Buy-to-let Mortgage Guide

Information & support for **landlords**

THE FINANCE ROOME

Mortgages & Insurances

Welcome

Buying a property to let can be an excellent form of income and investment for the future.

The key to investing successfully is to plan your finances. Be aware of what's happening in the market and choose the right buy-to-let property. Before you start looking for the perfect property there are a few things to think about - our handy guide can help you do just that.

Why buy-to-let?

Interest rates have been at an all-time low since 2009, leaving many people looking for alternative ways to invest their savings. A buy-to-let property can be a great option, either to provide a regular income or to potentially grow your capital if property values increase over time.

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T: 01242 226353 **E:** enquiries@thefinanceroome.co.uk thefinanceroome.co.uk

Choosing the right property

When choosing your buy-to-let property, consider the potential rental returns. Study the local area and try to buy in a location you know will be attractive to prospective tenants. Who do you intend to rent your property to? Students, families and young professionals have different requirements for a property and for the location they choose to live in.

Features that can make a property more appealing

- Within walking distance of public transport.
- Good commuter links to the nearest city or town.
- Close to hospitals or universities.
- In the catchment area of good schools

Targeting who you want to rent to will ensure you buy the right type property in the right place, making it easier to rent out.

About a buy-to-let mortgage

Once you've found the perfect property, the next step is to decide what sort of mortgage is best for you. To help you decide, think carefully about what you want out of your buy-to-let investment. If you want to own the property in the long run, a repayment mortgage might be your best option. But if you want to sell when house prices rise, you may want to consider interest only. In order to secure any buy-to-let mortgage there are a few things to consider:

How much deposit will I need?

You'll need a larger deposit for a buy-to-let property than you would with a residential mortgage. Most lenders require 25% deposit although some will ask for more than this. Whilst there are a handful of lenders who may lend at 80-85% it's often very tricky to get the rental income to fit at this level.

What income will I need to earn?

Most lenders require you to have a minimum income of £25,000 in addition to any rental income, to cover periods when the property might be empty. However, there are some lenders that do not insist on this.

Can my first property be a buy-to-let property?

There are very few lenders who will lend a buy-to-let mortgage to a first-time buyer and some lenders insist that you own your main residence. Not all mortgage providers have the same rules and because we search the entire market, nine times out of ten we're able to find a lender to meet your requirements.

Will the property be owned in my name or under a Limited Company?

For tax reasons more and more people are choosing to let properties under a limited company name. This will have an impact on which mortgage companies will lend. We always recommend asking your accountant for tax advice before you purchase the property to understand the best options for you. For Limited Company buy-to-let's most lenders require a property portfolio schedule, assets and liability statement and a business plan.

Will my choice of tenant and the type of property affect my mortgage possibilities?

Some lenders will want to know the type of tenant you're planning to attract and the type of tenancy you intend to offer. This differs from lender to lender. For example, they may want to know if the property will be let on a short-term basis like Airbnb, an Assured Shorthold Tenancy agreement (AST) or a corporate let. They will then ask whether your tenants are to be students, DSS rental, a house of multiple occupancy or a family let. Lenders will also vary depending upon whether you're asking them to lend on a flat (particularly if it's above a commercial unit) or a house.

Is there a limit to the number of properties I can own?

Again, this varies from lender to lender. Many cap the amount of properties you can own at 4 at which point they classify you as a portfolio landlord and stress test your existing portfolio before lending on any future property. Other lenders have no limit at all.

How much rental income will I need?

This is the most complicated part as every lender is different. Depending on your own income, the product and the loan-to-value can make a difference. **On the following page is an example of one lender** and how they calculate how much the rental income will need to be to allow them to lend.

Stress rates and interest cover ratio (ICR)

To reflect the different taxable income levels of landlords. They apply:

ICR		
Buy-to-let and Let to Buy		HMO
Tax rate of 20% or less	Tax rate of 40% or more	
125%	145%	170%

Example

£100,000 mortgage x 5.5% x 125% divided by 12 **= £572.92 per month**

Stress rate	Product term under 5 years			Fixed rate 5 years and over
	65% LTV and lower	65% LTV and lower	65% LTV and lower	
Remortgage without capital raising	4.99%	5.50%		4.99%
All other application types	5.50%		5.99%	

Case Study

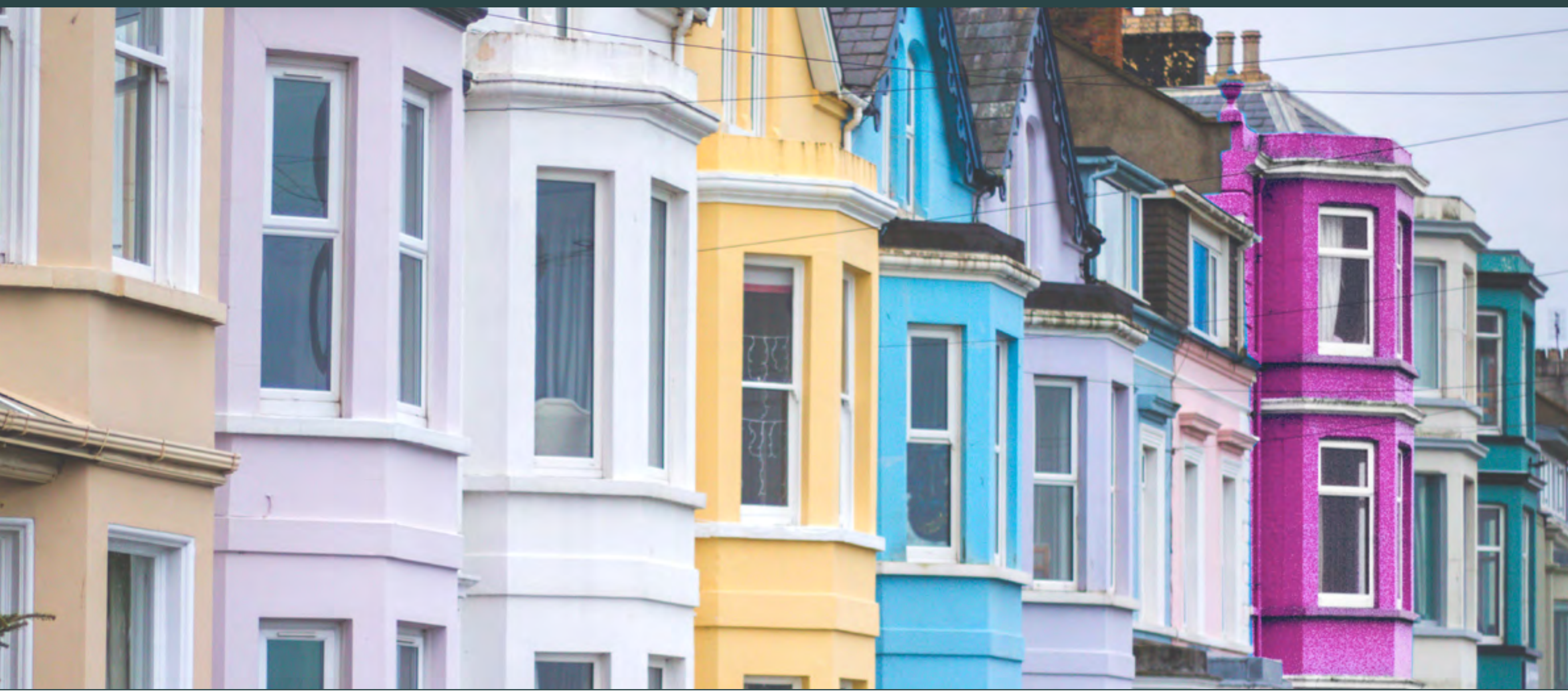
Purchase price: £650,000
Mortgage: £390,000
Estimated rent: £1,950

How much rental should be charged?

Loan: £390,000
Stress Test Rate: 5.50%
Monthly rental needed
140% = £2,502.50

As the rental coverage was over 100% and the personal income was over £50,000, the client qualified for buy-to-let top slicing. This is when a customer's rental income falls short, some providers can top it up by considering the client's overall income and expenditure. If they have enough spare income to cover the shortfall, they would look to lend the full amount.

The customer was £552.50pcm short to borrow the amount he wants. Because it was identified that he had sufficient surplus income to cover the £552.50pcm monthly rental shortfall, this lender was able to lend him the full amount.



Additional costs

Make sure you think about the upfront and ongoing costs that are involved before becoming a landlord.

Upfront costs

- Stamp duty and legal fees, including surveys/valuations.
- Your deposit.
- Compulsory inventories, and gas and electricity safety certificates.
- Any minor repairs required before tenants move in.
- Furnishings (you can let your property with or without furniture, and your rental price should reflect this).
- Refurbishment and development if you need to improve or update your property. Letting agents, if you choose to go through them to find tenants.

Ongoing costs

- Long term repair and maintenance
- Void periods – there may be times when you are between tenants and your mortgage payments aren't covered by rental income.
- Landlord's insurance/building insurance.
- Renewing annual safety certificates i.e. gas, which should cover all appliances and flues in the property.
- A management agency fee, if you decide to use one to help with the ongoing management of the property.
- Service charges.
- Ground rent.

Changes to energy performance rating

From the 1st April 2018 a new legal requirement was introduced for any properties rented out in the private rented sector to have a minimum energy performance rating of E on an Energy Performance Certificate (EPC). Where existing tenancies are in place, the legal requirement came into effect from 1st April 2020.

Stamp duty

From 1 April 2016, an additional 3% was added to Stamp Duty Land Tax (SDLT) for people buying additional residential properties. The Scottish Government also introduced higher rates on Land and Buildings Transaction Tax (LBTT). These rules apply if you own two or more residential properties at the end of the day you complete the purchase, and you are not replacing your main residence.

Stamp Duty Land Tax (England Wales & Northern Ireland)	**Land & Buildings** Transaction Tax (Scotland)	**Standard Rate**	**Higher Rate**
£0 to £125,000*	£0 to £145,000*	0%	3%
£125,000 to £250,000	£145,001 to £250,000	2%	5%
£250,000 to 925,000	£250,001 to 325,000	5%	8%
£925,000 to £1,500,000	£325,001 to £750,000	10%	13%
£1,5000,000 plus	£750,001 plus	12%	15%

*Higher rates do not apply to properties costing £40,000 or less

Your responsibilities as a landlord

When investing in a buy-to-let property, there are a few things to consider. As a landlord, you must:

- Treat your tenants fairly.
- Understand and comply with all legal requirements, including any licensing or registration rules and health and safety obligations towards the tenant. This includes gas safety, electrical equipment safety and fire and carbon monoxide safety. You'll also need certificates to prove these regulations have been met. This is not an exhaustive list.
- Understand the consequences of being unable to comply with your obligations under a buy-to-let mortgage.

Please remember; if you are unable to comply with your obligations, such as keeping up repayments on your mortgage, lenders have the power to take possession of and sell the property to secure repayment of the mortgage loan, or to appoint a receiver of rent for the property. Think about how you would cover the mortgage and other costs during void periods if your property is empty and you don't receive any rental income. Protect your property's value by keeping it well-maintained and, for a leasehold property, meeting valid requests from the freeholder and/or the managing agent. Make sure you have appropriate buildings insurance in place from exchange and throughout the mortgage term.

Finding tenants

Finding good tenants is a serious business. After all, they'll be living in your investment. To attract quality tenants, make sure your property is in the best possible condition.

If you already have tenants in while prospective tenants are viewing your property, ask them to clean and tidy up, and to make sure all the furniture is in its original position. Choose neutral colours when you decorate, as this will work with whatever furniture, bedding and ornaments your prospective tenants may already have.

Rent

Working out how much you'll need to spend on buying and running your property will help you plan how much rent to charge. You'll need to take into account your buy-to-let mortgage payments, insurance, agent's fees, any repairs and add on any estimated periods when the property might be empty. This is a useful exercise as it will help you decide whether the rent you'll need to charge is viable.

It's a good idea to research the rental market in the area so you can set a realistic price for the size and location of your property. Have a look online and in local newspapers to get an idea of what other people are charging. Make sure you get a deposit from your tenants and confirm they can pay this upfront. This will usually be at least one month's rent (and you have the right to ask for more), to safeguard against any damages or to make your mortgage payments if your tenants move out unexpectedly.

Tenant deposits are no longer held by landlords - instead, they're held in a tenancy deposit protection scheme. You'll need to set this up and provide your tenant with details within 28 days of taking their deposit.

You don't want to be travelling miles to sort out any problems a tenant might have

Security checks

It's important to get professional and personal references to make sure you're comfortable with your new tenants. You might even want to run a credit check to make sure they'll be able to make their rental payments, as well as to verify they are who they say they are. The National Landlords Association offers a tenant check that includes bankruptcy and county court judgement searches. Alternatively, letting agents will usually carry this out as part of the tenant finder package.

How will you manage the property?

Do you intend to manage the property yourself, or use a letting agent? The answer to this question will help to narrow down your location. You don't want to be travelling miles to sort out any problems a tenant might have. Using a letting agent will mean you could buy a property further afield in an area that might have a higher demand for rental property. They'll usually charge a fee as a percentage of the tenant's total rent but for that they'll be able to do some or all of the following:

- Draw up a suitable tenancy agreement.
- Advise on and arrange inventory and condition reports.
- Help with changes to utility accounts and council tax.
- Market appraisals to assess the rent the property will fetch.
- Collect rent and pay the money to you.

If you decide to use a letting agent, it's still worth meeting the tenants yourself to establish contact from the start and make sure you're happy.

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How can we help you?

If you'd like to speak to us, call our Cheltenham office today on **01242 226353** or email us: **enquiry@thefinanceroome.co.uk** to request a call back.

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