

Reduce your rental profits by maximising expense and interest claims

For the Taxman to allow expenditure against rental income, it has to obey the following rules:

1. **Wholly and exclusively** – you pay a cleaner £60 per week for ten hours work. The cleaner spends four hours a week at your home and six hours cleaning your investment properties. Therefore you can claim 6/10ths against your rental income.
2. **Paid by you** – if it is your tenant's responsibility to pay the council tax and TV licence then you cannot deduct these expenses against any rental income you receive.
3. **Not capital** (see additional fact sheet) – although the capital costs cannot be deducted against your rental income they can be deducted from your sale proceeds when you sell the property.

One area that is commonly misunderstood is that in relation to interest and finance costs, a summary of the rules with examples is shown below

Allowable Expenditure - Interest Charges

Buying a property to rent usually involves some level of borrowing; you can offset the **interest paid** on these loans against your rental income. The general rule is you can claim interest on any loans that are incurred for the purposes of property investment. **Whether the loan interest is an allowable deduction does not depend on which property the loan is secured on, but rather on what the loan funds are used for.**

TIP – As a property investor, it is important for you to plan your mortgage strategy. As you can't get tax relief on a loan to buy your own property, aim to borrow as much as possible against your investment properties and use the additional funds generated to pay off the mortgage on your own property. That way you will get tax relief on your borrowings.

NB. This fact sheet is designed to show some examples of mortgage interest that can be claimed. It is not intended to cover all mortgages and does not cover interest on personal loans or finance agreements.

Interest on a mortgage on the investment property.

If you take out a mortgage to buy the property you can offset the interest element of the mortgage against the rental income.

Interest on a mortgage on your own home.

You cannot deduct the interest on a loan taken out to buy your own property. However if you later extend your mortgage and use the funds to purchase another property then the interest on the extended portion can be offset against the rental income.

It is unlikely your mortgage lender will give you a separate interest statement so you will need to work out the interest on the additional loan. This is done by apportioning the loan.

Example

You increased your original mortgage by £40,000 to £80,000 to help buy an investment property and the total interest charged for the year was £4,000. The amount of interest that you can claim against your rental income is £3,000 ($\frac{£40,000}{£80,000} \times £6,000$).

Interest on a re-mortgage

Over the past few years your property has risen significantly in value. Rather than sell the property you could then realise the “profit” by re-mortgaging and getting some cash out of the investment.

If you re-mortgage for a greater amount then you can only offset the interest on the additional amount as long as it doesn't exceed the value of the property when it was first let.

Example

Original Purchase Value £160,000

Mortgage required £128,000 (monthly interest £550)

The property has now increased to £200,000

Re-mortgage to £160,000 (additional £32,000) (monthly interest £680)

If you use the additional amount to modernise the kitchen and bathroom in the rental property or your own home, then the interest can be offset against rental income.

Example

Original Purchase Value £160,000

Mortgage required £128,000 (monthly interest £550)

The property has now increased to £200,000

Re-mortgage to £170,000 (additional £42,000 but now re-mortgaged above the original purchase value of £160,000)

If you use the additional amount to modernise the kitchen and bathroom in the rental property then the interest can be offset .If you use the additional funds for your own home, then you can only offset the proportion of interest that relates to the loan on the initial value of the property