

Do you have to declare property rental income?

You've let out a house for years, but your total income has always been less than your tax allowance so you haven't declared it to HMRC. Will you need to reconsider in view of the impending major changes to the tax rules for landlords?

Non-declaration

One of our clients owns a property jointly with his wife, which they've let to the same tenant for many years. Our client is a higher rate taxpayer, while his wife's income almost entirely consists of the rent. The rent has been £21,000 per year for a while, which after expenses produces taxable income of around £14,000. Our client has always declared half of this on his tax return, but his wife hasn't reported anything to HMRC.

Is a tax return required?

Because of the changes in the tax system affecting landlords (see below) our client thinks his wife might need to start reporting the income. He's worried that HMRC might ask why she hasn't done so before, which might result in penalties for failing to declare income.

Tip. The good news is that our client can rest easy. Contrary to popular belief, you're only required to complete a tax return if HMRC asks you to do so. However, you do have an obligation to notify HMRC if you believe you owe tax. Our client's wife's income was well below her personal tax allowance so there was no chance of that.

New rules for finance payments

Our client's other worry was that the new rules from 6 April 2017, which reduce the deduction that can be claimed for interest and other finance expenses, will increase the taxable income. Would this be enough to take his wife's income to the point where tax will be payable?

Complex calculations

The new rules for working out the reduced tax deduction are some of the trickiest we've ever seen for such a simple adjustment. However, in a situation where your total income is currently below your personal allowance you won't be affected by the reduction of tax relief for 2017/18 unless the interest etc. you pay runs to well in excess of £100,000 (assuming of course that your income doesn't rise dramatically). Therefore, our client's wife needn't be concerned.

Tip. As our client is a higher rate taxpayer he will be affected by the reduction in tax relief in April 2017. He could therefore save some tax by diverting some or all of his rental income to his wife.

MTD spells trouble

One tricky issue on the horizon for both our client and his wife is “Making Tax Digital”, (MTD), which is scheduled to take effect in April 2018. This will require landlords who receive rent of £10,000 or more to report their rental income and expenses online to HMRC quarterly, even if they aren’t liable to pay tax on it. Consultation about MTD is ongoing. As you would imagine there’s a great deal of opposition, particularly to the timetable, which in most experts’ view is unrealistic. The best landlords can do is to keep an eye on how MTD progresses. We’ll keep you up to date with any developments.

Summary

A reduction in tax relief for interest etc. payable applies from April 2017, but as long as your income is within the basic rate band you won’t be affected. However, under current proposals landlords who receive rents of £10,000 or more per year will be required to send quarterly reports to HMRC from April 2018.