Limits to the regulation of establishment of real estate through urban plans – the hotel sector and retail as examples

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Summary

Often, local governments regulate the establishment of new businesses in a local area. They want to prevent oversupply of certain goods or services. An important way to reach this objective, is by use of urban plans. The question this paper addresses is: to what extent is it legally allowed to regulate an economic sector by way of an urban plan? This question is relevant for many countries.
Two segments of the real estate market are selected to answer the research question: hotels and retail. In these segment, the problem seems most pressing.
This papers shows that only under specific conditions it is allowed that local governments restrict free competition through limiting the establishment of new businesses by way of their urban plan. It is assumed that in practice, often these conditions are violated.
The answer to the research question is relevant for prospective investors in real estate, in particular hotels and retail, in EU countries.

Keywords

Urban plans; limitation of new businesses; restriction of competition; Services directive; hotel sector; retail sector

1. Introduction

In many countries, local governments feel the need to regulate the supply of a certain segment of the real estate sector in a defined geographical area. Usually, their main objective is to prevent the oversupply of certain goods or services in a specific area. As a consequence, the existing suppliers receive (economic) protection, in the form of limitation of competition. Such practices are at odds with the principle of freedom of establishment – a cornerstone of the European Union. As Korthals Altes puts it: 'It is this principle of freedom of establishment that may affect retail planning policies which lend themselves to interpretation as a set of administrative procedures and practices that place constraints on the establishment of new retail complexes outside current town centres'.[2]

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[2] W.K. Korthals Altes, Freedom of establishment versus retail planning: The European case. *European Planning Studies*, 2016, Vol. 24, no. 1, p. 163-180.

Several EU membership states are known to have had regulations that restricted the access to the market for new retailers.[3] In this paper, both the hotel and retail sector are taken as examples of real estate sectors for which regulation of supply often occurs in practice.

An important way for local governments to regulate the establishment of real estate is through (legally binding) urban plans. For example, the local urban plan limits the accession of new hotels or retail to a certain number, percentage or other unit in a distinct geographical area. Under such circumstances, new business locations of hotels and retail are tested against the urban plan in the framework of a permit procedure.

This paper addresses the question to what extent such practices are permitted. Is it legally allowed to regulate an economic sector, like hotels or retail, by way of an urban plan? In other words, under which conditions is it allowed to restrict the maximum number of activities of a specific economic sector in an urban plan and thereby limit competition between suppliers? In this paper, the regulatory framework of the Netherlands will be taken to answer the research question. However, the answers to this question are relevant for many countries. In particular, the answers are of relevance to prospective investors in real estate in EU countries.

The topic of this paper is largely covered by EU law. Therefore, conclusions for the Netherlands in principle also apply to other EU-membership states.

2. Permit procedures for new businesses

The control of the establishment of new businesses, like hotels and retail, runs via a permit procedure. Every developed country has a permit procedure, in which the application for the construction of a building is tested against an urban plan.

2.1 Legally binding instruments

In the Netherlands new hotels and retail need an *environmental permit for a building project* (Dutch: omgevingsvergunning voor een bouwproject) (art. 2.1, para. 1, Environmental Licensing Act). Applications for environmental permits for a building project are tested against the local land-use plan (art. 2.10, para. 1, under c, Environmental Licensing Act).[4] Hence, stimulating tourism and retail can take place by including much space for hotels and retail in local land-use plans. Conversely, control of tourism can take place by limiting the space for hotels and retail in land-use plans.

Apart from municipalities, in the Netherlands, provinces have legal power to control or stimulate hotels and retail. Both economic sectors can be ingredients of provincial *general rules*.[5] They are laid down in the legal form of a provincial bye-law. These rules are primarily directed towards municipal governments. This is stipulated in article 4.1 Spatial Planning Act:

> *If necessitated by provincial interests in order to achieve proper spatial planning, rules regarding the content of local land-use plans (…) may be issued by or by virtue of provincial bye-law.*

[3] In his paper, Korthals Altes (see footnote 2) gives examples from Spain, France, Poland, Portugal and Germany.
[4] For a full description of the assessment framework for environmental permits for a building project see F.A.M. Hobma and P. Jong, *Planning and Development Law in the Netherlands*, IBR, The Hague ,2016, p. 38.
[5] See F.A.M. Hobma and P. Jong 2016, p. 68.

The wording of this article shows that provinces can only include rules regarding tourism or retail (or any other spatial relevant theme for that matter) in this bye-law if it is necessitated by provincial interests. So, the interests must be overriding the local scale.

2.2 Extra-legal instruments

Apart from legal instruments municipalities may deploy extra-legal instruments to control or stimulate tourism or retail. Examples are (a) a regional hotel strategy or retail strategy for a certain region, (b) a hotel ladder and (c) a hotel monitor. Typically, these instruments monitor the growth of hotels or beds or retail in a city and express a policy to control the number of hotels or beds or (a certain type of) retail in certain areas of a city.

2.3 Additional obligations for establishment of new services?

One could wonder, is it possible to impose additional obligations to initiators of establishment of new services (like hotels), to the effect that only after implementing the additional obligations the new services can be established? Additional here means: additional to the standard requirements an applicant of a building permit needs to meet. The additional measures serve as a kind of extra requirement that needs to be fulfilled because of certain negative effects of the new facility.

Additional obligations may relate to contribution to a fund for the construction of affordable housing. Another example of a possible additional obligation is that permission for a new hotel or retail is given once the hotel owner agrees to upgrade another existing hotel in the city (for example, from a 2 star hotel to a 3 star hotel).

In the Netherlands, under public law, this type of additional obligations are not admissible. Dutch law *does* allow for private law agreements between municipality and developers. However these agreements relate to the recovery of municipal costs of public infrastructure (what is generally known as 'development contributions').[6]

3. Restriction of competition through urban plans

In the Netherlands, the local *land-use plan* (Dutch: bestemmingsplan) is the urban plan which holds binding regulations regarding land-use and building plans.[7] Tourism and retail may be two of the sectors regulated in the land-use plan by way of land-use objectives such as 'hotels' or 'retail'. Land-use plans are an instrument of spatial planning and not an instrument of economic planning. Economic planning includes a restriction of competition. The act stipulates that land-use plans hold rules 'in the interest of proper spatial planning' (art. 3.1, para. 1, Spatial Planning Act).[8] Spatial planning is not the same as economic planning.

In fact, it is *not* allowed to use the land-use plan for economic planning, *in casu* restriction of competition. Two articles of the Spatial Planning Decree (Dutch: Besluit ruimtelijke ordening) are of relevance here.

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[6] Hobma and Jong 2016, p. 48.
[7] In the context of the questions of this paper, the local *management regulation* (Dutch: beheersverordening) is not very relevant and therefore will not be discussed.
[8] Hobma and Jong 2016, p. 54.

Article 3.1.2, para. 2, Spatial Planning Decree reads:

> *For the purpose of a proper spatial planning, a land-use plan may hold rules*
> *(a) (…);*
> *(b) with regard to branches of retail and hotel and catering industry.*

This article, in itself, may lead to the false conclusion that a land-use plan may include economic planning. However, it follows from article 1.1.2 Spatial Planning Decree that it is not allowed to use land-use plans for economic planning:

> *In setting rules for a land-use plan (…), or a decision regarding an application for an environmental permit for deviation from a land-use plan (…) conflict needs to be prevented with article 14 (…) of the Services Directive (Directive 2006/123/EC) of the European Parliament and Council of the European Union of 12 December 2006 regarding services in the internal market (PbEU L 376). (…)*

Accommodation and food services such as hotels, restaurants and caterers are covered by the directive.[9] For retail, it is not certain if it is covered by the Services Directive. The Court of Justice of the European Union in Luxemburg is asked by the Dutch administrative judge (the Administrative Jurisdiction division of the Council of State) – in the so called Appingedam case – an explanation if the Services Directive applies to retail in Dutch land-use plans.[10, 11]

Irrespective of that, the rules of land-use plans need to be in conformity with the Services Directive. The Services Directive is enforced by national member states and by the European Commission. If a member state (including a municipal body as part of the member state) violates the Services Directive, the European Commission has enforcement powers. It can file a complaint to a member state in an unofficial procedure. Also, the European Commission has the power to start infringement procedures against a member state if the Commission is of the opinion that the member state does not comply with EU law. This could lead to an order by the European Court of Justice to put things right (or a fine).

4. The EU Services Directive

The interesting question now is: to what extent does the Services Directive impose restrictions on the regulation of hotels in land-use plans? Similarly, to what extent does the Services Directive impose restrictions on the regulation of retail in land-use plans?[12] This question, in essence, is a question regarding the limits between spatial planning and economic planning. In other words: when is regulation of tourism (hotels) and retail in land-use plans still spatial planning – and thus allowed and

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[9] European Commission, *Quick Guide to the Services Directive*, https://ec.europa.eu/growth/single-market/services/services-directive/in-practice/quick-guide_nl.

[10] Afdeling bestuursrechtspraak Raad van State (Administrative Jurisdiction division of the Council of State), 13 januari 2016, ECLI:NL:RVS:2016:75.

[11] Recently, on 18 May 2017, attorney general Szpunar (Court of Justice of the European Union) concluded in his opinion addressed to the court that retail in terms of selling goods to consumers indeed must be seen as 'service' in the framework of the Services Directive. See CJ, 18-05-2017, nr. C-360/15, nr. C-31/16. For a full text of the attorney general's opinion see http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:62015CC0360. The court has yet to decide.

[12] This question is relevant should the Court of Justice rule that retail must be seen as 'service' in the framework of the Services Directive.

when is regulation of tourism (hotels) and retail in land-use plans economic planning (restriction of competition) – and therefore in principle not allowed.

In answering these questions, in this paper reference is frequently made to the following report: *Vesting van detailhandel: de toepassing van de verdragsvrijheden van het VWEU en de toepassing van de dienstenrichtlijn* (VU Amsterdam, 2015).[13] The English translation of the report would be: *Establishment of retail: the application of the Treaty freedoms of the Treaty of the Functioning of the European Union and the application of the Services Directive*.

The report discusses the establishment of retail in the framework of the Treaty of the Functioning of the European Union and the Services Directive. Authors explain (p. 13) that if a national regulation falls within the scope of the Services Directive, the regulations must be tested against the Service Directive and not against article 49 of the Treaty. Now that hotels (for certain) fall within the scope of the Service Directive, we will focus on this directive. Actually, Heutink argues that it doesn't make much difference if national regulations are tested against the directive or the treaty, now that the rules of the directive find their origin and cause in the fundamental rights of the treaty – amongst which the freedom of establishment of article 49 Treaty of the Functioning of the European Union.[14]

The answer to the question – to what extent does the Services Directive impose restrictions on the regulation of establishment of real estate sectors in land-use plans? – follows from *five steps* which are discussed below.

(1) Conditions under which a State can make access to a service activity subject of an authorisation scheme

Article 9 Services Directive stipulates the conditions under which a State can make access to a service activity subject of an authorisation scheme. (Regulation of hotels and retail by an urban plan can be seen as being subject of an authorisation scheme.)

a) the authorisation scheme does not discriminate against the provider in question. (This means that the scheme does not make differences between nationalities);
b) the need for an authorisation scheme is justified by an overriding reason relating to the public interest;
c) the objective pursued cannot be attained by means of a less restrictive measure, in particular because an a posteriori inspection would take place too late to be genuinely effective.

(2) Criteria for authorisation schemes

Article 10, para. 2 lists the criteria for authorisation schemes. The criteria shall be:

(a) non-discriminatory;
(b) justified by an overriding reason relating to the public interest;
(c) proportionate to that public interest objective;
(d) clear and unambiguous;
(e) objective;

[13] E. Steyger, J. Struiksma and M.R. Botman, *Vesting van detailhandel: de toepassing van de verdragsvrijheden van het VWEU en de toepassing van de dienstenrichtlijn,* VU Amsterdam, 2015.
[14] G.H.J. Heutink, Het VU-rapport over de vestiging van detailhandel en verdragsvrijheden: beschouwing en opinie. *Tijdschrift voor Omgevingsrecht*, oktober 2015, nr. 3.

(f) made public in advance;
(g) transparent and accessible.

The criteria limit the free power of the competent authorities, so that permission is not granted arbitrary.

(3) Economic tests

Article 14, para. 5 Services Directive is relevant, now that in many countries investments are made subject to an 'economic test'. The outcome of this test determines whether or not permission is granted for the establishment of a new business.

Article 14, introduction and para. 5 reads:

> *Member States shall not make access to, or the exercise of, a service activity in their territory subject to compliance with any of the following:*
>
> *the case-by-case application of an economic test making the granting of authorisation subject to proof of the existence of an economic need or market demand, an assessment of the potential or current economic effects of the activity or an assessment of the appropriateness of the activity in relation to the economic planning objectives set by the competent authority; this prohibition shall not concern planning requirements which do not pursue economic aims but serve overriding reasons relating to the public interest.*

Steyger, Struiksma and Botman argue that the mere fact that establishment of a new business may lead to bankruptcy or diminished turnover of a competitor, is not a reason to deny the establishment of a new business.[15]

The last part article 14, para. 5 is of particular interest: *planning requirements which do not pursue economic aims but serve overriding reasons relating to the public interest* are allowed. Steyger, Struiksma and Botman explain that 'overriding reasons relating to the public interest' include the protection of the urban environment. Such planning regulations are allowed, under the condition that they are proportional[16].

(4) Lasting disruption of the quality of services

Dutch jurisprudence in spatial planning cases follows the elements of the Services Directive mentioned above. Steyger, Struiksma en Botman made an analysis of rulings of the Administrative Jurisdiction Division of the Council of State (Dutch: Afdeling bestuursrechtspraak van de Raad van State). Their conclusion from case law is as follows[17]:

- The Spatial Planning Act does not protect businesses against establishment of competitors in their service area.

[15] E. Steyger, J. Struiksma and M.R. Botman, *Vesting van detailhandel: de toepassing van de verdragsvrijheden van het VWEU en de toepassing van de dienstenrichtlijn* (VU Amsterdam, 2015), p. 31.
[16] Steyger, Struiksma and Botman, 2015, p. 31.
[17] Steyger, Struiksma en Botman 2015, p. 48.

- In spatial planning, competition between businesses is not an interest that is taken into account, unless a lasting disruption of the quality of services will occur, which is not justified by compelling reasons.
- The council has ruled that for 'lasting disruption of the quality of services' it is decisive whether the inhabitants of an area cannot meet their needs of *primary necessities of life* within an acceptable distance of their houses.

In the context of quality of services, 'primary necessities of life' likely refer to food, drinks and clothes.

(5) Retail planning research

In the Netherlands, often retail planning research (Dutch: distributieplanologisch onderzoek) takes place prior to taking governmental planning decisions. The research is performed by specialised consultancy firms. In such research, the need, the feasibility and the effects of the possible establishment of a new business is examined. In the framework of spatial planning, the results of the research may only be used to make an inventory of the *spatial effects* of the establishment of new businesses. The report cannot be used for economic planning; they can be used for spatial planning.

6. Conclusions

It is plausible that hotels are not seen as services which provide *needs of primary necessities.* In section 4 above ('Lasting disruption of the quality of services') it was explained:

(a) that in spatial planning, competition between businesses is not an interest that is taken into account, unless a lasting disruption of the quality of services will occur, which is not justified by compelling reasons;
(b) that the Council of State has ruled that for 'lasting disruption of the quality of services' it is decisive whether the inhabitants of an area cannot meet their needs of *primary necessities of life* within an acceptable distance of their houses.

Hence, hotels cannot be seen as a 'primary necessity of life'. Specific retail, however, will qualify as 'primary necessity of life': retail that deals with food, drinks and cloths.

Consequently, Dutch law does not allow a regulation of competition between hotels in local land-use plans. However, pursuant 'overriding reasons relating to the public interest' (art. 14, para. 5, Services Directive) planning regulations regarding hotels are allowed, provided they are proportional. *Spatial planning motives* to regulate establishment of hotels may, for example, have to do with:

a) prevention of vacancy of hotels to avoid deterioration, which in its turn leads to devaluation of a specific urban environment;
b) limitation of noise hindrance from hotels in a certain area;
c) prevention of traffic nuisance which would occur as a consequence of a new hotel in a certain area.

We can now answer the following questions: *Under which conditions is setting up a maximum number of activities of a specific economic sector admissible? Would a criteria of maximum density be admissible?*

The answers to these questions is that setting up (1) a maximum number of activities of a specific economic sector or (2) using criteria of maximum density or (3) a maximum of square meters for a certain type of business, are only admissible insofar as spatial planning motives are used as a foundation of the planning regulations.[18]

In this respect, Steyger, Struiksma en Botman make an important observation: mapping the economic effects from the viewpoint of 'a proper spatial planning' and mapping the economic effects per se, are very close.[19] So, there is a thin line between both. This makes it difficult to clearly assess upfront whether a regulation is motivated by economic purposes or planning purposes. However, for initiators of new hotels and retail, it is vitally important that local authorities only use the outcomes of economic tests like retail planning research for 'planning requirements which do not pursue economic aims' (art. 14, para. 5, Services Directive). It is very difficult for an investor to assess upfront whether planning requirements indeed do not pursue economic aims. Looking at the amount of jurisprudence – not only in the Netherlands, but in other EU countries as well – we can assume that many local authorities do not use economic tests in a legally correct manner. This is an important point of attention for planners and their advisors. They should be aware of the fact that that only under specific conditions it is allowed that local governments restrict free competition through limiting the establishment of new businesses by way of their urban plan. This paper has indicated the outline of these conditions. Hotel and retail planning is not forbidden, but must proceed within clearly defined boundaries.

Finally, the conclusions of this paper are not only relevant for planners and their advisors, but for local governments too. Local government should prevent claims for compensation for loss resulting from unlawful administrative acts, *in casu* adoption of a land-use plan against the law.

[18] As described above, this is different if we are dealing with businesses occupied with 'primary necessities of life' like supermarkets. Hence, there is more room for local authorities to regulate retail supermarkets in their local urban plans. In their urban plan, local authorities are allowed to take competition between providers of primary necessities of life into account if inhabitant's access to such necessities is not within acceptable distance.

[19] Steyger, Struiksma en Botman 2015, p. 85.