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Is the Rent Cap Law at a Tipping Point?

The implementation of the rent cap law, also known as "rental break" (*Mietpreisbremse*) over two and a half years ago has sparked a lot of controversy in terms its effectiveness and appropriateness. Some experts criticised the law as an interference in property rights and contractual freedom (see our [February 2017 newsletter](#)). The two latest decisions by the district courts *Landgericht Munich* and *Landgericht Berlin* are currently causing a stir in the legal situation of this law. The former has declared the rent cap ineffective in Bavaria while the latter has doubted its constitutionality and submitted the case to the *Bundesverfassungsgericht* (Federal Constitutional Court), the last authority who can officially declare a law unconstitutional.

Landericht Berlin has doubted the constitutionality of the rent cap law

A quick recap: The rent or price cap was adopted by the Bundestag in 2015. It empowers each federal state to cap rents to maximum 10 percent above the average local rent in tense housing markets, unless the property was already let at a higher level. Exemptions apply for newly constructed or extensively renovated property and in some cases for furnished apartments.

Once the law is enacted by a federal state, it is effective for a limited period of five years. Berlin was one of the first to implement the rent cap in June 2015 and hence, it is set to expire in 2020 unless legal conditions change.

Today, two and a half years later, the rental break is widely regarded as a failure, although controversies continue over the reasons for it. As a matter of fact, the price cap neither alleviates housing shortage nor has it been able to prevent further rent increases, as several analyses have shown (see our [February 2017 newsletter](#)). Moreover, the law has been criticised for intervening in contractual freedom.

In December 2017, the *Landgericht Berlin* (District Court) has decided that the rental break is unconstitutional and passed the case to the Federal Constitutional Court for a final decision.

The decision of the *Landgericht Berlin* came after two tenants in Berlin-Wedding appealed to the court amid a dispute with their landlords over rental prices.

The *Landgericht* argued the rent cap would be incompatible with fundamental rights as it violates the principle of equal treatment:

- As the average local rent varies across Germany, using this value as reference point for the maximum allowable rent leads to a different treatment of owners depending on the location of their property. A landlord in Munich would be entitled by law to ask for a much higher price than a landlord in a region with much lower prices, e.g. Berlin.
- Moreover, landlords who made use of excessive price increases before the rent cap was enforced, could still charge these higher prices.
- Additionally, because it is up to the individual states to enact the law, it would depend on the ruling political party whether or not the rent cap is implemented in a given federal state, again, leading to unequal treatment depending on the location of property.

Tenants' supporters on the other side argue that the disadvantage resulting from lower rent levels is compensated for by lower investment costs (purchasing prices) in those areas.

Landgericht Munich Declared Rent Cap Ineffective in Bavaria

While the decision of the judges in Munich who declared the rent cap ineffective due to formal errors sounds not as fundamental as in the case of Berlin, it has definitely contributed to a climate of legal uncertainty around the rent cap law.

The decision was the court's response to a lawsuit filed by a tenant from Munich's central neighbourhood *Maxvorstadt*.

The *Landgericht* argued that the Bavarian government has failed to make it sufficiently clear what criteria define tense markets and hence, where the law should be applicable.

The judges emphasized, however, that the law is not unconstitutional per se and does not violate owner's rights. They also did not doubt that Munich has a tense housing market.

The government of the Free State of Bavaria has already attempted to correct the formal error by specifying the conditions that define a tense market (the criteria population growth and building activity as well as their weighting factors). As a result, 137 cities and municipalities out of previously 155 have been declared as tensed housing markets.

It is not yet clear, however, if this amendment is sufficient and according to the tenants' association Munich, a new lawsuit would be required in order to verify the effectiveness of the law in its improved version.

The fact remains, however, that the rent cap was not effective in Bavaria for the past two years since its enactment in August 2015. Theoretically, landlords could be entitled for retroactive corrections of rent prices, some experts say.

Although the court's ruling has only legal consequences for the affected tenants who took the legal action as well as their landlords, it has sort of a model character and would likely entail similar decisions in other pending cases, despite the fact that other courts can make autonomous decisions.

The affected tenant family is now taking legal steps, supported by the legal service provider *wenigermiete.de*, against the Free State of Bavaria for breaching its official duty by committing the error in the rent cap ordinance.

What to Expect?

As there are always two sides in the rent cap dispute, different experts have different opinions in terms of what the given events could mean for the future of the rent cap.

Experts supporting tenants' rights view the reasoning of the *Landgericht Berlin* as groundless and expect the Federal Constitutional Court (Bundesverfassungsgericht) to dismiss the complaint about the unconstitutionality of the rent cap.

Meanwhile, the Left party has submitted a reform proposal to the Federal Government, demanding a nationwide effect of the rent cap and the abolishment of its five-year limitation. They also want to oblige landlords to a disclosure of previous rental rates and entitle tenants to repayments with retroactive effect in cases where rents exceeded the permitted maximum level.

On the other hand, the German Realtor Association IVD (Immobilienverband Deutschlands) is appealing to the Social Democratic Party (SPD) as CDU/CSU's likely coalition partner in the new German government to respect the latest judiciary decision and consider it in coalition talks. The social democrats' priority is to close the legal loopholes that would prevent the rent cap from unfolding the desired effects. While the CDU/CSU do not support the rent cap, there is a possibility they could give in to the demands of their coalition partner.

In case the Bundesverfassungsgericht confirms the unconstitutionality of the rent cap, the regulation will be ineffective with retroactive effect.

The expert Johann-Frederik Schuldt, an associate at Greenberg Traurig Germany, advises landlords to take this circumstance into account when concluding new letting agreements. He suggests to include a special clause for an alternative rental rate as well as a clause that will entitle landlords to subsequent payments in case the rent cap becomes void.

Experts think the Federal Constitutional Court's is likely to take its decision in 2018.

Please note that the contents of this newsletter have been researched and written according to the best of our knowledge; however they are in no way to be accepted as a legal advice or suggestion. Therefore we exclude any liability.

Sources

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