want you to feel comfortable in the investment process, in the belief that we are delivering the best advice. With this in mind, it is important to follow three simple rules when investing:

1. **Never feel pressured.** Many property sales companies work on urgency. This is the wrong approach. You should take the time to decide what is right for you and your family. If this means you miss a particular property then be rest assured another opportunity will arise.
2. **Be transactional.** This means trying not to be emotive about a property. Remember you are not living in it. Ask yourself, do the numbers work financially for me?
3. **Ask yourself, what if?** In life, we never know what's around the corner. Sometimes your circumstances can change. If things do change, how will it impact me? Whilst you can never legislate for all contingencies, it is advisable to invest with your eyes open.

If you are interested in off-plan opportunities, or completed property direct from the developer, then visit our developments page. Alternatively, if you would prefer to start your investment journey by having a no obligations, free investment review, Then contact a member of our team who will be happy to help.