Consultation document about perpetual ground lease for newly allocated ground in Amsterdam

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1. Consultation about perpetual ground leasing for newly built property

The City of Amsterdam is planning to introduce a perpetual ground lease system, which will provide more certainty to leaseholders with regard to the costs of leases. The college of mayor and aldermen initially wants to apply this new system to newly issued ground leases. You can participate in the discussions about the City's proposals relating to the introduction of a perpetual ground lease system from 22 February to 4 April 2016.

Reading guide
This consultation document is intended to assist you in forming your opinion. It contains information about the new system and the rules that apply to it. The rules are defined in the ground allocation policy and the General Conditions. You can read the draft text of both documents in chapters 5 and 6.

On which issues is the City of Amsterdam asking for your opinion?
The college of mayor and alderpersons have presented the new perpetual ground lease system for consultation. This system consists of the General Conditions for Perpetual Ground Leases in Amsterdam, 2016 (hereafter: General Conditions) and the ground allocation policy. This policy describes how perpetual ground leases will be issued.

The General Conditions include the following points:

- that there is a case for a perpetual ground lease,
- how annual indexing is calculated in the case of an indexed ground rent,
- the mutual rights and obligations of the leaseholder and the City,
- procedures applying to changes requested by the leaseholder, such as a change to the use of the ground or a division of the lease.

The City of Amsterdam can never unilaterally change the agreements; in this way the General Conditions guarantee certainty to the leaseholder.

We would like to hear your opinions about the City's proposals for dealing with perpetual ground leases for newly issued ground, i.e., newly built housing. Additionally we would like to know whether you would choose for a fixed ground rent, an indexed ground rent, or a lump-sum payment.

To whom does this consultation apply?
The new perpetual lease system will apply to all commercial and private leaseholders, with the exception of housing associations and the Port of Amsterdam.

- *New leaseholders*: once ratified, the new General Conditions will automatically apply to new leases (for new building projects). This does not affect any agreements the City

might have with a future leaseholder that are based on the current ground leasing system. In such cases, these agreements remain in force, and switching to the new system can take place at a later date. For this to occur, a transition regulation for existing leaseholders must first be drafted.



- *Existing leaseholders*: people with an existing lease contract will be given the opportunity to voluntarily switch to the perpetual ground leasing system later. The City is still formulating a transition regulation to this end, which will be presented in a second public consultation. The General Conditions will then also apply to those who make the switch.
- *Residents of Amsterdam*: this updating of the ground lease system can impact on the Municipality's budget and is therefore important for all of Amsterdam's residents.
- *Other interested parties*: for example, interest groups such as the Stichting Erfpachters Belang Amsterdam (SEBA), which represents leaseholders' interests; the house owners' collective Vereniging Eigen Huis; and professionals such as notaries, banks and estate agents.

The following topics are excluded from this round of consultations:

- The choice for a perpetual ground lease system is stipulated in the coalition agreement, and the options of 'purchasing' or 'full ownership' are therefore unavailable. At present, we want to hear your opinions on how the new perpetual ground lease system should be implemented.
- The costs to existing leaseholders when switching to the new system. These will only become clear after the transition regulation has been formulated and presented for public consultation.
- The ways in which leaseholders can apply for changes to their lease, for example, with regard to ground use, subdividing property into apartments, plot expansions, etc. This policy will be dealt with separately.
- Ground valuation policy, ground rent percentages and information about lump-sum buyouts. These are established annually by the city council, and include the actual ground price per square metre, the way in which the ground rent is calculated, and the lump-sum buyout options available to leaseholders.

Information fair

The City is organising a three-day-long information fair as part of the consultation. At the fair you can request additional information, ask questions and even share your reactions to the proposals.

You are welcome in the first floor foyer of Amsterdam town hall, Amstel 1, on:

- Tuesday 15 March 2016 16:00-21:00
- Wednesday 16 March 2016 16:00-21:00
- Thursday 17 March 2016 16:00-21:00

The route and parking facilities can be found at:
www.amsterdam.nl/contact/routestadhuis

How can you respond?
You can respond in the following ways:

- with the online form: www.amsterdam.nl/erfpacht
- by post: Gemeente Amsterdam, re: ´Consultation Perpetual Ground Lease´, Antwoordnummer 10999, 1000 RA Amsterdam
- during the information fair
- by e-mail: (10)(2e) @amsterdam.nl re: ´Consultation Perpetual Ground Lease´

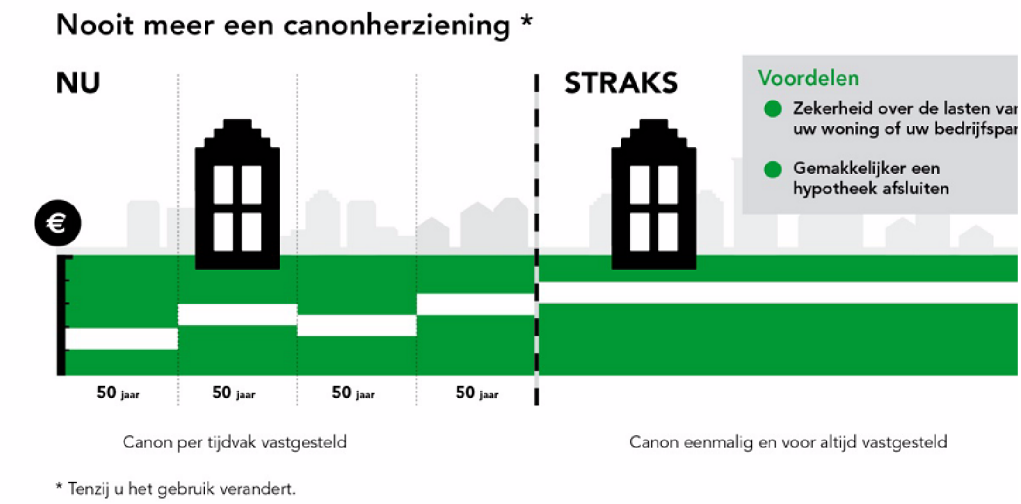
We must receive your feedback before 24:00 on 4 April 2016. Any input that arrives after this deadline will not be included in the deliberations.

What happens to your input?
The City processes all the reactions into a so-called Memorandum of Responses, which contains a summary of all your feedback. It also details any adjustments to the General Conditions or the ground allocation policy that have occurred in response to your feedback. After processing the reactions, the college of mayor and alderpersons will present the General Conditions, the ground allocation policy and the Memorandum of Responses to the city council. The associated ground price policy for new perpetual ground leases will also be submitted to the city council. If the council approves, the new perpetual leases will begin to be issued.
For the latest information and to subscribe to the newsletter about these changes to the ground lease system, go to: www.amsterdam.nl/erfpacht.

2. What is a perpetual ground lease?

After 100 years of a renewable ground lease system, the City of Amsterdam is introducing a perpetual ground lease system. In this new system, the City calculates the amount that leaseholders have to pay for the use of the (built-up) ground it owns only once and for all time. This means leaseholders will have more clarity about the cost of their ground lease.

A large proportion of the houses and businesses in Amsterdam are built on ground that is owned by the City. People with a house or business on City-owned ground pay the City a fee for this use. This fee is called a ground rent. The City uses this money to develop the city and its facilities for its residents.



What is leasehold?

Leasehold is the right to use immovable property owned by another, in this case, the City of Amsterdam. Immovable property means the land as well as the buildings and greenery that are on that land.
For convenience immovable property is referred to as 'ground' in this consultation document.
As a leaseholder, you are permitted to build on the City's ground. You can also sell the leasehold or take out a mortgage on the lease. However, the City remains the owner of the ground and the buildings thereon. You pay an annual fee, the ground rent, to the City.

Certainty

The City currently has mostly renewable leases. With renewable leases, the City can unilaterally impose new General Conditions at the end of each period (every 50 or 75 years). In addition, the ground rent is recalculated at the end of each period, based on the value of the ground at the time. This causes uncertainty for leaseholders, as well as for banks and estate agents, something that the City wants to put an end to. In fact, in the current system the ground rent can only be calculated a few years before a new period begins. If it transpires that the value of the ground has increased, the ground rent increases too.

Predictable

With a perpetual lease, the ground rent will be determined once, and for all time. The ground rent is then only indexed annually (inflation). The ground rent and other agreements will never again be revised, unless the leaseholder changes the way the ground is used. The new system provides clarity and certainty for leaseholders and the City. Mortgage providers will also be assured of the value of the leasehold as collateral for their loans.

Changes to the use of the ground

The ground rent can only be adjusted under the new system if the leaseholder wants to alter the terms of the lease, for example, if he or she changes the use of the ground from a residence to a hotel, or from an office to a shop. The ground rent is also adjusted should a commercial building be expanded. Private residences can be enlarged without the ground rent being affected, as long as the number of buildings doesn't increase, the residence isn't commercially exploited, and has been occupied for at least four years after allocation.

3. How would you prefer to pay?

The proposal for a perpetual leasehold system provides two payment options for leaseholders: a ground rent that can only be indexed annually (adjusted for inflation), or the option to buy off the ground rent (with a one-off payment). The college of mayor and alderpersons have also considered the option of a fixed ground rent, which is not indexed, and is examining the possibility of mandatory lump-sum buyouts in some situations.

Indexed ground rent
The indexed ground rent is adjusted annually to meet the expected inflation, and only changes if the use of the ground changes. The indexed ground rent is initially lower than the fixed ground rent, but will increase each year due to inflation. After a long period (approximately 28 years in the example below), the leaseholder would pay more than the fixed ground rent. However, the exact point of convergence is dependent on actual inflation in the future. Under current tax law, the ground rent for owner-occupied residences is deductible from income tax.



Fixed ground rent
In the case of fixed ground rent, the leaseholder pays an annual fixed amount that will never be adjusted, unless he or she changes the use of the ground. Under current tax law, the ground rent for owner-occupied housing is deductible from income tax. The fixed ground rent is initially higher than the indexed ground rent. After a long period (28 years in the example below), the leaseholder would pay less than the indexed ground rent.

Lump-sum buyout
With a lump-sum buyout, the leaseholder pays all future ground rent in one go. As long as the function and/or use of the leasehold remains unchanged, no further ground lease will have to be paid, in perpetuity.
Under current tax legislation, the interest on any loans for owner-occupied homes is deductible from income tax for 30 years, subject to conditions.[1]

Comparison of the payment options for a newly built residence
The table below clearly illustrates the differences between the various forms of payment.

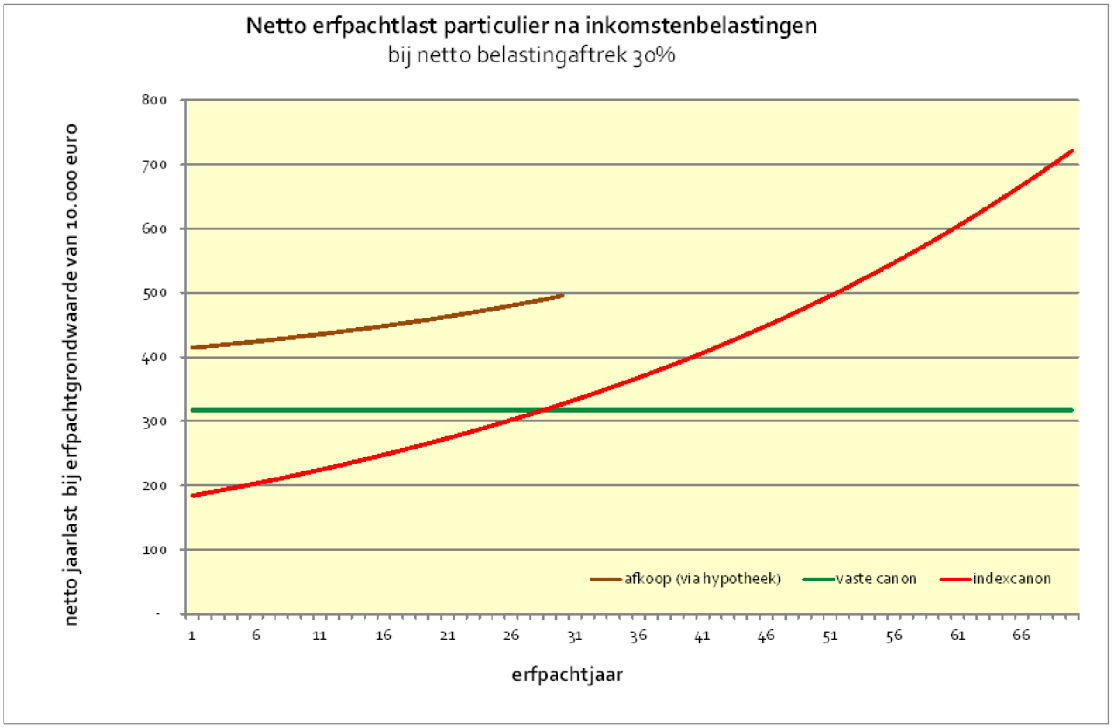
	Indexed ground rent	Fixed ground rent	Lump sum (one-off payment)
general	▪ periodic payments to the City ▪ annual correction for inflation ▪ indexed ground rent is initially cheaper, but after time is more expensive than a fixed ground rent	▪ periodic payments to the City ▪ a fixed amount, no correction for inflation ▪ fixed ground rent is initially more expensive, but over time becomes	a one-off payment to the City ▪ mortgage costs dependent on financing and length of fixed interest period

[1] The personal situation of the leaseholder may result in additional provisions for tax deduction.

		cheaper than an indexed ground rent	
income tax	▪ ground rent fully tax deductible without restrictions ▪ risk: potential limits in the tax deductibility of ground rent in the future		▪ only the interest on financing (subject to conditions) is tax deductible for max. 30 years ▪ risk: potential restriction of tax deductible mortgage interest in the future
borrowing capacity	▪ based on income ▪ dependent on ground rent payments (the amount) or lump-sum buyout ▪ borrowing capacity higher with ground rent payments than with a one-off payment ▪ borrowing capacity initially higher for indexed ground rent than for fixed ground rent (see housing costs, next page)		

The table below compares the net leasehold costs of the different forms of payment for a leaseholder of a home. This calculation is based on a leaseholder with a 30% tax deduction. The value of the leasehold ground has been set at 100,000 euros for this example. The indexed ground rent is adjusted by 2% annually. This results in the following differences:

Indexed ground rent	**Fixed ground rent**	**Lump-sum buyout**
▪ taking current variables into account, the indexed ground rent percentage is 2.63% ▪ the initial ground rent is 2630 euros and will increase annually by 2% ▪ the net amount after tax deduction is initially 1840 euros and will increase annually ▪ the indexed ground rent is higher than the fixed ground rent after approximately 28 years	taking current variables into account, the fixed ground rent percentage is 4.53% ▪ the fixed ground rent is 4530 euros and will remain so forever ▪ the net amount after tax benefits is 3170 euros ▪ the fixed ground rent is higher than the indexed ground rent for the first 28 years	▪ with 30-years annuity financing and 5-years fixed interest (average) ▪ nominal interest: 2.84% ▪ annuity: 4.95% ▪ net costs of mortgage interest repayments initially 4150 euros, increases annually ▪ free if paid off after 30 years; no more mortgage costs



Considerations when deciding on a payment method

The future perpetual costs of fixed ground rent, indexed ground rent and a one-off payment are identical at the moment the ground is allocated. Yet there are differences for the leaseholder. The lump sum is of course paid in one go, often by including it in the mortgage. Indexed ground rent initially costs the least, but depending on inflation can end up costing more in the future than fixed ground rent. The financial status of individual leaseholders will differ and likewise their preference for how to pay.

In the current system, there are several types of ground rent in addition to lump-sum buyouts. Besides indexed ground rents, there are also 5-, 10- or 25-year fixed ground rents. Having several different types of ground rent eventually leads to significant differences in annual payments for leaseholders. This creates a lack of transparency, especially for future buyers. For them, it is difficult to compare the selling price of similar properties with different ground rent models. The college of mayor and alderpersons want a simpler and more transparent system. In addition to the one-off payment, its preference is for one type of ground rent (indexed ground rent).

Should buyouts be obligatory ?

Paying ground rent doesn't mean that you are buying the ground. You could compare it to a perpetual interest-only loan. The ground rent is used to cover the interest on the loan, but the City's debt remains unpaid.

The City of Amsterdam borrows money to cover the costs it incurs whilst preparing ground for building and habitation. When leaseholders buy off their leases, the City's loans can be repaid with these lump sums. The City strives to keep its debts to a minimum, and is therefore examining ways to stimulate lease buyouts or even in certain situations to make them mandatory. This will reduce the City's debt.

We are examining the options for mandatory or encouraged lump-sum buyouts in the following areas:

• new ground allocations: because leaseholders can take a potential mandatory lump-sum buyout into account when considering a property, and furthermore include it in their mortgage applications.

• existing leases on ground with commercial real estate: if a leaseholder wants to switch over to a perpetual ground lease or alter the terms of the lease (change of ground use).

The college of mayor and alderpersons consider mandatory lump-sum buyouts for existing leaseholders who are also house owners to be unreasonable. Existing leaseholders could not have anticipated this, and the transition to a perpetual ground lease may not be the logical moment for them to arrange (re)financing.

Consultation question:
Would you choose a fixed ground rent, an indexed ground rent, or a lump-sum payment, and what are your reasons?