HOW IS RENTAL INCOME TAXED?

1. What is rental income?

Rental income is the sum of money collected by property-owners for the use of a specific area, such as land and buildings, including income from renting an apartment, house or any part of it for that matter , like a room or even a parking space.

2. UK property business

When you start renting a property you must report your income to HM Revenue and Customs (HMRC).
Profit obtained from renting a property is part of your total taxable income and as such is subject to income tax. If you are a basic rate tax payer, you will have to pay tax at **20%** , if you are a higher rate tax payer you pay **40%**, and if you are an additional rate tax payer you will be taxed at **45%**.

Where gross rental income is less than **£10,000** and profit (income less expenditure) is less than **£2,500** HMRC can be contacted directly and, provided there is no other reason for you to complete a self-assessment tax return, profits can be reported over the phone or via an email. Otherwise your property income and expenditure should be reported on your tax return.

To arrive at a taxable property income figure, the accruals basis should be applied.

The accrual principle involves taking rents chargeable rather than rents received. Chargeable means the rents that relate to a specific time frame, which is not necessarily the same as the cash collected to date. Property income calculations are always prepared in accordance with the tax year dates – i.e. from 6 April to 5 April.

Rents chargeable less all of the allowable expenses gives the taxable property income profit or loss for the year. Allowable expenses include, but are not limited to:

- Repairs
- Insurance premiums
- Utilities
- Cleaning
- Maintenance
- Ground rent
- Advertising

Property expenses are tax allowable only if they are incurred “wholly and exclusively” for the business purposes. The expenses in relation to rental property are deemed to be of a revenue rather than capital nature. Many property purchases are supported by way of mortgages. Relief is available for the mortgage interest paid. From 06.04.2017 only part of the loan interest paid is allowable as a deduction from income when calculating taxable profit. The balance of interest is entitled to tax relief at the basic (20%) tax rate and available relief is granted as a reduction in arriving at the individuals tax liability.

Capital allowances are not available in respect of furnishings in a let residential property.
However, a claim to be reimbursed for the exchange of domestic property items can be made. If the substitute item is not a like for like replacement the deduction will be limited to the cost of replacement on a like for like basis.

3. Rent-a-room relief

ROOMS

Different rules apply to landlord that are renting a room to tenants in their own home. There is a special relief called rent-a-room relief which, in the current tax year, is **£7,500**. If the total gross rent is no more than **£7,500** then rent-a-room relief applies automatically and rental income is exempt from tax.

Since 6 April 2017, a property allowance of **£1,000** has been made available to individuals who receive property income. However it is not possible to use both rent a room relief and the property allowance against the same property income.

4. Furnished holiday lettings

For tax reasons property rental income is usually treated as investment income rather than trading income.

Furnished holiday Lets (FHL) are an exception to this rule. If the property meets the requirements to become an FHL it qualifies for some of the tax benefits usually reserved for trades. Profits from FHL's are included in qualifying earnings when calculating the pension annual allowance. In addition capital allowances are available in relation to expenditure incurred on FHL's.

5. What qualifies as a furnished holiday letting

The property will be treated as an FHL if all of the following conditions are met:

- The property is furnished.
- The property is situated in the UK or any other state in the European Economic Area (EEA).
- The property is made available for commercial letting as holiday accommodation to the public for at least 210 days in the relevant 12 month period.
- Out of those 210 days, the property is actually let out for 105 days or more as holiday accommodation – this is called the ‘letting’ condition.

6. Overseas property business

If the property income is derived from overseas property all profits are taxed as foreign income.

To calculate profits from overseas rental property we apply the same principles as we would for a UK property business.

7. Property Rental Losses

If you make a "loss" from renting a property - it means that your allowable expenses are greater than your rental income.

Essentially all property income in the UK is treated as one "rental business", therefore losses from one property are automatically used against income from another. Otherwise, the loss is generally carried over to the next tax year and deducted from profit for that year.

Losses arising from renting a property abroad cannot, for income tax purposes, be combined with profits from UK rental income carried out by the same person.

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