



Hall Morrice
Chartered Accountants



KEY GUIDE

Taxation of property

Introduction

PROPERTY OUTLOOK

For anyone looking to enter the buy-to-let market as a new landlord, the decision is currently far from straightforward. On the plus side:

- Average English rents increased by 4.4% over the year to November 2025, with the average monthly rental now standing at £1,422; and
- Mortgage rates eased throughout 2025, with further cuts expected for 2026.

On the negative side, the recently enacted Renters' Rights Act 2025 means significantly increased rights for tenants. There are concerns about how quickly the changes are being introduced. Also, at the November 2025 Budget it was announced that from 6 April 2027 the income tax rates on property income will effectively be increased by two percentage points.

Please note that all examples included in this guide are fictitious.

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Taking in a lodger, short-term lettings, holiday rentals and commercial properties



Becoming a landlord

Anyone thinking of becoming a landlord should be in a fairly strong position if they are either a cash buyer or are able to put down a substantial deposit, especially as the property market has cooled somewhat, with only modest price increases forecast for 2026.

New landlords are now faced with a 5% buy-to-let SDLT surcharge when purchasing property in England or Northern Ireland. The surcharge means a landlord has to pay SDLT of £20,000 on a property costing £300,000, which is some £15,000 more than a normal purchaser. The surcharge for Welsh landlords is broadly similar, but Scottish landlords face a considerably higher cost.

Rental income remains reasonably attractive. UK rents increased by 4.4% on average over the year to November 2025, with rent inflation in the North East particularly high at 8.4%.

One particularly difficult decision is whether to opt for a fixed rate or a variable rate mortgage, and, if fixed, for how many years. It all depends on your view of where interest rates are going to go; an especially difficult decision given the four cuts to the bank base rate across 2025. A variable deal will mean an immediate saving if interest rates fall further, but a longer fixed-rate deal provides certainty; and a saving if interest rates were to increase again and then remain high for a few years.

FINANCE COSTS

For those looking to invest in property, an individual's finance costs, such as interest on mortgages and loans to furnish a property, are not tax deductible. A basic rate relief tax reduction is given instead.

One way to avoid the finance costs restriction is to use a limited company structure to purchase property. In the example below, a

company would have paid tax of just £1,900 ((£18,000 – £8,000) at 19% (assuming the company's profits do not exceed £50,000)) with 100% of the finance costs being deductible. However, as explained later in this guide, Alice would then face more tax when extracting the property income from the company.

EXAMPLE

Finance costs restriction

For 2025/26, Alice, a higher rate taxpayer living in Suffolk, has buy-to-let rental income of £20,000, allowable deductions of £2,000 and finance costs of £8,000.

None of Alice's finance costs are deductible, so her property income for 2025/26 is £18,000 (£20,000 – £2,000), on which she will pay higher rate tax of £7,200. She can then deduct tax relief at the basic rate for the finance costs (£8,000 at 20% = £1,600), resulting in a tax liability on her property income of £5,600 (£7,200 – £1,600).

JOINT OWNERSHIP

Income from a rental property owned jointly with a spouse or civil partner is normally shared equally for income tax purposes, even if the actual ownership is different. This can be quite advantageous if your spouse or civil partner pays tax at a lower rate than you. They can be given, say, a 10% share of the rental property, but 50% of the property income will be taxed at the lower rate.

If you wish to be taxed on your actual share of ownership rather than the deemed 50:50 split, this can be achieved by making a declaration of beneficial interests to HMRC.

For CGT and inheritance tax (IHT) purposes, the actual share of ownership is always used.

The question of joint tenancy or tenancy in common also needs to be considered. On death, a share of a property owned under joint tenancy automatically passes to the surviving joint tenant. With tenancy in common, the deceased's share of the property is distributed in accordance with their will or the rules of intestacy.

RENTING OUT A PROPERTY

Using a letting agent

A good agent will be invaluable when it comes to finding tenants (and filtering out bad ones) and ensuring that tenancy agreements are watertight. They will be up to date with property legislation, such as the Renters' Rights Act 2025 (see the section Future changes, below). They can take much of the stress out of maintenance and provide an impartial buffer should the tenancy go sour. However, lettings agents are not cheap, so one popular option is to use an agent just to find and vet tenants, and to set up the tenancy.

Basis of taxation

The basis for taxing property is not quite as simple as you might think. For individuals, property income is calculated on a tax-year basis, with accounts being prepared to 5 April (31 March is permitted). Income and expenses for all your buy-to-let properties are pooled together, with figures normally calculated on a cash basis. Rent and expenses are therefore included when received or paid. For companies, property income is calculated according to the company's accounting period and must be done on an accruals basis.

Making Tax Digital (MTD)

MTD for landlords will start to come into effect from 6 April 2026, initially applying if your annual property income is more than £50,000. Where MTD is applicable, MTD-compliant software will have to be used to create and store digital records of property income, along with the related expenses. Details will have to be reported to HMRC on a cumulative quarterly basis.

Allowable deductions and reliefs

Allowable expenses must be incurred wholly and exclusively for your buy-to-let business, and could include:

- letting agent's fees;
- cost of maintenance, repairs and gardening;
- council tax, water rates, gas and electricity;
- property insurance;

- advertising; and
- business mileage calculated using HMRC's mileage rates (45p per mile up to 10,000 miles, and 25p thereafter) or based on the actual cost.

You can also deduct any amounts spent on replacing furniture and furnishings, including beds, televisions, fridges and freezers, carpets and floor coverings, curtains, and crockery and cutlery. However, there is no relief for the initial cost of furniture and furnishings. The amount of relief is reduced by any proceeds from selling the old asset which has been replaced. Also, relief is not given for any cost which represents an improvement, for example, if a washing machine is replaced with a washer-dryer, only the cost of an equivalent washing machine qualifies for relief. However, this rule is relaxed if the improvement element is incidental, such as replacing single-glazed windows with the modern equivalent of double-glazed windows, or where a new boiler represents an upgrade due to advancements in technology.

Property allowance

An annual property allowance of £1,000 can be claimed as a deduction by individuals if this is more than your actual allowable deductions and reliefs.

Multiple occupancy

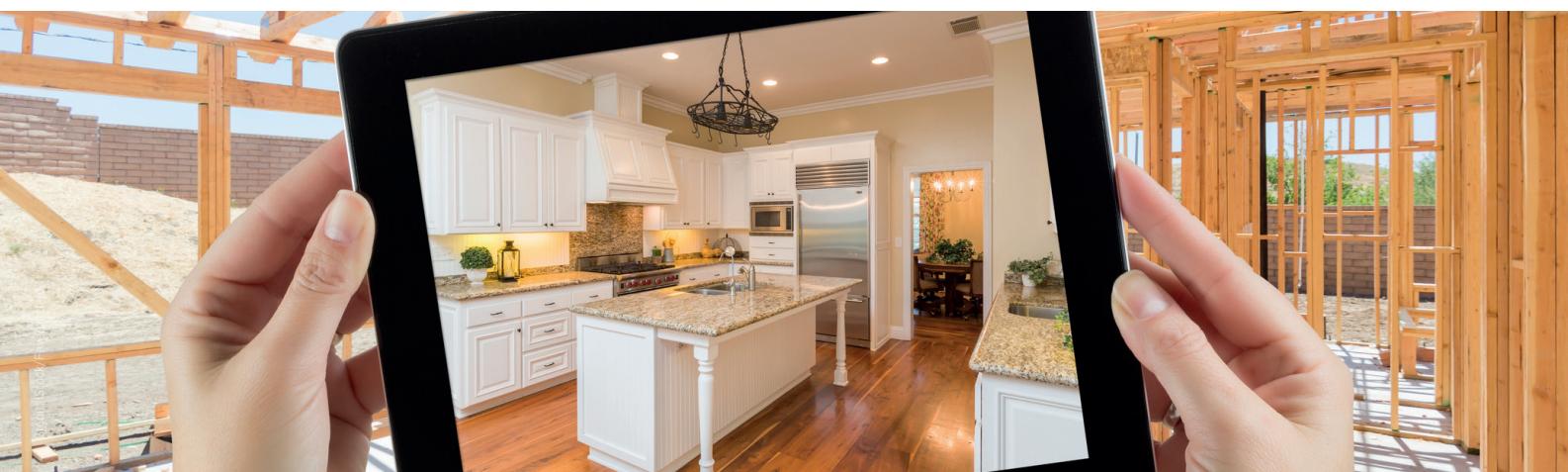
You need to be aware of the additional requirements if you rent out your property as a house with multiple occupancy (an HMO). This is a complex area, but essentially multiple occupancy means at least three tenants, forming more than one household, but who share facilities like a bathroom. Student lets are normally classed as HMOs. Fines can be punitive for renting out an HMO without having the required licence.

Selective licencing schemes

A number of councils have introduced selective licencing schemes for all rental properties within certain designated areas. Licences typically cost between £500 and £1,000, with schemes generally running for a five-year period. Licencing schemes are constantly changing, and landlords need to be aware that the fine for non-compliance can be substantial.

Future changes

It is not just the current rules and regulations that you need to be aware of, but also future changes.



From 6 April 2027, property income will have its own individual rates of income tax, which are all two percentage points higher than the rates currently applicable. The property basic rate will be 22%, the property higher rate will be 42% and the property additional rate will be 47%.

The recently enacted Renters' Rights Act 2025 will bring in various changes for English landlords, with the first phase of reforms set to be introduced from 1 May 2026. From that date, all existing assured shorthold tenancies in England will automatically convert to periodic tenancies, with only the new type permitted for new tenancies. Under a periodic tenancy, tenants can stay in the rented property for as long as they want, and will be able to end the tenancy by giving two months' notice. Other changes include:

- No-fault evictions will be abolished (so, in future, landlords may want to take out rent guarantee insurance to cover the risk of a tenant defaulting – the average rent lost when a tenant is evicted is estimated at more than £12,000 outside of London, rising to over £19,000 for a London property);
- Only one rent increase will be permitted a year, and tenants will be able to challenge rent increases where they consider rent to be higher than the open market rate;
- Landlords will not be able to unreasonably refuse a tenant having a pet (landlords will not be able to request pet insurance to cover any potential damage); and
- Landlords will not be able to discriminate against tenants who receive benefits or have children.

There are reports of landlords selling up in advance of the Renters' Rights Act 2025 reforms being introduced. However, a somewhat similar tenancy regime has been in place in Scotland since 2017, where there are no longer no-fault evictions. Scotland has also just enacted legislation that will impose rent controls in certain areas, (although this is not expected to be introduced until 2027), and is looking at introducing a minimum energy performance certificate (EPC) rating of 'C' for landlords by 2033. The 'C' rating requirement could be a major issue for Scottish landlords with just a few older properties. Although the previous Conservative government backtracked over changes to the minimum standard of energy efficiency for property situated in England and Wales, the Labour government

has announced that a minimum (EPC) rating of 'C' will be a requirement for landlords by 2030. Currently, the minimum required EPC rating for England and Wales is 'E'.

Planning point

It can make sense to retain existing tenants by foregoing rent increases. Apart from having an unlet period and the costs associated with finding a new tenant, there is generally no discount from council tax for empty properties.

FURNISHED HOLIDAY LETTINGS

Furnished holiday lettings previously qualified for various tax advantages, including not suffering from the finance costs restriction when calculating property income. However, the furnished holiday lettings tax regime has been abolished from 6 April 2025. Furnished holiday lettings are now treated exactly the same as any other buy-to-let for tax purposes, with the finance costs restriction being applied.

Despite the loss of the tax advantages, a furnished holiday letting situated in England will still normally be able to register for business rates rather than council tax. There will then be nothing to pay if small business rates relief is available. The qualifying conditions are essentially that a property must be available for letting at least 140 nights over the past 12 months, and was actually let for at least 70 nights. Scottish rules are similar, but Welsh rules are considerably stricter.

Another advantage of short-term holiday letting is that the various changes to be brought in by the Renters' Rights Act 2025 will not apply.

TAX IMPLICATIONS OF BUYING A PROPERTY

While finding the right property in the right area at the right price will be at the forefront of your mind when looking to buy, you should not forget the tax implications.

Stamp duties

Although you will incur various lending, legal and survey costs, SDLT is usually the biggest expense when purchasing a property in England or Northern Ireland. SDLT rates are increased by 5% when it comes to buy-to-lets, regardless of whether you buy the property personally or through a limited company.

Stamp duties on second residential properties

England and NI – Stamp Duty Land Tax	Rates	Scotland – Land and Buildings Transaction Tax	Rates	Wales – Land Transaction Tax	Rates
£0 to £125,000	5%	£0 to £145,000	8%	£0 to £180,000	5%
£125,001 to £250,000	7%	£145,001 to £250,000	10%	£180,001 to £250,000	8.5%
£250,001 to £925,000	10%	£250,001 to £325,000	13%	£250,001 to £400,000	10%
£925,001 to £1,500,000	15%	£325,001 to £750,000	18%	£400,001 to £750,000	12.5%
Above £1,500,000	17%	Above £750,000	20%	£750,001 to £1,500,000	15%
				Above £1,500,000	17%

If you are purchasing a buy-to-let in Scotland, you will pay land and buildings transaction tax (LBTT) instead of SDLT. For buy-to-let purchases in Wales, land transaction tax (LTT) applies. The buy-to-let surcharge is 8% for Scottish property and 5% for Welsh property (although there is an anomaly for Wales in that the surcharge is effectively 8.5% from £180,001 to £225,000, 2.5% from £225,001 to £250,000 and 4% from £250,001 to £400,000).

In each case, tax is paid on the slice of the purchase price falling within each tax band.

The 5%, 8% and 5% surcharge rates are not charged on a property costing £40,000 or less, meaning no SDLT, LBTT or LTT will be charged for such a purchase.

As a general rule, living in a property before letting it out will not get around the surcharge. The only situation where the surcharge will not apply is when your buy-to-let purchase is your only property, such as where you are personally living in rented accommodation.

EXAMPLE **SDLT calculation**

Emma, who already owns a main residence, purchases a buy-to-let property in England for £380,000 on 31 January 2026. The amount of SDLT payable is £25,500, calculated as:

First £125,000 at 5%	£ 6,250
Next £125,000 (£125,001 to £250,000) at 7%	£ 8,750
Final £130,000 (£250,001 to £380,000) at 10%	£13,000
	<u>£28,000</u>

Personal or corporate purchase?

An important decision that you will have to make at the outset is whether to purchase your buy-to-let property personally or through a limited company. The restriction to the tax deductibility of finance costs (explained above) has made the company route increasingly attractive. The relatively low 19% small profits rate of corporation tax also means that this option makes sense if you are aiming to retain profits for reinvestment in additional property or to repay some of your financing. However, higher rates of corporation tax apply if a company's profits exceed £50,000. Where a company's profits fall between £50,000 and £250,000, the small profits rate of 19% only applies on the first £50,000 of profits, with an effective rate of 26.5% applied on profits falling between £50,000 and £250,000. If profits exceed £250,000, a main rate of 25% applies to all of the company's profits.

A company structure makes it relatively easy to include family members in your property business, and control can gradually be passed to children or grandchildren which makes for good IHT planning. The overall tax charge might well be higher if profits



Credit: iStock/simpson33

are withdrawn from a company. If taken as remuneration, national insurance contributions could be payable. If extracted as dividends, there will be a double charge to tax for dividends in excess of the £500 tax-free dividend allowance. Capital gains may also suffer a double tax charge.

EXAMPLE **Tax charge on company dividends**

Winston, a higher rate taxpayer, has £20,000 of property income within his property company, which he wishes to withdraw as a dividend during 2025/26.

If Winston had received £20,000 of property income as an individual, then he would have paid income tax of £8,000 (£20,000 at 40%), leaving him with £12,000.

Assuming the small profits rate is applicable, the company will pay corporation tax of £3,800 (£20,000 at 19%), leaving £16,200 to pay out as a dividend. If the dividend allowance is not available, Winston will pay income tax of £5,468 (£16,200 at 33.75%) on the dividend, leaving him with net income of £10,732.

From 6 April 2026, the basic- and higher-tax rates on dividend income will both increase by two percentage points. For 2026/27, the income tax cost of taking a dividend will therefore increase to £5,792 (£16,200 at 35.75%) on the dividend, leaving Winston with net income of £10,408.

TAX IMPLICATIONS OF SALE OR DISPOSAL

Your buy-to-let property portfolio may increase in both size and value, and at some point, you may want to cash in some properties, possibly to pay down the finance on those to be retained. Another option as you get older might be to gift some properties to your children or grandchildren. CGT will come into play whether you sell or gift property, although this tax can currently be avoided by simply retaining property until your death. Your children or grandchildren inherit properties with an uplifted base cost for CGT purposes, although IHT then becomes an issue.

- **CGT** The gain will be based on what you sell a property for, or its market value if gifted. You can deduct the original purchase cost, incidental costs of purchase and sale (such as legal fees and stamp duties) and any expenditure which has enhanced the value of the property (and will therefore not have been deducted as repair expenditure when calculating property income). If a property has not been occupied as a

main residence, the only exemption, if available, will be the annual exempt amount (£3,000 for 2025/26 and 2026/27). Gains will then sit on top of your income for the tax year of sale or disposal. Any part of the gain that falls within your basic rate band will be taxed at 18%, with the remainder taxed at 24%. A payment on account of the CGT due is required 60 days after completion.

- **IHT** Outright gifts of property have IHT implications if you die within seven years of making the gift. If your property portfolio is retained until death, it will be included as part of your estate at its value at the time of death. Basically, IHT is payable at 40% once a nil rate band of £325,000 (up to £650,000 if you benefit from the nil rate band of a deceased spouse or civil partner) is exceeded.

Property retained after moving homes

Many landlords have built up property portfolios by retaining property when they move homes, with the retained properties then rented out. One attraction of this approach is that rental properties, having previously been occupied as a main residence, can often be sold in the future at little or no CGT cost.

A proportion of the gain arising on sale is exempt, based on the period of occupation. In addition to actual periods of occupation, the final period of ownership is also exempt. However, this final period exemption is limited to nine months.

Corporate disposals

If you have used a company structure for your buy-to-lets, then any gains will be made within the company and taxed at the company tax rate of 19% or 25% (or even 26.5%). But note that companies do not benefit from the annual exempt amount.

Should you wish to extract the proceeds of a company property disposal, you will face a potential double tax charge – the corporation tax payable on the gain, then personal tax on the withdrawn proceeds – which is inefficient compared to the tax cost of disposing of a personally owned property.

For gifts during lifetime or on death, the relevant asset will be the company's shares rather than the underlying property assets. The value of the company's shares will be included in your estate on death, with no uplift to the base cost of the property held within the company. IHT business relief does not generally apply to property company shares.

OTHER TYPES OF PROPERTY LETTING

The introduction of the finance costs restriction for buy-to-lets has spurred interest in other types of property letting which do not suffer the same restriction.

Commercial property

You might not like the idea of commercial property, but semi-commercial property, such as where there is a flat above a shop, could be an attractive proposition, being halfway between commercial and residential investment. The purchase of such a mixed-use property will not suffer the relevant stamp duty surcharge, and the finance costs restriction will not apply

to those finance costs associated with the purchase of the commercial element of the property.

There is an annual 3% write-off if you buy commercial property where the construction contract was signed on or after 29 October 2018. The cost of converting or renovating an existing property also attracts the 3% relief, but the value of land and any dwelling element are excluded.

The rental yield from mixed-use commercial property is often significantly higher than that from a traditional buy-to-let.

Renting a room

Do not overlook the tax advantage of renting out a furnished room or rooms in your own home, especially to a long-term lodger. Rents of up to £7,500 each tax year are exempt from tax, which will be quite beneficial for a higher rate taxpayer. The relief does not apply, however, if you have converted part of your home into a separate flat.

You can either rent to a long-term lodger or make use of an online site such as Airbnb to offer holiday lets. Don't forget to inform your mortgage lender, review insurance cover and check whether there are any local authority restrictions. Leaseholders may find, however, that short-term renting is not permitted under the terms of their lease.



Credit: iStock/Alena Kravchenko

HOW WE CAN HELP

We can help you to understand the tax implications prior to you purchasing a property, and the effects of using corporate structures.

We can help you understand what a sale will cost in tax terms. We can also discuss estate planning options that can help keep IHT liabilities to a minimum.

Important changes on how furnished holiday lettings are taxed have come in from April 2025. We can advise on the impact of these changes and keep you up to date with any further changes.



Hall Morrice
Chartered Accountants

**Hall Morrice
Chartered Accountants**

6&7 Queens Terrace
Aberdeen AB10 1XL

Tel 01224 647394
E-mail accounts@hall-morrice.co.uk
Web www.hall-morrice.co.uk

Partners

Shonagh L Fraser C.A.
Robert J C Bain C.A. C.T.A.
Derek J Mair F.C.C.A.
Derek J Petrie C.A.
Chris Colville C.T.A. T.E.P.
Louise Smith C.A.

Directors

Michael I Innes MCIBS
Paul Archibald C.A.
David Ewen C.A.
Peter Cowan C.A.

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