STRUCTURING YOUR PROPERTY PORTFOLIO

HOW TO BUILD AND PASS IT ON TO YOUR LOVED ONES TAX-EFFICIENTLY

Many property investors don't realise they can accidentally build a monster. In the process of growing a portfolio to pass to their children or fund retirement, they often end up with a huge tax liability. Instead of being a gift, it becomes a burden, defeating the whole purpose.

Setting your intention early and structuring your portfolio correctly can help you avoid the common pitfalls I see landlords regularly run into. It also ensures you develop a cash-flowing asset that supports you and your family, without losing significant value to tax.

Below is my advice on how to structure things tax-efficiently, so you can save money and pass your properties on with minimal inheritance tax.

Taxation: A Property Investor's Biggest Hurdle

I head up the Commercial Services team at Ison Harrison, an award-winning firm with 22 branches across Yorkshire. In my role, I work with everyone from small-scale property investors and developers to multi-million-pound business owners. My focus is advising on legal matters such as lease options, joint venture agreements, loan structures, and company setups.

One of the most common issues I see across the board is taxation. With the government's eye becoming increasingly focused on landlords, it's more important than ever for them to understand how the tax system can be navigated effectively.

Unfortunately, I see many investors doing things the wrong way around, especially if they're 'accidental landlords'. They start building a property portfolio without seeking the right advice, and only when it reaches a certain size do they turn to experts to mitigate the tax liability they've built up.

It's a sweeping statement, but owning an investment property in your personal name is rarely the most tax-efficient strategy. This can create difficulties down the line. While it's possible to incorporate those properties into a business later, it's much more complicated.

I have seen situations where investors who've been buying property for decades are suddenly concerned about inheritance tax. When their portfolio is spread across personal names and businesses, untangling it becomes much more difficult than if they had received the right advice at the start.

A Case Study of How the Right Advice Can Save You Thousands

To give you an idea of why the right advice matters and why we recommend coming to us before making any major purchases, here's a real-life case study.

A client approached me wanting to buy a sizeable commercial property on a lease option, valued at around £1.5 million. Many firms would have simply put the option to purchase in the lease. However, my team identified that the property was owned by a Limited Company, and it was the only asset in that company.

Richard Coulthard
Director and Head of Corporate

Instead of the usual approach, we recommended the client take a lease on the property but purchase shares in the Limited Company that owned it. At the time, stamp duty on shares was just 0.5%, while land tax would have been 6-8%. This advice saved the client around £40,000 in tax.

The Three Ways of Tax-Effectively Buying Property

It is not a one-size-fits-all approach, but below are four structures you'd typically use as the most tax-efficient method of building a property portfolio.

- Buy property through your pension – This is a highly tax-efficient method, but it's best used if you're buying commercial property.
- Setting up a group structure – Create a share structure and allocate the shares between you and your children. You can make your children shareholders in the business with a different class of shares so that you can receive the income while they have rights to the capital value. I'll explain this in more detail in the next section.
- Trusts – You can place property or the funds used to purchase property into a trust. This helps keep it out of your estate, which can reduce inheritance tax. However, the downside is that the original investor will no longer be able to benefit from the income generated by the property.
- Family investment Companies – This is a company where there are different share classes with different rights. The advantage of this is that you can reserve the growth of the business to certain share classes, for instance, the younger generation, whilst retaining a right to earn dividends or the existing capital.

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To determine the right option for you, ask yourself key questions like: What's your aim? How much income do you need from your portfolio? How are you funding your purchases?

These questions will shape the route you take. For example, many mortgage providers don't like trusts, and while lending into a pension scheme is possible, there are certain rules around it.

How to Pass Your Portfolio to Your Loved Ones Without a Big Tax Bill

I will dive into the most common structure we advise. To give you an example, let's look at a typical situation: a couple who've built a portfolio of buy-to-let (BTL) properties, perhaps with one or two houses in multiple occupation (HMOs). These properties are already owned through a Limited Company, and the couple plans to live off the rental income during retirement.

Here's the problem: Over time, that portfolio becomes very valuable. And when that happens, it can turn into a tax headache, especially when it comes to inheritance tax. The more it's worth, the bigger the tax bill your kids could face when you pass it on.

One smart way around this is to set up what's called a Family Investment Company. With this, you create different types of shares:

- One type goes to the parents, which locks in (or "ringfences") the current value of the portfolio (say, £1,000,000).
- Another type goes to the kids. They don't get access to that first million, but any future growth above that amount can go to them.

You can also split the dividends between share types however you want. This creates a situation whereby you are freezing the value of the existing assets to avoid a growth in the value of the estate and reducing the ongoing accrual of inheritance tax, whilst allowing the parents the opportunity to continue to receive an income.

A further reduction in inheritance tax may be possible through a combination of gifts, trusts, and potential reliefs.

YOU CAN PLACE PROPERTY OR THE FUNDS USED TO PURCHASE PROPERTY INTO A TRUST. THIS HELPS KEEP IT OUT OF YOUR ESTATE, WHICH CAN REDUCE INHERITANCE TAX

More Sophisticated Tax Structures

You can set up a separate company structure with a different share class to move money into a company for your children to invest through. It's also possible to create a separate development company, which either hires or contracts people to carry out the work.

This would be an active, trading business rather than just holding property. That kind of setup might qualify for Business Property Relief, which can reduce inheritance tax, and there could also be VAT and tax relief advantages on the goods and materials you purchase.

Owning an investment property in your personal name is rarely the most tax-efficient strategy

This is specialist territory, so you'll need advice from both a lawyer and a tax advisor. There are lots of odd exemptions in the rules, especially around things like agricultural land, which can sometimes be used strategically. The earlier you get advice and define your goals, the better. It's much easier to set these structures pre-purchase.

Cost-Effective Structures for Joint Ventures

In addition to structuring property portfolios, I often work on joint venture agreements (JVs). These take many forms. Sometimes, a property expert brings the experience while investors provide the funding. In other cases, a developer partners with a landowner to unlock the potential of a site.

There are several ways to involve others in your projects. One route is a straightforward loan. Another is to give investors a role within your limited company. That allows them to benefit from any increase in value and receive a return at the point of sale. Some prefer to leave the money in the business, using it for future developments. This can lead to tax advantages or smoother cash flow.

Need to Review Your Portfolio? We're Here to Help

My team and I are happy to help any investor looking to restructure their portfolio or make significant changes — such as adding children as shareholders — that could create complications if not handled properly.

We work with portfolios and deals of all sizes, so no matter your level of experience, feel free to get in touch. Even if you just need a few quick pointers on potential roadblocks, we're here to support you.

If there's anything we can assist with, contact our team using the details below.

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