

# Residential Rentals

## THE HOUSING MARKET, REGULATIONS, AND PROPERTY RIGHTS



According to the U.S. Census Bureau, rental housing now accounts for more than a third of the nation's housing market. This represents a significant shift from homeownership toward rental occupancies in the past decade, due in part to economic necessity brought about by the foreclosure crisis and recession, and a heightened sensitivity to the perceived risks of homeownership. At the same time, various benefits of renting, such as geographic mobility, financial flexibility and freedom from home maintenance responsibilities may be more appealing than ever.

In college and university towns, where housing is often at a premium and the market is stabilized by sustained demand, the conversion of single-family houses to rentals is increasingly attractive to investors. In tourist communities, the short-term rental market not only helps to fuel local and state economies, but enables many property owners to secure their future retirement homes.

Renting may be the only realistic housing option for low- and very low-income families. In post-recession years, demand for rental housing has caused a shortage of affordable housing nationwide, and there is growing concern among local governments that short-term and vacation rentals contribute to this shortage, in cases where property owners are opting to engage in these markets rather than offer their properties for long-term rental.

The *sharing economy* has changed the short-term rental game entirely, and the runaway success of online platforms that allow hosts and guests to arrange short-term rentals has far outpaced governmental regulation. Airbnb, a company whose value now exceeds that of several major hotel chains, claims to have generated hundreds of millions of dollars of economic activity in various major markets. Numbers like these not only pique state and municipal interest in revenue, they also raise concerns about fair competition, and the negative impact of short-term rental conversions on long-term rental inventory.

From construction and investment to tourism, residential rental homes are an integral part of our economy across the U.S. As long-term residential rental markets expand and certain short-term rental markets explode, local governments are increasing initiatives to regulate them. If rental restriction ordinances arise locally, understanding the implications will better equip REALTORS® and their clients.

This document was distilled from the Rental Housing Restrictions White Paper.



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Many communities have adopted some form of rental housing regulation, and many more are rushing to implement ordinances in response to the boom in short-term rental markets. Among the regulatory objectives most often cited are:

- **Protection of Neighborhood Character:** Both physical characteristics and “livability” issues such as noise levels and traffic.
- **Revenue:** Short-term rentals represent significant potential tax revenue for many jurisdictions. In order to capitalize on it, communities might impose registration or licensing requirements to identify properties subject to additional taxation.
- **Fairer Competition with Licensed Lodging:** Hotels and bed-and-breakfasts bear the expense of taxation and compliance with the Americans with Disabilities Act, which adds to operating costs in the competitive lodging market. Holding short-term rentals to the same standard “levels the playing field.”
- **Protection of Renter Safety:** The health, safety and welfare of visitors may be cited as a reason for operational restrictions on short-term rental properties.
- **Greater Compliance with Maintenance, Building and Nuisance codes:** A community might seek to strengthen its power to enforce existing codes by requiring registration and inspection of residential rental properties.
- **Increased Landlord Accountability:** Holding landlords responsible for the condition of their properties and compliance to applicable laws could result in the revocation of a rental permit.

## REGULATIONS AND IMPACTS

Restrictions on residential rental, and particularly short-term rental, can take many forms and have varying degrees of impact on renters, landlords and communities.

- **Prohibition:** The most severe restriction on rentals is an outright ban. This could be community-wide, or limited to certain neighborhoods or districts. A ban might prohibit exclusive-use vacation rentals, but allow home sharing, or impose limits on the length of short-term stays.
- **Amortization:** Establishing a ‘grace period’ in which communities can gradually eliminate certain rental practices allows the property owner to recoup an investment before being forced to discontinue rental use.
- **Geographically-based Regulations:** Communities will often use their zoning authority to restrict short-term rentals to certain districts.
- **Quantitative Restrictions:** The regulation of how many rentals are allowed, rather than where they are located, could take the form of either a fixed numerical ‘cap,’ or a maximum ratio between rentals and residential units.
- **Proximity Restrictions:** Prohibiting rental properties from being within a certain distance of another limits their density.
- **Registration / Licensing Requirements:** Registering for a license or permit for short-term rental may require an inspection, or even the completion of a landlord training program, in addition to fees. A business license, which is attached to an individual rather than the property, is not transferable.
- **Operational Restrictions:** Performance-type standards such as maximum occupancy limits, noise limits, parking requirements and trash and recycling facility storage rules are imposed to mitigate negative impacts often attributed to rental occupancies. Linking the status of a rental permit to tenant behavior is meant to give landlords incentive to screen tenants, and conform to applicable regulations.
- **Special Permit Requirement/Conditions of Approval:** Rental properties might be required to meet certain standards of a community’s land use regulations or adhere to conditions of the zoning board to be granted a special use permit.
- **Remedial Action Requirements:** A landlord or agent might be required to respond to a complaint or to remedy a violation within a given period of time, and in some cases, report back to the city agency that received the complaint.
- **Restriction on Number of Unrelated Individual Residents:** This type of restriction addresses overcrowding of rentals, especially by large groups of students or vacationers.
- **Taxation of Short-Term Rentals:** In order to capture tax revenue from short-term rentals, some states classify them as hotels or tourist accommodations, and may authorize local jurisdictions to do the same.
- **Crime Free Housing Programs:** These police-run programs offering special training in management and community awareness are generally voluntary, though some jurisdictions make participation mandatory for rental properties that exceed an established threshold for criminal activity.



- **New Strategies to Address Airbnb and other Sharing Economy Models:** To counter the trend of owners and investors converting long-term rental properties into short-term rentals, some communities have adopted regulations that require the owner-host to reside in the dwelling unit for a minimum number of days in the calendar year. To keep property owners from engaging in the short-term rental market without obtaining necessary permits or paying required taxes, a community may require online companies to notify hosts that their properties might be subject to local regulation. Some jurisdictions require companies to collect and/or remit taxes on behalf of the host. They may also require hosts to maintain a minimum amount of liability insurance for short-term rentals.

For some **property owners**, the adoption of rental regulations might result in the decrease of rental income, or the loss of it altogether. Many forms of regulation mean an increase in operational costs, and under regulations, a property owner can be held liable for a violation committed by a tenant. Depending on whether it was used as a rental prior to the adoption of regulations, the value of a property could either increase or decrease.

The impact of regulations on **renters** also can be significant. Rental property owners are likely to increase rents to recover increased operational costs; they might also increase security deposits to discourage tenant behavior that might violate a rental regulation. Rental properties might be subject to intrusive inspections, and tenants could be subject to higher risk of eviction. Restrictions that deter investors from buying up properties for the short-term rental market are intended to preserve long-term rental inventory. Others, however, could cause a decline in a community's rental inventory.

Beyond the individuals involved, rental regulation can have a marked effect on economic and societal issues of a **community** at large, including its real estate market, property values, tourism, tax revenue, governmental administrative costs and affordable housing.

## **RENTAL REGULATIONS AND PROPERTY RIGHTS**

Real property ownership in the U.S. is commonly understood to come with a *bundle of rights*—the three core ones being the right to live in it, to rent it and to sell it. It is also generally accepted that some degree of regulation may impose limitations on property ownership, namely through the power of a government to promote order, safety, health, and the general welfare of society, within constitutional bounds. Zoning regulation is derived from this same authority, at the state level, and may be granted to local governments.

Any ordinance that prohibits property owners from renting their homes, or significantly restricts the right to rent, strips them of one-third of their fundamental bundle of economically productive rights. Court decisions have established that property owners are entitled to use and enjoy their property, and that a regulation depriving an owner of property rights cannot be sustained unless it is required by due regard for public health, safety, comfort or welfare.

Constitutional limitations on a government's authority to regulate rental housing include the right to due process, equal protection, "takings" compensation, and protection from unreasonable search and seizure. Statutory limitations on the regulation of residential rentals include fair housing laws and private property rights protection acts. The most common rental restrictions, from licensing and inspection requirements to noise and maximum occupancy limits, and all those imposed by zoning authority, are subject to constitutional and statutory limitations.

## STRATEGIES FOR ADDRESSING PROPOSED RENTAL REGULATIONS

As advocates for property rights in their communities, REALTORS® should be paying attention to any form of proposed residential rental regulation. Does the local legislative body have the authority to adopt the proposed ordinance? Is there an actual need for the restriction?

REALTORS® should engage in collaborative problem solving, and urge local governments to seek input from all stakeholders when considering rental regulations. REALTORS® can help communities avoid over-regulation by suggesting alternatives to new residential rental restrictions, such as stronger enforcement of existing ordinances governing noise, public nuisances, parking and property maintenance standards.

A number of best practice provisions that have been implemented in various U.S. jurisdictions may be acceptable models for REALTORS®, depending on local markets:

- **Adopt narrowly tailored regulations** that address specific, justified concerns.
- **“Grandfathering” provisions** allow the continuation of rental use after the adoption of a restrictive ordinance.
- **Quantitative restrictions** such as fixed caps, proximity restrictions and maximum ratios may be a less severe compromise to an outright ban on rentals.
- **Operational restrictions** on noise, garbage, parking, and negligent property maintenance should be community-wide, rather than targeted at rental properties.
- **Licensing and registration requirements** should not be overly burdensome, and fees should not exceed the city’s cost in administering the registration.
- **Inspection requirements**, when adopted, should be on a periodic rather than an annual basis and/or under specific limited circumstances, such as after a fire.
- **Enforcement provisions** should not penalize rental property owners for violations beyond their control, and should establish a process for the investigation of a complaint or violation before a permit may be suspended.

As a last resort, legal action—or even the threat of legal action—can be an effective strategy for fighting undesirable regulation.

Ideally, when it comes to regulatory issues, REALTORS® should be proactive and vigilant. By pursuing state legislation to require more uniform, fair and market-sensitive regulation of rental properties, REALTORS® can maintain their valued leadership in the community and in the industry. ■

### FOR MORE INFORMATION

Visit <http://www.realtor.org/reports/rental-housing-restrictions-white-paper>

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