

Short-term lettings—snags in the sharing economy

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Property analysis: Partner, Dev Desai, and Associate, Thomas Bumstead, of Watson Farley & Williams LLP's Dispute Resolution Group give a brief guide to short-term lettings and examine the problems they present.

Finding a place to rest your head

One of the many consequences of the digital revolution has been the recent and rapid growth in the so-called 'sharing economy'. From lift sharing via Uber, pet-sharing on BorrowMyDoggy, to peer-to-peer lending via platforms like Zopa and RateSetter, users are embracing a range of digital platforms to maximise their earning potential and seek added value by sharing their assets.

Nowhere can this more clearly be seen than in the example of Airbnb which enables a homeowner to offer up a sofa, spare bedroom or indeed their whole home, to someone looking for a bed for the night. In London alone, more than 30,000 entire homes are currently listed on Airbnb with some estimates suggesting that around £600 million will be generated in the capital through the platform during 2017. Airbnb is but one (though perhaps the most prominent) of numerous online brokers of short-term lodgings. Others include FlipKey, HomeAway, HouseTrip, Onefinestay and CouchSurfing.

However it has not all been smooth sailing for these new hospitality marketplace brokers and their networks of property hosts, with their meteoric growth causing alarm bells to ring in a number of quarters. There have, of course, been anecdotal reports of anti-social behaviour from some guests and discrimination by hosts based on prospective guests' names. There are also concerns as to the tax positions of brokers such as Airbnb and the hosts as casual suppliers in a broader hospitality market. In addition, the popularity of short-term lodgings is being blamed for driving up rent and exacerbating existing problems of urban overcrowding by reducing the supply of accommodation available for medium-term leases. An increasing number of landlords are moving their properties from the assured shorthold tenancy letting market (dogged with stagnation of rents) to the short-term lodging market (at significantly higher per-night lodging rates).

In response, some cities around the world have taken far-reaching action to curb the use of lodging marketplaces in order to protect local communities. New York has banned all listings of entire flats for periods of less than 30 days unless the host is present. Meanwhile, Berlin has banned listings of entire homes on sites such as Airbnb altogether (although lettings of individual rooms are permitted). Even in San Francisco, the birthplace of Airbnb, the platform has been forced to accept regulations. In order for the city to monitor the use of housing stock, short-term lodging brokers are required to automatically enrol users in a database which tracks short-term lettings.

By comparison, the UK's approach has wavered. Under the Cameron government, changes to tax rules were mooted which were aimed at rewarding 'micro-entrepreneurs' by allowing them to earn up to £1,000 from online sources without having to declare, or pay tax on, the income. In comments promoting the change, the then-Chancellor George Osborne made it clear that these measures were specifically aimed at sites such as Airbnb and Ebay. This measure was quietly dropped from the Finance Bill in the build up to the 2017 election and there seems little prospect it will be resurrected in the near future. Hosts of short-term lodgings are still able to benefit from changes which came into effect in April 2016 which allow everyone who lets out rooms in their main residential property to earn up to £7,500 tax free (increased from £4,250). However, a paragraph buried in the 2017 Spring Budget suggests that this allowance will be subject to future consultation with a view to ensuring that the relief aligns with 'its intended purpose, to increase [the] supply of affordable long-term lodgings'. After seeming to jump into bed with Airbnb and the like as pioneers of the flexible short-term sharing economy, the UK government now appears to have got cold feet.

Nevertheless, the preferred approach in the UK has been to work with short-term lodging brokerages to allow them to police themselves. The most notable example of this has been the deal agreed in December 2016 whereby Airbnb took on responsibility for ensuring that its users in London adhere to the rules set out in the [Greater London Council \(General Powers\) Act 1973](#) (GPA 1973) as amended by the [Deregulation Act 2015](#). Since 26 May 2015, these rules have allowed London residents to rent out their home for short-term sleeping accommodation for up to 90 days in a calendar year without obtaining planning permission. Prior to the deal agreed with Airbnb, these rules were widely flouted by users, but Airbnb now prevents hosts from listing a property for more than 90 days without providing evidence that they have the necessary permission. It remains to be seen whether this pooling of responsibility between government and platform will lead to better regulation of the sharing economy. By way of contrast, none of Airbnb's competitors directly enforce the 90 day limit. Typically such sites include terms and conditions of use that require hosts to warrant to the broker that the host has all the necessary rights and authority to offer for short-term lodging. While effective in protecting the position of the site, one questions how many hosts fully investigate whether they are fully compliant and, albeit unwittingly, break the law. This pushes responsibility for enforcement on to stretched local authorities. Undoubtedly, should any of these competitors grow to truly rival the popularity of Airbnb, they will face similar pressure to automatically ensure compliance.

In any event, as we shall see, the listing of properties on an online lodging marketplace can lead to the host breaching a variety of obligations pursuant to their lease, statute and terms of insurance. Given the massive popularity of Airbnb and the like, many hosts are either unaware of these breaches or have calculated that the risk of enforcement is minimal. This relaxed approach embodies the buccaneering spirit of the sharing economy, but it can lead to real risks and problems which the prudent host may wish to avoid. In order to properly understand these risks, the would-be Airbnb host must consider a number of hurdles.

Problems for the leaseholder

Does your lease permit you to rent out your property?

The most obvious hurdle if the host is a leaseholder rather than a freeholder, is the provisions of the lease. Many people in London own their property as leasehold and the capital also boasts the highest concentration of Airbnb listings in the country, so this is likely to be a common issue.

So far we only have one case which explores the construction of leasehold covenants in the context of Airbnb lettings—*Nemcova v Fairfield Rents Ltd* [2016] UKUT 303 (LC) (*Nemcova*). Here, the Upper Tribunal (UT) was asked whether a covenant that required premises to be used as 'a private residence' prevented those premises from being used for short-term lettings through Airbnb. In short the answer was 'yes' as the UT did not feel that Airbnb guests using the premises for periods of a few days could fairly describe those premises as their private residence, stating that 'the problem in such circumstances is that the occupation is transient. So transient that the occupier would not consider the property he or she is staying in as being his or her private residence even for the time being'. The tribunal did not specify a period which would be sufficiently permanent to satisfy the covenant, but did state that it was of the view that 'in granting very short-term lettings (days and weeks rather than months) as the appellant has done [she] necessarily breaches the covenant under consideration.' Given that Airbnb is used almost exclusively for lettings measured in days and weeks, this is a fairly serious blow for leaseholders who wish to advertise their homes through the portal. The UT did offer the caveat that each case was fact specific and so it was not possible to definitively state that the ruling operated as a blanket ban. However, the wording of the covenant in this case is common and the facts of the case were far from unusual—the lease was granted in respect of a flat within a small block for a term of 99 years and no reference was made to any unusual terms which impacted on the outcome. Therefore, the prudent leaseholder should check the terms of their lease carefully and, if it restricts use to a 'private residence' or similar, proceed with extreme caution, if at all.

The risks for a leaseholder who decides to proceed regardless are severe should the landlord discover the breach of lease. In *Nemcova*, the landlord was seeking forfeiture (termination) of the tenant's lease. While it is likely that a tenant in these circumstances will be able to obtain relief from forfeiture and, ultimately, keep their home, they will be required to pay the landlord's legal costs, which could run to thousands of pounds.

Do you need to check the immigration status of your guests?

In light of *Nemcova* there are additional problems for short-term lodging hosts in the provisions of the [Immigration Act 2014](#) (IA 2014). IA 2014 requires landlords to check the immigration status of prospective tenants or other occupiers before granting a 'tenancy agreement' (defined as including any lease, licence, sub-lease or any agreement for any of these). IA 2014 applies to any tenancy agreement which grants one or more adults the right to occupy premises as their 'only or main residence' and which requires the payment of 'rent' (defined by the Code of Practice which accompanies IA 2014 as including 'any financial transaction in the nature of rent').

These requirements are subject to certain exclusions, among which are 'holiday lettings' where it is clear that the person intends to use the premises for leisure related purposes for a short period and will not remain in the premises once that period expires. Paragraph 3.4 of the Code of Practice indicates that where a person has booked accommodation for a period of three months or more, this may indicate that the person could be intending to use the accommodation as their main home.

Of course, in the vast majority of cases, the use will clearly fall within the 'holiday lettings' exemption and it seems unlikely that any hosts will have carried out right to rent checks. However, should a landlord seek to forfeit a host's lease on the basis of wording similar to that in *Nemcova*, the leaseholder could find themselves in the awkward position of seeking to argue, on the one hand, that the guest does use the premises as his or her 'private residence' (to comply with the lease covenant) but, on the other hand, does not use it as a 'main home' (so there is no requirement to carry out right to rent checks pursuant to the IA 2014). A difficult balancing act indeed!

Take care to reflect leasehold obligations in 'house-rules'

Nemcova has taught leasehold hosts that they need to examine the terms of their leases, particularly if they contain reference to use as a 'private residence'. Hosts should also review leasehold wording which limits parting with possession or occupation, or places a minimum time limit on the period during which the property can be sublet. Many leases also incorporate reference to a scheme of regulations which are designed to prevent tenants causing nuisance to their neighbours. These regulations might include restrictions on the playing of music past a certain time, the number of occupants or the use of common parts. It is not difficult to imagine the myriad circumstances in which short-term lodging guests might breach such regulations if clear 'house-rules' are not in place. The Airbnb site and others allow such rules to be spelt out to guests at the point of booking. Hosts should draft them with a careful eye to the provisions of the lease and any regulations.

In the future, it is possible that landlords will seek to dispel any uncertainty and expressly prohibit hosting. Alternatively some tenants may seek to insist that a right to host is expressly recognised, particularly where they own a share of the freehold or have set up a Right to Manage company and so enjoy a measure of control over the landlord entity. Indeed, given the popularity of short-term lodging sites, this could be one of the few aspects of a purchase which a buyer takes an active interest in, perhaps asking his conveyancer to provide advice or seek amendments.

Planning issue—is planning permission required to lodge guests?

As discussed above, in London planning permission is required if the property is to be used for short-term lets for more than 90 days in a calendar year (GPA 1973, s 25A). These restrictions do not apply to the rest of the UK, although in Northern Ireland it is necessary to obtain a certificate from the tourism office for properties offered for tourist accommodation.

Hosts should, however, be aware that their listing could be a 'House in Multiple Occupation' (HMO) for the purposes of the [Housing Act 2004](#). This requires property owners to obtain a HMO licence from the local authority when letting properties which are three or more storeys (including lofts and cellars), occupied by at

least five people belonging to more than one family (ie, persons who are not related in any way). If these conditions are met, it is a criminal offence to manage a HMO without a licence. While this will not affect a standard London flat, it is possible for groups of friends to club together to hire out larger premises and so it is likely that there are listings which are caught, although this is particularly likely to affect larger premises outside the capital.

In addition to the risk of direct action by the local authority in the event of breach of planning rules, most leases will contain a clause requiring compliance with planning permissions and obliging the tenant not to use the property for any illegal purposes. Failure to observe these requirements will give the landlord grounds to forfeit the lease, possibly in combination with the other matters discussed above.

Concerns for a mortgagor—will your mortgage permit short-term rentals?

There are further potential threats to owners whose properties are subject to a mortgage. Although the wording of each mortgage must be checked carefully, it is highly likely that parting with occupation will be prohibited without the prior consent of the lender. This wording is designed to protect against underletting, which could complicate the situation for a lender seeking to enforce its charge should the undertenant assert a right to remain in the property. However, the restrictions will also catch short-term lets through short-term lodging platforms and permission will be required from a lender before the property can be used for hosting. While the approach of lenders will differ, it is likely that many will refuse or charge administrative fees to process applications, together with requiring a declaration by which the occupant acknowledges the rights of the lender. Lenders might also require the borrower to move to a higher rate mortgage to cover the additional risk. It is likely that these requirements will make use of lodging brokerages either impractical or too costly to interest the typical host.

Should properties be used for hosting without permission in breach of the terms of the mortgage then the lender could require immediate repayment and, in default, exercise their charge and require possession. Admittedly it is unlikely that, where mortgage payments are being made on time, lenders will proceed immediately to accelerate the mortgage. A more likely approach may be to issue a warning, reminding the borrower of the terms of the mortgage and the need to get permission if they want to use sites like Airbnb to provide lodgings in the future. Lenders might require the borrower to pay an administrative fee to cover the cost of the warning and also require the borrower to pay any fees associated with authorising and regularising future lettings.

In practice, it is likely that the majority of hosts simply do not inform the lender and hope to go undetected. To date, there do not appear to have been any re-possession associated with unauthorised use through Airbnb and the like and it does not seem that lenders are actively searching these brokerage portals to discover whether properties against which they have lent are being used for hosting.

Additionally, there are a growing number of providers offering specialist mortgages which envisage that the premises may be used for Airbnb and similar services although the interest rates on these products are substantially higher than the rates available for typical residential property mortgages.

To date, it seems that lenders are exercising customary caution in treating the provision of a short-term lodging as the equivalent of a normal underletting. Given that a standard listing is clearly not a tenancy, but instead a mere temporary licence to occupy, this caution may be misplaced. Should a guest overstay their welcome they would be trespassing and a lender would be able to obtain an expedited court hearing to secure their removal if it wished to enforce its charge. In these circumstances there would be no question of a lodging guests' interest in the property having priority over the lender.

It is likely that lenders will continue to adopt a cautious approach while there is any ambiguity as to the legal status of short-term lets. Should further clarity be provided by the courts or by regulation which makes it clear that short-term lodging does not confer property rights then lenders may adopt a more tolerant attitude which allows borrowers to host without paying bespoke interest rates or incurring additional charges. For the time being, it seems that concealment on the part of borrowers, and ambivalence on the part of lenders, will remain commonplace.

Insurance issues

What happens if the property is damaged by short-term guests?

Owners will rely on building insurance as their ultimate protection against catastrophic loss or damage. This will usually provide that, in the event of the property being destroyed by an insured risk (fire, flood etc), the insurer will pay the cost of reinstating the building. However, many leases provide that in the event that a building is destroyed or damaged owing to an act of default by the tenant then the tenant will be required to indemnify the landlord.

While policies of insurance need to be reviewed carefully, many will only provide cover if the premises are being used by private individuals as their permanent home. Looking at the situation with a block of flats and taking a worst case scenario, if the building burns down as a result of a short-term lodging, the host might lose his or her home and, if the insurer declines to pay out on the building insurance, they could find themselves liable to other leaseholders. Moreover, many leases will contain provisions which spell out that, where insurance monies are irrecoverable as a result of tenant default, the tenant will pay to the landlord the irrecoverable portion of the cost of reconstructing the building.

There are other, less extreme risks. For example, where a guest causes minor damage to the carpets or walls in the common parts and the landlord makes a claim. If the claim is declined, the tenant could be obliged to indemnify the landlord. If the short-term let was in breach of the terms of the lease then it is likely that the lease will contain provisions requiring the tenant to indemnify the landlord against increases in the insurance premiums.

Will brokerages provide any protection for damage?

In terms of the host's property itself, there are some protections provided by online brokerages. For instance, Airbnb's host guarantee reimburses damage caused by guests up to £600,000, but, importantly, this does not extend to shared or common areas and so would not protect against catastrophic damage to the building as a whole. In addition, the policy only applies to cover damage caused while the guests are in occupation. Therefore, as a short-term let in breach of the terms of insurance could invalidate the policy in its entirety, the lender could decline a claim which occurs after the guests have left and which is not directly and immediately arising out of their stay. Here, the host would not be able to rely on either the policy of insurance or the host guarantee (or equivalent coverage provided by other online brokers). It is also likely that use for the provision of lodgings may invalidate the host's contents insurance. It is also noteworthy that Airbnb's 'host guarantee' does not apply to cash and securities or personal liability (should a guest injure themselves or others) so not all losses will be covered. It may be possible to address this problem by seeking specialist insurance policies which are designed to cater for short-term lodger hosting.

Is any other insurance available?

Insurers have responded proactively to the new landscape by offering a range of insurance products to protect against the additional risks of property hosting. Currently the real risk to hosts is that they look only at their own property and do not consider the potentially catastrophic implications of invalidating the building insurance as a whole. Moving forward, tenants and landlords will need to work together to assess whether leaseholders are prepared to pay the higher premiums associated with obtaining building insurance against use for short-term lodging arrangements. This may be seen as adding insult to injury for those tenants who do not wish to host—not only will they have to put up with the inevitable disruption caused by guests, but they may also be asked to pay for the privilege. Potentially, this tension could be resolved by offering leases which permit short-lets but carry a requirement to make greater contributions to the service charge to cover the increased premiums.

Conclusion

The use of one's own residential accommodation to host lodgers via an online marketplace can be seen as a dynamic way to generate significant additional income. Consequently, many hosts will turn a blind eye to the risks. However, once this marketplace proves to be a permanent feature of our modern economy, regulators, landlords, insurers and lenders will need to recognise and accommodate it (and even share in its rewards). This article touches on the early responses from some stakeholders, but the development of real workable solutions will need to balance the interests of those engaged in the business, the efficient and flexible use of property and the effects on the wider community. Until then, prospective hosts need to arm themselves with a good understanding of their own particular legal positions (under their leases, mortgages and otherwise) before they walk into this exciting new marketplace.