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100 YEARS



Letting out property: the tax angle

The way that income from property is taxed and reported is changing.

This adds new layers of complexity for residential landlords, who already have to deal with a far from straightforward regime.

What is income from property?

Understanding this correctly is key for tax compliance. Property income covers almost any income from land or buildings: rent from a flat or house; parking space on your drive; even from a permanently moored houseboat. It doesn't matter whether there are one, or multiple lettings; furnished or unfurnished; tenant-repairing or landlord-repairing. It doesn't matter if the tenant pays 'rent' by painting, decorating, or cutting the grass. As far as HMRC is concerned, it is property income, and profits are taxable - except where reliefs and allowances apply.

Not included: Income from a hotel or guesthouse is charged as trading income, not income from property.

Tip: Accidental landlord? Check your position

Misunderstanding what is classed as income from property can cause problems - especially for anyone accidentally becoming a landlord. This can happen if you inherit a property and let it out; move in with a partner and let out a previous residence; or go abroad to work while letting out the home, for example.

HMRC compliance

HMRC has a special disclosure process for income from letting residential property in the UK or abroad. The Let Property Campaign can be used where such income has not been declared to HMRC, either inadvertently or deliberately. Using the facility means the position should be treated more leniently than if HMRC uncovered it. We can help you navigate the procedure involved, should this apply to you.

How is it charged to tax?

Though HMRC refers to property income as arising from a property 'business', property income is not treated as trading income, but as unearned income.

You are treated as having a single UK property business for tax purposes – even if you have multiple properties. Receipts and expenses are combined, so expenses on one property can be deducted from receipts on another. Current year losses on individual properties are set off automatically. Any losses in the UK property business overall are carried forward, and can be used to reduce taxable UK property income in later years. Any overseas property is treated separately, forming an overseas property business. Profits or losses here are treated separately from any UK property business.

Special cases

The Rent a Room rules can be used to cover income from letting out a furnished room to a lodger in your own home, or to cover bed and breakfast income from the house you live in. No Income Tax is payable if gross rents in the tax year are no more than £7,500. If income exceeds this, you can choose to deduct actual expenses, or £7,500 (£3,750 for joint lettings).

Low levels of property income: If gross property income is £1,000 or less, using the Property Allowance means there is no need to declare the income to HMRC, or pay tax. For income above this level, the choice is to deduct actual expenses incurred, or the Property Allowance.

Structuring a buy to let property business

Property can be held by an individual; jointly; as a partnership; or through a company. For tax purposes, the real divide is the use of a company.

Tip: Take an all-round view

There is no one right way to structure a property business. The best plan is the one that takes into account your individual aims, circumstances, and your requirements for income and capital, long term and short term.

Tax for individual landlords

For 2026/27, income from property is taxed at the same rate as other non-savings income. For taxpayers in England, Northern Ireland and (currently) Wales income within: the basic rate band is charged at 20%; higher rate band at 40%; and additional rate band at 45%.

For Scottish taxpayers, the position is different. Income within the starter rate band is charged at 19%; basic rate band at 20%; intermediate rate band at 21%; higher rate band at 42%; advanced rate band at 45%; and top rate band at 48%.

From 2027/28, there will be separate tax rates for property income. These will be higher than rates for income, say, from employment. For English and Northern Irish taxpayers, the new property rate will be 22% for basic rate taxpayers; 42% for higher rate taxpayers; and 47% for additional rate taxpayers. In Scotland and Wales, the devolved governments will have authority to make a similar change.

Interaction with other tax changes: From 2027/28, there will also be change to the Income Tax ordering rules, so that the Personal Allowance (currently £12,570) will be applied first to income from employment, self-employment and pensions. Only then will it be available to set off against property income; savings income and income from dividends. At present, there is flexibility in the order of set-off.

Tip: Review income mix and strategies now

When combined with the new, higher tax rates for property income, and increased savings and dividend tax rates, the overall effect will be significant. Landlord tax bills stand to rise as income outside the shelter of the Personal Allowance is pushed into higher tax rates. We would therefore recommend reviewing possible mitigation strategies now.

Joint property ownership

Joint letting can be structured as a partnership, which can be useful where a couple plans to use both Personal Allowances, or access a lower rate of tax for one party.

But letting property jointly does not automatically constitute a partnership, and more often, each owner is treated as carrying on their own personal property business. Shares of property income are usually split according to the share of the property held by each, though this can be varied by agreement.

Where the joint owners are spouses/civil partners, the position is different. Income is deemed to be shared equally, unless an election is made to split income to reflect actual shares of ownership. The election is made by submitting Form 17 to HMRC, and is something we can help with.

Tip: Optimising household income

Used correctly, elections like this can help smooth out household income, allowing full use of lower rate tax bands.

Running the business through a company

Operating via a company presents a different tax profile. Note that if you incorporate an existing property portfolio, there can be significant up-front costs. Transferring ownership of personally held properties into a company can involve a charge to CGT, as well as Stamp Duty Land Tax, or equivalent in Scotland and Wales.

Tip: Check the numbers

Reviewing the costs involved will help you decide whether incorporation is the best option in your circumstances.

Pros and cons

With the small profits rate of Corporation Tax at 19% for taxable profits up to £50,000, and the main rate 25% for profits over £250,000, headline rates of Corporation Tax are lower than Income Tax rates. The difference is even greater for Scottish taxpayers.

For company directors, profit extraction via dividends can give flexibility. Add the fact that relief on residential property loan interest is restricted for individual landlords, but usually allowable for companies, and a corporate structure may look very attractive.

But the grass isn't always greener, and times are changing for small companies. Extraction via dividends is becoming more expensive. The dividend tax rate is currently 10.75% for basic rate taxpayers; 35.75% for higher rate taxpayers, and 39.35% for additional rate taxpayers. At £500, the Dividend Allowance is the lowest it has been since its introduction. In addition, HMRC is stepping up compliance and reporting obligations for close companies and their directors, especially round directors' drawings.

The annual tax on enveloped dwellings (ATED) regime can apply where companies own residential property worth more than £500,000, and may entail the need for reporting even if no tax is due.

On eventual sale of property by an individual, CGT is payable at 18% (where within basic rate) or 24% (for higher rates). Individuals can reduce this by any annual exemption available. By contrast, a gain made by a company is charged to Corporation Tax, and taxable at rates between 19% and 25%, with further tax on extraction of profits.

In short, there are both pros and cons to running a property business through a company, and we can help you assess your property portfolio with an eye to maximum tax efficiency.

Tip: Current HMRC compliance

HMRC is warning against use of a scheme being marketed to landlords, involving complex restructuring, and use of limited liability partnerships with a corporate member. HMRC considers this does not work and is tax avoidance, and extreme caution is advised with any such arrangement.

Deductions available for tax

This is an area where mistakes can easily be made, and one that HMRC monitors closely.

Allowable expenses include letting agent fees; legal fees for lets of a year or less, or to renew a lease for less than 50 years; accountancy fees; buildings and contents insurance; maintenance and repairs to the property (not improvements); utility bills; rent, ground rent and service charges; Council Tax; services such as cleaning; and other direct costs of the letting, such as advertising.

Costs must be wholly and exclusively for the purposes of renting out the property. Where costs are partly for the rental business, and partly for another purpose, a proportion can be claimed, if that part can be separately identified as being wholly and exclusively for the purpose of the business.

Capital expenditure: Capital expenses are generally not deductible. This category includes the cost of land and buildings, for example, or expenditure to refurbish a property bought in a run-down state.

Tip: Capital improvement or repair?

This boundary can be difficult to get right. The cost of maintenance and repairs to a property is allowable. Expenditure on capital improvement is not.

Definitions: HMRC considers capital improvement involves significantly improving an asset beyond its original condition. Extending the area of the original roof, or removing the roof to build another storey, is capital improvement. Repair is defined as

restoring an asset by replacing subsidiary parts of the whole asset: for example, the cost of replacing roof tiles blown off by storms.

Repairs include exterior and interior painting and decorating; stone cleaning; damp and rot treatment; mending broken windows, doors, furniture, and machines such as cookers or lifts.

Replacement of domestic items relief: applies to the cost of replacing certain items, such as moveable furniture; furnishings; white goods; and kitchenware. It is not available for the initial purchase, and does not apply to fixtures, or fitted furniture. It is not available if claiming Rent a Room relief.

Tip: Applies to like-for-like replacements

To qualify, the new item must be a replacement. If it is of higher quality than the old, relief is limited to the cost of an equivalent purchase. The replacement must have been bought for use by tenants in a residential property, and the item replaced must no longer be in use in that property.

Finance costs: Tax relief for finance costs on residential property (such as mortgage interest; interest on loans to buy furnishings, and fees incurred when taking out or repaying mortgages or loans) is restricted to a basic rate deduction of 20%. This increases to 22% from 6 April 2027, when separate Income Tax rates for property are introduced. Interest on loans to purchase commercial rental properties are deductible against the rental income.

New quarterly reporting regime

Making Tax Digital for Income Tax (MTD) is a new regime which will impact some landlords. It involves keeping digital records of income from property (and self-employment), and quarterly digital reporting of income and expenses to HMRC via MTD software. An end of year finalisation process involves various adjustments, and submission of the tax return, also via MTD software. MTD does not yet apply to partnerships.

MTD has already begun for those with what's called qualifying income from property and/or self-employment more than £50,000. Moving forward, it applies from 6 April 2027, for those with qualifying income more than £30,000; and from 6 April 2028 for those with qualifying income more than £20,000. Qualifying income here refers to gross income: for property, it includes both UK and overseas property income. Income from jointly owned property (based on each owner's share), premiums on leases and reverse premiums; and Rent a Room income, if declared on the tax return, all count towards the income threshold.

MTD presents special challenges for joint property owners, and there are some administrative easements to help. You need report only your share of income, for example, and though income must be reported quarterly, you can report your share of expenses, just once, in the end of year return.

Here to help

New rates of Income Tax for property income, plus new reporting requirements under MTD, put new pressures on landlords. Please contact us to review business profitability and exposure to tax going forward; to check that your property holding is structured appropriately; or for advice on MTD. We can help you navigate the challenges.

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