THE SUPPLY OF PRIVATE RENTED HOUSING IN CANADA

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ABSTRACT *Canadian housing policy objectives are generally pursued through a market framework. There is little provision of non-market housing. Thus, while Canada has a substantial private rented sector, it has only a small social rented housing sector. About a third of all dwellings belong to private landlords for market renting and only six percent are owned by public and private landlords for non-profit renting. The supply of dwellings newly constructed specifically for private market rental has fallen over the last 20 years. This fall has been compensated for in part by the supply of existing dwellings that have been transferred from other tenures. There has also been a fall in the proportion of private market rented dwellings owned by corporate landlords and an increase in the proportion owned by small-scale individual landlords, including individuals buying existing dwellings in other tenures to convert to private renting. These recent supply-side changes have been in response to three factors. First, changes to the federal tax system and direct supply incentives have reduced the attractiveness of investing in private renting for corporations but increased it for individuals. Second, the demand for private renting has fallen amongst middle- and high-income households because of demographic and tax changes. This has reduced the numbers of private renting households able to pay the rents needed to make new construction profitable. Third, other public policies have also had an impact on supply, including rent controls imposed by provincial governments and land use planning restrictions and building standards imposed by local authorities. An important feature of the Canadian private rental market is its geographical diversity, with supply-side trends varying in different provinces and urban areas in accordance with variations in demand and local policies.*

1 Introduction

This paper examines the operation of the private rental market in Canada, placing particular emphasis upon supply trends and their determinants. It looks at trends in the supply of private rented dwellings and examines government policies that have

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had an impact upon supply. These include federal tax and other incentive programmes, but also provincial rent controls and municipal planning policies. The paper also describes the demographic context and other factors that have shaped demand for private rented housing.

The paper draws on research conducted by the author in 1992. The research was based on secondary sources and interviews with key informants in the government (including a sample of provincial and local governments), the private sector, and universities. At the time of this research the British government had recently initiated policies to revive the private rented sector in Britain and had introduced tax incentives as well as rent deregulation to stimulate new investment (Crook et al., 1991; Crook & Kemp, 1996). The purpose of the author's Canadian research was to examine the experience of another country which had already used tax incentives to stimulate investment in market renting and to consider what lessons the experience had for Britain. The main objective was to examine the short- and long-run impact that tax policy and other incentives had had on the supply of private rented dwellings, both new and old, in Canada.

The paper has nine sections. The first two sections briefly examine the wider context of the private rented market and government housing policy. The third section examines trends in the supply of dwellings for private rental and in the types of landlords owning them. The fourth section examines the changing demographic context and the fifth section looks at trends in demand for private renting. The sixth section looks in detail at the impact that taxation policy and tax and grant incentives have had on the supply of dwellings. This is followed by sections examining rent controls and planning policies. Section nine concludes the paper.

2 Canada: constitution and geography

When examining any aspect of the Canadian housing market, it is important to bear three factors in mind: Canada's constitution, its geography, and the scale of international immigration.

First, Canada has a federal structure of government. The constitution does not, however, allocate responsibility for housing. There is thus some ambiguity about where the constitutional responsibility for housing matters lies (Pomeroy, 1995). Hence, policy at all levels of government affects private renting. Moreover, policies at different levels of government do not necessarily work consistently and have sometimes negated as well as reinforced one another.

The Federal government's responsibilities cover taxation, subsidies and loans. A Crown Corporation, the Canada Mortgage and Housing Corporation (CMHC), is the Federal body with responsibility for housing matters. Provincial government policies include incentive programmes, rent control, regulations about landlord-tenant relationships, shelter allowance programmes, and legislation to prevent the transfer of rented dwellings to the owner-occupier sector. The creation of municipal authorities is a function of provincial, not federal government. Municipal governments (or ad hoc boards) have responsibility for planning controls and the enforcement of housing standards.

Second, it should be borne in mind that Canada is a vast and very diverse country, stretching from the Pacific to the Atlantic. The population (27 million in 1991) lives in a narrow band stretching from Victoria and Vancouver in the West, across the Rockies, through the rural communities and metropolitan areas of the prairies, the industrial and metropolitan areas of southern Ontario and of Quebec, and through to the Atlantic communities in the East. It experiences 'long and inhospitable winters', which impact upon construction costs and maintenance (Miron, 1994a). Not only is it vast in extent, but its rural and metropolitan communities are diverse linguistically, culturally and ethnically. Most significantly, the provinces and metropolitan areas have diverse economic fortunes. This diversity needs to be borne in mind when considering the factors that have determined public policy towards the private rental market, as well as the diverse - and sometimes unexpected - way policy has impacted upon the market. Moreover, its proximity to the USA means that its economy interacts closely with that of the USA and that the capital markets of the two countries are closely integrated (Fallis, 1990).

Third, international inward migration is an important factor in population growth, especially in metropolitan areas. Between 1990 and 1991, the population grew by 381,000, of which 168,000, or 44 per cent, was due to net international migration (CMHC, 1991: Table 93). This is an important dynamic in the housing market (Pomeroy, 1995).

3 Housing policy context

Housing in Canada is produced largely by the private sector, and governments have generally pursued a private market approach in their housing policies.

Commentators have pointed out, however, that the emphasis given to social justice within Canadian society means that, in the past, governments have preferred a mixed economy approach rather than a neo-conservative approach to the role of the state (Fallis, 1990; Mishra, 1990, Chapter 4). They have, nonetheless, intervened in ways that support the workings of the market, rather than through non-market housing. They have also had a preference for supporting home ownership and for taxation arrangements that implicitly favour this tenure (interest payments are not tax deductible but imputed rents and capital gains on principal residences are not taxed). The social housing sector is hence small, accounting for only six per cent of dwellings.

Policy has dealt with both inefficiencies in market provision, for example by providing mortgage insurance, and with equity issues, for example by the limited direct provision of low-income rental housing. There have been two key target groups for policy: owner-occupiers on 'modest incomes' and 'low income' renters. Policy initially focused on the former, but more recently on the latter (Miron, 1994a, Chapter 1). The federal government reduced its direct housing expenditures in the 1980s. In the early 1990s (a period of tight fiscal constraint) it was examining the extent to which it should be involved in housing matters in the future. The general thrust of policy was to deal with core need at the bottom of the market rather than with increasing overall supply (see Pomeroy, 1995, for a general review of future policy issues and choices).

This general policy approach of working through the market has two implications. First, welfare arrangements have been important in enabling the poor to gain access to housing, including rented housing, since there have been (with the minor exception of two provinces) no rent allowance schemes for non-elderly tenants. However, housing and social policy matters have not been well integrated (Prince, 1995). Second, the poor have generally relied on market, rather than social housing, and on older rather than newly constructed stock for their housing. Additions to the housing stock available to poor renters have depended on the better-off generating the demand for newly constructed housing and on a subsequent filtering down of this stock over the years.

In recent years, the supply of stock to poorer renters has fallen. New construction rates have dropped. There is less demand to rent from those able to pay the rents needed to make new construction profitable without subsidy. Meanwhile older conventional rented housing stock has been demolished in inner-city renewal schemes to make way for higher-priced condominiums.

4 Trends in tenure, the supply of private rented dwellings and types of landlords

Tenure

The proportion of occupied dwellings in the rented sector has remained reasonably consistent over the post-war period. In 1991 just over a third were rented, almost the same as in 1951 (Table 1). There was an increase in the proportion to 38 per cent in 1971, associated with a boom in apartment construction in the 1960s, but this proportion has since declined. The available statistics do not separate social rented dwellings from purely private market rental dwellings. The former consist of public housing, co-operatives, and other forms of private and municipal non-profit rental dwellings. Altogether, they comprise about 640,000 dwellings, or six per cent of the total occupied stock (Miron, 1994b). Thus approximately 28 per cent of occupied dwellings in 1991 were privately rented market dwellings. There were significant variations. The proportion is higher in metropolitan than in non-metropolitan and rural areas - and higher in some provinces, particularly Quebec -- than in others.

The supply of newly constructed private rented dwellings

It is difficult to quantify trends in the supply of dwellings for private rental for two reasons. One reason is that, until recently, relatively little information was readily available about the intended market of newly constructed dwellings. However, figures are available for the completion of apartment dwellings. These were accepted as a surrogate for the output of new privately rented dwellings. Second, much of the supply in the private rented sector has been assumed to filter down from dwellings previously newly constructed for the owner-occupied market, with increasing pro-

Table 1 Tenure of occupied dwellings, 1951-1991

	Owner-occupied (x 1,000 dwellings)	Rented (x 1,000 dwellings)	Total (x 1,000 dwellings)	Rented as per cent of total
1951	2,237	1,172	3,534	33
1961	3,006	1,549	4,767	32
1971	3,612	2,393	6,342	38
1981	5,106	3,131	8,785	36
1991	6,273	3,719	10,773	34

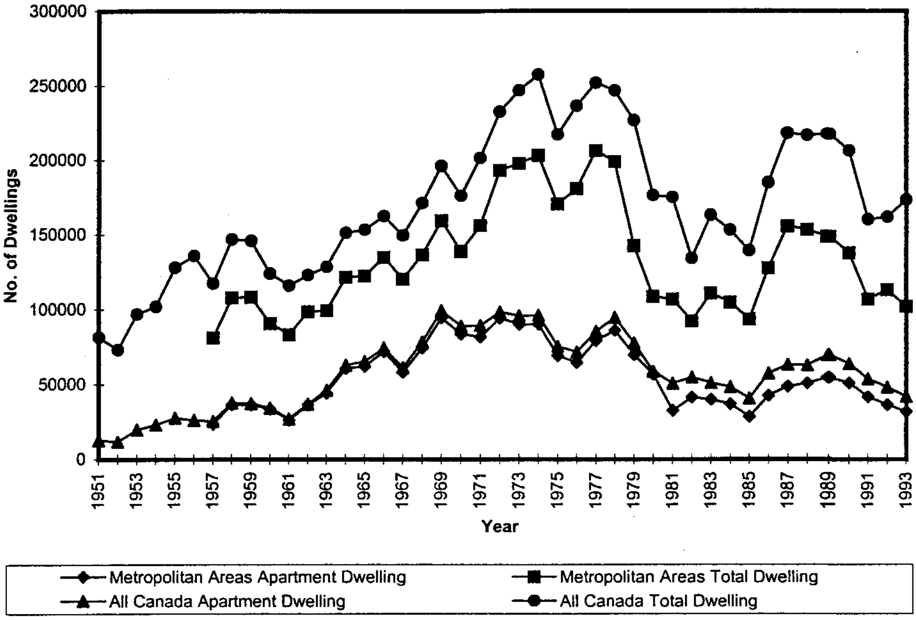
Source: Miron 1994b.

portions being converted into rental dwellings as they age, including physical alterations to intensify occupation as well as alterations to tenure (Steele, 1993). However, census and other data may incorrectly record the net numbers of dwellings created by conversion, alteration or demolition (Skaburskis, 1994; Vischer, Skaburskis Planners, 1979). Moreover, data on trends in the tenure conversion of the existing stock are not readily available, but they are important for an accurate account of the private renting stock. For example, 30 per cent of dwellings in Toronto changed tenure between 1976 and 1985 (Moore & Skaburskis, 1994). These data deficiencies masked important changes in the supply of dwellings for private renting in the 1980s (Steele, 1993).

As Figure 1 shows, there have been significant variations in the total number of new dwellings completed since 1951, as well as significant variations in the numbers of apartment dwellings completed. The total number of dwellings completed rose steadily in the 1950s and 1960s as the population and numbers of households increased, peaking and troughing in the mid-1970s, followed by a major reduction in output during the recession of the early and mid-1980s, with a subsequent recovery in the later 1980s, but declining yet again with the recession in the early 1990s. The output of new apartment dwellings follows a broadly similar cyclical pattern. What is also noticeable is that completions rose less than single-family houses in the 1950s, although they rose more in Quebec than elsewhere (Clayton Research Associates, 1989). They increased after the 1950s and peaked at a high level in the late 1960s and early 1970s, with output touching 100,000 per annum then (and again in the later 1970s). However, since these peaks, the completion of apartments has fallen, with new output running at an annual average of 55,500 in the 1980s, compared with 85,500 in the period 1965 to 1976.

As will also be observed from Figure 1, this pattern of completions was mirrored by the pattern within metropolitan areas. Moreover, it will be noticed from Figure 1 that the construction of new apartments was, until the 1980s, almost exclusively a metropolitan phenomenon; new completions in metropolitan areas accounted for over 90 per cent of completions throughout Canada. Figure 2 shows how the increase in the output of new apartments in the late 1960s and early 1970s

Figure 1 Completions of apartments and other dwellings, 1951-1993

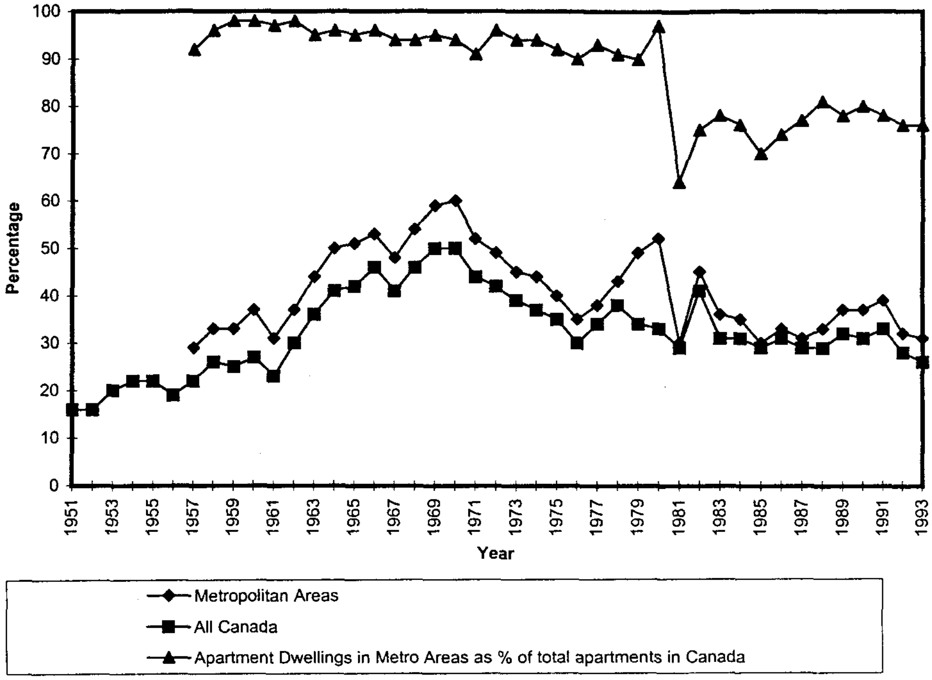


Source: Canada Mortgage and Housing Corporation 'Canadian Housing Statistics' (annual)

was associated with an increase in the proportion of all new dwellings accounted for by apartments, the proportion rising from around a quarter in the late 1950s to half in the late 1960s during the great boom in apartment building, since when it has declined. Within metropolitan areas, apartments accounted for a higher proportion of total new dwellings completed throughout the forty-year period, rising to 60 per cent in 1970, though falling to around a third in the later 1980s.

While these apartment completions have been a surrogate for new construction trends in the private rented sector, it is important to stress that new apartments are also intended for other tenures, including social renting and, more recently, condominium ownership. Exact estimates of the proportions involved are not easy to obtain, but Tables 2 and 3 provide some evidence. Table 2 shows the type of financing involved in new apartment starts (1969 to 1982) and completions (1983 to 1993). It shows, in particular, that funds authorized (i.e., insured) under the National Housing Act for social rented schemes accounted for between one in ten and nearly one in four during the years of the 1980s. It also shows that NHA funding accounted for significant proportions of market housing in the early 1980s. For example, over a third of starts in 1979 and 1980 were funded through NHA, although this funding had dwindled to only a small proportion by the early 1990s. By no means all the support for market housing was for rented apartments, however,

Figure 2 Apartment dwellings as percentage of total dwelling completions, 1951-1993



Source: Canada Mortgage and Housing Corporation 'Canadian Housing Statistics' (annual)

since some will have been for other tenures.

More recent evidence, shown in Table 3, provides a more precise account of the tenure destination of newly constructed apartments in metropolitan areas. In particular it shows that, whereas over two-thirds of the output in 1985 was destined for market renting and only 24 per cent for condominium ownership, by 1991 condominiums took nearly half the completions and market renting less than half. This fall in the output of new apartments destined for market renting in the 1980s, especially those constructed by property investment companies, prompted concerns about the adequacy of supply, a tightening of rental markets, assumed rent increases and therefore concerns about affordability issues. In particular, it was argued by some that the private rented market was able to sustain newly constructed dwellings to a much more limited degree in the 1980s than in the 1960s and 1970s, so that renters were increasingly having to rely upon older housing filtering down from the owner-occupied market much more than in the past. This trend, it was argued, was partly because renters were increasingly from lower-income groups, less able than their predecessors in earlier decades to afford the market rents needed to generate construction for private renting (for example, see Hulchanski, 1992).

These concerns were additionally prompted by evidence of falls in the vacancy rates for large (six dwellings or more) apartment buildings in a number of metropolitan areas. These buildings contain 55 per cent of all privately rented apartments (Table 4). For example, vacancy rates in Toronto fell from levels in excess of one per cent throughout the 1970s to figures under one per cent throughout the 1980s (CMHC, Canadian Housing Statistics, annually).

However, it is likely that the decline in supply in the 1980s has been overstated. Whilst there were substantially fewer new apartments constructed for market renting, there were increases in the numbers of dwellings converted to private rental from owner occupation. There was also evidence that significant numbers of condominiums were being bought for investment by individual landlords, and not for occupation, and that the inflationary environment of the late 1980s, the tax system, and rent regulation all contributed to this (Steele, 1993).

Table 2 Apartment dwelling completions (1983-1991) and starts (1969-1982) by financing method

	National Housing Act			Total
	Social housing %	Market housing %	Total NHA %	(x 1,000 dwellings)
1969	n/a	n/a	40	110,913
1970	n/a	n/a	37	91,898
1971	n/a	n/a	25	106,187
1972	n/a	n/a	20	103,715
1973	n/a	n/a	56	106,641
1974	n/a	n/a	44	74,025
1975	n/a	n/a	56	70,361
1976	n/a	n/a	63	89,324
1977	n/a	n/a	70	92,327
1978	n/a	n/a	49	77,327
1979	16	33	49	58,387
1980	17	35	52	48,329
1981	12	13	25	61,609
1982	22	13	36	53,162
1983	23	23	46	50,812
1984	23	32	55	48,178
1985	23	21	45	40,458
1986	18	9	27	56,991
1987	10	4	14	62,914
1988	10	4	14	62,527
1989	9	4	13	69,483
1990	9	4	12	63,616
1991	11	3	15	53,568

Source: Canadian Housing Statistics.

Table 3 Intended market of apartments completed in metropolitan areas 1985-1993 (%)

	Market rental	Owner occupation	Condominiums	Other	Total number
1985	68	1	24	7	28,301
1986	65	1	28	5	42,197
1987	62	1	34	3	48,534
1988	56	1	40	4	50,463
1989	48	1	47	3	54,515
1990	47	1	50	2	50,654
1991	46	2	49	3	41,513
1992	53	2	39	6	36,265
1993	45	3	44	8	31,698

Source: Canada Housing Statisics 1985 - 1993, Table 23

Table 4 Size of multiple dwelling structures (x 1,000 dwellings)

	Structures		Dwelling	
	Number	%	Number	%
<6	48,246	44.9	178	11.8
6-19	43,359	40.3	394	26.2
20-49	10,277	9.6	310	20.6
50-199	4,739	4.4	438	29.1
200	677	0.6	184	12.2
Total	107298		1503	

Source: Canadian Housing Statistics.

Types of private landlords

Although relatively little is known about private landlords in Canada, it is generally accepted that, comparing the 1980s with earlier post-war decades, individual landlords have become much more important than corporate landlords (Clayton Research Associates, 1989). There is little evidence about landlords in the 1940s and early 1950s, but the period between the mid-1950s and late 1960s has been described as the golden age of the multi-storey apartment developer (Lorimer, 1978). Developers were very actively involved with two types of scheme: first, large scale schemes that they constructed for their own investment; second, smaller schemes which they sold on to high-income individuals.

While corporate landlords made adequate returns in the 1950s and 1960s from the cash flows arising from the developments they built for themselves, inflation and tax reforms reduced these returns from the early 1970s onwards (see below). These changes reduced the attractiveness to corporate landlords of investing in private renting, but increased its attractiveness to high-income individuals. While these individuals participated in private renting either as passive landlords via syndications or as active landlords through the ownership of small-scale developments, many corporate landlords and developers left the industry. Alternately, they shifted to syndicating developments as tax shelters for high-income individuals and to the construction of condominiums.

Although changing taxation regimes have been important in shaping this trend, federal government incentive programmes (see below) delayed what would have otherwise been a more rapid decline in the numbers of corporate landlords.

The evidence suggests that high capital gains attracted high-earning individuals to invest in private renting, despite the low net rental returns to be earned. This was because interest payments were fully tax deductible at the income tax rate, whilst potential capital gains were not taxed until realized and were then taxed only at the lower capital gains tax. To ensure that their investments could be realized, these small-scale individual landlords needed to acquire dwellings that could be easily sold into owner occupation. Apartment dwellings were much less attractive to these landlords than newly constructed condominiums. This was because apartments would be less easy to dispose of than condominiums and because of the impact that rent regulation had on large apartment blocks. Detached and other types of dwellings recently constructed for owner occupation were much more attractive than apartment dwellings, encouraging a transfer of dwellings from home ownership to renting much earlier in their life cycle than in previous decades. The environment of the 1980s thus attracted small individual investors with high marginal tax rates to buy particular dwelling types for private renting, but it was less atttactive for corporations to continue constructing apartment blocks.

Conversion of dwellings in other tenures to the private rented sector

At the same time, it has been argued that substantial numbers of conversions from full owner occupation to part private renting also took place in the 1980s in the form of 'accessory apartments', such as the conversion of basements into rental units, unrecorded by official statistics, since these physical alterations often breached municipal zoning regulations and codes about physical standards (Poulton, 1995; Skaburskis, 1994). It has been estimated that between 10 and 20 per cent of detached dwellings and five to 10 per cent of the total stock in Canada contain accessory apartments. These are typically owned by younger households, needing the rent to supplement their incomes, and providing accommodation at rents below those in conventional apartments, but not at a level affordable by those on the lowest incomes. These apartments are therefore an important source of rental supply. In Vancouver, for example, it was estimated that between 1985 and 1989 there was a growth of 28,500 units from these 'non-conventional sources' and that they constituted three-quarters of the total additional supply over the five-year period (Clayton Research Associates, 1991). It is thought that, in the future, the supply of accessory apartments will fall because of the demographic decline in the number of younger home owners, although there will continue to be a demand for low-cost rental units, especially in metropolitan areas (Regional Real Estate Consultants, 1990).

To summarize, conventional new supply for private renting (apartment blocks) has fallen in recent years, prompting concerns about the adequacy of supply. At the same time, however, there has been additional supply from non-conventional sources, including accessory apartments, relatively newly constructed dwellings originally built for the home ownership market, and condominiums acquired as investments rather than as homes. At the same time, there has been a shift in the nature of landlords, with an environment more conducive to individuals and less to corporations.

5 Demographic context

Since the demand for private renting is partly a life cycle function, a key factor in the demographic context for the market is the numbers out of the total population who are in younger age groups and the numbers of households they form. Renters are much more likely to be young, single, divorced and (though less so than divorced) widowed (Miron, 1994b).

Canada's total population has grown considerably in the post-war years, rising from 18m in 1961 to 27m in 1991. This increase was due both to the 'baby boom' (younger and more marriages, earlier births and larger completed families) and net international in-migration (Miron, 1994a, Chapter 2). The numbers of households rose too (Table 5). It has been calculated that about two-thirds of this increase was the consequence of the increasing size and changing composition of the population, and that one-third was due to a greater propensity of non-family individuals to live alone and to rising real incomes (Miron, 1988). As the 'baby boomers' formed households and had children, there was an increase in the numbers of family households (Table 5). In addition, the post-war years have also recorded a considerable increase in the number of non-family households, rising from 385,000 in 1951 to 2,356,000 in 1986 (Table 5). The more recent 'baby bust', together with declining marriage rates has increased the numbers of non-family households. Thus, the proportion of persons living alone rose from 13 per cent of all households in 1971 to 23 per cent in 1991 (Miron, 1994b).

Recent years have seen a reduction in the rate of net household formation, falling from 225,000 over the period 1971-76 to 177,000 over the period 1986-1991. In particular there has been an absolute fall in the households headed by those aged 15 to 24, whilst the numbers of new households formed by those aged 25 to 34 has fallen from 82,000 over the years 1971-76 to 34,000 over the period 1986-91 (Table 6).

Table 5 Numbers of households in Canada, 1951-1986 (x 1,000)

	Family	Non-family	Total (including other types)
1951	3,024	385	3,522
1961	3,948	606	4,745
1971	4,993	1,108	6,324
1981	6,231	2,043	8,757
1986	6,635	2,356	9,046

Source: Canadian Housing Statistics.

Table 6 Net household formation (x 1,000 households) by age of head of household per period, 1966-1991

	15-24	25-34	35-44	45+	Total
1966-71	29	51	13	79	172
1971-76	34	82	17	92	225
1976-81	18	72	47	76	213
1981-86	-2	55	79	66	198
1986-91	-10	34	67	86	177

Source: Canadian Housing Statistics.

The post-war increase in persons living alone, as well as the fall recorded in the first half of the 1980s in the rate of increase in persons living alone, has been linked to changes in the housing affordability index, as well as to demographic changes and changes in preferences. Real incomes rose from 1951 to 1981, especially amongst married couple families, but also amongst others (with the incomes of the elderly poor supported by social security programmes). Although housing became more affordable in the 1970s, affordability fell in the 1980s, lowering both net new household formation and the demand for private rented accommodation, although at the same time increasing the demand for lower-quality and smaller accommodation (Miron, 1988; Miron, 1994a Chapter 2; Miron, 1994b).

6 The demand for private renting

Commentators examining the choices Canadians have made between owning and renting have pointed out that the big increase in ownership rates amongst urban households in the ten years before 1951 established owner occupation as the 'urban norm'. Even though the subsequent increase in single persons living alone has placed limits upon the overall rate of home ownership, the rate amongst traditional family households has continued to rise (Steele, 1994).

Steele examines tenure choice by looking at the advantages that accrue from home ownership compared with renting. These include more control, the accumulation of wealth, and tax benefits (although the tax system tends to produce lower rents because of the asymmetrical treatment of interest payments and capital gains). Offsetting these advantages are asset risks, transactions and maintenance costs. She argues that housing policy favoured home ownership in the early post-war years by supporting middle-income households through mortgage insurance in a manner that encouraged new construction. Subsequently, opposition to policies to encourage home ownership amongst low-income households diminished, and a range of programmes was set up to help them during the 1960s (although subsequently terminated).

Steele also shows how home ownership rates amongst male-headed family households have continued to rise in response to the rise in real incomes and to greater mortgage availability, but also that rates amongst non-family and female-headed households have also risen. The increase in ownership by non-traditional households is, in part, due to reduced discrimination by lenders but also due to the widening availability of condominiums. The growth of condominiums makes ownership accessible to large numbers who would otherwise look to renting, because of the way it combines many of the attributes of owning (control, asset accumulation and tax benefits) with those of renting (lower management and maintenance costs). Indeed, other commentators have argued that the growth of condominiums (legislation being enacted in all provinces by 1977) has significantly reduced private renting by reducing market demand (Hulchanski, 1994).

However, in addition to rising real incomes for traditional households and easier loan access, another factor explaining the increase in ownership rates was the differential change in house prices and rents (Steele, 1994). Real house prices increased by 34 per cent between 1945 and 1984, but real rents fell by 46 per cent (in part in the 1970s because of rent regulation and the additional supply generated by the incentive programmes discussed below, but also because of the tax system). The fact that this did not produce a large increase in renting was also a product of the significant capital gains made by home owners. The user cost of housing for owner occupiers is lower the greater the inflation rate, the greater the owner occupiers' tax rate, and the greater their equity in the home (Steele, 1992). Although renters also benefit from the tax system (if it is assumed that their landlords are high-rate taxpayers, because of the asymmetry in the way the inflationary component of their landlords' interest payments is all deductible, but that of capital gains is taxed at a lower rate), recent tax reforms have strengthened the tax benefit of owner occupation to higher-income groups. During inflation, the tax system also provided an incentive for low-income households with little equity to become renters (Steele, 1992).

As a consequence of the increase in ownership, there has been a significant fall in the demand for private renting amongst those able to pay the rents needed to generate new construction of private rented housing (Hulchanski, 1991). As Table 7

Table 7 Housing tenure by income quintile, Canada 1977-87

Year	Lowest	Second	Middle	Fourth	Highest	Total
Percent owning						
1977	47	53	63	73	82	64
1987	37	53	62	75	87	63
Percent renting						
1977	53	47	37	27	18	36
1987	63	47	38	25	13	37

Source: Fallis (1990 p. 890).

shows, home ownership rates amongst the highest-income groups rose between 1977 and 1987, but fell amongst those in the lowest-income groups. Thus, there are proportionately more renters amongst lower-income groups and renting has increasingly become the tenure of those on lower incomes. As a result, it has been argued that there are not enough tenants with the ability and willingness to pay the rents that provide viable returns on newly constructed rented housing (Hulchanski, 1994).

7 Impact of taxation and supply incentives

Although support for private market rental housing has, in general, not been a key issue in Canadian housing policy, there have been a number of instances when it has become more important. This is partly because of concerns about supply and about affordability, and partly because of the impact that new build for private renting can have in creating construction industry jobs (Sewell, 1994). As a result of these concerns, the federal government initiated a number of incentive programmes to stimulate output in the private rented sector. The starts associated with these incentives between 1946 and 1984 are shown in Table 8. There have been two phases of intiatives: a social housing phase, up to 1967, when private renting was used to create social housing; and an entrepreneurial phase thereafter, when government was intent on stimulating construction for market provision (CMHC, 1986). This section reviews these initiatives, but begins with a review of the impact of the tax system on investment in new private rented housing.

Capital cost allowances

Until the mid-1970s the private market produced substantial quantities of private rented apartments without a visible explicit subsidy for rented housing. There was no rent control and there was a growing demand for rented accommodation from newly forming households, including new immigrants from overseas. Hence falling voids and higher rents created profitable investment opportunities for individuals and

Table 8 Federal rental programme activity (dwelling units), 1946-1984

Year	LD	ARP	MURB	CRSP	Total apartments
1946	3,449				
1947	75				
1948	116				
1949	144				11,548
1950	94				15,192
1951	174				9,919
1952	841				17,190
1953	1,295				24,425
1954	2,261				28,455
1955	1,423				28,667
1956	1,620				27,250
1957	4,124				30,113
1958	6,282				49,411
1959	4,518				38,699
1960	1,591				31,988
1961	3,326				37,497
1962	1,328				44,677
1963	2,094				63,575
1964	1,717				79,873
1965	70				83,200
1966	0				56,551
1967	0				81,650
1968	1,956				111,425
1969	7,364				121,638
1970	19,440				108,953
1971	11,059				121,846
1972	8,470				120,695
1973	4,650				123,742
1974	2,022				88,957
1975	10,895	22,351			92,124
1976		25,151	10,068		123,000
1977		57,053	25,212		118,948
1978		18,198	61,891		97,706
1979			76,550		71,636
1980			0		59,731
1981			61,500		77,134
1982				10,405	65,149
1983				10,265	53,645
1984				3,452	45,657
Total	102,398	122,753	235,221	24,122	2,361,866

Source: CMHC (personal communication).
LD = Limited Dividend programme
ARP = Assisted Rental Programme
MURB = Multiple Unit Rent Building scheme
CRSP = Canada Rental Supply Programme
(see Section 7).

corporations. Whilst rents covered operating costs and mortgages, a key attribute of this investment was its tax advantages. Until tax reforms in 1972, favourable capital cost allowances (CCA) in excess of actual depreciation and generous tax deductions allowed for 'soft' costs (acquisition and development fees and other costs) made property in general and private renting in particular a highly tax-efficient investment. They enabled individuals and corporations to create paper losses on rental investments and thus reduced tax liabilities on other income (Clayton Research Associates, 1991). Estimates suggest that in the early 1980s, CCA cost $100m annually in tax expenditure (Dowler, 1983). A key advantage of the CCA provision was that it allowed landlords to reduce taxation on new dwellings in the early years of an investment, thus generating cash in the early years and deferring taxes until later years (when, in the case of individuals, personal taxation liability might be less). CCA was recaptured upon the sale of a dwelling if the sale price exceeded its depreciated value, although this could be deferred if more than one dwelling was owned by pooling it with the CCAs on others. Whilst this was an 'accidental' subsidy in the sense that it was not introduced as an explicit policy, it was nevertheless used in 1947 to stimulate new construction (Clayton Research Associates, 1989; Miron, 1988). Moreover, as has already been remarked in earlier sections of this paper, Steele has shown that, even without the accelerated depreciation provisions, the asymmetrical way in which interest payments were tax deductible and capital gains were taxed made private renting attractive for individuals (Steele, 1992, 1993).

The Limited Dividend programme

Very little social, non-market, rented housing was available in Canada in the immediate post-war years. Instead the federal government relied upon its Limited Dividend (LD) programme to stimulate new building by the private sector for low- and moderate-income households, thus using private landlords to provide social housing. This ran from 1946 to 1974, during which time LD was subject to significant changes in programme design, and produced just over 100,000 units, which accounted for six per cent of all apartment and row starts in the period. LD companies were given favourable loans in return for limiting their dividend, for charging below-market rents, and for limiting tenants to those in specific income groups. LD was re-launched in 1968 as a 'full recovery, low rental housing' programme to enable it to help private landlords produce housing at below-market rents for moderate income households. Thus there was a shift from a social housing focus to a programme designed to stimulate construction at slightly below-market rents. This reformulation resulted in more high-rise construction in contrast to the low rise that had characterized the previous phase. The programme as a whole came in for significant criticism because the dwellings produced were of poor standard and in inferior locations and because the agreements have proved difficult to enforce. Upon the expiry of the qualifying period, dwellings appear to have been sold into owner occupation (Dennis and Fish, 1972).

Assisted Rental Programme and the Multiple Unit Rent Building scheme

By the mid-1970s, the earlier incentives to invest in full market rented housing had diminished. Inflation in building and land costs rose and rising interest rates on debt financing turned positive into negative cash flows in the early years of new projects. There was an increasing gap between what tenants were willing to pay in terms of market rents and the rents landlords needed to charge to make new construction profitable. Tax reforms introduced capital gains taxation in 1972 (50 per cent of capital gains were included in income for tax purposes) and also meant that capital costs allowances could no longer be used by individuals to create or enhance losses to offset other taxable income. Only real estate companies could do this. Although CCA was available to individuals and non-real estate companies, it could no longer be set against other income. In addition, pooling was eliminated for everyone as a way of avoiding recapture. The depreciation rate was reduced after 1978, and soft costs deductibility was restricted to real estate companies after 1981 (for others it had to be included in the depreciation base and written off through CCA). Hence, the tax advantages of investing in private renting declined considerably.

Private rental starts began to fall (see Figure 1) and rents rose. All provinces responded to the federal government's request to introduce rent controls to support its counter-inflation strategy (these are still in place in all but five provinces). Rent controls introduced significant uncertainty for developers as well as, potentially, reducing market rents. However, controls were never draconian and new buildings were mostly exempted for an initial period. Moreover, rent controls in most provinces took the form of reviews, rather than price freezes. These allowed automatic annual increases and enabled cost increases to be passed on to tenants (see below). Nonetheless, the drop in new construction prompted the federal government to introduce two incentive programmes for market renting (at the same time as programmes to promote home ownership and a limited social housing programme were set up).

The two programmes, the Assisted Rental Programme (ARP - 1975 to 1978) and the Multiple Unit Rent Building scheme (MURB - 1976 to 1979 and 1981), together accounted for nearly 358,000 dwellings or 56 per cent of all new conventional market rented housing constructed over the lifetime of the two schemes. MURB accounted for 75 per cent of the combined output of these two programmes.

ARP was designed to keep economic rents down to market levels (and so enable new construction to proceed at rents which tenants could afford) by placing restrictions on equity returns and rents in return for, initially, tax-free grants or, in the later schemes, interest-free loans with repayments related to the rate of rent increases and levels of return on equity (Lithwick, 1977). Dwellings had to be modest in size and capital value. Although there were no income limits on tenants, evaluation suggested that the programme housed tenants on average incomes. The latter outcome was in part due to the constraints on dwelling size. It also helped the poor because it raised overall supply, since nearly 60 per cent of the ARP dwellings would not have been built without the ARP assistance or the capital cost allowances under MURB (see below) which were also available to the programme (Lithwick, 1977).

MURB did not involve such conditions and in essence restored many of the tax advantages of investing in private rental housing lost in the tax reforms of 1972. It thus recreated a tax shelter for individuals and non-real estate companies who invested in rental housing. This was equivalent to between 15 and 20 per cent of capital costs (Dowler, 1983). Syndications of tax shelters boomed (Clayton Research Associates, 1991). There was a substantial increase in starts (many targeted at the top end of the market), rents rose only moderately (partly because of rent review) and voids increased considerably. Because of the easing of market conditions, the ARP and MURB provisions were dismantled. In addition, the depreciation rate for CCA was reduced in stages between 1978 and 1987 and the soft costs allowed for deductions have also been more restricted since 1981. Subsequently, there was a considerable fall in starts. Nonetheless, syndications continued after the expiry of the MURB provisions in 1982, despite the reduction in the tax advantages (Clayton Research Associates, 1991).

The Canada Rental Supply Programme

In 1982 the federal government enacted the Canada Rental Supply Programme (CRSP). This produced 24,000 dwellings, or 15 per cent of all private rental starts before it was terminated in 1984. It was as much a counter-cyclical programme to increase jobs in the construction industry during the early 1980s recession as it was a programme to respond to the fall in private rental construction. In effect, CRSP re-introduced the ARP provision on a cash-limited basis giving an interest-free deferred repayment loan. In return, landlords had to agree to let five per cent of the dwellings to disabled tenants and to let a third of the dwellings under the Rent Supplement Programme (a rent allowance programme for low-income households meeting rent in excess of that taking a quarter of household income).

Recent developments

There have been no more federal programmes to assist the construction of new private rented housing. Provincial programmes supporting federal ones, such as those in British Columbia and in Manitoba, have also come to an end.

In addition, programmes designed to assist landlords to carry out renovation to the existing stock have been cancelled. The private rented element of the Residential Rehabilitation Programme (RRAP) provided landlords with CMHC loans towards improving substandard stock, which were written off where landlords charged less than market rents for the improved unit (Rostum, 1978; Vischer, Skaburskis, 1982). It was argued that these loans, whilst targeted at the worst stock, were poorly targeted because low-income tenants were not the ultimate beneficiaries, as a result of displacement (CMHC, 1988). The cancellation of rental RRAP has been much criticized by some municipal authorities because it undermines their attempts to enforce standards and get an upgrading of older housing areas which also have poorer tenants.

Meanwhile, revisions designed to ensure that the tax laws were neutral with respect to property (reduced depreciation; taxation raised to 75 per cent of nominal capital gains in 1990 after a lifetime allowance, initially introduced in 1985 and later fixed at $100k in 1987) have reduced some, but not all, of the remaining incentives of individual landlords to invest (who are assumed to be mainly interested in capital gains), most corporations having ceased to do so. It is now recognized that only small scale individual landlords have significant incentives to invest (with syndications becoming important as ways for individuals to secure their lifetime allowances), but that zoning and other planning policies may be inhibiting supply in some areas (see below).

Evaluation of incentive programmes

Evaluation of these incentive programmes suggests that, whilst the gross effect of the above programmes has been considerable and that much of the investment was additional in the short run, the net effect over the longer term is likely to be much less. It was estimated, for example, that 47 per cent of the LD starts were additional to those that would otherwise have occurred, and that 19, 36 and 41 per cent of the starts under ARP, MURB and CRSP respectively were also additional. Altogether multiple starts were over four per cent higher over the period during which these programmes were operational than they would have been without them (Fallis et al., 1989). However, the net effect in the longer run is likely to be less considerable. This is because the increased stock generated by the programme increased voids and reduced rents more than would otherwise have been the case. Reduced rents increased demand but also discouraged future investment. As a result, excess supply was reduced, leading to pressure on rents, a fall in demand and a return to long-term equilibrium, with fewer starts in later periods. However, since rent review procedures enable rents to be increased, the impact of the incentive programmes in reducing new starts in the longer run is likely to be delayed (Fallis et al., 1989).

Many analysts have been critical of these incentive programmes because they are temporary initiatives to overcome short-term problems and/or to create jobs in the building industry. They have not done much more than temporarily increase supply overall. Indeed, insofar as their main effect has been to increase voids, there is evidence in loose markets, like Winnipeg and Halifax, that landlords are defaulting on loan payments to CMHC (CMHC, personal communications). There is also evidence, from some other markets, where land supply is restricted, like Vancouver, that the subsidies have been capitalized into higher land prices in areas zoned for multifamily housing, with no net effect on profitability and, therefore, on new construction (Gau & Wicks, 1982).

Those programmes that attempted to target supply at low-income groups with deep subsidies in the form of favourable loans have created the greatest net addition to the stock. However, they have involved agreements that have proved difficult to enforce, with the result that they are sold into home ownership when operating agreements expire. Where incentives arise from tax shelters, there are few controls to ensure that specific tenant groups benefit from the increased supply. The principal beneficiaries appear to be professionals who bought into syndicated tax shelters. Finally, critics point to the inefficiency of subsidies and to the way in which their 'on' and 'off' nature has contributed to uncertainty, which in itself reduces investment.

In sum, critical analysis of federal (and provincial) incentives showed that they only had a temporary effect. In part, this is because they did not address the determinants of demand. Nor did they deal with other supply constraints that cannot be dealt with by tax and other incentives, particularly municipal zoning plans which inhibit supply response.

8 Rent controls and landlord and tenant law

Following the dismantling of wartime controls, rent control was virtually non-existent in Canada between the early 1950s and the mid-1970s, although security of tenure legislation had been adopted by many provinces before the introduction of rent controls throughout Canada in the mid-1970s. Despite the fact that real rents had fallen in post-war years, pressure for rent controls developed because of the unanticipated surge in rents with the onset of inflation in the early 1970s. Indeed, a number of provinces were contemplating introducing controls before the federal government's 1975 request to all provinces to introduce rent controls after the imposition of temporary wage and price controls. By April 1975, rent controls had been introduced in all provinces but have since been repealed in five provinces (Alberta, British Columbia, New Brunswick, Nova Scotia and Saskatchewan).

Quebec has a form of rent control similar to that prevailing in Britain before the latter's deregulation of new lettings in 1989. That is, landlords and tenants are encouraged to agree rent increases between themselves within a framework of guidelines provided by the provincial authorities. The rent becomes subject to binding arbitration only if they cannot agree. New construction is exempt. Although rents for new lettings of vacant properties are supposed to be the rents charged for the previous lettings, the evidence suggests that, in practice, market rents are charged (Clayton Research Associates, 1991). Most of the other provinces have a form of rent control known as rent review. This allows landlords to increase the rent of all dwellings as of right by an annual guideline. Additional increases for individual dwellings can be permitted upon a review of the specific circumstances, especially in relation to what are known as 'cost pass throughs', such as increases in management and maintenance and financing costs. New dwellings are often exempted for a period. In Quebec and Ontario, for example, this exemption runs for five years and in Nova Scotia it ran for four.

Rent review provides, in principle, a flexible form of rent regulation. Yet since the administrative discretion built into the legislation allows an examination of the specific circumstances that might justify increases beyond annual guidelines, rent control has come in for substantial criticisms. An important criticism is that, even if the outcome of review does not reduce existing returns, it raises the cost of supply. That is because landlords want higher returns to compensate them for the greater risk and uncertainty created by controls (Stansbury & Todd, 1990).

A notable body of criticism is found in the report of the official commission set up by the Ontario government to look at the operation of rent control in the province (Commission of Inquiry into Residential Tenancies, 1987). Having commissioned substantial research, the Commission concluded that rent control had resulted in a lack of new investment and the conversion and demolition of rental units. It had also resulted in deterioration of the existing stock because, despite the 'cost pass through' provisions, landlords failed to claim for higher repair costs because of the administrative and other costs of doing so. Nor was rent control an effective or equitable method of assisting low-income renters. Many of those who could have afforded to pay market rents got the benefit of lower rents, whilst low-income tenants in uncontrolled dwellings paid rents higher than would otherwise have prevailed (see also Fallis and Smith, 1984). The Commission accepted, however, that it was right to protect tenants from 'rent gouging' and 'economic eviction'. Accordingly, it favoured the introduction of a system of fair market rents to restore investment incentives, allied to the introduction of a system of rent allowances to help low-income tenants afford suitable accommodation (see Steele, 1985, for a discussion of potential rent allowance schemes; see also Smith, 1995, and Stansbury and Todd, 1990, for further critical discussion of rent controls).

However, political and other demands for rent control have been strong (see Hulchanski, 1994). Most provinces that have retained rent controls have in fact tightened up their systems, including the introduction of registration schemes, in ways that reduce supply incentives. As a corollary of tighter controls, provinces have introduced legislation to prevent the loss of existing rental units. Rental conversion legislation, for example, restricts the transfer of rental apartments into condominiums, although pre-registration of rental apartment buildings as condominiums limits the impact of the legislation. Landlord and tenant legislation has also been tightened up to increase tenants' protection.

9 Local markets and the impact of land use planning controls

Some of the most recent analysis of the private rental market has looked in detail at the varying performance of the rental market in different parts of Canada. In particular, it has examined performance in areas like Vancouver. There, even though rent controls have been removed, there is little new construction, despite low voids and rising rents. It has also examined other areas, like Montreal, where, in contrast, rent controls remain and voids are high, but new construction has taken place (Clayton Research Associates, 1991).

In Vancouver, although there was little new construction of conventional apartments, there was considerable additional supply of a non-conventional form, including accessory suites. Conventional construction was not profitable because of high land costs, a product of the condominium boom and restrictive zoning regulations, which provided an inadequate supply of pre-zoned multiple unit sites.

In contrast, the construction of new units continued in Montreal, where rents rose more than the retail price index and where there was little non-conventional supply. Most new investors were individuals who were not full-time landlords and who took a long-term view of their investments (including capital appreciation). Montreal also had an adequate supply of pre-zoned land. This, together with low land prices, enabled small investors to enter the market.

This analysis has pointed to the importance of planning controls in limiting market responses to increased rents and falling voids by restricting sites where new apartment blocks can be built, by limiting the intensification of existing rental dwelling units, and by preventing the creation of accessory suites in owner-occupied dwellings (see also Poulton, 1995).

10 Summary and conclusions

Following the termination of the CRSP scheme, private rental starts have fallen. The demographic and economic climate in the 1980s and 1990s has not been conducive to investment. The baby 'bust' generation has placed less demographic pressure on the market than its predecessor baby boom generation did, though migration from overseas compensates for this fall in certain markets, particularly Toronto and Vancouver. The recession of the early 1990s also reduced demand, with evidence that some young unmarried single households out of work were returning to the parental home as a means of coping with housing affordability problems.

Meanwhile, the attractions and affordability of home owning have meant that many upper- and middle-income two-earning households have left the rented market. This latter trend has been accentuated by the growing availability of condominiums which provide the ownership of new dwellings at relatively low cost. It has also been accentuated by other recent changes that reduce down payment requirements to five per cent for federally underwritten mortgages and which allow mortgagees to withdraw savings from retirement savings plans to fund deposits. As a result, the tendency for private renters to come from the bottom end of the income spectrum has been strengthened so that the gap between what can be afforded by tenants and what landlords need to fund new construction has widened further. Shelter allowance schemes are mainly restricted to helping pensioners pay rent and have rarely been seen as instruments to increase rents and hence increase demand for new supply. Instead they have primarily been seen as having a limited role in overcoming affordability problems for the non-working poor.

Moreover, new private rental construction has had to compete with the oversupply of condominium housing that resulted from the late 1980s property boom in cities like Toronto and Vancouver. Much of this was built speculatively with the expectation that the first buyers would be able to make capital gains by selling on without first having to move in. The subsequent property slump has left many investors holding assets worth less than they paid for them, and evidence shows many of them renting their properties. When prices rise, it is expected they will transfer to owner occupation (the condominiums having been registered so as to avoid being caught by laws preventing such transfer).

New rental construction has furthermore had to compete with an apparent increase in the supply of accessory apartments - basements and other parts of dwellings rented out by owner occupiers wanting help with their mortgage payments, often letting in defiance of zoning laws and building codes. Moreover, the reduction of tax incentives has meant that there has been little new construction, despite recent rent increases (Clayton Research Associates, 1991).

Recent debates about rental supply in Canada have focused on the best way to increase new rental construction and in particular on the appropriate balance between non-market provision (especially by municipal and private non-profits) and market provision.

Proponents of non-market provision argue that private rental housing does not necessarily provide the most efficient and effective way of housing the lowest income groups and that, from a cost-effectiveness point of view, an increase in non-profit housing is desirable, especially for low-income family households.

Proponents of market provision argue that supply should be stimulated by removing rent controls, by adjusting planning policies to remove unjustifiable constraints, by providing shelter allowances to assist the poor to pay the costs of provision and by encouraging small investors (though not by subsidies). Supply subsidies are argued to be inefficient by comparison with demand subsidies. The various schemes proposed would, it is argued, avoid some of the problems found in housing allowance schemes in the USA and Britain. In particular, it is argued that adequate pre-zoned land should be identified for new small-scale apartment construction and that the creation of accessory suites must be permitted - or their illegal creation tolerated (Poulton, 1996). If current planning constraints preventing intensification in low- and medium-density housing areas are removed, this will permit small-scale landlords to create small units in neighbourhoods where they have realistic expectations of getting capital gains. It has also been argued that renovation subsidies should be re-extended to private landlords, since existing substandard units are an important source of potential low-cost rental housing for low-income groups (Pomeroy, 1995). All levels of government thus have a role to play. Hence policy consistency will be important if new supply is to be increased

This brief examination of the Canadian experience does point to some general conclusions that may be of relevance to other countries as well. First, the strong contrast between the short- and long-run impact of supply incentives suggests that other issues -- including demand and other supply constraints -- must be addressed when developing policies to increase supply. Second, the balance between demand and supply subsidies in stimulating private renting needs examining. Canada has, on the whole, neglected demand subsidies (partly because supply subsidies worked faster in creating new units). Shelter allowances are targeted at the poorest, so that their role in assisting households in work is limited. However, shelter allowances may be more appropriate in dealing with affordability problems than in stimulating investment. Third, the Canadian evidence suggests that tax incentives that bring equity investment into the market can work quickly in creating new construction, particularly when companies and individuals can gear up by borrowing. What is needed, however, are schemes that will keep investment in the market rather than ones that are short lived, have heavy syndication costs, and whose dwellings transfer to the owner-occupied sector once the provisions of the schemes expire. Fourth, the Canadian experience shows how difficult it is to achieve housing for very low income groups by the market. Deep subsidies, such as loans and grants, are needed, together with agreements that are often difficult to enforce. This suggests that a balance has to be struck between deep subsidies for non-market agencies, subject to a range of controls, and shallower tax subsidies to stimulate market provision. These measures should be allied to shelter allowances to help individuals to cope with market rents, but with fewer controls over landlords in this market sector.

Finally, the Canadian experience shows how important it is to examine all constraints, including planning policy, and to recognize the diversity in local and regional markets. This suggests that single solutions are less likely to be effective than ones that take local circumstances into account. It also implies that co-ordination of financial, housing and planning policy at the local level is needed.

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