Individuals and Landlords

Landlords! There are significant savings you can make on property investment and rental income if your portfolio is optimised. Come and chat to us.

Occasionally, individuals will need to fill in tax returns due to changes or unusual circumstances in their working lives, capital gains and investments etc. A low cost accountancy service like Discountants is ideal for this as you can get the questions dealt with and get peace of mind for a very reasonable price. We specialise in rental property and property investment accounting so I will discuss these issues in more depth.

Worst case property scenario

Mortgage on your home, rental property paid for in full. Mortgage interest paid from earnings after tax, rental income taxed in full.

Best case scenario

Home paid for in full. All borrowing on investment property as interest only BTL (Buy To Let) mortgages. No after tax interest payments made on your home. All interest payments allowable as expenses before tax on rental income. Taxable proportion of rental income reduced correspondingly through use as coverage of interest payments.

A double whammy!

As you can see, there is a double tax winner here. Your interest payments are paid before tax instead of after tax and as your rental income is used to pay the interest before it is taxed there is a reduction of tax here too.

Capital and gearing up

A key objective of property investment is to benefit from capital growth. If you borrow on your investment you enter into a process called "gearing" In other word you gear up your gains like this...

Example property

You buy a £100k flat but you only put down £25k and borrow the remaining £75k. The property is therefore worth four times what you pay for it. A few years go be and you have some good luck. You find your property increases in value 10% so it is now worth £110k. You have made £10k. However, you only put down £25k so whilst the property increased in value 10% your return is £10k on £25k or 40%.

Needless to say you need to pay your mortgage but this is usually a similar amount to the rental income so, as we said at the top of this page, these two balance each other out before tax so the burden on you personally should be very small.

The current market

In the current market of falling prices the gearing of course works the other way and your losses are multiplied much as your profits used to be. If values fall far enough you may find you have lost all your deposit and be in what is euphemistically called 'negative equity'. However, you are not out until you sell and if your rent covers your outgoings, you will probably be blest with both time and choices. You must make a decision about the long term and you may feel, as many do, that prices will eventually recover.

The fundamentals of property demand in this country are...

We are an Island with limited land.

We have a highly developed planning system which impedes unbridled development and stifles supply

We speak the worlds favourite second language, which lowers anxiety in potential immigrants.

We are in the UT timezone, (eg our financial markets capture the opening times of most others across the globe). There pink areas on the map may have long gone but the little splodge of pink that is left (thats us!) is in the right place!

Currently lots of people still want to live here and there is a strong work and wealth ethic here. Laziness and dependency are generally disdained.

We are a tolerant multicultural society with a lenient immigration policy. EU free movement regulations may serve to increase work driven immigration - if there are any businesses left to work in by the end of all this!

Despite the exceptions, the UK is still a place where trust and decent business practices are generally the cultural norm.

Back to the theme...

Repayment mortgages :-(

Now you have borrowed to maximise the amount of capital you have "in the game". After all, the more capital you have under control the more you will benefit from house price inflation. If you have a repayment mortgage, you will not receive tax relief on the amount repaid (the capital). Remember your investment (deposit money) is increasing at roughly 4 times house price inflation. You will see that the capital you are paying off is only increasing at house price inflation which is only 1/4 of your potential growth. Using a repayment mortgage on a rental property is simply borrowing capital to maximise the capital you have by "gearing" and then immediately starting to pay back that capital, erode your important "gearing". Remember, that you are never going to live in your rental property (well you might for a year or so in the future but that is another story) so it is of no consequence that you will have to re-finance it or sell it at the end of the mortgage term. Therefore, actual ownership of the property is not really important, what is important is gaining from the capital growth, which is arguable the main reason for being in property as an investment.

Interest only mortgages :-)

Logically therefore, an interest only mortgage is the correct vehicle for property speculation or investment. The monthly charges will be lower than a repayment mortgage and are 100% allowable against rental income. At the very least, this gives you the choice of investing the difference in an investment but what it may do is allow you to afford a bigger investment property in the first place.

Things aren't really that simple are they?

Well if I was to say "yes and no", that wouldn't be simply "yes" so it must mean "no" of course! There are one or two major pitfalls, not least of which is your attitude to risk. Needless to say if you gear up your potential for return as your property increases in value, if there is a property crash, your investment loses 4 times as much as the fall as well. A case of no pain, no gain! From the tax and accounting point of view there is also a borrowing limit based on a property valuation when you started renting which acts as a limit. However, these technical questions are why we are here, so you should contact us for more information. Our IFA (Independent Financial Advisor) can help you with the selection of suitable mortgages for your investment portfolio.