Judgment of 19th April 2005, K 4/05

# LIMITATION OF RENT INCREASES FOR LIVING QUARTERS (II)

| Type of proceedings: | Composition of Tribunal: | Dissenting opinions: |
|---|---|---|
| Abstract review<br>**Initiator:**<br>Prosecutor General | Plenary session | 0 |

| Legal provisions under review | Basis of review |
|---|---|
| Prohibition on increasing rents by more than 10% per year, where the rent exceeds 3% of the annual reconstruction value of living quarters or will surpass this threshold as a result of the increase<br>[Amendment of the Protection of Tenants' Rights and Housing Resources of Communes Act and Amendment of the Civil Code and Amendment of Other Statutes Act (of 17th December 2004): Article 1 point 9 letter a; Amendment of the Protection of Tenants' Rights…(*ibidem*) Act (of 22nd December 2004): Article 1] | Rule of law<br>Principle of proportionality<br>Protection of ownership<br>[Constitution: Articles 2, 31(3), 64(1) and (2)] |

The process of adjusting, to free-market principles, legislation regulating the determination of rent levels for living quarters within private resources has already taken ten years and is progressing slowly. This is especially true as regards rents applicable under the "old" lease regime – imposed upon private owners during communist times (these relations still exist to a large extent, given strong statutory protection of the continuity of a lease). This process has been surrounded by political and social controversies, repeatedly inducing the legislator to adopt solutions that have raised objections from the perspective of constitutional guarantees of private ownership. The Constitutional Tribunal has twice already – in the years 2000 and 2002 – ruled that significant elements of the statutory regulation of rent levels failed to conform to the Constitution (see the summaries of judgments in cases numbered P 11/98 and K 48/01). The present judgment constitutes the next in this series.

In light of the hitherto legislation and the two aforementioned Constitutional Tribunal judgments, the end of 2004 represented a significant caesura. Following this date, rents applicable under the "old" lease regime were to be "released" in accordance with a specific promise contained in the 1994 Act and 2001 Act. Until such time – with the Constitutional Tribunal's approbation – there remained in force a prohibition on increasing such rents (in the form of terminating existing rent agreements by the property owner) beyond an amount equivalent to 3% of the annual reconstruction value of the living quarters (cf. Article 28 of the Protection of Tenants' Rights and Housing Resources of Communes Act and Amendment of the Civil Code Act 2001). Such limitations did not apply to so-called payments independent of the owner.

In addition to the aforementioned – transitional – limitation of rent increases under the "old" lease regime, following the Constitutional Tribunal's judgment in case K 48/01, only one other limitation of increasing payments for living quarters, dependent upon the owner, remained in force. It concerned all

forms of use of living quarters and prohibited increasing such payments more frequently than every 6 months (Article 9(1) of the aforementioned 2001 Act, in its original wording).

On 17th and 22nd December 2004, shortly prior to the crucial date of 31st December of that year, Parliament finally adopted two amendments to the aforementioned 2001 Act. In consequence of both amendments, Article 9(1) and (1a) of the amended 2001 Act obtained the following wording:

"1. An increase in rent or other payments for use of living quarters, excluding payments independent of the owner, shall not take place more frequently than every 6 months and, where the annual level of rent or other payments for use of living quarters, excluding payments independent of the owner, exceeds 3% of the reconstruction value of such living quarters, the annual increase shall not exceed 10% of the hitherto rent or hitherto payments for use of living quarters, calculated non-inclusive of payments independent of the owner.

1a. Article 9(1) shall also apply to an increase in rent or other payments for use of living quarters, excluding payments independent of the owner, where the annual level of rent or other payments for use of living quarters, excluding payments independent of the owner, would, as a result of the increase, exceed 3% of the reconstruction value of the living quarter."

From a formal perspective, the limitations of rent increases envisaged by Article 9 apply, without differentiation, both to rents applicable under the "old" lease regime (subject to the previous strict legal regulation) and to rents freely negotiated between parties to "new" lease relations. Such limitations also apply to payments for use of a living quarter, being the property of another person, within the framework of legal relations other than a lease.

Both amendments, as expressed in the second part of Article 9(1) and in Article 9(1a), were challenged before the Constitutional Tribunal by the Prosecutor General.

In the applicant's view, such amendments evidenced not merely the legislator's failure to comply with the principles of correct legislation (contained within the rule of law clause – Article 2 of the Constitution) but also lead to an excessive (disproportionate) interference with the right of ownership (Article 64(1) and (2), read in conjunction with Article 31(3), of the Constitution). They envisage regulation of rent increases for the purpose of protecting the rights of all tenants, regardless of whether in each case there exists a real social need for such protection, such as where dealing with tenants in a good financial situation.

The applicant also drew attention to the challenged regulation's incoherence with the special procedure for terminating rent agreements, as envisaged in Article 8a of the 2001 Act (which was not challenged) as supplemented by the Amendment Act of 17th December 2004. This provision states, inter alia, that a rent increase leading to a rise in the annual rent level exceeding 3% of the reconstruction value of the living quarters, may only take place "in justified circumstances". In such cases an owner is obliged, upon the tenant's request, to provide in writing the reason for such an increase and the calculation thereof. A tenant may "challenge" such calculation before a court. Until such time as the court's judgment becomes final, the increase shall not have any effect. This procedure is, however, inapplicable to increases which annually do not exceed 10% of the hitherto rent.

## RULING

**1. Article 1 point 9 letter a of the Amendment Act of 17th December 2004 (modifying the wording of Article 9(1) of the amended Act), in its part containing the phrase: "and, where the annual level of rent or other payments for use of living quarters, excluding payments independent of the owner, exceeds 3% of the reconstruction value of such living quarters, the annual increase shall not exceed 10% of the hitherto rent or hitherto payments for use of living quarters, calculated non-inclusive of payments independent of the owner", does not conform to Article 2, as well as to Article 64(1) and (2), read in conjunction with Article 31(3), of the Constitution.**

**2. Article 1 of the Amendment Act of 22nd December 2004 (inserting Article 9(1a) into the amended Act, precisely stipulating the scope of application of the amended Article 9(1)), does not conform to Article 2, as well as to Article 64(1) and (2), read in conjunction with Article 31(3), of the Constitution.**

## PRINCIPAL REASONS FOR THE RULING

1. None of the aims of the challenged statutory regulation have been achieved. The "release" of payments for living quarters within rational limits, taking account of the demands for justice and protection of owners' rights, did not occur. Nor were effective and precisely defined mechanisms introduced to protect tenants' rights against owners abusing the possibility to increase payments. Contrary to the legislator's own intentions, the challenged amendments excluded the market mechanism, whilst the aim of introducing limitations restricting rent increases was to protect persons who, in a particular case, do not consent to the increase proposed by the owner. This amounts to an infringement of the principles of correct legislation and, *ipso facto*, to the non-conformity of the challenged regulation with the principle of the rule of law, as expressed in Article 2 of the Constitution.

2. Legislation from the last decade and the Constitutional Tribunal's jurisprudence have carefully consolidated the social belief of interested owners and tenants that so-called regulated rents – limited to 3% of the reconstruction value and applying only in respect of some lease relationships – will remain in force only for a transitional period, until 31st December 2004. Adoption of the challenged regulation, promulgation thereof on 29th December 2004 and the entry into force thereof on 1st January 2005, infringed the "rules of the game" laid down in the earlier legislation, although no extraordinary circumstances or events occurred such as would justify prolongation of such "rules". Infringement of such a specific promise, expressed statutorily, must be treated as a reflection of particular irresponsibility on the part of public authority and, *ipso facto*, as a flagrant breach of the principle of protecting trust in the State and its laws, constituting one of the fundamental elements of the rule of law principle (Article 2 of the Constitution).

3. The principle of equal protection of ownership and other property rights stems from Article 64(1) and (2) of the Constitution. Amongst "other property rights" are included the right to lease living quarters and other rights connected with quarters serving to fulfil housing needs. Each of these rights – vested both in owners (lessors) and tenants (lessees) – enjoys constitutional protection, albeit not to an equal degree. Whilst it will be common for conflicts to arise in this area, it would, nevertheless, be an over-

simplification to assume that providing a certain level of protection for one of these interests must automatically lead to reducing protection of the other. It is the legislator's task to ensure the harmonious development of mutual relations between owners and tenants, reflected particularly in payments for use of living quarters, including rents payable within lease relationships. Such payments should allow an owner-lessor to cover the costs of exploiting and renovating a building, whilst also ensuring a return of invested capital (depreciation) and providing fair profits. It is also essential to take account of the justified interest of the lessee (tenant) and to create real mechanisms for protection thereof against an abuse of the owner-lessor's right.

4. In declaring the future abolition of regulated rents, the legislator never promised that, as of 1st January 2005, rent levels determined by the parties will be totally uncontrolled. Such control over rents, exercised by the courts, would, however, only be effective provided that statute clearly laid down its elements and formulated clearly-defined criteria of assessment. Nevertheless, this did not occur.

5. Furthermore, it is indispensable to create instruments to support tenants who find themselves in difficult financial or social situations. This may not take place, as it has until now, primarily at the expense of owners but, rather, it should consist in providing special public resources. The obligation of social solidarity and assisting the weaker rests on society as a whole.

6. The judicial decision that the provisions of the amendment Acts challenged by the applicant do not conform to the Constitution (insofar as indicated in the ruling), leads to the loss of binding force of the relevant fragments of Article 9 of the amended Act.

7. The findings in the present case were determined by the scope of the Prosecutor General's challenge. This judgment does not categorically and comprehensively resolve fundamental questions concerning the mechanism for balancing the respective interests of tenants and owners. Resolution thereof requires systemic changes.

**Provisions of the Constitution**

**Art. 2.** The Republic of Poland shall be a democratic state governed by the rule of law and implementing the principles of social justice.

**Art. 31.** […] 3. Any limitation upon the exercise of constitutional freedoms and rights may by imposed only by statute, and only when necessary in a democratic state for the protection of its security or public order, or to protect the natural environment, health or public morals, or the freedoms and rights of other persons. Such limitations shall not violate the essence of freedoms and rights.

**Art. 64.** 1. Everyone shall have the right to ownership, other property rights and the right of succession.
2. Everyone, on an equal basis, shall receive legal protection regarding ownership, other property rights and the right of succession.
3. The right of ownership may only be limited by means of a statute and only to the extent that it does not violate the substance of such right.