Buy To Let Tax Basics

With Iain Wallis

Revenue v Capital

Revenue expenses are those that relate to the ongoing cost of running your property business. They can be claimed against income tax at the end of the tax year in which you incur them.

Examples:

- Mortgage interest
- Agents' fees
- Repairs

Capital expenses relate to the costs of acquiring a property and making improvements to it. They are carried forward, and can only be claimed against capital gains tax when you sell.

Examples:

- The cost of the property itself
- Purchase-related legal fees
- Stamp duty
- Estate agents' fees when you sell

As a rule you want to have expenses classified as being **revenue** where possible, because:

- It's better for your cashflow
- It avoids the relative value of the expense being eroded through inflation
- You might never sell!

Acquiring a property

Start keeping track of your expenses now: costs you incur for up to seven years before your property business starts are allowable!

Mileage

All your property-related mileage (visiting properties, visiting your accountant, attending educational events etc.) can be claimed. The rate is 45p per mile for the first 10,000 miles, then 25p thereafter.

If you travel 10,000 miles in a year, that's £4,500 to offset against tax!

To avoid recording every single journey, track your property-related mileage for one month then multiply by twelve.

Sustenance

Food and drink when you're away from home on property-related business is allowable, as long as it's "reasonable".

Travel

Travel costs (public transport and accommodation) can be claimed, but you must be able to prove that the primary purpose of your trip was for your property business. It's OK to spend a couple of hours on the beach at the end of a long week of viewings and meetings, but you can't write off an entire family trip to Spain because you looked at an agent's window once!

Legal fees relating to finance

As a rule, your legal fees to acquire a property are of a **capital** nature.

But if you're taking out financing of some kind, part of your solicitor's work will relate to organizing it – and those costs can be claimed as **revenue**.

Ask your solicitor for a separate bill for that part of the work, and claim it in the current tax year.

Finance arrangement fees

Arrangement fees can be written off year-by-year.

For example, if you choose a product with a £1,000 fee and a 10-year term, claim £100 each year as a revenue expense.

If you refinance, write off the remainder of the fee in the current year. For example, if you refinance in year 3, you will already have claimed £200 so you can claim the remaining £700.

Abortive purchases

Unfortunately, any costs relating to properties that you don't end up buying (such as surveys) are a private cost and can't be claimed.

The holding phase

Allowable revenue expenses

As well as the obvious costs like mortgage interest and repairs, you can claim everything relating to running your property business – even down to postage stamps!

It all adds up, so it’s worth keeping track of.

Allowance for working from home

If you run your business from home, you can claim a share of all your household costs: mortgage interest, council tax, bills etc.

To calculate the share you can claim:

- Calculate the total number of rooms in your house, excluding kitchens and bathrooms. If you work from one room and your house has five bedrooms and three reception rooms, you can claim 1/8 of your costs

- Then claim 80-85% of that fraction, because the room probably isn’t being used wholly for your property business. For example, there might be a spare bed that guests use when they stay over.

Education costs

Acquiring a new skill is a private cost, but developing an existing skill is allowable.

So if you already have properties, or you have already undertaken property investment training, the cost of this course is allowable!

Iain says that a spend of around £200 on books and events should be enough to demonstrate that you have acquired the skill, and anything further is just developing it.

Repairs

If you are restoring something to its previous condition (e.g. a fresh coat of paint), it can be classed as **revenue.**

If you are making a clear improvement (e.g. converting the loft), it will be **capital.**

Be careful: any element of improvement (e.g. replacing the roof and converting the loft at the same time) will render the whole expense as capital.

If you are requiring a dilapidated asset for the first time, it can be tricky to prove what is an improvement and what is a repair. Iain recommends creating a one-week tenancy with a family member or your builder as soon as you acquire the property, which demonstrates that the property was habitable. Any future work can then be classed as repairs, and therefore treated as revenue.

To count as revenue, replacements should be like-for-like. There are exceptions for when this isn't possible: for example, replacing single glazing with double glazing wouldn't be treated as an improvement because you can't install single glazing these days.

VAT

You can't register for VAT and claim back the VAT that you pay out, but you can offset the VAT portion of your expenses.

e.g. If you're charged a total of £12, which is £10 + VAT, you can claim the whole £12.

Losses

If you make a loss in one tax year, it is carried forward to offset against the next year in which you make profits. Losses are carried forward in perpetuity until they are used up.

Losses are non-transferrable between partners and spouses. So if you split profits and losses 50/50 and your spouse dies, their share of the losses dies with them and can't be transferred to you to offset against future profits.

Refinancing

You can offset all your interest costs with no cap, **as long as the funds are used within your property business** – either as deposits for more property, for repairs, for education or anything else.

If the funds will be used outside the property business (e.g. for you to live on, or to invest in another business), the proportion of the interest you can offset is capped at the value of the property at the point when it entered the letting market.

Example:

- You buy a property with cash for £100,000
- After 10 years it is worth £200,000
- You refinance with a 75% BTL mortgage to pull out £150,000
- If your intention is to use the cash outside your property business, you can only get tax relief on 100 / 150ths of the amount of interest you pay – because the property was worth £100,000 at the point when it entered the lettings market
- But if you use £25,000 of the money inside your property business (e.g. as a deposit on a new property), you can now claim tax relief on 125 / 150ths.

Early redemption fees

Early redemption fees are a revenue expense, so can be claimed in full at the end of the tax year in which they were incurred.

Record keeping and summary

- Keep a spreadsheet for each transaction, allocating each as best you can to the relevant category (repairs, professional fees, other allowable expenses etc).
- At the end of the year, you can use that spreadsheet to generate your P&L – or pass it to your accountant. Don’t forget to add an allowance for using your home as an office, and your total mileage.
- Don’t pay an accountant to do your bookkeeping! If you can’t keep track of everything yourself, find a bookkeeper – it will work out cheaper.
- You need to keep your receipts for 6 years.
- A good accountant should save you more than they cost you…
- …but even if you use an accountant, you now know what you can claim so you can check that they’re not leaving any money on the revenue table on your behalf