

# The Private Rented Sector in the 21st Century – Policy Choices

Anthony McCashin  
*Trinity College Dublin*

**A Joint Publication between Threshold  
and St Pancras Housing Association**

**March 2000**



**ST PANCRAS HOUSING ASSOCIATION**



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Against the background of a 'housing crises', where the emphasis was very much on the affordability of access to homeownership, Threshold and St Pancras Housing Association undertook a programme of research with a view to placing the less prominent and less publicised aspects of housing policy more firmly on the public policy agenda. These concern the role of the private rented sector, the potential and problems of the non-profit and voluntary housing sector and more generally, the housing policies and provisions affecting individuals and families on low income. The first fruits of this programme are given in this study, which is concerned specifically with the private rented sector. A future study will deal with the non-profit and voluntary housing sector.

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Threshold and St Pancras Housing Association would like to thank Tony McCashin for his expertise, hard work, and enthusiasm in producing this report.

It is our hope that this report will make a substantial contribution to the ongoing debate about the future development of the private rented sector in Ireland, so that future generations of households can find private rented housing that is affordable, of good quality and offers genuine security of tenure.

*Aideen Hayden, Chair of the Board, Threshold.*

*Simon Brooke, Chair of the Board, St Pancras Housing.*

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The author accepts full responsibility for the content and for any errors or omissions.

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This report brings a fresh insight into the nature and structure of the private rented sector in the context of the wider Irish housing system and outlines a policy direction for the future of the private rented sector into the 21st century. This report widens the private rented sector debate into issues relating to tenure neutrality in housing finance and social policy principles under which a housing system might operate. The approach of the author has been to integrate the available data on housing policy with information gathered from a range of informants in the appropriate fields, alongside an extensive analysis of available literature.

There are several fundamentals of housing policy, identified in this report, which set the tone for the debate on the future for policy in the private rented sector. In brief these fundamentals are:

- Housing policies and markets have implications for the level of public expenditure, the labour market, the quality of the physical and social infrastructure, the operation of financial markets, and the financial and social well being of the population;
- Housing is a system and the inter-tenure links should be recognised in the formulation of policy. Housing policies should therefore facilitate access for all to adequate, affordable housing as well as general policies of income maintenance and income distribution;
- Excessive focus on promoting owner occupation by means of general subsidies and tax incentives encourages owners to acquire accommodation in excess of their needs, tending to create a combination of 'over housing' at one end of the system and 'under housing' at the other;
- The supply of local authority housing is critical in meeting the housing needs of those on the very lowest incomes, but the manner in which it is supplied can exacerbate social exclusion if it is provided in distinct areas; where this supply is inadequate it results in greater demand for private rented and therefore payment of a rent allowance to landlords.

Following on from these housing policy issues, and the discussion of tenure neutrality in Chapter 1, the author raises the question of equity in the housing system between the private rented sector and local authority provision. The current situation in Ireland is that the private rented sector is meeting the needs of many low-income tenants in receipt of SWA rent supplement. If the private rented sector is to continue to meet these needs, the author calls for a more neutral policy as between the private rented sector and local authorities, due in particular, to the differences in the operation of rent supplement and the differential rent system utilised by local authorities.

This study includes an international comparative of the private rented sector (Chapter 2) and the patterns, which have emerged in recent decades. The analysis then focuses on four countries in particular: UK, Germany, Netherlands and Canada.

### **The key issues emerging from this study**

- To sustain a large, good quality private rented sector it may be necessary to have a greater balance between owning and renting, and between private renting and social renting;
- Tax incentive strategies to attract investment are not especially effective at generating long-term development of the affordable part of the sector, particularly where landlords are small-scale;
- Most countries do not have any significant involvement by large-scale institutional investors in private rented accommodation. Significantly, where such institutional investment has been a feature it is associated with a non-profit housing sector. These organisations act in effect as financial conduits, developers, and providers;
- Non-profit housing in other countries have contributed to the provision of low-cost rented accommodation, assisted by bricks and mortar subsidies and also personal housing allowances. Countries such as Sweden are noted for combining good quality public rental and private rental sectors that draw to some extent from the same, broad tenant population;
- In many countries a *strategic* choice has been made to shift the emphasis in policy towards income support in respect of housing costs and away from direct State provision of housing; and
- The historic form of rent control has now all but disappeared. In some of the countries examined a rent indexing structure is in place instead, to varying degrees. Countries with some statutory framework governing rent increases have been more successful in sustaining both supply and demand in private renting.

The comparative study of this report demonstrates the need for a strong social housing programme in order to develop a strong private rented sector. Strong growth in the private rented sector is also linked in this report to reasonable security of tenure and regulatory structures. The comparative study shows how the non-profit housing organisations can successfully generate low-cost rental housing, and also raises the issue of tenure neutrality, clearly demonstrating that the position in Ireland is one of the most skewed in favour of home ownership.

Chapter 3 and 4 examine policy and the private rented sector in Ireland, in particular the interaction of supply and demand within the private rented sector and the impact that government subsidies have on this relationship. The author draws the conclusion that there has been no overall strategy by the government for sustaining the supply of affordable private rented accommodation.

A series of key recommendations are put forward in the report for the future development of the private rented sector, keeping in mind the social policy principles that the study is based upon and the related issues of tenure neutrality and housing tenures being interlinked. The bases of these recommendations are also grounded in the author's assertion that it is very difficult to justify an unregulated private rented sector; with regard to rent level increases, which ultimately results in continual increases in rent supplement levels.

The key operational recommendations emerging from this report are:

### ***Rents and Rent Supplement***

- a national system for rents, whereby rent changes are based on a pre-determined annual or other regular basis, utilising an index. The initial rent would be agreed by landlords and tenant and guidelines developed with regard to issues such as quality and local markets;
- a combination of regulation and housing allowances is the only strategy for building an affordable private rented sector. In the absence of regulations, there will be a continuing need to increase rent supplements; and
- rent supplement needs to be re-examined in relation to discretionary practices, the level of the support, the range of the population it targets and its inequity to tenants, in relation to the local authority rent structure.

### ***Supply Issues***

The author believes that the Section 23 tax incentive has not delivered an increase in the supply of affordable housing stock. Proposals are put forward in this report for developing targeted assistance for investors in the private rented sector, linked to the provision of affordable private rented housing. The report calls for:

1. A fresh review of the abolition of interest deductibility on borrowings for rental properties, eg a limit could be imposed on the *amount* of borrowing any one investor may be permitted; the level of deductible interest could be tiered according to the length of time the property will be in the rental market or related to the level of rents to be charged;
2. Development of investors incentives to supply accommodation at the *lower* end of the market eg cash grants for building costs; generous depreciation allowances or even direct current subsidies; and
3. Specific *grant* incentives to be devised to upgrade the older stock in the private rented sector; these incentives should be devised so that the accommodation becomes available to tenants on lower incomes at affordable rents.

### ***Security of Tenure***

In light of the comparative studies undertaken in this report, the author believes that the private rented sector cannot be sustained unless the demand side of the market is strengthened with improved security of tenure for tenants. A series of recommendations to tackle the issue of security of tenure are put forward in the report and include a call for the notice to quit period to be increased in relation to the length of occupancy by tenant; a minimum period to elapse before a rent increase can take place; a notice to quit to be allowed only under specified circumstances; short term leases to lead to rights for longer term leases; and a right of renewal of leases for tenants.

These potential reforms to the tenant – landlord relationship, in the private rented sector, are supported by Threshold. In order for this type of reform to take place, legislation is required. Additionally a mechanism is necessary, to ensure that tenants and landlords rights can be exercised, in a manner that leads to rapid dispute resolution. Threshold has put forward the model of a Housing Rental Board, which would act as a mediation service for these disputes. Additionally the Housing Rental Board could also hold rental deposits on behalf of both landlords and tenants, following models common in other countries such as Australia.

*And two final points:*

Firstly, there are inadequacies in the statistical information available on the private rented sector and indeed on housing tenures in general. In order to plan for the future of the structure of housing in Ireland as a whole, there needs to be a quicker turnaround of the availability of data, particularly in relation to the Census, but also in relation to the Household Budget Survey and the Quarterly National Household Survey. Administrative data should be more readily available for researchers and the Department of the Environment and Local Government need to develop new sources of housing information. This could be best served through the establishment of a regular household condition survey, following the models already in place elsewhere in Europe.

Secondly, when reading this report, a conclusion may be drawn that the dominant position that home ownership holds in the current housing system in Ireland, will continue to impact on the structure of rental housing (private or social sectors), and therefore on many low-income households, unless fundamental equity issues at the heart of the housing finance system are addressed.

**Clodagh Memery**  
**Head of Research and Policy Development**  
**Threshold**  
**27 March 2000**



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# Introduction

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This analysis of the role of the private rented sector in Irish housing is offered as a contribution to the ongoing debate on Irish housing policy.

In 1998 and 1999 public and political attention in relation to housing issues was focused very intensively on one housing problem – affordability of owner-occupied housing. The background to this was the very rapid escalation in house prices in the second half of the 1990s and the effect this was having on access to private housing. In the event the Government commissioned the Bacon reports (Bacon 1998; Bacon, 1999) and adopted the analyses in these reports as the basis for policy change.

A further effect of the understandable public and political concern with the ‘affordability crisis’ in home ownership was the tendency for other equally important issues in housing policy to command relatively less attention. One commentator (O Sullivan, 1998) was impelled to refer to “the other housing crisis”, manifested by rising numbers of homeless persons and increases in acute housing need. This ‘other crisis’ and the aspects of housing policy with which it is associated have commanded much less public and political attention despite its growing severity over an extended period of time.

At the time of writing (1999) two developments are underway which have the potential to shape housing policy in the future. First, the Government-appointed *Commission on the Private Rented Residential Sector* has commenced its work and is due to report in June 2000. As the first such Commission in this area it is likely to engender some debate. The analysis offered in this document hopefully anticipates some of the questions and problems that the Commission will address in its report. Second, the Government and the relevant interests are in the process of finalising the fifth national agreement on pay, social welfare, and social and economic policy, *Programme for Prosperity and Fairness*. Like its predecessors the programme document does not contain a substantial analysis of housing issues or a detailed agenda of specific policy changes.<sup>1</sup> However, the programme does offer a commitment to the establishment of a Housing Forum and makes an explicit commitment in regard to the formulation of policy for the private rented sector:

*The forthcoming report of the Commission on the Private Rented Sector will form the basis for reforming the sector and in particular for addressing a number of issues including security of tenure, appropriate regulation and enforcement, achieving an appropriate balance between the rights and obligations of landlords and tenants, measures to increase investment in and supply of rented accommodation and the removal of constraints to the development of the sector. (Government of Ireland, 2000, p.101)*

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<sup>1</sup> The earlier programmes were: *Programme for National Recovery* (Government of Ireland, 1987); *Programme for Economic and Social Progress* (Government of Ireland, 1991); *Programme for Competitiveness and Work* (Government of Ireland, 1994); *Programme 2000 for Inclusion, Employment and Competitiveness* (Government of Ireland, 1996)

The timing of this statement of policy intent, the imminent establishment of a Housing Forum, and the forthcoming report of the Commission taken together provide an immediate opportunity to stimulate analysis and debate about neglected aspects of housing policy. It is hoped that the discussion in this study of policy for the private rented sector will inform and enlighten this emerging debate.

Before proceeding to the main discussion a number of key principles guiding the analysis and the selection of issues that are dealt with are set out here.

**0.1 Housing provision and policy are central.** The housing system should be accorded greater prominence in public policy and in the formulation of national programmes and plans than has been the case in recent decades.

- Housing policies and markets have implications for the level of public expenditure, the labour market, the quality of the physical and social infrastructure, the operation of financial markets, and the financial and social well being of the population,
- More immediately, in a context where the social partners and the government are attempting to formulate another framework to guide the future evolution of pay and personal incomes, the role that housing costs and housing access play in shaping employees' and families' incomes is especially important, and
- Housing costs can form a very significant proportion of household expenditure and for some individuals and families these are the single largest item of household expenditure.

**0.2 Housing is a system.** The various tenures in the housing system are inter-related, and the links between the main tenures should be recognised in the formulation of policy.

- The supply of local authority housing is critical in meeting the housing needs of those on the very lowest incomes; where this supply is inadequate it results in greater demand for private rented and owner occupied housing and for other forms of State support such as rent allowances,
- If private rented accommodation for persons on lower incomes is expensive, or poorly regulated, or deficient in quality this will affect the housing system more generally. For example, the demand for directly-provided State housing will be greater or there will be an increased need for rent allowances, and
- If public policy focuses excessively on encouraging owner occupation by means of general subsidies and tax incentives it will encourage owners to acquire accommodation in excess of their needs, tending to create a combination of 'over housing' at one end of the system and 'under housing' at the other.



**0.3 Housing is related to poverty and social exclusion.** There are circular and complex links between poverty and social exclusion, on the one hand, and the structure and operation of the housing system on the other.

- Households with incomes below the poverty line will be less likely to afford adequate housing at market prices without some state intervention. Housing is so essential to the welfare of individuals and families that the state needs to have housing policies which facilitate access for all to adequate, affordable housing as well as general policies of income maintenance and income distribution;
- Families already in adequate accommodation (owned or rented) may find themselves unable to afford their housing if family income declines due to unemployment, bereavement, and reductions in earnings, and
- The state's response to the housing needs of the poor and those on lower incomes may itself exacerbate social exclusion in the way in which housing is structured and provided. If local authority housing is generally provided on a large scale in distinct areas and locations, social class divisions between high income and low-income families will be reinforced. These social class divisions and their consequences in terms of educational and social disadvantage will be further reinforced if the housing stock and housing estates are inadequately maintained and managed.

Taken together, these principles point to the need, in the current context, for an analysis of the problems affecting the 'lower' reaches of the housing system that does not ignore the 'systemic' nature of housing policy and problems. While this document is focused on the private rented sector as a whole the emphasis is on aspects of the tenure that relate to poverty and social exclusion. Chapter 1 puts the private rented sector in context by looking briefly at the issue of tenure neutrality. Chapter 2 offers an overview of the sector in Ireland and places it in comparative context. Chapters 3 and 4 respectively deal with policy principles and recommendations.

The aim of this document is to outline a policy direction for the future, based on the available data about housing issues. The document does not, therefore, contain a mass of statistical detail about the Irish housing system. A wide range of relevant publications already contains considerable detail about the size and tenure composition of the housing stock, trends in housing output, housing costs, public expenditure, homelessness and housing need, demographic trends and related issues (Dept. of the Environment, various years; Bacon, 1998; Bacon, 1999; Downey, 1997; O'Sullivan, 1996; O'Sullivan, 1998; Fahey and Watson, 1995; NES, 1988). Specific data are included where relevant to policy or where they offer new information on aspects of the housing system. Throughout, the approach is to integrate the available data on housing policy with the information gleaned from a wide range of informants and with discussion of policy principles.

# Chapter One – Tenure Neutrality

## 1.1 Introduction

The starting point for policy analysis in housing is the principle of tenure neutrality. This principle would require that the net income after tax and housing costs of two individuals in different tenures are equal, where they have equal housing conditions and where they are identical in all relevant respects. In practice, policy makers do not strive to achieve this precise form of neutrality but seek instead, in varying degrees, to achieve a broad balance in the way in which the various tenures are taxed, subsidised and regulated. The Irish housing system is very far from being tenure neutral, and the absence of neutrality is to the detriment of the private rented sector. As the analysis of other countries' experiences in Chapter 2 shows, a degree of tenure neutrality is essential in sustaining a role for the private rented sector. It is important at the outset, therefore, to focus on tenure neutrality, firstly by comparing private rented with the dominant tenure, owner occupation and, secondly, by noting the relative statuses of private rented and local authority rented accommodation.

## 1.2 Owner occupation

Ireland has a high level of home ownership; there are in excess of 1.1 million households in Ireland and about 80% of these are owner occupied, that is living in accommodation that is owned outright (without a mortgage) or owned with a mortgage. The equity and efficiency of the housing system as a whole is strongly shaped by the way in which this tenure is treated in taxation and subsidy terms. To consider the role of policy in relation to owner occupation it is necessary to set out some relevant analytical principles.

**Table 1: Tax Treatment of Owner Occupation:  
Illustrative Calculations, £ per annum**

	Renter	Owner	Mortgagor	Renter incl. RTA
Interest Income	3,900	0	3,900	3,900
Earnings	22,500	22,500	22,500	22,500
Total Income	26,400	22,500	26,400	26,400
Basic+PAYE Allowances	5,200	5,200	5,200	5,200
Mortgage Int. Relief	—	—	2,500	—
Rent Tax Allowance	—	—	—	500
Gross Tax Liability	9,944	8,150	9,944	9,944
Tax payable	8,696	6,902	8,096	8,576
Housing costs (Rent or Mortgage Int.)	6,000	0	6,000	6,000
Income after Tax and Housing Costs	11,704	15,598	12,304	11,824

Notes: Mortgage interest rate is 4%; interest rate on savings, 2.6%; value of house £150,000. All tax allowances are calculated at the standard rate and for the amounts that apply in 1999/2000. RTA is the Rent Tax Allowance. Rent is assumed to be £500 per month.

The standard analyses of housing tenures are usually framed within a three-cornered comparison of: owner occupation with a mortgage, outright owner occupation, and unsubsidised private rented accommodation (See Barr, 1987). Typically these analyses specify – as in Table 1 above – hypothetical individuals with identical gross incomes and financial capital who make different tenure choices. In this illustration, the outright owner spends £150,000 on purchasing a house, the mortgagor borrows the £150,000 to purchase a home while investing the initial capital and receiving interest, and the renter invests the capital while paying rent on an identical house

The first renter category does not take into account the Rent Tax Allowance [RTA] currently payable to tenants in the private rented sector, while the second renter category – shown in the right hand column – does. As Table 1 shows, the three cases start with exactly equal levels of gross income, but the two ‘owner’ categories have higher income net of taxation and housing costs than the two renter categories. This arises from the fact that the owners have the benefit of not having to pay housing costs, which of course the renters must pay. The absence of housing costs is not an income as conventionally understood, but it is a real benefit, as Table 1 illustrates. This benefit is usually defined as the *imputed income* from owner occupation. Equity would suggest that the cases should have identical net incomes and the policy logic derived from this type of analysis is that the imputed income from owner occupation should be subject to income tax. The non-taxation of this imputed income, in other words, is a measure of the subsidy to the owners. The nature of imputed income can be clarified by defining it as the rent the ‘occupier’ would pay to the ‘owner’. Where the ‘owner’ and ‘occupier’ are the same person no cash is exchanged but, as Callan’s (1991, p.6) ESRI study of this topic points out, the existence of the imputed income “is none the less real for that”. This logic can also be expressed in algebraic form.<sup>2</sup>

A number of further points should be made about the relative significance of mortgage interest relief and non-taxation of imputed income. First, imputed income will rise over time as properties appreciate in value, while interest relief for any given property will fall as the mortgage is repaid. Second, imputed income arises for those who are outright owners (i.e. without mortgages) as well as for those with a mortgage. From a taxation perspective, therefore, the non-taxation of imputed income is the greater subsidy by far. In other words, the taxation of imputed income would in principle be a far greater extension of the tax base than abolition of mortgage interest relief. It should also be noted that a third, indirect subsidy arises if the capital gain arising on the point of sale of the principal residence is not taxed (as in Ireland and the UK, for example).

2 Compare a renter and a homeowner. Assume their respective houses are identical and that they have the same market value,  $P$ . The renter’s income is  $Y_r$  and the owner’s is  $Y_o$ ;  $i$  is the rate of return on capital,  $t$  is the tax rate on money income, and  $E$  the owner’s equity in his house. If we assume that the owner and renter have equal total incomes (money plus imputed income), then:  $Y_r = Y_o + iE$ . If the renter pays a market rent  $iP$  and the tax rate applies to money but not imputed income, then the renter’s disposable income (after tax and housing costs) is:  $YDr = (1-t)Y_r - iP$ . For the owner, the disposable income is:  $YDo = (1-t)Y_o - I(P-E) + ti(P-E)$ . Here  $P-E$  is amount of the mortgage and the latter two terms are the mortgage interest payment and the interest tax relief. By definition, if the disposable income term for the renter is subtracted from that of the owner it is a measure of the difference between their disposable incomes. This can be shown to be  $iP$ , the non-taxation of imputed income.

Whether mortgage interest relief or non-taxation of imputed income is a more appropriate measure of the subsidy to owner-occupiers depends on the comparison being drawn. The non-taxation of imputed income reflects the advantage of owning versus renting, while interest relief measures the advantage to those who borrow for housing as against borrowing for other items where interest is not tax deductible.

To develop the policy implications of the analysis it is useful to return to the stylised outline in Table 1. A number of interventions might be considered to equalise the outcomes between owners and renters. For example, a tax allowance for rental costs has been introduced in Ireland to 'equalise' the position of the renter. As the fourth column in the table shows, the effect of the RTA is to reduce the arithmetic difference between owning and renting. However, the current situation – with a tax allowance for rent as well as for mortgage interest relief in place – still leaves housing subsidised relative to non housing expenditure. It also constitutes a further narrowing of the tax base relative to a benchmark position without RTA. Another approach would be to abolish mortgage interest tax relief. This would 'equalise' the situations of the mortgagor and the renter, but would still confer an advantage on the owner. Clearly, the intervention that would result in the most equitable, tenure neutral situation (and the greatest extension of the tax base) would be the inclusion of imputed income in the tax base. The development of policy in Ireland has been far from consistent with this underlying logic.

### 1.3 Owner occupation-Policy Development

It is not necessary here to offer a detailed account of the development of the subsidy arrangements towards owner occupied housing: three broad eras can be identified. First, in the period up to 1969 the imputed income from owner occupation was subject to income taxation (known then as Schedule A) and local rates were also levied on residential property; mortgage interest was fully allowable against income tax. While the Commission on Income Taxation (1959) in its *Second Report* argued against this (Schedule A) form of taxation, the Government's 1961 *White Paper on Direct Taxation* supported the principle of taxation of the benefits of owner occupation. In the event the Schedule A regime was abolished.

Second, in the late 1970s a period of very aggressive support for owner occupation was commenced. The remaining tax on owner occupation (local domestic rates payable to local authorities) was abolished, mortgage interest relief was retained, and cash grant schemes were introduced for first time buyers of new dwellings and local authority tenants 'exiting' to private owner occupied housing.

Third, commencing in the early 1980s and continuing to the present day, policy has uneasily altered interventions at the margins within a framework that has not been tenure neutral because of its support for owner occupation. Mortgage interest relief has been restricted to some degree and is now conferred at the standard rate of tax; a limited form of property tax has been in place for short periods, a tax allowance for private rented tenants was introduced (at first for tenants aged over 55 and then on a general basis) and a special payment for tenants in decontrolled rented housing was put in place.



During all of this period capital gains tax has not applied to the sale of principal private residences and the purchase of new homes has not been subject to stamp duty. The weight of subsidies to owner occupation has been very substantial and it led the authoritative analysis of the Commission on Taxation to conclude (First Report, *Direct Taxation*, 1982, p.138):

*We are concerned, however, that many of the present day incentives for housing do not contribute effectively to the stated objectives of housing policy. The tax and other advantages attached to owner occupation have encouraged people to acquire their own houses and have resulted in a very high proportion of owner occupied houses in Ireland by international standards. We consider that owner occupation is a desirable social goal, which should be encouraged by the provision of incentives. However, the present extremely generous treatment of housing for tax purposes has resulted in an undue proportion of investment in certain types of housing to the detriment of more productive uses. Demand in many cases has been increased above real needs which has bid up the price of existing houses making it more difficult for first time buyers to acquire their own homes. It has also led to over investment and trading-up in house property and a waste of scarce resources since the cost of holding on to accommodation in excess of needs is nil.*

In the years since the Commission on Taxation published its report the broad thrust of its critique has been supported by the NESC (NESC, 1990; NESC, 1993) and by other commentaries on Irish housing policy (Tansey, 1989; NESC, 1988).

#### **1.4 Current and Future Policy**

Currently, the owner occupied sector is subsidised by: some element of mortgage interest relief; non taxation of imputed income; exemption from capital gains on the sale of principal private residences; and, exemption of new houses from stamp duty (with some restrictions) as well as cash grants for first time buyers of new homes. The immediate policy question is: in what way is this regime implicated in the housing crisis – both the crisis of affordability in owner occupation and the more general crisis of lack of access to housing? Before offering specific answers to this question a general observation needs to be made about the terms of the recent debate on affordability of housing and the analysis of the Bacon reports (Bacon, 1998; Bacon, 1999). The analysis in these reports, reflecting Bacon's terms of reference, specifically relates to the crisis in affordability in the past two to three years. However, the current problems of the Irish housing system reflect in part the accumulated effects of the long-term pattern of public policy. Undoubtedly, the effects of the demographic, economic and social changes on demand for and prices of houses – so thoroughly analysed in Bacon – have been caused, in part at least, by the basic package of tax and other subsidies which has long been in place for owner occupation.

The first general point to note is that the sheer weight of subsidies to owner occupation channels demand for housing into one sector and correspondingly reduces demand for others. Any efforts to sustain a role for other tenures must contend with the sheer scale of incentives for housing consumers to purchase rather than rent. This has weakened the market for rented accommodation and has left local authority housing to the most financially vulnerable households.

Second, it is widely accepted that owner occupation is a desirable policy goal and that those with modest incomes in particular should be supported in attempting to buy homes. However, the current mix of subsidies is not an equitable way in which to pursue these goals. Recent policy has reduced mortgage interest relief and has left imputed income and capital gains untaxed; the latter two exacerbate the rise in property prices. Therefore, those who benefit most from the current arrangements are higher income owner-occupiers with properties that have appreciated significantly in value. The rise in property values makes it more difficult for those with modest incomes to enter owner occupation and this difficulty is now compounded by the limited amount of mortgage interest relief available.

Third, it is important to emphasise the inequality inherent in the current situation. This *distinctly benefits one group* – owner-occupiers with high incomes and a full or partial equity stake in a house that has appreciated in value. The current tax system allows these households to reap substantial capital gains, to ‘trade-up’ – possibly to a house in excess of accommodation needs – and to benefit from further interest relief. This fuels the rise in prices, which is taking place for natural market and demographic reasons. Meanwhile, low-income persons may be unable to afford a home at current prices.

Fourth, the recent rapid escalation in property prices, underpinned by the tax treatment of owner occupied housing, offers a strong incentive to owners of rented housing to sell. These owners may then sell the properties in the buoyant owner-occupier market, in which case the stock of available rented housing is reduced. Alternatively, the owners may seek substantial rent increases from tenants to reflect the enhanced value of the property; in turn this may cause financial problems for low-income tenants and – in some circumstances – a need for SWA Rent Supplement.

Fifth, the escalation of property prices that generates substantial gains for financially secure stakeholders in the housing system makes it more difficult to meet the housing needs of low income families and those with acute needs. Social housing organisations find it increasingly difficult to obtain affordable rented accommodation to resettle the homeless; more low income tenants will require a Rent Supplement to pay rents (or will seek increased allowances); low income families will need to apply to local authorities for housing, creating further demand for public provision and restricting the choices open to these families.

Finally, reflecting policy-makers’ preoccupation with the encouragement of owner occupation a variety of quite specific grants and subsidies have been used, or are in use, to support access to owner occupation, for example:

- cash grants to first-time buyers of new homes;
- discount sales of local authority dwellings to sitting tenants, and
- a ‘Surrender Grant’ for local authority tenants who move to private, owner occupied housing.

The accumulated evidence and analysis in a variety of studies and commentaries (Baker and O'Brien, 1979; NESC, 1989; Irvine, 1984; Threshold, 1987; Tansey, 1989) suggests that there may be too much emphasis in public policy on maximising the entry to owner occupation. In particular, it may not be appropriate to extend the principle of encouraging owner occupation to the point of giving 'multiple' grants to persons on low incomes to become owner-occupiers. For example, the Mortgage Allowance Scheme currently available to local authority tenants and tenant purchasers offers a direct subsidy of £4,500 to local authority tenants who purchase a private dwelling with a mortgage and return or sell the property to the Local Authority. The subsidy is paid in five instalments directly to the lending agency over a period of five years; and those tenants who are purchasing a new dwelling may also receive the £3,000 New House Grant. The policy interventions designed to increase owner-occupation may have serious flaws. For example;

- 1 The cash grant for first time buyers is likely to be self-defeating as the value of the grant is capitalised in the value of houses;
- 2 The sales schemes reduce the capacity of local authorities to make rented accommodation available to applicants for social housing; and
- 3 The short-lived Surrender Grant and the existing Mortgage Allowance Scheme encourage low-income households into private ownership, leaving these households vulnerable to the financial uncertainties of owner occupation (such as changes in interest rates or family income) and further residualising local authority housing estates.

What implications does this have for policy towards owner occupation in the future? A number of policy proposals have been advanced at various times in academic commentaries and official policy studies. While the details of these proposals differ, they all derive essentially from the policy principles set out above.

The most recent OECD report on the Irish economy (OECD, 1999) points out that housing is currently favoured as a form of investment "since mortgage interest is partially deductible (at the standard rate) and there is no tax on the imputed income from owner occupation" (p.106). The OECD then pointed out that the "bias" could be removed either by phasing out mortgage interest relief (as in the UK) or bringing imputed income into the tax base (as in Switzerland). In addition, the OECD report pointed to the merits of a residential property tax (greater incentives for landowners to use land efficiently and recapturing for the community the capitalised benefits on property of public infrastructure investment)

In the ESRI's national investment priorities report (Fitzgerald et al, 1999) the general principle was advanced that "the State's direct involvement in the housing sector should be confined to social housing and - - - all other grants and tax reliefs should be phased out" (p. xiv). Referring to the *Commission on Taxation*, the ESRI report argued that the use of tax relief to support policy objectives in the housing field is "wholly inappropriate" (p 152.), although it acknowledged a role for "targeted" subsidies. This study pointed out that in current Irish circumstances "granting tax relief to all those seeking accommodation will only serve to raise prices, with the ultimate benefit accruing to the owners of existing dwellings and to owners of zoned and serviced land" (p.152).

In its review of housing policy over a decade ago the National Economic and Social Council (NESC, 1988) recommended a "more balanced treatment of the various tenures" (p.59) and set out a series of proposals in relation to the taxation and subsidy treatment of owner occupied housing. The NESC proposed a general tax on residential property, taxation of real capital gains on the sale of residential property and (only if a general property tax is introduced) full mortgage interest relief at the standard rate of tax (p.23). Overall, the Council advocated a "less generous strategy of subsidising owner occupation" (p.58)

In summary, there is general agreement in the independent analyses of housing policy that the tax treatment of owner occupied housing needs to be reformed. A variety of proposals could be set out which would be consistent with the broad thrust of the kind of commentaries summarised above. What is stressed here is the inequitable nature of the current arrangements and the impact these have on the housing system generally.

### 1.5 Local Authority Tenancies

More briefly in relation to local authority tenants, it is important to note the different roles of the local authority and private rented sectors. Local authority tenants have *de facto* security of tenure (although legally their tenancies are periodic tenancies, like most of their private counterparts). In addition, the tenancies can be 'passed' on within families. Rents in the local authority sector are calculated on a replacement cost basis for maximum rents on dwellings. The rents for each individual letting however are assessed on the basis of the income and family circumstances of the tenant (the differential rent formula). As a substantial proportion of local authority tenants is reliant on social welfare payments, many are paying minimum rents.

In policy terms, local authority housing (less than 10% of the housing stock) has been used by some tenants as a route to owner occupation. Specifically, local authorities occasionally have a tenant purchase scheme, whereby tenants are permitted to purchase their dwelling on discounted terms related to the duration of their tenancy.



These schemes are limited to houses only. While these schemes do not exist as statutory right, they have been a significant part of the regime of local authority housing in the last three decades from which many tenants have benefited. The tenant purchase schemes and the schemes which confer financial subsidies for local authority tenants to buy private houses give local authority tenants a more favourable route to ownership than that available to private tenants.

The significance of a comparison between this tenure and private renting is not that local authority tenants are generally advantaged, but that the tenures draw to some degree from the same potential tenancy population while treating them differently in important respects. Private rented tenants can be subsidised by the State (through the SWA Rent Supplement) and yet have little security of tenure. The net income (after housing costs) of two tenants with the same gross income who have similar quality housing is likely to be very different. There are no representative data on these matters but it is likely that the contrast between tenures may actually be perverse in some instances: some local authority tenants may have distinctly better housing circumstances than tenants with the same income being subsidised through SWA Rent Supplement. The converse could also be true.

Overall, the role of local authority tenancies in Irish housing was one of providing a housing alternative for those unable to afford owner occupation. Now, however, with the private rented sector meeting the needs of many low-income tenants in receipt of a Rent Supplement the potential for serious horizontal inequity exists. Specifically, if the private rented sector is to meet these needs a more neutral policy as between it and local authorities will be necessary.

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## Chapter Two – Private Rented Housing

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### 2.1 Introduction

According to the well-known study on the topic, private rented housing in Ireland is the “forgotten sector” (Dillon and O’Brien, 1982). The essential logic of that description was that historically private rented housing in Ireland received little policy attention relative to the other tenures and that a consequence of this policy neglect was the absolute and proportionate decline in the role of private rented accommodation in the housing system. Before describing this ‘decline’ and placing it in comparative context the implications of a limited and poor quality private rented sector for public policy should first be noted.

In principle, private rented housing might offer quick access to affordable housing to mobile households or those on low incomes, or individuals and families in the early stages of their housing career and family cycle. If this tenure is substantially weakened it requires an enlarged role for the State and local authorities in meeting housing need. At a time of very rapid economic growth and employment growth – such as Ireland is currently experiencing – there will be a significant demand for rented accommodation from an increasingly mobile labour force. *Ceteris paribus*, a well functioning private rental market can respond more quickly in the short term to changes in housing needs and demands than direct state provision.

The remainder of this chapter is divided as follows. First, the basic attributes of the private rented sector are set out in terms of size, tenancy population, rent levels, and so on. This brief description is then put in the context of the evolution of policy in relation to the tenure. Second, a comparative overview is given of the private rented sector and the lessons that might be inferred from the policies and experiences of other countries.

An important preliminary point concerns the absence of basic data in Ireland on private rented housing. Over ten years ago the Council of the NESC prefaced its comments on the rented sector with the following statement (NESC, 1988, p.34):

*It will be an essential step in policy formulation to undertake basic research on this part of the (housing system), as there is a dearth of data on basic aspects of the tenure:*

- *the economic and social characteristics of tenants and of owners of rented accommodation*
- *the physical quality of the accommodation*
- *the rates of return to landlords’ investments*
- *the factors which determine the housing choices of tenants and the investment and supply choices of investors and landlords.*

No improvement has been made in the quality of the available official data in the intervening period. Some secondary data are available in the annual Labour Force Surveys on tenure, rent levels, and related variables; the *Household Budget Surveys* (undertaken every 7 years since 1966) likewise contains data on tenure, housing – related expenditure, income, household and demographic composition and so on.

The *Census of Population* is undertaken every 5 years and contains data on household structure, household and family size and other demographic and socio-economic data, but the question on housing tenure is included only in the decennial census. The annual and quarterly *Housing Statistics Bulletin* publishes material on housing activity (output, prices, sales, etc), housing finance, and housing need.

However, much of the official data are collected as a by-product of more general data collection exercises and the sample sizes, coverage, and publication formats all combine to considerably limit the value of the available data. For example, the *Census of Population* is the only body of data that contains figures on the number of households, families and dwellings in each tenure – these data are not published in appropriate form. While the *Labour Force Survey* (now named the *Quarterly National Household Survey*) collects tenure and rent and household data for a very large sample of households, the relevant publications do not contain these data. Unlike the UK and other jurisdictions there is no regular, dedicated survey of housing conditions and needs in Ireland. Analysts can make ingenious use of the available data, but it is clear that at a time of rapid change in the housing market more systematic, representative data is needed on the private rented sector in particular. Using existing published data it is not even possible to give a representative picture of current rent levels in the private rented sector – still less to discern accurately what the rate of increase in rent levels has been. Against this background it is important to stress that any attempt to devise future policies will be hampered by an absence of very basic data.

## 2.2 The Private Rented Sector

The data below give a descriptive account of the characteristics of the private rented sector in Ireland under a number of distinct headings, commencing with some relevant data on the size of the private rented sector.

### Size

Table 2 below records the shares of the various tenures in the Irish housing stock in recent decades.

**Table 2: Housing in Ireland by Tenure (%)**

Tenure	1961	1971	1981	1991
L. A. Rented	18.4	15.5	12.4	9.7
Owner Occup.	59.8	70.8	74.4	79.3
<b>Private Rented</b>	<b>17.2</b>	<b>13.3</b>	<b>10.1</b>	<b>6.3</b>
Other	4.6	2.4	3.0	3.0
Total	100.	100.	100.	100.

Source: *Census of Population*, various.

Note: Some data refer to dwellings others to households

## Chapter Two – Private Rented Housing

It is clear that the private rented sector has experienced a period long run *decline*, measured as a share of the total housing system. This long run trend is mirrored in many other countries (as will be seen in the next section). Further details on the size of the private rented sector can be seen in Table 3, which summarises relevant data for the last two decennial censuses.

**Table 3: Trends in Private Rented Housing 1981-1991**

Unit	1981	1991	% Change
Private Dwellings	90,315	81,424	- 9.8
Persons in Dwellings	222,756	185,471	-16.7
Permanent Private Housing Units	71,147	70,912	- 0.3
Dwellings/Units	1.27	1.15	- 9.4

*Source: Census of Population, 1981; Census of Population, 1991. A dwelling refers to the room or set of rooms occupied by a private household; a housing unit is a house or a structurally separate flat regardless of the number of households; a household refers to a person, or to a group of persons living together.*

The decline in the sector has continued into the early years of this decade – the national decline in the number of persons in private rented was 16.7% from 1981-1991. Separate data are given in Table 4 on the major urban areas. The declining ratio of dwellings to units shows the degree of decline in multiple dwelling/multiple household units up to 1991.

**Table 4: Trends in Private Rented Housing,  
Major Urban Areas, 1981-1991**

Area	Unit	1981	1991	% Change
Dublin	Dwellings	40,834	36,351	- 11.0
	PHUs	27,449	29,411	+ 7.1
	Ratio Dw/ PHUs	1.49	1.20	- 19.5
Cork	Dwellings	6,932	5,166	- 25.5
	PHUs	5,210	4,289	- 17.7
	RatioDw/PHUs	1.33	1.20	- 9.8
Limerick	Dwellings	2,163	1,805	- 16.6
	PHUs	1,716	1,525	- 11.1
	Ratio Dw/PHUs	1.26	1.18	- 6.3
Galway	Dwellings	N.A.	2,907	N.A.
	PHUs	N.A.	2,656	N.A.
	Ratio Dw/PHUs	N.A.	1.09	N.A.
Waterford	Dwellings	1,158	1,108	- 4.3
	PHUs	969	988	+ 2.3
	Ratio Dw/PHUs	1.19	1.12	- 5.9

*Source: Census of Population 1981, 1991.*

*Notes: N.A. is not available. Dublin includes all of the Dublin Boroughs and Dun Laoghaire/Rathdown. The other areas include only their respective Co. Borough, i.e. city areas. Dw and PHU respectively refer to dwellings and permanent housing units.*



The broad pattern is confirmed in greater detail in Table 4, showing the significant decline in all of the urban areas in the number of dwellings; the trend in relation to the more aggregated data for PHUs is less severe, with two areas, Dublin and Waterford, recording an increase.

There are no housing tenure data available for the 1996 Census and it is therefore not possible to establish definitively what the trends since 1991 have been. One indication of trends is the information on *household* units in the annual *Labour Force Survey*. The overall rate of household formation has accelerated in recent years, reflecting underlying changes in the economy and the labour market: the *Labour Force Survey* estimates of the number of households shows an increase of 120,000 over the period 1991-1997 – an annual average rate of increase of 1.8%. These data are not available on a tenure basis. However, it would be improbable if some of this increase in households did not arise in the private rented sector, partly because so much of increased housing demand is in the appropriate age group for renting and partly also because of the affordability problem in owner occupation (Bacon, 1998). It is reasonable to assume therefore that the rented sector has grown, measured in terms of *households*.<sup>3</sup> Table 5 below gives hitherto unpublished *Labour Force Survey* data classified by tenure for one year – 1997 – along with 1991 *Census* data.

**Table 5: Households in Ireland by Tenure in 1991 and 1997  
(Estimated), Classified by Tenure**

Tenure	1991 (000s)	%	1997 (000s)	%	% Change
Local Auth. Rented	98.9	9.7	92.7	7.8	- 6.3
Owner Occupied	808.4	79.2	944.9	79.3	+16.9
<b>Private Rented</b>	<b>81.4</b>	<b>8.0</b>	<b>131.5</b>	<b>11.0</b>	<b>+61.5</b>
Other	31.0	3.0	22.8	1.9	- 26.5
All	1,019.7	100.	1,191.9	100.	+16.9

Source: *Census of Population 1991, Special Tabulations; 1997 Labour Force Survey, Special Tabulations*

Table 5 shows that the number of private rented households has, in fact, grown very markedly in the period 1991-1997 – a growth of over 60%, which has increased the share of private rented households to 11% of the total. An important qualification about the trends indicated in Table 5 should be noted. First, the procedures for identification of households differ as between the Census and the *Labour Force Survey* [LFS] – the former referring to *usual residence* and the latter to *de facto* household composition when the LFS interview is undertaken. For any given population, the *Census* procedure will offer a lower number of households. Therefore, the comparison between a 1991 Census figure and a 1997 LFS figure *overstates* the rise in the number of households. Second, the figures in Table 5 refer to households rather than the physical housing stock (in the terms of the *Census* and the LFS a household is “a person or group of persons living together”).

<sup>3</sup> These Labour Force Survey figures refer to *households* rather than housing *units*. Furthermore, there is an important difference in the definition of household as between the Census and the Labour Force Survey: the former referring to *usual residence* and the latter to *de facto* residence at the time of the survey. The effect of this difference is to record a higher number of households for the LFS than the Census for any given population.

When account is taken of trends in the number of housing units a somewhat different picture emerges.

In 1991, there were 70,912 private rented units (Table 3 above). In the years 1991–1998 inclusive a total of over 212,000 new completions have been added to the total housing stock. If about 20% of these were added to the private rented stock it would bring the total number of private rented housing units in 1998 to about 90,000 (leaving aside the losses to the stock from tenure changes, obsolescence and demolition, and *other additions* through tenure change). Of the 212,000 units, approximately 37,000 are apartments or flats, and a significant proportion of these is in the private rented sector. If the assumption were made that *all* of the apartments and flats were added to the private rented stock, it would imply that the total number of private housing units rose to a figure in the region of 100,000 by 1998. Taken together, the data on households and housing units suggest that the absolute size of the private rented sector has risen during this decade. However, it would be premature to conclude that the long run trend of a falling *share* for the private rented sector in the physical stock housing has been reversed. Finally, if the number of households in private rented has risen very rapidly at a time when the number of housing units appears to have grown much less rapidly it may be indicative of a deterioration in the housing units/persons ratio, with more units containing multiple households.

### Quality

Turning from the size of the sector to its quality, one of the important aspects to examine is the *age* of the stock, data on which are given in Table 6. The key point to note in Table 6 is the relatively advanced age of the private rented stock in 1991. Over one third of the stock at that point was built pre-1919 and a further 12.5% were built in the 1919–1940 period: close to a half of the stock was 60 years old (almost) in 1991. This age profile will have been altered since the 1991 Census because of the scale of new build across all tenures. If the illustrative assumptions given above about the likely addition in recent years to the rented stock are adopted, then *ceteris paribus* the proportion aged pre-1919 is currently around 30%, and the respective figure for (almost) 60 years is a further 10%.<sup>4</sup>

The age of dwellings is at best an indirect measure of dwelling quality. Unfortunately, there are no published data on the physical quality of private rented dwellings with the exception of the census data on dwellings' heating systems. Some summary data by tenure are given in Table 7. Here it can be seen that in the private rented sector there is a significantly higher reliance on basic heating systems. Over one third of dwellings in this tenure (37%) in 1991 used either simple portable heaters or open fires as the principal heating source – this compares with a mere 5% in the owner occupied sector.

<sup>4</sup> Other factors will of course affect the changing age profile of the tenures – losses through demolition and changes in the tenure of dwellings, for example.

**Table 6: Percentage Distribution of Permanent Private Housing Units in Ireland, 1991, in Selected Tenures, classified by Period in which Built**

Period	Private Rented	Local Authority	Own Mortgage	Own Outright	All
Pre 1919	35.1	3.4	7.7	32.6	19.7
1919-1940	12.5	7.3	7.7	19.9	12.9
1941-1960	8.9	14.4	12.5	17.2	14.2
1961-1970	7.0	14.8	12.5	9.7	12.1
1971-1980	14.3	30.3	31.8	12.6	22.1
1981-1985	8.7	19.5	15.6	4.5	10.9
1986 +	8.3	8.4	11.6	2.5	7.3
Not Stated	5.1	1.8	0.5	0.8	1.3
Total	100.	100.	100.	100.	100.
N	70, 912	97,742	420,642	386, 697	1,006,506

Source: Census of Population 1991, Special Tabulations

Notes: The Category All includes the residual Not Stated and Free of Rent tenures.

**Table 7: Percent of dwellings in Ireland with open fire or portable heaters as the principal source of heating, 1991, Selected Tenures**

Tenure	No.	% of Total
Local Auth. Rent	23,904	24.2
Own. Outright	67,113	5.8
Own. Mortgage	17,876	5.0
Own L.A Mortgage	11,010	16.9
Private Rent	30,237	37.1
All Dwellings	157,332	6.5

Source: Census of Population 1991, Vol. 10.

*Tenant Population***Table 8: Percentage Distribution of Households in each Tenure in Ireland Classified by Age of Head of Household**

Age of HoH	Own Outright	Own Mortgage	Tenant Purchase	Local Auth. Rented	Private Rented	Other	All
-24	0.3*	1.3	0.0	3.5	32.0	9.8	2.8
25-34	2.8	20.0	1.5*	23.0	47.7	13.1	13.3
35-44	9.5	36.0	7.5*	26.1	6.5	13.1	20.4
45-54	17.4	27.0	16.4	20.1	4.6	14.8	20.4
55-64	25.2	11.1	17.9	10.4	2.6	3.3	17.0
65+	44.8	4.6	58.2	16.1	6.5	45.9	26.0
Total	100.	100.	100.	100.	100.	100.	100.
N	1306	1049	67	233	153	61	2866

\* These cells are based on very small numbers ( $n < 5$ )

Source: Living in Ireland Survey 1997 Panel

Before considering rent levels a summary profile of the private rented population is offered, based on an analysis of relevant data in the 1997 panel of the ESRI's *Living in Ireland Survey*<sup>5</sup>. The data on age in Table 8 confirm the relative youth of the population in the sector. Just under a third are 24 or younger, and close to a half is aged 25–34, giving almost 80% in the age category 34 or younger. Private rented households are largely adult, non-family households, as Table 9 shows. Only a small proportion of households is comprised of couples with children and the most common form of household by far is the one-adult household. The general pattern of younger, non-family households is confirmed in the data on marital status in Table 10: nearly 60% of private rented household heads are single and a further 10% are separated or divorced.

Finally in relation to the tenant population, the available data are not adequate to give a detailed analysis of their socio-economic characteristics. Private rented tenants appear from the limited data in the LIS 1997 panel to be representative of the socio-economic spectrum. The unemployment rate (see Table 11) is close to that for all households. The proportion deemed poor on the basis of the 50% of average income line is 20.6%, and the proportion in the lowest fifth of the income distribution is marginally above 20%. More complete data on the location of private rented households in the income distribution (not given here) shows a disproportionate rate in the highest income quintile. This is indicative of a pattern found in many countries— a bimodal shape to the income profile in the sector, with some households in the lowest income category and a distinct set of households in the highest category.

**Table 9: Percentage Distribution of Households in each Tenure in Ireland by Type of Household**

H'hold Type	Own Outright	Own Mortgage	Tenant Purchase	Local Auth. Rented	Private Rented	Other	All
1 Adult	17.3	4.3	34.3	11.2	31.0	50.0	14.0
2 Adults	28.0	16.0	22.4	9.4	22.4	20.6	21.8
3 or more Adults	25.3	11.5	26.9	12.4	18.6	8.1	18.8
2 Adults, 1 Child	1.2	7.8		5.5	9.3	6.5	4.5
2 Adults, 2 Child.	1.8	9.8		3.9	4.3	1.6*	0.5
2 Adults, 3+ Child	1.2	5.4		7.3	1.9*		3.2
1 Adult, Children	0.3	0.4		3.9	6.2	1.6*	1.0
3+ Adults, Child.	23.0	44.7	16.4	46.4	6.2	9.7	31.6
Total	100.	100.	100.	100.	100.	100.	100.
N	1365	1088	67	233	153	62	2976

\* These cells are based on very small numbers ( $n < 5$ )

Notes: Children are those persons aged 0-14

Source: *Living in Ireland Survey, 1997 Panel*

5 The 1997 panel of the LIS data contains just under 3,000 households. In the tables used here the sample size for the private rented sector is just over 150. While this sample is small it is nationally representative.



**Table 10: Percentage Distribution of Households in Ireland Classified by Marital Status of Head of Household**

Marital Status	Owned Outright	Own Mortgage	Tenant Purchase	Local Authority	Private Rented	Other	All
Married	63.4	87.9	52.2	55.2	29.3	27.9	68.9
Separated, Divorced	2.1	2.9	3.0*	13.0	9.2	4.9	3.7
Widowed	21.8	3.2	23.9	15.2	3.3	23.0	13.6
Single	12.7	6.0	20.9	16.5	58.2	44.3	13.9
Total	100.	100.	100.	100.	100.	100.	100.
All	1306	1049	67	230	153	61	2866

Source: *Living in Ireland Survey, 1997 Panel*

Notes: The Married category includes Cohabiting couples and Married persons living with a partner other than their spouse; Single refers to never-married; Separated, Divorced etc refers to formerly married persons not living with a partner.

**Table 11: Summary Data on Socio-Economic Characteristics of Heads of Households, Classified by Tenure-Percent of HoHs in Certain Categories**

Category	Own Outright	Own Mortgage	Tenant Purchase	Local Authority	Private Rented	Other	All
Unemployed	5.6	5.2	10.4	34.1	10.0	3.2*	8.0
"Poor"	22.8	11.4	31.3	51.9	20.6	41.9	21.4
Low Income	21.3	11.1	23.9	49.8	20.0	31.0	20.0

Source: *Living in Ireland Survey 1997 Panel*

Notes: Unemployed includes first time job seekers, people on 'schemes'; Poor refers to income below 50% of average income per capita equivalent; Low Income refers to income in the lowest quintile of the income distribution; \* these cells are based on very small numbers.

### Rent Levels

Any discussion of rent levels is severely impeded by the absence of up-to-date representative data.<sup>6</sup> Table 12 records some summary data drawn from a variety of sources. The first point to note from the data is the medium term trend in rent levels revealed by the *Household Budget Survey* data for 1987 and 1994. These data (based on samples in excess of 500 in both years) record an annual average rate of increase in rents of 11.5%; average rent in the private rented sector was IR£25.27 in 1987 and IR£54.49 in 1994.<sup>7</sup> A comparison with the rate of increase in the Consumer Price Index shows a very marked increase in the relative cost of housing.

<sup>6</sup> The relevant volume of the Census contains data on rents by tenure grouped by broad categories. However, these are only collected in the decennial Census and published some years after the year to which they refer. The *Labour Force Survey* questionnaire has a question on tenure and rent level, but these data have never been published. The *Household Budget Survey* is undertaken every seven years and data on rent and tenure and related variables are contained in the relevant volume and are also available for secondary analysis.

<sup>7</sup> When the calculation of the rent increase takes account of household size by first dividing the average rent by the average number of persons per household in the private rented sector, it does not affect the rate of

A second series of figures relates to expenditure on the SWA Rent Supplement. In current prices this rose from an insignificant figure in the late 1980s to a figure now estimated to be in excess of £100m. The reasons for the initial dramatic rise are well known and understood – a combination of changes in housing policy, economic and labour market conditions, and social and demographic change (see Government of Ireland, 1996). What is striking, however, is the continued rate of increase in the period from 1994 to 1999. This is *not* due solely to an increase in the number of recipients. On the contrary – although the published data on this scheme are very limited – the rise in the last two years is due significantly to increases in rent levels. The total level of recipient demand rose by just under 40% from 1994 to 1998. However, the average expenditure per case increased by 66% over the same period. (Department of the Environment, 1999, pp.5-6) Therefore, the rate of increase in expenditure on the scheme is broadly indicative of trends in rent levels at the ‘lower’ end of the rental market.<sup>8</sup>

**Table 12: Summary Data on Rents in Ireland, 1987-1999**

<b>Household Budget Survey</b>	Average Rent 1987 £p.w.per household	25.27
	Average Rent 1994 £p.w.	54.49
	Annual Average Increase %	11.48
	CPI Annual Increase %	2.81
<b>SWA Rent Supplement</b>	Total Expenditure 1989 £m	6.10
	Total Expenditure 1994 £m	44.80
	Total Expenditure 1999 £m( estimated)	103.00
	Annual Average Increase 1994-99 %	18.12
<b>Threshold Survey (1997/8)</b>	Average Rent-Low Income £p.w.	62.64
	Households facing Rent Increases %	42.00
	Households with SWA Rent Allow. %	31.00
<b>Living in Ireland (1997)</b>	Mean Rent £p.w.	52.87
	Households with SWA Rent Allow. %	30.60

*Sources: Household Budget Surveys 1987 vol.1, 1994, vol.2; Downey and Devilly (1998); Living in Ireland Survey, 1997 Panel; Department of Social, Community and Family Affairs (unpublished data).*

This interpretation is confirmed by the administrative data on the scheme. The Health Boards specify a ‘reasonable’ rent for purposes of assessing applications. This figure is reviewed annually in the light of local rent levels being charged. In the Eastern Health Board area the ‘reasonable’ weekly figure rose from £35 to £60 from 1996 to 1999 – an annual rate of increase of over 14%. The pattern of rapidly rising rent levels in the lower end of the market is confirmed in *Threshold’s* data for 1997/8. These data are based on a questionnaire completed in respect of 300 tenancies and show that over 42 % had incurred – or would incur – rent increases in 1997/8. In 1997/8 tenants in the income bracket £7000-£9000 per annum were paying on average £62.64 per week. Just under a third of those surveyed by *Threshold* were in receipt of a rent supplement. The *Living in Ireland Survey* data are based on a small sample and the estimate of the 1997 rent levels is subject to a wide margin of error. However, the mean rent figure it suggests for 1997 is broadly consistent with the 1998 *Threshold* data. The *LIS* figures also confirm the high penetration of the Rent Supplement system of the private rented market.

<sup>8</sup> This interpretation is supported by the discussions held with relevant officials.

Data collected by the Institute of Auctioneer and Valuers of Ireland [IAVI] and the Institute of Professional Auctioneers and Valuers [IPAV], reproduced in the second Bacon report (1999, pp. 23–24, Tables 2.7–2.8) and given below in Tables 13 and 14, confirm the picture conveyed in Table 12. The IAVI data offer figures on monthly rent levels for a wide range of accommodation in what the IAVI classify as ‘good’ and ‘average’ locations, although the data are confined to Dublin. Rents have increased significantly in the Dublin area according to these data and the increases seem to affect both the upper and lower ends of the market. For example, at the lower end of the market, the Dublin figures for older 1-bedroom flats show an average rent of £425 in an average location, an increase of 11.8% on the previous year. This suggests that the cost of modest rented accommodation for one person in Dublin is now in excess of £100 per week. The corresponding rent increases for older 3-bedroom semi-detached houses and newer 3-bedroom semi-detached houses are also about 12 %: the respective monthly rents for these types of property in Dublin in 1998 were £680 and £730.

**Table 13: Rent per Month (£) in 1997 and 1998 in Dublin  
by Type of Property and Location**

Type of Property	Good Location			Average Location		
	1997	1998	% Change	1997	1998	% change
Older 1-bed flat	415	480	15.7	380	425	11.8
Modern 1-bed flat	510	570	11.8	470	500	6.4
Older 2-bed flat	630	690	9.5	530	600	13.2
Modern 2-bed apt.	670	810	20.1	625	725	16.0
Luxury Penthouse	1,450	1,500	3.4	930	1,100	18.3
Older 3-bed semi	680	740	8.8	610	680	11.5
Modern 3-bed semi	770	880	14.3	650	730	12.3
Older 4-bed semi	840	1,075*	28.0	750	900	20.0
Modern 4-bed semi	1,000	1,250	25.0	850	1,000	17.6
Luxury detached house	1,650	2,200	33.3	1,300	1,650	26.9

Source: Bacon (1999), Table 2.7.

The IPAV survey of changes in rent levels for houses and apartments further confirm the impression of rapidly rising rent levels. These data – also reproduced by Bacon (1999, Table 2.8) – and given below in Table 14, give the IPAV results by region (with Dublin figures given separately) showing percent changes in rent for the period January to July 1998, classified by range of monthly rent. Rents for houses and apartments in the lower end of the market in particular seem to be increasing significantly, according to these data. For example, there was an 8% increase in the rent for apartments in the under-£400 per month category in Dublin for the January-to-July’98 period. The corresponding figure for houses was 8.3%. On average, across all price ranges for both houses and apartments, the percentage increase for the period in Dublin was 8.7%. In all regions, the detailed IPAV figures suggest that rent increases seem to be greater in the lower end of the market.

**Table 14: IPAV Survey of Rent Increases for Houses and Apartments, Classified by Area and Price Range, January to July 1998 (Percent changes)**

Area	Apartments £ per month					Houses £ per month					
	<400	400-600	600-800	800-1000	1000+	<400	400-600	600-800	800-1000	1000+	Average
Dublin	8.0	12.6	9.5	5.0	6.0	8.3	14.0	10.0	6.3	7.5	8.7
Leinster	5.3	3.9	2.0	2.0	2.0	6.3	4.9	2.0	2.0	2.0	3.2
Munster	4.4	3.6	1.3	0.7	1.1	4.2	3.9	2.1	0.9	2.9	2.5
Connaught	6.8	6.7	1.4	0.8	0.7	6.9	4.5	2.0	2.3	2.3	3.4
Ulster	0.0	0.0	0.0	0.0	0.0	2.9	3.2	3.2	3.2	3.2	1.6
Average	4.9	4.5	4.5	1.3	1.4	5.7	4.9	2.7	2.2	2.8	3.2

Source: Bacon (1999, Table 2.8), based on IPAV Survey

The data in Tables 13 and 14 refer to 1997 and 1998. There are no corresponding tables available for 1999 in the case of the IAV1 survey, but the tables from the IPAV's National Property Survey for 1999 are available; the figures for January to July 1999 corresponding to Table 14 are given in Table 15.

**Table 15: IPAV Survey of Rent Increases for Houses and Apartments, Classified by Area and Price Range, January to July 1999 (Percent Changes)**

Area	Apartments					Houses					
	<400	400-600	600-800	800-1000	1000+	<400	400-600	600-800	800-1000	1000+	Average
Dublin	17.9	12.6	10.4	2.5	2.5	19.3	12.9	12.0	5.0	5.0	10.0
Leinster	5.4	3.3	1.6	0.3	2.1	7.1	4.7	2.2	0.6	2.9	3.0
Munster	6.7	2.8	1.8	0.8	2.4	5.6	3.5	1.5	1.0	2.3	2.8
Connaught	4.4	2.9	1.6	1.3	2.0	4.4	3.5	1.3	0.0	1.8	2.3
Ulster	4.2	6.7	10.0	10.0	6.2	4.4	3.3	7.5	7.5	4.6	6.4
Average	5.8	3.7	2.4	1.3	1.3	6.1	4.0	2.3	1.2	2.4	3.1

Source: IPAV National Property Survey, 1999, Residential, Table 3.

In the first six months of 1999 the trend of rising rent levels seems to have continued. For example, the average rate of increase in Dublin was 10%, with the lower priced properties subject to much sharper rates of increase. A rise of almost one fifth was recorded for houses in Dublin in the lowest rent category. This tentative analysis of rent levels confirms the general impression of rapidly rising rent levels. These reflect an underlying trend that has become accentuated in the past five years and that may be affecting the lower ends of the market in particular. There may be a crisis in rented 'affordability' to match that of the affordability crisis in owner occupation. It is simply not possible to say with the data



available how much of the rise in rents can be ascribed to changes in the overall *quality* of rented accommodation, nor is it possible to analyse the patterns of rent increase by locality, quality of accommodation, or income of tenants.<sup>9</sup>

### 2.3 Comparative Context

This section offers an overview of some relevant international literature on private rented housing. Irish commentators on housing policy tend to start from an assumption that the Irish private rented sector is somehow qualitatively very different from its European counterparts. In 1982, in *The Forgotten Sector*, Threshold referred to the “many other Western nations who for most of this century had endeavoured to build strong private rented sectors along with other tenures” (Dillon and O’Brien, 1982, p. 29). More recently, Galligan contrasted the role of institutional investors in Europe with their absence from the tenure in Ireland. She invoked the experience of European and other countries as a potential source of policy lessons for Ireland, and referred in particular to the “cost rental accommodation available in Germany, the Netherlands and Australia” (Galligan, 1998). It is therefore useful at this point to start with a simple comparison of the share of private rented accommodation in other countries’ housing systems to see to what extent Ireland stands in contrast with other countries.

**Table 16: Share of Private Rented Accommodation in Total Stock, Ireland and Selected Countries, early 1990s**

Country	% Share
Ireland	7.0
UK	10.0
USA	32.6
Canada	28.0
Denmark	19.5
Sweden	20.0
Netherlands	11.0
Germany	39.3
France	22.0

Notes: The Irish figure refers to permanent private housing units

Source: CSO, Kemp (1998), Crook (1998), Premus (1998), Malpezzi (1998), Lunde (1999), Hubert (1998)

Table 16 shows the relevant data for the early 1990s. The contrast is striking, with Ireland’s share significantly below 10%. It is also striking that the highest figure in the selection is for the USA, almost 33%, with Canada having a figure close to 30%. These figures highlight the possible diversity of factors that affect the relative sizes of countries’ rented sectors. Among the European countries, Germany’s figure of 39% is the highest, with Denmark, Sweden and France having figures in the region of 20%. However, too much should not be made of the arithmetical contrast between Ireland and these European

9 The IPAV survey does not give details about the sample or the data collection procedures. Nor does the survey document show annual rates of increase, or indicate whether the rental categories refer to the rent levels before or after the time period being surveyed. For these reasons, individual figures shown in the tables above should be treated with caution.

countries, as the historical trend in the share of the European (although not the North American) countries' rented housing been one of long term decline. For example, the private rented share for the UK fell from 50% in 1951 to 10% in 1991. Sweden too has experienced long term decline; the share fell from 52% in 1945 to 20% in 1990, and the respective figures for the Netherlands (1947 and 1993) are 60% and 11%. Ireland's pattern of a historical contraction of the sector is therefore far from unique. On the contrary, Ireland's experience is in some respects reflected in other countries and the challenges faced by policy makers are somewhat similar across countries. Before attempting to summarise the detail of some countries' rented sectors, it is useful to outline some of the broad historical patterns identified in the comparative research (Harloe, 1985; Doling 1997; Mc Crone and Stephens, 1995; Donnison, 1982).

In all of the countries studied in the standard comparative accounts, private rented accommodation acquired political salience (and hence state intervention) in the years immediately before or after the First World War. These were years when the urbanised, industrialised working classes were highly politicised and basic housing conditions were the source of class conflict. The landlord class was politically less organised and not part of the state/capital elite. This provided the political context that facilitated governments of various political persuasions to intervene in the market for private rented housing.

Also, in many countries, the timing of intervention and the nature of the intervention were very similar. Wartime inflation after 1914 and again wartime economic conditions after 1939 provided the context impelling governments to intervene. Usually – for instance in Germany, Ireland, the UK, France and other countries the intervention took the form of rent control- a ceiling on rent levels expressed in nominal prices. Countries varied in the speed and degree of sophistication with they later attempted to rationalise their initial rent control system, but all countries quickly learned that the existence of a strict rent control regime sowed the seeds of later problems.

Even with rent control most European countries had learned by 1945 or so that “very little had changed in the inability of the private landlord to provide adequate lower income housing” (Harloe, 1995). Consequently, many European countries – Ireland, the UK, France and Denmark, for example, began to develop good quality municipal housing on a substantial scale. This changed the character of countries' rented sectors into a dual sector: private commercial renting and public, municipal renting. An exception to this was Sweden, which developed a “unitary” rental sector (Kemeny, 1991). In this system public and private rented housing are dealt with as parts of one overall rented tenure. Both parts of this tenure have been co-ordinated, regulated and managed in such a way as to create an overlap between ‘public’ and ‘private’ renting in rent levels, tenant population, quality of accommodation and access to rented accommodation

In 1945 most countries had over half of the housing stock-and in some cases over 60%-in private rented and by the end of the 1970s among West European countries only Germany and Switzerland had more than a third in this tenure. Regulation was common in all European countries, but it was not necessarily this factor which led to the long term diminution of the sector, as Harloe (1985, p. 297) has forcefully argued:

*As we have seen, the decline in private rented housing is not confined, as some allege, to countries with 'anti landlord' policies such as strict rent controls. While such policies have of course had their impact the reasons for decline are more complex and deep rooted and in some respects pre date the first imposition of controls.*

By the middle of the 20th century much of the stock of private rented accommodation was old, and comprised largely of poorer quality inner city flats which compared rather badly with the newly emerging municipal housing in European countries. This weakness was later compounded in the 1970s and 1980s when Governments began to address the need for inner city redevelopment and urban renewal. In pursuit of these objectives there was considerable demolition or refurbishment, resulting in a combination of loss of further rented stock and a change in the tenure status.

By the 1960s, countries' rented stocks were increasingly affected by growing and chronic inflation. On the demand side, while tenants' incomes were rising in real terms, they were rising less rapidly than incomes in general, imposing a cost squeeze on tenants. On the supply side, the largely buoyant but increasingly inflationary economies in Europe were generating long term appreciation in property values inducing many owners to sell off stock into owner-occupation.

In the decades after 1945 the degree of political support for private rented accommodation declined in some countries. One pattern – exemplified most strongly by Ireland and Britain – is of increasingly widening support for owner occupation across the political spectrum, with the Left and Right respectively tending to emphasise either public, municipal, provision or owner occupation. A variant on this pattern was the emphasis on non-commercial or voluntary or co-operative housing in countries such as Denmark, Germany and Holland, reflecting the stronger social democratic tradition in those countries.

Since the late 1970s/early 1980s the broad policy direction being followed across countries is characterised by:

- A general tendency towards less comprehensive regulation of private rented housing;
- A greater role for housing allowances paid to tenants rather than direct public provision of rented housing, and
- A renewed recognition of the potential role of the sector and a search for new incentives to increase investment and supply.

Finally, it is important to recognise that despite the long run trajectory of the tenure there is nothing inescapable or pre-determined about its declining share. The sector's history to date has been shaped in part by evolving political forces and social circumstances – and these can change. The brief vignettes given below about other countries' experiences illustrate the general patterns summarised above.

Table 17 offers a useful typology. On the one hand, there are countries with very large rented sectors (taking public and private rented in aggregate). These countries can be subdivided into those with dominant private rented renting within the rented sector and those where social renting is the larger of the two sub sectors. On the other, there are countries in which ownership dominates. Ireland is therefore in the top half of the typology and in the same cell as the UK, with private renting as a residual sector. This cell can be compared with the top right hand corner: here there are countries with moderately large private rental sectors such as Denmark.<sup>10</sup>

**Table 17: Classification of Countries according to Tenure Shares, Circa 1990**

<b>Ownership Vs Renting</b>	<b>Social renting &gt; Private Renting</b>	<b>Private Renting &gt; Social renting</b>
<b>Ownership exceeds all Renting</b>	UK, Ireland	Austria, Denmark, USA, Canada, France
<b>All renting exceeds ownership</b>	Sweden, Netherlands	Germany, Switzerland

*Source: MacLennan (1998)*

### **United Kingdom**

Like Ireland's, the UK's rented sector has been subject to "almost continuous decline since the early years of the century" (Kemp, 1998). This reflects the preference given to owner occupation in policy and subsidies (often leaving the sector with no specific incentives for new investment and supply), the growth till the 1980s of municipal housing as the housing of those on lower incomes, and the cumulative effect of increasingly complex rent control legislation. Currently, small landlords underpin the sector, with institutional investors playing only a marginal role. The tenants are from the 'tails' of the income distribution with one segment of very low-income households and another with very high incomes. At the lower end the sector is substantially subsidised by housing benefits and the state is "clearly an important determinant of effective demand in the private rented sector" (Kemp, 1998).

On average, the housing stock is of inferior quality and older than municipal housing or owner-occupier housing. Rent control has had a chequered history, commencing with the Rent Control Act of 1915 and continuing in comprehensive form through to the 1988 Housing Act. Rent control continued in the 1920s and 1930s, reflecting the views of the Onslow Committee's report of 1923. Wartime controls were re-imposed in 1939 and in 1945, following the Ridley Committee's report, a process of establishing the Rent Tribunal system began. In the 1950s, the Conservative government liberalised the rent regime by establishing a formula for maximum rents and for rent increases. In the 1970s the rent system was put on a 'fair rents' basis in both social rented housing and private rented: at this point the system of rent rebates and rent allowances was introduced.

<sup>10</sup> It is important to note the limitations of tenure-based international comparisons. Because of the complex and varied ways in which tenures relate to each other and to central and local government some forms of housing do not clearly fit into a standard tenure classification. Furthermore, the overall character- the equity and efficiency- of a country's housing system is shaped not by the balance of tenures it reflects but by the quite specific ways in which housing is financed and subsidised. In modern economies all forms are housing are subsidised or regulated in one way or another. This alerts us to the fact that although tenure information is useful in describing the structure of housing it tells us little about its economic status.



The sector is now governed by the 1988 Housing Act that followed a period of Conservative government intent on reducing the role of municipal housing and containing public expenditure. One authority has described the Act as “creeping deregulation” (Crook, 1992). Currently there are three broad categories of letting. First, there are lettings created since January 1989: these are not subject to rent control. Rents are set by agreement between landlord and tenant and the lettings are either assured tenancies or assured shorthold tenancies. In the case of assured tenancies, tenants have security of tenure provided they pay the rent and adhere to terms of the lease: there is no restriction on the minimum length of an assured tenancy. Assured *shorthold* tenancies must be for a fixed period of at least six months, at which point the landlord has the right to possession. Second, there are regulated tenancies, incorporated in the 1977 Rent Act, although originally introduced in the 1965 Rent Act to replace the controlled tenancies of earlier legislation. These tenancies give the tenant strong security of tenure rights and give both the landlord and tenant the right to register a ‘fair rent’. Fair rents are set by local rent officers. Third, there are tenancies to which the various rent acts do not apply or which are specifically exempt from the 1988 Act (these lettings include holiday lettings, resident landlord situations, lettings with no rent, employer/employee tenancies, and so on).

Since 1989 it has not been possible to create new regulated tenancies. This has meant that over time private renting has become- and will continue to become- increasingly deregulated. By 1993, according to Kemp’s (1998) data, 55% of lettings in England were of the post-1988 type, while regulated tenancies accounted for 19% of lettings- and a substantial segment of these did not have rents registered.

Currently, the private rented sector may be experiencing a period of stabilisation. The UK Government has experimented with financial arrangements for private investors as mechanisms for increasing investment and supply. One financial incentive was a Business Expansion Scheme introduced in 1988, allowing private individuals to become shareholders in BES housing companies by investing between £500 (minimum) and £40,000 maximum. The investment could then yield a dividend with tax relief at the investor’s marginal tax relief and full relief on capital gains tax if the shares were disposed of after 5 years. In this scheme the dwellings must be held for five years to obtain capital gains tax and they must be rented commercially. The latter condition excludes housing associations from the scheme. A second financial arrangement is the Building Societies Act of 1986, which gave new powers to building societies to finance, build and manage, rented dwellings. Oxley and Smith (1996) have described the actual response to this as “sluggish” in their comparative review of private renting.

A further feature of the UK regime since 1988 is the reduced significance of local authority grants for improvements and repair. These grant schemes are now discretionary rather than mandatory and the 1988 Act reduced the minimum standard to be attained by landlords. Where landlords are served notices to undertake repairs or improvement they are usually awarded a grant. But where a landlord applies for a grant to undertake repairs the amount of subsidy paid, if any, will depend on the income of the applicant (either the tenant or the landlord). Improvement and repair grants are allocated on the condition that the property is let for at least a further five years. It has been argued that the emphasis on discretionary grants and the reduction in required standards “will reduce assistance and have serious consequences for the private rented stock, particularly since so many dwellings are already in very poor condition” (Oxley and Smith, 1996, p. 157).

In relation to the financial incentives for investment, it is not clear what their effect has been. During the early to mid 1990s there seemed to be an increase in supply especially at the upper ends of the market. However, opinion is divided on whether this can be ascribed to the incentives or to more general conditions in the housing market (Kemp, 1998; Oxley and Smith, 1996). There is agreement, however, that even if specific supply and investment incentives are effective a greater degree of tenure neutrality will be required to improve the relative size of the sector in the housing system. (Coopers and Lybrand, 1989; Oxley and Smith, 1996; Donnison, 1982) One authoritative author concludes his review of the sector with the observation: "all this confirms the need for subsidy for private landlords" (Crook, 1992, p.109).

Finally, it is important to note the increasingly important role of the UK's housing allowance (Housing Benefit). Demand at the lower end of the market is substantially underpinned by this means tested payment. Its role has escalated as the deregulation of rents implicit in the 1988 Act has cumulatively affected market rents. The effect of deregulation on the demand for Housing Benefit was compounded by more general social trends such as the rising number of lone parent families and the stagnation in the earnings of young working-class men and women. In the early 1990s, the Department of Social Security was forecasting that housing allowance costs to private tenants and housing associations would grow by 7.1% per annum in the latter half of this decade.

### *Germany*

Germany has the highest share of private rented in Europe, and is in the polar opposite corner to the UK in the typology. Three sets of policies account for this (Harloe, 1985; Hubert, 1998). First, on the *demand* side the roles of other tenures have been constrained. Significantly, owner occupation is controlled, thereby creating a larger demand for rented accommodation. In practice no more than 60% of the value of a dwelling is borrowed and local taxes and property taxes are levied on owner-occupiers. In addition, Germany has not developed a large-scale system of publicly provided rented housing. More generally, demand for rented accommodation is supported by a system of housing allowances: as in the UK and Ireland, the most typical recipient would be a household dependent on social security. (The scheme is not without problems—newer, higher rents, for example, are inadequately covered by the scheme.)

On the *supply* side, the principle underpinning policy is that private rented investment "has always been treated in the same way as any other investment for tax purposes" (Oxley and Smith, 1996, p.141). Interest, maintenance costs, depreciation, and interest costs on borrowing for new investment can all be offset against tax liabilities. Losses from housing investment can be offset against other sources of income, although this provision has been restricted in recent years. For many years investors in all tenures were exempt from land tax for the first 10 years after construction: this considerable incentive was withdrawn in 1990. Currently, rented dwellings are subject to a capital assets tax and to a municipal land tax; rented property is exempt from capital gains tax if the property is held for more than two years. A generous system of depreciation allowances has always applied to rented property, but this system was reformed and improved in 1989 (Oxley and Smith, 1996). While the period over which depreciation could be claimed was reduced from 50 to 40 years the *rate* of depreciation was increased. Over the first four years the total depreciation allowable is 28%, and over the first ten years, 58%. Significantly, the

depreciation allowances are to some degree targeted at the lower end of the market. If owners rent a property to a low income household for a minimum period of five years at a rent not exceeding that applicable to comparable social housing, then a depreciation rate of 85% can be attained over the first ten years.

In 1989, in a context of growing concern about possible shortages, a further fiscal incentive was introduced to encourage renovation and repair work. Expenditures leading to the creation of rental accommodation through extensions and renovation to existing dwellings could be offset against income tax for five years. This scheme only applied to work commenced in 1989 and completed at or before 1984. The Landers also continue to have a role in the provision of various grants for property rehabilitation.

There is extensive *regulation* in Germany. It started as a form of outright rent control around 1914 and a rigorous form of control stayed in place until the early 1960s. In the 1960s rent control was relaxed, but in 1971 in response to rapidly increasing rent levels a new Rent Regulation Act was implemented: this gave strong tenure rights to tenants and altered the framework of rent setting. The three key elements of the framework are:

- Unilateral Security of Tenure for the Tenant;
- A limitation on rent increases for sitting tenants, to the level permitted by the index of local rent costs (*Vergleichsmiete*);
- Free negotiation of initial rents on a new lease.

Under this regulatory system all leases are indefinite and fixed term leases can only be permitted in limited circumstances (since 1983 leases of up to five years have been permitted). Tenants can only be evicted if the landlord or a member of his family take up occupancy of the accommodation or if the tenant does not adhere to the terms of the lease.

The *Vergleichsmiete* is a system in which rent increases are linked to a legally determined index of local rents, which is related to the quality of the rented accommodation. (It is also relevant that while the rents of new tenancies are freely negotiated the criminal law of usury can be enforced against landlords attempting to charge rents more than 50% of average local rents for comparable accommodation). The index is determined by the rent of leases agreed in the previous three years – the rationale for this approach being to prevent new rents running significantly ahead of existing rents. Rent increases can only be agreed with existing tenants where there has been an increase in operating costs or interest charges, an increase in expenditure due to improvement work, or evidence that similar accommodation locally is commanding a higher rent. A rent increase will not be permitted if there has been a rent increase in the previous year, and over a period of three years the total rent increase may not exceed 30%. Some portion of the improvement expenditure (up to 11%) may be passed on to a tenant, provided the tenant has agreed to the expenditure prior to the work being carried out.

It is important to note that despite the system of rent regulation rents have risen significantly in Germany for a number of reasons. First, the system of free determination of rents for new contracts gives a strong market character to the system because of the continuing supply of new stock and hence newly agreed rents. Second, political

reunification and the mobility it has engendered has created a large demand for rented housing in the 1990s. Third, the continual addition to the stock, combined with the financial support for improvement and renovation has led to a continual process of 'upgrading' and hence rent increases. One commentator observed that in Germany the emphasis on improvement is such that its rented housing might be described as "too good" (Hallett, 1993). The rent increases have been reflected in a significant rise over time in expenditure on housing allowances.

Germany has therefore succeeded in sustaining a large, good quality rented sector by a combination of regulation, support for demand at the lower end of the market, and a concerted approach to the subsidisation of investment and supply. A recent summary of the German experience suggests that the "two most important subsidies are housing allowances and depreciation allowances" (Hubert, 1998, p. 213). This account also points out that the sector has benefited from:

- Tenure laws that are liberal compared with those in other European countries;
- A "rather favourable" treatment in terms of taxation relative to owner occupation; and,
- A "social policy which increasingly relied on general housing allowances whilst abstaining from direct interference with the market" (Hubert, 1998, p.205).

### *Netherlands*

From a very high share in the housing stock after 1945 the role of private rented housing is in decline, quantitatively. In Holland, the sector is described as "two sectors" (Priemus, 1998) because of the dual nature of the rented regime. There is a clear 50/50 split between the newer 'commercial' stock provided by institutional investors and the older stock, which is largely the domain of the traditional 'small scale' landlord. In terms of social mix the commercial sub - sector has higher income tenants, and the small landlords have lower income tenants. The rented sector is more mixed in income terms and demographically than the rented sectors in Ireland: it is *not* confined in Holland to the largely younger, mobile segment of the population.

The rapid decline of the sector in the 1980s is in part attributable to the change from direct subsidies to a regulated cost rental system in 1975. Up to that time, subsidisation had taken the form of annual subsidies towards operating costs. Landlords receiving these subsidies were required to charge rents set by the Government. This system was replaced by the Dynamic Cost Price Rent System. DCPR rents were calculated over a fifty-year period, with subsidies being paid throughout the fifty years on a diminishing basis. The scheme assumed that the cost rents would be adjusted for inflation and that rents would therefore rise over time. However, the rate of inflation (and rents) did not rise as rapidly as anticipated (as the annual subsidy declined), and hence the rate of return for landlords became too low to sustain the supply. An integral element of this system was the 'points system' which also affected the level of rent payable: the standard increase in annual rents allowed under the DCPR was adjusted to reflect the number of 'points' a dwelling had, as indicated by the features and the quality of the dwelling.



In 1989 the DCPR was abandoned and subsidisation reverted to a grants system. Grants have been available to investors since 1984 to subsidise construction and development costs; these grants are targeted at low-cost construction projects to provide rented housing for low-income tenants. Grants are also available for maintenance and repair, with the grants related to the rules concerning rent increases. Rent control has been abandoned in the middle to upper end of the market, but below a certain valuation level rents may still only be set and increased according to a scale set by the government.

Housing allowances are payable in both the private and social rented sectors; these do not take into account property taxes and service charges. Reflecting the increasing role market forces are playing in setting rent levels, rents have been rising rapidly in recent years and this in turn has expanded the role of housing allowances. Overall, the sector is contracting and moving towards a more market driven system. Any attempt to reconstruct an expanded role for the private rented sector will confront one of the obstacles some other countries face- the declining interest of institutional investors in a context where the preference for owner occupation has eroded the commercial return on new investment and supply.

The most recent review of private rented housing concluded that “the share of commercial rented dwellings in the total stock is gradually decreasing and will decrease further in the future” (Priemus, 1998, p. 275). The background to this forecast is that housing policy is less tenure neutral than before. For middle and higher income groups owner occupation is now the preferred tenure, and for lower income groups direct social housing, provided to a high standard, is increasingly seen as the natural tenure. This pattern reflects the relative political strength of the tenant association movement in the Netherlands.

### *Canada*

Canada and the USA have one important demand aspect in common, which makes it especially difficult to interpret the impact of policy. Both countries have had high levels of net immigration. This has been true also of some European countries since 1945, but in the case of Canada/USA the economic resources of the immigrants have been more varied (with some high-income immigrants) and also much short-term and medium term immigration. A further common feature in both systems has been the political preference to minimise direct ‘welfare’ provision of housing. (However, Canada is distinguished from the US in the role it has created for a small co-operative and non-profit sector.) This mix of political and demographic factors has sustained demand over the long run; Canada now has 28% of its housing stock in the private rented sector although the figure fell in the early 1990s.

Throughout the post war years the supply of new units rose in response to buoyant demand and public policy continually attempted to sustain supply. Supply responded to this buoyant demand partly because of the underlying tax treatment of rented investment; there were substantial capital allowances in place. Also, the Federal Government used a “Limited Dividend” system, and other initiatives, for developers. Limited Dividend gave developers ‘soft loans’ in return for the provision of low cost rental units. In the 1970s, demand swung towards owner occupation because of the high rate of inflation and accelerating property values: owners increasingly sold to obtain capital gains. New provision and investment then



came by way of a tax driven subsidy similar to Ireland's 'Section 23': one consequence of this was that supply now came from individual investors rather than large scale developers and this contributed to a reduction in the inflow of new units.

The Limited Dividend programme illustrates a more general approach that has underpinned the approach to investment and supply: this approach attempts to assure investors and developers a fair return on their investment (Miron, 1995). An early example of this (introduced in 1948) was the federal Rental Insurance Plan. This provided long-term, low interest loans to builders of low rent housing and guaranteed landlords a 2% (net) return. In the 1970s, the Federal Government instituted an Assisted Rental Program to facilitate a flow of affordable private rented accommodation. This scheme was based on the provision of interest-free loans of up to 10% of the original loan amount over a ten-year period. The Assisted Rental Program resulted in the provision of over 122,000 units over the five-year period from 1975 to 1980. In the 1980s ARP was succeeded by the Canada Rental Supply Plan under which developers and sponsors obtained fifteen-year loans, interest free, up to a certain amount per unit provided. Over 24,000 units were provided under CRSP between 1981 and 1984.

Rent control was first introduced in wartime in 1940, but was abolished after the war and rents were largely unregulated until the mid-1970s. In 1975, when federal wage and price controls were being introduced, rent control was also introduced in all provinces and territories. The most common variant of rent regulation was to confine it to existing dwellings and to regulate increases in rents rather than rent levels. In Ontario, the system of 'rent control' was subject to a series of modifications and was then officially examined by a Provincial Commission. (Crooks, 1998; Miron, 1995) The Commission argued that rent regulation should be repealed and that policy should instead allow market rents to prevail while subsidising tenants with affordability problems. This approach was not implemented. Reforms were introduced in the early 1990s to exempt new rental properties from rent regulation for five years. This limitation on rent regulation was balanced by limits on the capital expenditure landlords could claim as the basis for rent increases, by legal rights conferred on tenants to seek rent reductions, by enhanced policing of landlords, and by other improvements in the rights of tenants. Over the period since 1945 landlord/tenant legislation has been considerably developed, and the Canadian system, especially in Ontario, is now quite regulated. There are limits, for example, on landlords' right to evict, on the level of rental deposit required from tenants and on the freedom in certain States and cities to convert and redevelop older apartments.

In summarising the Canadian experience, Crooks (1998) suggests that supply incentives through the tax system have had positive effects. However, he emphasises that "what is really needed, however, are schemes that will keep investment in the market place rather than ones that are short lived, have heavy syndication costs, and whose dwellings transfer to the owner occupied sector once the provisions of the schemes expire" (p.349). What may be most interesting about the Canadian experience is that it has achieved some success-unlike Ireland and Britain- in sustaining supply in a context in which many investors are small-scale landlords and developers.

### Key Issues Emerging – Irish Context

A number of key issues emerge for policy in Ireland from the problems and policies of other countries.

- 1 The **association between private renting and owner occupation is very striking**. To sustain a large, good quality private rented sector it may be necessary to have a greater balance between owning and renting, and between private renting and social renting. This applies to both the demand and supply aspect of renting. Ireland's lack of tenure neutrality is extreme by international standards.
- 2 A variety of financial incentives have been tried in many countries to stimulate supply. **It appears that tax incentive strategies to attract investment are not especially effective at generating long term development of the affordable part of the sector**. This seems to apply with particular force in those settings where landlords are private individuals operating on a small scale; the incentives in effect are tax driven and are used as tax shelters.
- 3 Most countries **do not have any significant involvement by large- scale institutional investors in private rented accommodation**. In those countries where there has been such involvement it is in decline. Significantly, where such institutional investment has been a feature it is associated with a significant non-profit/co-operative/housing association sector. These organisations act in effect as financial conduits, developers, and providers. The critical contribution that the non-profit or housing association sub sectors have made in some countries is the provision of low-cost rented accommodation. **This has been possible where the subsidy system subsidises construction and other costs and links the subsidy to rent levels**. This suggests that it may be necessary to devise financing mechanisms that increase the supply of *low cost* rented accommodation.
- 4 Some countries, notably Sweden, combine **good quality public rental and private rental sectors that draw to some extent from the same, broad tenant population**. This provides a social ethos broadly supportive of renting, and gives rise to a form of competition between the public and private landlords. These compete for tenants who have housing allowances that can be used either in public or private rented housing. Ireland and the UK, on the other hand, have undermined private renting somewhat by permitting its *public* rental sector to become residualised – reserved for a distinct sub-stratum of housing need
- 5 In many countries a **strategic choice has been made to shift the emphasis in policy towards income support in respect of housing costs and away from direct State provision of housing**. The benefits of this approach (better targeting, choice for tenants) have been reaped where the approach was strategic- linked with other elements of housing policy- rather than ad hoc as in Ireland's case.
- 6 **The historic form of rent control has now all but disappeared. The debate over rent control is now effectively over, with general control on rent levels no longer advocated**. The policy issue is now defined in terms of how rent 'indexation' can be achieved. Countries with some statutory framework governing rent increases have been more successful in sustaining both supply and demand in private renting.

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## Chapter Three – Analysis of Basic Policy Issues and the Private Rented Sector

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### 3.1 Introduction

In the previous chapter some countries' experiences in relation to the impact of public policies on the private rented sector were briefly reviewed. Here it is useful before advancing recommendations in relation to policy in Ireland, to briefly revisit the generally agreed objectives of housing policy and to consider how efficiency and equity principles can be applied to advance these objectives. (Barr, 1987; Culyer, 1980;)

### 3.2 Efficiency objectives

**Tenure neutrality is the first such objective<sup>11</sup>.**

The standard analyses of housing markets stress the importance of neutrality to the efficient functioning of a housing system. In practice, the pursuit of this objective is reflected in a concern that undue subsidisation should not be given to one tenure relative from another. In the Irish and British housing systems, which have three main tenures (owner-occupation, local authority housing, and private rented), the absence of tenure neutrality is quickly observed through a comparison between private rented and the other tenures. In relation to renting and owner occupation, the key issue is the tax treatment of owner occupation *vis-à-vis* private rented, as Chapter 1 showed. Where the imputed income from owner occupation is untaxed this violates the principle of tenure neutrality and undermines the role of private rented accommodation in the housing system as a whole. The policy implications of this analysis were set out in chapter one.

Turning to private renting and local authority renting, tenure neutrality would require a broadly equitable approach to the 'subsidies' for these tenures. There are a number of ways in which an equitable system might be approached. Ensuring that the net income after housing costs of comparable tenants in identical accommodation in the two tenures is one possible approach; having a broadly similar framework of housing allowances on the demand side or construction and other cost subsidies on the supply side is another. Whatever operational definition of neutrality is adopted it is clear that in Ireland (and also in the UK) the private rented sector has not been on a neutral footing with local authority rented accommodation. In Ireland local authority tenants have had *de facto* security of tenure for example, in contrast with private rented tenants; likewise, local authority tenants, but not private tenants, have had their rent liability determined within a statutory framework which is related to tenants' ability to pay. The international experience outlined earlier is confirmation that private renting will be sustained where it is on a relatively more equal footing with other tenures.

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11 Formally, tenure neutrality exists when "competitive markets leave individuals (on average and in the long run) financially indifferent between buying accommodation and renting it, with no artificial distortions (e.g. via the tax system) of their relative costs. An approximate example of tenure neutrality is the case of television purchase and rental in the UK." (Barr, 1987, p. 365)

**Mobility is the second, related objective**

Houses and units of accommodation have a fixed location. Unlike other commodities (clothing, food, personal belongings) a tenant or owner cannot bring housing to another location. It is therefore critically important that the housing market (and tenure-specific markets within housing) is sufficiently flexible to prevent persistent excess demand. Such excess demand can prevent individuals and families adjusting their housing situation to suit their evolving needs and – especially important in the Irish labour market today – prevent employees and the unemployed moving geographically within the labour market. A range of policy issues could arise here. For example, low income persons dependent on local authority housing may be unable to move residence to take up employment in another area if there are strict ‘residency’ requirements governing eligibility for local authority housing.

**Third, the housing system should offer an efficient quantity and quality of housing services.** Clearly, all of the resources of an economy or all of an individual’s income cannot be allocated to housing; nor can there be a zero allocation of resources to housing. Theoretically, the appropriate balance is where the marginal social cost of the resources used for housing equals the value placed on the marginal unit of housing. In practical terms this point may be impossible to identify. It is reasonable to infer, however, that this objective is not being attained in Ireland. There is substantial excess *need* for housing as evidenced by the growing waiting lists for local authority housing and the increase in homelessness, and there is a significant problem of *demand*, reflected in the affordability problems in both owner occupation and private rented. These co-exist with housing consumption in excess of needs among many households.<sup>12</sup>

**3.3 Equality objectives**

A variety of objectives can be identified here. First, there is a loosely stated *equality of opportunity* principle. This principle invokes the notion that generally throughout the population there should be access to the housing system and some degree of choice for the generality of housing consumers; Owner occupation, for instance, should not be the exclusive preserve of very wealthy families. Related to this objective is the objective of *minimum standards* in housing. This has a very direct distributional aspect, even those with very low incomes and/or extreme housing needs should be assured a minimum standard of housing (albeit that the definition of this minimum will change over time). It also has a bearing on the efficiency of the housing system: if large segments of the population or housing system are not subject to minimum standards then this may impose costs on society and the economy as a whole.

Both these equality objectives impinge on a third set of objectives that deal with *vertical equity*. In other words, the pursuit of housing policy objectives must have regard to the way in which housing is financed and in particular to the income distribution implications of state subsidies and interventions. The exact degree of vertical redistribution to be sought is a matter of judgement, as is the extent to which the pursuit of this objective should be traded off against other objectives.

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12 It is useful to distinguish between *need* and *demand*. Need refers to the amount of housing required to accommodate a population of a given size, age and so on, at an agreed minimum standard, without taking into account the individual households’ income or ability to pay for housing. Demand, however, refers to the amount of housing households can afford.



### 3.4 Policy Instruments

The general outline of objectives given above can be considered in the context of the current interventions in place – and being considered – in the private rented sector in Ireland. However, before considering specific policy questions, it is necessary to make some general distinctions about *how* policy objectives can be advanced. Is it valid to argue that a fully unregulated private market for rented housing is the best strategy to pursue in advancing the broad policy objectives above? To consider the general question of the rationale for and the nature of policy interventions the distinction between three broad categories of intervention should be noted: regulation of the *physical quality* of the stock, interventions to affect *demand*, and interventions to sustain and increase *supply*.

The first of these questions is relatively straightforward. There are no advocates of market approaches who stretch their advocacy of market provision to the point of rejecting regulation for basic physical standards. The underlying logic derives from both equity and efficiency principles. Equity is relevant, as many housing consumers will have low income; some will have poor education and so on. Such housing consumers are unlikely to have the capacity to enforce publicly agreed standards in relation to physical quality and structural quality of landlords' accommodation. There is, in other words, an imbalance of power in the market place rather than a perfectly competitive market of equal buyers and sellers. This logic does not, of course, clarify what the appropriate *specific* standards should be in any given context.

The efficiency issues are more general. First, to leave the market fully unregulated assumes that the appropriate conditions for perfectly competitive markets apply. One key condition is *perfect information*. Individuals renting housing can not be assumed to know the structural quality of the dwelling, the quality of the plumbing, electrical work etc.: nor is it a reasonable assumption that individuals will even know the prevailing official standards. Dwellings and housing units are heterogeneous, non-standard commodities, infrequently bought or rented, and consumers therefore have little opportunity to learn about housing standards in the market place. Renting a home, put simply, is not the same as renting a car, a television, or videotape.

A more important consideration is information about *prices*. In a competitive market for many goods (food, clothes, and so on) a consumer will have information about the costs of one choice relative to another and within his income (formally his budget constraint) will consume accordingly. However, renting a home and consuming 'housing services' takes place over a period of time. In a totally unregulated market the supplier (landlord) might alter the price (rent) at a date after the initial transaction. If this happens the tenant and landlord may agree on an adjusted price. But, whether this is the case or not, the fact that tenants would not know the rent over the likely period of future consumption is a departure from the preconditions for market provisions and on efficiency grounds is a justification for intervention. (A more common example of this type of reasoning in policy analysis is that of the private pensions market. Purchasers of pensions cannot be expected to have information about current and future inflation rates, interest rates and other financial and economic variables, which affect the quality of the pension, they might buy. This is seen as justification for regulation of the private pensions industry).



A final category of efficiency issues is *market failure*. The central concept here is *merit goods*. These are goods in respect of which the state supersedes the normal presumption of consumer choice and sovereignty (basic education is compulsory for example, no matter what the wishes of the parents or children). Analytically, this arises because the welfare of the 'well off' who pay taxes is affected more by the consumption of the 'poor' than by the income of the poor (formally, if there are consumption externalities). In other words, the well off are more willing to redistribute consumption *directly* in the form of housing, education and so on, than *indirectly* by means of income distribution. Housing, education and so on are viewed as 'good' consumption by taxpayers. Therefore, in the presence of these merit good circumstances a strong justification arises for some mechanism to ensure a minimum level of consumption. This could take the form of direct state provision of goods, or imposing minimum standards for market provided goods, or 'earmarking' redistributed income to specific merit goods (a grant for third level education is one example of the latter, a housing benefit or allowance is another).

The central conclusion to be offered at this point, therefore, is that on efficiency grounds alone there are *a priori* reasons for accepting that some departure from simple unregulated market provision may be necessary in the housing system as a whole and in the private rented market. The first general, and uncontroversial, conclusion is that regulation and inspection of minimum standards is necessary in all areas of the housing system.

Turning to *demand* the two principal means by which Government might attempt to directly affect demand are rent regulation or subsidies to tenants in respect of their rent (variously called 'Rent Allowances', Housing Allowances, or Housing Benefit). Rent regulation has historically been the most common intervention employed by governments in private rented housing. In the circumstances of today's housing market in Ireland it might be suggested that rent control is justified on the basis of the widely agreed objectives of housing policy. It might be argued that to pursue equity objectives the price of rented housing should be controlled, that tenants may not even have enough market information to act as sovereign consumers, that especially vulnerable groups can be discriminated against in the market, and that 'uncontrolled' market rents will act as inflationary pressures in the economy. However, the historical experience in many countries seems clear. Governments have increasingly deregulated rents on the grounds that comprehensive regulation has not historically achieved either equity or efficiency objectives. Rather than repeat the comparative accounts already given earlier, it is useful to examine how the relevant analytical principles have been applied to private rented housing. (Albon and Stafford, 1987; Albon and Stafford, 1988).

First, the usual exposition of the basic principles takes the form of conventional supply/demand curves: these logically show that rent control leads to a reduction over time in the *quantity* of rented housing supplied and in the *quality* of housing supplied, without a reduction in excess demand. This clearly violates the basic objective of adequacy in relation to the quantity and quality of the housing stock. The logic of the analysis also suggests that if there is rent control landlords then have to use *non-price* mechanisms to choose between prospective tenants. This in turn is more likely to generate discrimination

on ethnic or other non-price criteria. Rent control, furthermore, does not distinguish between tenants on the basis of either landlords' or tenants' *incomes* and is therefore ineffective in advancing equity objectives. In a dynamic analysis (and in historical experience) comprehensive rent control leads to demands for, and concession of, the exclusion of new dwellings or tenancies from regulation. A clear horizontal inequity is then built into the structure of the rented housing market: tenants with identical incomes and in identical relevant circumstances can face very different housing costs. In addition, the differentiation between 'new' and 'old' tenancies creates a tendency to immobility among those in the rent controlled stock: this can be both a *housing* immobility and a wider *geographical or labour market* immobility.

Rent control gives a landlord an incentive to evict as landlords are restricted in the rents they may charge: historically, this has lead governments to introduce *tighter* security of tenure provisions, thus widening the gap between tenants in regulated and unregulated tenancies. In these circumstances, a black market emerges in the access to regulated tenancies- a phenomenon known as 'key money' (as in Sweden, for example). This entails prospective tenants paying substantial lump sums informally to landlords and sitting tenants where the sitting tenant wants to move, and the prospective tenant wants to rent the rent-controlled accommodation. The sitting tenant then uses the lump sum to engage in a similar transaction for new accommodation. Experience in Sweden and elsewhere suggests that tenants with higher incomes may be best placed to operate in this market context. Furthermore, if strict rent regulation is combined with security of tenure, landlords can then only respond by minimising their costs in the areas of maintenance and refurbishment. Over the long run this leads to a cumulative deterioration in the quality of the stock - a very inefficient outcome.

Some commentators combine this type of reasoning with the historical observation that the private rented sector has been in decline in countries with extensive regulation and then advance trenchant conclusions about regulation being the 'cause' of the decline. Albon and Stafford (1988, p.20), for instance, summarise their work as follows:

*In conclusion, the effects of rent control are many: reductions in the quantity and quality of the rental stock; the stimulus to various "sharp", illegal and unpleasant practices; and the serious effects on the mobility of people. - - - - - If rent control is removed, the quantity of housing demanded may well be reduced, but the overall consumption of housing in the short run, since the supply is relatively inelastic, would not be affected. ————. In addition, rent control diminishes the incentive to 'ration' accommodation, because it encourages the continued occupation of large houses by small family, who would, in a free market, either sub-let or move to smaller dwellings. Moreover, a rent that denies a return competitive with alternative investments is clearly not going to encourage either new construction for rental or new lettings from the existing stock.*

The rhetorical claim of the famous Swedish economist, Assure Lindbeck, is also widely cited: "In many cases rent control appears to be the most efficient technique presently known to destroy a city- except for bombing" (Lindbeck, 1967, cited in Albon and Stafford, 1988).

Are we to conclude then, that general rent regulation in the private rented market is not justified on the basis of theory and general international experience? Or is it more appropriate to argue for an interpretation of the relevant principles, which focuses on the *a priori* rationale for intervention in the market? Two additional points are relevant here. First, Harloe's (1985) comparative account points out that while there is an association between regulation and decline across various countries, it is by no means as direct as might be expected. Some countries had active private rented tenures long *after* regulation was in place; in other countries the decline in the sector commenced *before* regulation was introduced. Harloe's work and other accounts (Doling, 1997; Donnison, 1982) argue that while the persistence of rigorous regulation contributed to an acceleration of decline, other structural factors (notably, the increasingly favoured treatment of owner occupation) were also important. In their review of the British experience Coopers and Lybrand (1989, para. 4.5) concluded that

*There is neither conclusive evidence nor general support for the proposition that the Rent Acts have been the major cause of the decline of private renting, although there is considerable evidence that they have played a significant role. (Emphasis in original)*

Second, one of the usually unquestioned assumptions in the standard (neo-classical) economic model of the impact of regulation is that the landlord is a profit maximiser. Recent empirical studies of landlords (Kemp and Crooks, 1996) show that this may not be the case. In the UK, Canada, Ireland and Sweden landlords are generally small scale operators – their knowledge of market conditions, regulations and so on is incomplete and their behaviour is not wholly consistent with a profit maximising approach. (The research to date does not offer any clear account as to why this might be the case. Kemp (1998), however, suggests that it may be related to the advanced age of the typical landlord, to the fact that landlords do not use equity or debt to finance their ownership of properties, or that they view the properties as extensions of their own or their families' property.) If this were the case it should not be taken to mean that landlords are indifferent to the economic and financial aspects of tenancies. It points to the fact that their behaviour may be affected by a wide variety of considerations – such as freedom to remove difficult tenants, problems in securing rent arrears, and the benefits of having their property tenanted by 'good' tenants who will care for the property.

Third, the conventional analysis of rent costs does not distinguish, as Barr (1987) points out, between a *dwelling* and a *home*. A landlord rents accommodation to a tenant and then the tenant turns the accommodation into a home by investing human capital and adding value. For example, by developing friends and acquaintances, by researching the best schools for children, discovering the most convenient route to travel to work, locating near extended family, and so on. These aspects of the 'value' of the tenancy are not transferable to other, similar accommodation at a similar price located elsewhere. In this logic the landlord is conferred a form of monopoly power when the rent is being renegotiated. The tenant's 'investment' has created part of the value of the tenancy for the tenant: if the landlord were a profit maximiser then this investment could be built into the landlord's demand for a higher rent than comparable dwellings of identical physical quality. For the sitting tenant the accommodation has become a *home* and for the (profit maximising) landlord it is a *dwelling*. This analysis does not suggest that rents should be controlled but that *changes in the rent of tenants could justifiably be linked to an appropriate benchmark.*

However, it is important to note that the standard analysis of the impact of rent controls drawn on above is based on static analysis which does not take account of the variety of rent control regimes or of the wider regulatory context for rented housing<sup>13</sup>. Increasingly, research on the impact of rent controls takes account of the specific forms of rent control, incorporates other features of the regulatory regime, and adopts a dynamic perspective which models the response of landlords to rent regulation. Recent analysis along these lines distinguished twelve variants on rent regulation and offered conclusions on the likely effect of each variant on the quantity and quality of private rented housing.<sup>14</sup> (Kutty, 1996). For example, rent control can be modelled as permanent or temporary; control can take the form of set annual increases in nominal terms or as maximum percentage increases, or many other forms; control may or may not be combined with minimum standards; minimum standards may or may not be accompanied by grants or other incentives for maintenance and refurbishment. The conclusion of one recent analysis is that it is critical to study rent control in the context of all of its provisions and of the housing market environment. Specifically, Kutty (1996, p.86) concludes that the

*negative impact of rent control on maintenance can be mitigated by policies that revise the rent ceiling upwards and policies that link rent increases to increases in the value of housing services (such as a policy of increasing rents by the market value of housing services that have been added through maintenance). Also, policies that enforce high quality standards and at the same time make compliance with the standards not unprofitable (through a maintenance subsidy, as practised in the Netherlands and Belgium) can lead to improvements in housing quality under rent control. These results suggest that countries that practice rent control can protect the quality of rental housing by including in the rent regulation a built-in response to changes in quality, a return on investment in housing maintenance and rehabilitation, and quality code enforcement.*

Rent control, however, is only one form of subsidy to demand in the private rented market. An increasingly common form is a housing allowance: an addition to the income of tenants linked, typically, to their rent and income, and family or dependency circumstances. (In the UK this is called Housing Benefit and in Ireland the SWA Rent Supplement). The analytical argument in favour of this approach is simply that it is more effective on equity grounds. The amount of subsidy can be tailored quite specifically to the incomes of tenants, and to other relevant circumstances, unlike rent control. On efficiency grounds this approach is more compatible with consumer choice.

However, the important analytical issue confronting this approach is the assumption about market conditions underpinning a housing allowance in any given context.<sup>15</sup> If the supply of rented housing is inelastic – not responsive to changes in price – then the effect of a housing allowance can be perverse; prices, i.e. rents, may rise and the benefit of the

13 Formally, the standard accounts are static, partial equilibrium models.

14 Specifically, the theoretical framework is a landlord's dynamic model of reinvestment under perfect competition. It models investment in housing and housing maintenance under uncertainty and assumes that landlords maximise the value of (the expected) stream of profits from rented dwellings; the landlord's time horizon is modelled as infinite. (Kutty, 1996)

15 The conventional exposition of this point is usually in the form of supply and demand curves. It can be shown that the effect of a housing allowance depends on the shape of the supply curve – the elasticity of supply. If the elasticity is low then the real incidence of the subsidy falls on the landlord, as rents will rise. (Oxley and Smith, 1996)



subsidy conferred, in part, on the landlord. In the Irish private rented sector this point may be especially important, as the stock of rented dwellings was relatively stable (and may have declined) as the number of recipients of SWA rent supplements grew in the period from the late 1980s onwards. The observed rise in rents at the lower end of the rental market during this period may therefore be due to some extent to the subsidisation of demand. Internationally, the trend is to enhance the role of housing allowances as demand-side subsidies either as a replacement for or a complement to rent regulation.

In relation to the *supply* of private rented accommodation, a similar theoretical issue arises about the effect of supply side subsidies such as general subsidies for existing tenancies: whether they increase supply critically depends on the elasticity of demand.<sup>16</sup> If the elasticity of demand is low it will mean that rents would have to fall very substantially to induce a corresponding change on the demand side. The benefit of supply side subsidies in these circumstances is passed on to tenants, but without an increase in the supply of accommodation. The practice in countries with supply side policies has been to find ways of subsidising *new* rented accommodation. A whole variety of approaches can be identified; subsidies for construction costs, tax incentives on new investment, cash subsidies to landlords to compensate for the gap between market rents and regulated rents, and so on.

There is no agreement in the literature on the most appropriate subsidy. However, it is clear that any attempt to subsidise new supply may be subject to the problems of *deadweight* and *displacement*. The former refers to situations where some or all of the additions to the supply would have happened in any case *without* the subsidy: the latter refers to the possible displacement of existing rented accommodation from the rented stock as the newer, subsidised supply is added to the rented stock. This could happen because the subsidised accommodation may drive down rents making current rents uncompetitive, or because the existing stock is older and inferior in quality. In these circumstances the *gross* inflow of new stock can be mistakenly taken as an indication of the 'success' of a subsidy, when the *net* addition to the stock could be small, or the change in the stock could be *negative*.

There have been no studies attempting to assess the impact of subsidies in Ireland. However, it is clear that these considerations have a distinct relevance to Ireland. During the 1980s (commencing in 1981) a tax-based scheme (popularly known as 'Section 23') was introduced to stimulate the supply of investment in rented accommodation.<sup>17</sup> A large volume of new rented stock (apartments and townhouses) was added to the supply of rented accommodation but, as the data given earlier shows, the total stock of private rented accommodation was lower in 1991 than in 1981.

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16 Here too the analysis of the effect of subsidies can be done in the context of supply and demand curves. It can be demonstrated that if supply is subsidised in a context where the price elasticity of demand is low then the impact of the subsidy on supply will be small.

17 In Budget 1981, the Minister for Finance stated that he would be introducing "a new special allowance of 100 percent in respect of expenditure incurred on the construction of moderate-cost rented residential accommodation. The new allowance, which would be set against rental income, should increase the attractiveness of investment in a sector where a recognised need exists, especially in our major towns and cities- - - (p.29)



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## Chapter Four – Policy Conclusions and Recommendations

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### 4.1 Introduction

The analysis in the earlier sections, both analytical and comparative, suggests that if the private rented sector is to fulfil its potential role in the Irish housing system a long-term, strategic approach is required.

Policy makers have a specific responsibility not only to respond to short-term problems and individual issues, but also to articulate clearly the State's view of the role of the private rented sector and to spell out its commitment to the mix of arrangements consistent with this role. It will also be necessary in Ireland to establish mechanisms for policy consultation, planning and research that include the relevant actors and interests. At present there is no established forum in which the needs and problems of the sector are addressed and in which conflicting interests can be managed. (The *Programme for Partnership and Fairness* contains a commitment to the establishment of a Housing Forum. It is not clear from the text of the draft *PPF* whether it is envisaged that the policy problems of the private rented sectors will be within the remit of the Housing Forum)

If the argument of this document that the private rented sector should play a more enhanced role is accepted, then it is critical that a greater balance across tenures is introduced in the tax/subsidy/regulatory regime. In the future the key to obtaining this balance will lie, firstly, in the reform of the tax treatment of owner occupied housing along the general lines advocated in many independent commentaries and analysis. Secondly, a new balance must also be struck between private renting and local authority renting: in a number of important respects there are inequities in the treatment of private rented tenants relative to local authority tenants.

In short, the housing system must confer a substantial, positive role on private renting, rather than leaving it as the tenure of last resort for those unable to obtain local authority housing or not yet ready to enter owner-occupation. Three sets of policies must be implemented to give effect to this strategy.

### 4.2 Demand

First, in relation to rent control as an instrument for supporting demand, general regulation in the form of comprehensive control on rent levels is *not* an appropriate policy to pursue if the sector is to be sustained and expanded. Aside from the review of the comparative experience and the discussion of policy principles given earlier, the historic legacy of the controlled rent sector in Ireland offers an indication of the deleterious impact of general rent regulation. However, while control of rent *levels* could have a serious effect on the private rented sector there is a justification for regulating the way in which rent levels are altered. This could be done by establishing a national system whereby rents would increase on a pre-determined annual or other regular basis. This would require the identification of a suitable index. In other words, the level of rent originally

agreed between a landlord and tenant would be a voluntarily agreed rent, but some framework would then govern the future evolution of the rent for that tenant. This would result in a system that reduces uncertainty for landlords, investors and tenants, but that also allows the long-term direction of rents to be market-driven.

A range of quite detailed issues would arise if this approach were being implemented. A necessary element in any system would be the freedom to increase rents in line with *improvements in the quality* of the accommodation. This might require a system of measuring and classifying the overall *quality* of rented accommodation. How would changes in state benefits and allowances be linked to a general system of rent indexation? Should the national housing system be treated as a unified system or should *local* housing markets be treated separately? How specific should the system of 'rent indexation' be? The options here range from a system of *guidelines* indicating an appropriate range within which rent increases should fall through to a defined range within which rent increases should lie, taking account of landlords' need to obtain an adequate return on rented property. Whatever the most appropriate system might be for Ireland, it is clear the current, wholly unregulated, system is not easy to justify. Many households are simply unable to afford rented accommodation and the cost of SWA Rent Supplement has been escalating at a very rapid rate.

A specific set of issues would arise in regard to the system of local authority rents. Currently, the general policy is that these rents are set on a replacement cost basis and the actual rent an individual tenants pays is related (according to a Differential Rents formula) to the tenant's income and family circumstances. (Local authority tenants have other advantages also, as indicated in Chapter One). The net implication is that if a policy is being formulated in relation to private sector rents it should be done in such a way that – at the very least – it does not widen the horizontal inequity between the two types of tenant.

In relation to the *second* aspect of demand-side interventions, housing allowances for tenants, the question as to whether this form of subsidy (related to their income and housing costs) is necessary is related to the presence or absence of regulation of rent levels or of changes in rents. In the absence of any rent regulation the pursuit of equity objectives would clearly suggest that low-income tenants would need significant financial support to obtain rented accommodation in the private rented market. The recent Irish experience is a clear demonstration of the significant role such housing/income supports must play in a context where rent levels are rising without any regulatory limit. If the current regime of unregulated rents continues in Ireland in the future, then a strategy of 'earmarked' income distribution via housing cost supports is the strategy which will be most consistent with both equity and efficiency objectives. In principle, it allows tenants some element of choice in the market (unlike state housing, which is allocated administratively) and it directs support on the basis of income. Some countries rely on a combination of regulation and housing allowances, and this is the broad strategy being advocated here. Therefore, if there is no form of regulation introduced in Ireland the role of the SWA Rent Supplement will be all the more significant; if rents continue to rise it implies a continuing growth in expenditure on the SWA Rent Supplement.

For the Rent Supplement to fully achieve its objectives some specific improvements are required. Briefly, the discretionary nature of the system, the level of rent afforded, the range of the population included, and the 'poverty trap' all require attention. The Rent Supplement system is local and discretionary and this leads to variations in the treatment of tenants in similar circumstances. This is difficult to justify when such a high proportion of private rented tenants is in receipt of the SWA Rent Supplement. It will also be necessary to remove the 'poverty trap' inherent in the Rent Supplement. If tenants take up employment they lose entitlement to the Rent Supplement. This is inefficient from a labour market point of view. It is also inequitable relative to the regime faced by local authority tenants; these tenants may face a rise in rent related to their *income* but there is no categorical distinction between employed and non-employed tenants. Furthermore, the exclusion of employed tenants from Rent Supplement further reinforces the image of private rented accommodation as a residual tenure in the housing system.

*Budget 2000* announced changes in entitlement to Rent Supplement for those returning to work under the Community Employment, Back-to-Work Allowance, Revenue Job Assist, and Jobstart schemes that will ameliorate the poverty trap effect in various ways. These changes are:

The current monthly limit on supplements will be abolished;

- Family Income Supplement and Back-to-Work Allowance will not be counted as means in assessing eligibility for the supplement;
- Withdrawal of the supplement will be tapered over four years at descending rates of withdrawal;
- Additional income paid to those participating in approved training course will not count as means, and;
- A weekly disregard of means will be introduced for part-time employees.<sup>18</sup>

These changes recognise the principle that Rent Supplements should not embody a 'poverty trap'. However, they make the Rent Supplement system very complex and inequitable by distinguishing between categories of people who take up employment on the basis of the route through which they return to work and treating these categories very differently.

Currently, Ireland has not only a Rent Supplement but also a Rent Tax Allowance. This was introduced on *ad hoc* basis for persons aged 55 and over and then extended. The tax allowance does little to advance equity objectives as it is very low (Ir£500 for a single person aged under 55 in tax year 1999/2000) relative to prevailing rents and not related to income. Tenants with very low incomes who are therefore not paying tax do not benefit from the allowance. *Contra* the Bacon (1999, p.10) analysis which suggested extending the tax allowance, the proposal here is that the tax allowance be abolished and the Rent Supplement improved.

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18 See Fact Sheet *Budget 2000*, [www.dscfa.ie/dept/budget00](http://www.dscfa.ie/dept/budget00)

It is possible that the Rent Supplement strategy being advanced has a potential negative consequence. As outlined earlier, rent supplements can simply become 'capitalised' in the rents being charged by landlords, thereby depriving the tenants of the effective benefit of the subsidy, unless there are measures in place to offer a flow of *new investment and new stock*. It is also the case that rent supplements may have a significant countervailing advantage. Landlords in the lower end of the market may see the rent supplement as a type of *guarantee* that low-income, welfare-dependent tenants can pay their rent, thus inducing the landlords to retain their properties in the market. The SWA Rent Supplement under these conditions is then an underpinning for *both demand and supply*.

In the longer run a more general institutional question arises about the link between Rent Supplement and the broader organisation of the supply, management and allocation of local authority housing. Currently in Ireland these inter-related functions are statutorily and administratively separate. However, a recent official study of the administration of Rent Supplement (Department of the Environment, 1999) argues that the Rent Allowance should not remain as part of the income maintenance system of the Department of Social, Community and Family Affairs. The study's main recommendation (p.iii) was that, subject to specific changes,

*rent assistance, where it is appropriate to meet housing need, should be provided by the local authorities as part of, and integrated into, housing policy. The strategic objective would be to make available to local authorities a comprehensive range of social housing options, including rent assistance and the direct provision of accommodation, to meet such needs*

The study suggested that tenants already in accommodation who begin to experience affordability problems due to loss of employment and so on would continue to be dealt with in the income maintenance system. In principle, this approach has much to recommend it, as it offers the prospect of an integrated local housing service under the aegis of the local authorities. However, it is less clear what the immediate effect of this strategy will be. A major organisational change such as this, at a time when the level of reliance on rent supplementation is growing, has the potential to create further difficulties for low-income tenants. Rent supplementation would be fragmented into two different categories of applicant; provision of the 'local' element would devolve to eighty-eight housing authorities; local authorities are unlikely, in the short term, to have the planning and management capacity to effectively deliver the proposed new 'integrated' service.

#### **4.3 Supply and Investment**

The general evidence from a range of countries is that the supply of new stock of private, rented housing is problematic and that many countries have attempted to apply specific incentives and subsidies to deal with this problem. Before considering Ireland's current and recent experience in this regard a general point should be made. Policies directed at improved supply will have a much greater chance of success if the broader context in housing is one of tenure neutrality. Specifically, if owner occupation is generously subsidised then it will direct housing demand into that tenure. It is hardly incidental that Germany and Switzerland, both of which have high levels of private rented provision, adopt somewhat restrictive stances towards owner occupation. In Germany, for example, it



is not common for borrowers to borrow more than 60% of the value of a property.<sup>19</sup> Furthermore, the social expectation is that individuals and families enter owner-occupation at a later point in the life cycle than would typically happen in Ireland or the UK. In Switzerland, imputed income is counted as taxable income whereas in Ireland it is excluded from the tax base.

Before turning to the potential role of specific incentives to increase supply the general tax status of landlords' income from rented residential property should be noted. Under Irish tax provisions this form of income is treated as *Schedule D, Case V* income, rather than *Schedule D, Case II*. Income from rented residential property is *not* treated, in effect, as business income. This stands in marked contrast to the treatment of rental income from commercial property in Ireland and in contrast to some other countries where income from residential property is regarded as business income. Under current arrangements in Ireland it should be noted (without attempting a detailed account of the tax provisions) that landlords can offset against rental income any rent or rates payable, the cost of goods or services provided, and the costs of repairs, maintenance, insurance and management. Interest on money borrowed to purchase, repair or improve a property is also allowable (although interest paid prior to the first letting is not allowable.) An important recent change in the wake of the Bacon report is the abolition of tax relief for borrowings to purchase accommodation for renting after April 1998 (investments with Integrated Area Plans are an exception to this change). In addition, there are certain capital allowances available, and expenditure on refurbishment and conversion undertaken from 1988 to 1994 is allowable for properties of certain sizes, subject to certificates of reasonable cost.

The argument can be made that, notwithstanding the variety of tax reliefs against gross rental income, there is a fundamental inequity in the distinction between *Case V* and *Case II* income. The key implications of the distinction are that: offsets against tax and losses cannot be set against other (non-rental) income; there is no generic 'depreciation' provision; and rental income is not taxed at the lower rate applicable to traded income. *Case V* income is, in part, a reflection of a historical distinction between 'active' and 'passive' income. Rental income was associated in pre-industrial times with the receipt by the aristocratic and leisured classes of large amounts of rental income from land and dwellings, with the landlord in many cases having little or no direct involvement with the land or dwellings or tenants. Arguably, this basis for the *Case V* classification is anachronistic. It could be argued, therefore, that the broad principle that should be followed is one that treats the provision of private rented accommodation in the same way as other businesses.

However, any judgement on this matter should be based on representative data about the actual *behaviour* of residential landlords. Such data is simply not available. It is distinctly possible that landlords are not economically dependent on rental income, that rental income is in many cases a supplementary income, and that they are by and large not 'professional' landlords. If this were the case it would greatly weaken the case for redefining the tax status of rental income. On balance, it is difficult to make the case that in Ireland the income from private rented accommodation should be treated as business

19 This is because of a law which prevents the bank from refinancing more than 60% of the value of the property by issuing 'Pfandbriefe' which, being protected in this way, are the cheapest source of refunding for the bank. Therefore the part of a mortgage above the 60% threshold will be more costly to the bank and hence to the borrower. (Personal communication, Franz Hubert, Free University of Berlin)



income. Such a change might only lead to a situation where landlords offset costs associated with renting against *personal* income, leading to a reduction in the tax liabilities of landlords and property owners many of whom would have substantial incomes.

In Ireland one specific incentive was put in place to generate new investment and supply- 'Section 23' so-called. This was first introduced in 1981 (for three years initially) and for some time it applied to the entire country. It was re-introduced in 1988 and following the Bacon report recommendations it was curtailed in 1998. It now only applies in areas that have an *Integrated Area Plan* under the terms of the *1998 Urban Renewal Scheme*. The scheme encouraged investors to buy or build new properties by permitting them to offset the capital cost (not including site costs, but including developer's costs, and professional fees) against rental income during the ten years after construction until the capital cost allowance had been used up. The allowance could be used as an offset against rental income from *all* properties, not just the new rented unit. Section 23 provisions also allowed interest on borrowings for S.23 investment as an offset against rental income and the combination of the interest relief and rent relief would have meant in practice that in some situations no tax was payable on the rent received. (Skehan, 1991; Hooke and Macdonald, 1988).

The tax attractions of the scheme were widely noted when it was first introduced and while it has undoubtedly contributed to the modernisation of the rented stock it is impossible to assess its impact in detail. This is because of the absence of data on the number of rented units it gave rise to, the cost in terms of revenue foregone, the displacement effect on pre-existing rented housing, and so on. During the 1981-1991 period the stock of rented accommodation *fell* in net terms. This suggests that while significant Section 23 units were added to the stock this was not sufficient to redress the long run structural decline in the private rented sector.

Section 23 may be a good illustration of experiences in some other countries. It offered a tax- driven incentive to investors (many of them not professional landlords) at the cost of a regressive narrowing of the tax base. While it resulted in a gross addition to the supply, in net terms its impact was not sufficient to leave the rented stock any larger in 1991 than in 1981. (Part of the background here is that the incentive was explicitly directed in the first instance at improving the supply of rented housing. However, the later variants of the scheme offered the reliefs to *owner occupier purchasers* in certain areas, undermining the earlier intent of the scheme). On the whole, it is wise to conclude that Section 23-type provisions may not be an effective way of increasing the stock of affordable rented housing. This conclusion is broadly supported by the international experience.

Bacon's analysis (1999) of the owner occupied market led him to argue against S.23 type provisions, the reasoning being that investor-led demand for property was a significant factor in sustaining the boom in house prices. Consequently, the Government repealed the S.23 provisions in 1998, and S.23 arrangements will only be allowed within the framework of an *Integrated Area Plan* under the terms of the *1998 Urban Renewal Scheme*. The effect of this provision must be viewed in conjunction with the other tax related recommendations in Bacon, also implemented in 1998, the removal of deductibility of

interest on borrowings for investment in residential property and the imposition of stamp duty on purchases of new houses by non-owner occupiers. These might all combine to *weaken incentives on the investment/supply side* of the rental sector: simultaneously the Bacon proposal to improve the rent tax allowance would, if implemented, *strengthen the demand side*. This is hardly an appropriate policy direction for private rented for the future.

The net position in policy terms currently is that there is *no overall strategy for sustaining the supply of affordable private rented accommodation*. It may very well be that if the sector is comprised of small-scale, non-professional landlords no significant improvement can be made through the use of financial incentives. A number of proposals, however, merit consideration.

- 1 The 'Bacon recommendations' affecting investment in private renting, in particular the abolition of interest deductibility on borrowings for rental properties, could be reviewed. For example, a limit could be imposed on the *amount* of borrowing any one investor may be permitted; the amount of deductible interest could be tiered according to the length of time the property will be in the rental market or related to the level of rents to be charged.
- 2 A series of measures is required which gives investors incentives to supply accommodation at the *lower* end of the market. These could take the form of cash grants for building costs; generous depreciation allowances or even direct current subsidies. The essential feature of any scheme is that it be linked to the provision of long-term, affordable accommodation. These kinds of subsidies in other countries have been integrated with rent regulation, where subsidies and incentives are tiered according to the 'affordability' of the rent.
- 3 Much of the emphasis in policy in Ireland has been on *new* stock to the possible neglect of repair, improvement and refurbishment. Much of the rented stock in Ireland is old, and while there are no reliable data on the physical quality of the stock, it is likely that some of the stock being rented – or which might be rented – does not meet the requirements of the 1992 legislation. Specific incentives – perhaps in the form of grants – should be devised to have this stock upgraded; these incentives should be devised so that the accommodation becomes available to tenants on lower incomes at affordable rents. (The grants could be made conditional on the tenants being in receipt of a Rent Supplement, for example)
- 4 One potential source of supply is the owner-occupied sector. Some of the owner-occupied stock is under occupied, measured in terms of the ratio of persons-to-rooms. Persons on lower incomes, who might benefit from additional income, may occupy a sub-set of this stock. It might be desirable to devise incentives for owners to sub-let, again conditional on the stock reaching the required minimum standard and being available at the lower end of the market.

#### 4.4 Regulation

The immediate context in which regulatory issues can be considered is the legal framework embodied in the Housing (Miscellaneous Provisions) Act, 1992<sup>20</sup>. In this legislation minimum standards for accommodation were specified, the provision of rent books was made mandatory, tenants acquired the right to a minimum notice to quit, and a legal requirement on landlords to register their properties was introduced. Three aspects of the framework set out in the legislation require reform and development if the private rented sector is to be sustained and expanded.

##### *Minimum Standards and Registration*

As Ryall (1998; 1999) points out in her review of the 1992 Act, the requirements of the Act are not especially onerous. In relation to the structural quality of dwellings, they are required to be in “a proper state of structural repair” (1992 Act, Art.5 (2))<sup>21</sup>. One important qualification to this is that in determining the standard of repair account will be taken of the “age, character, and prospective life of the house” (Art. 3(3) of the 1984 Regulations pursuant to the 1992 Act). This provides some leeway for landlords of older dwellings. In enforcing these minimum standards local authorities have the power to inspect dwellings and to oblige landlords to effect repairs; local authorities may also directly undertake work in a dwelling to bring it up to the required minimum standard, if necessary.

It is important to note that the official data on minimum standards suggests that there is a substantial amount of poor quality accommodation. Of the 5,501 dwellings inspected in 1997, 1,902 did not meet the minimum standards– a ‘failure rate’ of 34.5%; in the Dublin County Borough area the ‘failure’ rate was 50.3%. There are two immediate policy changes suggested, arising from these data.<sup>22</sup> First, the local authorities should be given additional resources to considerably increase the inspection rate. Over the period 1994 to 1997 the accumulated number of inspections nationally (about 18,000) is only a small proportion of the total stock, and even allowing for appropriate targeting of areas and dwellings the level of inspections is low relative to the potentially large number of sub-standard dwellings. Second, the amount of poorer quality dwellings suggests that specific intervention is required to bring much of the rented stock up to standard. Consideration should be given to the suggestion made above of *offering grants or some form of financial support targeted at the poorer quality dwellings*. This financial support should be tailored to ensure that dwellings are offered at appropriate rents to tenants with affordability problems.

The recommendation regarding local authorities’ resources also has implications for the enforcement of the requirement on landlords to register. The rate of registrations is low: in 1998 almost 24,000 dwellings were registered out of a total stock in the range of 100,000. Improved resources for inspection could also be used to *increase the registration rate*.

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20 The contents of the 1992 Act are summarised and its implications are discussed in Ryall (1998; 1999)

21 This means that a dwelling should be “essentially sound, with roofs, floors, ceilings walls, and stairs in good repair and not subject to serious dampness or liable to collapse because they are rotted or otherwise defective”.

22 The official data do not record the *outcomes* of inspections. It is not possible to determine how many of the inspected sub-standard units were subsequently brought up to standard.

### *Security of Tenure*

At present the great bulk of tenancies in Ireland are periodic, although leases of six months are becoming more common. 'Periodic' tenants rent their accommodation from week to week or month to month and although many of the tenancy agreements are oral the possession of a rent book acts *de facto* as a statement of the terms of the tenancy. Currently, the tenant has a right to 28 days Notice to Quit. A landlord wishing to eject a tenant must serve a valid Notice to Quit; if the tenant does not leave, the landlord can then proceed to obtain a possession order<sup>23</sup>.

Clearly, private rented tenants in Ireland have no security of tenure and it is difficult to see how, in the light of international experience, the sector can be sustained unless the demand side of the market is strengthened with improved tenure rights for tenants. It is also true, however, that conferring unlimited tenure on tenants on a general basis could act as a serious disincentive to investment and supply. There are two immediate issues that command policy attention. First, because of the flexibility and mobility that they allow it is important that periodic tenancies should continue to have a role in the sector. However, *these tenancies should be improved* in the following ways:

- The notice to quit should be related to the length a tenant has been in occupation;
- There should be a minimum time period required to elapse before a rent increase is allowed;
- A notice to quit should be permissible under specific circumstances (these should include the landlord wanting to sell, or wanting to live in the dwelling, the tenant being in breach of the terms of the tenancy, serious anti-social behaviour, and so on); and
- After a specific period of time in a periodic tenancy the tenant should acquire the right to a fixed term lease.

Second, tenants' commitment to the tenure would be strengthened if the arrangements for acquiring fixed term leases were improved and *if short-term leases could lead to rights to fixed term tenancies*. No specific formula is recommended here, but the essential principle would be that a sequence of periodic tenancies or short-term fixed tenancies would lead to a right to a longer lease. *Under longer-term fixed tenancies the responsibilities of both landlord and tenant would also need to be specified*. Tenants would have 'first call' on lease renewal (unless they breached the terms of the lease), tenants and landlords would be subject to longer periods of notice, and both tenant and landlord would be confined to specific grounds for terminating a tenancy.

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23 This discussion focuses only on periodic tenancies. Other forms of tenancy are fixed term tenancies, tenancies governed under the 1982 Act affecting decontrolled tenancies, and tenancies which become long-term tenancies under the terms of the 1980 Landlord and Tenant Act.

The policy proposals advocated here in relation to tenure rights are envisaged as part of a wider regime that would incorporate an element of rent regulation as outlined earlier. Rent levels would be set by agreement between landlord and tenant but rent *increases* during a tenancy would be governed within an overall statutory framework. Finally, it is important to note that with or without the reforms advocated here being in place, the sector would benefit significantly from a *local, non-judicial structure of dispute resolution in relation to deposits, leases, rents and so on*. The current legal framework of local Rent Tribunals for the very small decontrolled sector might provide an opportunity to learn from the experiences of these local structures and to devise new structures for the whole of the rented sector.<sup>24</sup>

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<sup>24</sup> The decontrolled sector comprises less than 10,000 units and is in long term decline. The current system of Tribunals was established in 1982 to determine rents etc, after the rent control legislation was found to be unconstitutional.



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