

Dealing With Non-Resident Landlords In 2018 – Income tax

(Lecture B1066 – 9.02 minutes)

These notes deal with the current tax regime where non-resident individuals own property in the UK which is being let out. We shall call these people “Non-Resident Landlords” (NRLs).

NRLs can be individuals, Trustees or companies. These notes will concentrate on the rules as they apply for individuals.

A NRL need not be someone who is non-UK resident under the Statutory Residence Test. The NRL rules apply where an individual’s “usual place of abode” is outside the UK which means that the individual lives abroad for at least 6 months of the year. It is very possible for someone spending less than 6 months of the year in the UK to be UK resident for tax purposes; however the NRL Scheme would still apply.

Income Tax

NRLs pay UK income tax on profits from the letting of land and buildings in the UK.

Profits from a UK property business are determined under normal commercial business principles being rents receivable less expenses attributable to the letting.

However for 2017/18 onwards, deductions for mortgage interest payments are restricted such that part of the interest cost is disallowed and replaced with a 20% tax reducer in the individual’s income tax computation. This has been discussed in previous lectures and will not be expanded on here. Suffice to say that the same rules apply irrespective of the residence status of the landlord.

NRLs will receive a UK personal allowance only if they are UK resident or (if not) they are British citizens, Crown employees or citizens of an EEA state (the latter may of course change under Brexit).

Tax withholding:

The NRL Scheme requires letting agents and tenants to deduct basic rate tax (currently 20%) from rents paid to the landlord and to pay the tax deducted to HMRC. Tax is accounted for on a quarterly basis for 3 month periods ended on 30 June, 30 September, 31 December and 31 March.

Tenants paying rent of less than £100 a week directly to a NRL do not have to withhold tax. This limit applies per tenant (therefore if 2 tenants rent a property from a NRL for less than £200 per week, no tax needs to be deducted). However where 2 or more people occupy a property but only one of them is the tenant under the lease, the threshold is £100 per week only.

There is no such lower rent limit for letting agents.

Expenses paid by the agent or tenant on behalf of the landlord during the quarter can be deducted from rents in order to calculate the tax to be withheld.

The letting agent or tenant can deduct expenses where they are “reasonably satisfied” that the expense they have incurred on behalf of the landlord will be an allowable deduction in computing his taxable profits. This will typically include cleaning, utility costs and repair and maintenance expenditure incurred by the agent or tenant. It will also include the letting agent’s own fees retained by the agent out of the rents.

If expenses in a quarter exceed rents, no tax is withheld for that quarter. The excess expenses are then carried back and deducted from rental payments made to the same landlord in previous quarters during the same NRL Scheme year (taking later quarters first). Any excess expenses remaining after carry back are then carried forward when calculating the tax withholding for the following quarter. Carrying back excess expenses triggers a “repayable amount” which can be set against tax due or is repaid by HMRC.

Application for gross payment:

Letting agents and tenants are not required to deduct income tax at source from rents paid to a NRL if HMRC has informed them in writing that the landlord has been approved to receive the rents gross.

NRLs who want to receive rents without tax deductions should complete and file a form NRL1i. Applications cannot be made any longer than 3 months before the NRL leaves the UK (HMRC will not consider applications made before that date).

The NRL1i asks for:

- Contact details (name, address, contact number etc);
- Personal information, such as a tax reference, most recent Tax Office and a NI number;
- How long a landlord will live outside the UK; and
- Information about any UK properties rented out.

HMRC will approve applications where the NRL1i is correctly completed, the NRL’s UK tax affairs are up to date and HMRC has no reason to believe that the NRL will not comply with his future UK tax obligations as regards reporting his property business profits. The NRL is notified of the approval. If a letting agent or tenant is named on the application form, HMRC will send a copy of the approval to that agent or tenant authorising them to pay rents without deduction of tax. Approval typically applies from the first day of the quarter in which the application is received by HMRC.

Approval does not mean that rents are exempt from UK tax. Approval simply gives NRLs a cash-flow advantage in that tax will be paid at a later date. HMRC can withdraw approval if the NRL fails to comply with his tax obligations (or HMRC has reason to believe he will no longer comply).

Where a NRL changes his letting agent or there is a change of tenant (where there is no agent), the authority to pay rents without deducting tax does not automatically transfer to the new agent or tenant. In this case the landlord should inform HMRC of the change and HMRC will send an authority notice to the new agent or tenant. Until this new notice is issued, tax should be deducted from any rents paid.

Registration

The NRL Scheme is not voluntary and all tenants of NRLs and letting agents acting on behalf of a NRL must comply. Registration responsibilities are however slightly different.

Lettings agents must register with HMRC no later than 30 days from the date on which they are first required to operate the Scheme (being 30 days from the beginning of the first tenancy). This includes letting agents who are authorised to pay rents to NRLs without deduction of tax.

Registration is normally made online by submitting for NRL4i. Lettings agents should supply their name, address, Tax Office and tax reference number (a contact name and telephone number is also requested). HMRC then provides a registration number to be used in future correspondence and on the quarterly and annual returns.

Tenants do not have to operate the Scheme if they pay rents to a letting agent in the UK. Otherwise tenants must register with HMRC. Tenants do not register using form NRL4i. Instead tenants should write to HMRC at Personal Tax International in Bootle.

Annual and quarterly returns:

Letting agents and tenants are also required to make annual and quarterly returns to HMRC declaring how much rent they have collected on behalf of the landlord and the tax they have withheld.

The quarterly return form NRLQ, together with payment of tax due, must be submitted to HMRC's Accounts Office, Shipley within 30 days of the end of the quarter. Interest is charged on tax paid late. Where a tax payment is not required for a quarter, there is generally no need to complete a quarterly return.

Letting agents and tenants are also required to send an annual rent report to HMRC on form NRLY. The report details rent payments and tax deductions for the NRL Scheme year to 31 March and is due by the following 5 July. Letting agents and tenants should also complete certificate NRL6 for the landlord detailing the tax withheld and paid on behalf of the landlord for the year to 31 March. This enables the landlord to complete his SA return. All forms are downloadable from the HMRC website.

NRLs themselves do not have special tax returns and instead the NRL will simply declare his rental income and expenses on the UK Property pages (SA105) of their annual self-assessment return. NRLs can credit any tax withheld at source by the letting agent or tenant against any tax liability. Any excess tax deducted will be repaid.

The maximum penalty for failing to make a return or filing an incorrect return is £3,000. This can be mitigated based on normal mitigation factors such as disclosure, degrees of culpability and extent of co-operation.

Joint owners

Where a husband and wife jointly own a property and both have their usual place of abode outside the UK, each is treated as a NRL in his/her own right and the NRL Scheme applies to each of them separately. Each spouse must therefore make a separate application to receive their share of rents gross. Letting agents and tenants should only pay rents gross to the spouse for whom an authority is held.

If one spouse normally lives in the UK and the other does not – for example one spouse is working overseas while the other stays behind in the UK – the NRL scheme only applies to the spouse living abroad. Rents can therefore be paid gross to the spouse living in the UK without any specific authority.

Finally

The NRL Scheme places a large responsibility on a tenant who is renting a property from an overseas landlord. One should expect professional letting agents to be aware of their responsibilities but the Scheme is harsh for tenants as it places an onerous burden on individuals who may not have the tax knowledge to accurately comply with the Scheme. But as people often say to me when I raise these things: “It is what it is”. Yes it is but it is still harsh.

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