How to maximise rental property returns – Ronnie Ludwig

30th December 2020 | By The Scotsman

Many people are turning to bricks and mortar investments, particularly the buy-to-let market, so it is extremely important to maximise the return on investment.

Capital gains tax is charged on most people at the upper rate of 28 per cent when selling a buy-to-let property at a profit. If borrowings have been obtained to purchase the property, tax relief on the interest payable to the lender is being reduced to basic rate tax relief only from April next year.

The good news is that a host of other expenses such as painting, decorating, repairs, insurance, letting agent fees and accountancy costs are still fully allowable against the rents. However, given the recent tax changes, it is more important than ever to maximise the return on the investment and the following tax saving strategies may be useful.

Take a husband and wife, where he is a high rate taxpayer and his wife is not. If he owns a buy-to-let property, he will pay top rate income tax on any net rents generated after deducting allowable expenses.

Sharing the cost

However, if he were to transfer ownership of even a very small part of the property to his wife, even 1 per cent, he will be taxed on only one half of the rental income, and not on 99 per cent of it. This is because the tax rules state that where a husband and wife (or civil partners) own an asset jointly, the income from that asset is taxed on them equally whether or not they own it equally.

The result is that the wife would be able to use her personal income tax allowance of £12,500 against her share of the rent, with any excess being taxable on her at the lower rate bands of 19 per cent or 20 per cent, if she has no other income.

There will be no capital gains tax on the gift between husband and wife as this is covered by the inter spouse exemption in the terms of which the wife will be deemed to have acquired her share at a proportion of the original cost price to her husband.

Another advantage is that when the property is sold, the wife's capital gains tax exemption (currently £12,000) will be available to set against her share of the gain.

A special provision in the tax statutes can produce an even more satisfactory result if a couple own a buy-to-let property in unequal proportions, then they have the option not to be taxed on equal shares but according to their actual shares in the property - but only if the spouse who owns the property is willing to give up substantially more than a 1 per cent share in it to the other spouse or civil partner.

Unmarried couples who jointly own a second home could simply enter into a partnership agreement allocating the lion's share of the net profits to the partner with the lowest income tax liability. The profit-sharing arrangement would relate only to the income generated, not to the underlying ownership of the property itself.