FINANCE UPDATES
MARCH 2020

ORCHID FINANCIAL SERVICES

BUY-TO-LET: IS IT STILL WORTH IT?

Weighing up the effects of landlord tax changes.

Since the mid-2000s, the UK private-rented sector has seen a huge surge in growth, with 2.8 million households in 2007 rising to 4.5m in 2017, according to the Office for National Statistics.

With low interest rates discouraging cash saving, and rising house prices offering chances of high returns, many people turned to property as a way of investing their money.

More recently, however, that growth has ground to a halt.

Data published in December 2019 by UK Finance shows that the share of new, mortgaged buy-to-let home purchases is 40% lower than in 2015, and the Residential Landlords' Association reports that up to 30% of landlords are seeking to exit the sector altogether in the next five years.

So, what's prompting so many people to give up on property – and is buy-to-let still a worthwhile investment?

THE BUY-TO-LET BOOM

In response to the global financial crisis in 2008, governments around the world began to cut their interest rates, aiming to encourage spending to revitalise their economies.

Here in the UK, the Bank of England reduced its base rate – the rate by which banks and lenders generally set their own interest rates – to 2% in late 2008, to 0.5% in early 2009, and down to 0.25% in 2016.

The rate has recovered slightly in the years since, but currently remains at 0.75%, and questions have been raised about whether another cut is in store in the near future.

From a personal financial planning perspective, this essentially means there's little incentive to keep your money in a cash account, where it's unlikely to grow above the rate of inflation.

This has led many savers to consider alternative options – property being one of them.

On top of that, rising property values have made it especially appealing, with Land Registry statistics showing that the price of an average property rose from £84,620 in January 2000 to £234,742 in December 2019.

While there are now signs that this growth could be stalling, year-on-year property prices still rose by 2.2% between November 2018 and 2019.

With those kinds of returns available, many people have kept hold of properties they would otherwise have sold, to pass on to their children in the future or as a way to save for retirement.

As well as the potential to benefit from the increased value by selling the property, there's the appeal of a regular source of income through monthly rent payments.

However, it's important to be cautious. With property just as much as any other investment, returns are not guaranteed, and market uncertainty paired with recent changes to buy-to-let taxation might sway your decision.

WHAT'S CHANGED?

In the last few years, a number of changes implemented by the Government have made a dent in the profitability of buy-to-let.

As a result, many landlords have needed to evaluate whether letting their property is worth the time and money they spend on it, and if another type of investment would suit them instead.

Stamp duty surcharge

In April 2016, the Government introduced an extra stamp duty charge in England, Northern Ireland and Wales of 3% for the purchase of additional property, including buy-to-let.

That meant stamp duty rates increased across all price bands for people buying more than one residential property in these parts of the UK.

Finance cost relief

Next, from April 2017, the Government began to restrict relief for the costs of finance on residential properties.

Previous to this, landlords were able to deduct 100% of their finance costs, including mortgage interest, from their property income when calculating profits.

In 2017/18, this was reduced to 75%, then gradually phased out in the following years. In 2020/21, the relief will have been removed altogether.

Tax year	Deductible finance costs
2017/18	75%
2018/19	50%
2019/20	25%
2020/21	Nil

In place of finance cost relief, landlords will be able to claim a basic-rate reduction from their income tax bill for those costs.

Private residence relief and letting relief

More tax changes for landlords are set to take place from April 2020, when changes to private residence relief are due to come into effect. Private residence relief usually covers people selling their main home from the cost of capital gains tax.

It applies for the years that someone lived in a property, as well as the last 18 months they owned it – this is known as the final-period exemption.

People who let a part of their property out can also claim letting relief on up to £40,000 of their chargeable gain.

From April, the final-period exemption will be reduced to nine months, and the qualifying conditions for letting relief will change, so that it will only apply where the owner of the property shares occupancy with their tenant.

For some landlords, that could mean much higher capital gains tax costs when they come to sell their property in 2020/21.

Letting fees

The Tenant Fees Act that came into force on 1 June 2019 means most letting fees charged to tenants are now banned.

In rental contracts made as of that date, landlords and letting agents can only charge tenants for things like rent, a tenancy deposit within certain limits, payments for utilities and council tax, and fees for late rent, replacing keys or security devices.

WHAT ARE YOUR OTHER OPTIONS?

In recent years, many landlords have started incorporating their property business. This is likely influenced by the changes to mortgage interest relief, which don't apply to limited companies.

Forming a limited company is an option that's worth considering if you own multiple properties, but it's a serious step to take, and there are considerable differences between renting property as an individual and as a company.

If you already own a property and want to move it to a limited company, your company may need to pay capital gains tax on the transfer, as it would be buying the property from you.

If you decide property's not for you, there are various other investment options which we can talk you through, which will vary based on your goals, attitude to risk, and so on.

Talk to us about your investment options.

IMPORTANT INFORMATION