



Buying to Let



A Landlords Guide

Buy to Let: A Landlords Guide



What is Buy to Let?

Buy to let is where a person buys a property and then rents it out to tenants. Most Buy-to-Lets involve a mortgage or a loan on the property. When you buy a property and rent it out you become a landlord, with legal responsibilities and duties in regard to your property and your tenants.

There are many examples of success stories, where landlords have started out with a single property and through investment, knowledge, and aptitude for business, have become large portfolio landlords with dozens, hundreds or even thousands of properties. Unfortunately, there are also several examples of property investors who have overstretched themselves, or small landlords who have taken on a property and found that rather than earning extra money, they have lost everything as a result of poor financial planning and a lack of knowledge of tax implications, property maintenance or landlord and tenant rights and responsibilities. The aim of this guide is not to provide detailed information on specific issues, but to provide a first step to potential landlords who are thinking about buy to let and are unaware of the implications.

Before buying a property to let, it is vital that you obtain relevant expert advice and information on issues such as finance, legal implications, tax implications and property management. There are stiff penalties for landlords who fail to comply with legislation within the law, and potentially serious personal penalties for those who do not correctly research this market before becoming a landlord.

What property should I buy?

The size and type of property that you buy should be determined by your own financial constraints. Proper planning and research of possible expenses must be carried out before you commit to a property purchase.

It is best to buy in an area that you are familiar with, close to your home to allow a rapid response should you need to visit the property in an emergency, and also to make routine inspections and tenant enquiries easier to deal with. Gather as much information as possible from local letting agents, papers, local authorities and other landlords on the current rental market and rental incomes in your area. In general, the older the property, the more on-going maintenance will be required.

In most towns, there tends to be areas where rented properties are more common than other areas. This may be due to the availability of cheaper housing, good transport links, or good access to facilities, such as universities or hospitals.

Students

Many landlords decide to invest in the student market, but be aware that damage to student properties tends to be greater. Properties in student areas do however offer a reduced risk of void tenancies and holiday times allow any necessary non-urgent remedial works to be carried out. Considerations:

- How many rooms does the property have?
- Could any other room be easily converted into a bedroom?
- Furniture and white goods will need to be provided, and will wear out more quickly so you will need to budget for their replacement
- Is the garden low maintenance?
- HMO (houses in multiple occupation) Licensing – if the property is three or more stories, with five or more occupants it will require a licence. Further details can be found in the DASH HMO Licensing guide **(1)**

Local HMO requirements – these enforceable regulations may require several changes to the property such as fire doors and interlinked smoke alarms. They may also place limits on room sizes and amenities **(2)**. Contact your local authority for their requirements prior to purchasing the property, even if the property is currently rented. It is the landlord's obligation to ensure a property is compliant with all legislation.

Family

If you would prefer to rent a property to a family, you may wish to purchase outside of student areas, but still close to town centres. The rental income tends to be lower; the tenants will expect better quality, though they are less likely to cause damage. Considerations:

- Access to schools (i.e. bus services and catchment areas)
- Local road and rail links
- Furnishing is not essential
- Access to town centre
- Access to local amenities (shops, recreational facilities etc)
- Clean accommodation – a family will not want to move a child into an unhygienic property. Out-dated fixtures and fittings increase the perception of poor hygiene.

Young Professionals

The top end of the rental market is usually taken by young professionals. This group demands very high quality fixtures and fittings, but will pay a higher rent. This end of the market is always very competitive and fashion sensitive, therefore if your property looks out of date a young professional will not want it. Considerations:

- The property needs to have a unique selling point – many young professionals rent flats in converted warehouses/churches etc with original features.
- Frequency of property improvement – the property may well look outdated after three or four years. As this group of tenants demand quality in all the fixtures and fittings, regular replacement of items such as kitchens, bathrooms, flooring etc as well as regular redecoration, should be considered.
- Local transport links, particularly the commuter belt
- Access to town centre and recreational facilities

Financial arrangements

Before embarking on buy-to-let, you should obtain financial advice. Expert advisors will be able to analyse your potential incomings and outgoings and find the right product to suit your own budget. Remember that the information that you receive will only be accurate if you know the current rental valuation of your property. Visit letting agents and study the property pages in the local paper so that you have a good idea of what sort of rental income you could reasonably expect from your property. There are many factors that have to be taken into account, such as;

- Voids – this is where the property is empty or is not at full capacity. If you have calculated repayments based on the property being fully occupied for 12 months, you may find yourself in arrears if void periods occur
- Regular maintenance – services such as cleaning at the end of a tenancy and on-going maintenance are costs encountered by the landlord.
- Rent arrears – if one or more of the tenants falls into arrears with their rent, can you still afford to pay your mortgage?
- Property management – knowledge of local authority standards is essential, as these can be enforced. You should be aware of the Housing Health and Safety Rating System (3) and local authority enforcement options. (4)
- Property redecoration – rented properties need to be decorated regularly and should be budgeted for. Properties in poor condition are harder to let than properties that have been regularly decorated with modern fixtures and fittings.
- Property upgrades – local authority regulations may demand improvements to the property which will cost the landlord - contact your local authority for further advice. You will also have to provide an annual CORGI gas certificate, and it is advisable to have an electrical installation check periodically as well. Some landlord associations offer a rebate on the CORGI certificate charge as an incentive.
- Set up a suitable savings account – if making a profit on your letting ensure that the bank account that you use is the right product for you. Current accounts provide less interest, while ISA's may be used to save some of your profits tax-free.
- Legal insurance – obtain quotes for legal insurance. This insurance will protect you from the costs of evicting tenants in the event of non-payment of rent. This process can be very expensive, so insurance is worth investigating.

Choosing a Mortgage

If you need a mortgage you will have a choice of repayment or interest-only. Lenders will probably require a suitable investment product if you choose an interest only loan, and will usually advise you to take out life cover. This should be budgeted for.

With buy to let mortgages, lenders may take into account the potential rental income from the property rather than your earnings. Ensure you are aware of lenders' policies before committing. You should also have a deposit of at least 15% and own a main residence. Bear in mind that taking out a mortgage on a rental property may affect your borrowing power should you decide to move home.

If you take out a repayment mortgage, you will have the choice of fixed or variable rates. A fixed rate gives certainty, but you may pay more than the base rate. There can also be tie-in periods meaning that you may incur penalties if you change your mortgage over a period of time, typically one to three years. Fixed rate mortgages are also more likely to attract set-up fees, which should be made clear to you by your financial advisor and in most cases can be added to the mortgage amount.

Variable rate mortgages change in line with the Bank of England base rate, but you should always budget for an interest rate rise over the term of the mortgage. If, for example, you take out a variable rate mortgage of £90,000 over 25 years at 4.5%, you will pay £500.25 per month. If interest rates increase to 6.5% over your tie-in period, you will pay £607.69 per month, meaning an extra £100 a month. Note that if you change your mortgage during the tie-in period, you may incur additional penalty fees. Any increases in repayments may not be immediately recoverable from the tenant through increased rent.

Your mortgage lender or financial advisor will be able to provide you with illustrated costs for various interest rates, ask them how an increase in mortgage rates would affect your own individual repayments.

You will also need to have some form of buildings insurance in place to satisfy the demands of the mortgage lender. Make sure you obtain several quotes and choose the cover that is best for you. You may also choose to take out contents insurance if you intend to furnish your property.

Tax Liability

You should also be aware of potential tax liability when deciding on your budget. Earnings from rented properties are taxable, meaning you will have to pay income tax on rental earnings and potentially stamp duty when you buy the property and capital gains tax when you sell it. Expert advice on this subject is necessary, as taxation changes occur frequently and can have a large impact on your income. Ensure you are fully aware of all tax liabilities before committing to a property.

Stamp Duty

Stamp duty is payable at the time of property purchase. The amount of stamp duty payable is dependant on the purchase price (not the marketing price) of the property. Current stamp duty rates are listed below;

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|-------------------------|-----|
| • Up to £125,000 | Nil |
| • £125,001 - £250,000 | 1% |
| • £250,001 - £500,000 | 3% |
| • In excess of £500,000 | 4% |

Income Tax

Rent earned is treated as income and will be taxed in line with the standard or higher rate tax bands as necessary. It can be more tax efficient to have a mortgage on your rental property as you will be able to offset mortgage payments, managing agent costs and maintenance costs against this taxable rental income. Tax relief on mortgage payments is not available if the mortgage is on your own home rather than the rental property.

Capital Gains Tax

Capital gains tax is payable when you sell your second home. The length of time you have owned the property will dictate the amount of CGT that you pay, this is called 'taper relief'. After three years you would be taxed on 95% of the gain. This amount decreases year on year and after ten years you would be taxed on 60% of the gain. On sale of the property, you will be taxed at between 20% and 40% on all relevant capital gains above a basic limit.

Managing Agents

Another factor to consider is who will look after the property management for you. Some landlords choose not to use a managing agent, but it is recommended that you use a reputable agent to look after your property, especially if you are an inexperienced landlord or work full time. Managing agents will provide an initial rental valuation of the property, carry out viewings for potential tenants, handle contracts, reference checking of tenants, ensure the deposit is properly protected **(5)** complete an inventory of the property, ensure rent is paid on time and, depending on your agreement with them, organise any necessary property repairs. Managing agents also have knowledge of relevant legislation and procedures that can help when dealing with problem tenants.

There are several professional bodies letting agents may subscribe to. These include, but are not limited to, Association of Residential Letting Agents (ARLA) National Association of Estate Agents (NAEA) and the Royal Institute of Chartered Surveyors (RICS). It is advisable to choose an agent that is a member of one of these bodies or similar, as you will have greater scope for complaint should you be unhappy with the service you receive.

Letting agents usually charge between 10% and 15% of your rental income for their services. Ensure that you speak to as many agents as possible before deciding which one to use. Choose the agent that offers the service level you require and has a good local reputation.

Landlord Development Manual

The Landlord Development Manual that has been produced by the Accreditation Network UK (ANUK) along with Local Authorities Coordinators of Regulatory Services (LACoRS) and the Improvement and Development Agency (I&DeA) is an essential guide to all landlords, whether they are new to the property market or have a portfolio of several properties with years of experience. The manual explains in a concise, easy to read manner, everything that a landlord needs to know about subjects such as pre-tenancy matters, tax, setting up and ending tenancies and landlord and letting agent rights and responsibilities. The manual is available for free download **(6)**

Related links:

- Abbey National - www.abbey.com/csqs/Satellite?c=GSProducto&cid=1139301819633&pagename=Abbey%2FGSProducto%2FGS_Producto
- Association of Residential Letting Agents - www.arla.co.uk/btl/lenders.htm
- Best For Let – Buy to let mortgage specialists - www.best4let.com/
- Buy to Let calculator - http://calculators.ft.com/calculators/buyToLet.html#expander_0
- Lloyds TSB - www.lloydstsb.com/mortgages/buy_to_let.asp
- Money Supermarket – Mortgage Broker - www.moneysupermarket.com/mortgages
- The MoneyCentre – Mortgage Broker - www.themoneycentre.net/
- UCB Home Loans (Nationwide) - www.ucbhomeloans.co.uk/ExistingCustomers/ch_buytolet.html



Decent And Safe Homes (DASH) East Midlands is a project funded by the Government Office of the East Midlands. We work with landlords, tenants and Local Authorities to raise standards in housing.

Further information on DASH, its associates, projects and successes can be found by visiting our website at www.eastmidlandsdash.org.uk or by calling 01332 715780.

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Also Available:

- Housing Act 2004 Guidance - Houses in Multiple Occupation - Licensing in the East Midlands
- Housing Act 2004 Guidance - Local Authority Enforcement Options. A Landlords Guide
- Housing Act 2004 Guidance - The 29 Hazards. A Landlords Guide
- Housing Act 2004 Guidance - Tenancy Deposit Protection Schemes
- Housing Act 2004 Guidance – Amenities and Space in HMOs
- The Decent Homes Standard. A Landlords Guide

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1 - <http://www.eastmidlandsdash.org.uk/docs/DASHLLHMOlicensingLandlordGuide.pdf>

2 - <http://www.eastmidlandsdash.org.uk/docs/DASHLLAmenities+SpaceBooklet.pdf>

3 - <http://www.eastmidlandsdash.org.uk/docs/LandlordsguidetoHHSRS.pdf>

4 - <http://www.eastmidlandsdash.org.uk/docs/DASHLLEnforcementBooklet.pdf>

5 - <http://www.eastmidlandsdash.org.uk/docs/DASHLTDPBooklet.pdf>

6 - <http://www.lacors.gov.uk/lacors/upload/12744.pdf>