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Seven Landlord Tax Mistakes

With good planning, investors can avoid making tax mistakes that can easily take a large chunk of their hard-earned profits. Specialist property accountant **Stephen Fay** ACA of Fylde Tax Accountants considers some typical tax mistakes that property investors make.

1. No tax planning at all

Many investors simply don't have a tax strategy, or even a basic understanding of the tax-saving options available to them. Some see tax as 'my accountant's job' - which of course it is - but then have no interest in understanding more, and improving their own knowledge. This is at odds with most small business owners - who typically take a keen interest in all aspects of their business.

Most investors understandably enjoy the buzz of a new purchase or a successful development. But, committing to gaining a wider understanding of the profit and losses, tax-planning options and financial affairs of their business would greatly benefit some investors - you know who you are!

Tax Tip: Work with your accountant to build up your wider business management and tax knowledge. Investors that have a good grasp of the financial and tax side of their business tend to be far more successful. Delegate the work - but not your understanding of it.

2. Paying Higher Rate income tax on rental profits

With interest rates at an all-time low, many investors are making rental profits and don't have the benefit of losses from previous years to use up. Planning ahead should be second nature for any business - and so tax-planning measures can be put in place to reduce the overall tax hit.

Options such as re-arranging the ownership structure, or using a management company, are often well worth looking at. Profit and unit projections are needed to determine the size of the tax problem - so that a suitable solution can be found.

Tax tip: Effective tax-planning requires an understanding of future plans & profits, so that cost-effective solutions can be found. Using the free Cash-flow Tracker Tool on our website can help investors to map out their business to develop short, medium and long-term plans.

3. Missing key deadlines and tax-saving opportunities

The tax regime is changing constantly, and some changes have strict deadlines that require investors to react, or even anticipate, changes. Recent examples include the October 2010 HMRC Briefing in relation to capital allowances - for some investors, missing this deadline meant the loss of tens of thousands of pounds in allowances (our office worked flat-out that week filing claims in advance of the changes!).

> **"Take professional advice to ensure that your property ownership, trading and management set-up (as relevant) is appropriate"**

Similarly, the change to the loss relief rules for European holiday lets had various key dates for claiming tax repayments. These were 'hard' dates that if missed were a painful lesson!

Tax tip: The UK tax regime has been built up over 200 years and is a mass of inconsistencies, loopholes and seemingly random rules. Being aware of changes and opportunities BEFORE these hit the mainstream media can be very beneficial.

4. Using a company / partnership / LLP / Trust

Don't get me wrong - each of these structures can be useful to investors. But it's surprising how many investors set up such structures unnecessarily and without adequate understanding of when each are useful.

This can lead to unnecessarily high professional fees, extra admin and red tape, more scope for HMRC Enquiries (particularly where property is transferred into a company), and in some cases, actually higher tax bills.

Investors need to ensure they have a clear requirement and tax strategy before setting up, and changing, business structures. For many investors, operating in their personal name is sufficient - keep it simple, wherever possible.

Tax Tip: Don't be an amateur - take professional advice to ensure that your property ownership, trading and management set-up (as relevant) is appropriate for your needs. Also, ensure that your adviser formally documents the rationale for any recommendations - so that you remember why you operate as you do-

5. Poor records...the Achilles heel

This is the boring bit for any business but it is also the area that HMRC will often have a field day, in the event of an enquiry. My advice is to give your business the attention and effort that it serves - setting up simple systems and processes ensures that investors can claim, and support, all the expenses

they can, and that the tax treatment of some items (like refurbishment costs) can be proven.

Paying cash to tradesmen (with no receipt), mileage records, rent payments in cash, business expenses incurred personally (not through the business bank account), records to claims against capital gains tax bills etc. - these are all areas that HMRC regard as 'rich pickings' for many property investors.

Tax Tip: Set aside some time to create your own record-keeping system - it's boring, it's mundane, but it's about taking your business seriously. Use our free & simple Excel Workbooks to help you to manage your monthly cashflow, income and expenses, record data for tax purposes, and log capital costs.

6. Expending more effort in saving tax then making money!

Nobody likes paying tax - from those on minimum wage to the top earners. But it's important to focus more on creating value. It's difficult to turn a loss into a profit.

Healthy rental profits enable investors to ride out voids, peaks in maintenance spending, and higher interest rates. While the 'private equity' model of running high debts against appreciating asset values is not the reckless gamble that some say (there are exceptions), when investors come unstuck it is usually because of a lack of actual profits and cash.

In other words, don't run the ship TOO tightly - few long-term investors have not had their share of scrapes - remember that running a sound business that makes profits andpays a bit of tax is generally regarded as a good thing!

Tax tip: Keep tax in proportion - get the big decisions right (ownership structure, using an experienced adviser, identifying all relevant expenses, planning property sales carefully, keeping significant receipts etc). Don't sweat the small stuff - penny-pinching versus good cost control.

7. Selling property without planning the sale carefully

With the CGT rate for Higher Rate income taxpayers now at 28%, there is all the more need to carefully plan strategic property sales (note - selling off poor-yielding properties with equity in them is often a good way to release 'lazy equity' for reinvestment into better property, or to pay down debt).

This means that tax considerations now need to consider the income tax position as well as CGT allowances and reliefs. For example, for business owners, could investing in your company and claiming EIS relief to defer any CGT be an option? Talk to your accountant - there may be options you may not be aware of.

Tax tip: 'Normal' businesses will engage the finance director before major financial decisions are made. Most property investors can't afford to pay for a finance director - so use your accountant to act as your 'part-time finance director' - that's partly what you are paying for! PIN