Guide to Calculating Rental Property Deductions

Guide No.10 in the Tax Guide Series

About This Guide

This Guide has been prepared to help you calculate your income tax deduction for Rental Properties. If you still have some questions after reading it, please call into the Income Tax Office.

Introduction

Rental income is treated as property income taxable under Part 2, Chapter 1V of the Income Tax Ordinance 2012. It is important to realize that rental income is not Part 1 taxable income (Income from Self Employment, Trade or Business) but all deductions that would be available to a person deriving income from self employment trade or business are available to a person deriving property income.

1. Classification of Expenditure

Expenditure incurred in deriving rental income can be classified under two broad headings. The first classification will be expenses that are incurred in bringing the rental property into existence. These costs are generally referred to as capital expenditure. Common examples of capital expenditure would include the cost of land, construction costs, the cost of acquiring an existing property or the cost of renovating a rental property. The second classification of expenditure will be those costs that are incurred as part of the process of deriving income. These costs are generally regarded as revenue expenditure. Common examples of revenue expenditure would be the cost of maintaining the property, the cost of annual services to the property or the costs connected with finding a tenant.

2. Examples of Non Deductible Capital Expenditure

Capital expenditure on rental property relates to all those costs associated with bringing the property into existence. These costs include:

- The cost of acquiring land;
- The cost of building on the land;
- The costs of constructing roadways and access paths to the building or property;
- The cost of connecting services such as power, water and telephone to the property;
- The cost of acquiring an existing property;
- The cost of any stamp duty and legal costs paid in relation to the acquisition of the property;
- The cost of renovating a property to make it suitable to rent;

- The costs of acquiring furniture, appliances and other fixture and fittings that will be installed in the building and used by the tenant.

3. Depreciation of Capital Expenditure

Paragraph 2 of Part D, Schedule 1 applies to allow a depreciation deduction on capital assets. To qualify for a deduction, the asset must satisfy the meaning of a depreciable asset.

4. Examples of Deductible Revenue Expenditure:

-

Allowable expenses and costs

As noted earlier, revenue expenditure relates to the costs incurred in deriving the rental income. Because of the varied nature of expenses that might be incurred by a person when deriving income, only a few deductions are specifically provided for in the Ordinance and the majority of deductions are allowed under the 'allowable expenses and costs' in Section 22 of Part 3 says that

"…there must be deducted from the income all outgoings and expenses to the extent that they are wholly and exclusively incurred during the relevant tax year by the person in the production of taxable income, including –

(a) sums payable by way of interest upon any money borrowed, if the Commissioner is satisfied that the interest was payable on capital employed in acquiring the income;

(b) rent paid by any tenant of land or buildings occupied for the purpose of acquiring the income;

(c) any sum expended for—
- repair of premises, plant or machinery;
- the renewal, repair or alteration of any implement, utensil or article; or
- the acquisition of any implement, utensil or article costing less than £1,000 and having a useful life of less than one year,

if the premises, plant, machinery, implements, utensils or articles are employed in acquiring the income;

(d) any sum expended for the acquisition of any tangible movable property or structural improvement to immovable property which—
- costs less than £1,000;
- has a useful life of more than one year;
- is owned by the person and used wholly or partly by that person in deriving taxable income; and
- is likely to lose value as a result of normal wear and tear, or obsolescence;

(e) any amount donated to a charitable organisation registered under section 7 of the Charities Ordinance, 2005, provided that the total amount allowable must not exceed 1% of the total taxable income of the donor, as referred to in section 8, which is derived during the tax year from self-employment, trade or business and income from property;

(f) the amount by which the value of the person's depreciable assets has declined during a tax year by reason of wear and tear from use in deriving taxable income (referred to as a "depreciation deduction") as determined in the manner prescribed by regulations;

(g) any loss incurred in a previous tax year which has been carried forward from the preceding year under section 24(2)*(b)…"*

In essence, this general allowance says that any expense incurred for the purpose of earning income is a tax deduction. However, Section 23 of Part 3 says that no deductions are allowable for certain categories of expenses. The categories that are most frequently excluded are:

- Capital expenses (see above), and
- Private or domestic expenses

Example 1. shown below illustrates how to calculate the depreciation deduction for item (f) above.

Year 1	Cost Depreciation Deduction (2%) Written Down Value	100,000 2,000 98,000
Year 2	Cost Depreciation Deduction (2%) Written Down Value	98,000 2,000 96,000
Year 3	Cost Depreciation Deduction (2%) Written Down Value	96,000 2,000 94,000
Year 4	Cost Depreciation Deduction (2%) Written Down Value	94,000 2,000 92,000
Year 5	Cost Depreciation Deduction (2%) Written Down Value	92,000 2,000 90,000

Example 1.

Deductions that satisfy the general allowance

There is no limit to the nature of a general deduction that would be allowable, provided it is not capital, private or domestic. Common examples include:

(a) The cost of electricity paid by the property owner.

(b) The cost of telephone, internet or other communication charges paid by the owner of the property.

(c) The cost of water paid by the owner of the property.

(d) The cost of any advertising to find a tenant.

(e) The cost of preparing a lease agreement.

(f) Any motor vehicle costs incurred for travelling in connection with arranging and or carrying out repairs, transporting materials, transporting tenants or any similar activities.

(g) Printing, postage and stationary costs connected with the property.

(h) The cost of keeping records of income and expenditure.

(i) The cost of having financial statements prepared.

5. Rental Property Profits (Paying Tax)

A profit on a rental property will arise when the total income received from the property exceeds the allowable tax deductions. Where a profit arises, it is taxable in the same manner as any other form of income. This means that all profits and gains are added together and tax is charged on the total amount remaining after deducting the personal allowance.

For example, a person earns £10,000 from employment during the tax year ended 31st March 2024 and has a rental profit of £3,500. The total chargeable income for the year is £13,500 less the personal allowance and tax is calculated on that amount at the normal rates.

Government of St Helena
Income Tax Office
April 2024