Tax on residential property

A guide for clients

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How has devolution affected what tax you pay?

First-time buyers in England, Northern Ireland – and for a short time in Wales – were the biggest winners in the most recent shake-up to affect property taxes in Autumn Budget 2017.

Philip Hammond's headline measure was to abolish stamp duty for first-time buyers on homes worth up to £300,000, and the chancellor didn't stop there.

He also introduced a reduced rate of 5% on the portion worth from £300,000 to £500,000, providing a welcome boost for many aspiring homeowners in London where the average residential property sold for £556,146 in 2017.

But while the chancellor received plaudits for a move that helped 121,500 people take their first steps on the property ladder up until 30 June 2018, existing homeowners still have to pay property taxes – most notably in the form of stamp duty and capital gains tax (CGT) – while devolution means that where you live in the UK also affects the property tax you pay.

Stamp duty

Abolishing stamp duty for first-time buyers was the latest in a long line of changes to Britain's main property tax, but it no longer applies in Scotland or Wales.

Scotland has been setting its own land and buildings transaction tax (LBTT) since April 2015 and Wales introduced its land transaction tax (LTT) for all homebuyers on 1 April 2018.

First-time buyers in Wales were able to benefit from the stamp duty holiday on homes worth up to £300,000 until 31 March 2018, after which the new £180,000 threshold applied on all homes.

Those in Scotland were not as fortunate, with Holyrood taking until June 2018 to add an extra £30,000 to its nil-rate threshold of £145,000 for first-time buyers.

Regardless of where you are in the UK, property taxes are charged on the portion of a property price that falls within each band – but how does it work and what can you expect to pay in 2018/19?

All of the examples and rates given below are based on the assumption that the second home stamp duty surcharge of 3% would not apply.

England & Northern Ireland

Residential property price	Rate
Up to £125,000	Nil
£125,001 to £250,000	2%
£250,001 to £925,000	5%
£925,001 to £1.5 million	10%
Above £1.5 million	12%

How does it work?

You buy a two-bedroom house in the up-and-coming Redfield area of Bristol for £275,000. The first £125,000 is free from stamp duty, while the next portion of £125,000 is taxed at 2% (£2,500). As 5% (£1,250) is liable on the remaining £25,000, your total stamp duty bill will be £3,750.

In comparison, no stamp duty would be due in 2018/19 if a first-time buyer was buying this house due to the property price (£275,000) falling below the £300,000 threshold.

Scotland

In Scotland, LBTT is in place at the following rates:

Residential property price	Rate
Up to £145,000	Nil
£145,001 to £250,000	2%
£250,001 to £325,000	5%
£325,001 to £750,000	10%
Above £750,000	12%

How does it work?

A two-bedroom apartment in the west end of Aberdeen costs £220,000, with the first £145,000 tax-free and the second portion of £75,000 liable for LBTT at 2%. The total tax due would be £1,500.

For first-time buyers in Scotland, the tax-free threshold of £145,000 rises to £175,000, so they would pay £900 in LBTT (£175,000 tax-free, 2% of £45,000 = £900).

Wales

LTT replaced stamp duty in Wales on 1 April 2018, introducing the following rates:

Residential property price	Rate
Up to £180,000	Nil
£180,001 to £250,000	3.5%
£250,001 to £400,000	5%
£400,001 to £750,000	7.5%
£750,001 to £1.5 million	10%
Above 1.5 million	12%

How does it work?

For example, you buy a three-bedroom house worth £260,000 in the leafy Cardiff suburb of Thornhill.

The first £180,000 is tax-free, the portion up to £250,000 is taxed at 3.5% (£2,450) and the remaining £10,000 is taxed at 5% (£500) – bringing your total LTT bill to £2,950.

First-time buyers are not treated any differently to other homeowners as the assumption is most first homes in Wales cost less than £180,000 and as such, should be tax-free.

Capital gains tax

CGT usually applies in relation to property taxation only if you are selling something other than your main residence, for example if you have a holiday home or you are a landlord with a property portfolio.

The main home is usually free from CGT through principal private residence relief, which allows homeowners to keep the entire proceeds from a house sale.

However, for other homes you may own, a CGT liability will arise on any gain worth more than the £11,700 annual exemption in 2018/19.

How much you pay depends on how much you earn in the tax year and which income tax band that places you in.

For instance, basic-rate taxpayers earning up to £46,350 pay 18% and this rate rises to 28% for taxpayers above this level of earnings or gains.

In Scotland, the CGT rates are the same as the rates and thresholds elsewhere in the UK, despite five income tax bands being in place for 2018/19.

Income tax

Residential landlords should be aware that income from property has the potential to nudge you into a higher income tax band, especially in light of recent changes to mortgage interest relief.

Landlords used to be able to offset their entire mortgage interest against rental profits before April 2017, at which point the government began phasing this out and replacing it with a phased in tax credit at the basic rate of tax of 20%.

In 2017/18, it was possible to deduct 75% of your mortgage interest. This went down to 50% in 2018/19 and will hit 25% in 2019/20, before being eliminated altogether by 2020/21.

For instance, let's imagine Katherine earns £38,000 a year as an employee and is a basic rate taxpayer. She has a buy-to-let property, which she rents out for £11,400 in 2017/18.

She paid £3,240 in mortgage interest last year, but can only deduct 75% (£2,430) of this from her profits.

The revised £8,970 of her buy-to-let profits pushes her into the higher rate band and makes her liable to pay 40% in income tax.

By 2020/21, Katherine – and hundreds of thousands like her – will pay more income tax on her rental profits.

There are ways she could mitigate her position, such renting a property through a limited company where loan interest remains a deductible expense against rental income.

Holding on to buy-to-let properties is becoming less attractive due to the increased tax liabilities, and in some cases has made keeping these properties unaffordable.

To discuss property tax please contact Sue Stephens or John Elliot.

FOR GENERAL INFORMATION ONLY

Please note that this guide is not intended to give specific technical advice and it should not be construed as doing so. It is designed to alert clients to some of the issues. It is not intended to give exhaustive coverage of the topic.

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