

## Soon there will be no new holiday apartments!

...or so you might think, since the Secondary Residence Initiative was approved.  
Read this informational bulletin to find out more about the initiative's implications.

### Background:

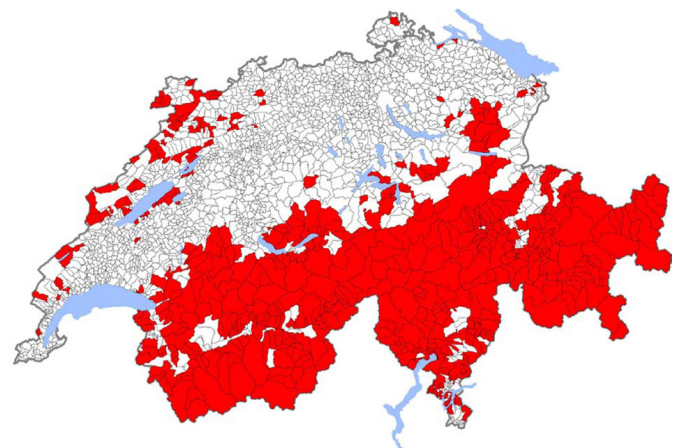
On March 11, 2012, the Swiss electorate passed a ballot initiative entitled "End the unlimited construction of secondary residences" and thereby resolved to put strict limits on the construction of such real estate. This initiative sets forth that the proportion of secondary homes to primary homes in any one municipality may not exceed 20%. As a consequence, this unleashed massive destabilization in the real estate markets of the affected communities, and a lot of contentious speculation about the impact of the initiative. The Ordinance, officially published in August, becomes valid and enforceable effective January 1, 2013 and helped put an end to many rumors, misgivings and much apprehension. The Ordinance is valid until the implementing legislation on the Secondary Residence Initiative takes effect – an effective date that may still be several years away. Among the affected communities – that is, municipalities with a secondary residence profile in excess of 20% – are virtually all tourist regions in the cantons of Bern, Graubünden, Ticino, Vaud and Valais.

### Transitional provisions / the Ordinance

Secondary residences may still be approved pursuant to existing law until 12/31/2012, which led to a striking glut in building permit applications in the tourism-based municipalities that will certainly persist until the end of the year. Effective January 1, 2013, building permits for the construction of secondary homes become void, pursuant to the Ordinance. Of course, exceptions have been grandfathered into the Ordinance; these are explained below in the section entitled "Building New Second Homes". What remains ambiguous is the handling of planning applications that were submitted prior to 12/31/2012, but were contested or have objections pending. Most likely the courts will have to rule on these cases.

### Building New Second Homes

Based on defined exception provisions, the ordinance will still allow for second homes to be built in the future. Thus, developers will still be permitted to construct managed secondary residences operated under a business plan similar to that of a hotel; the units must be offered under



In red, the municipalities in which presumably more than 20% of all apartments are secondary residences. Source: Federal Office for Spatial Planning

customary market terms and conditions, and cannot be individually furnished. Furthermore, secondary residences may be developed if the owner resides in the same building, the unit is likewise not individually furnished,



and its short-term use is offered to guests at customary market rates. The article envisions no minimum lease term, does not address the potential consequences of infringements or noncompliance, and does not specifically define “customary market terms and conditions.” Structures that characterize the landscape – like Alpine chalets or mountain pasture huts, etc., may continue to be converted into secondary residences while still complying with the spatial planning regulations. Conversion of hotel operations that already existed prior to the referendum on March 11, 2012 are likewise permitted if these prove to have a minimum operating term of 25 years. In addition, an independent appraisal must be available which establishes that the hotel business could not continue to be feasibly operated as such due to no fault of the owner.

## **Consequences for Primary and Secondary Residence Owners:**

The owners of secondary residences may also sell or bequeath their properties in the future as holiday residences. This still leaves the widely discussed ownership guarantee intact. Basically, nothing changes for owners of second homes. However, they will no longer be permitted to construct additions to existing living space. Primary residences that existed prior to the ballot, or that had been approved with legal force and effect, and that were not already subject to usage restrictions beforehand, are also free to be used, sold or bequeathed in the future. The conversion of primary residences into secondary, and vice versa, is permitted, subject to the pre-existing gross living space allocation. Municipalities are specifically charged with preventing any violations, i.e., misuse. Hence, replacement buildings – in other words, the sale of an existing secondary residence and the concurrent building of a new primary residence – is considered misuse. However, no sanction options were approved that benefit the municipalities.

### **Impact on the markets**

The ordinance will divide the real estate market in the tourism regions into three submarkets:

- 1) Market for any arbitrary, readily available secondary residences.
- 2) Market for managed secondary residences
- 3) Market for primary residences

Major price differences will soon be spotted among these three segments, since supply and demand evolve unequally.

### ■ **Secondary residences under old legislation**

The impending construction ban soon lead to a supply shortfall in the market for secondary residences with unrestricted usage, and thus drive prices upward.

At this point in time, it is doubtful when this supply shortfall will stop. Since the Ordinance does not take effect until 01/01/2013, applications were submitted – and approved, too – for numerous building permits.

Thus, we foresee a short-term oversupply of new units on the market, which might have a negative effect on price trends. More is being produced than the market can absorb. The total number of approved second homes depends on the zoning law for the respective municipality. Most municipalities have known about the curtailment of secondary residences for some time now. In these cases, open building permits are funneled through the planning office slowly, and thus will be issued over the next few years. In turn, the time it takes for that funnel to empty is influenced by local zoning codes. The municipalities use various time limits between the planning approval<sup>1)</sup> and the legally enforceable building permit<sup>1)</sup> (which is only issued when it is free of contingencies). For this reason, the construction boom may continue for another few years still, on a regional basis. As a rule, construction starts must commence no later than one year<sup>2)</sup> after issuance of the legally enforceable building permit.

This time limit exerts immense pressure on investors / developers, who would have to have sold some portion of the units in order to secure construction financing. Hence, distress sales under favorable terms cannot be precluded from this scenario.

### ■ **Managed secondary residences**

The market for managed secondary residences with mandatory lease-out has always been small, even until today, and in some regions it does not even exist. We can already see a price differential between “normal” and managed residences today, and will continue to do so in the future as well. We expect the market to become extremely dynamic. Managed property developments are typically major development

projects of between 30 to 100 units which could saturate markets in one fell swoop, and usher along a price collapse. However, if the demand in the market becomes rampant – for instance, if very few of these developments are realized – then prices tend to spiral upwards. Secondary residences subject to the terms of the old legislation equally have an influence on the pricing of managed residences. The more expensive and rare these become, the more attractive become the affordable residences with mandatory lease-up, which again causes a rise in demand. Forecasting here is exceedingly complex.

## ■ Primary residences

The prices of new first homes as well as of homes recorded in the Land Register might move to a markedly lower price level than those of second homes. Over the next few years, Credit Suisse anticipates not only a diminished price dynamic, but even price declines. The conversion of these homes will no longer be possible. This means that local demand will determine targeted prices, by buyers who have a substantially diminished

purchasing power. Even the price of development land will be determined by the demand for living space on the part of the domestic population over the next few years. The construction of managed secondary residences will not be able to compensate for the loss in demand for conventional secondary residences. This might lead to declining prices for development land.

1) These terms may differ from each other in the various zoning codes.

2) This time limit may differ in certain municipalities.

## Terms

### 1. Secondary residence:

“secondary residence” refers to residential units that are not used persistently by individuals domiciled in the municipality, or are used by individuals for acquisition or educational purposes.

### 2. Primary residence:

residential units that are consistently inhabited by local residents.

### 3. Managed residence:

residential units that are not individually furnished and that are run with a business operating plan similar to that of a hotel.

### 4. Quota on secondary residences:

Volume of secondary residences (typically in m<sup>2</sup>) that a municipality allocates each year and that are allowed to be constructed.

## Useful links/sources

Please click the symbol



**Ordinance on Secondary Residences**



**Explanatory information about the Secondary Residence Ordinance**



**Fact sheet on secondary residences**



**Fact sheet on the revised spatial planning law**



**Fact sheet on cantonal and municipal instruments**



**Fact sheet from Credit Suisse on Secondary Residence Initiative and its implementation**

## Final Word

Admittedly, the Ordinance provided some clarity once the voters passed the Secondary Residence Initiative – but it also left a lot of open issues. Each region must be looked at individually. But the demand for secondary residences in tourist destinations affects all of Switzerland. Many potential buyers are not stuck to specific regions. This is why – now as in the past – price trends in the various towns and valleys have correlated to each other, even if at different levels. The Secondary Residence Initiative will definitely be an influential part of the real estate pricing trend for second homes. What should not be underestimated – and nearly more important – are factors like the overall economic situation, the general prosperity, interest rates and the psychological expectations of the future. A holiday property is a luxury item, and it is only tolerated if the environment will permit.

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