Tax Secrets for Property Developers and Renovators

By

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About Lee Sharpe

Lee is a Chartered Tax Adviser and tax consultant with over twenty years' experience in helping individuals, families, businesses and advisers with their tax affairs.

Lee writes extensively on tax matters for taxpayers and their advisers, including through the Tax Insider publications, Bloomsbury Professional and the TaxationWeb website. He also lectures taxpayers, accountants and other financial advisers on tax issues.

While he has appeared on TV to comment on tax matters, it was only long enough to establish that he really has a face for radio, and to give fellow members of his local CIOT branch sufficient ammunition with which to embarrass him at committee meetings.

When he is not giving tax advice or writing about tax matters, he is busy looking after his two small children – not because he likes them, but because he wants to make sure that his office is not used exclusively for business purposes…

1 About This Guide

In recent years, there has been a great increase in interest in the property market, and this guide offers advice on the tax pitfalls and opportunities for those who are involved in this dynamic sector.

In particular, it is aimed at:

1.1 Homeowners

All of us who own our own homes hope we are sitting on a goldmine! For many people, their home is their most valuable asset – for some, it is their pension fund!

This section of the guide looks at the tax breaks available to homeowners, and how to get the maximum benefit from them. It also warns of the traps for the unwary!

It is not unusual for a homeowner to find themselves becoming a property developer, perhaps by building another property on their land, or by receiving an offer from a developer to buy their home. We will look at the (sometimes unexpected) ways that such projects are taxed by HM Revenue and Customs (referred to in this guide from now on as HMRC).

1.2 Buy to Let

It seems that these days, everyone is a landlord! In this section, we shall look at the tax treatment of buy to let investors, both on the income from their properties, and on the sale of those properties. We shall cover the letting (and selling) of residential and commercial properties, and that interesting hybrid, furnished holiday accommodation.

1.3 Buy to Sell

Not everyone buys property in order to enjoy the rental income – many intend to turn the properties over quickly by selling them again at a profit.

This sector can be subdivided into three broad categories, all of which we shall look at:

- “**Turnarounds”** These work on the basic commercial principle of “buy cheap and sell dear”. A property is bought for a bargain price, perhaps at an auction, and sold on almost immediately, with little or no work done on it to increase its value.

- **“Refurbs”** As the name implies, in a “Refurb”, a run-down property is bought, then refurbished, and sold – or a large property is bought, converted into smaller units such as flats, and sold.

- **“Property Development”** This can be more or less the same as a refurb, or it may involve buying a vacant plot of land and constructing a new building on it for sale.

Unless otherwise indicated, we shall be using 2018/19 rates and allowances. 2017/18 saw the first tangible divergence in Scottish Income Tax rates when compared to the rest of the UK: for non-savings income; 2018/19 will see a significant divergence when comparing Scotland with the rest of the UK, as the Scottish government has not just moved thresholds this time but has introduced entirely new bands, and rates.

Interestingly for tax geeks, the Scottish devolved taxing powers basically cannot affect savings income (including dividends) so that the Scottish Higher Rate threshold for bank interest, dividends and the like will be £46,350 in 2018/19, just like the rest of the UK – which potentially makes for some quirky calculations around the c£43,000 - c£46,000 income band for Scottish taxpayers, depending on the mix of incomes at that level.

There are also potential knock-on implications, such as eligibility for the new Marriage Allowance. However, it should be emphasised that in very many cases, Scottish taxpayers will end up with similar results to rest-of-UK taxpayers and, even where they do not, the differences are likely to be relatively modest. **This book will apply the 'standard' UK rates and thresholds throughout.**

The Scottish tax regime also includes "Land and Buildings Transaction Tax" (LBTT) instead of the Stamp Duty Land Tax (SDLT) with which most readers will be familiar. From 1 April 2018, "Land Transaction Tax" will be payable in Wales, instead of SDLT. While very similar, there are differences between the three regimes, and readers operating in Scotland or Wales should get specific advice on LBTT and LTT respectively; this guide follows the SDLT regime such as it applies in the rest of the UK

2 A Word about Limited Companies

This guide looks at the taxation of individuals who own property, or trade in property, as sole traders or as members of a partnership.

In some cases, it can be advantageous to use a limited company as the vehicle for investing or trading in property – the commonest examples being:

- If you are hoping to avoid the new Draconian rules that restrict tax relief on mortgage interest for residential lettings undertaken by individuals (and other persons subject to Income Tax)
- If you intend to plough the profits from a rental business back into buying more rental properties, rather than to draw them out for personal expenditure
- If you are a property developer

The decision whether to use a company or not can be a very difficult one, and it is beyond the scope of this guide.

If you would like detailed information and advice about whether a limited company would be the best way forward for your business, our guide "**Using Companies to Reduce Property Taxes**" is available from www.property-tax-portal.co.uk. Between the two guides, they offer a comprehensive guide to tax for the property investor or the property trader.

3 What This Guide is Not About

All of the tax strategies in this guide are legitimate ways of planning to minimise your tax liabilities.

In some cases, they involve “grey areas” of the tax legislation, where there is more than one way to interpret the law, and where this is the case, it is clearly indicated in the text.

This guide is not about complicated tax avoidance schemes, many of which do not work, or are vulnerable to retrospective legislation.

It is most emphatically not about ways to <u>evade</u> tax – that is, to reduce your tax bill dishonestly by telling the taxman less than the whole truth.

The above may seem obvious, but we mention it because we have sometimes been quite surprised by the advice taxpayers tell us they have received from other sources – in some cases, if they had followed that advice, they would have been straying over the line that separates (legal) tax avoidance from (criminal) tax evasion – a line that was famously described by Dennis Healey, the former Chancellor of the Exchequer, as having “the thickness of a prison wall!”.

This distinction is so important that we will begin by looking at what separates tax planning, tax avoidance, and tax evasion.