



# The changing institutions of private rental housing: an international review

Inquiry into the future of the private rental sector

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# Contents

<b>List of tables</b>	<b>viii</b>
<b>List of figures</b>	<b>ix</b>
<b>Acronyms and abbreviations used in this report</b>	<b>xi</b>
<b>Executive summary</b>	<b>1</b>
<b>1 Introduction</b>	<b>7</b>
1.1 Why this research was conducted	7
1.2 Policy context	7
1.3 Key concepts	9
1.3.1 Private rental housing	9
1.3.2 Institutions	9
1.3.3 Change	10
1.4 Research methods	10
<b>2 International comparisons of private rental housing</b>	<b>11</b>
2.1 Existing comparative research on private rental housing	11
2.1.1 From decline to diversity	11
2.1.2 Thematic analyses	12
2.2 Comparative theory	14
<b>3 International change in housing system contexts</b>	<b>16</b>
3.1 Private rental in the housing system	17
3.1.1 Private rental share of housing	17
3.1.2 Private rental built form	20
3.1.3 Housing trajectories and the PRS	23
3.2 Policy governance	26
3.3 Wider contexts	26
3.3.1 Population	27
3.3.2 Economy	28
3.3.3 Housing markets	31
3.4 Key findings	34
<b>4 International change in PRS market and policy settings</b>	<b>35</b>
4.1 Financial settings	35
4.1.1 Credit settings	36
4.2 Tax settings	39
4.2.1 Subsidies	44

4.3	Landlords and managers	46
	4.3.1 Landlords	46
	4.3.2 Property management	48
4.4	Regulation	49
	4.4.1 Rent regulation	49
	4.4.2 Security of tenure	52
	4.4.3 Registers	54
4.5	Key findings	55
<b>5</b>	<b>Case studies in institutional change—Germany, Ireland, United Kingdom and United States</b>	<b>57</b>
5.1	Housing system contexts	57
	5.1.1 Germany	57
	5.1.2 Ireland	59
	5.1.3 United Kingdom	60
	5.1.4 United States	60
5.2	Financial settings	61
	5.2.1 Housing checks and spurs: Germany	61
	5.2.2 Housing checks and spurs: Ireland, the United Kingdom and United States	62
	5.2.3 Specific-purpose subsidies	64
5.3	Large corporate landlords	65
	5.3.1 LCLs in the United States	65
	5.3.2 LCLs in Germany	66
	5.3.3 LCLs in Ireland and the United Kingdom	66
	5.3.4 LCL operations	66
5.4	Paths of regulatory reform	68
	5.4.1 Enduring regimes in Germany and the United States	68
	5.4.2 Diverging paths in Ireland and the United Kingdom	68
5.5	Key findings	69
<b>6</b>	<b>Conclusion: policy development implications</b>	<b>70</b>
6.1	Housing system contexts	70
6.2	Financial settings	71
6.3	Landlords	71
6.4	Regulation	72
6.5	The future of private rental housing	72
	<b>References</b>	<b>73</b>

<b>Appendix 1: Private rental housing in Germany</b>	<b>82</b>
<b>Appendix 2: Private rental housing in Ireland</b>	<b>98</b>
<b>Appendix 3: Private rental housing in the United Kingdom</b>	<b>116</b>
<b>Appendix 4: Private rental housing in the United States</b>	<b>131</b>
<b>Appendix 5: 10-country survey instrument</b>	<b>148</b>

## List of tables

Table 1: Policy governance: Australasia, Europe, North America (select countries)	26
Table 2: Housing credit settings: Australasia, Europe, North America (select countries)	36
Table 3: Tax settings, PRS and owner-occupied: Australasia, Europe, North America (select countries)	40
Table 4: Tax settings, PRS and property: 10 countries	43
Table 5: Subsidies to landlords: Australasia, Europe, North America (select countries)	45
Table 6: Subsidies to tenants: Australasia, Europe, North America (select countries)	45
Table 7: Landlords and managers, PRS: Australasia, Europe, North America (select countries)	47
Table 8: Rent regulation: Australasia, Europe, North America (select countries)	50
Table 9: Security of tenure: Australasia, Europe, North America (select countries)	52
Table A 1: Tenure change, UK, 2003/04 – 2015/16 (% households)	117
Table A 2: Length of residence	121
Table A 3: Restrictions of cost relief to individual private landlords	123
Table A 4: Landlord profile (2010), by % of landlord entities	125
Table A 5: Landlord profile (2010), by % of rented dwellings	125
Table A 6: Rental housing, ownership and subsidies, United States 2015.	132
Table A 7: Renter and owner profiles, United States 2015	134
Table A 8: Ownership of rental properties by landlord type and property size, United States 2012.	140

## List of figures

Figure 1: International comparison	2
Figure 2: Private rental housing and other tenures: Australasia, Europe, North America (select countries)	18
Figure 3: Private rental housing built form: Australasia, Europe, North America (select countries)	21
Figure 4: Household composition in private rental and other tenures: Australasia, Europe, North America (select countries)	24
Figure 5: Rental households by income quintile: Australasia, Europe, North America (select countries)	25
Figure 6: Population change: Australia, Ireland, New Zealand and Spain	27
Figure 7: Population change: Belgium, Sweden and the United Kingdom	27
Figure 8: Population change: Canada, Germany and the United States	28
Figure 9: GDP % change, 2006–15: Australia, Canada, New Zealand	29
Figure 10: Unemployment %, 2004–14: Australia, Canada, New Zealand	29
Figure 11: GDP % change, 2006–15: Belgium, Germany, Sweden	30
Figure 12: Unemployment %, 2004–14: Belgium, Germany, Sweden	30
Figure 13: GDP % change, 2006–15: Ireland, Spain, United Kingdom, United States	31
Figure 14: Unemployment %, 2004–14: Ireland, Spain, United Kingdom,	31
Figure 15: Real house price index—Australia, Canada, New Zealand	32
Figure 16: Real house price index: Belgium, Germany, Sweden	32
Figure 17: Real house price index: Ireland, Spain, United Kingdom, United States	32
Figure 18: Ratio of household debt to annual disposable income: Australia, Canada, New Zealand	33
Figure 19: Ratio of household debt to annual disposable income: Belgium, Germany, Sweden	33
Figure 20: Ratio of household debt to annual disposable income: Ireland, Spain, United Kingdom, United States	34
Figure 21: Large corporate landlords—United States, Ireland, Germany, United Kingdom	65
Figure A 1: Private renting by age	119
Figure A 2: Over and under-representation of household types in the private rental sector (2014/15)	119

Figure A 3: Over and under-representation of ethnic groups in the private rental sector (2014/15)	120
Figure A 4: Percentage of households in each income decile living in the private rental sector	120
Figure A 5: Costs of Housing Benefit by tenure (£ '000)	124
Figure A 6: Landlord and stock profile	125
Figure A 7: Landlord possession claims, England and Wales 1999–2016	127
Figure A 8: Housing completions by built form, United States 1975-2015.	133
Figure A 9: Rental housing built form (dwelling units in buildings), United States 2001-2015	137

## Acronyms and abbreviations used in this report

ABS	Australian Bureau of Statistics
AHS	American Housing Survey
AHURI	Australian Housing and Urban Research Institute Limited
BBSR	Bundesinstitut für Bau-, Stadt- und Raumforschung (Federal Institute for Research on Building, Urban Affairs and Spatial Development) (Germany)
CPI	Consumer Price Index
GDP	Gross domestic product
GFC	Global financial crisis
HAP	Housing Assistance Payment (Ireland)
HMO	Houses in Multiple Occupation (UK)
LCL	Large corporate landlord
LMI	Lenders mortgage insurance
LTI	Loan-to-income ratio
LVR	Loan-to-valuation ratio
LIHTC	Low-Income Housing Tax Credit (US)
MBS	Mortgage-backed security
NAMA	National Asset Management Agency (Ireland)
NHS	National Household Survey (Canada)
NRAS	National Rental Affordability Scheme (Australia)
NSW	New South Wales
PRS	Private rental sector
SAREB	Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria (Spain)
SFH	Single family homes
SPV	Special purpose vehicle
RAS	Rental Accommodation Scheme (Ireland)
RBA	Reserve Bank of Australia
RBS	Rental-backed security
REIT	Real estate investment trust
REO	Real estate owned (US)

UK	United Kingdom
US	United States of America (United States)

## Glossary

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## Executive summary

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- The growth of private rental housing in Australia is important across a range of policy areas, from the administration of housing assistance, to consumer protection, to macroeconomic policy.
  - This report provides a resource for considering policy settings and institutions relevant to the Australian private rental sector (PRS) by drawing on the international experience of 10 countries in Australasia, Europe and North America.
  - The report takes a ‘system-embedded’ approach to comparative housing analysis through interrogating the international experience of housing and impact of broader economic systems, financial settings, landlord and tenancy structures and regulation in the reference countries.
  - It is not the case that ‘everyone in Europe rents’. Most of the European countries surveyed have higher rates of home ownership than Australia. In 9 of the 10 countries including Australia, the PRS is the second largest tenure after owner occupation. In seven countries, the PRS is growing.
  - Australia’s PRS stands out in international comparisons for being less differentiated from the wider housing system in terms of its built form, household types and incomes. This suggests a high degree of integration between the Australian PRS and owner-occupier sectors, which is significant for policy-making.
  - Finance policy and market settings have undergone remarkable change before and after the global financial crisis (GFC). Particularly in countries that experienced a housing crash, finance settings have driven rapid change in PRS institutions, often without guidance from conventional housing policy objectives.
- 

### The report

This is a report of international comparative research into the institutions of private rental housing and how they are changing. The research was conducted as part of AHURI’s Inquiry into *The future of the Private Rental Sector* (AHURI Inquiry 51120).

We take a ‘system-embedded’ approach to international comparative analysis which considers the particular PRS policy settings and institutions of the reference countries in the context of their housing and wider socio-economic systems.

For our international review we looked at the 10 countries (Figure 1), with a detailed review of four (Germany, Ireland, the United Kingdom and United States).

Figure 1: International comparison



Source: Authors.

We took a broad view of 'institutions', to include:

- **housing and socio-economic system factors**, such as housing form, housing markets, household form and economic performance
- **financial settings**, such as housing credit, taxation and subsidies
- **landlords and managers**, both individual persons and large corporations
- **regulation**, with a focus on laws regarding security of tenure and rents.

## Key findings and policy implications

The international comparative literature shows that private rental housing, once regarded as a sector in terminal decline, is now mostly growing and diversifying, changing in some cases rapidly. Conventional typologies put forward in housing research are being overtaken by changes in the PRS and wider housing systems. A rising theme in the literature is the 'financialisation of housing', which refers to the increasing importance of housing in financial markets and the increasing participation of households in finance, particularly through leveraging property ownership for consumption or investment. Studies of PRS regulation indicate a diversity of approaches to questions of rent regulation and security of tenure.

From our 10-country survey, and from closer examination of changes in Germany, Ireland, the United Kingdom (UK) and the United States (US), our key findings and their implications for PRS policy development are summarised below.

### Housing system contexts

Private rental housing is the second largest tenure after owner occupation in all but one of the countries we reviewed (only in Germany is the PRS larger). In 7 of the 10 countries, the PRS share is growing, mostly at the expense of owner occupation, and nowhere is it significantly contracting. Wider system contexts—such as population growth, economic growth, house prices

and household debt levels—vary across the countries. Germany is exceptional for its extended period of stable house prices; other countries have had booms and some have had booms and busts. In all countries house prices are rising again. Australia is unusual for having had a long escalation in house prices and no recession—and now the highest level of household debt of the 10 countries.

In most countries, the profile of the PRS mostly tends towards apartments, small households and lower incomes. In this regard Australia stands out for having a PRS that is less differentiated from the wider Australian housing system than that in most other countries, in terms of building types, household form and household incomes.

### ***Policy implications***

The relatively high degree of resemblance between the profiles of the PRS and wider housing system in Australia implies a high degree of integration, particularly between private rental and owner-occupier markets. Hence, the policy settings and market conditions which apply to one may be transmitted readily to the other.

Australian housing policy discussions are usually directed to improving affordability; it would be wise to think also about how to conduct equitable housing policy in a post-crash market. The integration between the Australian PRS and owner-occupied sectors heightens the prospect of investment in both sectors collapsing with little established institutional capacity for counter-cyclical investment that makes necessary additions to supply. The question of managing and relieving housing-related debt involves doing justice not only between creditors and debtors, but between debtor and non-debtor households.

### **Financial settings**

Across the 10 countries, housing investment is mostly financed by credit, which is mostly provided by banks. Over the past two decades, housing credit has expanded—albeit punctuated by the GFC—with the development of new funding sources. Following the GFC, nine of the countries surveyed have implemented housing-specific macroprudential tools as a financial stability measure.

In those countries most affected by the GFC, government programs for the disposal of impaired property-related assets have significantly increased the position of large corporations in the PRS, both directly as landlords (as in the United States) and indirectly as owners of loans with PRS properties pledged. The responses of Ireland, the United Kingdom and the United States to their financial and housing crises have enabled some existing owner-occupiers and large financial institutions to increase their position in the housing market, though with some curbs around riskier bank lending. This may be no more sustainable or equitable than the pre-GFC housing credit expansion.

Looking at the range of tax settings applicable to housing and the PRS, we find some surprising results. Australia and Germany share several settings: both countries exempt owner-occupied housing from capital gains and both provide for negative gearing on similar terms. Yet Australia's and Germany's treatment of negative gearing and capital gains tax underlie quite different housing market outcomes: speculative inflation in Australia; relatively steady housing prices in Germany. In some respects, Australia has stronger settings against speculation: for example, land value tax. Significantly, we identified that eight of the 10 countries have recently introduced or reformed their tax regimes to provide for real estate investment trusts (REITs), which are emerging as a significant vehicle for PRS investment funding.

The major form of direct subsidy in the PRS is rent assistance payments. These were made in all 10 countries to tenants—and hence indirectly to their landlords. Some countries also provide specific-purpose subsidies to PRS landlords: Germany provides low-interest loans for energy efficiency modifications and Ireland pays landlords for low-income housing through its Rental

Accommodation Scheme (RAS). The United Kingdom's 'Build to Rent' incentives, which include loan and income guarantees, may be outweighed by its austerity-driven reduction in demand-subsidies paid to low-income tenants, which has significantly reduced the rental revenue base represented by that cohort in recent years.

Germany avoided the combined financial and housing crises experienced elsewhere because of a range of institutional factors, including its conservative home lending sector and the withdrawal of some housing subsidies. It may be that some features, such as negative gearing and capital gains tax exemptions, have a speculative potential which is active in other contexts, but not in the specific German context of an historically enduring large PRS, low population growth, conservative public financial institutions and rent regulation. In trying to shape the housing outcomes of a growing PRS, Ireland has taken a strategic approach that joins subsidies and regulation.

### ***Policy implications***

Particularly in countries that experienced a housing crash, finance settings have driven rapid change in PRS institutions, often without guidance from conventional housing policy objectives. Macroeconomic policy should look further than its effects on financial system stability or housing market levels to keep in view its effects on housing system institutions and housing policy objectives. This applies not just in responding to crises: for example, the specific effects of housing-related macroprudential tools on the investment strategies and borrowing practices of PRS landlords is worthy of investigation.

Of all the policy settings considered in this review, tax settings show best the necessity of considering policy settings in interaction with each other and in wider systemic contexts. It is the interactions which explain how similar tax settings can operate and shape housing outcomes differently: for example, negative gearing facilitating housing speculation in Australia and housing affordability in Germany. Strategy for the PRS should join consideration of finance, taxation, supply and demand-side subsidies and regulation with the objective of making PRS housing outcomes competitive with other sectors.

### **Landlords**

Smallholding private individuals are the predominant type of landlord in nine countries: only in Sweden are housing companies more common. Most countries, however, also have some large corporate landlords (LCLs), and a few have recently seen rapid growth in very large new LCLs. The origins of LCLs are diverse, but their recent activity has been facilitated by government activities: in Germany, municipal housing privatisation; in the United States and Ireland, post-GFC programs for the disposal of impaired assets.

The rising LCLs are not building much rental housing. Rather, they are mostly acquiring existing properties and actively manage their portfolios through renovations, modifications and sales. The LCLs have been active also in mergers and, especially in the United States, in devising new financial instruments. LCLs are often controversial and there is evidence of conflictual relations with tenants, particularly in Germany and the United States.

### ***Policy implications***

'Institutional landlords'—the LCLs—are now a standing item on the Australian housing policy agenda. Policy makers and stakeholders in the PRS should start specifying what sorts of LCLs are really wanted, and how desired housing outcomes will be delivered. Recent affordable housing policy initiatives have sought to develop community housing providers into a sector of large-scale, mission-oriented landlords. Care should be taken to ensure that these initiatives are not colonised by for-profit LCLs at the expense of affordable housing providers and outcomes.

## Regulation

The view of tenancy regulation as 'red tape' is out of step with the recent experience of most countries in this study. None of the recent growth in the PRS in the countries surveyed has been prompted or unleashed by deregulation (though arguably the United Kingdom's reforms of the late 1980s had such an effect). On the contrary, Ireland and Scotland are examples of successively stronger regulation being implemented as the PRS has grown. Only Spain has recently liberalised its tenancy laws.

The foremost approach to assuring tenants' security is to allow landlords to terminate on prescribed grounds only. This is the situation currently in Germany, Sweden, Scotland, most of the Canadian provinces and some major US cities. Only Belgium and Spain rely on long fixed terms and Ireland has a unique regime of cyclical restrictions on termination by landlords. Only Australia, New Zealand, the United Kingdom (other than Scotland) and some US jurisdictions allow termination without grounds. Notably, the State of Victoria in Australia is legislating to remove the provision for termination for no specified reason end the end of the first fixed term of an agreement.

Rent increases are regulated in four countries—Belgium, Germany, Spain and Sweden—most of the Canadian provinces and some major US cities by limiting them to a stated guideline or reference rent. Ireland and Scotland do so in designated 'rent pressure zones'.

Registers are an old regulatory technology which have been given a new lease of life in several countries with public registers of private landlords, in particular, providing a mechanism for monitoring and lifting standards of conduct.

### *Policy implications*

The view of tenancy regulation as 'red tape' is out of step with the recent experience of most countries in this study. Smallholding individual landlords and LCLs operate without undue difficulty in more strongly regulated PRSs than Australia's. The use of prescribed grounds for termination is consistent with Australian PRS institutional structures and could be adopted here; similarly, market-related rent regulations (e.g. limitation to guidelines or indices) could operate in combination with conventional Australian tax settings. The extension of registration requirements to mainstream PRS landlords could address some problems posed by smallholding landlords and LCLs, respectively.

## The study

We reviewed international changes in the institutions of private rental housing through three phases of research:

- a review of the international comparative literature
- a 10-country survey, involving experts in each reference country and follow-up research
- analysis of detailed country reports by experts in four countries commissioned for this research.

The first phase of our study was a review of the comparative literature and national studies of PRSs around the world. Our review of the literature was ongoing throughout the project with the second and third phases of the study directing our attention to further national-level sources.

The second phase was a survey of PRS institutions and change in the 10 countries, including Australia. A questionnaire about PRS institutions and change was devised and sent to experts in the nine international reference countries. Survey responses for Australia were provided as a guide to response formats. The international responses provided a rich source of data and

additional resources which we interrogated to identify themes in institutional change for closer examination in the third phase of our research.

The third phase comprised closer examination of four countries—Germany, Ireland, the United Kingdom and the United States—as case studies of the themes in PRS institutional change identified in the literature review and survey. We commissioned four experts—Stefan Kofner (Germany), Aideen Hayden (Ireland), Mark Stephens (UK) and Alex Schwartz (US)—to each write a report on their respective country according to these themes of change, which the research team then used to produce a synthesis analysis of institutional change. The four country reports are appended to this report.

# 1 Introduction

## 1.1 Why this research was conducted

The Australian PRS is growing, both in absolute terms and relative to the owner-occupied and social housing sectors. This means, necessarily, that the PRS is changing in terms of the types of households who live in it, its ownership and the buildings that comprise it. Behind these aspects of change we might expect further change in the wider contexts of the housing system and the economy; in the means by which investment in private rental housing is financed; in the ways in which rental property ownership is organised and conducted; and in the regulatory regimes that affect the terms on which tenants and landlords engage with each other and with the housing sector.

Internationally, private rental housing is changing too—in many countries, though not all, through growth in the amount of stock in the sector. By studying international experiences of PRS change we may gain alternative perspectives on Australia's PRS institutions and insights into the opportunities and challenges that change presents.

This study was conducted as a supporting research project within AHURI's Inquiry into the Future of the Private Rental Sector (AHURI 51120). The project was directed to the second research question of the Inquiry:

**Research Question:** What lessons can be drawn from institutional change in private rental sectors (PRSs) internationally which could enhance the equity, efficiency and effectiveness of the sector in Australia, particularly to improve outcomes for low-income tenants?

To that end, we adopted two subsidiary research questions for the project:

**Research Question 1:** What significant institutional developments or trends have been seen recently in private rental sectors in countries comparable with Australia?

**Research Question 2:** What can be learned from international experience that could inform change in the Australian private rental market, having regard to its particular institutional and market sector?

We have pursued these questions in a comparative analysis of the PRS in 10 countries—Australia, Belgium, Canada, Germany, Ireland, New Zealand, Spain, Sweden, the United Kingdom and the United States—with closer examination of Germany, Ireland, the United Kingdom and United States as case studies on contemporary PRS institutional change. We took a 'system-embedded' approach to the analysis informed by Stephens (2011), which considers the features of each country's PRS in the context of the country's wider housing and socio-economic systems as disclosed by a mix of research methods: a review of the research literature; a questionnaire survey completed by experts in each of the 10 countries; and commissioned reports by experts in Germany, Ireland, the United Kingdom and United States.

## 1.2 Policy context

Interest in the PRS is rising across different areas of policy in Australia. In housing policy, attention is being drawn to how the PRS is growing relative to owner occupation. More households are renting longer into their lives, including their child-raising years and beyond, and more households with moderate and higher incomes are renting. These developments challenge the historical assumption that owner occupation will provide secure, affordable housing to most persons over their lifetime and raise the question of how well equipped the institutions of the PRS are to substitute effectively for owner occupation.

There is a growing view that to deliver a sufficient supply of appropriate, affordable and secure rental housing a new sector of large, professionalised 'Build to Rent' landlords and special financial backing is required.

In the more specific area of housing assistance policy, the PRS has grown relative to social housing. More government funds are spent in the PRS than in the social housing sector with Commonwealth Rent Assistance expenditures having overtaken Commonwealth–State Housing Agreement funding in the mid-1990s and continuing to grow (DPMC 2014). With the decline in funding to the social housing sector, many applicants are waiting extended periods to be allocated a social housing tenancy. State and territory social housing authorities subsequently have developed forms of rental assistance that operate in the PRS, such as grants or loans for bonds, brokerage programs and private rental subsidy programs. Use of these forms of assistance has increased over the years and these are now the most common form of assistance provided by social housing authorities.

In 2015–16 state and territory housing authorities in Australia made allocations of public housing to 21,299 households and private rental assistance to 128,119 households (Australian Institute of Health and Welfare 2017). Social housing authorities are looking increasingly to PRS assistance not as a temporary measure pending an offer of social housing, but as assistance that maintains persons in the PRS without prospect of a social housing tenancy (see, for example, the proposed Rent Choice subsidy under the NSW Government's (2016) social housing agenda *Future directions for social housing in NSW*).

The social housing offer has been changing too. No longer generally conceived of as a permanent form of housing or a way into home ownership, social housing increasingly is being recast as a temporary measure pending the tenant's transition to the PRS. Most recently, the Productivity Commission's draft report on reforms to human services has proposed a further recasting of housing assistance policy, envisaging social housing operating more like the PRS. Under these reforms tenants would pay market rents subject to Commonwealth Rent Assistance and, in some cases, an additional subsidy. They would also be afforded more choice in respect to their housing, including a PRS tenancy (Productivity Commission 2017). Again, these developments and prospects raise questions as to how well the PRS is equipped to perform as an arm of housing assistance policy.

These questions have prompted policy-makers to consider the regulation of the PRS and the adequacy of the legal rights of tenants—especially as regards their security and autonomy. From the late 1970s to the early 1990s, all Australian states and territories enacted residential tenancies legislation on a similar model of prescribed standard forms of agreement, market rents, ready but orderly termination and dispute resolution through accessible forums. Most have now reviewed their legislation at least once, with NSW, Tasmania and Victoria having recently conducted major reviews and Western Australia and Queensland now at different stages of reviewing their Acts. These reviews are often framed by references to the growth of the PRS, but have mostly resulted in small fixes of specific problems.

Aside from housing policy, the PRS is also becoming increasingly significant in macroeconomic policy. As the PRS has grown, so too has the number of persons who own a rental property, with higher rates of growth for those who own multiple properties (albeit off a low base). Hence there is a broadening and a deepening of PRS ownership in Australia. The financial liabilities of PRS investors have grown even more: the stock of debt owed by PRS investors has grown by 50 per cent over the past five years to half a trillion dollars (ABS 2017a). The role of PRS investment in money creation has drawn the attention of the Reserve Bank of Australia (RBA) and the position of PRS borrowers and lenders is subject to ongoing analysis by the RBA in its regular Financial Stability Review reports. Pointedly, the recent Financial System Inquiry (2014) highlighted the risk posed to the stability of the financial system by housing investment, particularly in the rental sector, and the Australian Prudential Regulatory Authority has

## 1.3 Key concepts

In Chapter 2 we review the existing body of international comparative studies and other literature on private rental housing. We discuss briefly below three key concepts for the project and the wider AHURI Inquiry as indicated in our research questions: private rental housing; institutions; and change.

### 1.3.1 Private rental housing

We can be relatively clear as to what we mean by ‘private rental housing’ in Australia. The Australian Bureau of Statistics (ABS) definition ‘renter: private landlord’ constructs private renting as an economic relationship between a household and landlord, that being: ‘a household paying rent to a landlord who is: a real estate agent; a parent or other relative not in the same household; or another person not in the same household’ (ABS, 2017b). The definition refers predominantly to the ownership of the housing and excludes from private rental two important categories of ‘landlord’ recognised by the ABS—state housing authorities and community groups—which we distinguish as social housing. It might be noted that of the three categories of landlord included in the definition of private rental, the first, ‘real estate agent’, is not actually a landlord but an intermediary who acts for a landlord of another kind. Here the definition begins to describe wider institutional arrangements and practices in the sector.

Aside from ownership, the ABS definition also refers to the terms on which private rental housing is provided. The definition excludes arrangements where some other person owns the housing but no rent is paid: for example, where accommodation is incidental to a person’s employment and non-commercial housing arrangements between families and friends. This suggests, without insisting, that private rental housing is provided for profit, which in turn suggests that market mechanisms will be used to allocate it. It is possible to think of arrangements that make the definition problematic: for example, rental housing provided by a community housing organisation outside conventional social housing eligibility criteria and at market rents. Mostly, though, the elements of the ABS definition work to define a recognisable sector of the Australian housing market.

When we look internationally, other countries define private rental housing differently. In the statistics for European countries compiled by Eurostat, we find the question of ownership and landlord type dispensed with and ‘market rental’ distinguished from ‘below-market rental’. This follows from some European countries (e.g. Belgium, Sweden) having publicly owned municipal housing companies that own substantial proportions of ‘market rental’ housing. However, even the ‘market rental’ criterion can be problematic as some landlords may not be profit-maximising (e.g. Belgian and Swedish municipal housing companies); some may be subject to state subsidies and conditions of their allocations (e.g. the individual landlords who provide most of the ‘social housing’ in Germany); and some countries regulate rents in ways quite different from what is understood by ‘market rents’ elsewhere (e.g. Sweden’s system of collectively bargained ‘utility rents’). There are also countries where ‘rent-free’ housing is a substantial part of the housing system (e.g. Austria, Italy and Spain) (Carliner and Marya 2016: 8). How we define and distinguish private rental housing reflects national institutional arrangements, and these arrangements are subject to change.

### 1.3.2 Institutions

We define ‘institutions’, following Hodgson (2006: 2), as ‘systems of established and prevalent social rules’—a wide definition that encompasses laws, policies, cultural norms, corporate and organisational forms and patterns of practice by individual persons. Within this definition the smallholding individual landlords prevalent in the PRS in Australia and many other countries are collectively an ‘institution’ of each PRS. The institutional focus of our project is intended to bring attention to aspects of private rental housing that have received less prominent treatment in

recent research than issues of supply, affordability and other outcomes of housing policies and markets.

### **1.3.3 Change**

We are particularly concerned with recent changes in institutions. Such changes may be driven by policy or markets and may be radical or marginal. The key consideration is that a challenge is posed to established and prevalent social rules.

In thinking about change, we have been guided by Kemp's (2015) conceptualisation of PRS institutional change in the United Kingdom, which teases apart the different processes that can generate gradual but transformative change. These include the layering of new institutions or rules on top of old ones; displacement where new or previously subordinate institutions become increasingly important over time; conversion, where an existing institution established for one purpose takes on another one; and drift, where an existing institution is not updated to take into account new conditions and becomes increasingly less relevant over time (Kemp 2015: 603–604).

Our focus is on the past decade or so, though sometimes a longer perspective is warranted to properly conceive of the change process. Our concern with recent change focuses our institutional review and orients it to the larger AHURI Inquiry into 'The Future of the Private Rental Sector.

## **1.4 Research methods**

Our research was conducted in three phases, each with its own method.

The first phase was a review of the comparative literature and a range of national-level studies of the PRS around the world. Our review of the literature was ongoing throughout the project with the second and third phases directing our attention to further national-level sources.

The second phase was a survey of PRS institutions and change in 10 countries, including Australia. A questionnaire about PRS institutions and change was devised and sent to international experts in each of the survey countries, along with responses for Australia to guide implementation of the survey in those countries. The survey provided data and further literature and sources which we reviewed to identify themes in institutional change for closer examination in the third phase of our research. The survey was conducted according to the terms of approval granted by the University of New South Wales Human Research Ethics Committee.

The third phase comprised closer examination of four countries—Germany, Ireland, the United Kingdom and the United States—as case studies of the themes in PRS institutional change that we identified in the literature review and survey. We commissioned four experts—Stefan Kofner (Germany), Aideen Hayden (Ireland), Mark Stephens (UK) and Alex Schwartz (US)—to each write a report on their respective country according to these themes of change, which the research team used to produce the synthesis analysis of institutional change at Chapter 5. The four country reports are appended to this report.

## 2 International comparisons of private rental housing

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Much like private rental housing itself, the international comparative literature is growing and diversifying.

Conventional typologies are being overtaken by changes in PRSs and wider housing systems. The ‘financialisation of housing’ is a rising theme in the research, but its treatment of the PRS is not well developed. Studies of PRS regulation indicate a diversity of approaches to questions of rent regulation and security of tenure.

This project takes a ‘system-embedded’ approach, which considers a country’s particular PRS policy settings and institutions in the context of its housing and wider socio-economic systems.

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### 2.1 Existing comparative research on private rental housing

There is a substantial body of international comparative research on private rental housing, the development of which broadly follows the changing prominence of the PRS in housing markets and policy.

#### 2.1.1 From decline to diversity

Harloe’s 1985 study of private rented housing in Europe and the United States tracked private rental from its peak as the majority housing form at the end of the nineteenth century through a long decline over the twentieth century, the pace of change differing between countries. Looking ahead, Harloe (1985: 318) concluded:

*There is unlikely to be any revival of the large scale, organised capitalist provision of rental housing. Indeed, its decline will continue and even accelerate in those countries where substantial commercially provided rental housing remains.*

However, with an eye to the then recent reduction of state support for social housing construction in the United Kingdom and United States, Harloe (1985: 318) also acknowledged the prospect of ‘an expansion of small scale provision of rented accommodation by resident landlords and others’ to address the housing problem for those excluded from owner occupation and social housing.

By the end of the twentieth century the theme of PRS decline was under challenge by developments in housing systems and in housing theory. In an edited international collection of papers on private rental housing, Priemus and Maclennan (1998) drew attention to the ‘different faces’ of private rented housing with Maclennan (1998) also observing that in a number of countries—Australia, Germany, Sweden and the United States—the PRS had maintained its relative share for some time and that even a relatively declining PRS may in a growing population be growing absolutely, with noteworthy new investment and providers. Maclennan (1998: 388) emphasised that ‘an inevitable decline perception was never fully accurate and now inappropriate’, and detected instead a shift to a proliferation of housing system trajectories across different countries.

In a series of works, Kemeny (1995; 2001; 2006) set out a theory of housing systems that challenged conventional sectoral definitions and patterns. In particular, Kemeny criticised the notion that the rental sector was radically divided between residual, non-profit social housing and for-profit private rental which, because of high rents and inferior security, tended to decline

relative to owner occupation. This sort of ‘dualist system’ was specific to Anglophone countries. By way of contrast, Germany, Sweden and neighbouring countries were ‘unitary systems’ where for-profit private landlords competed with cost-rent housing providers including, in some countries, subsidised and regulated private landlords. This drove affordability and security outcomes that made rental housing a genuine alternative to owner occupation. These different national housing systems, according to Kemeny, reflected broader strategies of government expressed in welfare arrangements, as indicated by Esping-Andersen’s (1990) typology of liberal (dualist), conservative/corporatist and social democratic (unitary) welfare states<sup>1</sup>.

Since the turn of the century, private rental housing in many countries on both sides of the dualist/unitary divide has grown and accelerated—as has the literature. General comparative analyses of private rental housing across selected countries are provided by Haffner et al. (2009), Oxley, Lishman et al. (2010), Scanlon and Kochan (2011), Crook and Kemp (2014a) and Whitehead et al. (2016). Each addressed primarily the development of ‘revived’, even ‘vibrant’, PRSs, while also acknowledging divergent trends in the position of private rental within national systems and in the drivers of change (Crook and Kemp 2014b: 10). TENLAW, a massive research program on tenancy law and housing policy sponsored by the European Union, presents very detailed country reports and comparisons with a focus on law and state policy (see TENLAW 2015). Carliner and Marya (2016) provide a concise presentation of comparable quantitative data as to rental costs, demographics, built forms and conditions across Europe and North America.

### 2.1.2 Thematic analyses

Some researchers have taken more thematic approaches. One line of comparative research focuses on the relationship between the private rental and social housing sectors, following on from and critiquing Kemeny’s analysis. Haffner, Hoekstra et al. (2009), Hulse, Jones et al. (2010), Lennartz (2011) and Blessing (2016) present evidence from recent market and policy developments in various countries that complicates the dualist/unitary typology. For example, some subsidy programs in ‘dualist’ countries, such as Australia’s National Rental Affordability Scheme (NRAS) and Ireland’s RAS, have brought some private landlords into a ‘semi-social’ sector (Hulse, Jones et al. 2010: 151; Blessing 2016).

Meanwhile, in some unitary countries programs of social housing privatisation and subsidy withdrawal are allowing greater play of profit motives and divergence within rental markets (Lennartz 2011). The underrepresentation of some household types—in particular, families with children—in the PRSs of these countries indicates that private rental housing may not always be seen as a genuine alternative to owner occupation (Hulse, Jones and Pawson 2010: 149). These studies suggest that welfare typologies and trends are losing their analytical relevance for developments in rental housing and wider housing systems (also Schwartz and Seabrooke 2008: 256; Aalbers 2016: 88; Stephens 2016).

Another line of comparative research relates to housing finance. Whitehead and Lunde (2015) collected comparable accounts from Europe and Australia of developments in housing finance over the preceding 25 years. They found that in most of the countries studied there had been rapid innovation in housing-related financial instruments and expansion in housing-related debt, but with the countries starting in different positions and following different trajectories over the period—particularly around the global financial crisis (Lunde and Whitehead 2015a; 2015b).

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<sup>1</sup> Kemeny regards Esping-Andersen’s ‘social-democratic’ category as a ‘variant’ of the corporatist category, with which is aligned the ‘unitary’ housing category—a category which also admits considerable variation between non-profit *influenced* rental markets (e.g. Germany) and non-profit *led* rental markets (e.g. Sweden) (Kemeny, 2006).

In national and international housing studies, the ‘financialisation of housing’ has emerged as a compelling theoretical framework for researchers (Aalbers 2016; Beswick et al. 2016; Bryan and Rafferty 2015; Fields and Uffer 2016). The theme of this line of research is the increasing importance of housing in financial markets and operations, and the increasing participation of households in finance, particularly through owning housing and using it to leverage credit for consumption or investment. International comparative analyses using a financialisation perspective include Schwartz and Seabrooke (2008), who categorise countries according to their degree of housing-related debt and their degree of owner occupation. The resulting scheme reworks Esping-Andersen’s (1990) typology relating to ‘varieties of residential capitalism’: ‘liberal’ high-debt/high-owner occupation systems (e.g. Australia, the United Kingdom, the United States); ‘familial’ low-debt/high owner occupation systems (e.g. Belgium, southern and eastern Europe); ‘corporatist’ high-debt/low owner occupation systems (e.g. Germany); and ‘statist-developmental’ low-debt/low owner occupation systems (e.g. Sweden) (Schwartz and Seabrooke 2008: 244)<sup>2</sup>.

Aalbers (2016) reworks the ‘varieties of residential capitalism’ typology further to consider the connection of housing systems to global finance and to emphasise the dynamism of financialised housing systems. Aalbers does this by conceiving of housing financialisation as a global force which meets with national-level institutions as ‘filters’, resulting in countries following different ‘trajectories’ within the common trend. On this view, Australia, Ireland, the United States and the United Kingdom are on a trajectory of high financialisation; they are joined also lately by Spain, which has switched track from the low financialisation trajectory of other southern European countries. Germany is on another trajectory where financialisation has been resisted but may be taking hold.

Financialisation perspectives offer a promising conceptual framework for analysing contemporary change in housing and economic systems but, curiously, the treatment of private rental housing is relatively underdeveloped. For example, both Schwartz and Seabrooke (2008) and Aalbers base their typologies on criteria relating to owner-occupied housing. Aalbers does address the PRS through observation of the rise of ‘large, financialised investors, such as private equity firms and publicly listed real estate firms, buy[ing] up entire city blocks or even entire social housing companies’ (Aalbers 2016: 11)—an important, if still narrow field of rental housing financialisation.

Another line of international comparative analysis focuses on regulation and the PRS. Lind (2001) reviews rent regulation. Criticising the conventional dichotomy of ‘first generation/hard’ and ‘second generation/soft’ rent controls for obscuring the heterogeneity of the latter, Lind identifies instead five types of rent regulation across Europe and North America. Whitehead et al. (2012) investigate the relationship between PRS size and growth and the degree of regulation. Following an examination of 11 European countries, they conclude that there is ‘no clear relationship’ (Whitehead et al. 2012: 69). Hulse, Milligan and Easthope (2011) consider the degree to which ‘secure occupancy’ can be enjoyed by tenants in different countries. They find that this concept is properly understood as something more than ‘security of tenure’ and is a function not only of a country’s laws but subsidies, market structures and cultural norms.

From this brief review of the literature, two general points may be drawn, one about the subject matter and another about method.

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<sup>2</sup> The country examples are given by Schwartz and Seabrooke (2008). However, Germany and Sweden, in particular, do not fit the respective criteria well: Germany has a well-established housing finance system but housing debt is relatively low; and Sweden has relatively high rates of owner-occupation and housing debt.

- Neither 'decline' nor 'rise' really captures the changes that private rental housing has undergone: there has been a great variety of experiences across countries with different starting points and different trajectories. This presents a challenge for international analyses.
- International analyses have variously sought to compare, or more often contrast, features of systems across countries and to theorise the structuring of system features and change.

## 2.2 Comparative theory

Within the comparative literature several works specifically address conceptual and methodological issues relating to international comparative housing research: in particular, Kemeny and Lowe (1998); Haffner, Hoekstra et al. (2010); Stephens (2011; 2016); and Aalbers (2016).

Reviewing the growth of international comparative housing research, Kemeny and Lowe (1998) identify three broad approaches in the literature. One is a 'particularistic' approach, typically involving the presentation of a series of descriptions or measurements of countries' housing systems in which the analysis is juxtapositional, highlighting uniqueness and difference with a low degree of theoretical explanation of the differences observed. The second is a universalist approach, which looks across countries for evidence of common underlying imperatives and drivers of change, and in which the analysis considers differences as 'variations' on essentially similar or converging developments. Lying between these approaches is a third way, Kemeny and Lowe's own preferred 'divergence' approach, which tries to 'discern patterns or typologies of housing systems' and presents an analysis that 'explains how the types comprising the typology are generated and sustained' (1998: 170).

Haffner, Hoekstra et al. (2010) employ a similar conceptualisation in reviewing comparative approaches to private rental housing specifically. They argue for a 'middle way' between 'universalism' (which assumes, for example, that 'private rental housing' can be defined across countries by a common type of profit-oriented landlord) and 'particularism' (which focuses on the unique mix of corporate forms and business models of landlords in each country). This middle way consists of first finding 'commensurability' between features of national systems by identifying a 'key unifying feature: for example, private rental housing can be defined across countries by the feature of allocation other than according to need (Haffner et al. 2010: 368). The defined sector should then be contextualised in terms of its function and position within the wider housing system of a country and presented in a theoretically informed typology: for example, Kemeny's unitary/dualist typology, Esping-Andersen's typology of welfare regimes or Haffner et al.'s (2009) own typology of differential 'gaps' between private rental and social housing sectors.

Stephens (2011; 2016) presents a critique of these reviews. While accepting that the approaches Kemeny and Lowe (1998) and Haffner et al. (2010) set out are valid academic enterprises, Stephens detects in them a disparagement of policy-oriented comparative research which tends to be conducted in a descriptive or 'particularistic' mode (Stephens 2011: 339–341). Stephens (2011: 344) makes a case for comparative housing research that is especially attentive to the particularities of national context because of 'the distinctive nature of housing as a focus of public policy'. More than other 'welfare goods', its provision mixes the state and market and implicates a greater range of policy areas and actors. Its physical durability and spatial fixity also sets up greater path dependence and area effects.

This also means that the complexity of housing research multiplies when conducted across countries. However, the benefit of international comparisons is that 'the understanding of policies relating to complex and interactive systems may be enhanced if the behaviour of different policies in similar contexts or similar policies in different contexts can be captured' (Stephens 2011: 345). Doing this requires what Stephens calls 'system-embedded research'.

This entails:

*... recognising that housing policies operate within housing systems and housing systems in turn interact with wider social and economic systems. In other words, it needs to identify the dynamic between policy and institutions including the market; and the interaction between the housing system and wider socio-economic institutions ...*  
(Stephens 2011: 353)

The present research is consciously directed to informing policy development for the Australian PRS, and adopts the 'system-embedded' approach to its review of institutional change in private rental housing internationally. We first present an overview of PRS institutions in their wider contexts in 10 countries with attention to recent changes; we then provide a closer examination of how certain themes in PRS institutional change have played out in the four focus countries. We do not offer here a new theory or typology of the PRS or housing systems. However, we have considered the theoretical literature's themes and explanations as we specified the institutions under study.

What we have aimed to do is assemble a detailed information base about PRS institutions in a range of international jurisdictions to inform policy development and future research in Australia, and present this in a way that keeps the interactions between institutions and wider systemic contexts in view and provides insight into how institutional effects and meanings are generated by these interactions.

### 3 International change in housing system contexts

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Across the 10 countries surveyed:

- Private rental housing is the second largest tenure after owner occupation in nine countries, and in seven of those countries its share is growing.
  - The profile of the PRS mostly tends towards apartments, small households and people on lower incomes, but the degree of difference between the PRS and the broader housing system varies between countries.
  - The dwellings and households in Australia's PRS are more representative of the wider Australian housing system than those in most other countries.
  - Wider system contexts—such as population growth, economic growth, house prices and household debt levels—vary across the countries. Germany stands out for its extended period of stable house prices, while other countries have boomed—and some boomed and crashed.
  - Australia has had a housing boom, no crash and avoided recession, but our household debt is currently the highest of the 10 countries surveyed.
- 

This chapter presents an overview of changes in private rental housing systems in the 10 countries:

- Australia
- Belgium
- Canada
- Germany
- Ireland
- New Zealand
- Spain
- Sweden
- United Kingdom
- United States

The nine countries selected for analysis alongside Australia represent developed, market-oriented democracies and provide for a mix of different historic and recent experiences in housing provision and policy. Each of these countries has appeared in the international comparative literature, where some have an extensive record; all have their own bodies of research and information.

To guide our analysis, we asked experts in the international jurisdictions to complete a questionnaire about institutions and change in their respective PRSs. Model responses for Australia's PRS were also circulated to assist with the reporting and collation of survey responses in commensurable terms. The objective of the survey was to assemble broadly consistent information for comparative analysis on trends in PRS internationally; identify additional information resources; and identify themes in PRS institutional change for closer

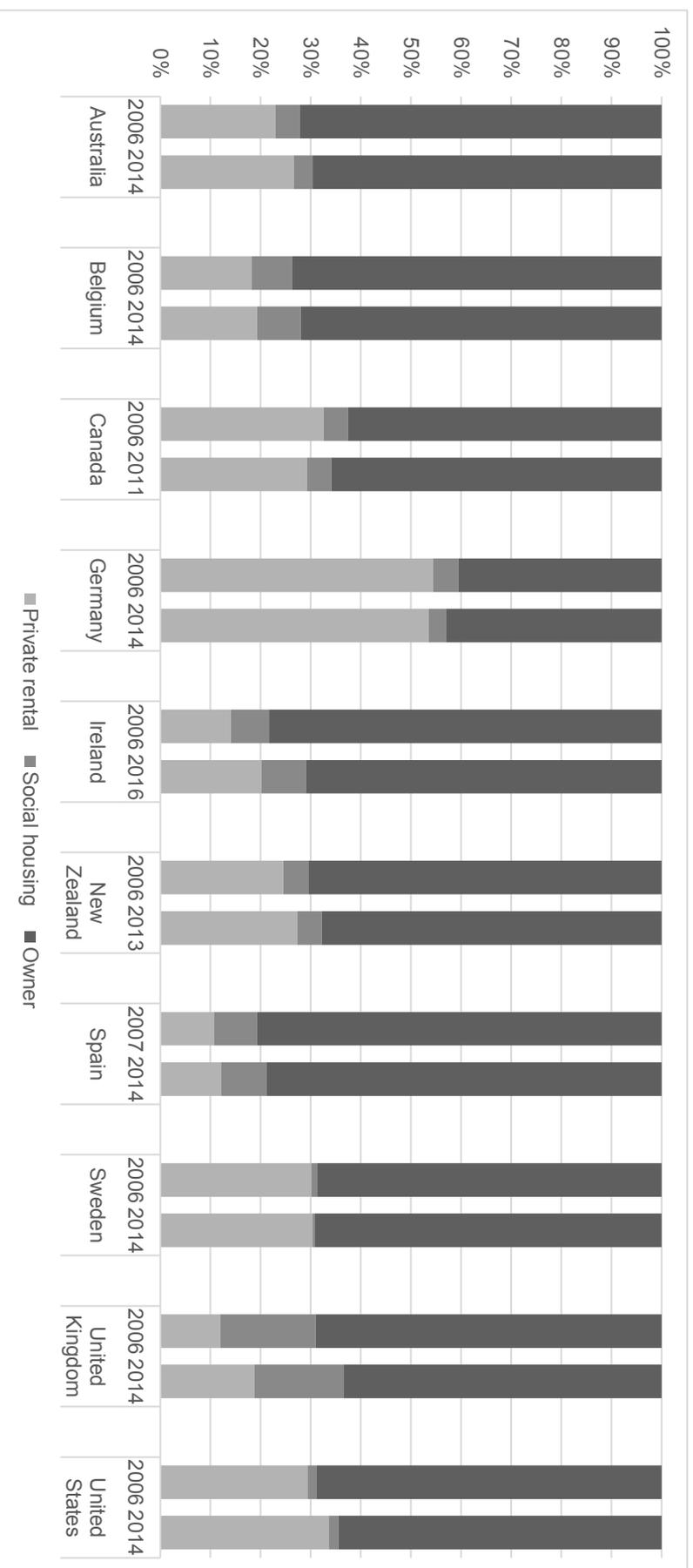
examination in the four focus countries: Germany, Ireland, the United Kingdom and the United States.

### **3.1 Private rental in the housing system**

#### **3.1.1 Private rental share of housing**

Figure 2 indicates the PRS share of each country's housing system and change over the past decade or so (periods vary according to data availability). In all countries except Germany, owner occupation is the majority tenure; however, in seven countries private rental housing is the growing tenure.

**Figure 2: Private rental housing and other tenures: Australasia, Europe, North America (select countries)**



Sources: ABS (2017a); CMHC (2014); Eurostat (2017); Kofner and Kemp (2014); Kirchner (2007); Statistics New Zealand (2014); Suttor (2016); US Census Bureau (2015).

As observed in Section 2.1.2, the PRS is considered and constituted differently across the 10 countries. For Australia we use the ABS definition of a 'private renter' household (see Section 1.3.1). The figures for Ireland, New Zealand and the United Kingdom are derived from national statistics which similarly distinguish rental housing where the landlord is a local authority or community organisation from other (private) landlords. The figures for Canada represent the total rental sector, less social housing dwellings as calculated by Suttor (2016). Similarly, the US figures are total rental, less public housing as provided by Schwartz. For Germany, the figures are for total rental housing, less 'social housing dwellings' as calculated by Kofner and Kemp (2014) and Kirchner (2007). It should be noted that many of these dwellings in Germany are owned by private individuals.

The data in Figure 2 for Belgium, Spain and Sweden are from Eurostat, which collects and presents comparative housing statistics across Europe. However, they differ from the data for other countries in two ways. First, the Eurostat figures refer to individuals, not households; secondly, the Eurostat figures refer to 'market rental' and 'below-market rental'. In Belgium and Spain these categories are approximate to social housing and private rental housing, respectively. Sweden, however, is different: almost all its rental housing is 'market rental' but a large part of the market is constituted by municipal housing companies which do not operate on a profit-maximising basis. Swedish 'market rents' are in fact set by a system of collectively bargained 'utility rents'.

Accepting these differences, we can see that the often-encountered view that 'everyone in Europe rents' is incorrect and that most of the European countries in our review have higher rates of owner occupation than Australia.

However, private rental is growing in most countries and over the past decade has mostly done so relative to owner occupation and, to a lesser extent, social housing. The most remarkable growth in private rental relative to owner occupation has been in Ireland and the United Kingdom, where the PRS grew strongly through the recent housing boom and bust phases experienced in those countries, and in the United States, where the PRS lost share to owner occupation through the housing boom but has lately grown rapidly. This growth in the United States includes the addition of former owner-occupiers who suffered foreclosure during the GFC bust. In Australia and New Zealand, neither of which experienced a housing bust, private rental has grown relative to owner occupation at a slower, steadier rate.

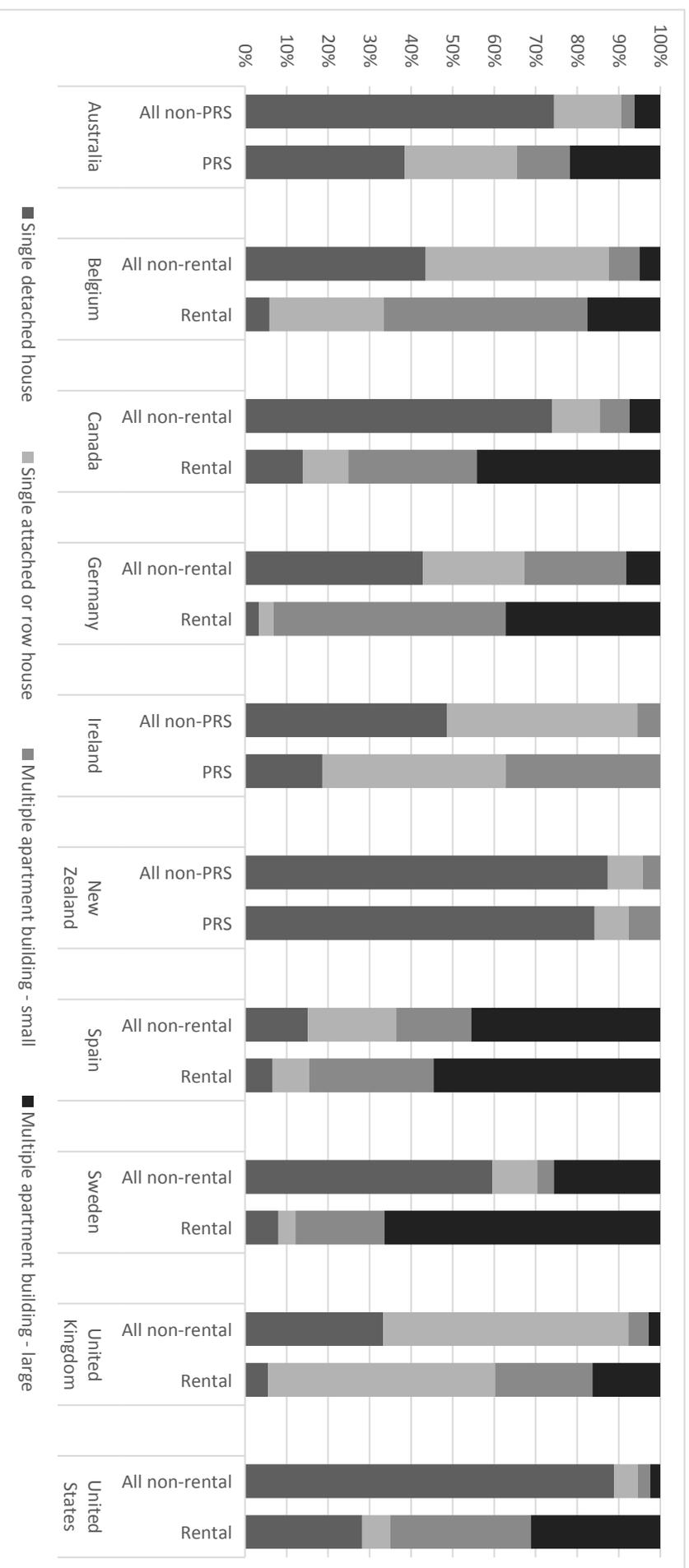
The PRS also grew relative to social housing in Australia, Germany, Sweden and the United Kingdom in different ways. In Australia, new social housing supply has fallen short of population growth with absolute losses in some jurisdictions. Social housing in the United Kingdom has undergone a similar decline. Germany, which had an extended period of little or no population growth, privatised much of the social housing owned by municipalities and allowed social housing subsidies to municipal housing companies and private landlords providers to expire (Lawson, Legacy and Parkinson 2016). In Sweden, in response to apprehensions about compatibility with European Union competition policy, municipalities have cut subsidy arrangements such as loan guarantees to the municipal housing companies, which are to operate on a more business-like basis (Holmqvist and Magnussen Turner 2013).

As we observed in Chapter 2, changes in housing assistance programs have also blurred the line between the sectors: these include the US Low-Income Housing Tax Credit (LIHTC) and, on a smaller scale, Australia's NRAS. Similarly, under Ireland's RAS, local authorities contract with private landlords to house persons in need of housing, with the authority determining allocations. Belgium's social rental agencies headlease private rental housing and sublet it to eligible clients (a mechanism similar to older community housing programs in Australia).

### **3.1.2 Private rental built form**

We can also consider the position of the PRS in terms of its built form. Figure 3 shows the profile of the built form of the PRS, or all rental (where the data do not distinguish the PRS), contrasted with other housing types, for each of the 10 countries.

**Figure 3: Private rental housing built form: Australasia, Europe, North America (select countries)**



Note: For Australia, Ireland and New Zealand, the data refer to private rental housing; for other countries, the data counts private rental and social housing together as 'rental'. All non-rental includes owner-occupied housing; 'all non-PRs' includes owner-occupied housing and social housing. For Australia, 'multiple apartment building—small' means units attached to shops and in buildings of 1–3 storeys; 'multiple apartment building—large' means units in buildings of 4 or more storeys. For Belgium, Canada, Germany, Spain, Sweden, the UK and the US, 'multiple apartment building—small' means units in multifamily buildings of 2–9 units; 'multiple apartment building—large' means units in multifamily buildings of 10 or more units. For Ireland and New Zealand, data for apartments cannot be split into smaller and larger buildings, so are counted together as 'multiple apartment building—small'. Australia and Ireland data is for 2016; Canada data is for 2011; New Zealand data is for 2001 (latest available); others for 2013.

Source: ABS(2017b); CMHC (2014); Eurostat (2017); Statistics New Zealand (2002); US Census Bureau (2015).

As Figure 3 indicates, the PRS profile tends towards apartments in most jurisdictions, but to different degrees in the represented countries. Australia stands out for having a relatively large representation of single detached houses in its PRS—only New Zealand is larger (note though that the New Zealand data, though the latest available, is old). More important, however, is how distinctive the PRS profile is within each country's housing system. The Australian PRS with its many houses looks more like the wider Australian housing system than does the PRS of most other countries. Spain, which has many apartments across its rental and owner-occupied sectors, and New Zealand, which has many detached houses across both sectors, are the most internally similar on this measure. The United Kingdom, which has many attached dwellings in both its rental and owner-occupied sectors, is also internally fairly similar. However, for Belgium, Canada, Germany, Sweden and the United States the profile of the PRS built form is quite different to that of the owner-occupied sector. In Canada and Germany, single dwellings are almost all in owner occupation and large apartment buildings almost all in rental.

Canada's distinctive profile is the historical result of it having had in the 1960s–80s a substantial 'purpose built rental' sector which might today be called 'build to rent'. These are multi-unit buildings, all rented, which now comprise slightly less than half the PRS throughout Canada and somewhat more than half in Canada's largest cities. Construction in this sector declined in the 1980s following the introduction of strata title and the exemption of owner-occupied housing from capital gains tax, which made condominium development more competitive. New construction has lately picked up but additions to the PRS now mostly filter from condominium apartments and detached housing that also trades in the owner-occupied sector.

In Germany and Sweden, a substantial part of new construction is specifically for private rental housing. In other countries, additions to the PRS stock come mostly from existing housing stock in other sectors—primarily ex-owner-occupied housing that filters into the PRS through sale or letting by owners and, to a smaller extent, from new construction marketed to both owner-occupiers and landlords. In the United States there recently has been a significant increase in the number of single detached dwellings shifting into the PRS through the purchase of properties subject to foreclosure. The public or social housing sector has also been the source of some private rental, particularly in Germany where municipal and state-owned industry housing was privatised from the late 1990s to the late 2000s, and in the United Kingdom where PRS stock came via 'Right to Buy' owner-occupiers (Copley 2014).

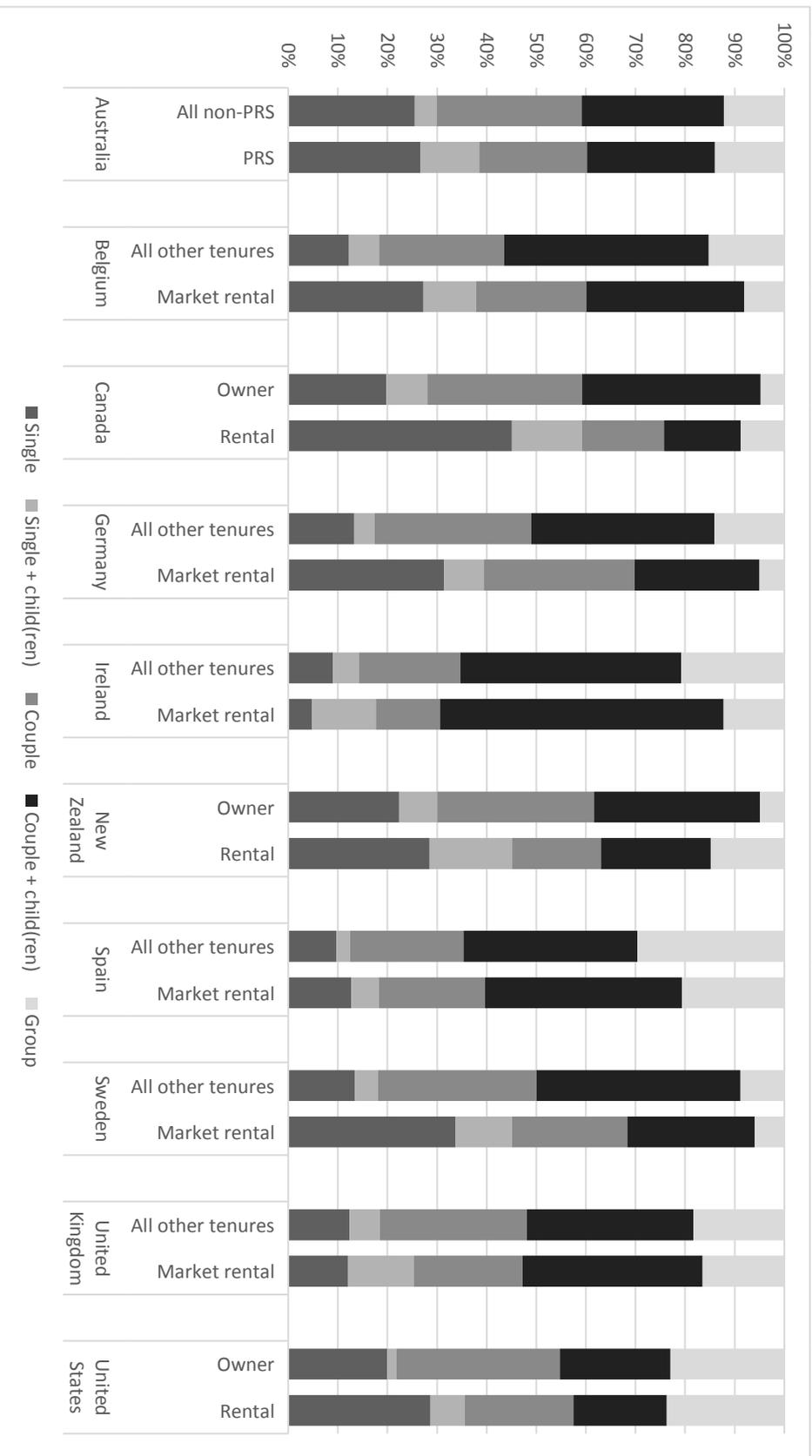
In our survey a number of respondents observed particular forms of segmentation and specialisation in their respective country's PRS. We observed, by way of example, the presence in some Australian states of residential parks or land lease communities where residents own a mobile or manufactured dwelling and rent the site on which it sits. Evident also as significant developments at the margins of the PRS was the emergence in some states of secondary dwellings ('granny flats'), new-built lodging and student accommodation. In most countries student accommodation is an increasing distinctive segment with distinctive practices around duration of agreements, specialist providers and built forms.

In Canada some provinces also have significant land lease communities, and in some Canadian cities secondary dwellings known as 'laneway houses' are a notable emerging segment. In the United States mobile dwellings or 'trailers' comprise 5 per cent of the total PRS. In the United Kingdom, lodging houses, known as Houses in Multiple Occupation (HMOs), are subject to specific licensing regimes, and in some large cities vacant residential and non-residential properties are being used for rental accommodation under 'property guardian' arrangements brokered by private companies (e.g. Camelot Europe, primarily in the UK but also operating in Ireland, Belgium and Germany).

### **3.1.3 Housing trajectories and the PRS**

Private rental's share of total housing and its built form profile is suggestive of the role it plays in each country's housing system and in the housing trajectories of tenants. In all countries rental housing tends towards singles with or without children. Figure 4 suggests that Australia's PRS household profile is less differentiated from other housing tenures in Australia than the respective household profiles in most of the reference countries. Germany, Sweden and Canada (where private rental and social housing are both incorporated under 'rental') have the most internally dissimilar profiles, with proportionally more single persons and fewer children in rental housing. This corresponds to the distinctive built form profiles of those countries. Ireland is notable for having a market rental profile in which children figure strongly.

**Figure 4: Household composition in private rental and other tenures: Australasia, Europe, North America (select countries)**

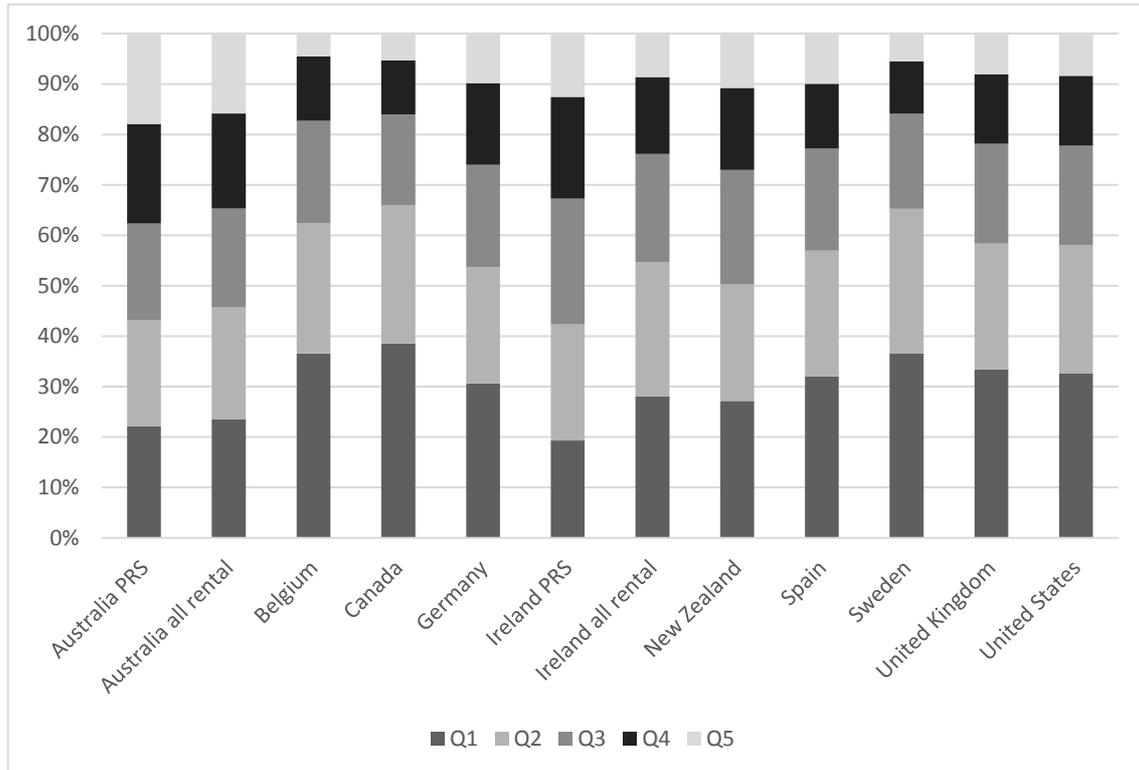


*Note: The New Zealand data are the latest available, but are old (2001).*

Sources: ABS (2017b); CMHC (2014); Eurostat (2017); Statistics New Zealand (2002); US Census Bureau (2015).

Rental housing in all countries tends also to be occupied by lower-income households (see Figure 5). Income quintiles across Australia’s PRS closely align with other rental tenures in Australia. Conversely, rental income quintiles in most other countries are more highly differentiated (though the data do not distinguish for most countries between private rental and social housing). In Belgium, Canada and Sweden, especially, few higher-income households (Quintiles 4 and 5) live in rental housing.

**Figure 5: Rental households by income quintile: Australasia, Europe, North America (select countries)**



Note: Q1 is the lowest quintile (20%) of households by income, Q2 is the second lowest, etc, and Q5 is the highest quintile.

Sources: ABS (2017a); Carliner and Marya (2016); CSO (2016); Statistics New Zealand (2014).

We asked survey respondents about the role of the PRS, noting in the case of Australia that private rental historically has been considered an intermediate tenure for new households on their way to owner occupation, but that this was changing as more households rented for longer. Respondents in Belgium, Canada, Ireland, New Zealand, the United Kingdom and the United States characterised the role of private rental housing similarly, with Belgian and Canadian respondents stressing the impetus towards owner occupation in those two countries. Respondents in Germany and Sweden, however, characterised private rental housing differently as an attractive sector that offered acknowledged benefits for households, particularly around security of tenure and certainty of housing costs.

The profiles presented in Figure 4 and Figure 5 indicate that a qualification must be added: renting may be attractive for certain types of households, but other types are more likely to satisfy their housing needs in owner occupation.

## 3.2 Policy governance

We can also think of the place of the PRS in terms of where it fits in relation to legislative responsibilities and policy governance across levels of government. As Table 1 shows, jurisdiction for taxation, rent subsidies and tenancy law differed between the countries, with responsibility for finance managed federally for all.

**Table 1: Policy governance: Australasia, Europe, North America (select countries)**

Country	Finance	Taxation	Subsidies	Tenancy law
<b>Australia</b>	National	National/state	National	State
<b>Belgium</b>	National	National/regional *	Regional	National/regional*
<b>Canada</b>	National	National/provincial	Provincial	Provincial/municipal
<b>Germany</b>	National	National/state	National/state	National/state/ municipal
<b>Ireland</b>	National	National	National/local authorities	National
<b>New Zealand</b>	National	National	National	National
<b>Sweden</b>	National	National	National	National
<b>Spain</b>	National	National	National	National
<b>United Kingdom</b>	National	National	National/devolved jurisdictions/local authorities	National/devolved jurisdictions
<b>United States</b>	National	National/state/ municipal	National/state/ municipal	State/municipal

*Note: \*Power devolved to regional governments in 2015, but regional governments have yet to fully replace national legislation.*

Source: survey responses

Of the 10 countries, 5 are formally federal states (Australia, Belgium, Canada, Germany and the United States); Spain and the United Kingdom have asymmetrically devolved power to some jurisdictions below the national level. All of the countries distribute responsibility for aspects of PRS-related policy over national and sub-national levels of government. Municipal or local government is particularly important in Canada, the United Kingdom and the United States, and is important in administering rent regulations in Germany.

Three countries—Belgium, Germany and the United Kingdom—have recently changed their respective distributions of policy governance responsibilities to devolve responsibility from the national level. Belgium’s regions have yet to assume all their new responsibilities and chart significantly new directions; this is starting to happen in the United Kingdom where Scotland, in particular, is formulating its own housing policies and legislation.

## 3.3 Wider contexts

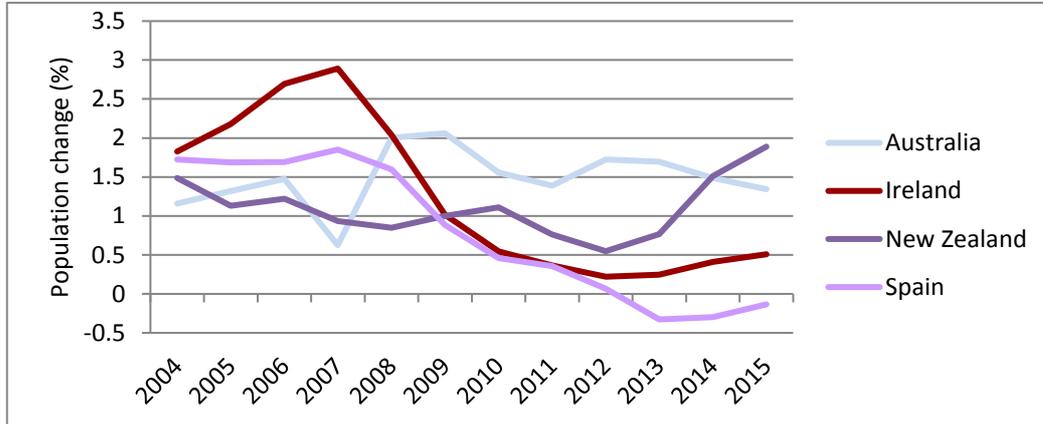
We have already observed some points where the PRS in different countries has been shaped by developments in wider contexts, such as housing market booms and busts, the GFC and ensuing recession and population change. We complete the sketch of these broader contexts

for each of the 10 countries, beginning with the high-level contexts of population and economy, then housing markets and household debt.

### 3.3.1 Population

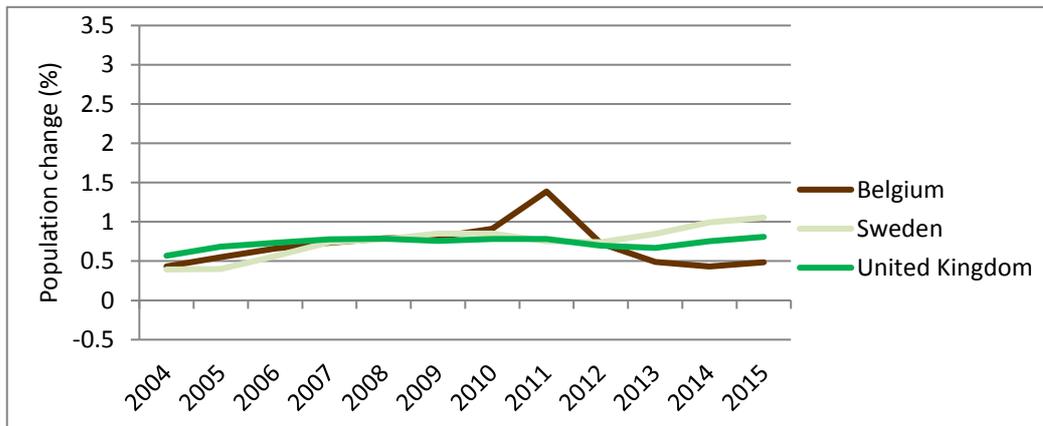
Rates of change in the population of each of the 10 countries over the past two decades (2004–15) are shown in Figures 6–8.

**Figure 6: Population change: Australia, Ireland, New Zealand and Spain**



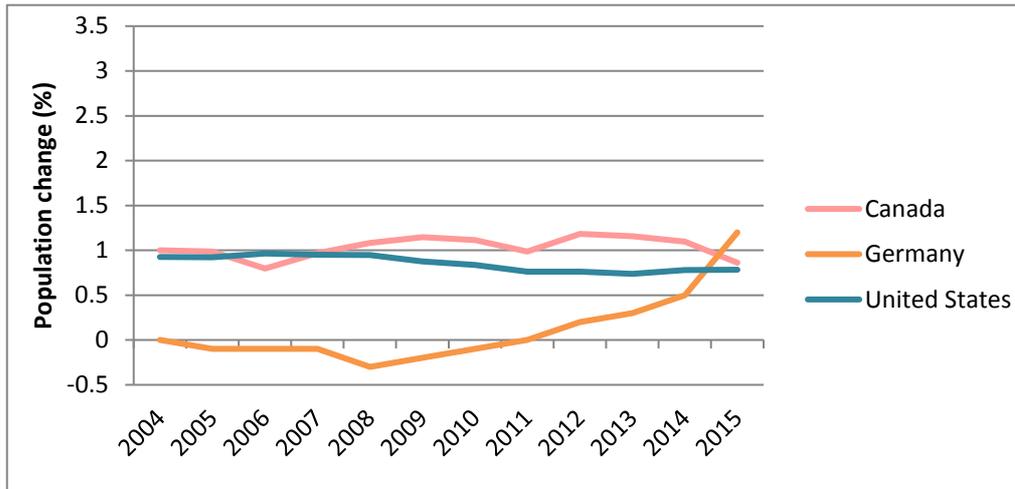
Source: World Bank (2017).

**Figure 7: Population change: Belgium, Sweden and the United Kingdom**



Source: World Bank (2017).

**Figure 8: Population change: Canada, Germany and the United States**



Source: World Bank (2017); Statistisches Bundesamt (2017).

Population growth is a basic, if often overlooked, factor in differences between housing systems. High population growth means that the housing system needs to continuously add new stock, which may have implications for the replacement of old stock; the investment of resources in new supply needs also to be financed and implemented. Volatility in rates of growth may pose challenges for the planning, financing and marketing of housing. All of these factors may have implications for the distribution of housing between sectors and between persons. Also, to the extent that population growth is underpinned by migration, there is a direct implication for the PRS because most migrants to a country contribute directly to PRS demand for at least an initial period following their arrival. A country with low or no population growth may have other problems, but it will not face the same degree of pressure for its housing system to perform effectively and equitably in this way.

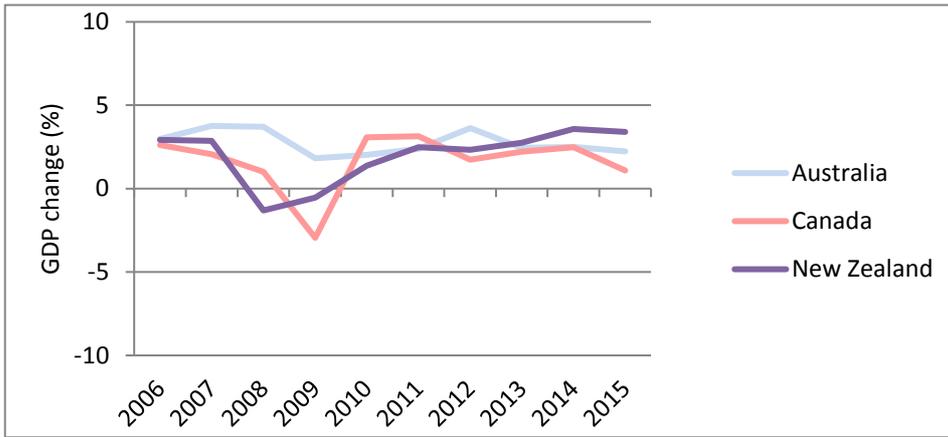
Over the past decade, Australia's population growth has been relatively high and somewhat volatile: less volatile than in Ireland and Spain, but more volatile than in Canada and the United States. Germany often stands out for its stable housing market and apparent equity between sectors. However, it is worth keeping in mind that until relatively recently it has performed this way without having to house a growing population. The humanitarian response in Germany to the refugee crisis of 2015 and beyond has begun to affect the market significantly.

### 3.3.2 Economy

A basic indication of each country's economic system and performance is given by changes in gross domestic product (GDP) (Figure 9, Figure 11 and Figure 13) and unemployment (Figure 10, Figure 12 and Figure 14). In housing system terms, these measures indicate how well a country's human and capital resources are being engaged in the production of goods and services for transaction, including housing construction and housing services. More particularly, the measures show how the 10 countries have fared over the course of the GFC and recession, the subsequent stimulus response of governments, and then, particularly in the Eurozone, the imposition of austerity.

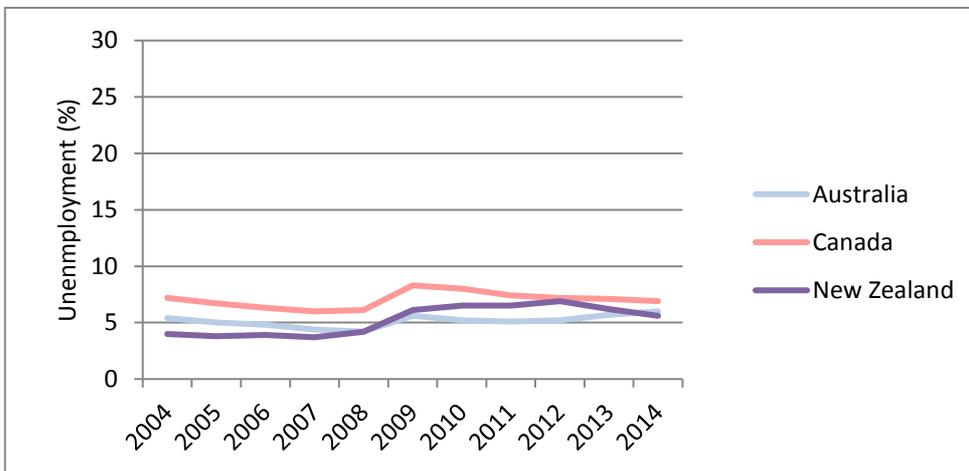
We should note a basic monetary difference here. 4 of the 10 countries (Belgium, Germany, Ireland and Spain) are members of the Eurozone and do not issue their own currency. They operate under a central bank that was not established with the same lender-of-last-resort functions as other national central banks. For Ireland and Spain this has hampered their ability to stimulate their economies and reduce unemployment in the wake of the GFC.

**Figure 9: GDP % change, 2006–15: Australia, Canada, New Zealand**



Source: World Bank (2017).

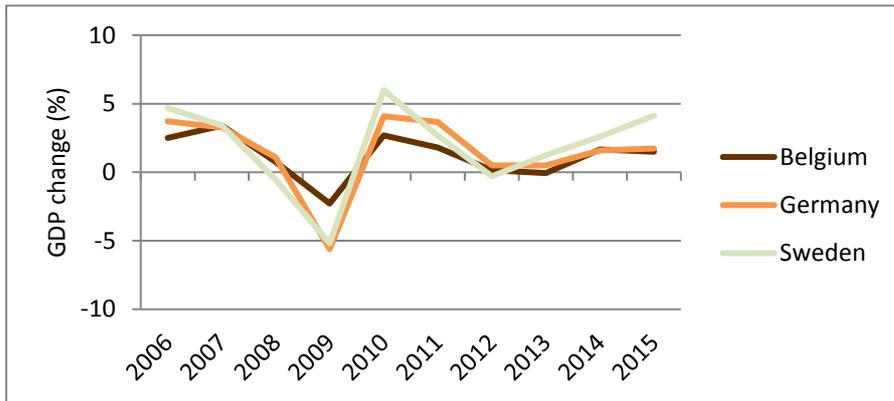
**Figure 10: Unemployment %, 2004–14: Australia, Canada, New Zealand**



Source: World Bank (2017).

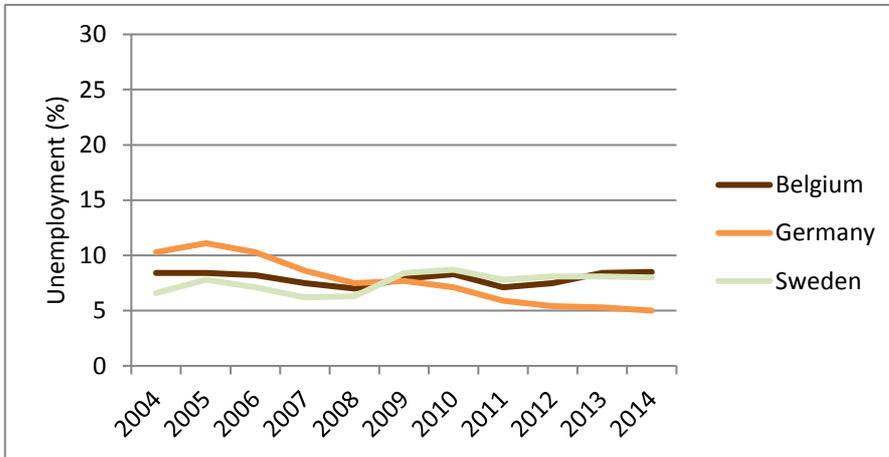
Australia was the only country among the 10 (and indeed of developed countries more widely) that did not experience a loss of economic output following the GFC. It was assisted in this by high population growth, although unemployment has been drifting up. The GFC and ensuing recession were felt more gravely in the United States and Europe. The flatlining of GDP in 2012 for Belgium, Germany and Sweden (Figure 11) is indicative of a second recession, with unemployment hovering at around 8 per cent in Belgium and Sweden (Figure 12).

**Figure 11: GDP % change, 2006–15: Belgium, Germany, Sweden**



Source: World Bank (2017).

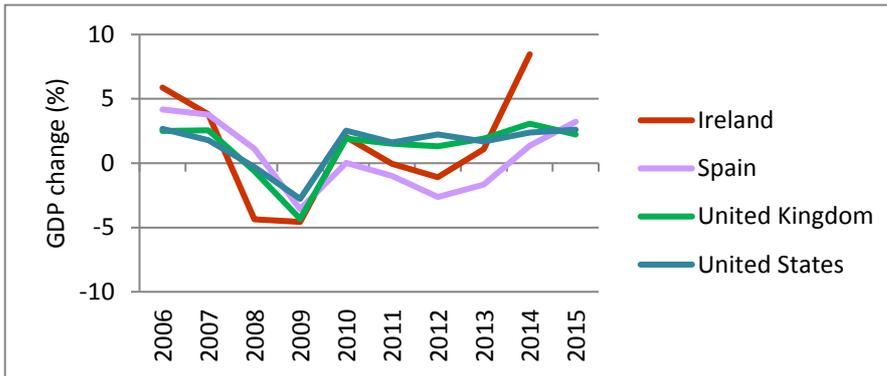
**Figure 12: Unemployment %, 2004–14: Belgium, Germany, Sweden**



Source: World Bank (2017).

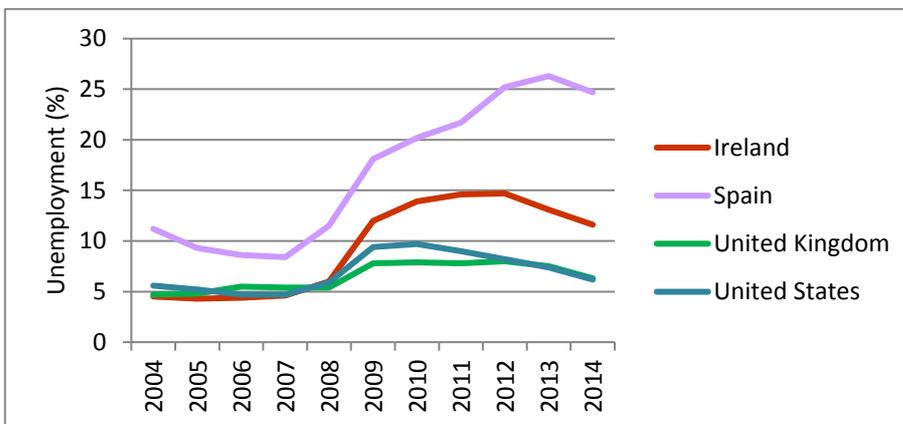
The most dramatic impacts of the GFC were felt in Ireland, Spain, the United Kingdom and the United States, where each experienced the collapse of financial institutions and a sharp recession (Figure 13). The United Kingdom and United States have recovered a low level of growth since that time, avoiding the Eurozone's second recession. However, the loss of output and high unemployment was persistent in Ireland and, especially, Spain (Figure 14). The more recent high rate of GDP growth in Ireland is the result of a few large transfers of domicile of multinational corporation assets.

**Figure 13: GDP % change, 2006–15: Ireland, Spain, United Kingdom, United States**



Source: World Bank (2017).

**Figure 14: Unemployment %, 2004–14: Ireland, Spain, United Kingdom, United States**

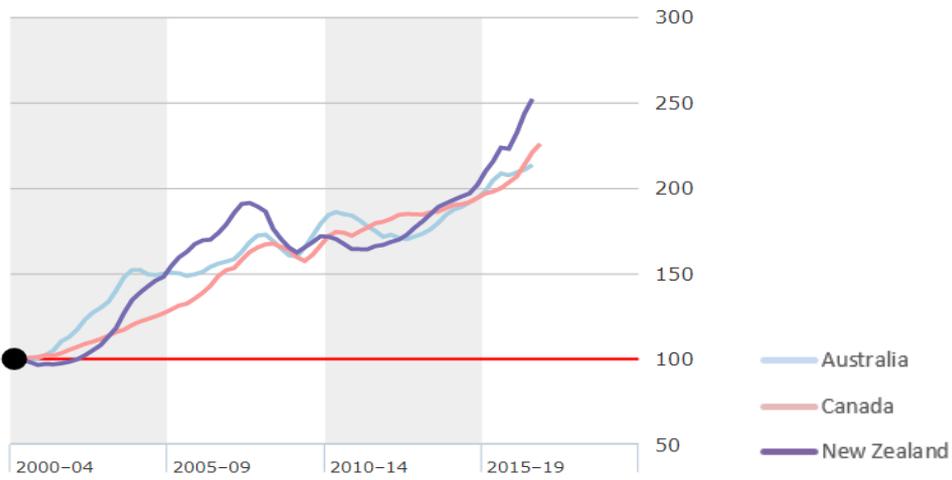


Source: World Bank (2017).

### 3.3.3 Housing markets

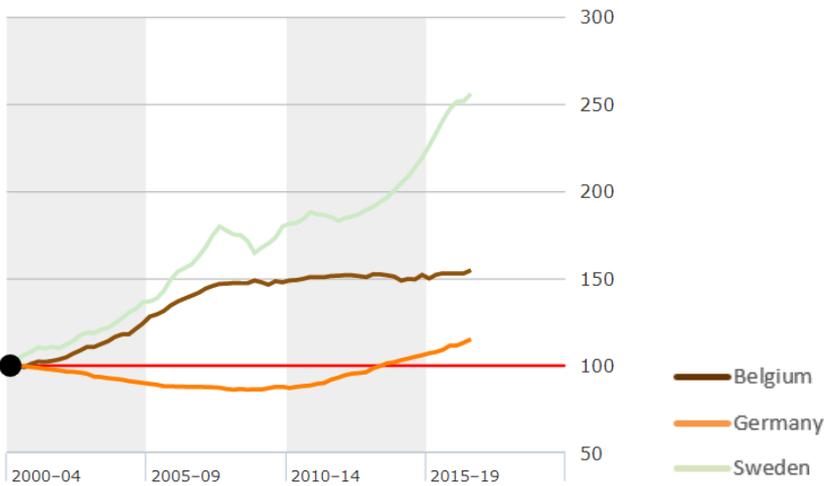
Indices of real house prices for the 10 countries since the turn of the century are presented in Figures 15–17. In all the countries except Germany real house prices rose. After the GFC, house prices faltered then rose again in Australia, Canada, New Zealand and Sweden. House prices crashed in Ireland, Spain, the United States and, to a lesser extent, the United Kingdom. Over the most recent five years, house prices have risen in all 10 countries including Germany, but only slightly in Belgium.

**Figure 15: Real house price index—Australia, Canada, New Zealand**



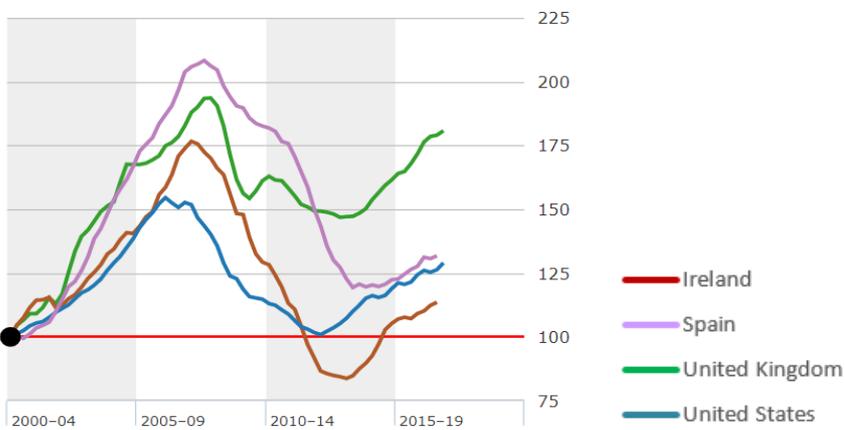
Source: The Economist (2017).

**Figure 16: Real house price index: Belgium, Germany, Sweden**



Source: The Economist (2017).

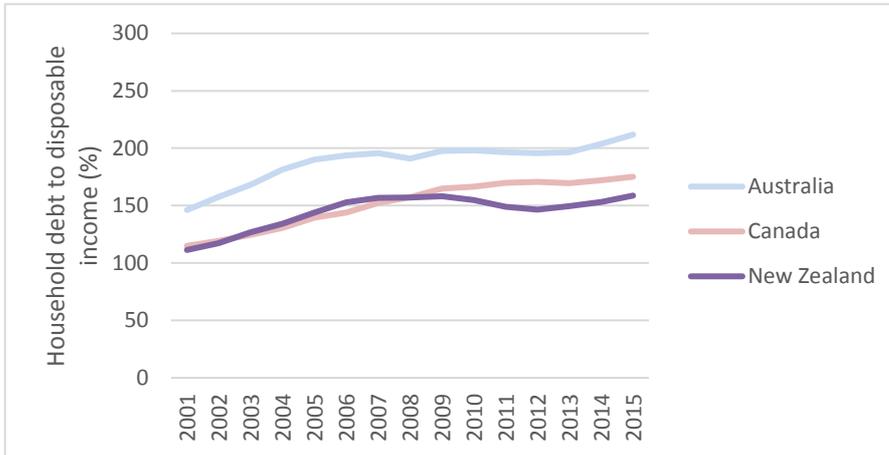
**Figure 17: Real house price index: Ireland, Spain, United Kingdom, United States**



Source: The Economist (2017).

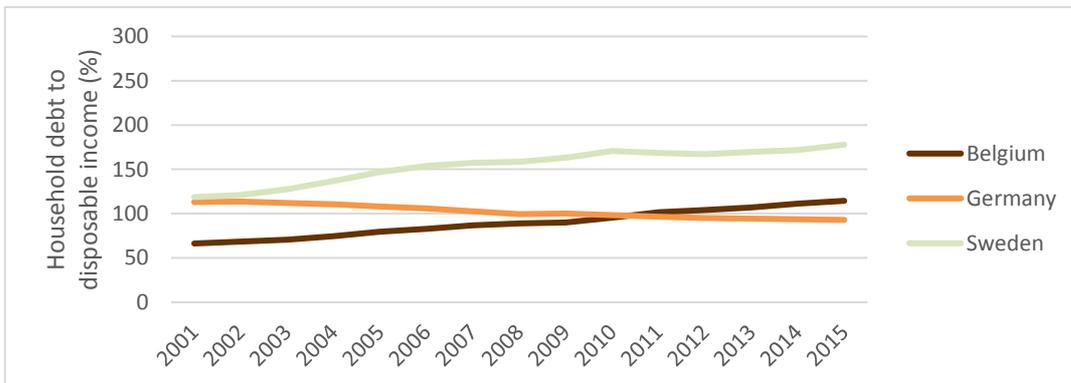
Finally, we consider debt levels in each of the 10 countries—in particular, the level of debt carried by households that are the primary buyers of housing assets both for owner occupation and private rental (this is discussed further at 4.3.1). Figures 18–20 show household debt relative to household disposable income.

**Figure 18: Ratio of household debt to annual disposable income: Australia, Canada, New Zealand**



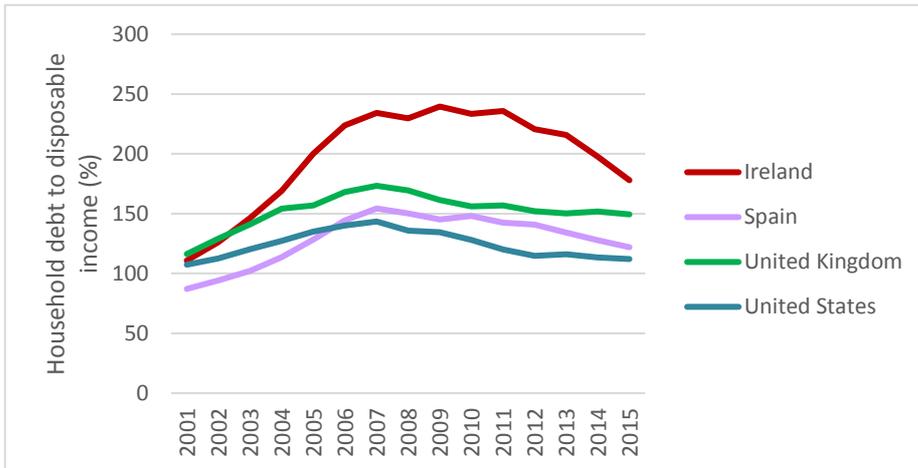
Source: World Bank (2017).

**Figure 19: Ratio of household debt to annual disposable income: Belgium, Germany, Sweden**



Source: World Bank (2017).

**Figure 20: Ratio of household debt to annual disposable income: Ireland, Spain, United Kingdom, United States**



Source: World Bank (2017).

Prior to the GFC, households in all countries except Germany were increasing their leverage. Since then, those in Australia, Canada, New Zealand, Sweden and, off a lower base, Belgium have continued to do so. Ireland, Spain, the United Kingdom and the United States have had reduced household leverage since the GFC, but ratios remain higher than at the turn of the century. Australian households now have the highest debt to income ratio of the 10 countries, a ratio surpassed only by Ireland at the height of the pre-GFC boom and in the years immediately following the GFC when the reduction in incomes also kept the ratio up.

### 3.4 Key findings

- In 9 of the 10 countries private rental housing is the second largest tenure after owner occupation; only in Germany is the PRS larger. However, in seven of those countries, the PRS share is growing, mostly at the expense of owner occupation.
- In most countries, the PRS is characterised by apartments, smaller households and lower incomes. However, the degree of difference between the PRS and the wider housing system varies between countries. In Australia, the dwellings and households in the PRS are more representative of the wider Australian housing system than those in most other countries.
- Wider system contexts such as population growth, economic growth, house prices and household debt levels vary across the countries. Germany stands out for its extended period of stable house prices; other countries have had booms, and some booms and busts. In all countries house prices are currently rising.
- Australia has had a housing boom, no crash and avoided recession, but our household debt is now the highest of the 10 countries. Australian housing policy discussions are usually directed to improving affordability; it would be wise to think also about how to conduct equitable housing policy in a post-crash market.

## 4 International change in PRS market and policy settings

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- Across the 10 countries, housing investment is mostly financed by credit, and housing credit is mostly provided by banks. Over the past two decades, housing credit has expanded with the development of new funding sources. Following the GFC, nine countries have implemented housing-specific macroprudential tools as a financial stability measure.
  - In those countries most affected by the GFC, government programs for the disposal of impaired property-related assets have significantly increased the position of large corporations in the PRS, both directly as landlords (as in the United States) and indirectly as owners of loans with PRS properties pledged.
  - Looking at the range of tax settings applicable to housing and the PRS, we find some surprising results. For example, both Australia and Germany exempt owner-occupied housing from capital gains and provide for negative gearing on similar terms. Yet their treatment of negative gearing and capital gains tax underlie quite different housing market outcomes: speculative inflation in Australia; relatively steady housing prices in Germany.
  - In nine countries, smallholding private individuals are the predominant type of landlord. But most countries also have some large corporate landlords (LCLs) and a few have recently seen rapid growth in very large new LCLs.
  - The origins of LCLs are diverse, but their recent activity has been facilitated by government programs: in Germany, municipal housing privatisation; in the United States and Ireland, post-GFC programs for the disposal of impaired assets.
  - There are various regimes for regulating rent increases, security against landlord termination and (less commonly) rents for new tenancies. There is also some innovation around the use of registers of landlords.
- 

Taking a broad view of ‘institutions’ in the PRS, our discussion of the survey responses and other sources is arranged according to the following themes:

- financial settings, including housing credit, taxation and subsidies
- landlords and managers
- regulation—particularly regarding security, rents and registers.

### 4.1 Financial settings

In this section we consider the institutional arrangements around paying for private rental housing, as regards the landlords who own it and the tenants who rent it. To this end we first review the market conditions and regulatory settings around the provision of credit for PRS and other housing investment. Next we consider the tax settings which influence whether and how

an individual may take a position in the housing market. Finally, we review the subsidies that some tenants may receive towards the rent.

#### 4.1.1 Credit settings

Across the 10 countries housing investment is mostly financed by credit, and housing credit is mostly provided by banks (i.e. credit-providers that also take deposits and operate payments). The United States has lately become an exception with non-bank lenders overtaking the historically dominant banks (Lux and Greene 2015; Lerner 2017). Table 2 shows two sets of settings around housing credit: sources of finance and funding; and macroprudential regulations that relate specifically to housing credit. These settings have seen recent changes which are discussed further below. More generally, housing credit has been undergoing profound transformation for more than two decades—a period punctuated by the GFC in 2008.

**Table 2: Housing credit settings: Australasia, Europe, North America (select countries)**

Country	Sources of finance and funding	Housing-related macroprudential regulation
Australia	Mostly banks, funded by deposits, wholesale lending, some MBS, very small covered bond Some non-bank lenders	Limit on growth in investor lending (10% p.a.) Serviceability buffers IO loans not more than 30 per cent of new lending, IO loans with LVR>80 per cent subject to special scrutiny, IO repayment plans
Belgium	Mostly banks (95%), funded by deposits, some covered bonds	Increased risk weight for housing loans
Canada	Mostly banks (88%), funded by deposits, wholesale lending, MBS	80 per cent LVR for landlords 2 per cent interest buffer No LMI on >\$1 million properties
Germany	Mostly banks (96%), funded by deposits, covered bonds, some wholesale lending Some private equity and capital raising (LCLs)	Provision for LVR ratios and limitation of repayment periods, not yet implemented
Ireland	Mostly banks, funded by deposits, some MBS, some covered bonds Some private equity and REITs	LVR 70% for landlords Loans with LTI>3.5 limited to <20 per cent of new lending 2 per cent interest buffer
New Zealand	Mostly banks (98%), funded by deposits, wholesale lending, MBS	Loans with LVR>60 per cent limited to 5 per cent of new lending to landlords
Sweden	Mostly bank-owned mortgage credit institutions (75%) or banks (25%), funded by covered bonds	LVR 85 per cent; amortisation requirement: >1 per cent each year, 50 per cent LVR after 5 years
Spain	Mostly banks (85%), funded by deposits, MBS, covered bonds Some private equity	–
United Kingdom	Mostly banks (91%), funded by deposits and wholesale lending, some MBS Some private equity and REITs	Repayment plan for IO loans Loans with LTI>4.5 limited to <15 per cent of new lending

Country	Sources of finance and funding	Housing-related macroprudential regulation
United States	Banks (about 50%), funded by deposits, wholesale lending, MBS Non-banks (about 50%), funded by MBS Some private equity and REITs, funded by wholesale lending, MBS and RBS	Ability to repay test and rules for qualifying mortgages: 80 per cent LVR, LTI ratios; rate bands.

Notes: IO = Interest only; LCL = Large corporate landlord; LMI = Lenders mortgage insurance; LTI = Loan-to-income ratio; LVR = Loan-to-valuation ratio; MBS = Mortgage-backed security; RBS = Rental-backed security; REIT = Real estate investment trust.

Sources: Australian Prudential Regulatory Authority (2017); CFPB (2014); European Mortgage Federation (2016); Reserve Bank of New Zealand (2017).

### **Credit settings pre-GFC**

In order to understand the post-GFC changes, we need to review the changes which preceded it. Prior to the GFC, credit provision for housing investment expanded in all of the countries except Germany, though with different starting points and growth trajectories (Lunde and Whitehead 2016: 36). One aspect of the expansion was innovation in funding for lending: that is, the monies required by banks to back the liabilities created when they advance credit to borrowers. Aside from their own capital, banks in most of the 10 countries had relied historically on the deposits of savers to fund their liabilities (this was particularly the case in Australia, Belgium, Ireland and New Zealand). In Europe, banks could also obtain funds from the issuance of covered bonds: that being, bonds backed by specified pools of mortgages pledged by banks. In the United States and Canada there has also been for decades bank funding through secondary mortgage markets in which rights to borrowers' interest and principal payments and the risk of default are pooled into mortgage-backed securities (MBS) and sold to investors. Unlike other means of loan funding, mortgage securitisation transfers the risk of default away from the original lender to the holder of the security, which improves the lender's risk-profile and hence ability to access more funding.

In the 1990s and 2000s these sources of bank funding were augmented by greater use of mortgage securitisation, especially by US banks and by banks in countries where it had not previously been used, such as Australia, Ireland and the United Kingdom. Funding was also augmented by wholesale lending to banks by non-bank financial institutions in international money markets ('shadow banking'). These developments were linked as mortgage securities became an important form of collateral in the shadow banking system (Blyth 2014). Mortgage securitisation also enabled non-bank institutions to become providers of housing credit by opening up competition with banks, and enabled banks to compete by becoming securitisers with lower interest rates and larger loans.

Lenders also expanded markets for housing credit, including home loans for owner occupation by persons previously considered not credit-worthy ('sub-prime' lending), equity release loans for existing owner-occupiers (for consumption and for investment) and loans for PRS investment. In Ireland and the United Kingdom, in particular, 'Buy To Let' mortgages were an innovation of the 1990s; in other countries such as Australia, where lending for PRS investment was already established, the scale of lending increased.

The design of mortgage securities—bundled from loans made in diverse housing markets—was thought to reduce the risk of default. However, the expansion they enabled in housing-related credit and house prices in fact increased the correlation of markets. When US house prices slowed in 2007 default risks rose and mortgage securities lost value as collateral, leading to a

run on the shadow banking system and the international collapse of wholesale lending to banks—the 2008 GFC.

The immediate impacts of the GFC varied across countries. Some significant banks and other financial institutions collapsed, while others in Ireland, Spain, the United Kingdom and the United States were nationalised or placed under state administration. Yet others in those countries and in Australia and New Zealand continued with the support of government guarantees over wholesale funding, central bank loans and government purchases of assets, including new mortgage bonds (Blyth 2014; Murphy 2011).

### ***Credit settings post-GFC***

In the period after the immediate emergency, we can observe further developments in three types of credit settings that are significant for housing and the PRS. First, in those countries worst hit by the GFC—in particular, Ireland, Spain, the United Kingdom and the United States—government programs were established to acquire impaired assets and dispose of them so as to avoid fire sales and put a floor under values (Byrne 2016; Beswick, Georgia et al. 2016). In Ireland, Spain and the United Kingdom, special asset management companies were established by their respective governments to hold the impaired assets of nationalised or administered financial institutions. In Ireland and the United Kingdom these included loans with residential properties pledged as security. In Spain they also included some actual properties that had been foreclosed. These assets were subsequently packaged and sold to large corporations, thereby creating a new sector of LCLs (Beswick, et al. 2016; Byrne 2016).

Similarly, in the United States, where the heavy use of foreclosure generated large inventories of real estate owned (REO) properties, the Federal Housing Finance Agency implemented a 'REO-to-Rental' pilot program of bulk sales to LCLs; since then bulk sales have continued outside the program (Fields 2014; Raymond et al. 2016: 4). One entity, the Blackstone investment group, has acquired substantial private rental portfolios in Ireland, Spain and the United States (Fields 2014; Beswick, et al. 2016). We discuss these landlords further in Section 4.3.

Secondly, most countries, not just those worst affected, have added to their regulation of bank credit provision generally and housing credit provision in particular. What might best be described as a slight change follows from the post-GFC revision of banking standards by the Basel Committee on Banking Supervision (Basel III), which requires somewhat higher ratios of capital in bank funding but still much less than typical capital ratios in other sectors and in banking historically (Admati and Hellwig 2013; Admati 2016). Banks therefore continue to be funded very largely by debt, if with some shift in composition with deposit funding having increased and the use of mortgage securitisation reduced but remaining significant.

Regulators in most of the 10 countries have also adopted various 'macroprudential tools' which specifically apply to bank provision of housing credit including PRS investment, as indicated in Table 2. Common tools include limitations on loan-to-valuation ratios (LVRs), as applied in Canada, Ireland, New Zealand and Sweden. In the former three countries, LVR limits are more stringent for landlords than owner-occupiers; in Sweden, the initial LVR limitation is combined with a requirement that the LVR after five years of the loan is reduced to 50 per cent (i.e. an amortisation requirement). Spain has not implemented housing-related macroprudential tools, because new lending for housing remains at a fraction of pre-crash levels; nor has Germany, though it has recently legislated to give its regulator power to implement macroprudential rules, including a maximum LVR, for housing-related loans (*Finanzaufsichtsergänzungsgesetz*).

In the United States, similar regulations have been made within the framework of the *Dodd-Frank Wall Street Reform and Consumer Protection Act 2010*. The Act requires lenders to assess a borrower's ability to repay and presumes compliance with the requirement where loans satisfy certain rules for 'Qualifying Mortgages' (including a debt-to-income ratio) and are

not 'higher-priced' (i.e. are proximate to prime mortgage rates). The effect is to encourage, rather than prescribe, lending to the standards (CFPB 2014). The question of how macroprudential tools shape the strategies and practices of PRS investors, as distinct from their effect on the financial position of banks, needs to be investigated further.

Thirdly, there have been developments outside the banking sector. At the retail level, banks mostly continue to dominate lending, and immediately after the GFC many banks extended their share as non-bank lenders left the market. Lately, however, non-bank lenders have increased their market share in Canada (Coletti, Gosselin and MacDonald 2016) and, especially, the United States. Blackstone, in addition to operating a private rental housing business of its own, also offers mortgage securitisation-funded finance to other investors in rental housing portfolios of 5–1000 properties (Fields 2014: 6). Blackstone and other LCLs have also accessed funding by securitising the rental revenues of parts of their portfolios (Fields 2014; Fields, Kohli and Schafran. 2016; Layton 2015). The first rental-backed security was issued by Blackstone in November 2013. In the following 18 months, a total of eight firms issued 21 securitisations (Fields, Kohli and Schafran. 2016).

REITs are also emerging as an important funding mechanism for rental housing investment. Used for decades in the Australian and US commercial property sectors, REITs are vehicles for the ownership of large portfolios of properties in which investors buy units that entitle them to receive rent and other revenue. REITs are restricted from retaining revenues and from some trading activities (restrictions vary between countries). Property revenues are taxed lightly or not at all at the level of the REIT, the rationale being that property revenues flow through the REIT to investors, at which level they may be taxed. For some years REITs have operated in the US 'multifamily' (apartment) rental housing sector, but have not been significant in PRSs in other countries (Newell et al. 2015). Over the past decade most of the 10 countries have either introduced regimes for REITs or reformed existing regimes; we discuss some of these in the next section on tax settings.

## **4.2 Tax settings**

Table 3 and Table 4 summarise a range of tax settings relevant to housing and the PRS in the 10 countries. The settings are selected for their ability to affect behaviours in the PRS, rather than the size of the revenues raised relative to other taxes. In Table 3, we also show settings that relate to owner-occupied housing, which are relevant to the PRS to the extent that assets held in one sector may be transferable to the other sector, and hence may be valued in light of the tax treatment they would receive in the other sector.

**Table 3: Tax settings, PRS and owner-occupied: Australasia, Europe, North America (select countries)**

Country	Owner-occupied		Landlord	
	Interest deductibility	Capital Gains Tax	Interest deductibility	Capital Gains Tax
Australia	No	No	Yes, including against other income (negative gearing)	Yes, 50 per cent discount if held >1 year; exempt if previously the landlord's own residence and rented for less than six years; also exempt if purchased prior to 1985
Belgium	Yes, varies by region and date of loan	No	Yes	Yes, but exempt if held >5 years
Canada	No	No	Yes, including against other income, subject to 'reasonable expectation of profit'	Yes, 50 per cent discount
Germany	No	No	Yes, including against other income (negative gearing)	Yes, but exempt if held >10 years and if the landlord is not a 'regular seller'
Ireland	Yes, for loans taken 2004–12 and at reduced rate	No	Yes, at reduced rate (moving to full deductibility)	Yes, but relief for properties bought 2012–14 and held >7 years
New Zealand	No	No	Yes, including against other income (negative gearing)	No
Sweden	Yes	Yes, at reduced rate, subject to deferral	Yes, including against other investment income (limited negative gearing)	Yes, at 30 per cent rate (same as rental income)
Spain	Yes, for loans prior to 2013 and subject to eligibility	Yes, subject to exemptions, deferral	Yes, but not to make a loss	Yes, subject to indexation
United Kingdom	No	No	Yes, at reduced rate	Yes
United States	Yes	Yes, subject to exemptions, deferral	Yes, including against other passive and, in some cases, active income (limited negative gearing)	Yes, discount (up to 57%) if held more than 1 year

Source: survey responses; Bááth (2015); CMHC (2017); Cornelius and Rzezniak (2015); Hafner and Bounjounh (2015); James (2014); Jordan (2015a, 2015b); Orji and Sparkes (2015); Roig (2015)

In Australia, where housing assets trade relatively readily across the sectors, the configuration of tax settings across the sectors is considered to be a powerful driver in housing system dynamics. In particular, the exemption of owner-occupied housing from capital gains tax encourages households to spend on owner-occupied housing, with untaxed home equity also a means for established owner-occupiers to access additional credit for investment. At the same time the deductibility of investment costs, primarily interest and depreciation, gives purchase for investment an advantage over purchase for owner occupation in terms of cash flow and hence debt serviceability. A further differential is the lighter rate of tax applied to capital gains relative to other incomes, including income from work and rents. The result is a substantial advantage and encouragement for established owner-occupiers to also become landlords and to prioritise capital gains rather than net rental income.

Tax settings differ across the PRS and owner-occupied sectors in all 10 countries. Generally, PRS housing is taxed as a capital asset: that is, subject to tax on income including capital gains, net of current costs such as interest, management expenses and depreciation. In seven countries, including Australia, there is no capital gains tax on owner-occupied housing (though in the case of New Zealand, there is no capital gains tax at all). In five of the countries there is also no deductibility of mortgage costs for owner-occupiers. This may be said to reflect a principle of treating owner-occupied housing as a consumer good that does not yield a taxable income and which must be paid for out of after-tax income. The inclusion of land in the good, and the acknowledged purpose of owner-occupied housing as a store of value, makes the principle dubious. However, treatment of owner-occupied housing as an investment good is not straightforward either.

Three countries currently allow mortgage interest deductibility for owner-occupiers as well as taxing owner-occupiers' capital gains: Spain, Sweden and the United States. Both Spain and Sweden apply limits: in Spain, for loans taken prior to 2013, 7 per cent of interest costs may be deducted subject to eligibility requirements. However, there is no deductibility for more recent loans. Spain also provides for a degree of equivalence in treatment with renters, for whom a portion of rental costs is also tax deductible. In Sweden, 30 per cent of mortgage interest is deductible. In the United States, all interest on loans to \$1 million is deductible (Internal Revenue Service 2016). As regards capital gains tax, each of Spain, Sweden and the United States provide for exemptions and deferrals, particularly where the vendor buys another home (Pareja-Eastaway and Sanchez-Martinez 2014: 91).

The two countries that do not pair settings in relation to owner-occupier mortgage deductibility and capital gains are Belgium and Ireland. However, these are exceptional only to a limited degree. Neither country taxes owner-occupied capital gains; however, in Belgium mortgage interest relief (*Woonbonus*) is provided by the regions at various capped amounts, while Ireland provides for mortgage relief only on loans taken out 2004–12 and the deductibility is being phased out.

As regards the PRS, Table 3 (above) shows that there is considerable variation between countries regarding the details of both the taxation of capital gains and the deductibility of costs. As noted above, New Zealand does not tax capital gains from any asset; Belgium and Germany exempt PRS investments held for more than five and ten years respectively. Like Australia, Canada, Ireland, Spain and the United States tax capital gains at lighter rates than other forms of income. Sweden also taxes capital gains lightly compared to wages, but at the same rate as rental income. Spain applies indexation to capital gains tax and discounts income tax on rents by 60 per cent. Prior to 2015, Spain allowed a discount of 100 per cent if the tenant was aged 18–30 years and below an income threshold (Roig 2015: 62).

Of particular interest is the treatment of negative gearing: that is, where interest and other costs result in net rental losses that are set against other income. Australia's system of allowing rental losses to be set against non-rental income is often thought to be extraordinary, if not unique.

However, both Germany and New Zealand have similar provisions. Three other countries provide for rental loss offsetting subject to limitations. In Canada, rental losses may offset other income where the investment is undertaken with a 'reasonable expectation of profit'. This means that continuous rental losses are generally not allowed to be offset against other incomes. In Sweden, rental losses may be set against other investment income but not wage income (a similar setting to the negative gearing reform recently proposed by the Australian Labor Party). In the United States, rental income is generally considered passive income and losses are set against other passive income only. However, where the landlord is actively involved in selecting tenants and managing the property, rental income may be considered active income and losses set against all other income, including wages (Oxley, Lishman et al. 2010; Internal Revenue Service 2017).

Table 4 shows a selection of other tax settings relating to property generally, and the PRS in particular.

**Table 4: Tax settings, PRRS and property: 10 countries**

Country	Property tax	Transfer duty	Landlord building depreciation	REITs
Australia	Land value tax varies by state, progressive rates 0–3 per cent, some surcharges for vacancies and foreign owners, owner-occupiers exempt; also local council rates	Varies by state, progressive rates 0–7 per cent	Rate varies by purchase date, mostly 2.5 per cent	Affordable rental housing provisions proposed 2017
Belgium	Immoveable withholding tax varies by region, 1.25–2.5 per cent of cadastral income (deemed rental value)	Varies by region, 10–12 per cent	3 per cent	Reforms 2014
Canada	Local property tax; includes improvements; some surcharges for vacant properties and foreign owners	Varies by province, mostly 1–3 per cent, 15 per cent surcharge on foreign buyers in Vancouver	Rate varies by purchase date, mostly 4 per cent, but not to make a loss	Regime introduced 2007
Germany	Property tax, includes improvements, varies by state and municipal ‘multiplier’, average 1.54 per cent	Varies by state, 3.5–6.5 per cent	Varies by age of building, 2 per cent or 2.5 per cent	Regime introduced 2007; allows investment in post-2007 properties only.
Ireland	Local property tax; includes improvements	Progressive rate 1–2 per cent	No	Regime introduced 2013
New Zealand	Local rates on occupied dwellings, includes improvements	None	No	General trust provisions
Sweden	Municipal property fee includes improvements, exemptions for new developments; state property tax on undeveloped residential land (0.4%)	1.5 per cent (individuals), 4.25 per cent (corporations, less for housing co-ops)	Mostly 2 per cent	
Spain	Cadastral income tax, includes improvements; also local property tax based on cadastral income	Varies by region, mostly 7 per cent	3 per cent (of cadastral value), but not to make a loss	Reforms 2013
United Kingdom	Council tax on occupied buildings, includes improvements	Progressive rates 0–12 per cent + landlord surcharge 3 per cent	No	Regime introduced 2007, reforms 2012
United States	Local property taxes, includes improvements	Varies by state, mostly <1 per cent	Mostly 3.6 per cent	Longstanding regime

Source: survey responses; Bååth (2015); CMHC (2017); Cornelius and Rzezniak (2015); Haffner and Bounjounh (2015); James (2014); Jordan (2015a; 2015b); Orji and Sparkes (2015); Roig (2015); PwC (2017).

Almost all countries allow deductions to reflect the capital costs or depreciation of buildings. Germany is probably the most deliberate in its use of this treatment as an instrument of policy. For a long time it treated generously the depreciation of new buildings to encourage growth of the rental stock. As population growth slowed and the need for additional supply reduced, reforms made the treatment less generous (Oxley, Lishman et al. 2010: 35–36). The United Kingdom is the exception on depreciation. It does not allow capital costs or depreciation to be deducted except for a 10 per cent ‘wear and tear allowance’ deductible from rental income from fully furnished properties. The UK Government currently proposes to replace the wear and tear allowance with a more widely applicable deduction for actual expenditures in furnishings.

All 10 countries have taxes that apply specifically to the holding of real property. There is a long history of advocacy, and some past practice, around using land value taxation (i.e. taxing the unimproved value of land) both as a means of raising revenue and as a policy instrument to encourage the development of land to its most valuable use and discourage speculative holding (George 1935; AFTSR 2010). However, across the 10 countries, property taxes are now mostly levied on improved values and are scarcely used above the level of local government (responsibilities at this level of government, and hence the level of property taxation, vary considerably between countries). In this regard Australia is unusual for having some jurisdictions (e.g. NSW) that use unimproved values for the local government property tax base, and having land value tax regimes above the local level (even if these too only imperfectly reflect land value taxation principles by exempting land under owner occupation and primary industry). The nearest comparable regime is Sweden’s tax on undeveloped residential land. Belgium and Spain tax ‘cadastral incomes’, which are deemed rental revenues that factor in improvements but which are well below current values.

9 of the 10 countries also have tax property transfers, known in Australia as stamp duties (New Zealand is the exception, having no transfer taxes at all). Transfer taxes have a mixed reputation in policy: most economists and other commentators criticise them as ‘inefficient’, because the costs they impose tend to discourage transactions that parties would otherwise enter into. However, others point out that they also discourage speculative flipping, and that the burden of transfer duty appears to aid affordability by reducing house prices (Davidoff and Leigh 2013). Belgium and Germany, which have had less price growth than other countries, have relatively high transfer taxes; so does Spain, which had a boom and bust.

Finally, there has been recent activity across most of the 10 countries in relation to REITs, which have been discussed above. REIT regimes have recently been established in Germany (2007) and Ireland (2013); Spain reformed its REIT regime in 2013 to remove taxation at the REIT level. The United Kingdom’s regime, though fairly recently introduced (2007), has subsequently been reformed. In 2017, the Australian Government proposed to open up the use of REITs for investment in affordable rental housing specifically.

#### **4.2.1 Subsidies**

Aside from preferential tax settings, governments may provide to landlords other subsidies in the form of cash payments, loan guarantees and other valuable assistance. We summarise some of these in Table 5.

**Table 5: Subsidies to landlords: Australasia, Europe, North America (select countries)**

Country	Subsidy
Australia	National Rental Affordability Scheme (NRAS) (closed to new entries)
Belgium	–
Canada	–
Germany	Social housing subsidies, low-interest loans for energy sustainability modifications
Ireland	Rental Accommodation Scheme (RAS) Housing Assistance Payment
New Zealand	–
Sweden	–
Spain	–
United Kingdom	'Build to Rent' fund
United States	Low-Income Housing Tax Credit (LIHTC)

Source: survey responses; Bääth (2015); CMHC (2017); Cornelius and Rzezniak (2015); Haffner and Bounjough (2015); James (2014); Jordan (2015a; 2015b); Orji and Sparkes (2015); Roig (2015)

As discussed above, some countries have provided subsidies for the purpose of providing 'social housing' or 'housing for a public purpose' (such that the sectors are defined by subsidy, rather than by ownership), while also providing subsidies to property owners for other purposes. This was historically the case in Germany, which has recently increased its social housing subsidies after a long period of little subsidisation. Ireland's RAS also operates to nominally bring private landlords within the social housing sector. The US LIHTC credit is similar, though the for-profit landlords who receive it are not considered to be social housing.

Other non-social housing subsidies include Germany's low-interest loans for energy sustainability modifications, which are available from the federal government's development bank, KfW (Cornelius and Rzezniak 2015: 57). Sweden's municipal housing companies historically benefitted from loan guarantees from their respective municipalities. These have been withdrawn in the shift to a more 'business-like' orientation (Lennartz 2011).

Overall, these sorts of 'supply side' subsidies are less extensive than 'demand-side' subsidies paid to tenants to support their rent payments. All 10 of the countries have some form of subsidy paid to low-income PRS tenants (Table 6).

**Table 6: Subsidies to tenants: Australasia, Europe, North America (select countries)**

Country	Subsidies paid to tenants	Eligibility
Australia	Rent Assistance. Co-payment subject to maximum rates.	PRS tenants and community housing tenants who receive social security payments
Belgium	Varies by region	Varies by region
Canada	Varies by province	Varies by province
Germany	<i>Wohngeld</i> : Co-payment subject to maximum rates. Housing Benefit for income support recipients. Covers rent for 'adequate' housing.	<i>Wohngeld</i> : low-income tenants and owner-occupiers (eligibility criteria) Housing Benefit: tenants and owner-occupiers, income support recipients

Country	Subsidies paid to tenants	Eligibility
Ireland	Rent Supplement. Co-payment subject to maximum rates.	PRS tenants who receive social security payments
New Zealand	Accommodation Supplement. Co-payment subject to maximum rates, varies by area.	PRS tenants and owner-occupiers on low incomes
Sweden	Housing benefit ( <i>Bostadsbidrag</i> ). Income-related payment.	Tenants and owner-occupiers on low incomes
Spain	Income tax deduction Rental aid for low-income households	Tenants (owner-occupiers may be eligible for tax deduction)
United Kingdom	Local Housing Allowance (Housing Benefit). Covers 'eligible rent'.	PRS tenants on low incomes
United States	Housing Choice ('Section 8') vouchers. Allocated on wait-turn basis.	Tenants on low incomes

Source: survey responses.

In Belgium and Canada there is no national-level subsidy system, with the regions and provinces respectively having their own systems. Germany, New Zealand and Sweden each has a subsidy that covers low-income owner-occupiers as well as tenants. Spain is unusual for having a limited degree of income tax deductibility for rental costs—10 per cent for low-income households—as well as 'rental aid' of limited duration.

In the United States, federal subsidies are provided in the form of 'Housing Choice' vouchers (also known as section 8 vouchers, after the relevant provision of the *United States Housing Act of 1937*). Vouchers are allocated by local housing authorities to eligible households and are rationed: that is, applicants apply and wait their turn for an allocation. Where a landlord accepts the voucher—not all do—it effectively reduces the tenant's own contribution to the rent to 30 per cent of their income and obliges the landlord to maintain the premises to specified standards. The problem of landlords refusing to give tenancies to voucher bearers has led some jurisdictions to proscribe refusal as unlawful discrimination.

In the United Kingdom, Local Housing Allowance is the specific form of Housing Benefit paid to PRS tenants and administered by local councils. Generally speaking it is paid at a rate sufficient to cover the thirtieth percentile rent for properties corresponding to the recipient's household. Provision is made also for local councils to pay a 'discretionary housing payment' in cases of additional need. Recently, Local Housing Allowance has been reformed under the UK Government's austerity policy to reduce individual payments, particularly to single persons under 35, and indexation of payments generally.

## 4.3 Landlords and managers

### 4.3.1 Landlords

Across the 10 countries the dominant owners of private rental housing are smallholding individual persons (Table 7). This is the case even in those countries where multi-unit rental buildings are a large part of the PRS: for example, half of Canada's purpose-built rental buildings are owned by individuals (CMHC 2017: 2). The only exception is Sweden, where housing companies (both privately owned and municipal) are more common; individual landlords are more common only in the lodging sector (i.e. letting rooms in the landlord's own residence).

**Table 7: Landlords and managers, PRS: Australasia, Europe, North America (select countries)**

Country	Dwellings owned by individual persons (%)	Landlords who own one property only (%)	Notable landlords	Management
Australia	–	70	Student accommodation landlords Meriton (3,000 units)	Mostly agents (70%)
Belgium	77	64	2 significant PRS REITs	Agents (40%), self-managed (60%)
Canada	–	–	Some REITs and other corporations in the purpose-built sector	Mostly self-managed
Germany	65	–	60 per cent of 'social housing' owned by private landlords LCLs include Vonovia (333,000 units)	Mostly self-managed
Ireland	–	65	I-RES REIT (2,800 units)	Mostly self-managed
New Zealand	70	42	–	Mostly self-managed (64% use agent to let, 44% to manage)
Spain	86	–	Azora group of companies (8,000 units plus student accommodation)	Specialist managers (housing companies)
Sweden	Individuals 'pretty uncommon'	–	49 per cent of PRS owned by municipal housing companies 13 per cent owned by largest 10 privately owned housing companies	Mostly self-managed (70%)
United Kingdom	71	78	Student accommodation landlords Housing Associations and council-owned BTR companies own total 40,000 PRS units Grainger (8,600 units)	Mostly agents (71%)
United States	71	–	Student accommodation landlords LCLs include MAA (REIT) (100,000 apartments) Invitation Homes (50,000 SFHs) and Starwood Waypoint Homes (32,000 SFHs), merging 710,000 units owned by 10 largest LCLs	Mostly self-managed or by unpaid agent (72%) 400,000 units managed by Greystar 1,413,000 units managed by 10 largest managers

Notes: BTR = Build to Rent; LCL = Large corporate landlord; MAA = Mid-America Apartments; REIT = Real estate investment trust; SFH = Single family home.

Source: survey responses

Larger institutional landlords are, however, present in most of the countries and their activities are becoming more significant. In most countries, including Australia, institutional landlords are active in niches of the PRS, particularly the student accommodation subsector. In some of the 10 countries LCLs are operating also in the mainstream PRS.

Sweden has the most corporatised PRS, with a substantial sector of privately owned housing companies operating alongside the municipal housing companies. The 20 largest own a total of 236,000 units (13% of all rental housing); the four largest own and manage a total of 100,000 units (5%) (Fastighetsvärlden 2017). In the United States, large real estate companies have been in operation for decades, particularly in the 'multifamily' or apartment sector. The largest 10 multifamily landlords currently own 691,000 units (about 2% of all multifamily units) and the largest 50 own almost two million units (5.5%) (NMHC 2017). These LCLs have been joined by new entrants that rapidly acquired large holdings of single-family properties in the wake of the GFC ('REO to Rental'). These include: Invitation Homes (50,000 single family dwellings), a REIT established by Blackstone; and Starwood Waypoint (32,000 single family dwellings), a REIT established by Starwood Capital through the merger of other corporate landlords. These two companies have recently announced that they too will merge (Goldstein 2017).

Germany has a few very large landlords. The nine largest publicly listed housing corporations own a total of 890,000 units (3.8% of all rental dwellings). One of them, Vonovia, is now the largest private sector landlord in the world (333,000 dwellings). This sector grew from the privatisation of municipal housing and industry-related housing around 2000.

Belgium has two publicly listed REITs involved in the PRS: Home Invest Belgium (1,700 properties, more than 80% residential units) and Aedifica (865 units, plus more than 7,000 units of seniors housing). Each has expanded operations internationally (to the Netherlands and Germany, respectively) (Haffner and Bounjouh 2015: 55; Home Invest Belgium 2016; Aedifica 2017). In Spain, the Azora group owns several PRS businesses including Lazora (7,000 rental properties), the Hispania REIT (680 apartments) and 13,000 beds in student accommodation. Blackstone has purchased 4,000 units as well as 94,000 loans with properties pledged under mortgages (Mount 2015; Byrne 2016).

In Ireland, LCLs are relatively small but have grown from nothing in the wake of the GFC. In Ireland, the I-RES REIT is now the country's largest landlord (2,400 properties). Blackstone and other North American equity firms have also acquired properties and loans with properties pledged under mortgages.

In the United Kingdom, 10 per cent of the PRS (by dwellings) are owned by landlords who own 100 properties or more. These landlords comprise both individual persons and corporations. For some years the UK Government has sought to encourage the growth of institutional landlords, particularly as a 'Build to Rent' sector capable of developing newly constructed rental housing. The largest PRS landlord is Grainger plc, a 100-year-old for-profit housing company that has lately stepped up acquisitions, development and fund-raising. However, most 'Build to Rent' activity to date has come from the non-profit housing association sector and council-owned companies (Future of London 2017).

The United Kingdom's approach contrasts with the experience of Ireland, Spain and, lately, the United States, where the recent growth of LCLs has been the result of responses to crises in the finance sector and wider economy, rather than deliberate housing policy.

### **4.3.2 Property management**

The prevalence in Australia of real estate agents as property managers is unusual. With the exception of the United Kingdom, in most other countries self-management is more common. This is the case in the United States, where most properties are managed by the landlord or by an unpaid agent (72%), although there are also numerous large management companies in the

'multifamily' sector: for example, Greystar, which has 400,000 properties under management and owns about 40,000 units.

We asked experts in each of the 10 countries to complete a questionnaire which included questions about changes in property management, technology and ancillary institutions, such as insurance and tenancy databases. However, responses to the questionnaire and a review of the literature identified only a few references—not because the sector is not changing but, as our 10 country experts reported, these institutions are generally under-researched.

Other research projects under the AHURI Evidence-Based Policy Inquiry into the Future of the Private Rental Sector will help address the deficit of research in this area in Australia. Research by Fields (2017) into the practices of US single-family LCLs indicates that that sector has sponsored a range of innovations in investment and management technologies including: systems for automated property valuations and bidding; maintenance requests and work reviews; and rent payment incentives. These technologies are not merely geared towards efficient services, but also the mass collection and use of data about property and tenants.

## **4.4 Regulation**

We consider regulation of the PRS primarily in terms of landlord–tenant law, with a focus on the regulation of rents and tenants' security against termination by landlords. We also consider what may be a developing field of regulation: landlord registration regimes.

The 10 countries represent a considerable range of regulatory approaches: from regimes that are strongly protective of tenants (e.g. Germany and Sweden) through to regimes which are more moderate in the protections offered (Australia and New Zealand). There is also diversity within some countries. This is especially so in the United States where some major cities heavily regulate rents and terminations (e.g. New York), while other jurisdictions regulate tenancies lightly. There is also diversity in Canada where the largest provinces have fairly strong regimes, while the smallest provinces regulate tenancies lightly. Of the 10 countries, four—Germany, Ireland, New Zealand and Spain—have national-level tenancy laws. Responsibility for tenancy law has recently been devolved in both Belgium and the United Kingdom. The level at which tenancy law is determined does not appear to correlate with the degree of regulation or, more specifically, how strongly the law assures tenants of rental and tenure security.

Looking across the recent history of the 10 countries there has been little radical change in their respective regulatory approaches—nothing on the scale of the United Kingdom's reduction in regulatory protections for tenants in the 1980s and 1990s. The most substantial recent changes have been implemented by Ireland, which has increased regulatory protections for tenants. Spain has recently liberalised its regime, which is based on prescribed fixed terms, to reduce strictures.

### **4.4.1 Rent regulation**

A few of the countries regulate rents at the commencement of new tenancies and most regulate rent increases once tenancies are in existence (although the ways in which they do this vary significantly) (Table 8).

**Table 8: Rent regulation: Australasia, Europe, North America (select countries)**

Country	Rent increases	New tenancy rents
Australia	Varies by state; mostly provision for disputing 'excessive to market' increases*	No regulation
Belgium	Increases in line with CPI	No regulation
Canada	Varies by province; most restrict increases to annual 'guideline' rate	No regulation
Germany	Restrictions by reference to 'reference rents' and caps; additional increases for improvements	Restriction by reference to 'reference rents' in specified areas (but regulation is in doubt)
Ireland	Rents must not exceed market rent; high pressure zones	Rents must not exceed market rent
New Zealand	Restrictions against 'excessive to market' increases	No regulation
Sweden	Collectively bargained utility rents	Collectively bargained utility rents
Spain	Increases in line with CPI; additional increases for improvements	No regulation
United Kingdom	Provision for disputing excessive rent increases*; in Scotland, high pressure zones	No regulation
United States	Mostly no regulation; a few major cities have rent regulation (by annual guideline rates) and rent control	Mostly no regulation; a few major cities have rent regulation

Notes: \*A very few tenancies remain subject to rent regulations under historic legislation; CPI = Consumer Price Index.

Sources: Survey responses; Bååth (2015); CMHC (2017); Cornelius and Rzeznik (2015); Haffner and Bounjoh (2015); James (2014); Jordan (2015a; 2015b); Orji and Sparkes (2015); Roig (2015).

Most of the 10 countries have an historical experience of heavy, 'first generation' rent controls, under which rents were set by fiat. Interestingly, in a few countries (e.g. Germany and Sweden) memories of this kind of rent control seem to be long, such that current rent controls are regarded as liberal, even though relative to other countries they are strongly regulated. A few countries have lately implemented innovative forms of rent regulation. Only Spain has recently lightened its regulation of rents, but it still regulates more strongly than most countries.

In Australian jurisdictions, rent increases are regulated lightly, with most jurisdictions regulating only the frequency of increases and providing for tenants to dispute increases that are excessive to the general market level of rents. The United Kingdom regulates rents similarly, although Scotland has recently introduced legislation that provides for caps on rent increases in 'high pressure zones'. A zone may be declared by the Scottish Government on application by a local council. The cap will be not less than the Consumer Price Index (CPI) plus 1 per cent and apply for up to five years. These provisions came into effect on 1 December 2017.

Ireland, too, has recently introduced provision for caps on rent increases in declared 'rent pressure zones'. In local government areas where rents have increased by more than 7 per cent in four of the last six quarters (all of Dublin, Cork and 14 other local government areas), the cap limits rent increases to 4 per cent per annum. These provisions apply in addition to an existing requirement that rents must not exceed the market rent, as demonstrated by reference to three comparable properties (Jordan 2015a; Residential Tenancies Board Ireland 2017).

In Canada, most provinces regulate rent increases by government-issued guidelines expressed as a simple percentage (e.g. Ontario rents may increase 1.5% in 2017) with provision for landlords to apply for 'above guideline' increases in certain circumstances (e.g. improvement work has been conducted). In Germany, rent increases are limited according to changes in a 'local reference rent', presented by each municipality in an instrument known as a *Mietspiegel*. The local reference is calculated by the municipality as the average rent paid under new and existing tenancies in comparable properties over the past four years. In 2013 further limitations were introduced: a cap on increases of 20 per cent over three years (even where the local reference rent would allow more); in specified tight housing markets the cap is 15 per cent. However, provision is made for rent increases out of line with the *Mietspiegel* and caps to recover the cost of energy efficiency modifications. Such modifications can be very profitable for landlords, especially when combined with the low-interest loans offered by KfW.

In Sweden, rents and rent increases are set by collective bargaining between the Swedish Union of Tenants (roughly 500,000 members) and municipal housing companies and other landlords.

A detailed review of rent regulation in all 50 states of the United States is beyond the scope of this report. Generally, in most states rents are unregulated, aside from the prescription of notice periods. In California, Maryland and New Jersey, some cities and localities have rent regulations implemented by municipal governments. In New York State some cities and localities have rent regulations under state-level laws and the District of Columbia has rent regulation throughout. Most of these regimes limit rent increases to a percentage declared by a government agency, and often with provision for increases in excess of those ordinarily allowed where improvements are done (e.g. Newark, New Jersey).

Coverage, however, varies. For example, in the District of Columbia all rental properties are covered by the district's regime; in New Jersey, renovated buildings are exempt for five years and newly constructed buildings are exempt for 30 years; and in New York, multi-unit buildings built before 1974 are covered, but may drop out of the regime in certain circumstances—for example, if the rent exceeds a certain threshold. About 1 million New York City apartments are subject to 'rent stabilisation'; a much smaller number are subject to a separate regime of 'rent control' that applies to tenancies from before 1 July 1971 (New York City Rent Guidelines Board 2017). In most of the states without rent regulation, state laws prohibit municipal governments from implementing their own rent regulations. This has led to some innovation at the municipal level: for example, the City of Portland, Oregon, where state law prohibits rent regulation, has recently passed an ordinance that requires a landlord to pay relocation costs to a tenant where the rent is increased by more than 10 per cent.

Spain has recently liberalised its rent regulation. Where previously rent increases were limited during the first three years of a tenancy to the increase in the CPI, now rent increases are as agreed in the tenancy agreement (Roig 2015).

New rents are regulated in Germany, Ireland, Sweden and in a few US cities, each in different ways. In Germany new rents are limited in specified localities to 110 per cent of the local reference rent. Introduced in 2015, the validity of this measure is now in doubt following an indication in September 2017 by the Berlin District Court that the measure may be unconstitutional (Landgericht Berlin 2017). This question has yet to be finally determined. Ireland's prescription that rents must not exceed the market applies to new and existing tenancies; so does Sweden's collective bargaining process. In the United States, New York's rent stabilisation regime limits the amount by which the rent for a new tenancy can exceed the rent for the previous tenancy in the property; in San Francisco, as a measure for the integrity of its regulation of rents and grounds for termination, a new rent may not exceed the previous rent where the vacancy was obtained by certain types of termination proceedings – for example,

where the landlord purported to be going out of business or moving into the property themselves.

#### 4.4.2 Security of tenure

Across the 10 countries, the degree of tenants' legal security against termination by landlords varies on a pattern with rent regulation. This reflects a necessary connection between effective rent regulation and security: rents cannot be regulated effectively if tenancies can be readily terminated and legal security is ineffective if rents can be increased without restriction. Table 9 shows the different ways in which security is afforded.

**Table 9: Security of tenure: Australasia, Europe, North America (select countries)**

Country	Fixed term and periodic tenancies	Grounds for termination by landlord
Australia	Short (6–12 months), fixed-term and periodic tenancies	No-grounds termination allowed; Victoria has proposed legislation to remove the 'no specified reason' ground
Belgium	9-year fixed terms, but most are 3-year terms	Termination at end of fixed term allowed
Canada	Mostly short (6–12 months), fixed-term and periodic tenancies	Mostly prescribed grounds only; some allow termination at end of fixed term
Germany	Little use of fixed-term tenancies	Prescribed grounds only
Ireland	Short fixed-term and periodic tenancies	Prescribed 6-year cycle with lesser restrictions on termination in initial 6 months, then prescribed grounds only
New Zealand	Short (6–12 months), fixed-term and periodic tenancies	No-grounds termination allowed
Sweden	Little use of fixed-term tenancies	Prescribed grounds only
Spain	3-year fixed terms with some provision for early termination	Termination at end of and, in limited circumstances during, fixed term
United Kingdom	Short (6–12 months), fixed-term and periodic tenancies	No-grounds termination allowed (England and Wales); prescribed grounds only (Scotland)
United States	Short fixed-term and periodic tenancies	Varies by state and municipality: most allow termination without grounds, a few large cities allow termination on prescribed grounds only

Sources: survey responses; Bååth (2015); CMHC (2017); Cornelius and Rzeznik (2015); Haffner and Bounjouh (2015); James (2014); Jordan (2015a; 2015b); Orji and Sparkes (2015); Roig (2015).

Germany, Sweden, most of the Canadian provinces and those major US cities with rent regulation have for some time afforded a reasonable degree of security for tenants, particularly by providing for termination by landlords on prescribed reasonable grounds only. In Ireland and Scotland, recent reforms aim to increase tenants' security. None of the 10 countries have recently taken steps to substantially reduce security, though Spain has reduced the length of its prescribed fixed terms.

Australian tenancies are insecure relative to those in most of the other countries, with no-grounds terminations allowed currently in all Australian jurisdictions, though Tasmania allows termination without grounds at the end of a fixed term only. Victoria has proposed legislation to remove the 'no specified reason' ground. Legal security in Australia, such as it is, is principally

afforded by the use of fixed term agreements which restrict both landlords and tenants from lawfully terminating the tenancy during the term with only limited exceptions. Use of fixed terms is a matter for agreement between the parties. Consequently, fixed terms tend to be short (6–12 months).

Most countries that afford greater security do not use fixed terms to do so. In Germany and Sweden most tenancy agreements are for no fixed period. Indeed in Germany a fixed term is permissible only if the landlord can demonstrate that they need the premises after the term for their own housing, a family member or employee or structural alterations, demolition or commercial use (Cornelius and Rzeznik 2015: 68). In both countries security is assured instead by the prescription of reasonable grounds for termination. In Canada, short fixed terms (6–12 months) are commonly used, but in most provinces security is assured more by the prescription of reasonable grounds for termination by landlords, which in most cases do not include termination at the end of the fixed term<sup>3</sup>.

In Ireland, tenancies often have a short fixed term (6 months) that restricts termination by landlords and tenants. However, security is assured more by a unique legislative regime of prescribed cycles of lesser and greater restriction on termination by landlords. Under this regime, the first six months of a tenancy are less restrictive (leaving aside the restrictions imposed by a fixed term), and a landlord may terminate a tenancy without grounds. Thereafter, the tenancy becomes a '*Part 4 tenancy*' under Part 4, Chapter 2 of the *Residential Tenancies Act 2004* (Ireland), and during the next five years and six months termination is allowed on prescribed grounds only. After that period the landlord may terminate the tenancy within six months by giving a notice with the reason for termination (not limited to the usual prescribed grounds). Otherwise, the tenancy continues as a '*Further Part 4 tenancy*', which may be terminated on prescribed grounds only. The period of notice varies according to the length of the tenancy. This regime was originally introduced in 2004 with a four-year cycle. It was amended in 2016 to lengthen the cycle to the current six years and introduce the requirement of reasons for terminating prior to the '*Further Part 4*' phase.

Belgium and Spain make use of longer fixed terms in different ways. Belgian tenancy law contemplates four types of tenancy agreement: a short-term agreement (less than three years); a nine-year agreement (with agreements for terms between three and nine years treated as nine-year agreements); a long-term agreement (more than nine years); and a life-long agreement. The nine-year agreement is assumed to be the standard; in fact, more than half of all agreements are short term (Haffner and Bounjouh 2015: 57). Agreements may be terminated at the end of the fixed term by either party without grounds; tenants may also lawfully terminate their agreements without grounds during the fixed term, though compensation may be payable if terminated in the first three years. Short-term tenancies may be extended once only for another short term at the end of their fixed term. They otherwise become nine-year agreements.

Spain provides for a standard three-year fixed term agreement after which either party may terminate without other grounds. The agreement is otherwise renewed with one-year extensions. Provision is made also for termination by a landlord after the first year of the three-year term where the landlord needs the premises for their own or a relative's housing. The three-year term was introduced in 2013 to replace the previous five-year fixed term.

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<sup>3</sup> Ontario, Quebec, Alberta, Manitoba, Nova Scotia, Prince Edward Island and Nunavut prescribe reasonable grounds for termination and do not permit termination by landlords at the end of the fixed term without some other ground. British Columbia prescribes reasonable grounds for termination, but also provides for tenancies to terminate at the end of the fixed term without other grounds where the agreement expressly provides for this. In Saskatchewan and New Brunswick, landlords may terminate the tenancy at the end of the fixed term without other grounds; otherwise, they may terminate on prescribed grounds only. Newfoundland, Labrador and Yukon provide for no-grounds termination (CMHC 2017).

In the United Kingdom, most PRS tenancies—‘assured shorthold tenancies’ in England and Wales; ‘short assured tenancies’ in Scotland—are afforded a degree of security similar to that of most Australian tenancies: that is, they are subject to a short fixed-term (usually 6–12 months), at the end of which the landlord may terminate the tenancy without other grounds. The Scottish Parliament has recently passed the *Private Housing (Tenancies) (Scotland) Act 2016*, under which new tenancies may be terminated on prescribed grounds only. The Act provides for 18 prescribed grounds of which some are grounds for ‘mandatory’ termination (i.e. if the ground is proved in proceedings before a tribunal, the tribunal must terminate the tenancy), and some are ‘discretionary’ (i.e. the tribunal must decline to terminate, considering the circumstances of the case). These reforms commenced in December 2017.

A detailed review of provisions in the United States is beyond the scope of this report. Generally speaking, those states that do not regulate rents also allow for termination without grounds at the end of the fixed term or period of an agreement, while in those municipalities in California, Maryland, New Jersey, New York and the District of Columbia where rents are stabilised, termination is allowed on prescribed grounds only. The Portland innovation is relevant in this regard too: relocation costs are payable where a landlord terminates the tenancy without grounds.

#### 4.4.3 Registers

Requirements around the registration of landlords, rental properties and rental agreements may not be the most dramatic form of regulation, but it is notable that there has been considerable recent activity in this area in the 10 countries.

Registers have been around for some time: numerous US cities have long had registers of rental properties for various purposes including rent regulation, taxation and the tracking of public health hazards (e.g. premises with lead paint). Belgium requires registration of tenancy agreements. Germany, Spain and Sweden, on the other hand, do not require any sort of rental-specific registration; Sweden abolished a registration requirement in 1988.

Several of the 10 countries have recently established registers. In some Australian states, registers for specific forms of marginal rental housing have been established. In NSW, Queensland and Victoria, specified forms of lodging accommodation must be registered; the Queensland regime also requires operators to undergo accreditation and the Victorian regime includes a ‘fit and proper person’ test. NSW also has a separate register of residential parks, and requires operators to satisfy an education criterion.

As part of its 2004 residential tenancy law reforms, Ireland introduced a requirement for landlords to register each tenancy with the Residential Tenancies Board. In the United Kingdom, landlord registration schemes have been established in Scotland (2006), Northern Ireland (2014) and Wales (2015), and provision made for local councils in England to establish, with the permission of the Department for Communities and Local Government, local landlord registers. The Scottish scheme also requires that landlords satisfy a ‘fit and proper person’ test, while the Welsh scheme requires landlords who self-manage to also apply for a licence, which includes a training requirement.

The requirement to register is backed by a provision that disallows rent increases by unregistered landlords. In 2013 when the provisions in England commenced, the Local Government Information Unit reported that one-third of local councils were considering introducing licensing schemes. Since then numerous local councils have established landlord registers, mostly on a selective basis: that is, only landlords of properties in specified areas are required to register. The first local register that of Newham Borough Council in East London, requires all landlords in the area to register. The council is now negotiating for its renewal in the face of apparent reluctance by the government. Separately, UK jurisdictions have also established registers for Houses in Multiple Occupation (HMOs): that being, lodging houses.

In Canada, the City of Vancouver requires all rental properties to be licensed and, since 2012, has maintained a 'rental standards database'. The database presents publicly available information held by the City about purpose-built rental properties and social housing. Recently, the landlords association, LandlordBC, has established its own voluntary register with training and certification (LandlordBC 2017). The City of Toronto in 2017 introduced a register for landlords who own multi-unit buildings and is also considering a licensing regime for landlords.

## 4.5 Key findings

- Across the 10 countries, housing investment is mostly financed by credit, and housing credit is mostly provided by banks. Over the past two decades, housing credit has expanded with the development of new funding sources. Following the GFC, 9 of the 10 countries have implemented housing-specific macroprudential tools as a financial stability measure; their effect on the investment strategies and borrowing practices of PRS landlords is worthy of investigation.
- In countries most affected by the GFC, government programs for the disposal of impaired property-related assets have significantly increased the position of large corporations in the PRS, both directly as landlords (as in the United States) and indirectly as owners of loans with PRS properties pledged.
- Looking at the range of tax settings that are applicable to housing and the PRS, we find some surprising results. Both Australia and Germany exempt owner-occupied housing from capital gains and provide for negative gearing on similar terms. Yet their treatment of negative gearing and capital gains tax underlie quite different housing market outcomes: speculative inflation in Australia; relatively steady housing prices in Germany. This highlights the need for considering the interaction of tax regimes with wider system factors.
- 8 of the 10 countries have recently introduced or reformed their tax regimes to provide for REITs, which are emerging as a significant vehicle for PRS investment funding.
- Some countries provide specific-purpose subsidies to PRS landlords, such as Germany's low-interest loans for energy efficiency modifications (available to both private and social housing landlords), and Ireland's RAS. However, these subsidies are not as extensive as the rent assistance payments made in all 10 countries to tenants—and hence their landlords.
- In 9 of the 10 countries smallholding private individuals are the predominant type of landlord. But most countries also have LCLs and a few have recently seen rapid growth in very large new LCLs.
- Australia has a comparatively high rate of management by professional agents (70%). Management and other ancillary institutions are under-researched internationally.
- Across the 10 countries, the foremost approach to assuring tenants' security is to allow landlords to terminate on prescribed grounds only (as in Germany, Sweden, Scotland, most Canadian provinces and some major US cities). Only two countries rely on long fixed terms, and Ireland has a unique regime of cyclical restrictions. Only Australia, New Zealand, the United Kingdom (other than Scotland) and some US jurisdictions allow termination without grounds. Victoria (Australia) has proposed legislation to remove the 'no specified reason' ground.
- Four countries—Belgium, Germany, Spain and Sweden—plus most of the Canadian provinces and some major US cities, regulate rent increases by limiting them to a stated guideline or reference rent, and two more (Ireland and Scotland) do so in designated 'rent pressure zones'.

- Registers are an old regulatory technology which have been given a new lease of life in several countries and provide a mechanism for monitoring and lifting landlords' standards of conduct.

## 5 Case studies in institutional change—Germany, Ireland, United Kingdom and United States

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- We can learn lessons relevant to Australia’s PRS policy development by taking a closer look at recent changes in the private rental sector in Germany, Ireland, the United Kingdom and United States.
  - A range of institutional factors helped Germany avoid the interlocking financial and housing crises that struck Ireland, the United Kingdom and United States in the GFC. Responses to these crises have assisted existing owner-occupiers and large financial institutions to increase their position in property, with some curbs around riskier bank lending. This may be no more sustainable or equitable than the pre-GFC housing credit expansion.
  - Large corporate landlords (LCLs) have not built much new housing and mostly purchased existing stock. In Germany and the United States they are active portfolio managers, acquiring, renovating and selling stock. They have also been active in mergers and, particularly in the United States, devising innovative financial instruments.
  - Ireland has increased regulation of the PRS as it has grown. The UK Government’s view of PRS regulation as ‘red tape’ is increasingly out of step with international experience and with the law reform path being taken in Scotland.
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This chapter presents a closer examination of themes in institutional change as they are playing out in Germany, Ireland, the United Kingdom and the United States. We selected these countries for special treatment for the potential lessons of their recent different experiences.

In Ireland, the United Kingdom and the United States, private rental is growing in the aftermath of a period of housing boom and crash which Germany avoided. Ireland has been pursuing a deliberate strategy that increasingly regulates the PRS while subsidising and encouraging its growth. The United Kingdom has specifically sought to nurture a sector of ‘Build to Rent’ landlords and the United States has a rapidly growing and changing sector of LCLs.

In presenting case studies of themes in PRS institutional change, this chapter provides more details, and more of an explanatory account, of the institutions and changes observed in overview in the previous chapters. It does this by drawing on reports for each country commissioned for this research. These reports—by Stefan Kofner (Germany), Aideen Hayden (Ireland), Mark Stephens (UK) and Alex Schwartz (US)—are also presented as appendices.

### 5.1 Housing system contexts

#### 5.1.1 Germany

Throughout this report and the international comparative housing literature, Germany stands out for a number of reasons. It is the only country reviewed here in which more households rent privately than own their homes, and where social housing, itself largely also owned privately, accommodates a small minority.

The housing situation in Germany is the product of the country's particular historical experience. In the first half of the twentieth century private rental housing was by far the largest sector of the German housing system, as it was in most western European countries and, to a lesser extent, North America and Australasia. However, Germany did not experience the same degree of decline relative to owner occupation as other countries. After the Second World War, both parts of divided Germany had critical shortages of housing, which was addressed in East Germany by the construction of vast state-owned social housing estates. West Germany adopted a number of measures including: social housing programs of low-interest loans and grants that were open to municipal housing companies and private landlords alike; tax settings (accelerated depreciation provisions and negative gearing); and exemption from heavy war-time rent control that encouraged new construction for rental.

Over the post-war period the municipal housing companies became major landlords, especially in West Berlin (Fields and Uffer 2016). State-owned industries such as the Federal Railways and private sector industrial conglomerates also owned significant portfolios of housing. From the 1960s the housing shortage eased and new social housing subsidies entered into a long decline. The government continued to encourage the development of new and modernised rental housing (private and social) through generous treatment of depreciation. At the same time, West Germany also instituted tenancy law reforms, replacing the war-time controls with the system of rent and security regulation that remains in place today. Over the period the PRS developed as a provider of good-quality housing to all income groups without the association with poverty it acquired in other countries.

Upon reunification in 1991, social housing construction was again subsidised to accommodate the associated shift in population from East to West. Around the same time, however, taxation reform removed the preferential treatment previously given to the municipal housing companies and over the 1990s and 2000s many of these companies and the state-owned industries privatised their housing stock. As population growth declined, some preferential tax treatment of housing investment was wound back, notably the accelerated depreciation deduction which was abolished in 2006.

Over the years Germany has had, and continues to have, policy settings that are preferential to owner occupation. Owner-occupiers are exempt from capital gains tax and previously were eligible for tax deductions for mortgage interest and depreciation for new-built owner-occupied housing. From 1996 the tax incentives were replaced by a grant for new builds (*Eigenheimzulage*) which was also abolished in the reforms of 2006 (Kofner 2016). Throughout this period, owner occupation never became the majority tenure in Germany. There is a popular conception of buying a house for owner occupation as something Germans do later in life (the average age of German first home buyers is 40) as a 'once in a lifetime' undertaking (Kofner and Kemp 2014).

Germany's housing system also stands out for not having experienced the house price boom of the 2000s, let alone the crash experienced in Ireland, Spain and the United States. The German financial sector was affected by the GFC, as German banks had heavily purchased mortgage bonds from the United States, but the financial institutions had not lent badly in the domestic housing market. Kofner (2014) characterises Germany's housing system as 'fundamentally resilient', the result of its relatively low rate of owner occupation and conservative lending practices. However, it also underlies a very uneven distribution of wealth (Kofner 2014). The system is not unchanging: since 2010 house prices have been rising, as have rents, and social housing expenditure has recently increased with some municipalities once more moving to build up their housing stocks (Lawson, Legacy et al. 2016).

### 5.1.2 Ireland

Ireland's housing system is majority owner-occupied, as it has been for most of the twentieth century, but over the last 20 years its PRS has been growing. It has done so through both a boom and a crash, the experience of which looms over current Irish housing policy and market conditions.

In broader perspective, the recent growth of the Irish PRS follows a longer and deeper decline than in other countries. Early in the twentieth century, as part of land reform, Ireland built a significant social housing sector in its rural local authorities (Norris 2014: 622–23). After secession from the United Kingdom in 1922, Irish governments gave strongly preferential treatment to owner occupation through grants, tax exemptions and, especially from the 1960s, sales of social housing dwellings to tenants. In the PRS, rent controls dating from the First World War remained in operation for a substantial part of the sector through to 1981 when they were struck down by the Irish High Court. These controls had also encouraged sales of properties to tenants. Owner occupation peaked at 80 per cent in 1991, by which time private rental housing accommodated just 7 per cent of households, behind social housing.

In the late-1980s, after decades of below-average economic activity and population growth mitigated by emigration, Ireland liberalised its economy and entered its 'Celtic tiger' phase, a period of strong export-led growth in skilled manufacturing and services and growth in population. It also reformed its provision of social housing, replacing local authority debt financing with smaller grants from the national government, contracting the sector. Through the 1990s and early 2000s, with incomes growing, new lenders entered Ireland's deregulated banking sector. From 1999, the adoption of the Euro reduced the banks' wholesale funding costs; Irish households leveraged hard into property, including new housing construction and housing for private rental (Conefrey and Fitz Gerald 2010).

Over the period 1990–2006, housing output relative to population tripled, average real house prices doubled and the ratio of housing debt to GDP tripled (Waldron and Redmond 2014: 152). In the later part of the boom, the social housing sector appeared again to grow, partly through development deals and partly through some private landlords being nominally brought within the social housing sector by the 2004 introduction of the RAS, under which local authorities were funded to pay private landlords to accommodate eligible tenants (Norris and Coates 2009; Norris and Byrne 2016).

When bank funding froze in the GFC the Irish banks were exposed with massive wholesale funding liabilities, on the one hand, and loan assets heavily concentrated in overvalued houses and property developments on the other (Connor, Flavin and O'Kelly 2012). There followed a crash in both the financial and housing sectors. One bank collapsed completely; four others were wholly or partly nationalised with the Irish Government assuming a massive liability in a currency it does not itself issue. House prices halved and building almost ceased. Amongst the austerity measures that ensured, social housing subsidies were reduced by almost 90 per cent (Norris and Byrne 2016) while the government's National Asset Management Agency (NAMA) was charged with disposing of impaired property-related loans amounting to almost 50 per cent of Ireland's GDP (Byrne 2016: 691).

The crash left Ireland with incomplete and vacant properties in speculatively developed estates, housing shortages in its major centres and global firms with a significantly increased position in Irish property. Declining rental affordability and rising homelessness prompted the Irish Government to formulate Rebuilding Ireland: action plan for housing and homelessness (Government of Ireland 2016a), which commits the government to increased social housing provision, and a *Strategy for the rental sector*, which envisages the PRS becoming 'a tenure of choice' and 'a stabiliser to mitigate boom or bust cycles' (Government of Ireland 2016b: 4–5).

### 5.1.3 United Kingdom

The trajectory of private rental housing in the United Kingdom is similar to that of the Irish PRS. Over the twentieth century, private rental housing experienced a long, deep decline from accommodating 90 per cent of British households in 1914 (Harloe and Martens 1984: 4) to just 9 per cent of households in 1991. This was well behind social housing and owner occupation, which became the majority tenure in the early 1970s.

Compared with other countries, the United Kingdom had an unusually prominent social housing sector over the latter half of the twentieth century. Private rental was marginalised, being both heavily regulated and associated with exploitative, even criminal, landlords. Throughout the post-war decades local authorities were the major builders of new housing. In the 1980s, the implementation of RTB social housing at substantial discounts and the loosening of credit provision saw owner occupation increase rapidly. Hence, social housing became a major source of owner-occupied housing through sales to tenants.

The decade also saw local authorities stopped from further housing construction. The residualised social housing sector largely shifted into the non-profit housing management associations and policy interest in rehabilitating the PRS began to emerge (Kemp 2015: 179). *The Housing Act 1988* (UK) deregulated rents and reduced security of tenure for new tenancies with the government consciously allowing the Housing Benefit system to take the strain of low-income renters' increased housing costs. In the mid-1990s, UK banks introduced mortgage lending for 'Buy To Let' investment. Owner occupation peaked at 70 per cent in 2001; since then, private rental housing has been the growing tenure in the United Kingdom, doubling its share of the housing system from 10 per cent in 2001 to 20 per cent in 2016 (Kemp 2015; Appendix 3).

Over that time, like Ireland and the United States, the United Kingdom experienced a housing boom and then a bust, though not so deep as elsewhere. UK house prices fell by 12 per cent, but subsequently rose and are now around their pre-GFC peak (higher in London). There is a strong theme in popular, academic and political discourse of a crisis in UK housing, a crisis that has unfolded over a longer period (Ferrari 2015). This is reflected in the title of the UK Government's February 2017 white paper on housing policy: *Fixing our broken housing market* (Department for Communities and Local Government 2017). The sense of crisis is evident also in the way in which the disastrous fire in the Grenfell apartment block in June 2017 became an instant symbol of a housing system and wider society beset by division and inequality.

### 5.1.4 United States

The United States has been a majority owner-occupier country since the 1950s, with its rate of owner occupation peaking at 68 per cent in 2005. Unlike most other countries, owner occupation increased during the 2000s boom and private rental contracted. In the aftermath of the GFC and housing market crash, however, the PRS has grown rapidly from 31 to 37 per cent of households in 2015.

The American PRS has always been significant: unlike other countries, the United States never built up a social housing sector that was more than marginal, and even the relatively small amount it did build in the 1970s has been reduced by demolition and disposal. Since the 1980s the federal government has subsidised through the LIHTC program the construction of rental housing owned variously by private landlords and non-profit organisations and dedicated to low-income households. The inspiration for Australia's short-lived NRAS, LIHTC has enjoyed bipartisan support but applies to less than 5 per cent of the rental stock.

For decades, the United States has treated owner occupation preferentially, particularly through generous mortgage interest deductibility provisions. Further support for owner occupation was given by the United States' system of secondary mortgage market funding and mortgage

insurance provided by the government-sponsored entities Fannie Mae and Freddie Mac and government-owned Ginnie Mae. These institutions, implicitly guaranteed by the US Government, were crucial in the development from the 1980s of the mortgage-backed securities market that greatly expanded shadow banking funding and housing credit provision, which would ultimately culminate in the GFC. Housing credit growth in the United States was strongest in the owner-occupied sector where it lifted the rate of owner occupation from its 1980s plateau of 64 to 68 per cent in 2005, and increased the debts of many existing owner-occupiers through equity-release loans. The variety of loans and complexity of repayment liabilities also grew and lending criteria declined as loan originators competed for market share (Immergluck 2015).

When it struck, the GFC had sharp housing impacts for many of these new and existing owner-occupiers: eight million American households lost their homes through foreclosure and related means in the period 2007–12 (Immergluck 2015). The share of households privately renting grew rapidly from 34.7 to 37.1 per cent in the two years 2013 to 2015 (AHS 2015) and has continued to do so even though the depths of the foreclosure crisis have passed.

There has also been relatively little new housing construction since the crash. This means that even as the share of construction represented by the multifamily (apartment) rental sector has grown in the post-crash period—averaging 26 per cent of construction over 2008–15, compared with 20 per cent in 1991—the absolute number of properties completed annually is less than those for the years preceding the crash (Appendix 4). Instead, the PRS stock has grown mostly through the acquisition of single-family dwellings, significantly changing its composition and introducing a host of new LCLs to the sector.

The United States' housing affordability and security problems are being agitated by grassroots organisations with some of them using innovative techniques to highlight issues: for example, the Anti-Eviction Mapping Project, which uses data visualisation technologies to map the impact of evictions in San Francisco Bay Area and campaign for housing justice (see Anti-Eviction Mapping Project 2017). The entry onto the bestseller lists of an ethnography of the housing crisis (*Evicted* by Desmond 2016) also indicates a rising interest in housing problems. However, housing policy has not found a place on a national political agenda that has lately become crowded with conflicts and scandals.

## 5.2 Financial settings

Over the past decade, three countries—Ireland, the United Kingdom and the United States—have had to contend with interlocking crises in their finance and housing sectors. In each country, the PRS has grown throughout. Germany was affected by the GFC, but without the complication of a speculative bubble and housing crash.

We take two lines of inquiry to financial settings relating to private rental housing in our detailed analysis of our four focus countries—Germany, Ireland, the United Kingdom and United States:

- how Germany avoided the complication of housing investment and financial instability and whether and how Ireland, the United Kingdom and United States may now be addressing it
- whether and how the countries are using subsidies to get outcomes from the PRS, particularly in times of economic adversity.

### 5.2.1 Housing checks and spurs: Germany

Looking across Germany's housing institutions, we can see a range of factors that arguably contributed to its avoidance of a housing boom and bust.

Our country expert highlighted the conservatism of the German finance sector: a product of sector structure, regulation and 'traditional lending habits' (Kofner 2016). Housing credit

provision in Germany is dominated by a network of regionally based public banks (*Sparkassen*) and building societies (*Bausparkassen*). These institutions are funded mostly by deposits and covered bonds (*Pfandbriefe*) with only high-quality loans (60% LVR, conservatively valued) eligible for admission as collateral to the closely monitored cover pool (Kofner 2016). Off-balance sheet securitisation and short-term inter-bank loans play only a very minor role<sup>4</sup>. These institutions apply conservative lending standards and make little use of credit products like adjustable-rate mortgages and interest-only loans. Our country expert described these instruments as 'exotic' in German housing credit.

Changes in the German taxation system probably helped check housing speculation. The treatment of depreciation looms large in German housing tax policy. For many years up to 40 per cent of acquisition and production costs could be deducted from rental incomes in the first 10 years of ownership under the 'declining balance' rule. This generous provision was removed in 2006, at the same time as the *Eigenheimzulage* home-owner grant. Motivated by a general objective of budget-balancing, rather than housing policy, this was nonetheless a move against the two most prominent subsidies for housing investment. Germany's high property transfer taxes would also function as a check on speculative trading.

German tax settings around rental loss deductibility and capital gains are curious. Germany makes similar provision for negative gearing to Australia, though it does not appear to command the same sort of attention. The crucial difference is context: unlike Australia, Germany regulates rents, which means German landlords do not enjoy the same degree of cash flow advantage as Australian landlords. It also means that negative gearing in Germany may be said to contribute to rental affordability by cushioning landlords who incur losses from submarket rents, whereas in Australia it allows landlords' market rent incomes to be leveraged further into higher purchase prices. As regards capital gains, Germany, again like Australia and most other countries, exempts owner-occupied housing. It also exempts landlords if they have held the property for more than 10 years. This is actually preferential treatment relative to other assets, which are subject to capital gains tax regardless of length of holding. However, to the extent that it affects behaviour within the property sector, the time-structure of the tax discourages speculative trading.

It may be that the speculative potential of these settings is inactive in the wider context of German society and economy. For an extended period Germany had no population growth so did not have the germ of real demand for housing that can lie beneath a speculative boom. The already large size of its PRS may also have played a role, because fewer households are able to lever housing equity growth into a rapid escalation of prices. The relatively high degree of separation of rental housing from owner-occupied housing in the built form of the stock could also help compartmentalise speculation and inhibit bubbles forming across the housing system.

### **5.2.2 Housing checks and spurs: Ireland, the United Kingdom and United States**

In Ireland, the United Kingdom and the United States, the general approach to the complication of financial and housing crises has been an extended period of low interest rates to accommodate the existing debt stock and new credit creation, and some degree of tightening in access to credit. This has advantaged existing property owners in each country, who have been able to leverage their housing equity into upgraded and costlier owner-occupied housing and

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<sup>4</sup> It should be said that the recent record of the German finance sector is not spotless. In 2005, the German federal government instituted the phased removal of a government guarantee for state banks. During the transition stage some banks issued bonds as a last use of the guarantee and, flush with funds, bought up American and Eastern European mortgage-backed securities. This meant they were badly exposed in the GFC (Kofner 2016). However, the *Bausparkassen* were less affected, and in any event seem to have conducted themselves conservatively in the domestic market.

into private rental investment. Each has also facilitated global financial institutions taking significant positions in private rental housing, either directly as owners of portfolios of properties or indirectly as owners of PRS mortgages. In the United States especially, this is opening up innovation in PRS finance and funding outside the banking sector, with LCLs directly accessing money markets and issuing new instruments, specifically rental-backed securities.

Looking at their finance and tax settings in detail, each country has made some adjustments. The United States has legislated for higher standards in housing credit provision, but none of the provisions are specific to lending for PRS investment—arguably a reflection of the 2000s bubble being driven by owner-occupiers. It has also made no changes to tax settings applying to either owner-occupied or private rental housing.

Ireland has introduced a macroprudential rule (a 70% LVR requirement) to curb lending for PRS investment. However, it has also moved to increase the rate of mortgage interest taxation relief for landlords from 75 per cent to 100 per cent. This is deductible from rental income only, so is still less generous than Australia's negative gearing provisions. Further tax reform is currently under consideration as part of the rental housing strategy under *Rebuilding Ireland* (Government of Ireland 2016a).

The United Kingdom, on the other hand, has turned its tax settings against PRS investment. In the 2015 Budget, the UK Government commenced a reduction in the rate of deductibility of mortgage interest, such that it will only be deductible from that part of the landlord's rental income to which the basic 25 per cent tax rate applies, rather than from income subject to the highest marginal rate. The stated rationale was that 'Buy-to-let landlords have a huge advantage in the market as they can offset their mortgage interest payments against their income, whereas homebuyers cannot' (Osborne 2015). Hence, the government moved to reduce the advantage.

At the same time, the government introduced a property transfer tax surcharge specifically for landlords and purchasers of second homes. Prior to the announcement of the changes there were suggestions that the government would seek to target small PRS investors in order to further encourage the institutional 'Build to Rent' sector, but the surcharge as announced applies to institutional landlords too. Our country expert anticipates that both the surcharge and the reduced deductibility of mortgage interest will mostly affect landlords with high incomes and larger portfolios, and hence more professional operations. Lately, the UK Prudential Regulatory Authority has moved also to bring credit assessment criteria for 'Buy To Let' lending, which had been left out of previous tightening, into line with those for other housing credit.

It remains to be seen what effect this deliberate turn in policy will have on the United Kingdom's resurgent PRS. Even before the changes, its tax treatment of landlords was less favourable than in other countries: even when allowed at the full rate, mortgage interest and other rental losses could not be deducted from other sources of income, as per Australia's negative gearing provisions. The United Kingdom also does not allow depreciation deductions as most other countries do. It may be that reforms directed to closing the preferential treatment of existing owner-occupiers, such as through capital gains tax or land value taxation reform, would better get at the base on which house prices and PRS growth have been leveraged.

It also remains to be seen across the three countries whether this approach is any more sustainable than the pre-crisis expansion of house prices and credit. Further, even if it is proven to be more durable—because the curbs work to keep out the riskiest borrowers and reduce defaults—it may not be more equitable if housing wealth concentrates behind mounting prices in fewer hands. This makes questions in relation to the terms on which private rental housing is provided and relevant institutions shaped by subsidy incentives or regulatory regimes all the more important.

### 5.2.3 Specific-purpose subsidies

Here we consider some specific-purpose subsidies that shape the PRS in Germany, Ireland, the United Kingdom and the United States, and the housing outcomes it produces.

Germany has lately increased its subsidies for social housing construction, having for years maintained them at a low base, and some municipal housing companies subsequently are again looking to acquire stock. As discussed earlier, these subsidies are available also to private investors and the properties subsidised are therefore subject to allocation rules. These properties are thus considered to constitute social housing stock. Germany has also maintained incentives for upgrading existing housing stock to modern standards with the KfW's provision of low-interest loans for energy efficiency modifications an important subsidy program, particularly in combination with the provision for above-*Mietspiegel* (rent index) rent increases.

In the United States, the major specific-purpose subsidy in the PRS remains the LIHTC program. This was disrupted by the GFC when the market for tax credits, and hence the funds available to developers, dropped markedly. The Obama Administration supported the program with additional funds and the market has since revived, though geographic differences in tax credit prices have opened up. The fate of the program itself under the Trump Administration is not yet clear; however, our country expert observes that if the administration's promised cuts to rates of corporate and income tax are implemented the value of program tax credits would fall.

Ireland is still developing all the measures flagged under its *Strategy for the rental sector* (Government of Ireland 2016b), but the elements already in place indicate a strategic approach which joins subsidies with regulation. Ireland has been charting such an approach since the early 2000s when it deliberately shifted to delivering housing support through subsidies to the PRS. The *Rebuilding Ireland* action plan recommitted the government to it, with some changes in form pending. Following a 2014 pilot, a new subsidy in the form of the Housing Assistance Payment (HAP), intended eventually to replace the Rent Supplement and the RAS, is being rolled out across local authorities. The HAP closely resembles the RAS, in that the local authority pays the amount directly to the landlord for the accommodation of an eligible person, with the exception that HAP tenants will have to find their own accommodation (rather than the local authority sourcing it for them) subject to rent thresholds. Significantly, under amendments to the *Equal Status Acts 2000-2015* (Ireland) that commenced 2016, it is unlawful for landlords to discriminate on the grounds of a tenant's receipt of HAP and other housing assistance. As well as a legal stick, the HAP employs a carrot: participating landlords will immediately become eligible for the 100 per cent rate of mortgage interest relief. Other elements of the strategy still in development include a 'cost rental' model for moderate income households.

In the United Kingdom, both the United Kingdom and Scottish governments have continued to develop subsidies targeted to the 'Build to Rent' sector. These include the 2012 establishment of a 'Build to Rent' investment fund, which offered government loans of up to 50 per cent of development costs. However, from 2016 this fund was rolled into a Home Building Fund, which is open to applications for a wider range of purposes including development for owner occupation. The UK Government has also launched a Private Rented Sector Housing Guarantee Scheme (effective from 2016), which is a government-guaranteed bond program for financing loans, and the Scottish Government is developing its own Rental Income Guarantee scheme to improve the viability of 'Build to Rent' proposals for private renting and hence access to finance.

At the same time, however, the UK Government's austerity policy has targeted the Housing Benefit paid to tenants: indexation rates have been frozen and, for single persons to age 35, payments reduced to a 'shared accommodation' rate. These are material reductions to tenants' incomes, and hence to the rental revenue base of landlords. By contrast, the 'Build to Rent' subsidies are contingent and less material. The balance may weigh against a net benefit or encouragement to build.

## 5.3 Large corporate landlords

Although smallholding individual persons remain the dominant type of landlord in all four countries, the more eye-catching institutional change is the growing significance of LCLs in each country (Figure 21). The origins of the LCL sector in each country are diverse, but all have at least some degree of government involvement.

**Figure 21: Large corporate landlords—United States, Ireland, Germany, United Kingdom**

United States		Germany	
Mid-America Apartments (MAA)	99,939 apartments	Vonovia	333,000 apartments
Starwood Capital	85,500 apartments	Deutsche Wohnen	158,000 apartments
Invitation Homes (including Starwood Waypoint)	82,000 single family houses	Grand City Apartments	83,000 apartments
Equity Apartments	78,000 apartments	Akelius Residential	20,000 apartments in Germany (46,500 worldwide)
Avalon Bay Communities	74,500 apartments	United Kingdom	
Hunt Companies	62,000 apartments	Grainger	8,600 dwellings
Edward Rose	61,500 apartments	L&Q PRS*	1,500 dwellings
Lincoln Property Company	60,000 apartments	Annington Homes	1,400 dwellings
Ireland		Folio London*	950 dwellings
I-RES	2,400 apartments	A2 Dominion Group*	850 dwellings

Notes: \*Subsidiary of a housing association; 'dwellings' refers to PRS dwellings only.

Source: BBSR (2017); NMHC (2017); Future of London (2017); Grainger (2016); Brennan (2017).

### 5.3.1 LCLs in the United States

LCLs have a long history in the United State. For example, in 1973 Trump Corporation was reported to have owned 14,000 apartments in New York City when the company's president made his first media appearance (as the subject of legal proceedings under fair housing legislation for discriminating against black prospective tenants) (Kaplan 1973). Currently, the largest American LCL in terms of units owned is Mid-America Apartments (trading as MAA), the product of the 2016 merger of Mid-America Apartment Communities and Post Properties, which were each established in the 1970s. The second largest LCL, Starwood Capital, commenced in the aftermath of a prior financial crisis in the United States: the Savings and Loans crisis of the late 1980s. Some of the largest landlords came out of ancillary sectors. Equity Residential began in the 1960s as a manager of student accommodation and still operates in that sector; Greystar (44,000 apartments owned) is also the United States' largest property manager (400,000 units under management).

The major change in respect to American LCLs is the rapid growth of a sector specialising in single-family properties. This sector emerged in response to the crash in house prices that followed the GFC, and particularly the massive incidence of foreclosures, with private equity funds using their scale to make bulk purchases of properties and to invest in the development of automated property search and valuation technologies for speedy bidding and acquisitions (Fields 2017). From 2012–24, private equity funds purchased 200,000 single family dwellings for rental, with Blackstone's Invitation Homes spending \$100 million per week at one stage in

2013. At 2016, the seven largest LCLs in the sector owned between them 170,000 single family dwellings (Green Street Advisors 2016). Typically properties are renovated prior to rental; the LCLs claim a role in overturning the ‘blight’ that mass mortgage foreclosures inflicted on neighbourhoods (National Rental Home Council 2017).

Another notable development in the sector is its consolidation: for example, the Mid-America Apartment Communities and Post Properties merger and the recent merger of Invitation Homes and Starwood Waypoint Homes—the latter (Starwood Waypoint Residential Trust) having previously merged with Colony American Homes (Goldstein 2017).

### **5.3.2 LCLs in Germany**

Germany has a sector of nine LCLs that are listed on the stock exchange. Some have been in existence for more than 100 years (if not operating at their present size and focus on the PRS), while others have emerged from the private equity firms that purchased former municipal housing and industry-related housing around the turn of the century. The largest German LCL, Vonovia, started life as Deutsche Annington Immobilien SE, which purchased 64,000 residential properties from the German Federal Railways in 2000. Deutsche Annington was established by Nomura International Principal Finance Group (PFG)<sup>5</sup> and named after Nomura’s initial UK housing venture, Annington Homes, which had purchased a portfolio of Ministry of Defence dwellings in 1996 (Watt 2017). Like the US sector, the German LCLs have been consolidating: for example, Vonovia is the product of a 2015 merger between Deutsche Annington and GAGFAH. It has subsequently sought unsuccessfully to acquire the second largest LCL, Deutsche Wohnen, and has acquired a large Austrian housing company with housing in Austria and Germany.

### **5.3.3 LCLs in Ireland and the United Kingdom**

By comparison with the largest LCLs in Germany and the United States, Ireland’s largest LCL, I-RES (2,400 apartments), is modest. However, several large private equity funds and REITs have taken indirect positions in Irish property, including the PRS, through the purchase of loans with properties pledged. Since the housing crash, 90,000 property-related loans have been disposed of by NAMA; at one stage NAMA was in receipt of rents from 10,000 rental properties (Pope 2016). In several cases, purchasers of mortgages in default have sought to evict tenants en masse, including the prominently reported Tyrrelstown case, where a Goldman Sachs affiliated fund bought the loans of a failed developer-cum-landlord and sought to gain possession of rented properties (Alderman 2016).

In the United Kingdom, successive governments have been encouraging ‘institutional landlords’ since the late 1990s with the particular objective of developing new rental housing supply. Grainger plc has focused its business on ‘Build to Rent’, but otherwise the major actors are non-profit housing associations, and it remains a nascent sector. Recent policy interventions to encourage the sector’s development include the subsidies discussed above, as well as planning system support (Future of London 2017).

### **5.3.4 LCL operations**

The business models of LCLs are not entirely clear. It has been assumed that LCLs would be more interested in rental yields than capital gains and would tend towards specifically configured housing stock: large complexes, possibly purpose built (Oxley, Lishman et al. 2010: 5). However, the German LCLs have made relatively little investment in new construction and,

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<sup>5</sup> Spun out in 2002 as Terra Firma Capital Partners. Terra Firma purchased Annington Homes from Nomura in 2012.

in contrast to the 'build and hold' strategy of the municipal housing companies, are quite active in buying and selling properties and in carrying out modernisations for energy efficiency, which allow rent increases above the local reference rent. Ireland's I-RES was reported to be planning to grow its portfolio by 25 per cent (600 units) through new construction but in fact has built 60 units (Brennan 2017). The American single-family LCLs have not invested in new construction, instead buying and renovating existing stock. Some have sold a lot of stock, even as they have grown, as properties have been found not to conform to the LCL's expectations or strategy (Olick 2017). These LCLs have also favoured 'sunbelt' over 'rustbelt' locations (Fields, Kohli et al. 2016), suggesting that they are at least as interested in the prospect of capital gains as in rent flows. Our country expert for the United States questions whether these LCLs may yet sell their holdings if house prices continue to climb.

The rise of LCLs has been controversial. In Ireland, LCLs are commonly known as 'vulture funds', because of the opportunism of the private equity firms that targeted impaired property-related assets following the housing crash. The association was unwittingly encouraged by Blackstone CEO Stephen Schwarzman, whose description of the company's acquisition strategy in a speech at the Goldman Sachs U.S. Financial Services conference in 2010 was re-reported in the Irish media some years later in the context of relevant acquisitions in Ireland:

*... As we look at the current situation in Europe, we're basically waiting to see how beaten up people's psyches get ... You want to wait until there's really blood in the streets. (The Irish Independent 2014)*

I-RES bristles at the 'vulture fund' term being applied to it, while acknowledging that other funds have 'sat on' the sites they acquired (Brennan 2017). In response to the Tyrrelstown controversy, the Irish Parliament legislated to impose additional obligations specifically on larger landlords in their dealings with tenanted properties. Consequently, where a landlord sells 10 or more properties in a multi-unit development within six months, the sales must be subject to the existing tenancies continuing (section 35A, *Residential Tenancies Act 2016* (Ireland)).

In Germany, the LCLs have a record of poor relationships with tenants to the extent of being the subject of popular protests in the 2000s (Lawson, Legacy and Parkinson 2016). Even Vonovia's company history acknowledges that in the early post-privatisation phase 'the business model pursued was not the hoped for success', with inadequate maintenance and investment, 'persistent tenant complaints' and reputation damage (Vonovia 2017). Since then, the LCLs have been publicly floated and original private equity firms have largely departed the sector, but relations with tenants are still reportedly 'strained and conflictual' (BBSR 2017: xi)<sup>6</sup>. Practices around rent increases appear to be a particular point of contention with tenants reporting LCLs mischaracterising repairs and maintenance as improvements to justify rent increases and seeking to challenge or avoid the *Mietspiegel*.

In the United States, some housing advocacy organisations have voiced concern about 'the rise of the corporate landlord', particularly in the single-family dwelling sector, and suggested that these LCLs might be more inclined than smallholding private landlords to increase rents, deny access to vulnerable or higher-risk persons (including Section 8 voucher holders) and fail to do repairs (Fields 2014). A study by Raymond, Dockworth et al. (2016) of termination proceedings in Georgia indicates that LCLs overall are more likely than other landlords to issue termination notices; they also observed significant variation between LCLs.

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<sup>6</sup> Based on a survey of tenants conducted by the German Tenants' Union and reported by the Federal Institute for Research on Building, Urban Affairs and Spatial Development (BBSR 2017).

## 5.4 Paths of regulatory reform

The recent experience of PRS regulatory change across the four countries has varied according to the history and circumstances of each country.

### 5.4.1 Enduring regimes in Germany and the United States

Germany's landlord–tenant legal regime has been in place for more than 40 years with a recent extension of regulation into rents for new tenancies. The basic features of the system enjoy popular support. These include rent increases according to local reference rents that follow but lag the market in new rents, and the assurance of tenants' security through limited prescribed grounds of termination. Our country expert suggested that supporters include landlords, who are conscious that an attractive rental market and stable tenancies are a benefit to their investment plans. There is no popular agitation for radically changing the system and our country expert thought it would be 'political suicide' for any political party to propose to do so.

At a national level, the United States has also largely stuck with its longstanding regulatory regime. It is involved in regulating against anti-discrimination through the *Fair Housing Act* (Title VIII of the *Civil Rights Act of 1968*) and ties conditions relating to the physical standard of properties to its Section 8 vouchers, but otherwise leaves most aspects of landlord–tenant regulation to the states and cities. In 1972 the National Conference of Commissioners on Uniform State Laws drafted the *Uniform Residential Landlord and Tenant Act 1972*, which has been influential in numerous states (National Conference of State Legislatures 2017). However, as we indicated in our overview, states and cities vary widely in the degree of protection afforded against rent increases and tenancy terminations by landlords, and change is contested between those levels of government.

### 5.4.2 Diverging paths in Ireland and the United Kingdom

Both Ireland and the United Kingdom have recent experience of deliberate programs of regulatory change. For over two decades of PRS growth, Ireland has successively increased regulation after the unplanned decontrolling of the sector (then much smaller) in the early 1980s, with the *Residential Tenancies Act 2004* (Ireland) being the major reform of the period. The experience has parallels with the Australian states that rolled back rent controls in the 1960s, leaving a patchwork of protection, older statutes and common law until modernised by the residential tenancies law reforms of the 1970s–90s. In Ireland's case, the 2004 reforms were also shaped by the government's shift away from social housing provision by local authorities, and a sense that increased reliance on private market provision should entail some assurance about landlords' conduct, rents and security.

Ireland's distinctive cyclical restrictions on tenancy terminations ('*Part 4*' tenancies, as discussed at 4.3.2) are the most remarkable feature of that phase of reform. The most recent phase of reform has extended regulation on this model, particularly in response to post-crash housing hardships, lengthening the cycle of '*Part 4* tenancy' protections and introducing additional provisions regarding rent increases in 'rent pressure zones' and protections against eviction where mortgagees become entitled to possession of a property. The Irish Government expressly presents these reforms as part of delivering 'a vibrant rental sector [that is] a flexible tenure choice for households and a bulwark against an over-reliance on owner occupation' (Government of Ireland 2016b: 1).

The United Kingdom has proceeded differently with parts of the UK lately taking divergent paths. With the introduction of the *Housing Act 1988* (UK), the British Government instituted a deliberate program of PRS deregulation which would unfold over the subsequent two decades as tenancies turned over and new contracts on the deregulated model (assured shorthold tenancies) were taken up. With access to owner occupation cut off by rising house prices and restraints on incomes, particularly for households with children, discontent with the lack of legal

assurance of security in the PRS has mounted. In response, the UK Government has resisted tenancy law reform as more 'red tape' and sought instead to subsidise home purchase by owner-occupiers (including through an extended 'Right to Buy') and encourage the 'Build to Rent' sector (Moore 2017). The Scottish Government, however, has pursued law reform as well as 'Build to Rent' development. After an extended process of consensus building around PRS law reform, it legislated in 2016 for limited prescribed grounds for termination and limits on rent increases in 'rent pressure zones'. As in Ireland, these reforms are presented as part of a strategy that 'inspires consumer confidence' in a growing PRS (Scottish Government 2015: 1).

The divergence of approaches is apparent even in an area of common activity: landlord registers. Scotland and Wales have established registers that take stock of their respective sectors and instituted a general improvement of standards (through training in Wales, and through a check for unfitness and impropriety in Scotland). The UK Government, however, having made provision for local authorities in England to establish registers, has gone to pains to make the registers partial and selectively applied to problem areas only.

Our overview of the 10 countries suggests that the 'red tape' view of tenancy regulation and investment is not supported by practice: most countries regulate to a greater degree than the UK and Australia and their predominantly smallholding landlords cope; the example of Germany indicates that LCLs, too, are not discouraged by a relatively high degree of tenancy regulation.

## 5.5 Key findings

- Germany avoided the combined financial and housing crises experienced elsewhere because of a range of institutional factors including its conservative home lending sector and the withdrawal of some housing subsidies. It may be that some features which are spurs to speculation in other contexts, such as negative gearing and capital gains tax exemptions, are not activated in the specific German context.
- The responses of Ireland, the United Kingdom and the United States to their financial and housing crises have facilitated existing owner-occupiers and large financial institutions to increase their position in property, with some curbs around riskier bank lending. This may be no more sustainable or equitable than the pre-GFC housing credit expansion.
- In trying to shape the housing outcomes of a growing PRS, Ireland has taken a strategic approach that joins subsidies and regulation. The United Kingdom's 'Buy To Let' incentives may be outweighed by the material reduction in demand subsidies paid to tenants.
- The rising LCLs are not building much rental housing but are mostly acquiring existing properties and actively managing their portfolios through renovations, modifications and sales. They have also been active in mergers and, particularly in the United States, devising new financial instruments. 'Institutional landlords' are a standing item on the Australian housing policy agenda. We should start specifying what we really want from them.
- The view of tenancy regulation as 'red tape' is out of step with the recent experience of most countries. Smallholding individual landlords and LCLs operate without undue difficulty in more strongly regulated PRSs than Australia's.

## 6 Conclusion: policy development implications

In the preceding three chapters we presented key findings from our international comparative analysis. These key findings are brought together in the Executive Summary. We conclude by considering the implications of our comparative analysis for the development of policies for the PRS in Australia.

### 6.1 Housing system contexts

The relatively high degree of resemblance between the profiles of the Australian PRS and the wider housing system (relative to those in the reference countries) implies a high degree of integration, particularly between the private rental and owner-occupied markets (see Figure 3). This implies that policy settings and market conditions applying to one will have effects which are transmitted readily to the other. Hence, policies that make special or preferential treatment for owner-occupied housing will also induce purchase of housing for rental. Similarly, rental housing investor activity will directly affect prices in the owner-occupied sector and the accessibility of properties for owner-occupiers.

A long line of AHURI research reports and other reports and representations from housing sector stakeholders has recommended that Australian governments should conduct housing policy through dedicated housing ministries with a brief that takes in the whole housing system. The present research underscores this recommendation. Our review of the situation in the nine international jurisdictions suggests that Australia needs this integrated approach to housing policy governance even more than most countries.

Another implication of the similarity in household composition (Figure 5) between the Australian PRS and wider housing system relates to equality. Australian households of similar composition and similar incomes differ in their housing tenure. Considering the traditional valorisation of and preference for owner occupation in Australia, this suggests that housing tenure may figure strongly in the subjective experience of inequality. The relatively stronger representation in the Australian PRS of higher income households (Figure 6) and larger households (i.e. with children) (Figure 5) also suggests that increases in Australian household size and incomes are less likely to entail a shift from renting to owner occupation. This raises the question as to whether housing may be a primary driver of inequality and not merely the outcome of inequality or difference in other aspects of life. If recent trends of reduced access to owner occupation and longer stays in the PRS continue, we might expect this experience to sharpen.

Australian housing policy discussions are usually directed to improving affordability; it would be wise to think also about how to conduct equitable housing policy in the event of a housing crash. At the level of the housing system, the integration between the Australian PRS and owner-occupied sectors heightens the prospect of investment in both sectors collapsing simultaneously, with little established institutional capacity for countercyclical investment that makes necessary additions to supply. Furthermore, Australia's extended period of house price growth has left a very high level of housing-related debt amongst households—though mostly not amongst households living in the PRS. In the event of a crash these liabilities remain, and the question of their relief involves doing justice not only between creditors and debtors, but between debtor and non-debtor households. In Ireland, the United Kingdom and the United States, finance-sector focused responses to the GFC increased the position of large institutions in the housing sector, and households who had sat out the housing boom have generally not seen their access to affordable home ownership or rental housing improve.

## 6.2 Financial settings

Finance settings have driven rapid change in PRS institutions, often without guidance from conventional housing policy objectives—especially in countries that have experienced a housing market crash. Australian macroeconomic policy should look further than its effects on financial system stability or housing market levels to keep in view its effects on housing system institutions and housing policy objectives. This applies not just in responding to crises: for example, the specific effects of housing-related macroprudential tools on the investment strategies and borrowing practices of PRS landlords are worthy of investigation.

On the other hand, tax settings—for example, the exemption of owner-occupied housing from capital gains tax and treatment of housing investment costs such as negative gearing and depreciation—have long been consciously used to shape housing markets and outcomes, although with a great deal of contestation around the objectives, operations and other consequences of these settings. As in other policy areas, housing policy generally regards taxation as a policy instrument par excellence, capable of both strong and fine influences on economic behaviour and outcomes, and market structures are often read or explained as the result of tax settings (Yates 2009; AFTSR 2010; Wood, Ong et al. 2012).

The present research, however, challenges some conventional readings with cases of unexpected synergies and relative oddities. For example, Australia and Germany's treatment of negative gearing and capital gains tax underlie quite different housing market outcomes: speculative inflation in Australia; relatively steady house prices in Germany. The United Kingdom taxes landlords more heavily than most other countries, yet has a faster growing PRS than most countries included in our survey.

Such conflicted findings should not to diminish the explanatory power or effectiveness of tax settings in each country's housing policy. Rather, they show the necessity of considering taxation and other policy settings in interaction with each other and in wider systemic contexts. Strategy in Australia for the PRS should join consideration of finance, taxation, supply and demand-side subsidies and regulation with the objective of making PRS housing outcomes competitive with other sectors.

## 6.3 Landlords

'Institutional landlords' are now a standing item on the Australian housing policy agenda. Considering the international variation and opacity in LCL business models, and the record of controversy and conflict in some of their operations, a key implication for policy development is to specify what sorts of institutional landlords we really want, how we will get them, and how we will ensure they deliver desired housing outcomes.

For years policy-makers and housing advocates have looked to the community housing sector as the prime candidate for this role, envisaging its transformation into an affordable housing industry that works across the housing sector towards a wide range of housing policy outcomes in housing supply, affordability, security, social housing renewal and community development (Milligan, Pawson et al. 2017). A crucial aspect of this vision is that the industry is mission-oriented and not-for-profit, with a distinctive ethos of housing justice and client service. Many housing affordability policy measures have been developed with these organisations in mind, both as a means of supporting the development of the industry and as a means of strengthening the integrity and effectiveness of the measures. Examples include the NRAS, development contributions and inclusionary zoning and the bond aggregator model of housing investment finance (Lawson, Berry et al. 2014).

With interest in the prospect of 'Build to Rent' and 'multifamily housing' rising in the property development and finance sectors, there is a risk that affordable housing policy may be

colonised by for-profit interests: for example, a large developer proposing to satisfy an inclusionary zoning requirement by placing housing units with an associated for-profit LCL. The development of a for-profit LCL sector may be desirable in terms of greater professionalisation and efficiencies in the management of tenancies and properties, but should be in addition to, and not at the expense of, a mission-oriented industry that makes a distinctive contribution to housing outcomes.

## **6.4 Regulation**

Both smallholding individual landlords and LCLs operate without undue difficulty in more strongly regulated PRSs than Australia's. The high degree of integration of Australia's PRS and owner-occupier markets has implications for PRS regulation, specifically as regards security, because the prospect of a property transferring into owner occupation is at odds with legal instruments (e.g. a long fixed-term lease) that ensure that a property will remain available for rent. However, even amongst countries with more differentiated sectors, security is more often legally assured by provision for termination on prescribed grounds only. This approach is consistent with the structure of the Australian PRS and could be adopted here.

The present research identifies a range of contemporary approaches to rent regulation, mostly variations on a stated guideline or reference rent, that could be considered for implementation in Australia. These curbs on rent increases are employed both in countries that treat rental losses similarly to Australia (e.g. Germany) and in countries with less generous provisions (e.g. Canada). In the Australian context, our negative gearing provisions would cushion losses associated with rent regulation, but the cash flow advantage for landlords relative to owner-occupiers, and hence potential leverage, would also be reduced.

Australia already has some experience in the use of registers, particularly in some marginal sectors of the PRS (e.g. boarding and rooming houses). Establishing registers for mainstream PRS landlords may be worthwhile too, considering current institutional changes. With regards to the smallholding landlords who dominate the PRS sector, a registration requirement, particularly if linked to light training and education obligations and disclosure of any disciplinary action, could help lift standards of service in a growing sector with many new entrants. Register data would also add to what we know about PRS landlords, especially multiple property landlords on whom detailed data is currently lacking. Should a for-profit LCL sector emerge, registers would provide important data as to their presence in local markets and potential for monopolistic rent pricing.

## **6.5 The future of private rental housing**

International comparisons cannot show us the future of private rental housing in Australia, as conditions in international jurisdictions will necessarily differ. The future of private rental housing in Australia will be made by a range of institutional actors—policy-makers, regulators, financiers, developers, managers, landlords and tenants—but not just under the circumstances of their choosing. The present research suggests that the salient features of these circumstances are the high degree of integration between the Australian private rental and owner-occupier markets, the high level of housing-related debt and the implication of housing in financial activity and regulation, and a growing body of international practice by LCLs. It also indicates scope for positive action through a cross-sectoral housing policy, encouragement of a sector of mission-oriented landlords, careful evaluation of the claims and activities of for-profit LCLs and regulation for improved security and other conditions in private rental housing.

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# Appendix 1: Private rental housing in Germany

By Stefan Kofner

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The most outstanding characteristics of the German housing system are the following:

- the development of a large rental housing stock by a combination of regulation and high housing subsidies (in particular fiscal) in the past
  - as a counterpart, a relatively low home ownership rate
  - at first glance, a high level of tenant protection, but with gaps, for example, generous modernisation-induced rent increases, and the effective limitation of newly agreed rents (split market)
  - comparatively static development of the legal framework of the rental housing market for almost 50 years, with the result that the system is rarely fundamentally challenged
  - a market-oriented rent price regulation setting, at least in the long term, which does not limit the returns of home owners too strictly
  - the pronounced tenure neutrality in housing subsidisation, in combination with a low level of subsidies for ten years (both home ownership and rented housing construction are minimally promoted)
  - conservative financing practices, embedded in the structure of the banking system, which ensure a high level of credit quality in home financing
  - low house price volatility
  - a very large private rental sector
  - the sale of some very large public and factory-related housing companies to financial investors and subsequently the formation of a major sub-sector of large listed housing companies
  - a previously significant, but now only modest, social housing sector
  - the temporary subsidisation of social housing, with subsidised housing losing its social status in the medium to long term.
- 

## 1.1 Housing system context

In international comparisons the German housing system stands out for its long-term house price stability—Germany avoided the housing boom and bust experienced in other countries in the 2000s—and a PRS that is remarkably large (housing 48% of households, it is the largest sector in Germany) and strongly regulated with regard to rents and tenants' legal security.

### 1.1.1 History

The origins of Germany's distinctive housing system lie in the country's experience, following the Second World War, of political division (into West and East Germany, and Berlin into West and East Berlin) and an acute housing shortage lasting until the early 1960s in the West and much longer in Eastern Germany (Kofner, 2014b: 267). In East Germany, the large majority of new housing was state-owned public property housing, often constructed as vast multi-unit estates. In addition, housing cooperatives have built a considerable number of apartments in the GDR. A smaller percentage was provided by individual owner-occupiers. The East German private rental sector was subject to heavy controls on rents and tenancy allocations (Kofner 2017) and as a result any profitability perspective soon disappeared for private landlords.

In West Germany, housing policy was conceived according to 'social market economy' principles. It provided strong incentives for new construction to municipal housing companies and private landlords alike. The policy was a mixture of heavy incentives and gradual deregulation. There were three levels of incentive creation:

- first, a generous tax treatment of depreciation and rental losses
- second, a gradual exemption from heavy rent, eviction and allocation controls starting with new residential developments (private rental)<sup>7</sup>
- third, social housing programs of enormous volume, that is low interest loans and direct subsidies, in return for which landlords submitted to limitations on rents and eligibility thresholds for tenants for up to 50 years (Whitehead, Scanlon et al. 2016: 50–51; Kofner 2003: 322–328).

In the reconstruction period the bulk of social housing subsidies was provided for by the Federal Government. The federal subsidies were, however, severely reduced after the large initial housing shortage had disappeared by the mid-1960s in West Germany. Since the turn of the millennium the design of social housing programs is assigned to the states. There is however still an important element of federal co-financing of the whole volume of subsidies. The federal states may increase the federal funds as they please and distribute the means according to their own priorities.

In West Berlin, the municipal housing companies were especially significant (Fields and Uffer 2016: 1491). Apart from that, a particularly large number of social dwellings was built in West Berlin and the rents in the older houses remained controlled longer than anywhere else in West Germany (Hanuske 2001).

In West Germany the formation of individual owner-occupied housing was encouraged from the outset by increased depreciation (Kofner 2003: 331). Also, from 1956 the focus of the social housing subsidies was shifted: from then on, home ownership formation was given more priority in order to help the low-income strata of the population to become owner-occupiers, too (Kofner 2003: 327). The share of home ownership permits of the total social housing permits (i.e. notice of grant approval) in the period 1950–56 was 42 per cent, then rose to 46.6 per cent in the period 1957–69.

Allocation, eviction and rent controls were largely abolished in West Germany in the 1960s, but this deregulatory phase was short lived. By 1971, the Federal Government implemented a new regime of rent and eviction controls that remains in place today (Kemp and Kofner 2010). In 1989, federal tax reform placed not-for-profit housing companies on the same footing as for-profit landlords. The special regulatory status and, therefore, the whole institution of public

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<sup>7</sup> Allocation controls meant that apartments could not be let freely, but were allocated by housing agencies to members of certain groups of needs.

interest housing was completely abolished. This is a major difference compared with Austria, the Netherlands and Great Britain.

Since the early 1960s to the late 1980s, federal grants for social housing have been steadily declining. However, following reunification in 1991, construction of subsidised rental housing throughout unified Germany again increased to accommodate an influx of persons from the former Eastern Bloc and also from the former GDR to West Germany. In East Germany rental housing in public ownership was transferred to communal housing companies (Whitehead, Scanlon et al. 2016: 53). Private landowners or their heirs could demand the return of their property.

Through the 1990s, German economic growth slowed, and social housing subsidies were curtailed by the Federal Government. Also former federal agencies like rail and postal services sold their factory-related housing stock to financial investors after they were privatised themselves or transferred into a private legal form, respectively. In the following decade some municipalities like Dresden, Kiel and Berlin also sold their municipal housing companies to financial investors (Held 2011).

Unlike in most other countries, where sales to sitting tenants were preferred, a considerable part of the ex-public housing stock in Germany went to the PRS, and in particular to an emerging subsector of large corporate landlords (discussed below). The sale of almost all of the private factory-related dwellings to such investors has also contributed significantly to the growth of this subsector. It is, however, still much smaller than the public or the cooperative housing sector. In addition, there have been hardly any new privatisations of public housing companies for years.

In 2006, the two major supply subsidies provided by the Federal Government—the increased rate of depreciation for tax purposes of new-built rental housing, and a grant for owner-occupiers (Eigenheimzulage)—were cancelled, and not replaced.

The significant cuts in housing subsidies were a government initiative not primarily motivated by housing market-related reasoning. In an environment of housing market relaxation the corresponding changes were enforced against heavy resistance by the affected lobby groups (Woebken-Ekert 2005). The abolition of the home ownership grant was basically justified with the need to improve the budget situation of the public sector (draft bill, Bundestagsdrucksache 16/108, 29 November 2005). This decision to abolish the two most important housing subsidies at the same time was a fundamental change of political priorities. Since then the German government runs the housing system with negligible subsidies, by international comparison.

In this entire period, owner occupation was never the majority tenure in Germany, despite continuous policies intended to increase owner occupation—such as the possibility to deduct depreciations on the cost of production and acquisition from income with changing depreciation rates, and the repeated phased introduction of a tax deductibility of mortgage interest. Also capital gains have always been 100 per cent exempt from income tax.

The tax deduction possibilities were replaced by a generous grant system in 1996 (Eigenheimzulage) which was abolished in 2006. Since then home ownership subsidies are negligible in Germany by international standards, except for the capital gains privilege which is consistent with the idea to regard the private home as a consumption good for tax purposes. The so called 'Riester' subsidy of old age provision schemes is available for purchases of owner-occupied housing, but it applies also to the accumulation of financial assets.. All in all, there has been a lack of continuity and persistence in the promotion of home ownership, so that greater successes have not been achieved. Also, there has never been a clear bias, compared with the subsidisation of rental housing.

Another part of the explanation for the low German home ownership rate might be found in cultural attitudes towards home ownership. Owner occupation, it appears, has a distinctive place in the German life-course: owner occupation—if at all—is entered into relatively late in life

(the average age is 40) and for many it is a 'once in a lifetime' undertaking (Kemp and Kofner 2010: 389). Also, German property transfer taxes (stamp duties) are relatively high: between 3.5 and 6.5 per cent depending on the state.

According to the results of the housing and building survey in 2011, one-third of the housing stock is accounted for by large multi-family houses (containing seven or more apartments), family houses and houses with two to six flats, respectively.

There is a clear correlation between built form and tenure: 80 per cent of the apartments are rented, whereas 80 per cent of the individual houses are owner-occupied (Kemp and Kofner 2014).

For the past 20 years, Germany's population has been fairly stable (except for a spike in growth from the response to the Syrian refugee crisis). In fact over the past 10 years it has slightly contracted, though the number of households has grown.

However, the development of the population is spatially very differentiated and characterised by an increase in internal migration. A polarised situation emerges between demographic winner and loser regions, which, of course, also affects housing markets. Over the last five years, house prices have sharply increased in more cities, as have rents. However, even in a year of federal elections, wealth inequality and the role of Germany's distinctively structured housing system in creating and cementing wealth inequalities is hardly ever discussed publicly.

### **1.1.2 Tenants**

The majority of younger and middle-aged households are tenants in Germany. More than 90 per cent of households under 30 are tenants. In the 30–40 age group, the proportion of tenants is about 70 per cent.

Also, households in lower income strata and smaller households (especially single person households) have a higher probability to be tenants. Whilst 72 per cent of one person households (the largest group of households) are tenants, the proportion is less than 50 per cent in all other household size groups and falls with household size.

Not surprisingly, there is a clear correlation of home ownership and income. In the group with a household income above €4,500 only 25 per cent rent. In the income class €3,200–4,500 about one third of the households are tenants. On the other hand, 71 per cent of the households with an income below €2,000 are tenants. Thus, the smaller and the poorer a household is in Germany, the higher is the probability that it is a tenant household.

There is no data available about the structure of tenants in the different subsectors of the rental market. Only about the tenants of the small private landlords is some information available (see below). What we know for sure is that the German PRS houses a wide range of households of all generations, income groups and household sizes. Due to its enormous share in the total rental housing market (78%), the distribution of PRS tenants according to these three criteria (age, size and income) should be similar to the distribution of tenants as a whole across all subsectors of the rental housing market.

The major professional landlords are more or less all focused on the lower to middle income strata, because their housing stock largely consists of current or former social housing. Explicit positioning strategies are rare. Among the listed companies Akelius specialises in the luxury segment and Grand City Properties in the lower end of the market. There are also landlords who have focused on certain target groups such as students.

The competition among tenants with different income levels is very strong in tight housing markets. The low-income tenants also come under pressure because offensive revaluation strategies inevitably lead to displacement effects and may contribute to the gradual

gentrification of neighbourhoods. However, some smaller private landlords tend to be the main perpetrators in this field, by modernising old-town residential buildings extensively.

A recent survey of private landlords (only private persons including co-ownership and communities of heirs) of multi-family houses and condominiums indicates that the fluctuation rates are above average and the average length of a tenancy is below average. The fluctuation rate is 14 per cent for condo tenants of small private landlords (BBSR 2015: 125) compared to 9.3 per cent among all tenants<sup>8</sup>. In the survey commissioned by the BBSR agency, the highest fluctuation rate was found at 19 per cent for the smallest units (one and two room apartments). Larger dwellings exhibit significantly lower fluctuation rates, between 11 and 13 per cent, and thus longer tenancies. The average length of a tenancy for a condominium is only 6.9 years (BBSR 2015: 125) compared to around 10 years for all tenants. It is even lower (around five years) for smaller apartments.

In terms of family structures, 44 per cent of new tenants are single households (the total share of single households in Germany was 41.4% in 2015). Couples without children make up 24 per cent (building ownership) and 32 per cent (condo ownership) and couples with children account for 18 and 16 per cent, respectively. Also, the proportion of single parents is somewhat higher among building owners (9% compared to 6%). Apartments in large multi-family buildings were often given to singles, whereas couples with children were common in smaller multi-family houses (BBSR 2015: 128–129). Unemployed tenants are clearly underrepresented in newer buildings.

The proportion of tenants with an immigrant background (21%) corresponds exactly to their share of the total population in the case of condo owners, whereas it is significantly lower (11%) for building owners (BBSR 2015: 132).

## 1.2 Financial settings and subsidies

### 1.2.1 Finance

The German system of housing finance has some peculiarities. German banks' lending practices remain conservative: interest-only loans are regarded as exotic and are rarely used (Kofner 2014b: 270–271).

This could be a reflection of the structure of the German banking system. Regionally limited public and cooperative credit institutions and specialist banks (Bausparkassen) play a major role in the system. These institutions have particularly high market shares in private home financing. The refinancing of mortgage loans is obtained less by securitisation and more by deposits, including building savings deposits and covered bonds. These structures have a favourable influence on the credit quality and tend to decrease the spread of innovative mortgage loan products in the housing finance system.

Thus, the conservative nature of housing finance in Germany is primarily a consequence of the specific and unique structure of the banking system. Another factor is a lack of demand for mortgage credit from younger and poorer households, since they use the large and differentiated rental housing market to meet their housing needs. Government regulation directed at restricting the mortgage lending behaviour of banks played no significant role until very recently.

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<sup>8</sup> techem Pressemeldung Number 5, 3. May 2016.

## 1.2.2 Tax

As explained above, the German PRS was built up with the support of tax settings that subsidised new construction, particularly through generous deductions for depreciation. Since 2006, these settings have been removed. The main features of the current German taxation system for private lettings are:

- taxation of residential letting as an investment and hence mortgage interest, operating and depreciation cost deductibility
- immediate deduction of repair expenses from rent income
- negative gearing
- capital gains taxation privilege.

Residential letting is taxed as an investment in Germany. Landlords pay income or corporate income tax on their net rental income. The profit from letting for the purposes of taxation is calculated as follows:

*Rent revenues minus Interest cost minus Operating costs minus Depreciation minus Maintenance costs.*

The deductible costs have to be incurred and traceable and they have to have a causal relation with the respective rent revenues. If these prerequisites are met, they are fully deductible. There is only an upper limit on depreciations.

Borrowing costs including mortgage interest payments are deductible as income-related expenses insofar as they are paid for a loan taken up in order to earn the respective letting income.

Operating costs include administration costs, current maintenance costs and rent losses due to vacancies or rent arrears, and are also fully deductible.

Depreciation is linear with 2 or 2.5 per cent for older buildings, respectively<sup>9</sup>. This should be consistent with economic depreciation by and large. Depreciation costs can be deducted for both newly built and existing properties acquired by the landlord for a period of 50 or 40 years depending on the year of completion. Each time a property is sold, the depreciation is reset. Thus, a property can be depreciated over centuries by successive owners.

Until 2005 the decreasing balance method of depreciation for new residential development was applicable. According to this rule, 40 per cent of the acquisition and production costs could be deducted from rental income already in the first 10 years of use of the property (today only 20 per cent). Consequently, in the past multi-family rental buildings were regarded as good tax-saving vehicles, especially by self-employed people like master craftsmen and other high earners.

Buildings under monumental protection and buildings located in statutory redevelopment or preservation areas still benefit from a higher depreciation scheme.

The most important general tax subsidy for German landlords is the possibility to deduct repair expenses immediately from rent income under certain conditions.

*Negative gearing*, the possibility to offset losses from rental property against other income, has been applicable in Germany since 1949, and is independent of the type, status and construction year of the property. Tax losses from a real property can be offset with profits from another real property without limit (horizontal loss offset). The vertical offset of losses is subject to certain

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<sup>9</sup> 2.5 per cent for buildings completed before 1 January 1925 and 2 per cent for buildings completed thereafter.

limitations. For example, foreign losses may only be offset with profits from the same country. In principle, however, even high losses from income letting and leasing can be deducted in full from surpluses generated from other sources of income (say income from self-employment). An exception applies to so-called ‘tax deferral models’, where losses can only be offset against future profits from the same investment. Tax deferral models are structures which aim to achieve tax benefits in the form of negative income. A directly possessed residential property can never be a tax deferral model. This applies only to closed-end property funds.

Both the deductibility of income-related expenses as well as the possibility of negative gearing can only be restricted by the German legislator within narrow limits because of the institutional property guarantee stipulated in article 14 of the German Grundgesetz. According to German understanding, these schemes cannot be regarded as generous or even as subsidies, as long as the depreciation rates applicable are within the scope of the economic depreciation of the assets.

On the other hand *capital gains* from the sale of rental properties are treated generously. Realised capital gains from the sale of residential rental property held privately for more than ten years are tax free unless the seller is considered a ‘commercial real estate dealer’ (i.e. a regular trader) or a corporation. Capital gains on buildings held as real business assets may be transferred to ‘replacing assets’ (i.e. newly built or acquired property). The complete tax exemption of capital gains from the sale of owner-occupied housing is even more generous, however. Compared with the tax treatment of capital gains on financial investments (25% withholding tax, regardless of the holding period) rental housing is privileged. In the current environment of rising house prices that may be an important investment motive for some buyers.

Public housing companies use private legal forms and are thus subject to the same tax rules as their private competitors. Housing cooperatives do not pay income-related taxes, however, if more than 90 per cent of their income comes from residential letting. Income from social housing stock is taxed just as income from any other type of rental housing—there is no difference in either determining the tax base, or with the tax rates.

This tax environment and, in particular, the tax exemption of capital gains could in itself be conducive to property speculation, however the abolishment of declining balance depreciation and the high rates of property acquisition tax restrain speculation. In addition, mortgage loans without adequate collateral and creditworthiness are difficult to obtain. This is due not least to the structure of the banking system and to the special refinancing conditions (Pfandbriefe, Bausparen).

German property acquisition tax is uniform, borne by the buyer and does not differentiate according to the type of buyer or seller or the type of property. The tax rates vary between 3.5 and 6.5 per cent (as of January 1, 2017) depending on the state. However, the property acquisition tax can be largely circumvented if, instead of the property, shares in real estate companies are traded. This means that the private homebuyer pays the full tax, whereas financial investors or listed housing companies hardly pay any tax at all, even if they take over residential portfolios with tens of thousands of dwellings.

### **1.2.3 Subsidies**

Subsidies benefit home owners and landlords or tenants, for example tax incentives for monuments (for home owners and landlords) or housing allowances (for home owners and tenants) but there seems to be no subsidies specifically tailored to rental housing. Federal housing subsidies have declined rapidly in recent years—federal subsidies for housing (grants and tax concessions) amounted to €6 billion in 2005, but in 2016 they had fallen to €0.8 billion. This large decline is attributable primarily to the almost complete abolition in 2006 of home ownership subsidies and the degressive depreciation scheme for new housing construction.

Supply side subsidies are currently focused on specific issues like energy efficiency modernisation, senior-friendly reconstruction, preservation of buildings and urban redevelopment, but do not include general tax subsidies any longer.

Social housing expenditure, on the other hand, is currently on the rise: federal funds for social housing promotion have been increased in two stages from €518.2 million to €1,518.2 million per year. However, the distribution of the funds depends on the population shares of the Länder. From 2020 onwards, after the expiry of the compensatory means, the states will have additional sales tax shares available (non-earmarked). Completion numbers in social housing are rising from a low level, but the number of newly built social rental dwellings is still very low. Since 2008, it has stagnated between 10,000 and 15,000 units a year.

Demand side subsidies for housing are much more important in Germany than supply side. There are two types of housing benefits:

- The instrument of housing allowances (*Wohngeld*) helps low-income families to finance their rent. *Wohngeld* is in fact a co-payment, that is it pays part of the rent, and the tenant pays the balance, hence the tenant still feels an incentive to try to find an affordable rental. If, for example, the tenant moves to a more expensive apartment, the subsidy will only cover a part of the additional costs. The *Wohngeld* allowance of a household is determined by the number of family members in the household, total family income, and rental amount. There is a legal claim to the housing allowance and it is independent of the status of the dwelling. Income limits and rental limits are applicable depending on household size and local rent level. At the beginning of 2016, the *Wohngeld* was adjusted to the rent and income development since the last reform in 2009. In 2016 the expenditure for *Wohngeld* amounted to almost €1.5 billion. The number of recipient households is around 900,000. The 2016 reform has significantly increased the number of entitled households. A two-person household, which received an average of €113 per month before the reform, now receives about €186 per month. The effectiveness of this instrument especially in tight housing markets is questionable, however if housing supply is rigid, it tends to raise rents.
- People living on social assistance cannot claim *Wohngeld* but receive housing benefit (and help with their heating costs) as part of their income support benefit. For example, unemployed people with insufficient income get housing benefit as part of *Arbeitslosengeld II* (ALG II). It is not a complementary social security benefit like *Wohngeld*, but instead a last resort safety net meant to ensure that people's basic living needs are met. Housing costs are fully covered, but only for what is deemed to be an 'adequate' home. Adequacy is subject to size and rent ceilings that vary regionally. This means that a tenant could rent a more expensive property, and pay the amount above the rent ceiling himself. The number of ALG II recipient households is much higher than the number of *Wohngeld* recipients—in January 2017, 3.268 million households (8% of all households) were in receipt of housing benefit and heating cost support with their income support benefit (ALG II). The total cost for this housing benefit was €14 billion in 2014.

## 1.3 Landlords and agents

### 1.3.1 Small landlords

Most German landlords are private persons: they own 65 per cent of all rental dwellings, and 83 per cent of the privately rented dwellings. In the case of the private landlords, the investing forms of acquisition predominated—45 per cent were purchases of existing dwellings and another 25 per cent were new apartments purchased or constructed by private investors. 17 per cent of the rented apartments of private individuals were inherited and only 12 per cent were donations (BBSR 2015: 62).

Among the acquisition motives, old-age provision and high security of the asset class were identified as particularly important or very important by a large number of respondents (80% and 72% respectively). Tax advantages, expectation of capital gains and purchase opportunity were identified as important by 40 and 50 per cent, respectively (BBSR 2015: 101). The numbers suggest that the amateur landlords have a long investment horizon for the most part, however, in the past five years, condos have increasingly been acquired for speculative reasons.

There is no clear picture of the financing structure (BBSR 2015: 104–108). While the average leverage ratio for newly built multi-family houses (a multi-family house is a building with at least 3 apartments independent of the tenure according to the definition given in the report) as well as for condos has declined from 65 to 54 per cent and from 72 to 59 per cent, respectively, if we compare the decades 1991–2000 and 2001–10, the leverage ratio has risen for the purchase of existing multi-family buildings (from 70% to 82%).

Especially in the case of solely condo property owners, small and very small monthly rental income streams from letting dominate, due to the fragmented ownership structure: 57 per cent of the private landlords have only one rented apartment and 87 per cent no more than five. Even among the owners of buildings, 65 per cent have no more than five apartments (98% of the condo owners). In terms of their letting income, 44 per cent of the solely condo owners have a rental income of up to €250 per month and 85 per cent of this group earn up to a maximum of €1,000 per month. Due to the higher average number of rental units, the owners of buildings have a significantly higher average income from letting. But also in this group about 16 per cent of the owners have rental income of less than €250 per month and over 40 per cent earn less than €1,000 monthly (BBSR 2015: 81, 88).

19 per cent of multi-family houses owned by private individuals are in third party administration (BBSR 2015: 124). There is a positive correlation with the portfolio size of the respective owner and the distance of the property to his place of residence.

The composition of private landlords by occupational status is similar to the composition of the total working population—42 per cent are pensioners (presumably holding the properties for stable rent revenue to supplement their pensions), 29 per cent are employees, 16 per cent are self-employed and 11 per cent are civil servants. While the latter two groups are overrepresented among private landlords, other groups such as students and the unemployed are clearly underrepresented (BBSR 2015: 92).

The age structure of the private landlords differs significantly from the total population—on average they are older (their average age being 59) and the under 30s are hardly represented at all.

In terms of distribution channels, the most important channel is advertisements. The second most important way to find tenants is recommendations, and thirdly brokers are mentioned with a frequency of 10 per cent (building ownership) and 20 per cent (condo ownership). (BBSR 2015: 126–127).

With regard to fixing the rental price for new tenancies, 70 per cent of the private owners of multi-family houses rely on their own experience. External sources such as *Mietspiegel*, advertisements and brokers do not play an important role (BBSR 2015: 134). The proportion of stepped rents and index-linked rents for new leases by private individuals is 10 per cent (so in 90% of new leases the local reference rent LRR is agreed upon to determine future rent increases). There is a slight positive correlation with the demand situation on the local housing market (BBSR 2015: 137).

### **1.3.2 Large landlords**

As already stated private persons dominate the German PRS. The rest of the privately rented dwellings (17%) is owned by private professional owners including corporations. All private

landlords combined account for 78 per cent of the rental housing stock, and the remainder is owned by public housing companies (11.3%) (municipal housing organisations for the most part) and housing co-operatives (9%). A small section is the property of churches and non-profit organisations.

Though still a minority, large corporate landlords are increasing in the PRS, with nine major publicly listed housing corporations owning 890,000 dwellings (3.8%) of the German rental stock (at end of 2015), and the largest of them—Vovonia—owning and administering about 400,000 dwellings (BBSR 2017: 8–10). This makes Vovonia one of the largest landlords in the world.

The origins of today's listed housing corporations vary: in addition to the formerly private equity controlled housing companies, there are also former industrial and transportation companies which have been operating for a long time and have refocused their business model on residential real estate. Other companies were newly established with the focus on residential real estate investments. A large part of the housing portfolios of publicly listed landlords stems from the purchase of formerly public or factory-owned housing companies.

Since the turn of the century, there has been a significant consolidation in corporate ownership, beginning through sales of municipal housing and employee-housing portfolios, then through acquisitions and mergers of private housing companies. The primary (pre-float) investors in these corporations have now almost entirely exited from their investments. Their known major shareholders are international investment funds, government funds and insurance companies with long term cash flow-based strategies (BBSR 2017: 75–84).

Typical strategies of Germany's large publicly listed landlords differ significantly from the municipal housing companies and the smaller private housing companies (BBSR 2017: 85–126). There has been relatively little investment by the large corporate landlords in new construction, but they have engaged in active portfolio management (acquisitions and sales)—in contrast to the conventional 'build and hold' strategy of the municipal companies. Some large corporates have invested in modernisation works, in order to increase rents while others have sought to minimise their maintenance costs.

Individual stock-listed large scale landlords have introduced tenant participation instruments—for example, there are local tenant councils at Vonovia. The largest listed companies are very concerned about their public reputation—Vonovia draws attention on all channels and on every occasion to exemplary projects with a particular benefit for the tenants or the local community. On the other hand, their management methods are very controversial. Tenants' associations denounce problems with this class of landlords, and relations of the tenants to their listed housing organisations can be described as strained and conflictual, research by the tenant associations has revealed. There are many disputes about operating cost statements in particular, but also rent increases have been controversial. The willingness to deal with conflicts varies significantly between the individual listed housing providers.

Tenants' representatives have identified inadequate operating costs settlements, insufficient stock maintenance, rent increases, socially incompatible modernisations and poor accessibility of the landlords as the main conflicts of interest in the tenant-landlord relationship (BBSR 2017: 137–139). This is also evidenced by a survey of the German tenants' association (DMB NRW 2016).

Operating costs are a constant issue between tenants and the listed landlords. Companies are 'creative in inventing new operating costs' (Mieterverein Dortmund about Vonovia). From Bonn and Hamburg, formal errors are reported in the operating costs final accounts, which point to organisational problems.

Also, in the case of defects, tenants often seek advice from tenants' associations. Neglected and poorly maintained housing stock is common, for example at Grand City Properties in the

Echeloh settlement in Dortmund. The neglect affects mostly individual properties and dwellings rather than whole buildings or neighbourhoods.

Energy efficiency modernisations create many conflicts. Tenants are displeased with the type of insulation (Berlin), sometimes with balcony extensions (Dortmund) and, of course, with the modernisation-induced rent increases, which usually exceed the saved heating costs. Another conflict zone is the demarcation between modernisation and (non-redeemable) repair costs. In the case of modernisation-related increases of rents, the number of Vonovia tenants complaining is above average in the DMB survey, but this is a result of the company's particularly active modernisation strategy.

Rent increases in current tenancies lead to conflicts, especially if the landlords resort to underhanded methods, for example, challenging of *Mietspiegel* due to methodological questions, avoidance of *Mietspiegel* via flat rates or citing the rents of 'comparable apartments'. Conflict about rent increases in ongoing leases is particularly high at LEG and Vonovia.

Tenant organisations repeatedly state that the tenants' contact with the listed housing companies is difficult in case of queries, deficiencies and necessary repairs.

There are differences in the willingness of companies to settle disputes, for example the different behaviour of Deutsche Wohnen and Vonovia in Berlin—compared with Vonovia, Deutsche Wohnen is perceived as a particularly hostile landlord.

## 1.4 Regulation

For many years Germany has had strong regulations regarding both security of tenancies and rents. Changes have been made recently to rent regulations to tighten controls. The ability to apportion the costs of modernisation work to the rent has not changed until recently. In Germany's system of government, the Federal Parliament has power with respect to tenancy law.

### 1.4.1 Security

The German Civil Code (*Bürgerliches Gesetzbuch*) provides strong assurance of security, specifically through regulating the grounds and periods of notice for termination by landlords, rather than through fixed terms.

Since fixed-term leases are only admissible in exceptional cases, rental agreements for an indefinite period of time are usual in Germany, and the effective duration of these contracts and the average length of a tenancy is more than ten years.

Under a rental agreement for an indefinite period of time landlords may give a termination notice only where there is a 'legitimate interest', specifically:

- wilful or negligent substantial breach of contract by the tenant
- 'hindrance to economic exploitation' (in practice, demolition of the premises)
- personal need of the landlord (i.e. to use the property as a residence for themselves or a family member)
- conversion of adjoining rooms to living space.

The demolition decision of the landlord must be 'reasonable and comprehensible', and is subject to judicial review when giving notice to the tenant. A poor state of the building and equipment deficits or other deficits against modern housing standards are indicative of the necessity of a new building. The question is whether a modern building standard can be achieved by means of cost-effective renovation.

In practice the 'personal need' interest is the most commonly used. The German Civil Code, however, precludes its use within three years (or up to ten years depending on regulation by ordinances of the state governments) by a landlord purchasing an apartment, if the property had been split into condominiums after the handover of the apartment to the tenant. The Civil Code also provides that the need must be proven by the landlord.

The termination notice must be given by the third working day of a calendar month for the end of the second month following. For example, if notice was given 5 July 2017 (the third working day of the month), the expiry date is 30 September. If given on 6 July, the expiry date is 31 October 2017. Hence the notice period is almost three months and if you miss the date it could be almost four months. For the landlord (not for the tenant), this period of notice is extended by three months after five and eight years.

The Civil Code also allows landlords to terminate without notice in certain limited circumstances (Para 543), such as unlawful subletting and late payments.

In case of a dismissal with due notice, a tenant may object to termination proceedings where they would cause the tenant 'undue hardship', and a court may determine whether a tenancy may continue 'taking into account all the circumstances' (Para 574a). Evictions must not be effected without a court order.

Tenants may terminate without grounds, with due notice (notice period: see above). Germany's strong legal assurance of security has remained largely unchanged for decades and there are no proposals or movements to alter it: it appears well accepted by landlords because it makes renting an attractive proposition and sustains demand for rental housing. 'These rules seem to be so deeply ingrained that it would be tantamount to political suicide to touch them' (Kofner 2014b: 42).

#### **1.4.2 Rents**

The German Civil Code also regulates rents. At the earliest, one year after the last rent increase, the next rent increase can be announced and a consideration period must be allowed of two months—thus, rents can only increase every 15 months. Also, the effective frequency of rent increases is considerably lower among private persons as lessors, and is dependent on the demand situation and the price level in the local housing market (BBSR 2015: 139).

Rent increases during a tenancy are limited to the 'local reference rent' (LRR, which is the average rent paid under newly agreed and existing contracts (if raised) for comparable dwellings (by type of dwelling, location, size, condition and equipment) in the last four years. Thus, the LRR is not a current market rent, but describes the long-term trend of local rents with an emphasis on historic rental costs. Because the law does not prescribe in detail the method or structure of the LRR in a '*Mietspiegel*' (an instrument for surveying and exhibiting the LRR structure in a community), most municipalities produce their own *Mietspiegel* which sets out the presumed LRRs for the local market (Kofner 2014a: 15).

There are additional rental restrictions as well as the LRR system—rent caps. In 2013, the existing rent cap system was tightened. In Germany, the rent in an existing contract may be increased by a maximum of 20 per cent within three years. Since 2013, this maximum increase can be limited to 15 per cent in tight housing markets. These rent caps apply even if a comparison with the relevant LRR would permit a higher rent increase.

In 2015, a control on rents for new tenancies ('*Mietpreisbremse*', or rental price brake) was introduced, limiting new rents in tight markets (as specified by the state governments) to not more than 110 per cent of the LRR. Until then, there were no effective restrictions on new tenancies.

There are severe doubts about the effectiveness of the *Mietpreisbremse*: it appears tenants have not been disputing rents asked for new tenancies after having signed the contract. Rents for new leases continue to rise almost unchecked in tight housing markets—most landlords simply ignore the regulation because there is no penalty and the tenants do not claim their rights.

There are also many exceptions to the rental price brake: ongoing leases are not affected; rents do not have to be reduced in ongoing rental agreements; and the rent level that has already been set in the individual contract with the previous tenant is 'protected'. Additional exemptions apply for new rental dwellings and for the first lease agreement after a comprehensive modernisation of a dwelling.

Local tenant organisations, owners' associations and city administrations in the Hessian capital cities of Darmstadt, Frankfurt, Offenbach and Wiesbaden all report that the instrument was hardly ever used. After a year of rental price brake, there were no court procedures in Hesse where residents sought to impose a rent reduction because their landlord had violated the rules of the rental price brake (Frankfurter Allgemeine Zeitung, 1 December 2016).

Six court proceedings were received by the Berlin District Courts by October 2016. In Hamburg, Munich, Frankfurt am Main and Stuttgart there were no claims pending on the basis of the rental price brake, according to the local courts (Die Zeit, 6 October 2016).

The Civil Code provides for rent increases outside these restrictions where the landlord has carried out work to modernise the premises, particularly for the enhancement of energy efficiency. As an alternative to an LRR-related increase, a charge equivalent to 11 per cent of the cost of modernisation works may be added to the annual rent. Hardship considerations apply, including: The 'works carried out', the 'structural effects', 'previous investments of the tenant' and the 'expected increase of the rent' (except for production of contemporary general standard).

Energy efficiency modernisations are highly profitable for the landlords. From the point of view of tenants, the modernisation apportionment is often a multiple of the saved heating costs (BBSR 2017: 105–109). The modernisation-related increases in rent often cause considerable gentrification pressure.

The emerging class of large corporate landlords is bringing only limited pressure against Germany's strong regulation. Their profit-oriented business models, of course, generate the desire to be free from statutory rental restrictions, but the organised tenant representatives in Germany have greater support and better mobilisation possibilities due to the large number of tenants. The regulatory measures of recent years reflect this greater influence on the tenant's side—it may be easier to politically justify strong regulation against large corporates.

German tenancy laws have changed rapidly in recent years and the system has gradually become more restrictive. It is evident that essential price functions are already disrupted. A growing number of urban housing markets seem unable to return to an equilibrium state—very low vacancy rates have occurred in these markets for many years.

The number of tight housing markets in Germany continues to grow (e.g. Hamburg, Munich and Frankfurt, with vacancy rates of 0.6, 0.2 and 0.5% respectively, according to the CBRE-empirica vacancy index). It is not only metropolitan regions that are affected by falling vacancy rates, but also a growing number of medium-sized cities such as Darmstadt, Freiburg, Regensburg and Ingolstadt. Often, these are university cities or they are subject to special economic factors. The nation-wide average vacancy rate has declined for nine years in a row and was 3 per cent at the end of 2015.

The quoted rents (new contracts) in the largest cities in Germany grew significantly more in the district-free cities in the period 2011–16 as compared with the national average. In more than

half of all German cities and counties, the quoted rents are currently rising by more than 4 per cent per year and the rate of growth is already above six per cent in 22 per cent of the cities and counties.

The regulatory system also became more complex and non-transparent while trying to cope with these market tendencies in a spatially targeted way (Kofner 2014a: 4–5), for example the spatially inconsistent determination of the local reference rent. The latest interventions have focused on both ongoing contracts and newly agreed leases, but were limited to local housing markets regarded as 'tight'. It is not clear whether this regulatory tightening is a transitional or a permanent phenomenon. What is certainly missing is a long term vision of an adequate and stable regulatory framework of the housing market.

Apart from these deficiencies German tenancy laws still have a degree of market orientation. It is a second generation rent control system with a differentiated and moving anchor based on the empirical development of rents.

Short-term letting for tourists is a problem in some larger German cities which are attractive to tourists. Municipal authorities in these cities fear that due to short term letting, too many housing units are removed from the general housing market. There is no federal policy to restrict short-term letting for tourism, but local authorities can ban the misuse of property using municipal statutes. It seems that the most affected cities are making a regulatory stand against Airbnb. The most important Airbnb market is Berlin, and the Senate of Berlin has recently introduced a license requirement for Airbnb hosts in order to slow down short term tourism letting—licences are only granted in exceptional cases. Such harsh reactions are understandable against the backdrop of an already very tight housing market.

## 1.5 Summary

The most outstanding characteristics of the German housing system are:

- the development of a large rental housing stock by a combination of regulation and high housing subsidies in the past
- as a counterpart, a low home ownership rate
- overall, a high level of tenant protection, but with gaps, for example, generous modernisation-induced rent increases and the effective limitation of newly agreed rents (split market)
- the static legal framework of the rental housing market for almost 50 years, with the result that the system is rarely fundamentally challenged
- a market-oriented rent price regulation setting in the long term, which does not limit the returns of home owners too strictly
- the pronounced tenure neutrality in housing subsidisation in combination with a very low level of subsidies for 10 years (both home ownership and rented housing construction are hardly promoted)
- conservative financing practices, embedded in the structure of the banking system, ensure a high level of credit quality in home financing
- low house price volatility
- the large private rental sector
- the sale of some large public and factory-related housing companies to financial investors and subsequently the formation of a major sub-sector of large listed housing companies

- a previously significant, but now only modest, social housing sector
- the only temporary subsidisation of social housing, with subsidised housing losing its social status in the medium to long term.

The individual elements of the German housing system do not exist independently. The low home ownership rate is the counterpart to the large rental housing sector. It is embedded in a conservative financing environment, which results in high credit quality, and this is conducive to stable development of house prices.

The large rental sector characterised by small private landlords is the result of the historic high level of tenant protection: German legislature has designed rental housing as a tenure similar to property, and hence it was always attractive for tenants with a long-term planning horizon. Rent controls were compensated by comparatively large tax subsidies for a long time, but these subsidies ended in 2006. Finally, the regulatory screw was tightened slightly, and consequently an unbalanced situation has developed, with investment incentives seriously reduced.

The system is currently experiencing a stress test in an environment characterised by increasing market tension. If demographic pressure continues, policy is likely to react with a significant expansion of housing subsidies. This is already evident in the increased funds for social housing construction. The electoral programs of the two major popular parties have also announced a further expansion of the subsidies. Fortunately, the budget should permit such a redirection of housing policy.

The extraordinarily uneven distribution of wealth in Germany in comparison to the other countries of the Eurozone is partially due to housing policy. The median net household wealth in Germany is among the lowest in the entire Eurozone (especially if compared to the Eurozone without CEE countries, see European Central Bank, 2016) and this is primarily due to the low German home ownership rate. On the other hand, it seems hardly conceivable that the distribution of wealth could be significantly improved without significantly increasing the home ownership rate. If there is such a thing as an optimal home ownership rate, then it is time and space dependent. In Germany in 2017 it would be higher than 45 per cent. The rate could be increased considerably without necessarily causing markedly higher macroeconomic instability.

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## Appendix 2: Private rental housing in Ireland

By Aideen Hayden

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In Ireland, the rental sector has traditionally been regarded as a residual sector in which households, who would prefer either to own their own home privately or access permanent social housing, must serve time on their way to their true tenure of choice' Rebuilding Ireland (Government of Ireland, 2016)

During Ireland's economic boom, 1996 to 2006, a policy shift in low income housing provision—from social housing construction to reliance on the private rental sector—together with rapidly rising house prices fuelled by population growth and expanding low-cost credit, drove the growth of the PRS. This was a major factor in triggering the first significant attempt in 2004 to regulate the PRS, for the first time since the early twentieth century.

Following the economic crash, house prices initially fell by as much as 50 per cent. However, falling incomes, together with a lack of willingness to lend by financial institutions which had been badly damaged—in one case fatally—by excessive property lending, and a collapse of the construction industry, meant that home ownership has remained inaccessible to a large part of the population, and the private rental sector has continued to grow.

With a rapid rise in rents driven by lack of house building and ongoing population rise, state support for low income housing did not keep pace with the market, resulting in a homelessness crisis. This in turn has resulted in further moves to regulate the PRS, notably placing restrictions on rent increases and introducing greater security of tenure.

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### 2.1 Housing system context

Ireland's experience of an extraordinary housing market boom and crash—with a deep financial sector crisis and generalised economic recession followed by recovery—looms large in recent policy and market activity, including in relation to the PRS. While the housing market boom and subsequent recession had a major impact on the PRS in terms of policy development, the subsequent recovery of the Irish economy has also had an influence in bringing about significant changes in the recent past. Unemployment within the Irish economy, for example, has dropped to just over 6 per cent from a high of 15.1 per cent at the height of the recession in early 2012 (CSO 2017a). GDP growth is well above EU average and the house price collapse which followed the recession has seen a reversal in trend, with a report from the Central Statistics Office in April 2017 suggesting that prices are now closer to 30 per cent (as opposed to 50% following the crash) below the level seen at the height of the boom in 2007 (CSO various years).

The size of the Irish PRS is now close to the European median—around 19 per cent of households rent privately (Housing Agency 2017), having grown through both the boom and the bust, and significant other changes have occurred. The recently published *Strategy for the Rental Sector* (DHPLCG 2016) states that 'a strong and viable private rental sector should be a

key component of a healthy housing market, providing a housing option to those who either cannot or choose not to enter the owner occupied market' (DHPCLG 2016: 4). Indeed, the discourse around recent changes to rent regulation and security of tenure suggest that a more vibrant and balanced PRS would have protected Ireland from some of the worst effects of its property-fuelled housing crash (Government of Ireland 2016: 69)

### **2.1.1 History: before the boom**

The development of Ireland's housing system over the latter part of the twentieth century are broadly similar to those of Australia's. Majority owner occupation increased after World War II, rising to a peak of 80 per cent in 1991, on the back of state-subsidised lending and grants for owner-occupiers, and a social housing sector developed by local authorities, that built and sold a large volume of housing to tenants (Norris and Byrne 2016; Norris 2014). Through to the 1990s, the Irish PRS was a declining sector, representing only 7 per cent of housing stock by 1990. For many years a significant, although declining, minority of PRS properties (34% in 1971) remained subject to rent and eviction controls (which effectively froze rent levels) enacted during the First World War, although these were struck down as unconstitutional by the Irish High Court in 1981 (Kenna 2011).

For most of this period Ireland's economy remained relatively underdeveloped, with rates of economic growth persistently below the European average, and while its population grew, it was offset by high rates of emigration (Kennedy, Giblin et al. 1988). The seeds of the revival of the PRS lie partly in the dramatic turnaround of the Irish economy in the mid-1990s but also in the decline in the model of social housing provision, on which housing provision for low income groups was based. The decline in government commitment to new social housing, particularly from the early 1990s, had a significant role in the future development of the PRS. Tenant Purchase, a policy of selling social housing stock at significantly discounted rates to tenants, prompted in large part by the evolution of an unsustainable social housing model, added to a significant decline in social housing stock.

Between the mid-1960s and the late 1980s, a combination of rents significantly discounted from market rents, and rights of members of the tenants' extended family to succeed to the tenancy through custom and practice (without any assessment of need), undermined the sustainability of the social housing sector. As a result, the sale of housing became an imperative for local authorities (Hayden 2014). This unsustainable social housing model was also a major influence encouraging government to shift emphasis away from social housing provision towards the PRS. Moreover a move towards direct funding of social housing in the late 1980s, through capital grants from central government rather than long-term borrowing from local authorities (Norris 2016), meant that when government finances came under pressure after a period of economic recession, social housing construction declined accordingly—exacerbating the reduction in overall stock via tenant purchase.

Tenant purchase policy in Ireland ensured the sale of two-thirds of all social housing units built in the state by local authorities, vastly exceeding the proportion of stock sold under the UK Right to Buy scheme. The extent of sales to tenants also ensured that the social rental sector was increasingly residualised, given that it was the lowest-income tenants who generally were unable to afford to buy the houses that they rented. The most significant impact of this overall dynamic was to undermine the longer-term future of the social housing system, and Ireland never returned to the large-scale house building programmes that it had embarked on in the period from the 1930s through to the 1970s (Hayden 2014). Social housing construction contracted sharply in the late 1980s and early 1990s. This had a significant impact when the Irish economy experienced a period of extensive growth from the mid-1990s on. Though social housing construction recovered in the late 1990s it has been only as the economy has recovered after the recent crash that political support for social housing construction, in the face of a growing housing supply crisis, has strengthened. Evidence can be found in the most recent

Census of 2016, which indicated that social housing has shown the largest increase of all sectors, up 11 per cent from 129,033 in 2011 to 143,178 in 2016 (CSO 2012, 2017b). This represents the first increase in the sector's proportion of total housing stock since the early 1960s.

### **2.1.2 Boom and Crash**

In the mid-1990s, Ireland entered its 'Celtic tiger phase', a period of high-skill manufacturing and services-led economic growth, population growth and financial deregulation, coupled with low interest rates set by the European Central Bank, which set the scene for a large expansion of credit for housing. Between 1993 and 2001 the annual real growth of the Irish economy increased from 3.8 per cent to 8 per cent (ESRI 2001). Over the period 1990–2006, housing output relative to population tripled, average real house prices doubled, and the ratio of housing debt to GDP tripled (Waldron and Redmond 2014: 152). Between 1994 and 2004 the national average price of a new home increased by 243 per cent (Drudy and Punch 2005). The number of lenders operating in Ireland grew from 12 to 17 over the decade 2000–2010—in part due to the unusually high penetration of foreign lenders into the Irish market which accounted for approximately 30 per cent of all mortgage lending in 2007 (Norris and Coates 2014: 304). Furthermore the number of interest-only mortgage products expanded significantly, one quarter of new loans in 2006 were 100 per cent loan to value (Kenna 2015). During the 2000s, the growth in lending went disproportionately to landlords, and the rate of owner occupation declined (Norris and Coates 2014: 306).

The growth of the economy drove a strong demand for housing, enhanced by demographic factors such as net inward migration and a significant reduction in the cost of finance (NESC 2004). While the increase in the level of construction was unprecedented when compared to other European countries (Norris and Shields 2004) social housing construction did not keep pace: in 1989, an historic low of 768 units were constructed, with a slight recovery thereafter (Norris, 2014). Social housing as a proportion of the overall housing stock declined significantly. Affordability issues emerged sharply as both rents and house prices grew at rates not experienced previously (Downey 1998), and households who had previously accessed home ownership crowded out those on lower incomes.

From the time of the economic collapse in 2008, house prices fell by 51 per cent from their peak values in 2006, significantly more than the fall in rental values which occurred over the same period. Levels of overall housing construction fell dramatically, particularly in Ireland's major urban areas. From an historic high of 88,211 units constructed in 2006, a mere 12,666 units were completed in 2015 (Houses of the Oireachtas 2016). While estimates vary, somewhere between 20,000 and 25,000 units will be required annually for the foreseeable future to meet Irish housing demand (Housing Agency 2017). Population increase, coupled with the fall in construction, have led to severe housing shortages and an affordability crisis within the Irish housing system, most evident in the PRS. In the last quarter of 2016, rents increased nationally by 13.5 per cent—the largest increase in the history of the rent report, with the average monthly national rent at a record €1,111 (note: this figure does not include the cost of utilities). This is the third consecutive quarter in which this figure has increased. In Dublin, the annual rate of rent inflation in 2016 was 14.5 per cent, with rents in this area now averaging €1,643 per month. The extent of the affordability crisis in the PRS is most visible in the numbers of families entering homelessness services. In December 2016 homelessness figures show that nationally there were over 7,000 people in emergency homeless accommodation, nearly 40 per cent of them being children (with the majority—over 5,000—in Dublin) (DHPCLG 2017). The total number of homes that paid €300 or more per week in rent to private landlords increased by 166 per cent from 18,485 in 2011 to 48,993 in 2016 (CSO 2017b).

While the fall in house prices might in other circumstances have been expected to lead to a rise in home ownership levels, significant negative equity experienced by those who purchased

during the boom and an unwillingness or inability to realise losses appears to have trapped some owners in the sector as landlords (DKM 2014). Between 2006 and 2011 the number of households renting in the PRS rose by 64 per cent, while the home ownership rate declined from 75 to 70 per cent (CSO 2012).

The 2016 Census shows a figure of 497,111 households renting, an increase of 4.7 per cent on 2011. This meant that renting was the tenure status for almost 30 per cent of all of occupied dwellings in the last census. The significant rise in the share of the PRS can be attributed to the features of boom and bust. Inward migration before the recession increased demand for rental accommodation; rising costs of home ownership; low cost Buy to Let mortgages often priced out home owners; and a limited supply of social housing led to demand for housing from low income households. Ultimately an economic collapse and credit freeze favoured private renting economically by removing the option of purchase from a large proportion of those seeking housing and pushing up rent levels in the PRS (DKM 2014; NES 2015; Houses of the Oireachtas 2016).

In addition, Ireland has experienced a period of significant population growth, from 3.5 million in 1991 to 4.8 million in 2016, an increase of 37 per cent in 25 years (CSO 2017b) adding to the pressure of demand, which would have been more severe had there not been significant net emigration during the recession (CSO various years). However, the PRS has ultimately also been affected by the constraints on building of new housing, and its growth has been slower since 2011. In the 2016 Census, the total number of *households* in the private rental sector increased by only 1.42 per cent although the total number of *people* in the sector increased by 7.95 per cent, indicating rising problems of overcrowding and continuing build-up of demand (CSO 2017b).

Research by Byrne, Duffy et al. (2014) indicates that the post-crash growth in the PRS has come from an increase in the rate of household formation, a response to the initial decline in rents after the crash, a relative collapse in mortgage lending and the collapse in expectations of future capital gains accruing to owner-occupiers in the immediate post-crash phase (which results in the net costs of owning rising relative to renting). However, recent statistics on lending would suggest a steady and growing appetite for purchase. Mortgage approval figures released in early 2017 by the Banking and Payments Federation indicate that mortgage approval figures were up—albeit from a historically low level—by 41 per cent year on year in the three months to the end of January 2017. First time buyers accounted for 48.2 per cent of all approvals, even before the Help to Buy scheme was introduced by the Irish Government in January 2017 to assist first time buyers.

The figures also show growth in the numbers of investors taking out a mortgage to finance a property purchase. While there has been a significant rise in those aged 30 to 34 renting over earlier periods, initial falls in the level of rents in the post 2008 period have been reversed. Moreover, attitudes among tenants towards the PRS as a long term home are negative, with a majority of renters wanting to own their own homes (DKM 2014).

Census 2011 demonstrates that the number of households who rented either from a private landlord or voluntary body rose by 64 per cent between 2006 and 2011 (during a time when total households rose by 15.8%), while the overall ownership rate declined from 75 to 70 per cent (CSO 2012). Figures from Census 2016 show that this trend has continued and that the overall rate of home ownership has now dropped to 67.6 per cent (CSO 2017b).

Whether the significant rise in those renting over the last decade, and a fall in the overall rate of home ownership suggests a shift in preferences towards other tenures, or is the result of latent demand and a highly conservative lending environment, remains unclear at present. What is clear is that the home repossession rate has increased since 2013, particularly as one-third of mortgages in arrears have been behind on payments for more than one year. If Ireland's rate of

home repossessions (0.2%) increases to levels like those of the UK (3%) or US (5%), then significant numbers of mortgages could enter the repossessions process. Ireland has had a historically low rate of repossession, and—partly for deep-rooted historical reasons—repossession of a family home is culturally unacceptable (Department of Finance 2011). Moreover the government seems determined to ensure such a large scale of repossession does not occur and in 2016 launched a programme (Abhaile) to deliver targeted assistance to those in long term mortgage arrears. Ireland exited its bailout programme in 2013, although the continuing social, economic and political challenges posed by the collapse of the property bubble remain a threat to the recovery of the property market.

Attitudes to the repossession of Buy to Let properties are significantly different however, with the former Governor of the Central Bank advocating that a proactive approach be taken by lenders to such accounts (Pope 2014). The increasing housing crisis for low-income families, evident to policy makers since 2014, has prompted a renewed Government commitment to social housing construction. *Rebuilding Ireland—Action Plan for Housing and Homelessness*, published in June 2016 (Government of Ireland 2016) is the leading policy document in the area of housing in Ireland. It follows on previous policies to address the mounting housing crisis *The Social Housing Strategy: 2020 and Construction 2020*. *Rebuilding Ireland* sets the objective of investment of €5.5 billion in social housing and housing infrastructure, and sets targets to double the annual level of residential construction to 25,000 homes and deliver 47,000 units of social housing in the period to 2021.

Importantly, *Rebuilding Ireland* continues the pattern of delivering social housing supports through the PRS. This means that schemes which subsidise housing provision through the PRS such as the Housing Assistance Payment scheme, where the local authority enters into a direct relationship with landlord, are also officially counted as social housing support, with the tenants deemed to have their social housing needs met. The Government then published a national Strategy for the Private Rental Sector in December 2016.

This national strategy has introduced significant changes in the regulation of the sector which show greater commitment to its long-term development. Significantly, the strategy introduced measures to control rental inflation, described by Minister Coveney as ‘*a time bound intervention ... that will not negatively impact existing or new supply*’ (Government of Ireland 2016: 2). However, the introduction of greater regulation of rents for all tenancies in designated zones that account for most of the stock in the sector, cements previous moves, and may be difficult to change when normal levels of supply are achieved. The strategy, while proposing actions to protect existing rental stock, also recognises the emergence of affordability issues for ‘middle income’ households locked out of both the purchase market and social housing, and contains measures to encourage additional supply from outside the traditional landlord class, signalling a recognition of a changing culture around long term renting in Ireland.

The final part of the housing system context is lodging accommodation. Those renting in this fashion are also deemed licensees. There are at least 4,000 reported lodgers renting a room in another person’s owned principle private dwelling under the ‘Rent-a-Room’ scheme (see below). However, no accurate assessment is available, as the reporting of revenue under the scheme is not mandatory if the exemption limit is not exceeded (House of the Oireachtas 2016: 31).

There are only around 3,000 purpose built student accommodation units provided in a mixture of on campus and off campus student housing schemes, the latter being provided by companies using specific tax incentives to do so. Ireland’s third-level student population is projected to grow by around 20,000 students (or 1.5%) to 193,000 students by 2024. The *2015 Report on Student Accommodation: Demand and Supply* by the Higher Education Authority (HEA) estimates an existing level of unmet demand of about 25,000 student beds nationally. The Irish

Government has committed to the development of a national student accommodation strategy in 2017 to address this gap (Government of Ireland 2016: 74).

### 2.1.3 Tenants

The composition of the PRS has changed over the last decade. While the sector has for some time had a high proportion of single people and lone parents, and this has continued, the more recent development has been the rising profile of families in this sector. Just over 35 per cent of young people (18–34) are renting from a private landlord, and 61 per cent of single people also rent. There has, however, been a significant rise in the number of families renting; in 2006, 22 per cent of families with pre-school children rented, and 18 per cent of families with primary school children; compared to 35 per cent and 29 per cent respectively, in 2011 (CSO 2012). Recent research indicates that the private rental sector has expanded strongly since the 2011 Census, driven in part by the impacts of the economic recovery (DKM 2014; NES 2015).

The PRS has historically been seen as a stepping stone to other tenures such as home ownership and social housing (O'Brien and Dillon 1982). This remains true, with a recent survey finding that only 17 per cent of private renters saw themselves as renting long-term (DKM 2014: iv). Home ownership remains a strong aspiration among renters, with 68 per cent saying that they had to rent because they couldn't afford to buy. A similar percentage, 70 per cent, in the Dublin region and 80 per cent nationally, plan to buy a home when they leave the PRS (DKM 2014: 27). However, strict lending criteria introduced by the Irish Central Bank (though these have been loosened somewhat) continue to make it difficult for first time buyers to access the home ownership market and many renters feel trapped in the PRS. Just under 50 per cent however agreed that they would be more likely to rent long term if there was a possibility of rent stability over a three to four year period. The plight of renters experiencing rapidly rising rents gave rise to public calls for rent certainty, which significantly influenced government actions in introducing rent regulation limiting rent increases in December 2016. Extensive media coverage of tenants from the PRS becoming homeless due to affordability issues also has led to a public image of the sector as expensive and insecure.

Affordability and security of tenure issues within the PRS have been the main drivers of the significant rise in family homelessness. Threshold, a housing service working principally in the PRS, reports that the principal source of queries in 2015 in the PRS related to tenancy terminations, rent reviews, standards of accommodation and the appointment of a receiver to a Buy to Let property (Threshold 2016). Threshold reports, for example, that current landlord and tenant legislation does not protect tenants where a receiver is appointed to a property by a lending institution. Given the number of Buy to Let properties in significant arrears, they predict that this will become an even more serious issue. The high profile media attention given to the Tyrrelstown case has emphasised the difficulty faced by tenants, but the 2016 amendment to protect sitting tenants does not apply to developments of less than ten properties. Given the profile of the Irish rented market, there is little protection for most tenants in a repossession situation.

A significant proportion of PRS households receive state assistance with their housing costs in the PRS, however these supports, described above, have not proved adequate in enabling these households to either access or retain PRS housing. Substantially increasing the Rent Supplement limits in July 2016 have significantly helped to address this issue. Following the formation of a new Government in May 2016 an agreement was reached between the majority Government Party (Fine Gael) and the chief opposition Party (Fianna Fail) to enable the stable functioning of government (Fianna Fail 2016). As part of the terms of that agreement both Rent Supplement and the Housing Assistance Payment were to be increased by up to 15 per cent. However there are no long term plans to ensure that state assistance to those who require it in the PRS keep pace with rental inflation. Rental pressures have led to overcrowding, though there is no evidence of the extent of the problem.

Reliance on private rental accommodation has been particularly marked for immigrants. Census 2011 shows that 157,000 households headed by a foreign national were renting in 2011, making up 42 per cent of all households renting privately. People of an ethnic minority background make up only 18 per cent of the total population (CSO 2017b; NESC 2015: 190).

## 2.2 Financial settings

### 2.2.1 Credit

From the 1990s, Ireland's finance sector was deregulated, international institutions entered the market, and housing credit expanded substantially. From the late 1990s a significant fall in mortgage interest rates arising from Ireland's membership of the European Monetary Union (EMU) stimulated a sharp rise in mortgage lending. By 2006 the average first time home buyer's mortgage had risen to eight times annual earnings and the average new house price nationally was ten times the average earnings (Kelly 2009). By 2008 100 per cent loan to value mortgages accounted for 12 per cent of all mortgages granted (Norris and Winston 2011). Intense competition in the mortgage market played a key role in liberalising lending standards (European Central Bank 2009). One marked feature of the growth in mortgage lending was the rise in lending specifically for Buy to Let properties. By the end of 2013, these accounted for 22 per cent of all outstanding residential mortgage loans (Kenna 2015).

Reliance on retail deposits, traditionally the key source of funding for mortgage lending, was replaced in large part by borrowing from the wholesale money markets and from debt securities (Conefrey and Fitzgerald 2010). Real estate related lending increased significantly and reached a peak of 72 per cent in 2006 of total lending by Irish mortgage lenders (Norris and Coates, 2014). While concern was expressed at the vulnerability of the Irish banking sector to the real estate market (Kearns and Woods 2006) rising house prices over the period led many to expect a 'soft landing'.

However, from 2007 house prices began to fall and new house construction declined dramatically. The collapse of the property bubble had serious repercussions for the banking sector. Together with a deteriorating macro economy, rising unemployment and a collapse in domestic demand, Irish banks found it increasingly difficult to access the wholesale money markets. In 2008 the Irish Government bailed out the Irish-owned banks by guaranteeing all deposits and senior debt (Waldron and Redmond 2014).

For the financial sector, the crash resulted in a massive impairment of the loan books of Irish banks. One bank, the most aggressive property lender in the market, collapsed completely. Four of the five remaining major local banks were wholly or partly nationalised due to their resulting insolvency, and a new institution, the National Asset Management Agency (NAMA), was established to acquire and deal with impaired debt (Byrne 2015). The Housing Agency was also established, with a brief that includes dealing with unfinished housing construction developments.

Mortgage arrears rose from just over 3 per cent of all total residential mortgage accounts in 2009 to 12.3 per cent in 2013 (Central Bank of Ireland various). However this trend has since reversed and for the first quarter of 2017 the Mortgage Arrears and Repossessions report showed a drop to 10 per cent. Buy to Let mortgage accounts in arrears though, while falling, still represented 18 per cent of the total outstanding balance on all Buy to Let mortgage accounts (Central Bank of Ireland 2017).

Ireland has also significantly amended its insolvency laws and introduced new types of Insolvency arrangements. The *Personal Insolvency Act 2012* set up the Insolvency Service and established an out-of-court debt settlement regime and reduced the duration of bankruptcy from

12 to three years. This was further reduced to one year commencing in 2016 (*Bankruptcy (Amendment) Act 2015*).

From 2007 onwards the economy experienced a significant reduction of credit, and access to mortgage finance has been limited. However, as the economy recovered in the period after 2013 the central Bank imposed restrictions commencing in February 2015 on lending to first time buyers, requiring minimum loan to value and income to loan ratios in order to 'reduce the risk of bank credit and house price spirals from developing in the future' (Central Bank of Ireland 2017: 1). It was only in 2017 that these restrictions were partially relaxed following public consultation.

### 2.2.2 Tax

While debate in the media has focussed primarily on the difficulties faced by tenants, there has been some recognition of the high costs faced by landlords, with additional costs being imposed during the recession (2009–13). Budget 2017 introduced some minimal relief for landlords, with a gradual reintroduction of 100 per cent mortgage interest tax relief (MITR). However a number of measures were introduced during the recession which have reduced the return on rental property. Together with the reduction in MITR from 100 per cent of interest charged to 75 per cent, universal social charge (a universally applicable flat rate tax) was imposed on rental income, together with property tax and water charges, which are currently under negotiation. Unlike the case with other commercial income, there is no tax allowance applied to rental income to offset expenses such as maintenance costs. The *Strategy for the Rental Sector* has set up a working group to look at the taxation of landlords and put in place a tax structure to support landlords entering and remaining in the sector. Landlord representatives have sought the immediate reintroduction of 100 per cent MITR and measures to place private landlords on an equal footing with commercial landlords in recognition of business expenses.

The renting of rooms in private dwellings is supported by the tax code. The 2017 Budget, in an effort to encourage more households to rent out rooms in their homes to relieve pressure on the traditional rental market, increased the ceiling for exemption from income tax under the Rent-a-Room scheme from €12,000 to €14,000 (Government of Ireland 2017).

### 2.2.3 Subsidies

Since the early 2000s, there has been a significant and sustained rise in the numbers of tenancies in the PRS supported by state aid, as well as an incremental development of hybrid forms of social housing. Currently the main subsidies are:

- **Rent Supplement** (65,000 tenants at 2016)—The purpose of Rent Supplement (RS), paid by the Department of Social Protection (previously the Department of Social Welfare), is to provide short term income support to assist with reasonable accommodation costs of eligible people living in private rental accommodation, who are unable to pay their accommodation costs from their own resources, and who do not have alternative accommodation available to them. The payment is only available to those in receipt of social welfare and not those in full-time employment even if on low incomes; the level of support provided is capped depending on the size of the property and the geographical location; and every tenant must pay a contribution to the rental costs, with the maximum contribution set in 2017 at €55 per individual and €60 per couple. Generally, payments are made to tenants and these payments are then passed on to their landlords.
- **Rental Accommodation Scheme (RAS)** (23,000 tenants at 2016)—Under the Rental Accommodation Scheme (RAS), in operation since 2004, local authorities have contracted private landlords to provide housing for people with a long-term housing need. The landlord continues to manage the property. The local authority pays the rent directly to the landlord, and unlike under the Rent Supplement (RS) scheme, RAS provides a longer term contract

and more security of tenure. Tenants may have to continue to contribute to the rent, but this contribution is paid to the local authority, not to the landlord.

- **Housing Assistance Payment (HAP)** (8,000–10,000 tenants at 2016)—The Housing Assistance Payment (HAP) scheme is a new form of social housing support, paid by the local authority directly to the landlord, currently being introduced by local authorities across Ireland. Unlike RS, HAP is available to those on low incomes whose income qualifies them for social housing supports and more approximates a housing benefit. HAP will eventually replace Rent Supplement for households who have a long-term housing need. It will also replace the RAS as the principal support for those who qualify for social housing support.

The regime of subsidies to the PRS has changed since the introduction of Rent Supplement in 1979. Rent Supplement, intended as a short-term housing support, became the main means by which social housing support was delivered. The rapid growth in the number of recipients brought about calls for reform and a recognition of the long-term housing needs of those in receipt of RS for 18 months or longer. This led to the introduction of the Rental Accommodation Scheme (RAS) in 2004, which transferred responsibility for long-term rent supplement recipients from the welfare ministry to the housing ministry. The principal idea behind the transfer was to achieve savings on an ever-growing RS bill. Lower rental payments were offered to landlords, in return for longer term agreements. Landlords would benefit by having a guaranteed income from the relevant local authority without the risk of voids (i.e. periods with loss of rental income due to vacancy), or of tenant failure to pass on the rent to them.

Additional benefits accrued to the local authority through this new hybrid form of housing, delivered through the PRS. RAS tenants would remain in the PRS and be subject to PRS regulatory control, rather than tenants of the local authority, reducing the management burden. It was also thought that RAS would facilitate greater social integration than traditional social housing, by reducing the number of housing developments visibly defined by tenure or class status.

Tenants also received benefits more traditionally associated with the social housing from the scheme. Higher security of tenure was achieved by means of long-term leases agreed between local authorities and private landlords. Tenants also paid differential rent subsidised by the state (i.e. rent based on income)—a positive feature of social housing not available to RS tenants. Unlike RS, which is only available to social welfare recipients, with RAS the tenant could take up employment without losing all financial support from the state (Hayden 2014).

Currently landlords can access some state subsidies for the renovation of property. However, a number of measures were introduced during the recession which have reduced the return on rental property.

*Rebuilding Ireland* acknowledges both the importance of the traditional landlord and the need for diversity in PRS provision, and puts forward new models and subsidies. A 'cost rental' model for middle income households, long favoured by the National Economic and Social Council (NESC), is supported, and an expert group will be convened to further develop the model (Government of Ireland 2016).

Local Authorities are encouraged to use state land to develop mixed tenure projects containing affordable private rental housing, which is subject to a permanent reduction from market rents and no ongoing cash subsidies. Local authorities have also been requested to give priority to 'Build to Rent' projects. These projects, expected to be funded by pension funds or REITs, have the potential to deliver significant growth in supply, particularly in urban areas, and the planning system is to be adjusted accordingly.

While these projects are ambitious and aim for a more sustainable rental sector, it is early days, as few of these projects have been realised, though there is an example of mixed tenure being delivered by one of the largest Approved Housing Bodies (i.e. officially designated social

landlords other than local authorities). In contrast, institutional investors tend to favour provision for the upper end of the market and their business models favour buying while the market is low and selling later for capital gains.

## 2.3 Landlords and agents

The Irish PRS has long been dominated by small holding individual landlords. The Strategy for the Rental Sector (DHPCLG 2016) notes that there were 324,222 tenancies registered with the Residential Tenancies Board (Quarter 3 2016), an increase of over 60,000 tenancies from 2011. Furthermore according to the RTB's figures there were just over 174,000 landlords and 705,000 tenants in Ireland, a significant increase in landlords on the 2014 figure of just over 160,000. This indicates that the proportion of house owners who are landlords has risen above 11 per cent, with the average landlord owning 1.86 properties. The volatility in the number of registered landlords demonstrates the difficulty of making categorical assumptions about the factors motivating their entry and exit from the sector. Research indicates that a large proportion of landlords had plans to exit the sector although this has not as yet occurred (DKM 2014). Nonetheless Threshold (2016) reported that landlords' stated intention to sell is a major reason given for tenancy termination.

The private rental sector is very fragmented—65 per cent of landlords own just one property, 82 per cent own two or less and almost 91 per cent own three or less. The DKM survey of landlords, referenced above, found that 36 per cent were 'accidental' landlords, and almost 20 per cent had become landlords as their first house was in negative equity and they could not sell it. Mortgage arrears remains a persistent, though slightly declining, problem. At the end of September, Central Bank statistics revealed there were 132,571 residential mortgage accounts for Buy to Let properties, with 21,435 (16%) in arrears for over 90 days. The Central Bank further noted that receivers had been appointed to over 6,000 Buy to Let properties, and 288 properties had been repossessed, either through voluntary surrender or by way of court order, in the third quarter (Central Bank of Ireland 2017a).

The profile of PRS landlords is changing, with the entry of some large scale corporate landlords. During the crash, many developers were caught with properties they could not sell, and became accidental landlords. The extent of this is hard to gauge, however many of these developers would have had their loans sold to NAMA and these properties would have appeared on NAMA's balance sheet. In 2012, NAMA revealed before the Parliament's Finance Committee that it had income of around €100 million per year from the rental of over 10,000 private rental properties, mostly apartments, making it by far the largest landlord in the state (McDonagh, 2012).

Also, in the post-crash restructuring of the financial sector, particularly through the activities of NAMA, the prospect of direct involvement of large corporations in the sector opened up. Several multinational corporations have acquired large portfolios of impaired loans from NAMA (and, to a lesser degree, directly from distressed entities). While these are acquisitions of loans contracts, not PRS properties themselves, the loans are secured by PRS properties and the purchaser may take possession or exercise powers of sale. This has happened—in Tyrrelstown, where loans to developer-cum-landlord Twinlite were sold to Beltany Property Finance, funded by Goldman Sachs, Beltany took action to evict 60 families ahead of property sales, which prompted law reform (see above). Some continuing institutional ownership of private rental housing is emerging: IRES, Hines, Kennedy and Wilson, and Oxley Holdings (Byrne 2015; 2016).

There is a small but growing institutional investment sector in Ireland in the form of Real Estate Investment Trusts (REITs), which are estimated to own 3,000 rental properties, mostly in Dublin. Current projections suggest this could grow to 15,000 properties, or 2 per cent of the market, in

five years. (House of the Oireachtas 2016: 31). The extent of rising rents, coupled with a lack of supply has supported the growth of REITs. The *Finance Act 2013* provided the tax framework for REITS. The rationale for their introduction was to remove the double layer of taxation from institutional investors. Before the introduction of amending legislation, revenues earned in a company were taxed both in the hands of the company, and subsequently in the hands of the shareholder, on any dividends distributed. Following tax changes, shares can be purchased in a REIT which holds a property portfolio, a REIT is obliged to distribute at least 85 per cent of its net rental income and is tax exempt on qualifying income and gains within the REIT. REITS were introduced as a means of allowing smaller investors to purchase a tax-effective interest in property, without the burden of property management and the benefits of a diverse portfolio. Irish Residential Properties (IRES), the state's largest private landlord (with 2,378 apartments), reported on 15 February 2017 (Brennan 2017) that its profit had risen to €47 million, from €30.6 million the previous year, an almost 50 per cent jump, driven by acquisitions and increases in average monthly income of 8.6 per cent. REITs have been criticised for their tax advantages in comparison to the private investor, from groups representing smaller private landlords, as the taxation regime favours REITS over traditional landlords. A representative of the Residential Landlord's Association noted in the Irish Times: 'Investors are coming in at the top end of the market who get tax breaks and who are rolling in money after buying up apartment blocks on the cheap. Small-time operators, who are the backbone of the industry, and who for the most part are decent people not there to rip off tenants, experience huge difficulties' (Taylor 2016).

The Government's recent Rental Strategy, while reiterating its support for the development of REITS in Ireland as an important component in increasing supply, have established a working group to examine the tax treatment of landlords.

However the media has recently focused on distressed asset portfolios acquired by so-called 'vulture funds'—large private equity investors that buy distressed debt at a cheap price, hoping to make a quick sale and to achieve a large profit on their investment (Irish Times 2017). In the wake of the Irish economic collapse they invested heavily in Ireland. The taxation regime in place since the 1990s allowed companies holding various financial assets to set up in a way that generated very little taxable income (section 110 of the *Taxes Consolidation Act 1997*). As reported by Brennan (2017), when it emerged that firms such as Cerberus, CarVal, Goldman Sachs and Davidson Kempner had used SPVs to acquire Irish property in such a tax efficient manner the Government came under pressure to act. The *Finance Act 2017* contained measures to remove such tax loopholes although the Master of the Irish High Court has recently said that he believes that the measures have not been entirely successful. The extent of property in the PRS currently held by such funds is not known.

## 2.4 Regulation

Since the turn of the century, the Irish Government has successively strengthened the regulation of the PRS, starting with the *Residential Tenancies Act 2004*. It may appear that the strengthening of regulation of the PRS in Ireland runs counter to international trends; however, it should be seen as part of a broader strategic shift by government from reliance on public sector to private sector provision of low-income housing (Hayden, Gray et al. 2010). Growth driven by the unique events of the 1990s—a growing affordability gap for those wishing to access home ownership, a significant decline in social housing provision which led to its developing role in housing low-income groups, net inward migration, decreasing household size and its importance to a rapidly developing economy—together with media and NGO pressure about the inadequacy of tenure security led to a 'perfect storm' which allowed moving the regulation of the sector forward by decades. In the period between the end of rent control and the introduction of the *Residential Tenancies Act*, only minor changes to the legislative code regulating the PRS

had occurred, principally in 1992 obliging landlords to register tenancies (unsuccessful) and to provide rent books. Limited minimum standards for rented housing were introduced at the time.

The introduction of the *Residential Tenancies Act 2004* was a landmark change in the regulation of the PRS in Ireland. The Act set up the Residential Tenancies Board, which all private landlords are legally required to register with. While there remain cases of landlords failing to register, unlike after the 1992 legislation, those still failing to comply are now approximately 15% of the total. The Board provides mechanisms for resolving disputes between tenants and landlords, providing a more accessible, and generally speedier, channel for both parties to seek to have their legal rights upheld.

The most remarkable feature of the Act is the set of provisions regarding security of tenure in the PRS (Part 4). These mean that if a tenancy continues past six months of occupation, the tenant is entitled to a 'Part 4 tenancy', which cannot be terminated by the landlord for three and half years (i.e. a total of four years from commencement) except on specified grounds: breach by the tenant; sale of premises; change of use; or where the landlord or a family member needs the dwelling for their own occupation (Section 34). Thereafter, the cycle starts again, with a six-month period in which the landlord may give a termination notice without grounds, then three and a half years in which termination is restricted. Part 4 does not impose fixed terms; fixed term tenancies coexist alongside the provisions of the Act but in the event of conflict the provisions of the Act take precedence. A fixed term lease cannot defeat the right of a tenant to a Part 4 tenancy if they have fulfilled the six month probationary period without breaching the provisions of the lease. A lease however can offer superior terms to the Act. For the tenant a fixed term tenancy, most often for a period of 12 months, can offer more security as it precludes a landlord from terminating within the six month period. A tenant who breaches a fixed term lease however may be liable for a landlord's losses arising from the premature termination. A tenant may terminate an agreement at any time in the Part 4 cycle with appropriate notice.

Ireland's second phase of PRS regulatory reform is ongoing, and influenced strongly by post-crash factors. In December 2015, in the face of rapidly rising rents, the Government introduced legislation to increase the rent review period from every year to every two years. The initial two-year period could be extended by a further two years though the measure was intended to be time limited. As Minister Kelly said, '*The housing market at the moment is dysfunctional ... rents are escalating far higher than peoples' incomes because of the housing shortage and the growth in employment*' (RTE 2015). Notice periods for the imposition of rent increases were also increased from 28 days to 90 days. The *Residential Tenancies (Amendment) Act (2015)* also specifies that the landlord seeking a rent increase must specify the rent amount for three comparable dwellings of a similar size, type and character and situated in a comparable area.

In order to prevent abuse of the measures enabling landlords to gain vacant possession, landlords intending to sell a property or to terminate a tenancy in order for a family member to use the dwelling were obliged to supply a statutory declaration (*Residential Tenancies (Amendment) Act 2015*). The legislation also allowed for the introduction of a Deposit Protection Scheme to be administered by the Residential Tenancies Board (RTB) though this section has yet to commence.

In December 2016, following a review process, the Irish Government introduced the *Planning & Development (Housing) and Residential Tenancies Act 2016* and published a Strategy for the Rental Sector. Some provisions of the new legislation were enacted with immediate effect:

- **Protection against mortgage lenders taking possession.** This is the so-called 'Tyrrrelstown amendment'; triggered by a highly publicised case of eviction of tenants in a property in Tyrrrelstown, a western suburb of Dublin, sold to an overseas fund.
- **Restrictions on rent increases in 'rent pressure zones' (RPZs).** An interesting innovation in rent regulation that the Government characterises as 'a more targeted, objective, time-

bound intervention to provide for rent predictability in high pressure areas in a way that will not negatively impact either existing or new supply' (Government of Ireland 2016). An RPZ is defined as an area where the average rent is above the national average rent, and where the annual rate of rent inflation has been 7 per cent or more in four of the past six quarters. In an RPZ, rents may not be increased more than 4 per cent per year. At enactment, the four local authority areas in Dublin and Cork City met the criteria and immediately became RPZs, and further areas have since been added that ensure that RPZs now include over 50 per cent of all privately rented properties. Those areas not covered still benefit from the two-year rent freeze legislation introduced in 2015.

- **Improved security of tenure.** Part 4 tenancies will move from a cycle of four years to six years. The housing charity and reform organisation, Threshold, suggests that this may lead to further reform to remove the cycle and maintain the Part 4 restrictions on terminations indefinitely.

#### 2.4.1 Standards of accommodation

There have been significant moves in recent years to improve the minimum standards of private rental housing, which have been relatively weak and largely unenforced. For example, under 1993 regulations, a landlord providing furnished accommodation was not required to provide a tenant with a cooker, a refrigerator or central heating, and toilet/washing facilities could be shared by up to four flats (*Housing (Standards for Rented Houses) Regulations 1993*). New regulations introduced in 2009 provide for greatly improved cooking, heating and laundry provisions, minimum space and storage provisions to facilitate family living, require landlords to maintain the exteriors of dwellings, and completely banned the traditional 'bedsit' (with shared facilities) by 2013 (*Housing (Standards for Rented Houses) Regulations 2008 and 2009*).

However, enforcement remains a problem, with a 2016 review conducted by the National Oversight and Audit Commission (NOAC) finding that 55 per cent of the private rental accommodation inspected by local authorities in 2014 was deemed non-compliant with the Standards for Rented Houses Regulations (NOAC 2016). The most common reasons for non-compliance with minimum standards were not meeting fire safety standards, or ventilation issues. Other breaches of minimum standards include issues relating to heating, sanitation, damp and mould.

The significant shortage of accommodation in the sector has led to difficulties in tenants enforcing their rights, with reports of landlords failing to make basic repairs, and tenants in fear of bringing a dispute in relation to repairs, in case of retaliatory eviction or a rent raise (Threshold 2016). Moreover recent high profile media reports have identified instances of significant overcrowding (O'Halloran 2017; Holland 2017).

License arrangements for rental accommodation under the law—typically for occupation of just one room—are very informal in nature, with little if any meaningful protection for the licensee. Licensees are not protected under Residential Tenancies legislation but must use the general courts system, which is costly, and issues such as the return of deposits is particularly problematic, requiring the licensee to have recourse to the Small Claims Court. Evidence from frontline service suggests that a growing number of people are becoming licensees, in particular students and younger people on social welfare or low incomes. While official data on the size of this sector does not exist, and it remains a small part of the overall housing stock, it is apparently becoming a sector of some significance.

There is growing concern also with the use of short-term rental arrangements such as Airbnb because of perceived negative impact on the availability of rental properties in the general private rental market. A recent Revenue Commissioners' directive made it clear that the Rent-a-Room scheme does not include such temporary lettings. The Strategy for the Rental Sector has

set out the government's intention to provide clarity in legal terms to address the unintended consequences of short-term lettings (DHPCLG 2016: 28).

## 2.5 Summary

There have been many changes in Ireland within the PRS in the last two decades. Many predate the GFC and the impacts of collapse of both the banking and construction sectors in Ireland. The introduction in 2004 of legislation moving Ireland from a relatively unregulated PRS in European terms to one which provided some measure of security and a measure of rent certainty was a significant change. Legislation governing minimum apartment sizes in 2006 envisaged that the sector would continue to grow and would provide an improved housing option for families. The introduction of the Rental Accommodation Scheme in 2004 had the impact of extending some of the benefits of social renting to tenants in the PRS—providing greater security in the form of longer leases—but more importantly extended the benefit of the differential rental system (rents based on income) and permitted improved labour market activation if the household desired. The benefit of differential rent is also available to tenants on another scheme introduced in 2014, the Housing Assistance Payment, though the contract is entirely governed by residential tenancy law. However, when one compares the rights of private renters as opposed to those who rent from a social housing provider, or who have purchased a home, while there has been some equalisation amongst them and a blurring in law of the distinction, renters—particularly economically vulnerable renters—continue to suffer disadvantage in the PRS, in particular a lack of long term security.

However, measures introduced since the financial crisis in 2008 have continued a trend in the better regulation of the PRS: Improved regulations on PRS standards, improved rent certainty and security of tenure and a strategy designed to deliver a strong and vibrant sector as a key component in a healthy housing market. Arguably the increased *regulation* of the sector has mirrored the increased role of the sector within the housing system. Whether some of the recent changes protecting tenants, deemed to be time limited, survive a recovery in supply and in the housing market generally, remains to be seen.

Change within the sector such as the emergence of new institutional landlords has occurred in large part due to the sale of distressed loan portfolios and not through new construction. Whether the government's aspirations to see more institutional investors in the market is consistent with limiting their investment returns will be shown in time.

The age profile of the sector is changing—it now houses more families and middle-income households—and whether a market emerges for affordable rental housing, cost rental housing or build to rent will depend on viability and state supports, while the question remains whether these middle-income families will wish to remain renting in the long run. The outcome will be influenced in part by the kind of regulatory environment that continues to evolve, particularly around the level of long term security provided in the sector. However, in spite of the uncertainty, changes have occurred which are unlikely to be completely reversed, ensuring a permanent change in the institutional profile of the PRS in Ireland.

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## Appendix 3: Private rental housing in the United Kingdom

By Mark Stephens

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Private renting has undergone a significant revival in the UK, and now houses almost one in five households.

The private rental sector is now houses a wide range of household types, with both lone parents and couples with children being over-represented.

Almost half of tenants have lived in their property for less than two years.

Private renting is very insecure in the UK and rents and rent increases are not regulated. However, security of tenure and provision for rent regulation in pressurised markets is being introduced in Scotland.

The private rental sector is dominated by small-scale landlords: more than 60 per cent of landlords own no more than four properties and 40 per cent of tenants are housed by these landlords.

The tax treatment of private rental housing is become less attractive. Mortgage interest tax relief is being restricted and a 3 per cent surcharge on transaction tax has been introduced.

Institutional investors have entered the market in recent years, although this 'build to rent' sector is in its infancy.

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### 3.1 Housing system context

The contemporary UK housing system is dominated by private provision, but with a legacy of local authority housing which, at its peak in the late 1970s, housed one-third of households (Stephens 2013; Stephens and Stephenson 2016.)

In the first 70 years of the twentieth century, owner-occupied housing, and social rented housing grew, and private renting declined. These trends were the result of rent controls in the private rental sector (first introduced in 1915), the increasing availability of mortgages from the 1930s, which financed the first and subsequent booms in home ownership, and the subsidies made available to local authorities to build social rented housing. The decline in private renting and the rise of social renting was also linked to slum clearance policies (dating from the 1930s) and urban renewal (after the Second World War). Home ownership, which also benefited from favourable tax treatment, became the majority tenure around 1970, and social renting peaked at about 33 per cent of households in the late 1970s. The balance was made up of private renting that had declined from perhaps 90 per cent before the First World War.

These trends began to change in the 1976 financial crisis, when the IMF 'bailed out' the UK which resulted in public expenditure cuts, leading to a permanent reduction in public finance for social rented housing investment. Then in 1980, the Right to Buy policy was introduced, resulting in the permanent loss of social rented (especially local authority) housing, as tenants took advantage of the large discounts made available. The policy was possible on a large scale because the housing debt was quite mature and had been eroded by inflation in the 1970s. In

the 1980s owner occupation was further boosted when mortgage markets were liberalised and lending criteria loosened. This also coincided with the emergence of house price volatility in the market. Within the social rented sector, housing associations emerged as the principal providers of new social rented housing from the late 1980s due to government policy. These housing associations financed new build housing with a mixture of government grants and private finance. Further, transfers of local authority housing to housing associations facilitated refinancing and rehabilitation in the 1990s and 2000s. But overall, the social rented sector continued to decline.

**Table A 1: Tenure change, UK, 2003/04–2015/16 (% households)**

2003/04	Owned outright	Buying with mortgage	Social rented	Private rented	2015/16	Owned outright	Buying with mortgage	Social rented	Private rented
16–24	1	22	29	47		1	9	20	71
25–34	2	56	18	23		3	33	18	46
35–44	7	64	18	11		6	51	17	26
45–54	22	56	15	7		19	50	17	14
55–64	49	31	16	5		48	26	17	9
65+	65	4	26	5		73	4	18	6
All	30	39	20	11		34	29	18	20

Source: DWP (2016).

A new phase occurred in the early 2000s, when owner occupation peaked and then began to fall. The headline figure disguised much larger reductions among younger age cohorts (see Table A 1). The principal cause was simply that housing had become too expensive, even in the context of liberalised mortgage markets. This was further exacerbated when the availability of mortgage finance became constrained as a result of the GFC and subsequent regulatory reforms. As the owner-occupied sector has matured, the proportion of households with a mortgage has declined by around 10 per cent over the past decade and is now eclipsed by the 34 per cent of all households who own their property outright.

The revival of the private rental sector began after the deregulation of new tenancies in 1989—ending rent control and regulation and allowing short-term (six month) tenancies without security. Greater mortgage finance was also made available with the introduction of buy-to-let mortgages in the mid-1990s. Slightly more households now live in the private rental sector than in the social sector.

Since the early 2000s, there has been a growing awareness that housing shortages were re-emerging, as house construction lagged behind household growth. Planning reforms in the early to mid-2000s had a limited impact before the GFC struck and severely reduced the capacity of the industry, which required government support. Further emphasis has been placed on planning reforms in recent years. However, there is also a growing focus on the building industry, which operates on a speculative model and appears to hoard land to make speculative gains and ‘drip feeds’ new properties onto the market by varying the speed of build out. Issues of paying for infrastructure and using taxation as an additional lever to encourage development have been widely discussed (Aubrey 2015.)

The UK’s pattern of housing subsidy has also changed radically. In the mid-1970s, some 80 per cent of subsidy (including tax subsidies) was broadly ‘supply side’—aimed at facilitating new development. Now more than 90 per cent is ‘demand side’, largely because of the Housing

Benefit for private and social tenants. Rent rises in the social rented sector in the 1980s increased dependence on this means-tested benefit, but more recently growth in private renting has been the main source of pressure. The austerity programs adopted by governments from 2010 have led to significant tightening of the Housing Benefit, however it remains the largest single 'cash' housing subsidy. Nonetheless, it should be noted that a series of schemes to support access to home ownership have been implemented, and include equity shares, loans, guarantees and other support, and amount to almost £43 billion over the period 2015/16—2020/21 (Wilcox, Perry et al. 2017: Table 2.4.1).

There is increasing diversity in housing policy throughout the UK, and particularly between England and Scotland (Stephens 2016). Devolved Parliaments and Assemblies were established in Scotland and Wales in 1999 and the Northern Ireland Parliament was established a few years later. The Scottish Government now provides more extensive protection to homeless people, is undertaking a significant social and affordable rental house building program, has abolished the Right to Buy and has legislated for security of tenure in the private rental sector and for second generation rent controls in pressurised markets. This contrasts with the policy in England, where Right to Buy has been 'enhanced', subsidy for traditional social rented housing virtually ended, and a series of policies such as fixed term tenancies are altering the nature of the social rented sector.

### **3.1.1 Economic context**

It is important to note many of the developments in the housing system have been influenced by the wider economic context following the Global Financial Crisis.

The Bank of England's Monetary Policy Committee responded to the GFC by reducing base rates to an historic low of 0.5 per cent (subsequently lowered to 0.25% following the Brexit referendum) and a large scale program of quantitative easing (revived in the aftermath of the Brexit referendum result). These measures were intended to support asset prices, and have had that effect. This is one reason why house prices did not fall as much as one might have expected as a result of the GFC, and also why borrowing, and in particular mortgages, are cheap.

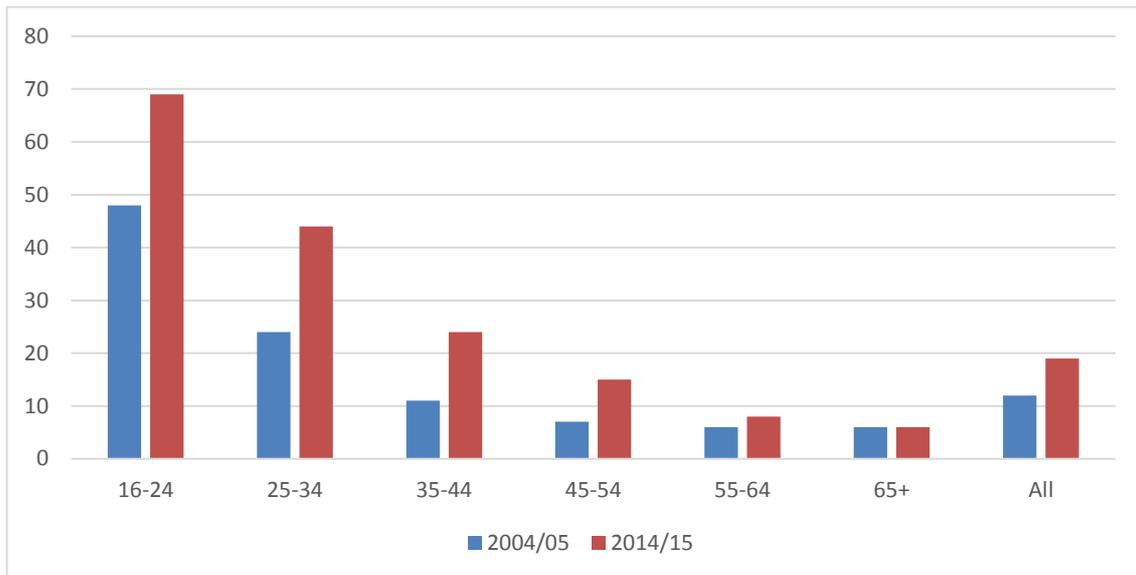
The terms of mortgages are now more onerous, however, due to the GFC's impact on bank balance sheets, and the subsequent regulatory reforms relating to capital adequacy, micro- and macro-prudential regulation (including mortgage regulation)—in particular, larger down payments are favoured and in many cases required.

Together this creates a further barrier for first time buyers who do not have sufficient savings for a deposit, but favours established home owners with large amounts of equity in their houses, who are able to make large deposits and secure favourable mortgage terms to invest in rental property. Real estate investment is attractive because returns from other investments are so low, and the decline in occupational pensions means that they are looking for long-term sources of income.

### **3.1.2 Tenants**

Using data from the Family Resources Survey of UK (DWP, 2015; DWP, 2017), we see that among UK private tenants, there is a clear age profile for private renting, but the rises are working their way up the age spectrum. The private rental sector is now the most common (modal) tenure for 16–24 year olds (69%) and 25–34 year olds (44%), and these proportions have risen dramatically over the past decade. It is notable that the private rental sector has grown in all age cohorts other than the oldest (65+). The proportions of 35–44 year olds and 45–54 year olds who were private renters more than doubled over the decade to 2014/15.

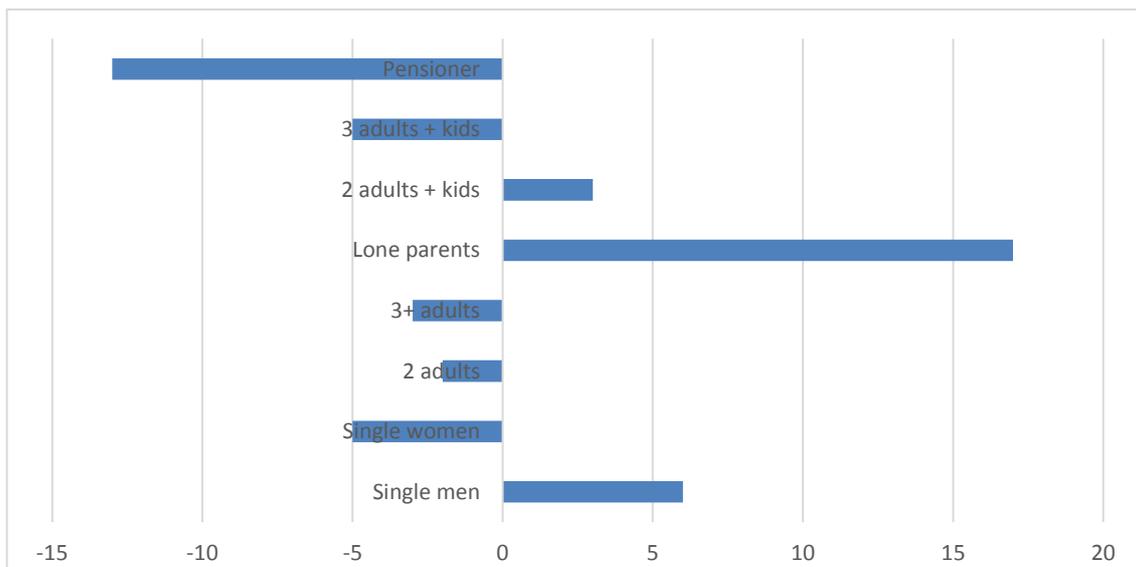
**Figure A 1: Private renting by age**



Source: DWP (2015).

The private rental sector was once the preserve of the young, single and transient, together with a declining number of older people living in historic secure tenancies with regulated rents. As Figure A1 shows, that profile has changed. One of the features of the contemporary private rental sector is the rise of children living in it. Now, although 25 per cent of single men are private renters (so are over-represented) only 14 per cent of single women live in the sector (and are therefore underrepresented). Some 36 per cent of lone parents and 22 per cent of households with two adults and children are private renters. Only 6 per cent of households headed by someone over pensionable age are private renters, the most under-represented group.

**Figure A 2: Over- and under-representation of household types in the private rental sector (2014/15)**

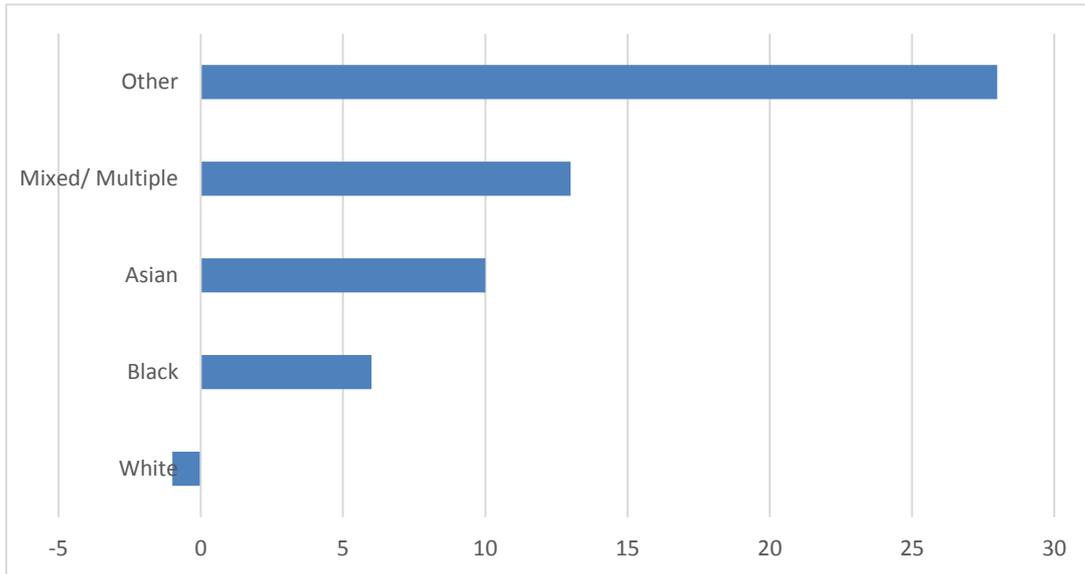


Note: Percentage point difference between average % of households living in the PRS (19%) and % of each household type in PRS.

Source: DWP (2015).

Among ethnic groups, people identifying as 'white' are proportionately slightly under-represented in the sector, whilst minority ethnic groups are over-represented. However, this generalisation does not hold for every sub-category of ethnic group.

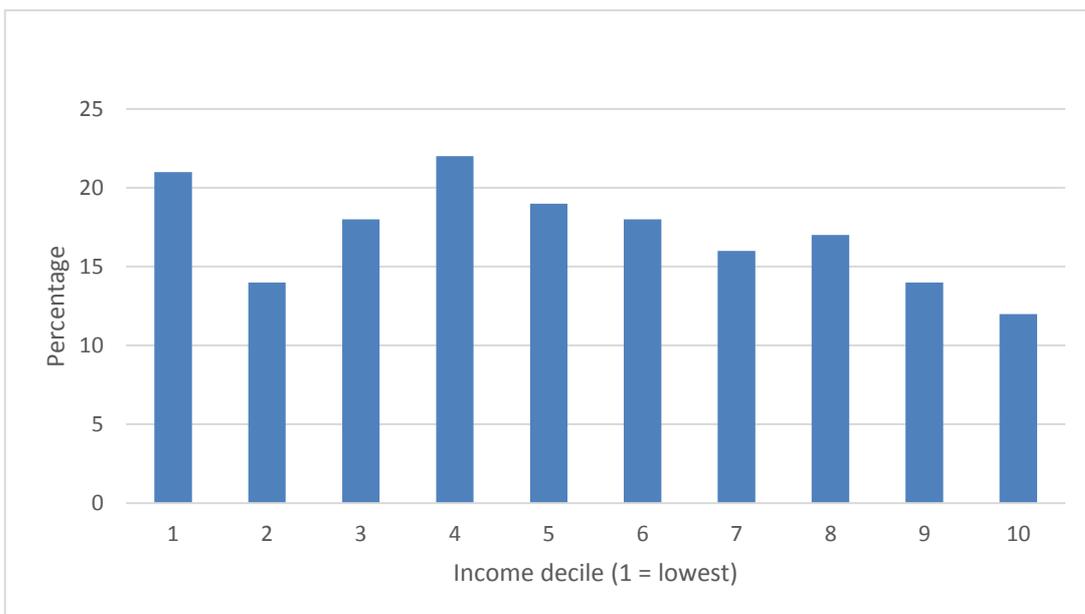
**Figure A 3: Over and under-representation of ethnic groups in the private rental sector (2014/15)**



Source: DWP (2015).

Of all of tenures, private renting is the most evenly distributed by income. At least 12 per cent of households in each income decile are private tenants whilst no more than 22 per cent are private renters. In seven of the income deciles more than 15 per cent of households are private tenants. There is some fall away in the top two income deciles, but the proportion of private renters in these income deciles are similar to those in the second lowest income decile.

**Figure A 4: Percentage of households in each income decile living in the private rental sector**



Source: DWP (2015).

Of course this does not mean that there is equality within the sector! Rather it shows the diversity of the tenure. However, it does mean that the legal framework that governs the sector is experienced by a significant proportion of people from across the income spectrum, which would not be the case with the rules relating to social rented housing, or Housing Benefit.

Private tenants have been resident in their homes for substantially less time on average than is the case across all households, where the average length of residence is 28 years compared to just four in the private rental sector.

**Table A 2: Length of residence**

	<12m	12m<2yr	3<5yr	5<10yr	10<20yr	20+yr	All
All	9	9	7	9	17	21	28
PRS	25	23	15	15	13	6	4

Source: DWP (2015) Table 3.4

One quarter of private tenants have been resident for less than a year and almost half for less than two years (compared to 18% of the whole population). In contrast 38 per cent of all households have been resident for more than a decade (compared to 19% of private tenants). There is a limit to what can be read into a single year's data—because the private rental sector is growing, we would expect a greater prevalence of shorter-term residencies. And considering that the sector was relatively small 20 years ago, it is simply not possible for many private tenants to have been resident in the same property long term. As the private rental sector matures, we anticipate the proportions of longer-term residencies to grow. More than one-third of private tenancies exceed five years and almost one-fifth exceed 10 years.

The tenant profile of the private rental sector has changed significantly as the sector has grown—it is now a tenure in which people from across the income spectrum are well represented, and it houses many households with children. As it grows and its nature changes, there is a growing question mark over the appropriateness of the current legislative framework governing the sector.

## 3.2 Finance settings and subsidies

The UK Government governs almost all aspects of finance, taxation and subsidy for private renting.

### 3.2.1 Financing purchase

The growth in the private rental sector was boosted by the increased availability of mortgage finance, especially after the agreement between landlords and the Association of Residential Landlords that led to the introduction of the buy-to-let (BTL) mortgage in the mid-1990s, on more favourable terms than previously. The sector is also financed by landlords' equity in their own homes. BTL mortgages are currently subject to less onerous regulation, with a consequence that interest-only mortgages are more readily available to landlords than to would-be owner-occupiers. In the first quarter of 2015, more than 80 per cent of advances of non-regulated mortgages were interest-only, compared to less than 10 per cent of regulated advances (Wilcox, Perry et al. 2016).

The 2010 Landlord Survey found that 56 per cent of dwellings were acquired with a mortgage and 21 per cent with savings. The figures for private individual landlords were 64 per cent mortgage and 22 per cent savings (Table A3). The 2016 landlord survey found that 41 per cent of landlords had used savings, 36 per cent BTL mortgages, and 17 per cent inherited funds

(Scanlon and Whitehead 2016). The two sets of figures are not comparable, so it is not possible to discern a trend.

We can turn to macro-level data to identify mortgage finance trends. Taking Q1 data from each year from 2007, we see that gross advances for all residential mortgage lending fell from £86 billion in Q1 2007 (i.e. before the credit crunch) to £33 billion in Q1 2009. A sustained increase in lending volumes began only after 2013 (when Q1 lending was £30 billion). In Q1 2016 the figure was £64 billion—still some £22 billion below the 2007 figure (Bank of England, MLAR Statistics Residential loans to individuals, March 2017). The BTL share of these totals fell from 11 per cent in Q1 2007 to 6 per cent in Q1 2009 and 2010 before recovering to 12 per cent in 2013 and 21 per cent in Q1 2016. In terms of volume these data imply that in Q1 2007, BTL gross advances were £9.5 billion in Q1 2007 and £13.4 billion in Q1 2016, having been as low as £2 billion in Q1 2010.

A further caveat is that the purchase of properties to rent are often financed by the remortgaging of the landlord's own home. If the owner can demonstrate that the loan was taken out to purchase a rental property it is still eligible for interest rate deduction. This has the advantages of greater flexibility of use for the new property, a likely lower interest rate, and the de facto LTV on the new property is probably higher than the de jure LTV based on the landlord's own property.

### **3.2.2 Taxation**

For much of the 1960s to the 1990s home ownership received favourable tax treatment over private renting. From 1963 owners paid no tax on imputed rental income, but received unlimited tax relief on mortgage interest. This arrangement was dismantled incrementally, mainly from 1990, when the rate at which interest could be deducted was first limited to the basic taxation of, and then reduced in stages to zero in 2000.

In contrast, private landlords always paid tax on rental income, but could offset mortgage interest costs against tax. Close to parity was reached in 2000, except for one important fact: home owners continued to be exempted from capital gains tax on their principal dwelling, unlike landlords.

There is no provision for 'negative gearing' (i.e. offsetting rental losses against other sources of income) in the UK.

Nonetheless the Government is reducing the rate at which costs (mortgage interest) can be offset against income for higher rate tax payers, until it will be equal to the standard rate of tax (25%). Rules about the way 'wear and tear' expenses can be deducted from tax are also changing from being based on a yearly allowance to actual costs.

**Table A 3: Restrictions of cost relief to individual private landlords**

	<b>Maximum share of interest that can be deducted at marginal tax rate</b>	<b>Minimum share of interest that can only be deducted at basic rate</b>	<b>Saving to Government (£ million): Restriction of interest tax relief (£ million)</b>	<b>Saving to Government: Reform to Wear and Tear Allowance (£ million)</b>	<b>Saving to Govt: SDLT surcharge on BTL and 2<sup>nd</sup> homes (£ million)</b>
2016/17	100%	0%	n.a.	n.a.	n.a.
2017/18	75%	25%	0	205	625
2018/19	50%	50%	225	165	700
2019/20	25%	75%	415	165	760
2020/21	0%	100%	665	170	825

Source: Wilcox, Perry et al. (2016).

In April 2016, houses purchased as second homes or for renting became subject to a 3 per cent surcharge in transaction tax (known as Stamp Duty Land Tax)—a measure intended to reduce the bidding power of landlords compared to would be home owners. Together these measures are expected to raise in excess of £1.6 billion each year by 2020/21.

The recent landlord survey by Scanlon and Whitehead (2016) suggests that the tax changes will have the greatest impact on the more ‘professional’ landlords (rather than those who own just one property). This is because they have larger portfolios; are more likely to buy and sell properties, and so be liable to the surcharge on transactions; are more likely to have mortgages; and be higher rate taxpayers, so vulnerable to tax relief reductions.

### **3.2.3 Support for tenants**

The UK has an extensive housing allowance system, generically called Housing Benefit, but known as Local Housing Allowance in the private rental sector which is by far the largest subsidy to assist tenants.

Housing Benefit was introduced in 1972/73, and has been subject to notable reforms. The current design has been in place since 1988, and is designed to prevent post rent incomes falling below the social assistance threshold. Consequently, it can pay 100 per cent of rent for people with incomes at or below the social assistance level. It also means that if rent rises by £1, HB rises by £1, and vice versa. The PRS was deregulated in 1989 and new tenancies freed from rent control—the idea that HB would ‘take the strain’ was deliberate policy.

HB in the private rental sector was reformed in 2006, when it became the Local Housing Allowance. This reform included setting standard eligible rents based on the median local market rent (in place of actual individual rents), intended to incentivise tenants to obtain cheaper accommodation, as they could keep up to £15 per week if their actual rent was lower than the LHA rate. The benefit was now paid directly to tenants—whereas before there was the option to pay it to the landlord—intended to give tenants a greater sense of responsibility.

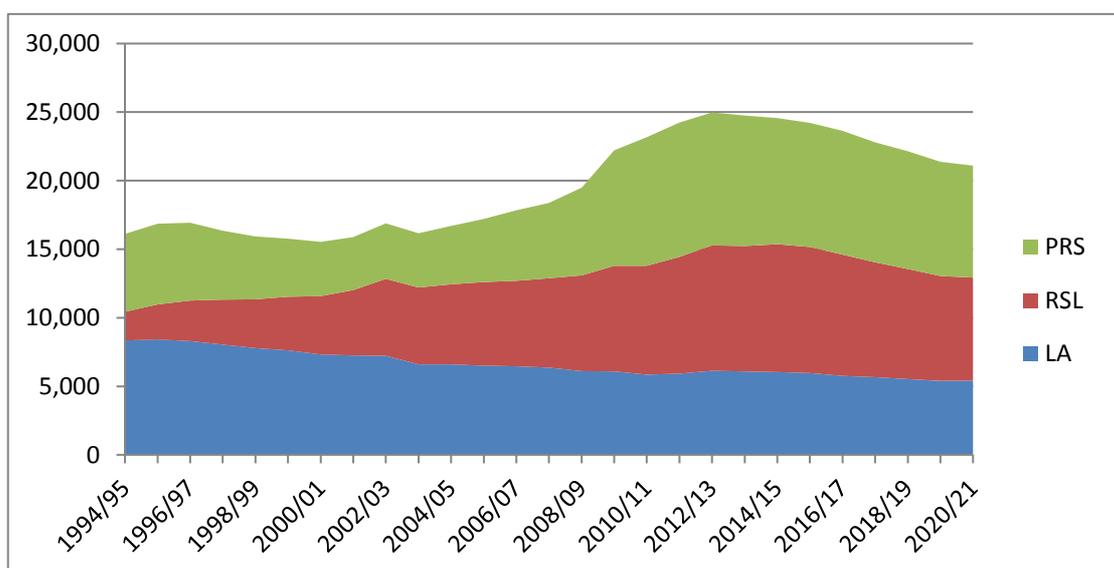
The cost of HB rose rapidly for a number of reasons, including the growth in the PRS and the effect of the GFC. Consequently, it has been a target for post-2010 austerity policies. The PRS was targeted by the Government first, with a series of restrictions. These included the removal of the up to £15 allowance associated with LHA; extension of the ‘shared accommodation rate’ from single people aged up to 25 to 35 (eligible rents are based on the rent of shared

accommodation in the area); and limiting the LHA to 30 per cent of median local rent (initially increased with CPI, rather than actual rents, and now frozen).

The UK Government is also introducing a new system of social security called Universal Credit, which involves the merger of six working age benefits into a single one. Housing Benefit would disappear and be absorbed within it—thus removing HB as a transparent source of housing subsidy.

Social security still operates on a more-or-less uniform basis in Great Britain. The Scottish Parliament recently gained the ability to alter the ‘housing cost element’ within Universal Credit and some administrative aspects to the housing element, but this doesn’t provide much flexibility. For example, the Scottish Government wishes to retain the ‘automatic entitlement’ to HB for 18–21 year olds, but the legal mechanism for doing so is unclear.

**Figure A 5: Costs of Housing Benefit by tenure (£ '000)**



Notes: PRS = private rental sector; RSL = registered social landlord; LA = local authority. Figures are outturns except from 2015/16 where they are forecasts.

Source: DWP (2017).

The cuts in Housing Benefit and other social security benefits seem to be driving an increase in evictions or non-renewal of tenancies. The expiry of private contracts is now the largest immediate cause of homelessness in England, which may have been a factor in the passing of the Homelessness Reduction Act, which increases local authorities’ obligations to help single people threatened with homelessness.

### 3.3 Landlords and agents

The CLG landlord survey of 2010 confirmed that the sector is dominated by private individuals—almost 90 per cent of all private landlords are private individuals, 5 per cent are companies, and 6 per cent ‘other’ organisations. The other organisations may include charitable landlords or trusts which are not registered as social landlords. Weighting the landlord profile by the number of dwellings owned we see that about 70 per cent of properties are owned by private individuals, 15 per cent by companies and 14 per cent by other organisations. Note that ‘companies’ does not necessarily imply large landlords, as even the owner of a single property can register as a company, and recent tax changes may make it worthwhile to do so. However, the figures show that companies clearly own more properties on average.

Figures in the tables below suggest that this trend is strengthening, because the proportion of private individuals is higher among new landlords. Given that statistically there are no landlords with more than 100 properties (in fact there are some, just too few to register in that column), portfolios are self-evidently much smaller than among local authorities or housing associations.

**Table A 4: Landlord profile (2010), by % of landlord entities**

	New landlords	Longer-term landlords	All landlords
Private individuals	98	89	89
Companies	1	3	5
Other organisations	1	8	6

Source: CLG (2011), Tables 2.1a and 2.1b

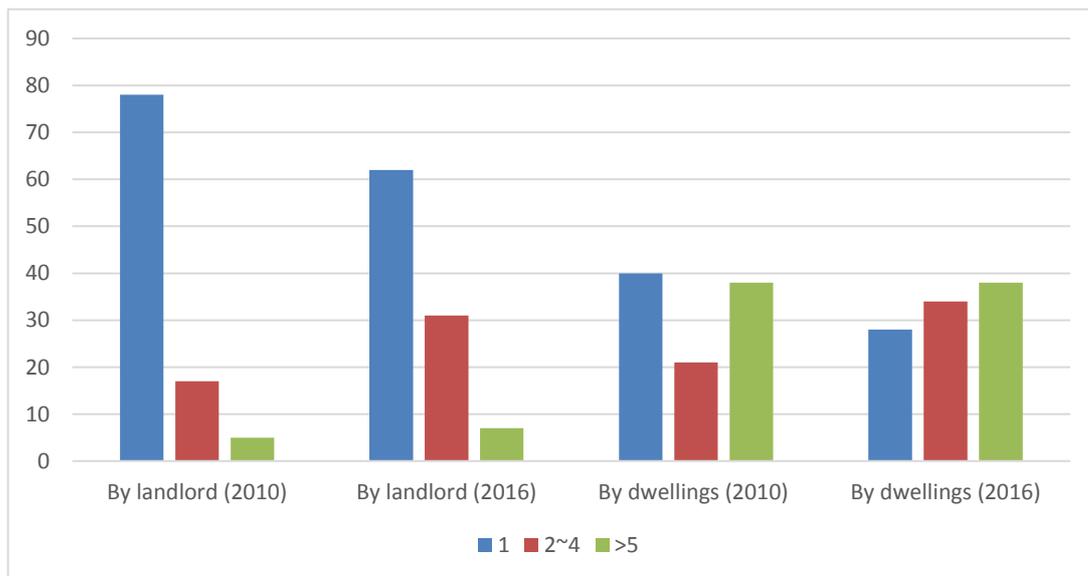
**Table A 5: Landlord profile (2010), by % of rented dwellings**

	New landlords	Longer-term landlords	All landlords
Private individuals	93	69	71
Companies	5	14	15
Other organisations	1	17	14

Source: CLG (2011), Tables 2.1a and 2.1b.

The CLG 2010 survey can be compared with the more recent (2016) survey for CML for the distribution of stock between landlords. To the extent that the data are comparable (there may be sampling differences) there may have been a reduction in the number of landlords managing only one property, and an increase in the proportion managing 2–4 properties. There does not seem to be much change in the proportion of landlords managing more than five properties.

**Figure A 6: Landlord and stock profile**



Source: CLG (2011); Scanlon and Whitehead (2016).

This trend is reflected in the figures for the number of dwellings managed by landlords of different sizes. The 2010 survey found that 40 per cent of dwellings were managed by single property landlords; in the 2016 survey this had fallen to 28 per cent. The proportion of dwellings managed by landlords with portfolios of between two and four properties was reported as 21 per cent in 2010 and 34 per cent in 2016. The 2016 survey has a catch-all category for landlords with five or more properties. The 2010 survey provides breakdowns for 5–9, 10–24, 25–100 and >100 properties, and found that 11 per cent of dwellings were managed by landlords with portfolios exceeding 100 properties, 10 per cent by those with 25–100 properties, 9 per cent by those with between 10 and 24 properties, and 9 per cent with between 5 and 9 properties.

### **3.3.1 Institutional investors**

The institutional investment (now called Build to Rent) sector has grown in recent years, following decades of unfulfilled expectations. A government-sponsored report on barriers to institutional investment, the Montague Report (2012) suggested that the historic yield of 3.5 per cent p.a. was inadequate and needed to be supplemented with capital appreciations. The report suggested that the sector should be assisted by: waiving affordable housing requirements in the planning system; the government sharing development risk; and that a separate planning class be established whereby newly built houses would have to remain in that tenure for 10–21 years. This was based on the curious assumption that land values are driven by owner-occupied housing values, which are above rental values. The lobby for such subsidies is persistent and includes the British Property Federation (BPF) and the Royal Institution of Chartered Surveyors. A recent government commissioned report also recommended tax incentives and ‘planning breaks’. The Government intended to exempt large-scale landlords from the 3 per cent transaction tax surcharge on non-primary homes, but abandoned this proposed concession.

Institutional investors are believed to be planning to commit £50 billion to the build to rent sector by 2020, according to a property consultancy survey (Financial Times 15/05/17). The BPF announced that 22,293 units were under construction in the year to October 2016—a 214 per cent increase on the previous year, and in total 35,121 units have planning permission. Investors are a mix of developers and institutional investors.

The case for supporting the sector is partly that it should produce better quality rental accommodation. The recent Housing White Paper for England makes a cautious commitment to consult on whether it would be possible to introduce ‘family-friendly’ tenancies in this sector (tenancies of up to three years’ duration).

The White Paper also proposes to give local authorities the duty to provide build to rent developments where there is a need for it. This falls well short of the lobbied separate planning class, exempted from planning obligations (i.e. contributions to infrastructure based on the uplift in land value arising from granting of planning permission).

It should also be noted that some housing associations have entered the build to rent sector. This is partly to recycle profits into affordable housing, but also reflects a drift away from their original mission by large housing associations, now substantial organisations in their own right. Reductions in government subsidy for new development also makes housing associations reconsider their business models.

## **3.4 Regulation**

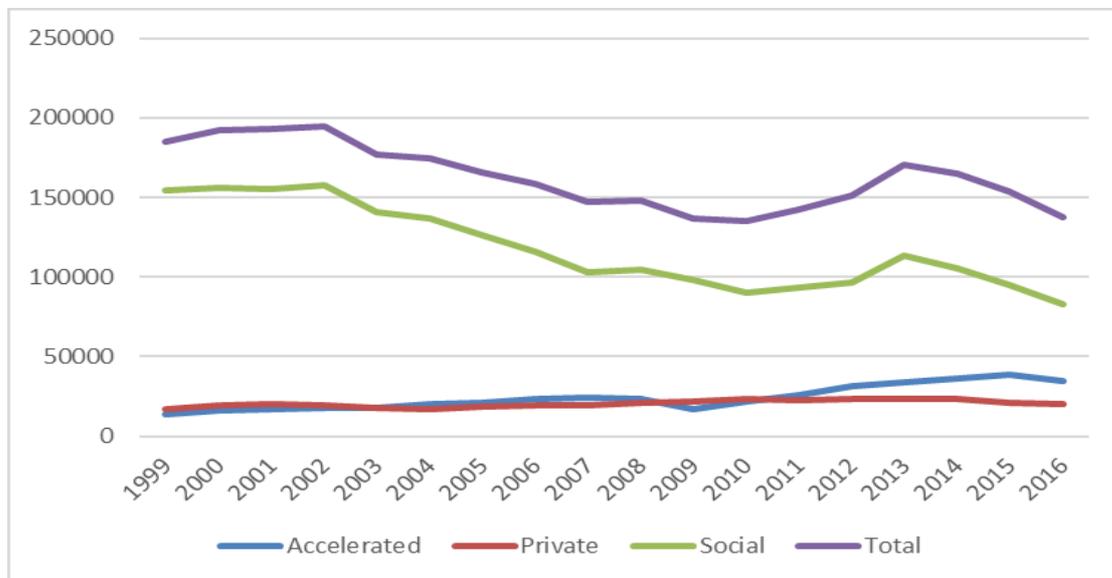
Before 1989, private tenancies in the UK were secure and subject to rent regulation. However, various legal loopholes were employed by landlords in an attempt to avoid providing the protection intended for tenants. For example, ‘licences to occupy’, which were intended for

hotels and short-term hostel accommodation, were used by some landlords, leading to various court cases.

From 1989 this changed. Landlords could now employ one of two types of tenancy: ‘assured’ tenancies which are secure, but not subject to rent restrictions, and ‘assured shorthold tenancies which are fixed-term (for a minimum of six months) and are also not subject to rent restrictions. These assured shorthold tenancies allow landlords to regain possession of the property when a tenancy expires without giving a reason. If tenancies are allowed to lapse they usually become monthly periodic tenancies (the month being determined by the frequency of rent payment). This means that tenants are no more than a month away from potential eviction proceedings.

The tilting of contractual rights in the landlord’s favour was seen as being necessary to revive the sector, and there were no attempts to roll it back during the 13-year period of Labour Government from 1997–2010, during which time the sector grew substantially. Almost all tenancies are now assured shorthold (or short assured, as they are called in Scotland).

**Figure A 7: Landlord possession claims, England and Wales 1999–2016**



Source: Ministry of Justice Mortgage and Landlord Possession Statistics (2017).

Since the late 1990s, the numbers of landlord possession claims from private landlords rose from 17,000 in 1999 to 23,000 in 2014, but fell to an intermediate level since then. However, the true extent of possession claims from private landlords is unknown because the ‘accelerated’ claims figures do not distinguish between social and private landlords. It is worth noting that although the vast majority of social tenants have security, the absolute number of (non-accelerated) evictions is four times the level in the private sector. However, they have also fallen substantially, so the gap is now smaller than it was.

### 3.4.1 Tenancy Reform

A major reform of tenancy is taking place in Scotland. After considerable deliberation, the Scottish Government introduced legislation to provide tenants with greater security of tenure and provision for selective use of second-generation rent controls in pressurised markets. The legislation commenced December 2017. Landlords will be able to gain vacant possession of a property if tenants breach one of the grounds listed in the Act, such as owing three months’ rent arrears or breaching other terms of the tenancy. ‘No fault’ evictions are restricted to the landlord wishing to use the house for another purpose, such as selling it, renovating it, or living in it

themselves. If a tenant is wrongly evicted because (for example) a landlord said they were going to sell the property, but instead re-let it, the tenant could be entitled to compensation. The Bill contained provision for initial fixed-term tenancies, after which either party could walk away, but this was removed—therefore there is no provision for short-term lets, however, a tenant may leave with 28 days' notice.

The Act also introduces provision for second generation rent controls. Local authorities will be able to request that Ministers designate all or parts of their jurisdiction as 'rent pressure zones'—in which rent increases are to be limited to inflation plus 1 per cent for a maximum of five years.

Relatively minor reforms are being introduced in Wales. Tenancies will be either 'secure' or 'standard'—the latter being modelled on the assured shorthold model.

### **3.4.2 Licencing schemes**

There is no comprehensive licencing scheme for mainstream (i.e. not HMO) private landlords in England. Local authorities were permitted to introduce selective licencing schemes, but the Government now requires them to seek permission should they make up more than 20 per cent of their area. Some schemes have been withdrawn on the grounds that they are administratively cumbersome and ineffective in tackling the worst problems (Wilcox, Perry et al. 2016).

The Scottish Parliament approved the mandatory licencing of private landlords in 2004, and this was introduced in 2006. All landlords must register with the local authority where they rent property, and pay a fee. The legislation was intended to identify rogue landlords (there is a 'fit and proper' persons test), but in reality only 40 had their applications rejected between 2012 and 2016 (Wilcox, Perry et al. 2016). The Welsh scheme, which began in November 2015, requires landlords to undergo some basic training. Northern Ireland has also introduced mandatory licencing.

### **3.4.3 Tenancy deposit schemes**

Tenancy deposit schemes are now mandatory throughout the UK. These schemes are intended to ensure that tenants do not have their deposits withheld unreasonably, after the tenancy has ended, and that they are returned in a timely manner.

### **3.4.4 Housing in Multiple Occupation (HMOs)**

In Scotland, HMOs are defined as dwellings in which three or more unrelated people live, and cover student halls or residences and hostels, as well as houses and flats. The owner must have a license (obtained from the local authority) in order to rent out the accommodation. This involves a fit and proper person test and the accommodation must meet various safety criteria. In England, HMOs are defined in a similar way, but a license is required only if it is a 'large' HMO, that is, it houses at least five people who are from more than one household, the property is at least three storeys high, and the tenants share toilet, bathroom or kitchen facilities. Local authorities have a discretionary power to require smaller HMOs to be licensed. The recent White Paper indicates that the Government will extend the scope of mandatory licencing in England.

## **3.5 Conclusions**

The private rental sector in the UK has experienced a significant revival in the past 25 years, and represents an important restructuring of the housing system. In the 1970s and 1980s most professional households and many others could expect to become home owners. If they experienced private renting, it would be likely to be a temporary and transitional stage between leaving the parental home and becoming a home owner.

Now the private rental sector houses a wide spectrum of households. It is clear that its growth has worked its way up the age cohorts and it will be the destination tenure for many households. The sector is no longer characterised as being for the young, single, transient and old—it now houses disproportionate numbers of couples with children, for example.

Yet it is a very insecure tenure—tenants can be evicted by landlords after six month tenancies have expired. Such arrangements may have been tolerable in the past, but they are far from ideal for families with children. Substantial tenancy reform is occurring in Scotland, where security of tenure is being introduced, and provision made for restricting rent increases in pressurised markets. Far more modest reforms have been mooted in England – perhaps tenancies of up to three years in private rental accommodation provided by institutional investors and housing associations. Such build to rent landlords are relatively new in the market, but much hope has been attached to them, both in terms of providing new housing, and on improved terms for tenants. It seems likely that the PRS will be focused on by Government policy for the next few years.

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## Appendix 4: Private rental housing in the United States

By Alex Schwartz

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Rental housing in the United States has grown sharply in the aftermath of the country's massive housing crisis that began in 2007 and has only recently abated. Prior to the crisis, rental housing had been declining as a share of all housing, but since the late 2000s it has generated most of the growth in housing stock. Moreover, the post-crisis years have seen sharp increases in the number of single-family rental housing.

This report summarises key features of rental housing in the US, focusing on its physical characteristics, its ownership and regulation, and the socioeconomic and demographic characteristics of its occupants. Throughout the discussion, the report highlights the effects of the housing crisis on the rental sector.

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### 4.1 Housing system context

#### 4.1.1 Overview of the rental housing sector and its development since the housing crisis

Nearly all rental housing in the US is privately owned. Almost 44 million households rented their homes in 2015 (37% of all households), and approximately 95 per cent of these households rent from private, for-profit landlords. About 5 per cent rent from public or non-profit owners: these forms of rental housing include public housing, the oldest low-income subsidy program in the US, and various types of subsidised housing owned by non-profit organisations. Non-profit organisations account for all federally subsidised housing designated for low-income elderly and disabled households, about 25 per cent of all housing produced with Low-Income Housing Tax Credits (LIHTC), and perhaps 30 per cent of all other federally subsidised low-income housing.

The vast majority of rental housing in the US is unsubsidised. In 2015, there were about 2.5 million renters living in public housing or in other housing with project-based rental assistance. In addition, 2.1 million renters resided in housing that was financed with federal LIHTCs—a flat subsidy that serves households with somewhat higher incomes—and 2.4 million renters received portable 'Housing Choice Vouchers' that enable them to lease housing in the private market (Table A6)<sup>10</sup>.

Subsidised rental housing has seen little growth over the past decade. Of the three major deep-subsidy programs that limit rent payments to about 30 per cent of household income, only the Housing Choice Voucher program has grown, albeit slightly. At the same time, the public housing program has lost about 10,000 units annually to demolition and disposal. There has also been very little growth in project-based rental assistance ('Project-based Section 8'), whereby the US Government subsidises the rent of housing under private and non-profit

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<sup>10</sup> Rental housing subsidy programs are discussed in more detail later in the report. It is important to note that Table 1 excludes housing subsidised exclusively with state and/or local funds (without any federal support), as well as 'affordable' housing provided through inclusionary zoning (also discussed later).

ownership. The LIHTC program has increased by about 100,000 units annually (Department of Housing and Urban Development, 2015).

**Table A 6: Rental housing, ownership and subsidies, United States 2015.**

	Total	Per cent
Total rental housing units	43,930,000	100%
<b>Ownership</b>		
Private	41,714,482	95.0%
Public Housing	1,119,864	2.5%
Non-profit	1,095,654	2.5%
<b>Federal subsidies</b>		
None	36,822,095	83.8%
Housing Choice Vouchers	2,447,016	5.6%
Public Housing, Project-based Section 8, and other deep subsidy programs	2,509,520	5.7%
Low-Income Housing Tax Credit (LIHTC)	2,151,369	4.9%
Total subsidised	7,107,905	16.2%

Source: Department of Housing and Urban Development (2015).

With regard to the physical characteristics of the housing stock, Table A7 shows that while more than 80 per cent of all home owners occupy detached single-family housing, the same is true for just 29 per cent of all renters. Conversely, 39 per cent of all renters reside in multi-family buildings with five or more units, compared to just 3 per cent of all home owners. Renters tend to occupy older housing than home owners, and their homes are more than twice as likely to have severe or moderate physical problems than home-owner housing—although the overall incidence of physical problems is far lower than that of affordability problems (see below).

#### **4.1.2 Rental housing growth trends**

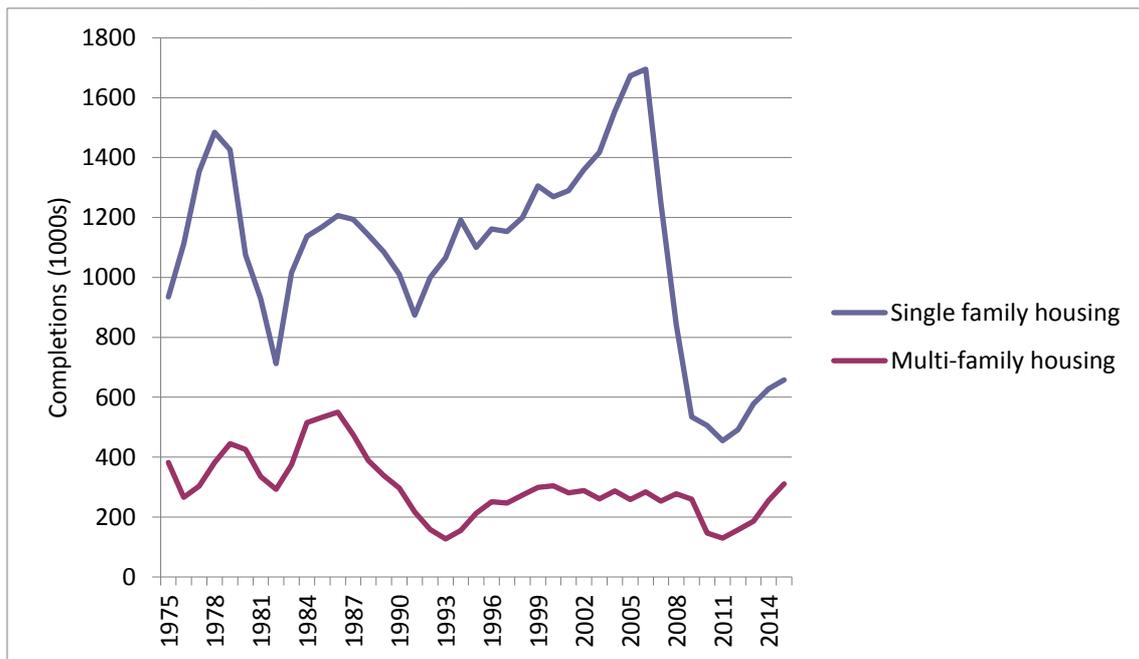
For most of the post-war era the housing market in the US has been dominated by owner-occupancy. Home ownership increased rapidly after the Second World War, reflecting among other things, the availability of federally insured mortgage insurance, and long-term, self-amortising mortgages. Most of the housing built during this period consisted of suburban, single-family homes. Rental housing tended to be concentrated in cities, and saw much less new construction than housing built for owner-occupancy. Single-family construction has always outpaced rental construction, but the latter has been especially depressed since the late 1980s, when the government instituted changes in the tax code (including removal of provisions for negative gearing, similar to those still operating in Australia) that greatly diminished incentives to invest in rental housing. Most rental housing is situated in multi-family buildings, although detached single-family houses has usually accounted for about one-fifth of all rental housing. In general, ownership of rental housing has been widely dispersed. Few owners possessed more than 10 or so units, although some landlords owned much larger portfolios.

From 1995 to 2005, around the peak of the housing bubble, total occupied rental housing declined by about 200,000 units. This was followed by the worst financial crisis since the Great Depression of the 1930s. Rental housing increased by 1.4 million units from 2005 to 2009, and by more than 8.5 million units from 2009 to 2013. Meanwhile, owner-occupied housing, after increasing by nearly 13 million units from 1995 to 2009, dropped by more than 2 million after 2009. The rental sector's share of all occupied housing fell from 35 per cent in 1995 to a low of 31.2 per cent in 2005, but then climbed up to a peak of 37 per cent in 2015. The recent growth

in the percentage of occupied rental housing reflects the concurrent decrease in the home ownership rate, from 68 per cent in 2005 to 62.3 per cent in 2015. In just two years, from 2013, home ownership dropped from 65.3 per cent to 62.9 per cent as the share of rental housing increased from 34.7 to 37.1 per cent (See Table A7).

Most of the growth in rental housing reflects the transfer of previously owner-occupied units to renters. Whereas the total number of renter-occupied units increased by more than 8.5 million units from 2009 to 2015, the number of newly constructed multi-family housing units (not all of which is for renter occupancy), increased by less than 1.5 million units. Indeed, relatively little multi-family housing has been built since the Tax Reform Act of 1986, which greatly reduced financial incentives to invest in market rate multi-family rental housing (Schwartz 2014). As a share of total residential completions, developments with five or more units dropped from 31.3 per cent in 1986 to 19.9 per cent in 1991, and remained at less than 20 per cent until the housing market collapsed in 2008, when completions rose to 24.8 per cent. From 2008 to 2015 multi-family completions have averaged 26 per cent. However, this increase in market share represents the collapse of single-family construction, not a resurgence in multi-family construction. In absolute terms, annual multi-family completions from 1991 to 2007 averaged 244,600 units, exceeding the 2008–2015 average of 215,400. Completions of single-family housing plummeted from an annual average of 1.3 million units from 1991 to 2007 to just 586,700 from 2008 to 2015 (see Figure A8).

**Figure A 8: Housing completions by built form, United States 1975-2015.**



Source: US Census Bureau (2017a).

### 4.1.3 Overview of renter households

Renters differ from home owners in numerous respects. As shown in Table A7, which presents a variety of data from the 2015 American Housing Survey, renters reside far more often in multi-family housing, they are more likely to be from a minority racial or ethnic group, and they have much lower incomes and less wealth than home owners. They are also far more likely to experience housing affordability problems.

**Table A 7: Renter and owner profiles, United States 2015**

	<b>Owners</b>	<b>Renters</b>
<b>Total</b>	<b>76,091</b>	<b>38,816</b>
Moved Into Unit 2010–15	25%	76%
Moved Into Unit 2000-2009	18%	12%
Moved Into Unit Before 2000	41%	7%
Non-Hispanic White	76%	52%
Non-Hispanic Black	9%	20%
Hispanic	10%	19%
Asian	4%	5%
Detached Single Family	83%	29%
Attached Single Family	5%	11%
Multi-family (5 units +)	3%	39%
Median Year Structure Built	1978	1973
Severe Physical Problems	1%	2%
Moderate Physical Problems	3%	7%
Median Age of Householder	56	42
Elderly Householders (65+)	30%	14%
Households with Children Under 18	28%	33%
Married Couple Households	59%	27%
Female-Headed Households	11%	24%
One-person Households	23%	36%
Households with a Disabled Person	22%	22%
Bachelor's Degree or Higher	38%	25%
Citizen of US	96%	88%
Median Housing Cost Burden (% of income)	17%	28%
Spending 30 per cent or more	25%	51%
Spending 50 per cent or more	12%	28%
Median Household Income (\$)	\$65,010	\$32,796
Households in Poverty	9%	26%
Households with low or very low food security among adults	5%	16%
Median Net Wealth in 2010 (thousands \$)	\$174.5	\$5.1

Source: US Census Bureau (2015); Schwartz (2014).

Renters are far more transient than home owners, who also move frequently. More than 75 per cent of all renters in 2015 had been in their current homes for five years or less (i.e. had moved in between 2010 and 2015), compared to 29 per cent of all owners. Conversely, only 7 per cent of all renters had moved into their current unit before 2000 compared to 41 per cent of all home owners. The high rate of residential mobility among renters probably reflects a combination of factors, including their age and their incomes. People tend to move more often when they are young, and people with low incomes experience increased levels of residential instability as a result of difficulty affording their housing costs (Desmond 2016).

In terms of race, about half of all renters are non-Hispanic White, compared to three-quarters of all home owners. The representation of Blacks and Hispanics among renters is double that of

home owners. On the other hand, Asians make up a similar proportion of all renters and home owners.

Renters tend to be younger than home owners. The median renter is 42 years old, compared to a median of 56 for home owners. 14 per cent of all renters are 65 years or older, compared to 30 per cent of all home owners. Renter households are slightly more likely to include children—33 per cent as opposed to 28 per cent of home-owning households. However, renters are far less likely to be married—27 per cent versus 59 per cent, and female-headed households are far more prevalent among renters than owners—24 per cent versus 11 per cent. Single-person households also account for a larger share of renters than of owners. There is no difference, however, in the incidence of disability among renter and owner households, as 22 per cent of both groups include a disabled person. Renters are less likely to have completed college than home owners, and they are slightly less likely to be US citizens.

Renters are far less affluent than home owners. The median annual renter income, less than \$33,000, is less than half the median home owner income. More than 25 per cent of all renters are in poverty compared to less than 10 per cent of all home owners. Similarly, renters are three times more likely to experience food insecurity than home owners. Conversely, home owners are three times more likely than renters to earn more than \$100,000 a year (30% vs. 10%). The disparity between renters and owners is even more extreme regarding wealth. In 2010 (the most recent year for which data were available), the median net worth among home owners, at \$175,500 was 35 times the median for renters, which was only \$5,000.

The American Housing Survey—the source for Table A7—does not separate out data for the private rental sector. However, given the sector's sheer dominance, it is highly unlikely that the demographic and socioeconomic characteristics of its households differ in any meaningful way.

## **4.2 Finance settings and subsidies**

### **4.2.1 The housing crisis and growth in rental housing**

The recent increase in rental housing stems directly from the housing crisis and subsequent recession that began in 2007. During the early and mid-2000s mortgage lending increased sharply. Fuelled by investor demand for ever more complex mortgage-backed securities, mortgage underwriting standards became increasingly lax. Subprime and other high-risk mortgages assumed a growing share of total mortgage originations, as investors and mortgage originators favoured mortgages offering higher yields (Schwartz 2014; Immergluck 2016).

The boom in house selling and mortgage lending was predicated on the assumption that house prices would continue to rise, and that if borrowers could not make their mortgage payments, they could either sell the property or refinance on more favourable terms. However, housing prices reached a peak in 2006 and afterwards fell, sharply in many parts of the country. As a result, a rising wave of home owners who had taken out mortgages on terms they could not afford went into default, often triggering foreclosure. Millions more home owners fell 'underwater', with the value of their homes falling below their total mortgage debt. The confluence of shrinking home prices and rising levels of mortgage default and foreclosure undermined the value of mortgage-backed securities, which in turn wiped out the capital of major financial institutions, including Bear Sterns, Lehman Brothers, AIG, Fannie Mae and Freddie Mac. The ensuing financial crisis triggered the worst recession since the 1930s (Blinder 2013; Immergluck 2015).

The most immediate way by which the housing crisis and subsequent recession caused the rental sector to grow was through mortgage foreclosure and related transactions. From 2007 through 2012, more than eight million home owners lost their homes to foreclosure, short sales, and other related means. Initially, most victims of foreclosure were risky subprime mortgage

holders, but the Great Recession caused millions of people with conventional, lower-interest mortgages to go into default, starting around 2009, due to unemployment and income loss (Immergluck 2015). Although the government instituted several programs to prevent foreclosure, these initiatives fell short of their goals and ended up helping only about two million home owners (Immergluck 2015).

Most households who lost their homes to foreclosure and related causes became renters. Some were able to purchase other homes, or moved in with relatives or friends, but most ended up renting. In some cases, families rented the very homes they had previously owned. Foreclosures probably account for an increase in several million renters since the onset of the housing crisis.

The second way the housing crisis triggered growth in the rental sector is by changes in mortgage lending. Whereas mortgage foreclosures, short sales, and the like displaced millions of home owners into renting, post-crisis changes in mortgage underwriting prevented millions of other households, who would previously have qualified for a mortgage, from acquiring one. Stricter underwriting standards including down-payment requirements, minimum credit scores, and maximum income-to-debt ratios, have made it much more difficult to qualify for mortgages and have thus required people to remain renters. According to the Joint Center for Housing Studies at Harvard University, compared to the early 2000s, there have been no home-purchase loans made to applicants with subprime credit scores (below 620) and a sharp retreat in lending to applicants with scores of 620–600 (Joint Center for Housing Studies 2016: 2). In addition, the slow recovery from the recession following the GFC has caused real incomes to fall or stagnate, further depressing growth in home ownership. For example, inflation-adjusted incomes for 25–34 year olds decreased by 18 per cent from 2000 to 2014 (Joint Center for Housing Studies 2016: 2).

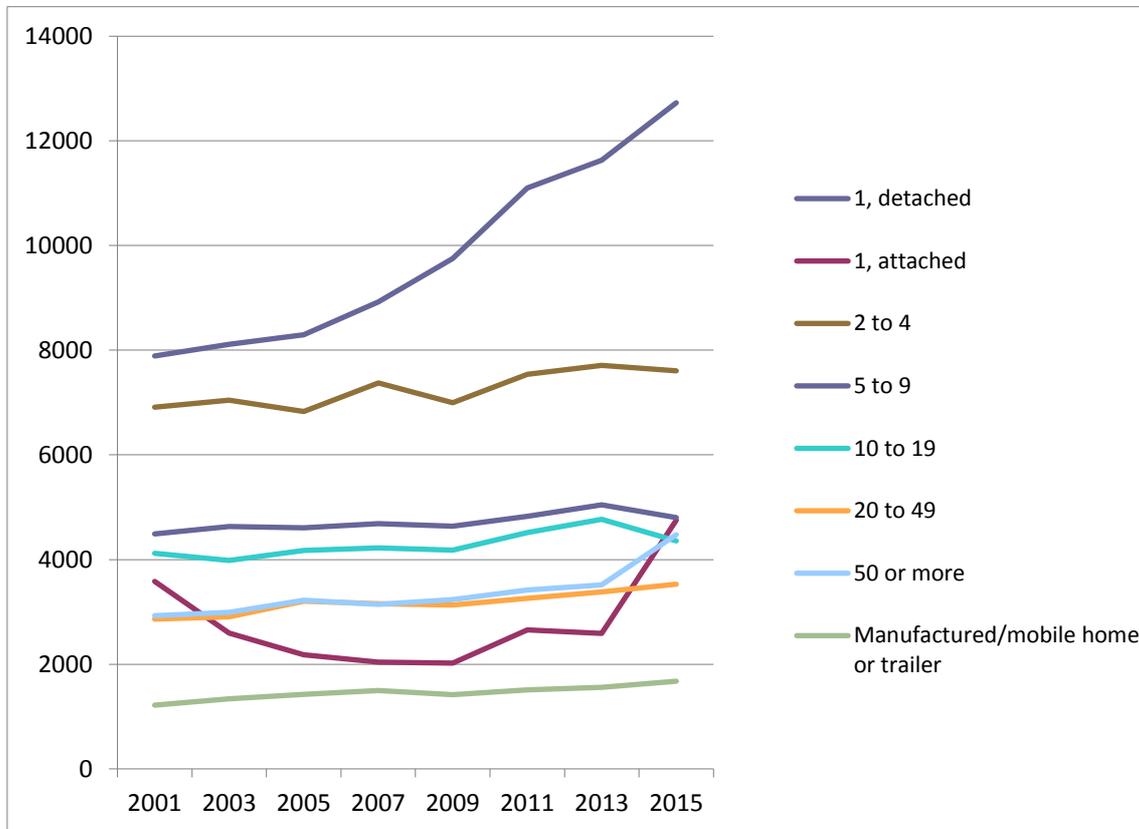
Although the US Government has prohibited the most risky lending practices that characterised the lead up to the housing crash, the underwriting standards adopted by many banks and other mortgage lenders are more restrictive than what is required. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 instituted numerous regulatory changes in the financial system, including, but not limited to, mortgage lending. Dodd-Frank established minimum underwriting standards for mortgages, and prohibited many of the products and practices that contributed to the mortgage crisis. For example, the legislation limits the fees and other expenses than can be charged to borrowers, and requires lenders to base their lending decisions on the borrowers' ability to pay back the loan. Dodd-Frank also established the Consumer Finance Protection Bureau to regulate mortgages and other consumer finance products (see Immergluck 2015 for summary of Dodd-Frank). Prior to the crash, lenders engaged in risk-based pricing, whereby borrowers with higher risk profiles were steered to mortgages with higher interest rates, higher fees, and restrictions on their ability to refinance. In the aftermath of the crisis, lenders often decline credit to borrowers who would previously have qualified for a mortgage product that is now prohibited. Further, lenders have tightened their underwriting standards so that many borrowers who would have qualified for lower-cost mortgages no longer do so.

#### **4.2.2 The growth of single-family rentals**

Most growth in rental housing involves single-family houses. Single-family housing has long been associated with home ownership, especially in suburban communities. More renters have long resided in detached single-family homes than in any other building type. In 2001, for example, 23 per cent of all renters lived in detached single-family houses, followed by 20 per cent in 2–4 family structures. However, as illustrated in Figure A9, detached single-family rentals rose sharply after 2005 while other rental configurations remained more or less flat. Between 2005 and 2015, the total number of detached single-family rentals increased by

56 per cent and attached single-family rentals by 72 per cent. Together, these two types of single-family housing accounted for 70 per cent of the total increase in occupied rental units.

**Figure A 9: Rental housing built form (dwelling units in buildings), United States 2001-2015**



Source: JCHS (2016).

Given that most home owners reside in single-family properties, it follows that most victims of mortgage foreclosure also lived in single-family homes. When they vacated their homes as a result of foreclosure many of these properties became rentals. As will be discussed later, a variety of investors, including some of the largest private equity firms in the US, acquired substantial portfolios of foreclosed properties for rental purposes.

In addition, some of the increase in single-family rentals, especially before the onset of the mortgage crisis, reflected an increase in the acquisition of houses for investment. An increasing share of properties financed with home mortgages were not acquired for owner-occupancy but rather as an investment—for capital gains from the quick sale of the property to another buyer (flipping) or as a rental property (Schwartz 2014).

### 4.2.3 Subsidies

About five million renters in the United States receive deep subsidies that essentially ensure that they pay no more than 30 per cent of their household income on rent. Another 2.1 million renters benefit from 'shallow' subsidies through the LIHTC. An unknown number of additional renters receive shallow subsidies through a variety of state and local programs as well as through various forms of inclusionary zoning whereby jurisdictions require or incentivise developers designating a portion (usually 10–25%) of the units in a new housing development for low or moderate-income households.

There are three basic types of deep subsidy programs. Two, public housing and project-based Section 8, are legacy programs that have produced little net new housing since the early 1980s. Public housing, the nation's oldest low-income housing subsidy program, is owned by local housing authorities. Project-based Section 8 comprises several programs through which the US Government contracts with private and non-profit owners of rental properties to provide rent subsidies for some or all of their units. Nearly 4,000 properties that previously received project-based Section 8 exited the program from 1998 through 2014, often because the owners decided not to renew their Section 8 subsidy contract and converted the property to market-rate occupancy (Finkel, Hanson et al. 2006; Ray, Kim et al. 2015). In 2013, the Government launched a program to transfer public housing developments to the project-based Section 8 program. The conversion makes the property eligible for bank loans and tax credits to finance physical rehabilitation or redevelopment, and enables the property to benefit from a more stable funding stream from Congress (Schwartz 2017). It is important to emphasize that this program, Rental Assistance Demonstration, does not involve an increase in the number of housing units with deep subsidies; it only involves a transfer from one deep-subsidy program to another.

The only deep-subsidy housing program to see substantial increases over the past two decades is the Housing Choice Voucher program. Under this program, housing authorities issue vouchers to low-income households to rent existing housing in the private market. As with public housing and project-based Section 8, voucher holders pay 30 per cent of their income in rent. The Government pays the landlord the difference between the tenant's payment and a payment standard that is keyed to a 'fair market rent' for the metropolitan area. Fair market rents are based on the 40th or 50th percentile of rents of units that have seen a recent change in occupancy<sup>11</sup>. Rents must not exceed the payment standard, and the unit must meet the government's housing quality standards. It is not known how many recipients of Housing Choice Vouchers reside in privately owned housing, but given the dominance of the private rental sector, it must be the great majority<sup>12</sup>.

The LIHTC is now the largest supply-side housing subsidy program in the US. Created in 1987, the program makes housing affordable to low-income households by giving investors tax credits in exchange for investments in low-income housing. Each dollar of tax credit entitles investors to a dollar reduction in their federal income taxes. These investments reduce the amount of debt required to finance a rental housing development, thereby reducing the amount of rent necessary to make the property financially viable. Whereas deep-subsidy programs serve households with extremely low incomes—well below the poverty line—LIHTC targets households with somewhat higher incomes. The maximum household income for eligible tenants is set at 60 per cent of the area median family income (AMI), more than double the average income of most deep-subsidy recipients. Rents must not exceed 30 per cent of 60 per cent of AMI. Unlike public housing and other deep-subsidy programs, if tenant income declines, the rent does not change, forcing residents to pay an increased percentage of their income on rent.

The LIHTC has helped finance more than 2 million housing units since its inception. The program also became more efficient over time. In the early years of the program, housing developers typically received about 40 cents in equity investment for every dollar of tax credit allocated to the property<sup>13</sup>. By the late 1990s they were receiving more than 70 cents per tax-

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<sup>11</sup> Housing Authorities can set the payment standard at between 90 to 110 per cent of the Fair Market Rent, and up to 120 per cent under certain circumstances.

<sup>12</sup> See Schwartz 2014 for more information on the Housing Choice Voucher program.

<sup>13</sup> State Housing Finance Agencies (HFAs) allocate tax credits to projects based on specific criteria they develop. HFAs allocate two types of credits—the most valuable credit is based on 9 per cent of a property's eligible development costs and the amount of this credit that can be allocated is capped by a multiple of the state's

credit dollar, an amount that increased to one dollar or more by 2006. However, the housing crisis, the subsequent near collapse of the banking sector, and the nationalisation of Fannie Mae and Freddie Mac<sup>14</sup>, caused demand for tax credits to plummet. Tax credit prices dropped sharply to about 60 cents per tax credit dollar by 2009, and less in some parts of the country. Many properties languished because they did not attract tax-credit investment, or the investment received was less than the anticipated amount (Schwartz 2014).

The Obama Administration adopted two programs during the crisis years to assist troubled tax-credit properties. It provided additional funds to properties that were stalled because their tax credit investments were inadequate; without additional funds, the amount of debt that would be required would push rents above the maximum allowed. In addition, the administration established an 'exchange' program whereby states could provide funds directly to proposed developments instead of relying on private investors to purchase tax credits.

The market for the LIHTC eventually revived, and by 2013 developers were receiving amounts of equity per tax-credit dollar close to what they received before the crisis. However, the amount investors will pay of tax credits varies geographically. Investors pay the most—often in excess of one dollar per dollar of credit—in the largest cities on the east and west coasts, as well as in Chicago and some other major metropolitan areas. They pay substantially less elsewhere. A key reason for this is that major banks are the dominant investor in the LIHTC, and they invest more heavily in the regions they have a physical presence in, and are evaluated for their compliance with the Community Reinvestment Act. Investor demand for LIHTC tends to be weaker in areas where the top banks do not maintain offices<sup>15</sup>.

The recent election of Donald Trump as President of the US has ushered in a new period of instability in the market for the LIHTC. In the months since his election, the average price paid per tax-credit dollar has dropped from more than \$1 to about 80 cents, and less in some regions (Woellert 2017b). It is reported that an increasing number of projects are unable to close because their tax-credit investments fell short of expectations. Many investors expect President Trump and the Republican-controlled Congress to reduce income tax rates. Should tax rates decline, the tax liability of banks and other investors would likely decline, thus diminishing their appetite for tax credits. It is also possible that Congress could weaken or eliminate the LIHTC as part of a wide-reaching tax reform. The LIHTC has enjoyed bipartisan support, but the possibility of major tax reform makes the status of the LIHTC uncertain.

In addition to the LIHTC, residents in privately owned, for-profit, rental housing also benefit from shallow housing subsidies through inclusionary zoning and other 'mixed-income' schemes. As noted above, inclusionary zoning (also known as inclusionary housing) refers to land use and other regulations that either require or incentivise developers to designate a portion of the units in a new development for low and/or moderate-income households. Often developers are allowed to build at a greater density than would be otherwise allowed or receive other benefits in exchange for providing affordable housing. Inclusionary programs vary widely in terms of the

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population. In 2016 states could allocate an amount totalling \$2.35 per capita times the state's population (or \$2.60 million if greater). The less valuable credit, based on approximately 4 per cent of the eligible development cost is not limited, and can be assigned to any property that also received tax-exempt bond financing (Schwartz 2014).

<sup>14</sup> The federal government took the two institutions into 'conservatorship' in 2007. Previously, that accounted for 40 per cent of all tax-credit investments. These investments came to an abrupt stop when the two companies were nationalised (Schwartz 2014).

<sup>15</sup> The Community Reinvestment Act of 1977 requires depository institutions to serve the communities from which they draw deposits. They are evaluated on the basis of their lending, investment, and service. Investment in LIHTC is one way to earn 'CRA credit' on the investment test. When banks do not draw deposits from an area, they are not subject to CRA evaluation in that area.

percentage of affordable housing allocated; the maximum rents of the affordable units and the maximum income of the tenants; the extent to which affordable units must be integrated with market-rate units or built offsite; the option of paying into a housing trust fund instead of building the affordable housing directly; and the duration of the affordability period (Hickey, Sturtevant et al. 2014; Jacobus 2015). Not all inclusionary zoning programs involve rental housing; many focus exclusively on owner-occupied housing. It is not known how many affordable units have been created by means of inclusionary zoning<sup>16</sup>.

### 4.3 Rental property ownership and management

Most rental properties in the US are owned by individual investors, but larger properties tend to be owned by other entities, such as limited liability partnerships and corporations. Table A8 presents data from the Rental Housing Finance Survey, a survey conducted by the US Census Bureau of rental property owners. It is important to note that the unit of analysis is at the property level, not at the building or unit level. Properties can include multiple buildings, contiguous or not. The data are not weighted by the number of units in each property size category.

**Table A 8: Ownership of rental properties by landlord type and property size, United States 2012.**

Owner Type	Total	Property Size			
		2–4 units	5 to 24	25 to 49	50+
Individual investor	71%	83%	53%	23%	8%
Trustee for estate	5%	4%	9%	4%	1%
Limited Liability Partnership (LLP)	4%	2%	4%	25%	27%
Limited Liability Company (LLC)	10%	5%	19%	32%	38%
Tenant in common	1%	1%	1%	0%	1%
General partnership	1%	1%	1%	2%	4%
Real Estate Investment Trust (REIT)	1%	1%	1%	0%	3%
Life insurance company	0%	0%	0%	0%	0%
Other financial institution	1%	1%	0%	0%	1%
Pension fund or retirement fund	0%	0%	0%	0%	0%
Real estate corporation	1%	0%	4%	2%	1%
Other corporation	0%	0%	2%	5%	4%
Housing cooperative organization	0%	0%	1%	0%	0%
Non-profit organization	2%	1%	3%	7%	11%
Other	1%	1%	0%	2%	1%
Total	100%	100%	100%	100%	100%
N (total Properties in 000s)	1,995	1,417	438	57	79

Source: US Census Bureau (2014).

<sup>16</sup> See Jacobus (2015) for an excellent overview of inclusionary zoning.

Overall, Table A8 shows that 71 per cent of 2 million rental properties in 2012 were under individual ownership. Limited Liability Partnerships and Corporations<sup>17</sup> together accounted for an additional 14 per cent, followed by trustees for estates at 5 per cent. Non-profit organisations accounted for 2 per cent of all rental properties. The incidence of individual ownership is inversely related to property size. Individuals own 83 per cent of all properties with 2 to 4 units, 53 per cent of properties with 4 to 24 units, 23 per cent of properties with 25 to 49 units, and 8 per cent of those with 50 or more units. Conversely, the share of properties owned by limited liability partnerships and corporations increases from 7 per cent for 2 to 4 unit properties to 65 per cent of properties with 50 or more units. The table also shows that the share of properties owned by non-profit organisations increases with property size, from 1 per cent of all 1 to 4 unit properties to 11 per cent of all 50+ unit properties.

The Rental Housing Finance Survey began in 2012 (it was also conducted in 2015, but the results were not available at the time of writing). It replaces the Residential Housing Finance Survey, which focused only on mortgaged properties, both owner-occupied and rental. The latter survey is not directly comparable to the Rental Housing Finance Survey, making it impossible to show change in the number of properties over time by category. However, we can use both surveys to examine changes in the proportion of mortgaged properties under individual ownership from 2001 to 2012 (the last year of the Residential Housing Finance Survey and the first year of the Rental Housing Finance Survey). Rental properties with 2 to 4 units remained overwhelmingly under individual ownership, dropping from 86 to 84 per cent over the 2001–12 period. However, individual ownership decreased from 59 to 51 per cent of all properties with 5 to 49 units, and from 12 to 7 per cent of properties with 50 or more units. Unfortunately, changes in ownership categories used in the two surveys makes it impossible to compare changes in the incidence of most other types of ownership—including limited liability corporations and partnerships.

### **4.3.1 The emergence of large-scale owners of single-family rentals**

The Rental Housing Finance Survey does not reflect the most recent change in rental housing ownership: the rapid emergence of private equity and other corporate owners of large portfolios of single-family rental housing<sup>18</sup>. Single-family housing has always been a major portion of the rental housing stock. Single-family rentals had typically been owned by ‘mom and pop’ investors—individuals and families owning one to 20 or so houses for rent (Immergluck and Law 2014; Dill 2012). However, in the wake of the mortgage foreclosure crisis several institutional investors, among them Blackstone and other private-equity firms, acquired thousands of houses at deeply discounted prices to rent them out. They frequently acquired foreclosed properties at steep discounts in bulk sales from banks and other lenders, as well as from Fannie Mae and Freddie Mac. From the spring of 2012 to the spring of 2014 these firms had invested more than \$20 billion to acquire about 200,000 homes to rent. The Blackstone Group alone spent more than \$8 billion in this period to acquire 43,000 homes in 14 metro areas (Gittlelsohn and Perlberg 2014). At one point in 2013 Blackstone was spending \$100 million every week to acquire single-family houses (Gittlelsohn and Perlberg 2014). Blackstone has also acquired a large portfolio of foreclosed properties from Fannie Mae—an issue of some controversy (Woellert 2017a). As of 2016, the seven largest institutional investors owned nearly 170,000

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<sup>17</sup> Limited liability corporations (LLC) are similar to partnerships and sole proprietorships in that income from their holdings flow to owners and are subject only to personal income tax. LLCs differ from partnerships in that stock holders are not personally liable for their debts and liabilities. Individual investors often form LLCs to shield their identities.

<sup>18</sup> The property-level scale of the Rental Housing Finance Survey makes it impossible to discern the number of single-family units contained within a property (e.g. hundreds of single-family units may belong to the same property).

single-family homes. These units account for less than 1 per cent of all single-family rentals as of 2015, but the number of such units has grown exceptionally rapidly. Several of the largest institutional investors have issued bonds and other securities backed by their single-family portfolios, generating billions in proceeds (Raymond 2014; Fields, Kohli et al. 2016).

Private-equity and other institutional investors have been particularly active in areas that were hit hard by the foreclosure crisis. However, they have invested far more heavily in some of these regions than in others, favouring 'Sunbelt' locations over the 'rustbelt'. Their portfolios of single-family rentals are largest in metropolitan areas such as Phoenix, Atlanta, Dallas, Houston, Los Angeles, Orlando and Tampa (Fields, Kohli et al. 2016; Davidson 2013). On the other hand, they have acquired far less single-family housing in New Jersey, Ohio and Michigan (Fields, Kohli et al. 2016). It appears that institutional investors favour housing in growing regions where the prospects of home price appreciation are strongest.

The long-term intentions of the institutional investors in single-family housing are not clear. Nor is it clear that these investors will continue to acquire properties if home prices continue to increase. The total financial return for the institutional investors is predicated on a combination of rental income and appreciation (i.e. capital gains from the sales of the property). Once home prices reach a certain level it may be advantageous for investors to sell their holdings. Moreover, the bonds that several institutional investors have issued backed by their portfolios of single-family housing are 'driven by the value of the underlying collateral and not by rental income' (Raymond 2014). In other words, investors are at least as interested in capital appreciation as in rental income<sup>19</sup>.

### 4.3.2 Property management

Overall, 74 per cent of all rental properties with 2 or more units are managed by the owner or an unpaid agent of the owner. However, larger properties tend to be managed by paid agents or management companies. The Rental Housing Finance Survey for 2012 shows that while 88 per cent of properties with more than 49 units are managed by paid agents or management companies, the same is true for just 13 per cent of all 2–4 unit properties and 32 per cent of all 5–24 unit properties.

Conversely, 83 per cent of all 2–4 unit properties are managed by the owner or by an unpaid agent, as are 64 per cent of all 5–24 unit properties.

## 4.4 Regulation

Rental housing in the US is regulated mostly at the state and local level, with some federal-level regulation in specific policy areas. For the most part states give landlords considerable leeway in setting rents, selecting tenants, and choosing whether or not to renew leases. Most regulations apply to narrow aspects of landlord–tenant transactions. Megan Hatch (2017), identified 22 most common landlord–tenant laws among the 50 states, and put them in the following under four categories:

- prices
- health and safety

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<sup>19</sup> If the single-family portfolios of institutional investors correlate with trends in the overall stock of single-family rental housing, it's possible that institutional acquisitions of single-family housing may have peaked. According to the Joint Center for Housing Studies, annual growth in the number of occupied single-family rental housing was greatest in 2012, and the number of such units declined slightly in 2015 (Joint Center for Housing Studies 2017: 26–27).

- rental unit possession
- anti-discrimination.

#### 4.4.1 Price regulation

Very few states and localities currently regulate the amount of rent that landlords can charge. Rent regulation was widespread throughout much of the country during and immediately after the Second World War, as it was throughout most of Europe. Governments imposed strict controls on rents to prevent landlords from taking advantage of war-time housing shortages and charging excessive rents. Most states and cities phased out this 'first generation' of rent control by the early 1960s. A second, less stringent, form of rent regulations was adopted in a number of places during the inflationary years of the 1970s. These ordinances generally allowed for larger rent increases than was the case before, and they often permitted landlords to charge higher rent increases during a change of tenancy, or in some cases allow rents to reset at market levels. However, most jurisdictions eliminated rent regulation by the late 1990s and 30 states prohibit local governments from instituting any form of rent regulation (Keating and Kahn 2001; Keating, Teitz et al. 1998). At present, rent regulation remains in effect in New York City and other cities in New York state, in New Jersey, Washington, DC, and in a few communities in California.

New York City has had rent regulation in place since World War 2, and it is authorised by state law to continue as long as the city's rental vacancy rate remains under 5 per cent. As of 2014, more than one million rental units were rent-regulated, constituting 49 per cent of the city's rental housing stock, and 56 per cent of all unsubsidised housing (US Census Bureau 2017b). Under the city's principal rent regulation program, the Rent Guidelines Board (consisting of nine members appointed by the Mayor) determines the maximum allowable rent increase (in percentage terms) for a one or two-year lease. It also sets the maximum increase landlords can charge when there is a change in occupancy. The system also allows landlords to increase rents to cover certain capital improvements.

In 1993 state legislature amended the rent stabilisation program to allow for 'luxury decontrol'. When vacant regulated rents reach a designated threshold (currently \$2,700 per month), the unit is no longer subject to rent stabilisation and the owner is free to charge whatever rent the market will bear. The state also permits units to be deregulated when landlords can show that a tenant's income surpasses a minimum threshold (currently \$200,000) in two consecutive years and the rent also exceeds a minimum amount (currently \$2,700 per month). As a result of these and other forms of deregulation, the number of rent-stabilised housing units has fallen by more than 151,000 units from 1994 to 2015 (New York City Rent Guidelines Board 2016)<sup>20</sup>.

Other than rent regulation, the other forms of state and local regulations that affect pricing issues are security deposits required by landlords (the amount that can be charged, the interest that landlords must pay, the maximum time to return the deposit to the tenant); the landlords' obligation, if any, to renew a lease to a sitting tenant; the amount of advance notification, if any, that is required for rent increases; the minimum amount of time after the rent is due that a tenant must pay the rent before he/she is in default (and be subject to eviction) and/or must pay a late fee; and late fees landlords may charge tenants who fail to pay rent on time. The incidence of these forms of regulation varies widely across states, with the most common being rent default time and security deposit return time (Hatch 2017: 105).

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<sup>20</sup> See Keating, Teitz et al. (1998) for more information on rent regulation.

#### **4.4.2 Health and safety**

Many states have laws designed to protect the health and safety of renters. All but six states provide a 'warranty of habitability' for renters. This means that landlords must 'maintain the premises and keep it in compliance with health and safety codes' (Hatch 2017: 118; Bryson 2006). States and localities, however, vary widely in the extent to which they enforce this warranty, and in the remedies allowed to address violations of it. For example, some jurisdictions permit tenants to withhold rent if the landlord fails to address a health or safety violations after proper notice; others allow renters to fix the problem themselves and deduct the costs from the rent. Jurisdictions may also enable landlords to charge tenants for the costs of addressing health and safety concerns. Another type of health and safety regulation adopted in some states is a prohibition against shutting off heat, water, and/or electricity if a tenant has violated the lease or failed to pay rent on time.

#### **4.4.3 Rental unit possession**

This category of regulation pertains to a tenant's right to occupy a unit at the start of the lease, and his/her right to privacy. If a unit is not ready for occupancy at the start of the lease, states may require landlords to provide monetary compensation to tenants. Tenants are also entitled to what is often termed 'quiet enjoyment' of the unit, meaning a minimum degree of privacy. States may require landlords to give the tenant 'reasonable' advance notice before entering the unit. Finally, some states may specify a 'default length' of a lease if the duration of the lease isn't specified (Hatch 2017).

#### **4.4.4 Anti-discrimination**

Federal law prohibits landlords from discriminating against potential and current tenants on the basis of their race, ethnicity, and disability. The Fair Housing Act of 1968 and its Amendments of 1988 outlaw discriminatory practices throughout the housing market, including the private rental sector (Schwartz 2014). In addition, some states have adopted statutes prohibiting discrimination on the basis of sexual preference, marital status, and other characteristics. Some states and localities also prohibit landlords from discriminating against applicants with rental vouchers or other forms of public assistance ('source of income discrimination') (Hatch 2017; Freeman and Li 2013). Some states also ban retaliatory actions on the part of landlords (evictions, rent increases, harassment) against tenants for complaining about health and safety violations or other concerns (Hatch 2017).

Hatch found that the number of landlord-tenant policies in force per state varies from 4 to 19, with a mean of 12. The most common regulations concern rent default times (96% of the states), security deposit return time (94%) and warranty of habitability (88%). The laws least often adopted by states include rent grace period (16%), quiet enjoyment (18%) and source of income non-discrimination (24%). She conducted a cluster analysis of the regulations in place in the 50 states and identified three groupings of states based on their approaches to landlord-tenant policy. She found that 13 states adopted 'protectionist' policies with 'implicit' pro-renter policies. Conversely 17 states exhibit 'pro-business landlord-tenant policies.' These states are less likely to adopt any landlord-tenant laws at all than other states, and when they do adopt them, the laws tend to favour landlords. The third cluster consists of 20 states with 'contradictory' policies with a combination of pro-renter and pro-landlord laws. Hatch found that these states 'are likely to legislate health and safety and rental units possession in favor of renters while demonstrating no pattern in regulation of prices or prohibition of discrimination' (Hatch 2017: 111).

## 4.5 Conclusion

More than one-third of all households in the US currently reside in rental housing, and the number of renters has increased sharply in the wake of the housing crisis. This report has documented the recent growth of the rental sector, in particular the rapid increase in rented single-family housing as a consequence of the housing crisis. It also described the ownership of rental housing and the prevalence of private, for-profit owners. Public housing and rental housing owned by non-profit organisations account for just 5 per cent of all rental housing. Individuals are the dominant owner for small rental properties while other ownership forms, mainly limited liability partnerships and corporations, are more prevalent for larger properties. Recently, private equity firms and other ventures have acquired large portfolios of single-family properties for rent.

The report also shows that the vast majority of renters receive no subsidy from the government to help cover their housing costs. Deep subsidies that limit housing cost burden to around 30 per cent apply to only about 11 per cent of all rental housing. The LIHTC accounts for about five per cent more.

Compared to home owners, renters have far less income and less wealth. They are far more likely to confront severe housing-cost burdens, paying 50 per cent or more of their income on rent. Renters are more likely to be from minority racial or ethnic groups than home owners, tend to be younger, and are less likely to be married. Renters also tend to be far more mobile than owners, seldom remaining in their residence for more than five years.

Rental housing is regulated at the state and local level, and states vary widely in the extent of such regulation. Only a few places, most notably New York City, regulate the rents that can be charged to tenants. Most states require that rental housing comply with health and safety codes, but they vary in how they enforce these regulations, especially in the ability of tenants to hold landlords accountable.

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## Appendix 5: 10-country survey instrument

### *The Changing Institutions of Private Rental Housing: An International Review – 10-country survey*

The City Futures Research Centre at the University of New South Wales, Australia, is conducting an international review of changes in the institutions of private rental housing. The international review is part of an Inquiry, funded by the Australian Housing and Urban Research Institute (AHURI), into the future of private rental housing.

As part of the international review, we are inviting experts from 10 selected countries to participate in a survey about institutional changes in the private rental sector (PRS) of their respective countries.

We would be very grateful if you, as an expert on the PRS in your country, would participate in the survey.

The survey is open until **30 October 2016**. Participation is voluntary and without reward. You may decline to participate without detriment to your existing or future relations with City Futures and the University of New South Wales. If you are unable to contribute we would be grateful for your recommendation as to an alternative expert for your country, so that we may contact them.

Information provided by country experts will be used in a report of the review to be published by AHURI, with participants acknowledged, with our gratitude, by name in the report.

Some key concepts of the survey are discussed below.

#### **'Institutions'**

In this review we define **'institutions'** broadly as 'systems of established and prevalent social rules'—so the institutions you refer to may include laws, policies, cultural norms, organisations and patterns of practice by individual persons. For example, the small-holding individual landlords prevalent in the Australian PRS are, collectively, an 'institution'.

#### **'Change'**

We are particularly interested in **changes** in institutions. The changes you refer to may be driven by government, the market or broader social trends; or driven internally by institutions. Changes may be radical, or marginal – so long as you think the change is important to the system.

We will need to put any change into perspective, so we also ask that you indicate the **base or starting point** from which the change is occurring, and the **timeframe** of the change. We are focusing on current and recent change (roughly the past 10 years), but you may refer to longer-term developments if you think they are important.

#### **'Private rental housing'**

We consider 'private rental housing' to be, primarily, rental housing provided on market terms by individual persons and corporations. However, we are conscious that 'private rental housing' so defined may itself be a changing institution, and are interested in developments that challenge the definition (for example, for-profit landlords who allocate tenancies according to non-market eligibility criteria and charge sub-market rents according to the terms of an affordable housing program; and social housing landlords who also manage some tenancies on market terms).

If you have any queries about this invitation or the research project, please do not hesitate to contact me by email: [c.martin@unsw.edu.au](mailto:c.martin@unsw.edu.au)

Thank you

Yours sincerely

Dr Chris Martin

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