

Public ground lease in Amsterdam and the effects on housing

by Iris van Veen MSc MRE, December 2005

1. Introduction

Over a century ago, in 1896, ground lease was set as the standard for land disposal by the municipality council of Amsterdam. And that has not changed ever since. Nevertheless the ground lease system in Amsterdam has changed over time and still is: it has been adapted to meet changes and challenges in its civil and political environment.

In this paper three issues will be addressed. At first the ground lease system, its financial mechanism and its development in time will be described. This will be followed by a description of the present organisation of the ground lease administration. The last part will deal with the effects on housing. Since a long time good housing is an important issue in Amsterdam too. Has the system of ground lease affected the production, distribution and affordability of housing?

2. Ground lease system in Amsterdam

The size of the municipal area of Amsterdam is 21.907 hectares. Amsterdam owns about 70% of it. Over 125.000 ground lease rights have been granted on a total of 3.238 hectares. But what is ground lease? Ground lease is a legal right on land. In the first section the legal system in the Netherlands in relation to ground lease will be shortly sketched. The next section will describe the types of ground lease that the municipality of Amsterdam has granted over the years, and the types of lessees that are distinguished. The last two sections will focus on the financial aspects of the ground lease system. It starts with a brief history of ground lease in Amsterdam from a financial point of view. It ends with an overview of the possibilities of payment of the ground rent and how that ground rent is fixed and changed.

2.1 Dutch legal system

The legal base of the ground lease system in the Netherlands is the Napoleonic Code, which is derived from Roman law. The general principles are therefore shared with other countries which have a legal system based on the Napoleonic Code. In this system a right in rem is different from a right in persona. A right in rem is a right that exist independently of the person that owns the right. It also means that the right can be traded and has a monetary value (Needham, 2003). A right in persona is a right that can only be exercised by the person who it was issued to first: this means that it can not be transferred, and therefore not traded. A right on land is usually a right in rem. Freehold interest is a right in rem and so is ground lease.

Ground lease is defined as the right *“to hold and to use land property owned by another”* (Dutch Civil Code, book 5, title 7, article 85). A building on leased land is therefore also owned by the lessor, although he may not use it and has to pay compensation when the ground lease is terminated!

Anyone who holds the free interest of land may grant a ground lease on it. But ground lease is most known as done by municipalities (Van Veen, 2004).

Municipalities, like other public bodies in the Netherlands, have two sorts of powers available: powers under public law and powers under civil law. Public law gives a public body the power to impose obligations on others (Needham, 2003).

When granting a ground lease and managing it a municipality is using powers under civil law.

Therefore a municipality has to follow the regulations of civil law. Civil law regulates obligations that are freely entered into by two parties (Dornette, 2004). The Civil Code regulates that two parties first agree on the terms (offer and acceptance). In case of a right in rem this process must continue: a contract is made, the notary makes a deed and this deed is registered in the land registry. Only after registration the right in rem is created and/or transferred. The terms of ground lease often include the use of the land: the land may only be used according to the use recorded in the deed.

2.2 Types of ground lease and lessees

Under Dutch law ground leases can have very different forms and shapes, since parties can negotiate on the terms and conditions. Nevertheless ground leases are usually characterized by the duration of the right:

- a ground lease for a limited period;
- a perpetual ground lease with periodic revision¹;
- a perpetual ground lease.

The municipality of Amsterdam has been granting ground leases for a limited period, but most of its ground leases are of the perpetual kind with periodic revision. Perpetual ground leases without periodic revision are not granted, as do other Dutch municipalities.

In the table below a comparison between freehold interest en ground lease in its several and most common shapes is presented.

| | <i>freehold interest</i> | <i>ground lease</i> | | |
|--------------------------------|-----------------------------|--|--|--|
| | | <i>for a limited time</i> | <i>perpetual with periodic revision</i> | <i>perpetual without periodic revision</i> |
| <i>period of lease</i> | perpetual | limited | perpetual | perpetual |
| <i>payment</i> | once, at purchase | annual ground rent or premium | annual ground rent or premium | once, premium |
| <i>mortgage</i> | possible | possible | possible | possible |
| <i>rights to the buildings</i> | to the owner's full benefit | to the lessee's full benefit | to the lessee's full benefit | to the lessee's full benefit |
| <i>transfer by inheritance</i> | possible | possible | possible | possible |
| <i>transfer by sale</i> | possible | possible | possible | possible |
| <i>termination</i> | expropriation | by council resolution (like expropriation) | by council resolution (like expropriation) | by council resolution (like expropriation) |

Table 1: Comparison of freehold interest and ground lease (source: 'Land leasing in Amsterdam', 1999)

¹ The ground lease itself is perpetual, but this time is divided in periods of lease. At the beginning of a new period of lease predetermined elements of the ground lease right may be revised. In Amsterdam the ground rent is revised and a new set of general conditions can be applied.

It shows that the main difference is the period that the right holds (period of lease) and the payment.

In Amsterdam ground leases are sometimes also characterized by the lessee:

- private person
- social housing association

This is done because traditionally the regulations for building and exploitation of social housing have been very different of those for other uses. Therefore social housing associations have special arrangements: special general conditions and a special land price policy.

2.3 A brief history with a financial focus

In this section a brief history of the ground lease system in Amsterdam will be given. The lead is a chronological story showing the changes with a financial impact. Usually these changes resulted in new general conditions. And the changes were the result of problems or flaws in the ground lease system which lessees and/or lessor experienced in practice.

1896

As stated before, in 1896 ground lease was set as the standard for land disposal by the municipal council of Amsterdam. The discussion on the introduction of ground lease as a standard had lasted six years. On 23rd September 1896 eighteen out of thirty four council members supported the resolution. The main reasons for the introduction were financial and of planning:

1. to capture the increase of the land value for the community;
2. to extend the influence of the municipality on housing and planning.

With ground lease as the standard of land disposal came the first set of general conditions (AB 1896²). The AB 1896 clearly state that it was ground lease for a limited period, in this case the period of lease is 75 years. A fixed ground rent has to be paid in two half-yearly instalments. The use must be according to the one recorded in the deed of granting. The municipality has to give permission before a lessee is allowed to change the use or the building.

1915

After another six years of discussion and several suggestions on 3rd December 1915 the municipal council adopted a resolution that meant a major change in the ground lease system. The reason for this change was that there had been a general crisis in building in 1907 and 1908 and that the system of ground lease for a limited period had some flaws. Lessees found it difficult to get a mortgage on these rights. Ground lease was also not popular among investors, because at the end of the period the value of the building was not compensated to the lessee. And the municipality feared that lessees would not maintain their buildings properly near the end of the lease (Jesterhoudt, 2004). Perpetual ground lease with a periodic revision was the answer to these flaws. It was introduced for grounds that were to be used for housing, except when the lessee was a social housing association. And it worked.

² AB 1896: AB is the abbreviation of Algemene Bepalingen, which means General Conditions. To indicate the specific set of general conditions it is followed by the year the municipal council adopted them.

To implement these changes new general conditions were adopted: AB 1915. They describe the perpetual nature clearly and the procedure of the revision. The revision includes the determination of a new ground rent and the possible application of a new set of general conditions to the ground lease right in a new period of lease.

1934

As a result of a change in national legislation - Housing Act - in 1931 the AB 1934 for perpetual ground lease with periodic revision were adopted by the municipal council in 1934. The terminology for describing the land use had changed compared to that in the AB 1915. None of the financial conditions were changed.

1937

In 1937 new general conditions were adopted, in which the option of paying a premium (payment of ground lease instalments in advance) was introduced.

In 1915 the mayor and aldermen (municipal executive) had agreed that motivated requests for extensions of ground leases for a limited period would be complied with. Nevertheless, the industrial sector had some problems with the uncertainty that came with the limited period: e.g. lessees were never certain if they would get an extension and under which conditions. They also felt uncertain if they would be able to pay the ground rent in economically difficult times (Jesterhoudt, 2004). One must bear in mind that specially the 1930's were times of economic recession. In 1934 a municipal committee came with a final report that presented a number of measures to solve the problems. E.g. lessees were given more certainty for extension and bigger compensation of losses when leases were not extended. And as an answer to the concern of not being able to pay the ground rent in more difficult times, the option of paying a premium was suggested.

After discussing this report sets of general conditions were prepared and adopted by the municipal council in 1937: AB 1937 for ground lease for a limited period for industrial use, AB 1937 for ground lease for a limited period for non-industrial use (used when the lessee was a social housing association, although the option of paying a premium was always excluded in their contracts) and AB 1937 for perpetual ground lease with periodic revision.

Again, the faced problems were met resulting in a change of policy and the implementation of new general conditions.

1955

In 1951 the Apartment Act was adopted by the national parliament. This legislation regulated the ownership of apartments ('horizontal ownership'). As a consequence the three sets of AB 1937 had to be adjusted to this legislation (Jesterhoudt, 2004). Three new sets were adopted in 1955. No financial conditions were changed.

1956

In 1956 a special set of general conditions was adopted. They were to be used for grounds with an agricultural use. To give way to new housing neighbourhoods farmers were relocated to new land. Nowadays ground lease rights with these general conditions are almost non-existent (Jesterhoudt, 2004).

1966

In 1966 the AB 1966 for perpetual ground lease with periodic revision were adopted by the municipal council. Again this meant a major change in the history of the system in Amsterdam. The change consisted of three things. First of all, these AB 1966 were to be used in all cases, except in case of social housing. Second, the indexation of the ground rent every five years was introduced. And third, the period of lease was limited to 50 years: after 50 years the ground rent would be revised. Both the indexation and the limitation of the period of lease had to do with inflation. After World War II and especially in the 1960's the value of money had decreased: inflation occurred. The ground rent was not adjusted during a period of lease (75 or 50 years), but its value was decreasing. Land prices on the other hand were not. In the short term the municipality wanted to have a ground rent that would not suffer from inflation so much (Jesterhoudt, 2004). Inflation also increased the land values and the longer a period of lease, the longer the municipality might have to wait to capture this increase.

1985

In 1982 the municipality and the federation of social housing associations (AFWC) started to negotiate on several issues in housing. The municipality had bought many houses from private landlords in urban renewal areas and wanted social housing associations to manage them: they were to be granted in ground lease. And as the first ground leases for a limited time were about to expire, this issue was brought up by the social housing associations.

In 1984 an agreement was reached. The social housing associations would take the houses on ground lease from the municipality: they would renovate and then manage them. A special arrangement was designed: the period of lease would be 30 years and the ground rent would be adjusted to inflation after 15 years. But it was still ground lease for a limited period: the municipality did not want to change this policy. This type of ground lease provided the municipality after expiration with the land and the buildings without the need to compensate the social housing association: the municipality would therefore be able to continue to provide good housing.

Since 1966 social housing associations were the only ones that got new ground lease rights for a limited period. This set was not specially designed for this purpose, so in practice several conditions of the AB 1955 were excluded (Jesterhoudt, 2004).

Although it took some time, in 1985 social housing associations got their own set of general conditions, especially for grounds for social housing: AB 1985.

1990

In 1990 the municipal council adopted a bye-law ('Moderniseringsbesluit' or Resolution of Modernisation). This bye-law contained several regulations of which two are relevant here. The first one states that the period of lease can be extended with 50 years (maximum), if the lessee of a perpetual ground lease right with periodic revision requests it. In that case the ground rent has to be paid as a premium (till the end of the extended period of lease). This premium consists of two parts: the premium for the rest of the original period of lease and the premium for the extension. The premium for the extension is a percentage of the premium for a full period of lease (50 years) at the start of this period of lease. The percentage was fixed at 25%. This premium compensates the municipality for the fact that the ground rent is not revised after 50 years. N.B. This option of extension for lessees was withdrawn in 2000. The second one states that the indexation every five

year (AB 1966) can be excluded. In that case the ground rent is increased by a maximum of 25%. The increase is lower when ground rent indexation has taken place in the past.

The changes were initiated through discussions with the business community of Amsterdam. In these discussions many issues were brought up including ground lease. At the beginning of the 1980's the interest rates were high. A lot of people could not pay their mortgage and were forced to sell their house. The high interest

rates made buying a house very unattractive or even impossible. So the supply of houses increased and the demand decreased: as a result prices in the real estate market dropped dramatically. The drop in prices included the prices of land. On the other hand inflation was still around increasing the ground rents.

This made ground leases financially very unattractive: a bad and unwanted development for both

lessees and lessor. Both measures (the extension of 50 years under the condition of premium payment and excluding the indexation) gave the lessee the option to stabilize their expenses on housing for a longer period of time.

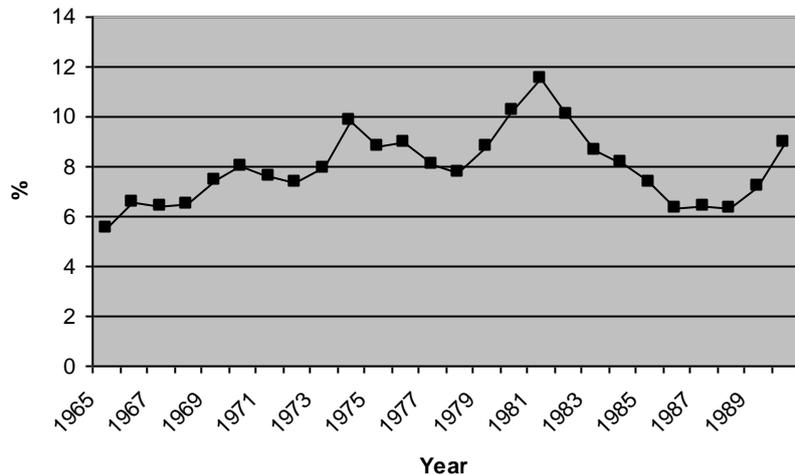


Chart 1: Interest rate at capital market 1965 – 1990
(source: Centraal Bureau voor de Statistiek)

1994

On 1st January 1992 the New Civil Code took effect. Therefore it became important to adjust the AB 1966. A new set - AB 1994 - was the result.

These AB 1994 included the policy change of 1990 (the extension with 50 years and excluding indexation), as well as some other -juridical- changes. No other financial conditions were added.

1998

In the beginning of the 1990's a change in policy on a national level took place: government and social housing were separated. As a result the social housing sector became independent and had to take financial care of their business themselves: loans and subsidies were abolished. Social housing became a local matter and social housing had to be realised through agreements between social housing associations and the municipality. And as the first ground leases for a limited time were about to expire, the issue of ground lease was brought up by the social housing associations.

Till then the municipality had always denied perpetual ground lease with a periodic revision to social housing associations: after expiration the municipality would always get the land and the buildings without compensation for the social housing association, and would therefore be able to continue to provide good housing. In the light of the new developments of the social housing sector this was no longer considered necessary. In 1994 the municipality and the federation of social housing

associations (AFWC) in Amsterdam started to negotiate about converting the ground leases. Criteria of the municipality were (Jesterhoudt, 2004):

- different lessees should be treated as equal as possible;
- the revenues must be used for investments in the city.

Criteria of the federation were (Jesterhoudt, 2004):

- security about the conditions under which social housing was to be exploited in the long term;
- the conditions need to be in line with the financially necessary and socially desired rent and investment policy of social housing associations. The conditions should make it possible to exploit the property competitive to property on owned land.

In 1997 an agreement was reached. New grounds will be granted in perpetual ground lease with a periodic revision. The period of lease is 75 years.

Existing ground leases for a limited period can be converted at three occasions:

1. at expiration of the ground lease
2. in case of major investment in the property
3. in case of division of the property for sale to the tenants

After the conversion a period of lease of 75 years will start. The ground rent has to be paid as a fixed premium. These premiums are indexed (full inflation) every year. Not only do the premiums differ from year to year because of the index, the premium differs also according to the age of the property. Four groups are seen: before 1945, 1945-1958, 1959-1975 and after 1975. Generally the groups represent a style of building (size, volume, etc.), a method of financing social housing and a certain rent. During the negotiations rents were compared, land was valued and ground rents were reported by appraisers. The groups were formed and the premiums agreed upon, finally in exchange for extension of the period of lease from 50 to 75 years. The surplus of the premiums would be transferred into the 'Fund to Stimulate Building Houses'. Social housing associations would get a contribution from this fund for the realization of redevelopment of their property in certain areas of the city.

On 18th September 1998 the municipal council adopted a new set of general conditions, especially for social housing associations. Many conditions were derived from those in the AB 1994 (remember that the first municipal criterion was that different lessees should be treated as equal as possible). In a separate bye-law the conversion, its conditions, the premiums and the indexation are described.

2000

On 15th November 2000 the municipal council adopted a new set of general conditions for perpetual ground lease with a periodic revision. It marked the end of a period of four years of discussion and research on the question what the municipality wants with ground lease and what the system should look like.

It started in September 1996 when the ground lease system celebrated its centennial anniversary. A meeting of friends and opponents of the system was organized. It brought up the question if the system was accepted and still legitimate. Early 1997 the municipal executive ordered a thorough investigation: operation 'Big maintenance' started.

In 1998 a report was published by the municipality and several involved groups, like representatives of businesses, real estate developers and real estate agents, were invited to give their comment. This resulted in a final report in January 2000.

The report had four conclusions (Jesterhoudt, 2004):

1. the arguments to introduce the ground lease system still hold;
2. the financial system is out of balance at some points;
3. the communication needed to be improved, to increase acceptance of the ground lease system;
4. the use of revenues of the ground lease system for new investments in the city should be made visible, to increase acceptance of the ground lease system.

The second conclusion will be explained. First of all the expenses of a lessee with a ground rent that is indexed every five year are relatively high. This is mainly caused by the ground rent rate which is based on a municipal rate which covers inflation too. Therefore one can state that inflation is to be paid twice. On the other hand the expenses of a lessee that pays a fixed ground rent or a premium are based on expected economic developments. Secondly a premium for a full period of lease (50 years) was usually higher than the land value and therefore difficult to explain to lessees. In case of housing paying a premium was by obligation and not by choice.

After looking carefully into the ground lease system and other options an alternative system was developed (Gemeente Amsterdam, 2000). Criteria for development were:

1. more freedom of choice for the lessee;
2. the financial system has to be in line with the market;
3. to capture the increase of the land value for the community.

Foundation of the system was still perpetual ground lease with a periodic revision in which the period of lease is 50 years. Experts stated that financial agreements for longer periods like one hundred years were very uncommon in the (financial) market, and shorter periods would cause uncertainty and therefore were no option (Gemeente Amsterdam, 2000). So after 50 years the ground rent will be revised in line with the values at the time of revision. This also meant that the extension as introduced in 1990 and entered into the AB 1994 was not wanted anymore.

Options of payment in the alternative system were:

1. a premium;
2. an annually indexed ground rent;
3. a 10-year fixed ground rent;
4. a 25-year fixed ground rent.

A premium for the full period of lease would be fixed at the land value. A premium for a period starting after the start of a period of lease would be based on the index-linked land value (Gemeente Amsterdam, 2000).

The annually indexed ground rent was introduced, because it shows a clear relation to the land value. Every year the ground rent is indexed. The suggested index was based on inflation +/- 1% (inflation of 5% would give an index of 1,04) to keep in line with ground rents after revision (Gemeente Amsterdam, 2000).

The 10-year and 25-year fixed ground rent are adjusted every 10 or 25 years. In the Dutch mortgage market (for houses) the interest rate can be fixed for a chosen period of time: semi-long is 10 years and long is from 20 to 30 years (30 years is usually the maximum time of a mortgage). And where the new interest on a mortgage is calculated by using the actual interest rate, here a new ground rent is calculated by using the actual ground rent rate. All ground rent rates are derived from the returns on bonds issued by the Dutch national government and will be fixed every three months instead of every year to be more in line with the market. (Gemeente Amsterdam, 2000).

The municipal council agreed with the conclusions and so the choice for ground lease was confirmed. A new set of general conditions was prepared accordingly and adopted in November 2000. The option of extension of a period of lease as far as a part of the Resolution of Modernisation was withdrawn. Of course this was not possible for rights under the AB 1994. The new policy on calculating a premium would apply for all premiums independent of the general conditions: the calculation is described in a bye-law and this bye-law was changed accordingly.

2.4 Ground rent: options of payment and calculation

In Amsterdam the ground rent is calculated as the product of the land value and the ground rent rate: $\text{ground rent} = \text{land value} * \text{ground rent rate}$. Since the land value is the base the land value will be discussed first. It is followed by two sections about the choices of payment: ground rent and premium. The final section addresses the adjustment of the ground rent and its problems.

2.4.1 Land value

A well known and often used approach to value land is the residual value approach: $\text{land value} = \text{proceeds} - \text{costs}$. The municipality of Amsterdam has a land price policy that is updated at least every year. Since 1996 the 'standardized residual value' approach is used to value most of the grounds³. This means that the land value is determined from the standard building of that size and use at that location. A use that generates a higher rent or sales price means a higher land value.

Before the ground lease is granted the lessor and the intended lessee negotiate on the land value (and the ground rent). In essence both parties use the same approach, but argue about the value of the parameters. Although negotiations can be tough, this approach does not cause many problems in the process of granting a new ground lease.

Problems start as soon as a building has been erected on the land and the ground rent has to be adjusted because of a change of use, change of building and periodic revision at the termination of a period of lease (see section 2.4.4.).

A very important reason for these problems is the lack of one approach to value a ground lease right where a building is present on the land. Experts do not agree on the approach: not in the Netherlands as well as in other parts of the world (Hong, 2003). They also discuss the parameters. In the end very different values are the result.

Many approaches start at: $\text{land value} = \text{value of land and building together} - \text{value of building}$ (Van Veen, 2004). But how can the value of land and building be separated? Here we find the second reason. In Amsterdam the sale of a ground lease right (for housing) is hardly considered as the sale of only the building. Lessees are not well informed that they have a ground lease right and they are

³ E.g. this approach is not used when the ground is used for social housing (fixed prices) or recreational use (tailor made pricing).

often not aware what it means that it is a ground lease right. It is an example of the non-transparency of the real estate market.

The third reason follows from the second: the lessees do not take the financial consequences of ground lease into account. They are not able to calculate the difference in value between a ground lease right with a ground rent paid as a premium and a ground lease right with an annually indexed ground rent. A research of the Department of Local taxes showed that only around 60% of ground rents that are to be paid in the future was in the sale price of houses (Francke, 1996).

The fourth reason can be found in the behaviour of real estate agents. They should inform their clients well, but some of the may not understand the financial consequences completely themselves and others have other personal interest as well. E.g. their commission depends on the sales price: noting the fact of ground lease may lower the price and therefore their commission. Another example is that some of them act as expert appraisers in process of revision at the termination of period of lease and they may not want to be known as the ones that fix high land values, for people might not come to them for the sale of their house.

2.4.2 Options of payment: ground rent

In January 2006 a premium has been paid for 75% of all ground lease rights; on 25% a ground rent is paid in two instalments per year. The total of annually collected ground rent is around € 80 million.

The ground lease system has had its share of shapes of ground rent. An overview:

- fixed ground rent: AB 1896, AB 1915, AB 1934, AB 1937, AB 1955;
- ground rent to be indexed every 5 years: AB 1966 and AB 1994;
- ground rent, indexation every 5 years excluded: AB 1966 and AB 1994;
- ground rent, to be indexed every 15 years (social housing associations only): AB 1955 and AB 1985;
- annually indexed ground rent: AB 2000;
- 10-year fixed ground rent: AB 2000;
- 25-year fixed ground rent: AB 2000.

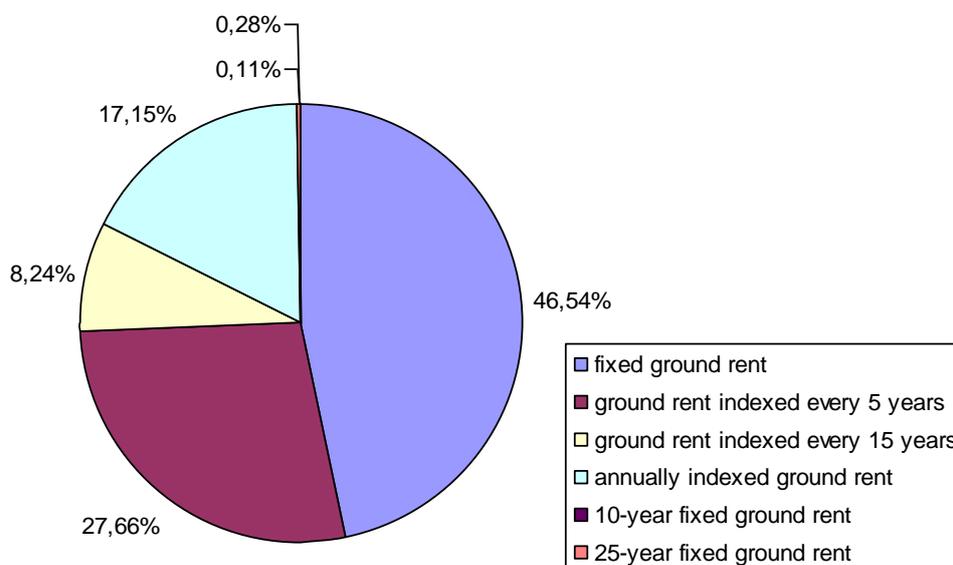


Chart 2: Share of ground rent (as on 24th January 2006, source: Ground Lease Office)

The ground rent is the product of land value and ground rent rate. Until 2000 the ground rent rate was fixed every year by the municipal council. The rate was derived from the (weighted) interest rate that the municipality was paying on its own loans. If the interest rates were high, the ground rent rate would be fixed high too.

From 2001 on the ground rent rates are fixed every three months by the municipal executive. And they are derived from the returns on bonds issued by the Dutch national government. The rate for an annually indexed ground rent is derived from the returns on those five bonds (Treasury bonds) which have the longest term (Gemeente Amsterdam, 2000). These bonds are considered to be risk-free. And since the ground rents are to be indexed annually, they will stay in line with the long-term development of land values and have no risk too. The 10-year fixed ground rent rate is derived from the returns on bonds with a term of 9 till 10 years, and the 25-year fixed ground rent rate is derived from the returns on those five bonds (Treasury bonds) which have the longest term (Gemeente Amsterdam, 2000). These rates have a supply added. The reason for this supply is the difference in rates on bonds and loans for national government and municipalities, and the debt risk and administration costs.

2.4.3 Options of payment: premium

Premiums were introduced for the first time in 1937. Nor in the AB 1937 nor in its successors one will find a description of how the premium is determined. The method to calculate the premium is described in a bye-law, adopted by the municipal executive and according to guidelines of the municipal council.

The premium is the payment of the ground rent instalments in advance. Until 2000 the premium was calculated as the present value of ground rent instalments until the end of the period of lease (maximum of 75 or 50 years depending on the set of general conditions)⁴. In the years 1991 until 2000 the discount rate was fixed at the same level as the ground rent rate (and above 6,38%). This explains why it was possible that the premium could exceed the land value.

In 2000 the municipal executive adopted a new bye-law as a result of operation 'Big Maintenance'. The premium for a full period of lease (50 years) was fixed at the land value. The consequence was that the discount rate is now calculated from the expression that is usually used to calculate the premium. With the introduction of three new ground rents the municipality realized that the level of these ground rents could differ a lot on the long term. To continue using the method of calculation would cause huge differences in premiums (for comparable properties): lessees would not understand that and would protest. The method of calculation was adjusted: instead of using the real ground rent of the right a ground rent would be calculated as the product of the index-linked land value and the actual ground rent rate.

$$^4 A = \frac{C * (1+i)^t - 1}{2 * (1+i)^t} * \frac{(1+i)^{\frac{t}{2}}}{(1+i)^{\frac{t}{2}} - 1}$$

in which:

A = premium for t years

C = ground rent

i = discount rate;

t = number of years of payment in advance.

The index-linked land value is the land value at the start of the period of lease indexed with the inflation +/- 1%: it shows the average development of land values on the long term. This way the premiums are calculated from a form of actual ground rent and differences in premiums will depend on the difference in land value and not on the shape of the ground rent.

2.4.4 Adjustment of the ground rent

The ground rent can be adjusted during the period of lease in case of:

- a change in use;
- a change of the building.

The general conditions state that the municipality has to give permission for these changes. If the requested change is in line with the town planning, permission will be given under the condition that the ground rent is adjusted.

These changes were mostly detected when a lessee applied for a building permit, since he would need that permit before starting. The process of changing a right is basically the same as that of granting: offer and acceptance, followed by a resolution and deed that is registered at the land registry.

The adjustment is calculated as the product of the change in land value and the ground rent rate⁵. The change in land value is calculated as the difference of the land value after and before the change, and the land value being the product of area (in m²) and land price (per m²). The land prices are derived from building in mass. This causes problems when it is only a small change: the increase of the property will not cover the costs of the change including the adjustment of the ground rent. Lessees who wanted to change relatively small things on their house, like an extension of the living room or the attic, started to protest the last 5 to 10 years. It is also this period that the number of owner-occupied houses in Amsterdam increased, as well as that the economy prospered very much. Since January 2003 building permits are not necessary in all cases of a change of the building. This and the protests have led to the latest change in the system (effective August 2005). Now lessees of rights that are to be used for housing, do no longer need to have their ground rent adjusted in case of change of the building.

The ground rent is also adjusted at the termination of a period of lease. This is the periodic revision. This adjustment is easy to detect since it is triggered by time. The general conditions and the legal regulations from the Civil Code create the process of change: lessor and lessee choose an expert and they choose a third, these three experts value the ground lease right and fix a completely new ground rent, the lessor sends the lessee a letter with the new ground rent, a resolution is adopted and a deed is recorded and registered.

This adjustment can be high, because usually the ground rent has been unchanged for 75 years. In the mean time the land value increased and inflation did its job. Lessees have protested and some have filed a lawsuit. In section 2.4.1 reasons for this problem were mentioned: a lack of an accepted approach to value land (ground leases), a lack of communication and a lack of information. What worsens it from the municipal point of view is the decrease in trust in the government and the

⁵ A negative adjustment is set to zero: the ground rent may not decrease as the result of a change requested by the lessee.

increase of behaviour as a 'home economicus' (a maximum of revenues with a minimum of effort) (Van der Laan, 1997). At the moment of writing no proper solution has been found, although the municipality is investigating several options.

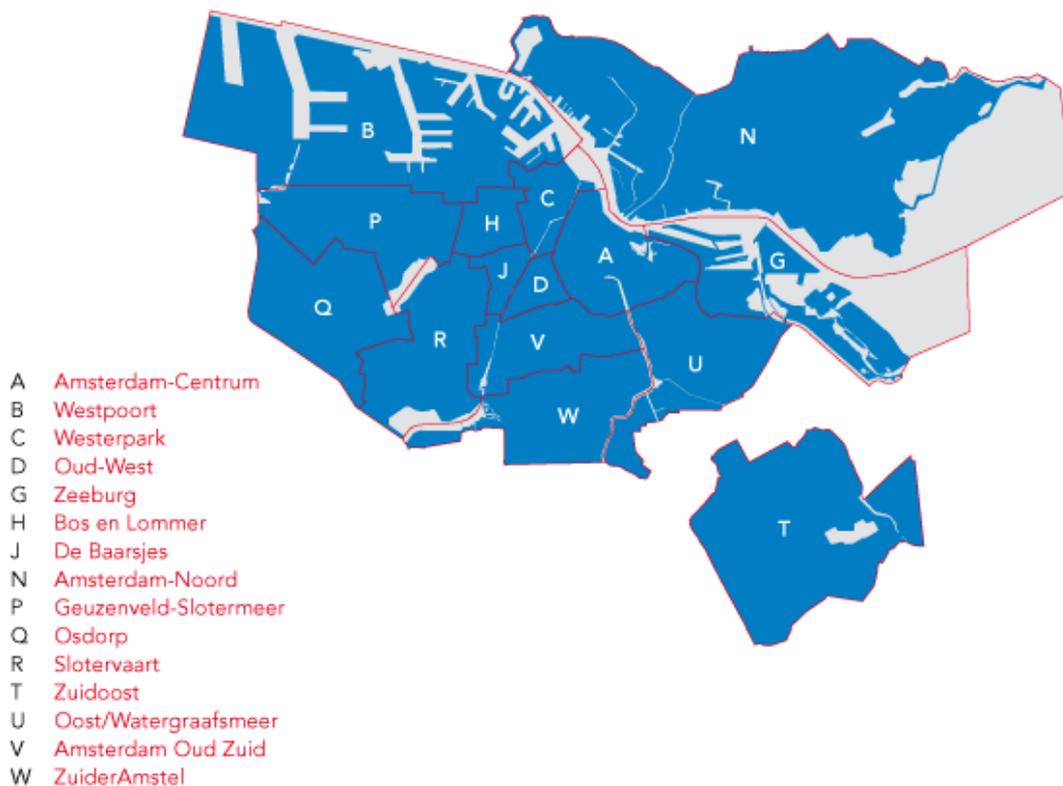
3. Administration of the ground lease system

The ground lease system is administered by the municipality of Amsterdam. To understand how it is administered the first section describes the organisation of the municipality and the several tasks and responsibilities of its parts. The second section shows the relation between real estate development projects and ground lease administration. Finally the last section deals with the Ground Lease Corporation and its results.

3.1 Organisation of the municipality of Amsterdam

The Municipality of Amsterdam is governed by the municipal council. Daily business is done by the Mayor and Aldermen (or municipal executive).

The municipality of Amsterdam is divided into 14 urban districts and one area which includes the harbours (and which is named Westpoort). The municipal council has transferred an extensive part of her powers to the urban district⁶ councils. Roughly said: the urban districts function as municipalities within the municipality of Amsterdam.



⁶ Urban districts are also known as city districts or neighbourhoods.

Picture 1: Boundaries of the urban districts and the harbour area of the municipality of Amsterdam⁷

In the urban districts daily business is done by the urban district executive. They also have their own budgets and civil servants. Westpoort on the other hand is governed by the municipal council. The municipal council and municipal executive also have their own budget and civil servants. The civil servants are organized in several department and corporations, e.g. Town Planning Department and the Development Corporation. Part of the Development Corporation is the Ground Lease Office, the department that administers the system and some ground lease rights.

The relationship between the central municipal council and the urban districts councils and the transfer of powers is described in a resolution of the municipal council, called 'Verordening op de stadsdelen' (Bye-law Urban Districts).

Among the powers that are transferred from the central municipality to the urban districts are those concerning town planning, the production of building plots and the administration of ground lease contracts. Although an extensive part of the powers are transferred to the urban district councils and their executives, the municipal council can still give guidelines in many fields. In this way it is secured that citizens are treated equally in equal cases or that a coherent policy is implemented.

From the above the conclusion is that the ground rent system is administered by Ground Lease Office and the urban districts together. But which organisation does what?

The administration of ground leases located in the urban districts is done by the urban districts. This implies that they are authorized to grant ground leases, to change them and to check if the conditions are lived up to. Checking is done according to a policy as to prevent from being accused of arbitrary. Therefore checking is done area wise or theme wise: e.g. checking use of grounds as garden in an urban district or checking size and use of grounds in an industrial area.

The administration of ground leases located in Westpoort is done by the Ground Lease Office. The Office grants, changes and checks ground leases just as urban districts. It may therefore not be a surprise that it also supports the urban districts if required. But the Ground Lease Office is also the part of the municipal organization where the system is administered: they take care of the policy on ground lease. The policy does not include land price policy: this speciality is done by another department of the Development Corporation. And last but not least: the Ground Lease Office is responsible for the collection of ground rents and premiums and also for the production of the annual budget and accounts of the Ground Lease Corporation.

3.2 Real estate development projects and ground lease

The municipality of Amsterdam has an active ground policy. It means that they are active in realizing real estate according to their plans, and therefore their ideas: the municipality has an active role in the realization of projects of real estate development and part of the project is granting ground leases. But how is the development separated from the administration of ground lease?

The active role may include buying property (or if necessary expropriating), tearing down buildings and preparing plots for new buildings, granting new ground leases and lay out streets and parks

⁷ As published on www.os.amsterdam.nl (23rd January 2006)

(public space). For these real estate developments the municipality draws up a land exploitation scheme. This scheme includes the cost of property acquisition and of preparations for buildings as well as the proceeds of the 'sale'. However, in Amsterdam the land is not sold, but the ground lease right. And it may only be sold to the Ground Lease Corporation at the land value as agreed with the lessee. The Ground Lease Corporation subsequently administers these rights and thereby collects the ground rent or premium (Van Veen and Van Asselt, 2002).

In this way the relatively short period of land production and the longer period of administration are clearly separated. This separation also makes it possible to establish the result of each separate plan. The project has its proceeds from the 'sale', but it also has costs. After realization of the development the future value of the proceeds minus the future value of the costs determine whether the project has a profit or a loss. Is the result negative and should money from public funds be contributed or is the result positive thus allowing money to flow into public funds? For this purpose the municipality of Amsterdam has the Equalization Fund; this fund is administered by the Development Corporation. Surplus balances are paid into this fund and it can be used to fall back on in case of deficits. (Van Veen and Van Asselt, 2002)

3.3 Ground Lease Corporation and its results

The financial result of the ground lease system is shown every year in the annual accounts of the Ground Lease Corporation. The net result is a source of income for the municipality. The total net result consists of three parts: the net result of exploitation, the net result premium and the net result for the Fund to Stimulate Building Houses.

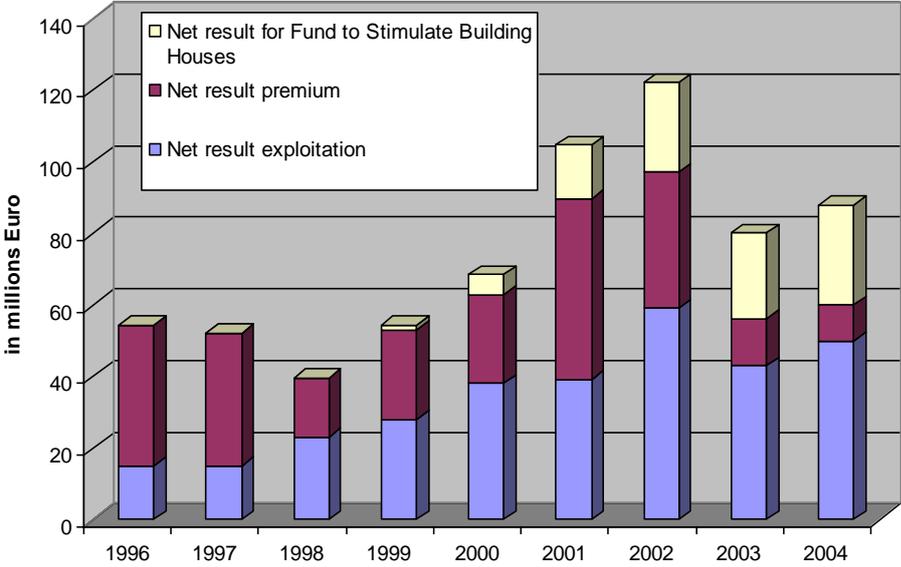


Chart 3: Net result of the Ground Lease Corporation (Gemeente Amsterdam, 2004)

The net result premium is the surplus of premiums paid by private lessees. The net result for the Fund is the surplus of premiums paid by the social housing associations when converting ground

leases (see 2.3.). These two results are incidental results, and therefore may change substantially every year. The net result of exploitation is a structural result and much more stable. The net result of exploitation is the difference between the proceeds and the costs of the ground lease system. The largest portion of the proceeds is the collected ground rents. Costs are made for staffing, lawsuits, communicating, IT etc. The largest portion of the costs is costs of interest that have to be paid on the loan for buying the ground lease rights from the projects. These costs are over 90% of the total costs, so the costs depend heavily on the interest rate and the volume of the loan. The loan is given by the Central Financial Department and they yearly fix the interest rate. The volume of the loan is the total of the book value of those ground lease contracts which pay the ground rent (non-premium).

4. Effects on housing production, distribution and affordability

As much as ground lease is part of the Amsterdam, so is good housing. But has the system of ground lease affected the production, distribution and affordability of housing? In the first section a brief history of the housing market in Amsterdam is given to show the factors that have dominated housing. In the next sections the housing production, distribution and affordability are related to the ground lease system.

4.1 Housing in Amsterdam

In the second part of the 19th century thousands of people move from the country side to the towns and cities as a result of the agricultural crisis, and workers settle near the upcoming industries. E.g. in 1900 Amsterdam had 2,5 times as much inhabitants as in 1830 (Ottens, 2000). So the pressure on the housing market is huge attracting many small businessmen that go into housing. The risks are small and the revenues are certain as the demand is rising. Some speculate on land value increases, some get rich by building and others become rack-rent landlord. In a short time land prices go sky high (Ottens, 2000). The quality of the houses is bad and hardly improves: on the average 4 to 5 people lived in houses of an average size of 20 m² with hardly any toilets and no water (Ottens, 2000; Van Dieten, 2000). It also causes health risks as in these complexes diseases emerges and start to spread among the whole population of towns. The state did not interfere for it was believed that its duty is only to secure the nation, the public order and the authorities. The well-being of citizens is their own concern. And why should the freedom of enterprise that made the industry bloom not work in urban expansion? (Ottens, 2000)

Municipalities did not always agree with the non-interference view, but had limited finances and limited public powers. In Amsterdam the introduction of the ground lease system in 1896 provided the municipality with planning powers: the use could be recorded in detail in the deed of granting and compliance of the use accordingly could be enforced! It was an important reason for the introduction of the ground lease system, since they had no public powers to do so. Even nowadays ground lease provides the opportunity to describe the use in more detail than possible in zoning plans or in land use plans; the municipality of Amsterdam uses this feature of ground lease as much as possible.

In the course of time the state's attitude towards non-interference changed and the Housing Act was adopted in 1901. The Housing Act gave municipalities the obligation to adopt local regulations on

building (building permit and inspection, also on existing houses). And it made it possible to provide social housing associations with loans and annual financial contributions. Social housing associations were only acknowledged in case their only objective was providing housing in a non-profit way to those who could not provide housing to themselves (Van Dieten, 2000).

Until World War II (in the Netherlands: 1940-1945) social housing was not important in Amsterdam:

still most of the building was done by private parties, but now according to local regulations.

After World War II social housing became very important, not just in Amsterdam. During the war over 80.000 houses had been demolished and they needed to be replaced. In the 1960's the demand for housing was still much higher than the supply as children had grown up and wanted to get married and move out. Amsterdam had relatively many low income citizens, as usual in large towns and cities.

To provide them with housing the municipality and the social housing associations worked together to build new neighbourhoods with mainly social housing.

During the 1970's the attention shifted from urban expansion to urban renewal, from quantity to quality of housing. This meant that on the national level the policy of expanding smaller towns in large ones to provide people in the main cities with housing was adopted and implemented. This emphasized the policy of urban renewal in the cities. In Amsterdam tenants protested against urban renewal after some time, because they could not or hardly afford the rents of the new houses. Urban renewal included both renovation of complexes (often preceded by buying from private parties) and tearing down and building. It was done by the municipality and the social housing associations on a large scale, within a system of loans and annual and one time contributions. Again: state financed and government controlled. The ground lease system was adapted to it.

Around 1990 the field of social housing changed completely (operation Heerma). The system of loans and annual contributions was abandoned: in return social housing associations got a lump sum. From that moment on social housing associations were 100% responsible for their finances. In the long run they have to make money through wise portfolio management, smart property management and partly profitable projects to finance the building and exploitation of social houses. This process of change is still going on and they are acting more and more commercial to secure their financial position. The ground lease system has adapted to this again. Nevertheless the existing ground lease rights can not be adjusted to the new circumstances. This may result in problems in the future now the system of checks and balances in social housing in relation to ground lease is disturbed. On a national and local level the 1990's also brought the insight that there is still a demand for housing, especially for houses to own. And nowadays the demand and the providing of housing is still an issue: four years ago the alderman for housing determined the goal to have the building of 16.000 houses starting within four years; the goal was achieved.

From the above two conclusions can be drawn. The first conclusion: the demand for housing has been higher than the supply for a very long time, and continues to do so. Mainly the demand has

| Year | private | social | Total |
|------|---------|--------|-------|
| 1910 | 1233 | 120 | 1353 |
| 1920 | 317 | 420 | 737 |
| 1930 | 5263 | 845 | 6108 |
| 1940 | 2176 | 0 | 2176 |
| 1950 | 45 | 2665 | 2710 |
| 1960 | 533 | 4198 | 4731 |
| 1970 | 421 | 3357 | 3778 |
| 1980 | 982 | 13 | 995 |
| 1990 | 1500 | 3299 | 4799 |
| 1999 | 2497 | 955 | 3452 |

Table 2: number of new houses per year in Amsterdam in 1910 – 1999 (source: Van Dieten, 2000)

come from its low-income citizens. The second is that social housing and social housing associations have played a major role in Amsterdam during the period of urban expansion and urban renewal.

4.2 Housing production

As shown in table 2 till World War II most houses in Amsterdam were built by private parties to use them themselves or to rent them out to others. Social housing associations built a small number of houses for their members.

From World War II till 1990 these positions changed: most houses in Amsterdam were built by social housing associations, except in the period of urban renewal. Other parties build only small numbers of houses compared to the numbers by social housing associations. The municipality wanted to provide housing to its low-income citizens. Social housing was mainly financed by the state and government controlled. The ground lease system was adapted to the financing system of social housing: a fixed ground rent was paid and later this changed to a premium for the first period of lease (52 years: 50 years of exploitation and 2 years of building). Land values for this type of use are based on the financial system of social housing and not on the market, since these investments show a negative net present value (assuming exploitation as social housing for the complete lifetime). Since the ground lease system was adapted to the financing system of social housing it caused no problem to build houses. The policy in Amsterdam to realize housing through social housing associations created a very well functioning machine. It is most likely that this policy has prevented others from the 1970's to build housing on a large scale: it closed the doors for others. On the other hand developers and investors find development of agricultural land (urban expansion) usually more attractive (easier and less financial risks) than urban renewal

As a result of the high production of social housing around 17% of the houses in Amsterdam in 1990 were indicated as an owner-occupied house. From 1990 many commercial rental houses and owner-occupied houses have been built by professional housing developers according to demand. This period has shown that now housing production is much more sensitive to the economic situation than before. When people have less money or do not feel too confident about it, they will not buy a house or move to a more expensive apartment, in which case no houses will be built.

All together the housing production in Amsterdam has not been effected by the ground lease system, but by the way the financing is structured and the involvement, or lack thereof, of government.

4.3 Housing distribution

The social housing system did not only made it possible to realize social housing, but also had strict rules for assigning its houses to tenants, like maximum income levels or a minimum number of family members. Considering the fact that the total of social houses outnumbers those of other housing types this means that the housing distribution in Amsterdam was and is mostly regulated by laws and bye-laws.

Through the ground lease system the use of land can be regulated and compliance accordingly can enforced if necessary. This prevents that use is easily changed when another use is economically more interesting, e.g. from housing into shopping space or from rental housing into owner-occupied housing. This gives ground lease the feature of conservation, if wanted by the lessor.

With the independence of social housing associations they also got the opportunity to sell houses from their portfolio of social houses to tenants. This attributes to the municipal objective to increase the total of non-rental houses. It also generates cash-flow for the social housing associations that is to be used to build new social houses and to redevelop social housing complexes. The municipality allowed that the involved ground leases were split; in fact a special unit was added to the Ground Lease Office to do this quickly and efficiently.

Housing distribution was affected by the ground lease system, but almost only when and in the way the municipality, being the lessor, wanted.

4.4 Housing affordability

The social housing system also includes rules for setting rents of social houses, like the size of the house and its facilities (but not the location). These rules plus those for assigning (e.g. maximum income level) should regulate that tenants pay rents that they can afford, or they may be entitled to receive a monthly rent contribution from the state. Of course this system has its drawbacks. When the income of tenants rises, they only want to move out of their house to another house if the new house is according to their demands (rent or owner-occupied, size and often features like garden, in relation to the price). These houses are often not available, so these tenants wait longer before they move. This means that others who depend on social housing have to wait for a house for a longer time.

Land prices are derived from the selling prices and commercial rents; like Ricardo stated: 'corn is not high because rent is paid, but rent is paid because corn is high'.

And as land prices are as high as market values, the ground lease itself does not affect the affordability.

But ground lease also has this feature of conservation. This does not only affect the housing distribution, but also the affordability in a way: since the use of the land (in categories like social housing, commercial rent or owner-occupied house) is recorded in the deed and compliance of the use accordingly can be enforced, the ground lease system has kept houses in their category.

Therefore housing in Amsterdam is still affordable to those with a low-income, even though the demand is high.

5. Conclusions

Ground lease in the Netherlands is a legal right that comes in many forms and shapes. And since it is an agreement between two parties many details can be agreed upon, like the duration of the ground lease right, the size of the building on the land and the use.

In Amsterdam the municipality started with ground lease for a limited period in 1896, but nowadays rights of perpetual ground lease with a periodic revision are granted. So the ground lease changed over time to keep in balance with its environment.

In Amsterdam the ground lease system was introduced for financial and planning reasons. Nowadays the financial reason gets almost all attention. A lot of money is involved: in Amsterdam the municipality has a structural net result of over 40 million Euro per year from the Ground Lease Corporation. This result comes from a system in which legal conditions and finances are mixed and balanced.

From the surface the planning reason seems to be of little importance nowadays, but when we look closely, we see a different picture. This clearly shows when housing is related to the ground lease system. In Amsterdam the housing production has not been affected by ground lease, but the housing distribution and affordability have. Ground lease has the feature of conservation when the use is recorded. This feature has kept houses in their categories like social housing, commercial rent housing or owner-occupied house. It supports the municipal housing policy.

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