# WHAT CAN I DO WITH SPARE FUNDS HELD IN MY PROPERTY COMPANY?

By specialist property accountant **Stephen Fay FCA**

**Many property investors now operate a limited company but may not be able to tax-efficiently take all of the company's profits out, due to their personal income. This article looks at what options are available to company property investors who want to be tax-efficient by retaining spare funds within their company.**

## Spare funds in a property company? That sounds nice, how does that happen?

Many residential landlords now invest in property via a company, or may have a property management company, and may have personal income that is already at or above the Higher Rate income tax threshold (or, the investor may have a well-paid non-property PAYE employment role and property investing is a side-line).

If the director has a director's loan account in credit – meaning, the company owes the director back for initial funds loaned to the company – the director can then access the company's profits by treating funds taken from the company as a director's loan repayment, which is tax-free.

However, eventually the director's loan account will be repaid, and then the director would need to take taxable dividends to personally access the company's profits (for 2019 onwards, only the £2k/person dividend allowance is tax-free). Basic Rate dividends are only taxed at 7.5%; however Higher Rate dividends are taxed at 32.5% – which, combined with the 19% corporation tax payable, makes for an excessive tax burden.

### 1. Use spare funds to buy new properties

It sounds obvious, but if the company has spare funds, these can be used as deposits for more properties owned by the company. In a company, all the mortgage interest payable is fully tax-deductible so all the usual benefits of using leverage (mortgages) to buy property apply. As the funds are not being extracted from the company, there is of course no tax charge to use the company's spare funds to buy more property.

### 2. Make pension contributions

The company can make a gross pension contribution of £40k/person, which is a tax-deductible expense for the company. This can be a very smart use of spare company funds, because the company not only gets a corporation tax deduction for the pension contribution, but the funds within the pension are then very Inheritance Tax-friendly, as pensions can be passed to dependents tax-free. Potentially, over £1m of property profits could be transferred to a pension, and then the pension could be allocated IHT-free to dependents – effectively 'converting' IHT-unfriendly profits into IHT-friendly funds.

### 3. Pay down company borrowings

Most property investors reach a portfolio size that they are happy with, and decide not to expand the portfolio. At that point, spare funds can be used to make lump-sum mortgage repayments, or interest-only mortgages can be converted to repayment loans.

For many investors, a modest debt-free property portfolio is the ultimate goal – for Higher Rate taxpayers, not extracting company profits and instead paying down debt tax-efficiently, is a great way to achieve their ultimate goal.

### 4. Invest in the company's properties

It's a rare property investor who hasn't got some repairs to spend money on! There are the usual very visible (to tenants) repairs, such as decorating, carpets, kitchens and bathrooms, which can alone add up to serious investment – but also the less noticeable investment into the fabric of the building itself, such as brickwork, pointing, roof, gutters and fascias, electrics, plumbing, etc.

For properties that are planned to be held for the long-term, spending spare funds on protecting the building is usually money well spent, and usually pays for itself in terms of lack of future leaks, tenant complaints, voids, rental levels, etc.


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### 5. Pay yourself claimable expenses

Some funds can usually be taken from a company as legitimate expenses, which are not taxable income for the director in any event. Such expenses might include business mileage (ie the company is paying the director to hire the director's personal car for business use, usually @ 45p/mile), home office allowance (ie the company is paying the director to use the director's home for business use), interest on a director's loan, reimbursement for expenses incurred on the company's behalf, etc.

### 6. Pay salaries to family and friends

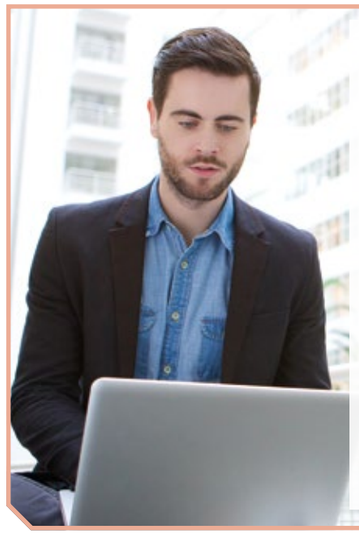
It is possible to involve family members or trusted friends / business partners, if those individuals do genuine work for the company – such as: property management, refurb advice and monitoring, insurance and mortgages review, book-keeping and financial management, etc.

A 'Lower Earnings Level' (2018: £5,876) salary can be paid to a person without the company needing a formal PAYE scheme, and any self-employed person can invoice a company for services provided. Of course, the recipient of the company's funds ought to declare that income as income, but that is a matter for the person concerned.

### 7. Use the company's spare funds as your personal savings

Although dividends can't be permanently taken from a company without tax being paid, it is possible to run up a director's loan account 'debit' (overdraft) with a company, ie to borrow money from your company on a non-permanent basis.

'Non-permanent basis' means that the funds have to be repaid to the company within nine months of the company's year-end (not within nine months of having borrowed the money). So, for example, borrowing money in July 2018 from a company with a year-end of 31st March 2019, would mean that the loan from the company needs to be repaid by 31st December 2019 to avoid a tax charge on the loan, ie the director has 17 months to repay the loan. (Note: some interest must be paid to the company to cover the 'Benefit-In-Kind' tax that would otherwise arise, but this is very minimal, ie 3% per annum.)



### 8. Buy new consumable assets

All companies need 'consumable' assets to operate and a property company is no different. Such assets would be computers, phones, tablets, printers, scanners, monitors, office equipment, etc. And, even luxury pens (eg Mont Blanc), folders, briefcases, etc, are allowable expenses if genuinely used for business.

The key is that there is a credible reason why the item is a business expense – there is no specific amount as an allowance, although it's unlikely that a diamond-encrusted solid-gold iPad is likely to be accepted by HMRC as having no personal 'dual purpose' whatsoever!

> "Using a company is often a very tax-efficient way to invest in property"

### 9. Lend funds to other investors

Many company directors with spare funds are investing those spare funds with other property investors, typically those at an earlier stage in their property investing career, and have made good profits as a result. Sometimes this will be for a fixed % rate return, and sometimes it will be for a share of the anticipated profits of a development of rental investment.

### 10. Finally – don't buy or lease a company car!

A fairly common question is, 'should I buy a company car?' – the answer is almost (99.9%) always a resounding 'no'! The reason is that company cars are taxed on both the director **AND** the company, which makes for a prohibitive tax bill, unless the car in question is an electric car of very low CO2 emissions. In practice, most reasonable cars are far better owned personally by the director, and mileage of 45p/mile charged to the company (note – this is an important topic and will be covered in depth in the September 2018 edition of YPN).

## In summary ...

Using a company is often a very tax-efficient way to invest in property, or manage property, following the 'Section 24' mortgage interest relief restrictions that started in tax year 2018. However, for many property investors who use a company and have exhausted their in-credit director's loan account, paying 32.5% Higher Rate dividend tax on funds taken from the company isn't an attractive proposition. This article sets out a number of ways in which such investors can retain funds within their company and so grow their wealth as a result.

It may well be that at some future point in life such investors may revert back to being Basic Rate taxpayers, and so extracting company funds at that point becomes much more acceptable. Or it may be that such investors decide that their personally-held portfolio profits are for day-to-day spending, and that their company is for long-term wealth-accumulation, perhaps with estate-planning and succession planning in mind. Either way, Higher Rate taxpayers have to make the classic investment decision – do I take more income from my company and just pay the extra tax, or do I retain profits within my company to build wealth rather than spending it now?