# HOW TO OPERATE A PROPERTY MANAGEMENT COMPANY ('PMC') COMPLIANTLY

By specialist property accountant **Stephen Fay FCA**

**Using a property management company ('PMC') to manage their personally-owned property portfolio can offer some landlords a useful tax advantage. Operating the company compliantly is essential however, to prevent being able to challenge the validity of the company**

## How using a property management company can save tax

If a Higher Rate taxpayer private landlord pays management fees to a PMC, the individual would save income tax at 40%, whereas the company would pay tax at 19%, meaning that there is a 21% tax saving to be made, potentially.

Other benefits include the option to make larger pension contributions through the company than the landlord could make personally, and have the company pay for property training and similar expenses that are often not allowable for private landlords (for example, see HMRC BIM3566 – these rules do not apply to companies).

The 'Section 24' mortgage interest relief restriction has increased the taxable profit of the private landlord who uses mortgages, meaning that many private landlords are now Higher Rate (40%) taxpayers, whereas before Section 24 they would have been Basic Rate (20%) taxpayers.

Property management is of course a legitimate landlord expense, and so reduces rental profits accordingly, effectively saving the difference between 40% Higher Rate income tax and the lower corporation tax rate.

**EXAMPLE**

***Bob makes rental profits of £50,000, after paying mortgage interest of £30,000. With Section 24 in force, Bob will pay income tax of £13,540.***

***Jill makes the same rental profits as Bob, but Jill operates a PMC, which makes a charge of £30,000 to Jill to cover all of its services. Jill's income tax bill is £1,540, and the PMC has a corporation tax bill of £ £5,700: meaning an overall saving of £6,300 (less PMC costs) as a result of Jill avoiding the Section 24 mortgage interest relief restriction.***


## Other reasons to operate a property management company

The Limited Company is the most common business structure in the UK, however most mortgaged landlords did not build their portfolio in a company because personal BTL mortgage rates, fees and choice is better.

Landlords run a 'rental business' (the HMRC term) as just that – a business – which requires significant time and effort to manage, has cashflow challenges, creates personal business risk, and potentially high rewards.

However, a private landlord may legitimately wish to operate a PMC alongside their personally-owned portfolio for any number of reasons, such as:

1. To create a corporate, more professional 'front' to tenants and other stakeholders
2. To gain access to property-related services and discounts that only companies can access
3. To recognise that a rental business has both an investment (I) side and a management (M) side – which may be run by different people e.g. husband / wife
4. To create a separate business model (property management services) which could be sold, or expanded, in the future



## Staying on the right side of HMRC – details matter!

A PMC needs to be operated compliantly, to avoid the risk of HMRC successfully challenging its validity.

HMRC have the 'General Anti-Abuse Rule (GAAR) as a catch-all to challenge any arrangement that they deem to be mostly about tax-planning, rather than having a genuine commercial basis. So, the 'careful' landlord operating a PMC would ensure that:

1. **Payments for services are actually made during the year:** HMRC are often focussed on whether payments are actually made, and when, and so it is prudent to ensure that payments are actually made i.e. the PMC is not a sham year-end paper exercise. Payment frequency can be monthly or quarterly ideally, although a year-end accrual for extra fees is acceptable
2. **The company has the 'look and feel' of a normal commercial entity:** a website, dedicated phone number, letterheads, business email addresses, corporate memberships (e.g. NRLA), all serve to make the PMC look and feel like a genuine business, operated in the way that any letting agent / property management company would be. Not essential, but certainly helps!
3. **Fees and charges are at commercial rates:** generally, fees and charges should be made in the normal range at which such services are offered by local similar businesses e.g. it would be strange – and therefore open to HMRC challenge – for a letting agent to charge 50% of the gross rent to cover its services, no matter how good that service was, since this is clearly well above what a reasonable rate might be
4. **The company has multiple customers:** while it is often the case that any business may be reliant on one or a small number of initial customers initially, over time one would expect that the number of customers a business might serve would increase. This helps to defend against HMRC attack that the PMC is in place solely to benefit the private landlord. So, managing at least some other landlords properties would be helpful if at all possible.

### What kind of services could a PMC charge for, and at what rates?

Most PMCs charge a management fee as a % of the gross rent – this will differ according to the local market, and of course depends on the quality of service and number of services that the PMC may make e.g. budget no-frills vs all-in option. Charges may be made for a wide variety of services:

**General management: 10-25% of gross rent**
**Tenant find: around 0.5-1.0 months rent**
**Inventory: £200-£500 each**
**Review of legal compliance:**
**Tenancy deposits / gas safety / EPC / HMO licenses other as part of on-boarding service: £200-£500/property**
**Provision of bespoke AST and similar documentation: £200-£500/landlord**
**Managing S8 & S21 evictions, court attendance, etc: £300-£800/case**
**Liaison with utilities, councils, EHO: £75/hour**
**Refurb management / sourcing tradesmen and materials: £500-£5,000 *(depending on complexity and costs involved)***

## Day to day operation of a PMC

Rents, mortgages and repairs (etc) are managed through the private landlord's bank account (i.e. non-company account). Each month, or quarter, the private landlord pay the PMC for the management and other services provided, via a simple online bank transfer. A simple invoice is raised, and this is income to the PMC, and a cost to the private landlord.

Note that tenants continue to pay their rent directly to the private landlord, and so there is no disruption to rental income, or any requirements to ask tenants to change their payment arrangements (which can be a significant extra task).

## PMC and corporate BTL lenders

Ideally, for private landlords wishing to buy residential property in a company, they would be able to use their PMC to do so. However, some lenders will only lend to an SPV company (Special Purpose Vehicle) i.e. a company that ONLY rents property and has no other income. Advice should be sought from specific lenders / brokers to check that a lender is happy to lend to a PMC (otherwise an entirely separate SPV company may be required for company ownership of rental property).

## A note on VAT …

VAT is only chargeable on PMC fees and charges once total PMC income (excluding rent, which is the landlord's income) exceeds £85,000 in a 12-month period. This is typically well below what an average small PMC has as income and so such small PMCs have no need to register for VAT.

## Summary ….

Compliant operation of a property management company is essential to ensure that HMRC isn't able to challenge the validity of the company. Commercial reasons should be the main reason that a PMC is operated, with any tax benefits being a secondary consideration … although a PMC can offer significant tax advantages to the private landlord.

Get in touch

www.fyldetaxaccountants.co.uk