

Consultation to Inform the Residential Rental Strategy



November 2016

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Template

Below is a list of questions which you might find useful to structure your response. Some questions may be more relevant to you than others, feel free to skip a question if you do not wish to answer it or you feel it is not relevant to you. There is space to include any additional points you want to make. Additional documentation or information that you think will help to inform the Strategy, can also be submitted.

First, we would like to find out a bit about you

1. Contact name and address:

Construction Industry Federation/ Irish Home Builders Association
Construction House
Canal Road, Dublin 6 **e-mail: hfitzpatrick@cif.ie**

2. Are you making this submission as an individual or on behalf of a group (please tick)?

Landlord	1-2 properties	<input type="checkbox"/>	Individual Tenant	<input type="checkbox"/>
	3-10 properties	<input type="checkbox"/>	Tenant organisation	<input type="checkbox"/>
	11+ properties	<input type="checkbox"/>	Landlord organisation	<input type="checkbox"/>
	REIT	<input type="checkbox"/>		
Estate Agency/ Management Company		<input type="checkbox"/>	Social Landlord	<input type="checkbox"/>
Academic / Policy Analyst		<input type="checkbox"/>	Member of the Public	<input type="checkbox"/>

Other (please specify) Representative Body for the House Building Industry

Submissions will be published and in any case may be released under FOI. All comments, observations and submissions will be subject to the Freedom of Information Acts 1997-2003. The onus is on persons making submissions and comments not to include material of a private nature in the body of their submission.

3. Four key themes have been identified to structure the Residential Rental Strategy, and your comments and suggestions are invited on each theme:

A. **Security** – bringing greater certainty to tenants and landlords.

Your comments and suggestions:

Adequately Resource the PRTB: The number of disputes addressed by the PRTB in 2015 was 4,023 while the total number of registered tenancies in 2015 was 324,000, i.e. a dispute rate of circa 1.24%. It is important to ensure that actions contemplated by government are realistic and appropriate having regard to the scale of the problem to be addressed. The most significant nature of all disputes referred to the PRTB related to rent arrears and overholding of a property. Deposit retention by the landlord was the third highest reason for dispute being referred to the PRTB.

Legislative amendments enhancing the tenants' rights in their rented accommodation are such that, after the initial six month period of tenancy, a right to a tenancy of 4 years exists unless the landlord requires vacant possession for meeting a specified need as outlined in legislation. Further protections have been afforded to tenants in the publication of the Housing (Miscellaneous) Provisions Bill 2016.

Unintended consequences can be a feature of many government interventions. One of the more recent interventions in the rental sector was the restriction on rent reviews to every two years. This had the effect of putting unnecessary upward pressure on residential rents by landlords as rents are now fixed for a 24 month period.

The key to enhancing security for both landlord and tenant is to ensure the appropriate staffing of the PRTB so that an objective period for determination of disputes could ideally be within a 21 day period.

The PRTB adjudicates on disputes between landlord and tenant. Delays in adjudication and settlement of disputes can be prolonged. Greater enforcement powers should be given to the PRTB to enforce its decisions against landlords and tenants while a more streamlined approach to dispute resolution can facilitate an earlier determination of decisions by the Tribunal.

Deposit Protection Scheme: When a property is let, it is normal practice for the tenant to pay one month's deposit to the landlord which is refundable when the tenancy comes to an end. Holding a tenancy deposit by the landlord means that tenants take responsibility and not do anything that would cause deterioration in the condition the dwelling was in at the commencement of the tenancy and the extent of occupation of the dwelling.

Where a tenant fails to pay rent or fails to leave the rented property in the condition in which it was when rented to the tenant at the outset, the landlord will retain the deposit or the element of the deposit that is required to make good the damage to the rented accommodation or the rent not paid.

The PRTB has the power to adjudicate on disputes in relation to refund of deposits and determine if deposits should be refunded or withheld. According to Indecon's Assessment of the Feasibility of a Tenancy Deposit Protection Scheme in Ireland, Indecon noted that, of all the cases referred to the PRTB for adjudication in relation to refund of deposits, there are only approximately 625 cases annually where the PRTB ruled that deposits should be returned. In most cases, landlords may have returned these deposits without any requirement for further intervention by the PRTB. With a total of 324,000 registered tenancies, those

adjudications for refund of deposits by the PRTB (625 cases in total) would account for only 0.2% of total private residential tenancies existing in the State.

Recommendation:

1. The key to enhancing security for both landlord and tenant is to ensure the appropriate staffing of the PRTB so that an objective period for determination of disputes could ideally be within a 21 day period.
2. Greater enforcement powers should be given to the PRTB to enforce its decisions against landlords and tenants while a more streamlined approach to dispute resolution can facilitate an earlier determination of decisions by the Tribunal.
3. A 'sledgehammer to crack a nut' approach should not be adopted in putting complex costly arrangements in place providing for a tenancy deposit protection scheme which is unnecessary. Some alternative arrangement could be considered through the Department of Social Protection if required to address any special needs that may arise in relation to this area.
4. In the commercial sector, if a tenant is in the property for more than 4 years and 9 months, this gives them automatic rights of renewal. This could be looked at for residential. Giving a tenant a 2 year + automatic right of tenancy after a short period of say 6 months would be a major deterrent for investors (who ultimately will be the cohort who will fund new supply)_because it inhibits their ability to sell the unit with vacant possession.

B. Supply – maintaining existing levels of rental stock and promoting additional supply through encouraging new investment and bringing unused capacity to the market.

Your comments and suggestions:

The current rental sector is characterised by individual small scale landlords many of which own two to four rental properties. In many cases, individuals' motivation and incentive to owning rental properties was to have an investment which could act as a pension fund at retirement.

Investment in residential property at the time was also encouraged by:

- High anticipated levels of capital appreciation;
- Up to 100% mortgage availability for residential investment property;
- Availability of interest only mortgages;
- Low rate of capital gains tax applicable at the time of 20%;
- Availability of Section 23 type reliefs on a widespread basis; and
- 100% relief on interest paid on borrowings to fund property acquisition.

The entire landscape for investment in residential property has changed with the result that the small time investor will now be reluctant to invest in this sector due to the following:

- Realisation that property prices will not always increase, and that prices may fall as well as rise;
- More stringent bank lending policies requiring substantial equity investment to fund a residential investment property;
- Non-availability of interest only mortgages;
- Increase in capital gains tax rate to 33% from the previous 20% rate;
- Non availability of Section 23 type reliefs;
- Restriction on availability of mortgage interest relief for residential investment property to maximum of 75% of interest paid;
- Costs for registration of tenancies with the PRTB;

- Landlord liability for property tax in respect of rental property; and
- Potential landlord liability for payment of water charges for rental property.

The impact of these realities could deter future investment by both non-professional individuals and professional long term investors, which in turn will impact upon the scale of residential investment properties that will be available for letting purposes. Shortage of demand from residential investors for new investor type rental accommodation will result in shortage of construction of new accommodation for rental, hence the continued shortage or shrinkage of supply of new rental accommodation that may be available into the future.

Benefits of encouraging and retaining the small residential investor in this investment sector include:

- The availability of mixed tenures in residential developments with dispersal of individual private rented residential units among owner occupied housing;
- Support renewal of construction of rental type accommodation in sustainable locations where demand for such accommodation prevails; and
- The availability of a regional distribution of private rented residential units throughout towns and villages countrywide.

While it is important to encourage corporate investment on a larger scale in private residential investment, it is equally important that one does not end up with only corporate investment in this sector. This would result in investment of this nature only taking place in selected urban centres and a potential 'centralisation' of private rented sector in specific buildings and locations.

In saying that, we need a wholesale solution to a wholesale problem. Allowing corporate investors to fund new units of scale will be a much quicker fix than trying to suit the retail investors who will do it unit by unit. Interfering in market rents will deter investment. Logic tells us that supply will curb the continuance of dramatic rental/price growth so anything which deters corporate investment into the supply of new units should be avoided... it will have the unintended consequence of adding to the problem.

Professionalising the private rented sector should encourage investment by both the large scale corporate investors and the continuation of investment by the small time residential investor on the basis that standards and regulation are fully adhered to.

Investment in residential property for rental purposes will only happen when a reasonable rate of return is achievable in respect of the investment. Supply and demand for rental accommodation are key factors influencing rates of return on investment including the tax laws pertaining to the sector.

It is in government's interest to encourage supply of rented residential accommodation to ensure that supply and demand are broadly in equilibrium and that any imbalances in supply and demand do not pose any competitive disadvantage to the economy in attracting foreign direct investment and job creation.

Due to higher construction costs for multi-unit developments, i.e. apartment buildings, it is not possible to secure a realistic rate of return on investment for investment in such new units when one factors in reduced mortgage interest relief available for private rented accommodation, the associated regulatory costs and the updated tax rules including property tax applicable.

VAT on the construction costs of new rental accommodation is non-refundable. Where residential units are built for rental purposes, some provision should be made in the VAT code that provides for VAT relief where units are retained in a PRTB registered rented use for a period of up to 10 years.

Recommendation:

1. Mortgage interest relief should be restored to 100% of interest costs incurred in servicing a mortgage for rented residential units. 100% of interest relief applies as a trading expense in non-property sectors and for investment in other sectors including the office and commercial sector.
2. Provision should be made in the VAT code that provides for VAT relief where new residential units are retained in a PRTB registered rented use for a minimum period of 10 years.
3. Property tax paid by a landlord should be allowable for taxation purposes so as to avoid the concept of double taxation.
4. Reduction in construction/delivery costs of units such as reducing VAT, reducing levies/contributions and a regulatory standards review. This would benefit both private and social rental unit delivery costs, including private housing.

C. Standards – improving the quality and management of rental accommodation.

Your comments and suggestions:

All landlords have a legal obligation to ensure that their rented properties comply with minimum standards provided for in law.

Minimum standards are set out in the Housing (Standards for Rented Houses) Regulations 2008 and the Housing (Standards for Rented Houses) (Amendment) Regulations 2009. The regulations specify requirements in relation to a range of matters such as structural repair, absence of damp and rot, sanitary facilities, heating, ventilation, light and safety of gas and electrical supply.

Responsibility for enforcing the standards rests with local authorities. Inspection programmes by local authorities vary significantly with the result that confidence levels in the inspection regimes can be lacking.

All landlords are obliged to register their tenancies with the Private Residential Tenancies Board. There is no requirement for any independent certification that the Housing (Standards for Rented Houses) Regulations are complied with.

The Building Control (Amendment) Regulations 2014 address any existing concerns that may arise in relation to standards for rented residential units where construction of such units commences after 1 March 2014. The difficulty exists in respect of older properties that are rented and which may not meet the required standards.

In many cases, quality management company arrangements are established where an entire development may be rented by a professional landlord. In these cases, an amended standard requirement could operate to enable amended utility/ storage arrangements where laundrettes or centralised storage facilities are provided. Flexibility is required to stimulate increased investment in this sector.

Recommendation:

The first registration of any property for rental purposes should:

1. Carry a certification by a chartered engineer, a building surveyor or registered architect that the property complies with the building regulations applicable when the building was originally constructed and/ or meets the requirements of the Housing (Standards for Rented Houses) Regulations;

2. The cost of securing this certificate should be allowable for tax purposes against the rental income received from the property by the owner;
3. This requirement should be introduced over a two to three year timeframe.
4. Flexibility is required relating to mandatory standards pertaining to matters such as storage requirements and centralised recreational areas in those developments where quality management company arrangements are established. This would apply in conjunction with the long terms rental of the majority of residential units in any one multi residential unit structure.

D. **Services** – broadening and strengthening the role and powers of the Residential Tenancies Board (RTB) to more effectively provide key services to tenants and landlords.

Your comments and suggestions:

Many of the points referred to at 3 (A) above are relevant for this section of the consultation document and are not repeated at this stage. The RTB is a useful assistance to helping an efficient operating system in the rental sector. However, it is there to provide oversight and implement policy as opposed to creating it. The focus needs to be creating supply in a constrained market place.

In framing your submission under the above headings, you may consider the following questions

Vision for the residential rental sector:

- *What role should the rented sector play in the overall housing system in Ireland?*
- *How do we make the rented sector an attractive long term tenure of choice for households?*
- *How do we ensure the rented sector can provide secure and stable returns for landlords?*
- *What role can cost- and affordable rental models play in the long term development of the rented sector?*

There is space here for your comments and suggestions.

- **Role of Rented Sector:** As demographics and migration/ movement of people continues to evolve, the demand for rental accommodation is likely to continue to grow. The key to meeting this demand is to facilitate the environment within which industry can deliver the required new housing output levels, and that the supply of suitable housing is available in the right places. When new housing supply is increased to the level that it satisfies demand for the appropriate size and location sought, then future occupiers will determine the housing tenure most suitable to them.
- Rentals account for 25% of all occupations in the Greater Dublin area. However, as a sector, it is demonstrably premature as compared to the UK and there are few measures being implemented to assist in attracting corporate investment into it. Arguably, some recent measures are a deterrent. If rental controls are brought in, it will render the sector un-fundable as the returns will not be sufficient to attract equity investment in a first loss scenario where the returns are capped.
- **Rental Sector as Attractive Long Term Tenure Choice:** Home ownership should continue to be the preferred tenure facilitated by government. Home ownership ultimately reduces an individual's potential liability on the State as they grow older and enter retirement. A person renting their home during their entire working life may be more likely to experience a shortfall in income as ongoing

rental obligations apply during retirement while for owner occupiers, no such ongoing liabilities may apply as home mortgages have been paid off during their working life.

- **Provide Long Term Stable Returns for Landlords:** Taxation of residential investment property should be on a par with commercial investment property. All outgoings, as referenced above including local property tax paid and 100% of interest costs incurred on borrowings should be allowable costs for taxation purposes. Similarly, uncertainties with proposed legislative change must be minimised as this distracts from investment decisions by investors and can even add to an exodus of investors from the marketplace. Fear of fixing of rents or retention of deposits by the PRTB all add to uncertainties which can have a detrimental impact on level of investment required in the sector. Returns landlords/investors require from existing stock are different to what an investor would require to finance the development of new supply, the riskiest form of property investment. Any interference in market rents for investors who are investing in development for new supply will render the sector un-fundable.
- **Cost and Affordable Rental Models:** While these models can play their part in delivering tenure of choice in some major urban settings, the likelihood of these models being available outside of the greater City areas is unlikely. It is for this reason that the requirements of the smaller residential property investor must not be overlooked, and that measures be available to retain such investors in meeting the demand in provincial towns and villages nationwide. Social housing and Not for Profit housing is primarily a/the cost and affordable rental model.

Stability in the rental sector, predictability for tenants and landlords and rent affordability in pressure areas

- *What approach to rent regulation would be appropriate for the Irish rental market?*
- *Are there examples from other countries of approaches to regulation of the rental sector that you think could work in Ireland?*
- *What measures could be used to balance potential negative impacts on supply arising from measures to provide greater predictability around rents?*

There is space here for your comments and suggestions.

- **Rent Regulation Appropriate for the Irish Rental Market:** Putting Ireland to one side, rent regulation in any market simply does not work from a Funder's perspective. Take Germany as an example. In the main, the residential sector there is dominated by outdated and not fit for purpose residential stock as current rents do not provide the investor with a sufficient return to build new stock. The majority of Investors in Germany acquire thousands of existing units and hold for income. Coming back to Ireland, this model does not work because any interference in rent renders investment unviable. See Appendix A for worked example. The industry will be able to prove from international investors that rent regulation renders the sector unviable should the request be made.
- Introduction of any form of rent regulation in the Irish rental market will mean that long term investors will simply look for more commercial rates of return on alternative investment decisions. This will be compounded whereby development funders will not have the appetite to fund new building of rental stock including apartments. Introduction of such measures will also likely result in investors leaving the market compounding current difficulties with lack of the

required housing stock for the tenure sought (rental). Any form of rent regulation will have a further destabilising effect on existing levels of rental stock and future development decisions for building such new housing stock for rental purposes.

- Regulation or over regulation and intervention generally hinder supply and detract from investment. Supply and choice are what is required to create competition of supply rather than competition of demand.

Increasing investment and protecting existing supply

- *How can we improve the investment environment for the rented sector?*
- *How can we increase the supply of dedicated for-rent accommodation in areas of high demand and at more affordable levels? What is the role and capacity of the not for profit sector in this regard?*
- *How do we ensure fairness for all parties in terms of enforcement of existing standards for rental accommodation?*
- *How do we support landlords and protect tenants in cases of encumbered buy-to-lets?*

There is space here for your comments and suggestions.

- **Investment Environment for the Rented Sector:** Investment environment for the rented sector can be improved by removal of the uncertainty that prevails in relation to government regulation of rents, PTRB holding of deposits, and ensuring that the taxation treatment of residential landlords is put on an equal footing as that for commercial landlords.
- **Increase Supply of Dedicated for-Rent Accommodation:** Any measures contemplated must be such that they complement existing activities of the private development sector and not act as an unlawful State Aid to some providers of rental accommodation. The experience of the 1990s when Section 23 type investment relief was introduced meant that it was then viable to build a new stock of residential investment properties. The positives of this period should be looked at again and determine if such equivalent initiatives could be targeted in a measured way to key towns nationwide and assist in eliminating some urban dereliction that exists countrywide.
- **Enforcement of Existing Standards for Rental Accommodation:** See 2 (c) above.
- **Encumbered buy-to-lets – Support landlords and protect tenants:** Mortgage providers should be capable of presenting banking solutions that support retention of tenants in situ while the outstanding mortgage difficulties are being addressed with the owner. Existing rights of the tenants should not be altered as a result of the potential sale of the distressed asset.

Encouraging More Secure, Durable and Long-lasting tenancies

- *Is the current balance of rights between landlords and tenants in relation to security of tenure appropriate? If not, how could it be improved?*
- *What forms of non-adversarial dispute resolution could be used in the rented sector?*
- *How can we improve information and awareness for landlords and tenants?*
- *How do we effectively protect deposits?*

- *What sort of services and systems will help encourage more successful tenancies which will enable tenants to consider their rental property as a safe and stable “home” and landlords to depend on the same property as a permanent and dependable source of a regular income.*

There is space here for your comments and suggestions.

- **Balance of rights between landlords and tenants in relation to security of tenure:** Existing protections together with those included in the Housing Miscellaneous (Provisions) Bill 2016 appear adequate.
- **Non-adversarial dispute resolution that could be used in the rented sector:** Scope for independent arbitration/adjudication by a qualified chartered building surveyor could assist in resolution of disputes. This would be akin to a building contract dispute between a builder and an employer.
- **Improve information and awareness for landlords and tenants:** In fairness to the PRTB, PRTB issue quality documentation to both the tenant and the landlord on registration of a tenancy. Perhaps the principal letting websites which market properties available for rent could also host standard information and awareness for both landlords and tenants who are the principal users of these sites.
- **Protect Deposits:** This has been addressed above under Section 3 (A)

4. Please use this space to provide any other comments and suggestions you would like to make. For example, if you would like to comment on a specific segment of the rental market, or how the sector might better serve the needs of a particular group or groups.

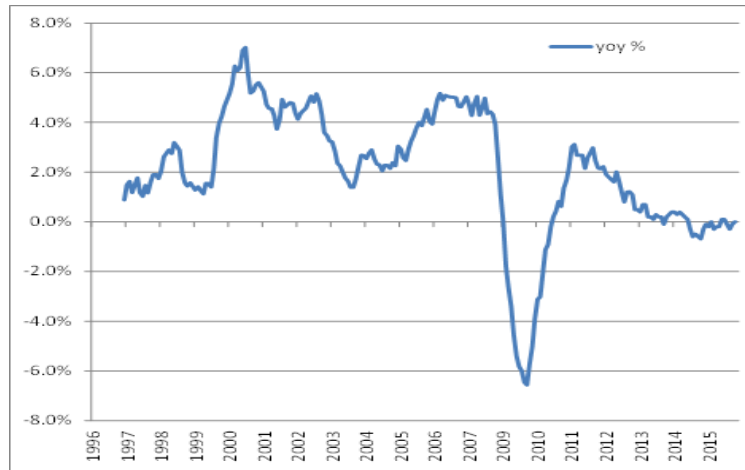
Looking at The Provision of Multi-Family Units from a Funder’s Perspective

The matrix of returns are analysed using scenarios where rental controls exist and where open market determines rent on the following basis:

1. Rental control: capped at 2% per year
2. Rental control: rents linked to annual CPI
3. Rental growth in line with open market

1 & 2 Rental control – qualitative analysis:

- Funders taking equity risk (first loss) will usually not allow equity upside to be capped
- Limited number of potential investors – capping upside is a major deterrent
- Deterring funding means no increase in supply, which in turn will result in rent increases
- Each unit will require re-basing when unit becomes vacant
- Requires minimum lease terms in inflationary environment, otherwise no security
- This will create a two-tier market where tenants will pay key money to access locations / buildings
- Strong rental hikes are inevitable in the current inflationary environment, particularly where there is a lack of supply due to absence of funding.



Annual CPI – 1996 - 2015

Financial Analysis – Case Study. Key Basic Assumptions across all three scenarios

- Ten year hold period in order to acquire site, develop and retain
- Site input value at zero
- Scheme of 226 units with mix of 1,2&3 beds with 120 car spaces
- Market rents in typical Dublin 1 location
- Rents grown in line with SCSl figures of 7.5% in 2016; assume 5% in 2017 and 3.5% thereafter
- Assume tenant remains in-situ during hold period
- 5.75% gross exit yield
- Utility costs and landlord non-recoverables assumed at 25% gross to net
- Construction costs per recent tenders received – construction period 24 months
- Tax at prevailing rates with QIAIF structure used as the holding vehicle

Scenario	Funder's Projected Returns			Conclusion
	IRR ungeared during construction	IRR ungeared during investment hold	Combined IRR ungeared construction and investment hold period	
Rental Growth Capped at 2% per Year	5%	6%	6%	This does not provide a Funder with sufficient return commensurate with their risk
Rental Growth pegged to CPI*	3%	5%	5%	As above
Rental Growth in Line with Open Market**	12%	7%	8%	Further work on costs of delivery will be required as the site price assumed will mean that other uses will take precedence.

NOTE: In all scenarios, the site price is entered as 'zero' meaning the land value will add to the cost

*0.4% CPI for remainder of 2016 and 1% thereafter for hold period

**2016/2017 at 7.5%, 2017/2018 at 5%, 3.5 % for the remainder of the hold period

Conclusion

- Introducing or interfering in rent control will cap an equity funder's return and will act as a major deterrent to investment (corroborated by global investors of scale)
- Allowing rents to grow in line with the open market will aid to facilitate supply
- Not allowing rents to grow in line with open market will render PRS schemes unviable
- PRS investment tends to attract institutional capital that will usually hold for the long term
- There is a significant volume of capital waiting to be deployed into an Irish PRS strategy once it becomes financially viable to do so
- Any effort to control or cap rents could indirectly lead to stronger rental growth levels on units that become vacant on new lease this will make a two-tier and sub market trade in leases as are in other countries that have rent controls.

- If measures are implemented to make PRS financially viable in Ireland, the supply can be turned on in a relatively short timeframe. The opposite is true.

SCSI Report (Dec 2015) in relation to Dublin residential rental growth:

Expected average percentage change in rental prices during 2016 by region
December 2015 to December 2016

	Dublin	Leinster (excl. Dublin)	Munster	Connaught/ Ulster
1 Bed Apartment	7.9%	6.3%	6.4%	5.5%
2 Bed Apartment	7.8%	6.8%	6.7%	5.8%
3 Bed Semi-Detached	7.2%	7.3%	6.7%	5.7%
4 Bed Semi-Detached	6.9%	6.8%	7.0%	5.5%

Source: SCSI Members Survey, Dec 2015

The Dublin Region has been identified as the region likely to experience the greatest levels of year-on-year growth in the cost of renting in 2016, with members expecting increases of 7% to 8%.