Guide to

Owning a Holiday Let in a Limited Company and other Business Structures

Produced by Zeal Tax.

February 2025

ZEAL

Introduction

In March 2024, the government announced new regulations that will result in Furnished Holiday Let (FHL) tax changes, effective from 6th April 2025 (1st April 2025 for limited companies). The new legislation means that holiday let owners holding properties in their personal name will no longer be able to offset mortgage interest against profits.

Due to a compensating tax credit, this particular change will not affect the tax on most basic rate taxpayers, although owners will see taxable incomes rise by the value of their annual finance costs. Limited companies are not affected by the changes to the finance costs restrictions.

As a result, there is a growing trend towards buying or owning holiday lets via a limited company, driven by the appeal of tax advantages and reduced personal liability for holiday let owners.

One popular approach is transferring FHL properties from personal names into a limited company. This option offers benefits such as lower corporation tax rates and the ability to fully deduct mortgage interest.

This guide explores the key benefits of owning a holiday let in a limited company compared to owning as an individual. It also explores alternative business structures.

What is a Limited Company?

A limited company is a distinct legal entity that separates personal finances from business assets, offering a layer of protection for individuals involved. Owned by shareholders or guarantors, companies are able to reinvest profits back into the business, enabling growth and further investment while keeping assets securely within the company structure.

When choosing between buying and operating a FHL in personal ownership or limited company ownership, this separation of liability is a key factor that makes forming a limited company an attractive option, particularly as your business expands and key tasks are delegated.

Other benefits include the professional image of your business and to have a corporate interface between you and your clients. The ability to store profits in the company may result in greater liquidity for reinvestment in your business.

Tax Benefits of Owning a Holiday Let in a Limited Company

Potential for Lower Annual Tax Charges

A limited company provides the ability to tax profits at lower rates than personal tax rates (19% to 25% versus 20% to 45%). However, should you choose to draw the profits from the company then you will pay personal tax on the drawings (subject to dividend tax rates).

Whether it is more tax efficient to own and operate in a limited company, depends upon factors including the extent of the drawings/dividends taken, the finance costs and your taxable income from other sources. It is generally considered that the flexibility to manage drawings results in a more tax efficient outcome over time.

An important consideration is that if you initially fund your property purchase in a company structure by investing personal money into the business, you can create a loan owed to you by the company (known as a directors loan), and can draw this loan, tax-free, from the company reserves, as an alternative to taking drawings that are subject to personal tax.

This structure can be particularly beneficial for those whose total annual income exceeds the basic rate tax threshold.

By storing profits within the company, you can benefit from lower tax bills and accumulate reserves over time, which can be reinvested in new assets.

Setting up a limited company for a holiday let offers several tax advantages:

- Potential for Lower Annual Tax Charges.
- Pension Contributions.
- Inheritance Tax Planning.

Furthermore, a limited company can introduce other shareholders, including adult family members, who could take drawings from the company, either as salary or dividends, making optimum use of their personal allowance and basic rate tax bands.

For rental property owners, including FHL owners from April 2025, taxable income differs from true profits where finance costs on rental properties are involved. The taxable income is the true profit plus the finance costs.

The higher rate tax threshold is currently £50,270. Earnings above this are taxed at 40%. The highest earner in a marital partnership pays additional tax from a taxable income of £60k, where child benefit is received.

From £100,000 to £125,140, the tax rate is 90% (referencing loss of personal allowance). From £125,140, the tax rate is 45%. Student loan repayments are calculated based upon the taxable income.

Pension Contributions

Along with the removal of the tax benefits of FHL, the income from an FHL will no longer be considered "qualifying income" for pension contributions. However, a limited company has more flexibility to organise pension contributions via employer contributions.

Inheritance Tax Planning

Limited companies have more flexible options for inheritance tax planning compared to personally owned FHLs.

For example, organising the company as a Family Investment Company (FIC) can shield the growth in value of the properties from the value of your shareholding. Shares in the limited company can be passed on to heirs. The IHT paid on the shares would not be reflective of the increased value of the company, due to capital growth of its properties.

The limited company structure also provides asset protection by separating personal wealth from the property business, reducing exposure to legal claims or business debts.

Furthermore, the company structure allows for more flexibility in managing profits, whether reinvesting them back into the business or taking them out as dividends or salary.

Potential Financial Detriments to Limited Company Ownership

It should be kept in mind that the administration and accounting costs of a limited company may be higher. Mortgages specific for limited companies may also be slightly more expensive than equivalent mortgages on properties held in personal name.

Corporation tax rates range from 19% to 25%, depending on the number of companies owned and the profits of the companies. Establishing a new limited company can therefore impact on the tax paid by another owned limited company. However, this is not always the case, if the companies are sufficiently independent of each other.

Transferring a FHL to a Limited Company

Transferring a FHL into a limited company can be a strategic decision for property investors aiming to benefit from tax advantages and enhanced asset protection.

When making this transfer, it's important to consider potential capital gains tax (CGT) and SDLT/LBT/LBTT liabilities, as the transfer may trigger CGT if the property has appreciated in value.

However, reliefs like incorporation relief and SDLT/LBT/LBTT relief might be available to reduce the tax burden. Additionally, if there is an existing mortgage, you may need to apply for a new one under the company's name, and mortgage terms could differ from those on personal loans.

While transferring the property involves legal and financial processes, such incorporation of the company, the long-term benefits of tax efficiency and asset protection can make it a worthwhile move.

Properties sold following transfer to a limited company will benefit from a lower capital gain, because the capital gain prior to transfer is excluded from the calculation, which usually results in significant tax savings and a major perk of incorporation.

Holiday Let Mortgages for Limited Companies

Under the current FHL regime, mortgage interest is fully deductible. However, this rule will no longer apply from April 2025. Despite these changes, limited companies will still be able to deduct holiday let mortgage interest against profits earned.

Legal and Tax Requirements

When setting up a limited company for a holiday let, there are several legal and tax requirements to consider.

First, you must register the company with Companies House, providing details such as the company name, structure, and directors. The company must also have a registered office address and comply with all legal obligations, including submitting annual financial statements and tax returns.

Additionally, if you are transferring an existing property to the company, this will be treated as a sale for tax purposes, potentially triggering capital gains tax (CGT) and SDLT/LBT/LBTT. The company will also need to maintain proper records of income, expenses, and any deductions, such as mortgage interest or maintenance costs.

It's essential to work with a tax specialist to ensure proper tax planning, as the structure offers opportunities for reinvestment, dividend payments, and potentially more efficient management of profits.

For more information on tax planning, Zeal offer free specialist tax advice tailored to your individual needs. Our team will be able to determine whether transitioning to limited companies or other business structures would be appropriate to your circumstances.

Alternative Structures

General (Ordinary) Partnership

Where all the profits of the business provide for household living costs without surplus, a limited company can be less tax efficient than personal ownership.

In particular, this would be the case where finance costs are low or there is the opportunity to share the income with a spouse or other adult family members. Where this is the case, a partnership may be a more tax efficient structure to personal or joint ownership.

A partnership is defined by S.1 of the 1890 Partnership Act, S15 of the Finance Act 2003, SDLTM33110 and PIM1030 as *"The relationship which subsists between two or more persons carrying on business in common with a view to profit".*

It is not necessary to jointly own the property(ies) to establish a registered general partnership. But it would be necessary for the operation to be a "business" (simplistically defined by requiring more than an average of 20 hours a week to operate) as opposed to an "investment".

FHL is currently classed as a business, but from 6th April 2025, it will need to meet this business test to be classed as such. However, the test will include other non FHL rental properties such as long term lets.

Where family members work together on the business, a general partnership can be registered. The partnership would have its own bank account, a partnership agreement and send and receive invoices in the partnership name. The partnership would also compile accounts on an annual basis.

The profits of the partnership can be shared amongst the partners on a non-equal basis, subject to limitations. Whilst all the profits must be declared across the tax returns of the partners in the tax year they are earned, and the finance cost restrictions still apply, the sharing of income can result in a very tax efficient outcome.

Where this results in taxable incomes below the higher rate threshold, the punitive effects of the finance cost restrictions will not apply. In smaller businesses, this is often more tax efficient and less costly than a limited company structure.

Transferring a personally held business to a partnership is straightforward and does not involve any transitional taxes, such as CGT or SDLT/LBT/LBTT. There is no effect on personally held mortgages.

Limited Liability Partnership

The tax treatment of a LLP is very similar to a general partnership as described previously. However, unlike limited companies, partnerships do not benefit from the ring-fenced liability status, therefore personal assets remain exposed to unplanned liabilities. This can be overcome by establishing a Limited Liability Partnership (LLP).

A LLP operates in a similar manner to a partnership. The main difference is that it is a separate legal entity (similar to a limited company). Therefore, to operate a LLP, the property will need to be transferred to the LLP. It is not necessary to transfer the legal title as the transfer of beneficial ownership can be affected by a legally drafted members agreement.

Some mortgage loans prohibit the transfer of beneficial interest, so this will need to be checked. If the property is to be remortgaged at any time following the transfer of beneficial interest, then the mortgage loan would be to the LLP, and it would be necessary that the legal title is conveyed to the LLP.

Income Sharing as Joint Owners

Married couples can currently share the income of a jointly owned FHL property business at unequal proportions. This can result in tax efficiencies, particularly where one partner has income from other sources.

From 6th April 2025 this will change. A jointly owned property will be assumed to be owned equally, and the income must be split equally across the tax returns of the joint owners. Where the joint ownership is as "tenants in common", the couple can elect to transfer part ownership to a chosen proportion.

A Declaration of Trust will officiate the transfer of beneficial ownership. This can then be registered with HMRC using form 17. Income must then be apportioned based upon the elected proportions. It would be costly and impractical to adjust the ownership each tax year.

If the joint ownership is not "tenants in common", then the legal title will need to be changed to "tenants in common" before the ownership can be adjusted. This may impact on mortgages. Whilst there is no CGT triggered on such transfers, there could be a trigger of SDLT/LBT/LBTT if there is a mortgage on the property.

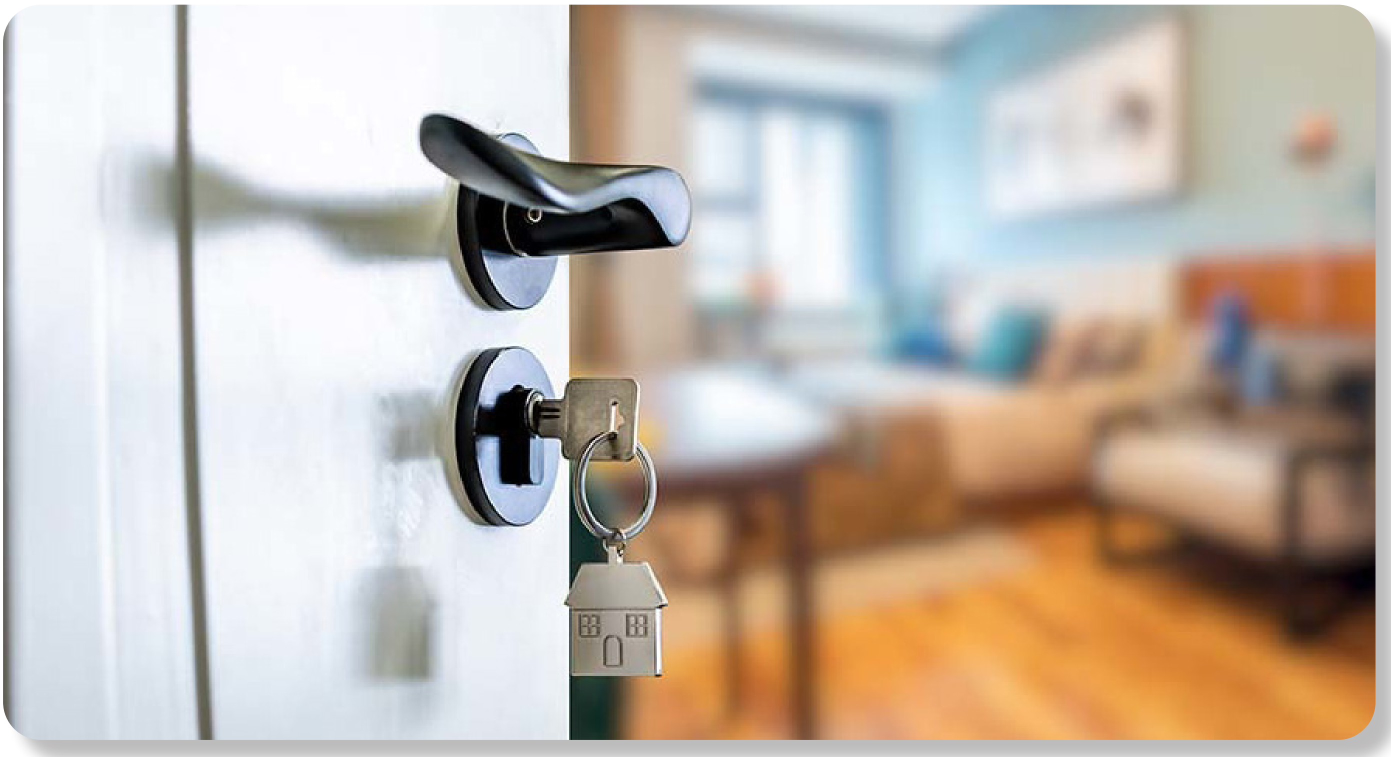
Professional legal advice should be taken if you are considering a Declaration of Trust.

Working with a Holiday Let Management Company

It is possible to establish a management company to operate your personally owned FHL properties. Where the management company has common ownership to the properties, it is important that transactions reflect commercial market terms.

For example, the management company could charge 20% of the gross rental income to the owner for its services. The management company would pay corporation tax, but the profits do not need to be drawn. The management fee would reduce the personal tax of the owners.

The tax benefits would need to be balanced against the additional costs of administering such arrangements but could be beneficial in certain circumstances.



Partnering with a Holiday Let Agency

Partnering with a holiday let agency offers long-term planning advantages, making it a strategic choice for many property investors.

Not only does it reduce the work burden and the fast-developing marketing knowledge requirements of the owners, but it can also result in greater income due to increased occupancy.

Contact our friendly team of property experts today for guidance on holiday letting as a limited company.

What's the best structure for you?

There is not a preferred structure that suits every situation. So many factors come into play when determining the best structure for your situation. This includes many circumstances not referred to in this guide.

By consulting with a Zeal Business Structuring Specialist, your personal family and business circumstances will be considered holistically, together with your future aspirations and succession planning requirements.

Comparative calculations will determine the tax efficiencies of numerous options, which will result in the optimum personalised plan for the coming years, ensuring your tax bills now and in the future are as low as legally possible.

Where this is detailed in a report, such a document can be used for years to come, by yourself, your family, accountant, lawyers, pension advisors, IFAs, VAT advisors and mortgage advisors.

Many clients of this service report tens of thousands of pounds of savings from such plans. Those that adopt the succession planning are likely to make millions of pounds of savings through the generations.

For more information, contact the team at Zeal

01633 742243 | hostplanet@gozeal.co.uk

Additional Consideration – Have You Claimed Capital Allowances?

Whether you choose to own or operate your holiday let in a Limited Company or not, another consideration to help you become as tax efficient as possible ahead of the upcoming FHL tax changes, is ensuring you have claimed all the capital allowances available to you.

When the FHL tax regime is abolished from April 2025, one of the major changes will see the removal of capital allowances tax relief for holiday let owners.

Whilst you may have heard of capital allowances already, you may not realise that there's an extra level of capital allowances that can be claimed on part of the costs you incurred to purchase, build, convert or refurbish your property.

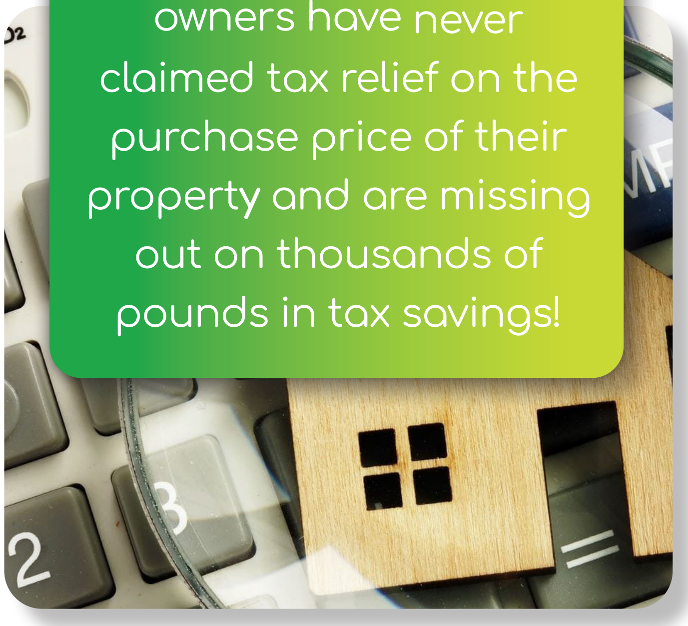
This tax relief can be claimed on embedded 'fixtures' in the fabric of the property, like heating and electrical systems, kitchens, bathrooms and more.

Even if you incurred the expenditure years ago, you could still be able to make a claim now, **but time is of the essence!**

Find everything you need to know in Zeal's free capital allowances guide for FHL owners.

DOWNLOAD

80% of holiday let owners have never claimed tax relief on the purchase price of their property and are missing out on thousands of pounds in tax savings!



A claim on these fixtures can generate tens of thousands of pounds in tax savings and cash repayments. However, if you don't claim soon, your entitlement will be lost forever!

The reason most owners have not yet claimed is because it is **not a service a general accountant can typically provide.** You need quantity surveyors and capital allowances specialists like Zeal, to determine qualifying expenditure.

Even though an accountant can claim capital allowances, it is usually restricted to items like furniture and equipment that you purchase.

Any tax benefit secured before the deadline can also continue to be claimed even after the rules change, and can also be offset against tax due on ANY property income, not just FHLs!

If you have not yet claimed these capital allowances, you could be sitting on thousands of pounds which Zeal can unlock for you.

It'll cost nothing to find out if you qualify – only a few minutes of your time.

Zeal are Chartered Tax Advisors & Surveyors who specialise in holiday let taxes and capital allowances.

With time running out to secure the tax savings available to you, it is vital to review your capital allowances and ensure you have not missed a claim, whilst there is still time.

CASE STUDY: *Beachmount Holiday Apartments*

Purchased in 2002 for £352,000

Capital Allowances Identified: **£92,000**

Tax Savings Unlocked: **£26,000**

Owner Cash Rebate (after fee) of: **£4,500**

Key Information:

- Not a service an accountant provides.
- It's not too late to claim on historical expenditure.
- Allowances identified before the deadline can continue to be claimed after the rules change.
- Any benefit secured can also be offset against tax from ANY property income post April 2025.
- No impact on future Capital Gains Tax if you were to sell the property.
- There could be an average of £15,000 in tax savings available to you.
- You could also be due a cash rebate from HMRC for tax you have unknowingly overpaid.
- If you don't claim soon, you will lose the tax relief forever!

THE CLOCK IS TICKING . . . SO ACT NOW!

Zeal are offering **a free capital allowances review** to ensure you benefit from any unclaimed tax savings, **before it's too late.**

SCHEDULE YOUR REVIEW

Disclaimer from Zeal Tax

This content was written by Matt Jeffery of Zeal Tax, a leading holiday let tax specialist firm in the UK, as an educational piece to help short-term let and furnished holiday let owners understand their tax responsibility.

1. *The information provided is of a general nature and guidance only, and does NOT constitute accountancy, tax, financial or other professional advice. It is not a substitute for specific advice on your own circumstances. You are recommended to obtain specific advice from a professional before you take any action or refrain from action.*

2. *Whilst we endeavor to use reasonable efforts to furnish accurate, complete, reliable, error free and up-to-date information, Zeal Tax make no representations or warranties with respect to the accuracy or completeness of the contents of this publication, and cannot accept any responsibility for any liability, loss or risk, personal or otherwise, which may arise, directly or indirectly, from reliance on information contained in this publication.*

3. *Please note that tax legislation, the law and practices of UK government and regulatory authorities (e.g. HM Revenue and Customs) are constantly changing. Furthermore, your personal circumstances may vary from the general information contained in document, meaning information may not be applicable or suitable for your situation. We recommend that for accountancy, tax, financial or other professional advice, you consult a suitably qualified accountant, tax specialist, independent financial adviser, or other professional adviser who will be able to provide specific advice based on your personal circumstances.*

4. *This guide covers UK taxation only and any references to 'tax' or 'taxation', unless the contrary is expressly stated, refer to UK taxation only. Please note that references to the 'UK' do not include the Channel Islands or the Isle of Man. Foreign tax implications are beyond the scope of this document.*

ZEAL

Contact Zeal Tax

www.gozeal.co.uk | 01633 742243 | hostplanet@gozeal.co.uk