Summary of Stephen Johnson's presentation on HMO valuation

Earlier this year, the Royal Institute of Chartered Surveyors put out a consultation on new valuation guidelines for HMOs. As this is a guidance note, these are recommendations for best practice, rather than hard rules. In his speech at our December Investor Day, Stephen Johnson went into more depth about the new approach. In this summary we have brought together the key points of his speech.

RICS categories

RICS has three categories of buy-to-let variations

- *Category 1* – A single unit containing a single household, with a single Assured Shorthold Tenancy Agreement
- *Category 2* – A single unit, containing a sharing household of up to four people, with a single Assured Shorthold Tenancy Agreement
- *Category 3* – Licensable houses in multiple occupation

Valuation approaches

- **Single residential units:** Single residential units are comparable in value and rents to existing valuation methods.
- **HMO valuation:** When it comes to HMO valuation, the valuation must fit with the "tone" of values in areas of mixed investment and owner-occupied areas. The extent of works is fundamental to considering the HMO's value. If there are going to be minimal works, it is likely to be classed as a private dwelling. In an area of owner occupation, where there is no Article 4 Direction, the property is likely to be valued as a private dwelling, with a little expenditure in order to comply with an HMO license.
- **Areas of mixed owner-occupied and HMO:** These are typically larger Victorian or Edwardian properties, often occupied by students. With regards to valuation, both single dwelling and HMO valuations could apply. It is important to check the sustainability of rents given room sizes and bear in mind that securing an HMO license is no guarantee of full compliance as an HMO. Only when there has been an inspection by the environmental health officer, are you covered. This inspection is measured against the Housing Health and Safety Rating System (HHSRS) and is valid for up to five years.
- **Article 4:** In those areas with Article 4 Directions in place, the development of further HMOs is restricted.
- **Multi-unit blocks:** It is possible to consider valuing and selling the blocks as individual units but then you must consider whether they will appeal to owner-occupiers or a single investor.

Rental evidence

When considering rental value and evidence, the new build premium must be factored in. Higher than average maintenance costs must be identified in the report and equally, it is critical that issues that could result in enforcement are identified. This will affect income and therefore value. You should consider the costs likely for that property and the nature of the tenant profile in the yield. These will be higher, for example, if there is turnover, void periods, or you have higher costs with welfare tenants. Be careful not to double count the deductions from rent applied to the yield factor. The gross rent, net of utilities, is critical for lenders.

When working with valuers, the service level agreement must take account of the complexity of the property. At the point of inspection, lenders must know if the property condition means that it could not be re-let at the same rental level. On a remortgage this may prove an indication of the way the landlord maintains his properties.

HMO standards

There are central government standards but increasingly it is local authority expectations that introduce more onerous requirements. For example, the valuers need to assess compliance with regards to the sustainability of rental income. This applies to minimum room sizes and facilities such as separate toilets, the length of the kitchen work surface etc.

These notes are a brief summary and for fuller details, you should always consult a professional.

Stephen Johnson; Shawbrook Bank

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