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# Rent Regulation: The Balance between Private Landlords and Tenants in Six European Countries

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**ABSTRACT** *The private rental sector has been declining in many European countries. In describing the decline of the private rental sector, it is often suggested that a causal relationship exists between the decrease in private renting and rent control. The assumption is that the stricter the form of rent control, the greater the decrease in private renting levels. Or, conversely, that with fewer rent controls there are more opportunities for the private rental sector. At the same time, however, an unregulated rental market may result in insecurity for tenants.*

*This text focuses on conflicts of interest between private landlords and tenants in the regulation of rents, from a welfare economics viewpoint. We present the results of a comparative study that involves France, England, Germany, Spain, Sweden and the Netherlands. We describe the system of rent regulation in each country. We conclude that the balance achieved between landlords and tenants as a result of rent regulation may not be as clear-cut as it is often presented to be.*

**KEY WORDS:** Comparative housing research, private rental sector, rent control, rent regulation, tenant security

## **Introduction**

The development of the private rental sector and the way in which rents are regulated appear to correlate. Strong rent regulation is said to discourage investment and to produce a shrinking private rental sector. Indeed, strong rent regulation was common in many countries, in particular in the period from World War I until after World War II (Van der Heijden & Boelhouwer, 1996). The shrinking of the private rental sector, especially in the period after World War II, has also been ascribed to rent control.

Meanwhile, the private rental sector has appeared on the policy agendas in many countries. The background for this new focus could be the fact that a choice between

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social renting and home ownership is considered to be a limited choice. The goal of furthering private initiative may also play a role. It may also be the case that it is hard for young people to become home owners because of affordability problems, and governments regard the private rental sector as a good alternative to social housing, and one which is less costly. Various instruments have been considered to encourage investors to invest in private rental housing and to prevent private landlords from leaving the private rental sector. Rent deregulation is often part of this policy package. Rent deregulation means less protection for the tenant and it may also mean more return on investment for landlords. The resulting balance between the interests of the landlord and the tenant in the private rental sector depends greatly on the alternatives for landlords – returns on other investments – and for the tenants – other housing tenures.

The focus in this paper is the balance between tenant and landlord in the private rental sector,<sup>1</sup> analysed from a theoretical welfare framework. We use a qualitative analysis to explore how this balance can be characterized in the rent regulation systems in six European countries.<sup>2</sup> To that end, we will present reasons for rent regulation in the next section. The third section discusses a typology of rent regulation. The fourth section introduces the six countries – England, France, Germany, Spain, Sweden and the Netherlands. The fifth section contains the comparison across the countries. The last section presents the paper's conclusion.

### **Reasons for Rent Regulation**

According to welfare economics, the most important reason for intervening in a market is efficiency; intervention is justified if economic efficiency is improved (Barr, 1998; Vandembroucke *et al.*, 2007; Haffner & Boelhouwer, 2006; Doms *et al.*, 2001). If a market operates efficiently, according to this approach, society's total welfare will be maximized. The resulting distribution of welfare in such a situation, however, does not need to be such that society or politicians are comfortable with it. According to the welfare economics, improving social equality between citizens is a second legitimate reason for the government to intervene in a market and to change the welfare distribution. Arnott (1995), however, finds that the emphasis of traditional advocates of rent controls on distributional concerns has little merit, because of the poor targeting of the redistribution in comparison to other instruments. Even though rent control generally may not greatly improve social equality, there are a few examples of rent control that can be considered to do just that: the income-linked (or differential) rents in the social rental sector as applied in Belgium and Ireland.

Nevertheless, this paper does not focus on rent regulation for reasons of distribution, but on rent regulation for reasons of efficiency. Economic efficiency can only be achieved if four standard criteria are met: perfect information, perfect competition, complete markets and no market failures (Barr, 1998). If these criteria are not met, the government can improve economic efficiency by other means: regulation, for example, or subsidies.

Conditions for perfect information are not generally met in the rental sector. Information asymmetry will exist if the landlord has a greater insight than the tenant into the quality of the accommodation and any possible defects; thus the price–quality ratio of the dwelling. When the dwelling stock is heterogeneous, the landlord’s knowledge advantage will even be more important. Rent regulation can play a role in reducing this asymmetry by linking a specific quality to a maximum rent.

The criterion of perfect competition, requiring that all players have equal power, is also often not met in the rental market. If the accommodation acquires the status of a home for a tenant and the tenant becomes attached to his home, the landlord acquires a monopolistic power to raise the rent. Indeed, the tenant must incur high financial and emotional costs to move and thus avoid the rent increase. Arnott (1995) refers here to so-called imperfectly competitive models. The landlord acquires greater market power, because tenants facing high search costs will more readily accept a rent that is higher than the market rent.

In this line of reasoning any system of rent regulation is set up for the protection of the tenant, either from arguments of information asymmetry or imperfect competition. The tenant’s advantage may turn out to be a disadvantage for the landlord. If rent regulation is strong, return on investment will decrease and in the long run the landlords might exit the private rental market. No new landlords will enter the market. Therefore, the regulation of rents will be a search for a balance of interests between the tenants and the landlords.

### **Typologies of Rent Regulation**

Arnott introduced two types of rent control in his seminal article of 1995. He called the freeze on nominal rents ‘hard’ or ‘first-generation’ rent control, and used the terms ‘soft’ or ‘second-generation’ rent control to designate regulation that usually permits an automatic rent increase percentage related to the inflation rate. The possible undesired (long-term) effects of rent control, such as falling property values, benefiting insiders, reducing maintenance, creating excess demand for regulated housing, reducing housing and labour mobility, and increasing discrimination against disfavoured groups that are associated with first-generation rent control systems, may not necessarily be associated with second-generation rent control systems. Based on monopolistically competitive models where landlords have more market power than tenants, Arnott argues that rent control may be able to improve the equilibrium of an imperfect market: ‘Rent control is then desirable when the distortion is the unavailability of insurance against a sharp and unanticipated rise in rent’ (p. 108). As the rent control systems are heterogeneous, it may be impossible to generalize about their effects, he warns.

From an overview of empirical evidence on the costs and benefits of rent control, Turner and Malpezzi (2003) conclude that the effects of rent regulation vary greatly among countries and regions, depending on the specific housing market situation. In

general, second-generation rent regulation models seem to perform better than first-generation models. However, systematic comparative research on the effects of rent regulation is relatively scarce (see also Arnott, 1995); most of the studies reviewed by Turner and Malpezzi were case studies of a single housing market. This makes it difficult to draw general conclusions.

#### *Lind's typology*

Lind (2001) draws a distinction between five different types of second-generation rent control. In his typology, Lind interweaves the reasons for imperfect competition and/or asymmetric information to justify government interventions in the housing market.

First, Lind distinguishes rent regulation based on high transaction costs for the tenant. In this example of market imperfection the landlord can impose a higher rent than the market rent (that which would be charged to a new tenant) on the sitting tenant. Lind designates protection against this increase as the 'weak' rent regulation based on transaction costs (type A).

Lind indicates the rent control as 'strong' if the rent regulation for the sitting tenant is limited, not to the market rent but to a cost price increase including a reasonable return or yield (type B). This type of regulation therefore refers to a more stringent regulation which is not calculated from the market rent, but from a specific return for the landlord.

The third form of rent control distinguished by Lind is the regulation of all types of contracts where the cost price and a reasonable return form the reference points (type C). Such regulation can be applied if one pursues the objective of avoiding segregation. In fact, all households will then be able to rent accommodation in an attractive location, assuming that there are negative external effects of segregated neighbourhoods. According to Lind, of all the types of regulation, type C comes the closest to first-generation rent control. Everyone can rent at a price below the market rent, and market effects are never considered in determining rents.

The fourth type of rent regulation is monopoly-related rent control (type D). All tenants are protected against a rent that is higher than the market rent. The aim of this type of regulation is to prevent landlords from using their monopoly position in heterogeneous housing stock. Lind indicates that this type of regulation does not demand strict rent regulation by definition, but that prohibiting extortionate rents, for example through the penal code, may be sufficient.

The final type of rent regulation is aimed at limiting the short-term price effect (overshooting), which arises from an increase in demand for rental accommodation in a situation where there is an inelastic supply of rental dwellings (type E). The intention is that the long-term market rents are followed by this type of regulation, which should protect against peaks in market rent.

Lind's observations do not entirely match the theoretical welfare arguments mentioned earlier. For instance, he splits up some of the arguments, as when he separates

**Table 1.** Characterizing rent regulation, using Lind's typology

	Not higher than cost-price rent	Not higher than market rent
Sitting tenants	B	A
All tenants	C	D+E

*Source:* authors' adaptation of Lind (2001).

the transaction cost motive from the monopolistic motive for regulation. What is notable, furthermore, is that Lind names overshooting as a reason for rent regulation, whereas Barr (1998) indicates that volatility is intrinsic to the market and should not be regarded as a market failure. When Lind indicates that the type C rent control comes closest to a first-generation regulation, he implicitly assumes that cost-price rent is lower by definition than market rent.

#### *Observations*

Lind makes it clear that two criteria are crucial for characterising types of rent regulation (see Table 1):

- To whom does the regulation apply? To all tenants or only to sitting tenants?
- What is the basis for regulation? Cost-price rent or market rent?

These criteria will now be discussed, mainly from the point of view of advantages for the tenant. This section ends with some possible advantages of rent regulation for the landlord.

#### *Sitting tenants or all tenants*

The selection of the sitting tenant instead of all tenants will often be made from the standpoint that sitting tenants may not be able to bear sudden rent changes, when there is no way to insure them. Because they must incur high costs to relocate it seems reasonable to protect sitting tenants (type A and B). However, when the regulation leads to rents being lower than the market rent, what arises is protection of insiders (sitting tenants) at the expense of outsiders (new tenants). Such an argument can play a role in the choice to protect all tenants against rents that are too high (types C, D and E). Rent regulation will only have an effect if the tenant's rent protection is also arranged (tenant security). If the rental contracts are short-term or the tenant enjoys no rent protection, a certain degree of rent regulation will not provide the tenant with sufficient protection. Indeed, if rent regulation does not follow the market rents, in such a situation the landlord could evict the tenant in order to take in a tenant who will pay the market rent.

#### *Market or cost-price rent*

As market rent and cost-price rent will usually differ from each other, the selection of one of these concepts is an important choice. The degree to which cost-price rent regulation is limiting depends on the way in which the cost price is calculated. If a low yield or return is assumed when determining the cost price, then it is relatively unattractive for investors to invest in the private rental sector. When the cost-price rent is lower than the market rent, types B and C offer the most protection for the tenant and thus the greatest yield limitation for the landlord. Cost-price rent is not lower than the market rent by definition. There could be a temporary cost-price rent that is higher than the market rent, for example in a housing market in which the supply of dwellings exceeds the demand for dwellings. In that case a tenant would probably prefer a market rent-related rent regulation to a cost price-related one.

#### *Protection of the landlord*

The effects of protecting the tenant may not only be negative for the landlord – they may also be positive. If controlled rents ensure that the tenant knows what he is dealing with, the tenant is less likely to relocate and the landlord's transaction costs will decrease: fewer switchover maintenance costs, fewer search costs and fewer vacancy costs. Rent regulation may have a function only if tenant transaction costs are higher than landlord transaction costs.

Limiting relocation costs is known as 'turnover minimizing' and in practice appears to occur as an important strategy for optimal returns on the investment of smaller landlords in particular (Turner & Malpezzi, 2003). In relation to this, there may be a 'length of tenure discount' for faithful tenants (Kemp, 2004). In other words, both the tenant and the landlord benefit from a long occupancy and tenant security. Rent regulation can contribute to this but it is not necessary for such a balance. After all, the landlord himself can opt for a reasonable rent increase.

### **Rent Regulation in Six Countries**

In this section we describe the rent regulation schemes implemented in the Netherlands, France, Spain, England, Germany and Sweden. These countries were chosen because of differences in the size and features of the private rental sector: Germany for the large size of its private rental sector, France and Sweden for the medium size of their private rental sectors, Sweden for its negotiations in setting rents, Spain and England for the attention policy makers have given to encouraging the private rental sector, and the Netherlands for the relatively large share of institutional investors in its private rental sector.

The development of the share of the private rental sector in recent decades has been different among the countries studied. In the Netherlands, Spain and England

**Table 2.** Development of shares (per cent) of the private rental sector

	Share in 1950	Share early this century	Growth?
Germany	48, Western Germany	56, reunited Germany	Yes
France	44 in 1955	22	Stable since 1988
Netherlands	60 in 1947	11	No
Spain	55	11	No
Sweden	52	17	No
England	53	10*	Yes, from 9 per cent in 1990

*Note:*\* 12 per cent for 2005/2006 (provisional results, The Department for Communities and Local Government, 2006).

*Sources:* Around 1950: Van der Heijden & Boelhouwer (1996), except Spain; Sweden estimate from early this century: Karlberg & Victorin (2004); other information based on Elsinga *et al.* (2007).

the private rental sector decreased from over 50 per cent to around 10 per cent of housing stock from around 1950 until into this century (see Table 2); in Spain and England this decrease was compensated for mainly by home ownership, while in the Netherlands the social rental sector became an alternative for the private rental sector.

In the other three countries the share either stabilized or increased. Germany stands out because of its very large private rental sector, which has grown in recent decades, in part because of the temporary bricks and mortar subsidy system (Kirchner, 2007) and because of re-unification with East Germany. The rental sector in the former East Germany with a market share of 74 per cent (Haffner, 1998) was labelled private rental after reunification. In France the share of the private rental sector decreased significantly after 1947 but has been stable since the second half of the 1980s because of special financial and/or fiscal concessions to produce intermediary rental housing. In England the private rental sector has increased very recently. Rent deregulation in combination with the increase in the buy-to-let properties has contributed to the present stabilization of the market share of private rent.

The country descriptions, which are about the formal systems of rent regulation, follow the main criteria derived from Lind's classification: at which tenants (all or sitting) is the rent regulation aimed and which basis for rent regulation is used (cost price or market rent)? In the next section the countries are compared based on these aspects.

### *The Netherlands*

All rents in the rental sector have been regulated since World War II. In 1989 an important change occurred in Dutch rent regulation. From that time, rent regulation



no longer applied to new contracts for dwellings with a rent that was higher than the so-called liberalization threshold. Dwellings in the social and the private rental market with a rent higher than €615.01 (in 2006) fall within the so-called liberalized area and are exempt from rent regulation. Liberalized accommodation comprises 5 per cent of total rental housing stock.

The current rent regulation encompasses a maximum rent for each vacant dwelling and a maximum annual rent increase. The *maximum rent* for a dwelling is based on what are known as 'quality points'. The points system provides a picture of housing quality. To a degree it involves the objective characteristics of a home: the surface area and the home's facilities. A rental committee establishes the number of points for a dwelling's environment, such as the presence of facilities (shops, public transport, schools, etc.).

Next to the maximum rent level per dwelling based on the quality points, there is also a *maximum average rent increase* for social landlords, not for commercial landlords; thus for social landlords the rent regulation is more strict. For the total rent increase in the social rental sector (say for all dwellings per landlord) the average rent increase is maximized. This maximum is lower than the maximum rent increase allowed per dwelling.

Within the limits of rent regulation, landlords have freedom in setting their rents and rent increases. Some of them set the rents at the maximum that regulation allows while others chose to set the rents at a lower level. Rents in the social rental sector on average are well below the maximum rent: 70 per cent of the maximum rent allowed for a dwelling (Ministerie van VROM, 2003). This illustrates the shared responsibility between government and social rental sector for the affordability of rental housing. Commercial landlords' rents on average are 83 per cent of the maximum rent.

The maximum annual rent increase is the subject of political decision making. In recent years it has been set at the rate of inflation plus a specific percentage. After years of stormy discussion about making rent regulation more flexible, in 2007 it was decided to implement a maximum rent increase of 1.1 per cent (= inflation). Instead of more flexibility, the result has been less flexibility.

### *Sweden*

Rent regulation in Sweden changed from a cost-based system to a 'use-value-system' in the 1970s (Lind, 2001). Landlords were to charge new and sitting tenants rents that were not to be higher than the long-run equilibrium rent. The system was adapted stepwise into the current system, where rents in the non-profit sector (municipal housing sector) are taken as the lead. Rents in the private rental sector should be set no higher than five per cent above rents for similar apartments in the municipal sector (Atterhög & Lind, 2004). Rents may be set lower than those in comparable municipal apartments, if that is required by market conditions. But in general, rent regulation affects all tenants in the rental sector.

Rents in the non-profit sector are set as a result of bargaining between the local tenants' union and the municipal housing company. They are still mostly based on cost increases. Municipal housing companies are not required to make a profit, although a local government providing some funds to the municipal housing company may require a 'normal' rate of return. How the rent increase is to be divided across estates is determined in the bargaining process. Changing all rents proportionally is one option, increasing rents more in attractive areas than in unattractive areas is another.

The Swedish system of rent control might seem to make it difficult for private landlords to make a profit. Turner *et al.* (1992) argue that tenants with a short-term perspective may choose lower rents instead of more maintenance. Also, a municipal housing company is in the position to misuse its leading position and to try to set rents strategically, when there is competition from private landlords (Turner & Berger, 1998).

According to Lind (2007) there is a general dissatisfaction with the Swedish rent regulation system. In 2002 this resulted in a Three Party Agreement between the central organizations of the municipal housing companies, the private property owners and the tenants' union. It was agreed that the private landlords should be involved in bargaining at the local level, that demand factors should play a bigger role in rent setting and that rent control should be stronger for sitting tenants than for new tenants. The agreement did have a small effect on negotiations at the local level, especially on the Stockholm housing market.

In the future the argument about the competitiveness-constraining Swedish rent control system may be strengthened by legislation on competitiveness by the European Union. The European Property Federation filed a complaint in 2005 about the subsidization of municipal housing companies. If they are determined to be subsidized, according to EU legislation, competition in the Swedish housing market might be determined to be biased, in part because private landlords are bound by rent setting in the non-profit sector. A governmental committee is currently at work on revising the rental legislation in a direction that is consistent with the Three Party Agreement and in agreement with EU legislation.

### *France*

The rent regulation in the French private rental sector has changed significantly over time. Times of very strong regulation were followed by times of liberalization and vice versa. The last big change in French private rental sector rent regulation took place in 1989, when the *loi Mermaz-Malandain* was introduced. Many elements of this act are still in force today.

In the unsubsidized private rental sector,<sup>3</sup> leases extend for three years for individual private landlords and six years for institutional private rental landlords such as commercial companies (Donner, 2000, p. 270). The initial rent can be freely set for new or refurbished private rental properties. The initial rents charged for existing

private rental dwellings are set on the basis of reference dwellings: dwellings in the same region, with characteristics that are comparable to those of the rental dwelling for which the rent needs to be set. During the term of the lease, the annual rent increase cannot be higher than the INSEE index of reference rents. This is an index calculated on the basis of three other indices: the index of consumer prices, the index of maintenance and renovation costs and the index of construction costs.

At the end of the lease the tenant normally has the right to renew it, unless the landlord has a good reason for not doing so (for example, because he or she wants to occupy or sell the dwelling). If the lease is renewed, the landlord can opt to have a new rent set, based on reference dwellings. If the landlord does not take such initiatives, the former rent will remain in force.

### *Spain*

Spain's very strict rent regulation changed in 1985 when it was almost completely liberalized. But the new law produced insecurity for tenants and instability in the rental housing market. Rent regulation was thus revised once more.

The 1994 Urban Tenancy Act (*Ley de Arrendamientos Urbanos*) aimed to restore a specific balance between tenants' and landlords' interests (Blas Lopes, 2004, p. 3). This law is still in force today. Setting rent at the beginning of the lease is not subject to conditions. But during the first five years of a lease, the annual rent increase may not be higher than the index of consumer prices. For leases lasting longer than five years, parties are free to agree on new rent increase conditions after year five of the contract. But if nothing was agreed at the conclusion of the lease's term, the consumer price index serves as the basis for rent increases during the whole term of the lease (Blas Lopes, 2004, p. 40).

After the lease expires, the landlord is free to decide whether he/she wants to keep on renting the dwelling, and if so, to which tenant (to the current tenant or to a new one). If the landlord decides to rent the dwelling to the current tenant, new rent negotiations take place. In principle, the landlord then has the opportunity to ask for a significantly higher rent. However, if he/she is satisfied with the current tenant and that tenant wishes to continue occupancy, the rent in the new lease will often be comparable to the rent that the tenant currently pays.

### *England*

According to Kemp (1998, 2004) strict rent regulation is one of the most important factors accounting for the shrinkage of the English private rental sector since the early part of the last century. The Thatcher government, which took office in 1980, intended to halt this trend, and introduced 'regulated tenancies' where fair rents determined by rent officers had to balance the interests of landlords and tenants. With the 1988 *Housing Act*, rent regulation for new leases in the private rental sector was abolished. All new leases were to use market rents, which were to be negotiated between the

tenant and the landlord. Early this century, the market share of not-regulated rents had reached more than 70 per cent (ODPM, 2004). Although rents in principle can be negotiated, it seems to be customary that the landlord (or intermediary) makes a rent proposal which the tenant will accept (Kemp, 2004).

Although England no longer applies rent control to new contracts, part of the private rental market is characterized by some kind of indirect rent control. Since 1996 the subsidization of 'local reference rents' has been introduced for housing allowance recipients (Stephens, 2005). These rents restrict the level of eligible rents for housing allowances for private sector tenants to the average market rents for a dwelling in a particular area. As experiments with a 'Local Housing Allowance' that was based on local reference rents showed, almost half of the private landlords set their rents close to the local reference rent level (Department for Work and Pensions, 2006). If this is the case, it could be regarded as an effect of indirect rent regulation, not because of rules on rent regulation, but because of rules on rent allowances.

### *Germany*

Rents for new leases in the private rental sector are not formally bound; they can be negotiated freely, as long as they are not considered usury rents under criminal law. For rent control for sitting tenants in the private rental sector law allows several methods. For instance, rent changes for sitting tenants can be based on the rents of three similar rental dwellings. Or they can be based on a 'Mietspiegel', a database with local reference rents (Haffner, 2006). The bigger a municipality, the bigger the likelihood that there is a Mietspiegel in place (Deutscher Bundestag, 2003; Bundesministerium für Verkehr, Bau- und Wohnungswesen, 2001).

A Mietspiegel is a database that keeps track of non-subsidized market rents agreed to in all contracts between landlords and tenants in the four years preceding the reference date for the Mietspiegel. The rents collected and calculated for a Mietspiegel are known as local reference rents. These reference rents are based on comparable quality characteristics of buildings and dwellings and their locations.

The main purpose of a Mietspiegel is to enable rent increases to be set in line with market rents. When increasing rents, a landlord can use the Mietspiegel to find out what rents have been charged for homes of similar quality during the four years prior to the Mietspiegel's reference date. The landlord sets the rent increases for his own property based on this. The landlord has to obtain the tenant's permission for any rent increase. The Mietspiegel makes this easier, providing the landlord with a stronger judicial position. An extra regulation prevents usury rents: rents are not to be increased by more than 20 per cent over a period of three years for running contracts.

Rent regulation for sitting tenants is important, because it strengthens tenant security. Changes in the 2001 Rent Law have made it possible to compile a 'scientific' Mietspiegel instead of a 'regular' one. Such a Mietspiegel must be compiled along

scientific lines, providing a stronger judicial status and making rent rises easier to implement than with a regular Mietspiegel.

German rent regulation appears to succeed in damping rent increases when rents are rising. Early this century the rent of new contracts on average was about 5 per cent higher than the average rent (Deutscher Bundestag, 2003). For sitting tenants the rent was on average about 8 per cent lower than average rent.

### The Countries Compared

Table 3 shows an overview of the types of rent regulation that we found in six European countries. It deviates from Table 1 (Lind's classification of rent regulation) in order to fit the classifications that we found. It shows the distinction between running contracts and new contracts, instead of sitting tenants versus all tenants, and no rent regulation as an extra 'type of rent regulation'. We also added information on tenure protection to see whether there might be a link between both; for the sitting tenants (existing contract) the length of the contract is shown in brackets.

**Table 3.** Rent regulations in six European countries (length of tenancy contract<sup>1</sup>)

	Cost-price regulation	Market rent regulation	No regulation
New contract	Netherlands <sup>2</sup> : regulated stock Sweden <sup>3</sup>	France: existing dwelling	England <sup>4</sup> Germany <sup>5</sup> Spain France: new or renovated dwelling Netherlands: non-regulated stock
Existing contract	Spain (5 year) France (3–6 year) Netherlands <sup>2</sup> : regulated stock (mostly permanent) Sweden <sup>3</sup> (permanent)	Germany (permanent)	England <sup>4</sup> (6 months) Netherlands: non-regulated stock (permanent)

*Notes:*

1. There appears to be no clear correlation between tenure protection (length of contract) and rent regulation.
2. Rent adjustment is a political decision based on inflation (1.1 per cent in 2007) plus a certain percentage (that was set at 0 in 2007); rent level depends on quality norms.
3. Rent is based on costs, but negotiated between tenant unions and municipal housing companies.
4. Possible indirect rent regulation via local reference rents for housing allowance recipients in the private rental sector.
5. Separate legislation on usury rents. No written information has been found on this option for other countries, but it is not unlikely that other countries have general legislation against usury, which also applies to usury rents.

Table 3 shows that in most countries rent increases for sitting tenants are regulated. Spain and France protect sitting tenants with running contracts by increasing rents according to an index that represents inflation. In the Netherlands the maximum rent increase for regulated housing stock is a political decision, and each year the government decides on the maximum annual rent increase, normally expressed as inflation plus a certain percentage. Germany is the only country using market-led rent regulation for running contracts. Rent regulation for sitting tenants with indefinite contracts is based on reference rents that follow market rents. If a *Mietspiegel* is in place, rents actually lag behind because of the way they are determined. An extra regulation ensures that rents do not increase by more than 20 per cent over a period of three years for running contracts. England is the only country without formal rent regulation, not only for existing contracts, but also for new contracts. All contracts are subject to market rents and tenant security is limited to six months. This effectively means that rents are not regulated and there is little security of tenure, contrary to the other countries studied. In the other countries strong rent regulation does not necessarily go hand in hand with strong tenure protection, as Table 3 shows.

Table 3 also shows that most new contracts in all of the countries studied are not regulated. The regulated sector in the Netherlands, all contracts in Sweden, and new or renovated dwellings in France are exceptions. In the Netherlands and Sweden the same rent regulation is applied to new and existing contracts. Sweden's regulations are rooted in a cost-based, regulated system, although it is the negotiation power of the tenants in the non-profit sector that actually determines the general rent level. The situation in the Netherlands is more ambiguous. The points system, a system reflecting the quality of a dwelling, is used as the norm for the rent level in the regulated sector, and also for new contracts. We characterized it as a kind of cost-based regulation. In France a market-rent-based regulation is applied to new contracts for existing dwellings; this is in contrast to no regulation for new contracts for new or refurbished dwellings and cost-price regulation for sitting tenants.

The comparison shows that in many of the countries studied here (except Sweden, and the Netherlands and France to some degree) rent regulation denotes protecting the sitting tenant with an ongoing contract. As we saw earlier, this protective 'arm' most probably arises from the idea that the sitting tenant is essentially trapped if the landlord wields his market power to set the rent higher than the market rate. Governments appear to find such protection less necessary for new contracts; if it is applied, reasons of fairness and equality can most probably be expected.

As was noted before, if the tenant is protected, the landlord in principle forfeits his maximum achievable yield in terms of the entirely free determination and adaptation of rents. One needs to realize, however, that if market rents fall below the floor of the regulation, the regulation will lose its function, at least if the market is somewhat transparent. One specific case here in a situation of cost-price regulation is if the cost price rent is higher than the market rent.

### **Balance Between Tenant and Landlord**

Rent regulation offers the consumer protection against an unreasonable increase in rents. The assumption is that the costs a tenant incurs when relocating are higher than the landlord's costs to find a new tenant. Against the advantage for the tenant there is a disadvantage for the landlord. Rent regulation may limit the yield or return for the landlord. If rent regulation is too strong and it is impossible for the landlord to realize a satisfactory return on his investment in the rental dwelling, he will withdraw (over time) from the rental market, so that supply will decline. Neither will new entrants be attracted to the rental accommodation market.

Rent regulation appears to specifically protect the tenant, and to offer few benefits for the landlord. However there could be indirect positive effects for landlords. Broadly accepted rent regulation could have a positive effect on the image and popularity of the private rental sector, and thus on individual landlords. Also, rent regulation may aid the landlord in a strategy to minimize turnover, thus allowing consistent returns.

The countries studied can be ranked according to the type of regulated contracts they use, whether new and/or existing. England must then be regarded as the first, with no rent regulation for either existing or new contracts, in combination with provisions for short-term leases only. Arrangements for housing allowances can be considered indirect means of rent control, however. The other countries all have rent regulation governing some contracts, in combination with longer-term leases, and no regulation for others. Germany and Spain regulate existing contracts only. France regulates new contracts for existing dwellings. The Netherlands follows, both for existing contracts and for new ones in the regulated sector. The non-regulated sector, with 5 per cent of rental stock, is small however. Sweden has the strongest regulation system, with cost-based rent control for all existing and new contracts.

Looking at the various types of regulated contracts is not sufficient to determine the advantages and disadvantages of rent regulation for landlords and tenants. Whether regulation takes place based on cost price or market rent, the allocation of advantages and disadvantages of a system of rent regulation becomes more complex and depends also on the relationship between the market rent and the cost-price rent. If the market rent is higher than the cost-price rent, the landlord will prefer the market rent for regulation, while the tenant will prefer the cost-price rent. But the situation may be the other way around as well.

Another aspect that may play a role is the way the rent is actually determined. Our comparison shows that if it is about cost-price regulation, some actors may prefer a negotiation situation at the local level (Sweden) whereas others may prefer a national political decision (the Netherlands) and whereas others may prefer the use of some index of inflation (France, Spain). If rent regulation is market-lead, the regulation appears to involve the rent of reference dwellings with similar characteristics (France, Germany).

Based on our comparison, one can conclude that the countries that have either a stable share of the private rental sector or have a growing private rental sector in

recent years (England, France and Germany) are more likely to have less regulation than the countries where the private rental sector still is giving up territory. Of course, the causality of this relationship has not been proven, only the co-existence of these two aspects.

Ultimately, rent regulation is a compromise between protecting the tenant and protecting the landlord's yield requirements. On balance, rent regulation will be advantageous for a society if the benefits for the tenant are greater than the costs for the landlord. The theoretical view shows that rent regulation can be deployed to compensate for market imperfections. Quantitative proof of this, however, has yet to be found (Turner & Malpezzi, 2003).

As we have shown, the balance between the interests of tenants and landlords not only depends on the way the system is designed, but also on the way the system interacts with the housing market in allocating advantages and disadvantages. When these are tallied, they may show that there are not only disadvantages from rent regulation for landlords.

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### Notes

1. Privately owned rental dwellings which presently are not subsidized with bricks and mortar subsidies. Possible subsidization via the tax system is disregarded in this definition.
2. For this text we mostly used information from Elsinga *et al.* (2007) and Vandenbroucke *et al.* (2007). The information on Sweden is from other sources.
3. A part of the French private rental sector is owned by landlords who receive financial support of the government (subsidies or tax concessions). In exchange for this support, the rent levels of the dwellings may not exceed a certain maximum that is determined by the state. In this paragraph, rent regulation in this subsidized private rental sector is left out of consideration.

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