

An Examination of the Standard Rent System for its Suitability as a Solution to Korean Rental Housing Market

Hyewon. Kim, Kabsung. Kim, Jihye. Han

Abstract— In recent years, Chonseil prices are soaring at the housing market of Korea. Thus, Chonseil is changing into monthly payment, which gives an extreme financial burden on the tenant to housing. The city of Seoul decided to start presenting ‘a standard rent’ by residential location and housing types next year in order to indicate fair housing rental prices to tenants who wear damage due to lack of information and to provide house owners the standard for housing rental prices. The standard rent is planned to be guidelines for future housing rental prices of private rental housings. Accordingly, it is important to calculate the standard rent suitable for Korea. This study analyzes the methods to calculate the fair rent of England, the fair market rent(FMR) of USA, Germany and France and also attempts to know which type of fair rent or standard rent for housing is appropriate for Korean situation.

Keywords—Fair Market Rent, Housing Rental Price, Housing Stabilization, Standard Rent

I. INTRODUCTION

HOUSING is a basic right for human life of a citizen but it has been left to the market without any institutional protection. Also, the percentage of public housing to the total housing stock is 5%, which is very low, so Korean government has no way to ensure publicity of housing. In addition, the housing market of Korea in recent years has severe financial burden on housing to the tenants. Chonseil prices are soaring and payment of many housings is turning from Chonseil into monthly rent, which burdens tenants because of slow economic growth and job insecurity although government attempts to solve housing problems by many ways including providing more public housing.

According to the Korea Appraisal Board, Chonseil price for housing of Seoul went up rapidly than that of average Korea. Also, the rapid conversion from Chonseil to monthly rent led the households whose incomes are at the bottom 20 percent in Seoul to pay 33 percent of their income as a rent every month while many experts say Rental income ratio(RIR) should be managed by less than 30 percent[3].

Hyewon. Kim is with the Dept. of Urban Engineering, Yonsei University, Seoul, Korea. (phone: 82-10-4767-0497; fax: 82-2-393-6298; e-mail: kimhw210@gmail.com).

Kabsung Kim, is with University of Pennsylvania, PA USA. He is now with the Department of Urban Engineering, Yonsei University, Seoul, Korea as a professor. (e-mail: kabsung@yonsei.ac.kr).

Jihye. Han, is with the Dept. of Urban Engineering, Yonsei University, Seoul, Korea. (e-mail: jiny574@naver.com).

The city of Seoul proposes a standard rent by the region and the type of housing and plans to utilize the standard rent as future guidelines in private housing rentals from next year in order to offer appropriate rental prices to tenants who are suffering from incorrect statistics of housing market prices. House rentals are determined by various factors such as region, type of housing, contracts, mortgages settings, so fixed rent method is difficult to apply in reality. Thus, it is important to calculate the standard rent that meets the situation of Seoul and Korea.

This study analyzes and compares the fair or standard rent system of England, USA, Germany and France so that which part of those systems is appropriate for Korean housing market.

II. THEORETICAL BACKGROUND

A. The Concept of Fair or Standard Rent

Fair or standard rent scheme is a system to adjust the rent of the lease renewal on the assumption that the lease is retained. A fair rent system is different from the controlled rent scheme. The basic principle of the fair rent system is to prescribe the rental with agreement between tenants and landlords. If tenants and landlords could not find the rent with agreement of both sides, the fair rent is determined through an administrative dispute resolution procedures of the Rent Adjustment Commission and Rental Trial Court’s judgement. Thus, the operation is closely connected with the dispute settlement system of rentals.

A fair rent system is accompanied by rent increase rate ceiling to stabilize residence since tenants have no choice but to move to another region if the determined rent rises more than the tenant’s economic capacity[8].

A fair rent means an appropriate rental price that landlords are able to get when a similar type of housing in the region is in the equilibrium of demand and supply. It effectively refers to the maximum rent that the landlord may require[6].

B. Literature Review

Seoul Development Institute(2012)[11] defined ‘a fair rent’ to a rent of private cooperative public housing as a meaning of affordable rent and examined the dimensions of the international fair rent system to define the criteria for fair rents in Seoul. Also, it proposed a fair rent calculation method by analyzing the living situation and market rent of a detached, multi-household and multiplex private rental housing that is subject of private cooperative public housing.

Ministry of Land, Infrastructure and Transport(2012)[5] examined whether the introduction of a standard rent is desirable and specific method if it is desirable to introduce a standard rent to South Korea by analyzing introduction background, key issues, effects and side effects of main housing welfare policies such as rent regulation, housing vouchers, public rental supply. It focuses on three policy measures; tenant protection systems, rent supplements such as housing vouchers, and construction and operation of public rental housing.

TABLE I
UNITS FOR MAGNETIC PROPERTIES

	Seoul Development Institute(2012)[11]	Ministry of Land, Infrastructure and Transport (2012)[5]	Kim (2015)[8]
Countries	England, USA, Germany, Japan	England, France, USA, Canada, Germany, Japan	Germany, France, England, USA, Japan
Study details and results	To examine international fair rent systems to define criteria for fair rents of Seoul To propose methods to calculate fair rents by analyzing the living situation and market rent by types of private rental housing	To analyze backgrounds for introduction, key issues, effects and side effects of main housing welfare policies To examine whether the introduction of a standard rent is desirable and what is the best method to introduce a standard rent to Korea	To examine transition of the rent regulation system and international cases of standard rent systems To propose introduction methods of standard rent system to Korea

Prior researches including these three studies mostly attempted to apply standard or fair rent system to public housing policy and housing welfare policy of Korea by analyzing international cases of standard and fair rent system of rental housing. However, what Seoul tried to do by a standard rent is to open Chonse prices and monthly rents of standard housing by the type of housing, scale and location to the public and the target is not limited only to rental housing. Therefore, this study attempts to get the implications to estimate the standard rent of Chonse and monthly rent housing market of Korea.

III. CASE STUDIES

Generally, a fair rent means an affordable rent but there is little difference between names and ranges by country. This chapter will have a look on fair rent systems or standard rent systems of four countries that are frequently examined by prior researches and have a significant meaning on the housing market of Korea: England, USA, Germany and France.

A. England

1) Background

Lease system of England can be divided into three stages depending on the time period: the rent control period, the rent regulation period, and the deregulation period[1].

Government of the United Kingdom strongly controlled rental prices after wars in order to reflect the needs of public for low rental prices and to stabilize instable market due to housing

shortage. The government had been continuously regulated rental prices from rent control policy between 1915 and 1960. However, strong regulation caused the problem of housing supply shortage and poor quality of regulated housing. Thus, the fair rent system is introduced in order to adjust the skyrocketing rental prices in 1965.

2) Purpose

Rent Act 1965 introduced a fair rent that rent officers estimated and ensured lease periods for tenants in order to balance between landlords and tenants. For tenants, the fair rent system of England prevents instable housing and rapid increase of rental prices. Also for landlords, it ensures a certain profit through the rental housing.

3) Calculation Method

A fair rent is determined by rent officers considering years elapsed from construction, characteristics, location, quality of maintenance, the number and status of furniture, utility fees such as heating and hot water of the housing. However, these following things are not included: personal circumstance of tenants or landlords, the value of rarity of housing due to supply shortage of similar types of housing, damages that tenants are responsible for.

4) Renewal and Rise limit

The fair rent of England is renewed every 2 years by rent officers and is open to the public by region and housing type. In addition, new lease law revised in 1999 applies the Maximum Fair Rent to regulate increase rate when a fair rent is reregistered. This is affected from the existing fair rent system that led rental prices to skyrocket in the past.

5) Meaning

For now, the fair rent is used for appropriate rent price to calculate Housing Benefit (HB) subsidy. Also, after 2008 Local Housing Allowance (LHA) was introduced and LHA is determined not by housing characteristics but by 30th percentile by region and the number of bedrooms. This method using percentile is more advantageous than fair rent in that it reduces time and cost.

B. USA

1) Background

It was not until 1982 when the US Congress created a committee to investigate slum areas in cities that US Congress is concerned with low-income housing. Housing assistance for the low-income group had been passive and insignificant until 1930 [4]. However, public housing program was completely changed by Housing Act of 1937, and Regional Housing Authorities performed public housing business according to this act.

Section 8 Housing Voucher Program of Housing Act is the key for low-income rental housing assistance program and makes it possible for residents to select areas and houses that they want to live by themselves. Section 8 decides Fair Market Rent and Housing Voucher Program, and bridges the gap between the standard rent by Fair Market Rent(FMR) and 30% of income of the household. Therefore, households could have a wide range of choice sets since they are able to rent houses which are more expensive than their incomes.

2) Purpose

Section 8 of the USHA authorizes housing assistance to aid lower-income families in renting safe and decent housing[2].

FMR stabilizes residence and improves housing environment for the lower-income group.

3) Calculation Method

FMR is set with 40 percentile or 50 percentile of regional rental prices for standard-quality rental housing of each FMR region that moved in past 15 months by the number of bed rooms. In addition, FMR is the rent as a comprehensive concept. It includes the rent of the house itself and utilities (water, electricity, gas, etc.) but telephone, satellite TV and Internet access fee are not included. FMR is various depending on whether the house belongs to the area of geographical factors, the size of homes and whether homeowners or participating households pay utility[12]. However, public rental housings and houses whose residential construction year is less than two years are excluded.

4) Renewal and Rise limit

Department of Housing and Urban Development(HUD) annually publishes FMR. HUD annually reflect Consumer Price Index(CPI) into rents and utilities of 530 metropolitan areas and 2,045 nonmetropolitan county areas and trend FMRs forward to the mid-point of use period[9]. At this time, rents and utilities are updated utilizing CPI data for areas that have CPI index but HUD Regional RDD Gross Rent Factor is applied for areas that do not have CPI index.

5) Meaning

FMRs are primarily used to determine payment standard amounts for the Housing Choice Voucher program, to determine initial renewal rents for some expiring project-based Section 8 contracts, to determine initial rents for housing assistance payment (HAP) contracts in the Moderate Rehabilitation Single Room Occupancy program (Mod Rehab), and to serve as a rent ceiling in the HOME rental assistance program.

C. Germany

1) Background

Germany, unlike other European countries, has been pushing private sector-led housing policies that private capital markets and private developers lead housing supply since 1960. Private rental housing basically respects an agreement between the parties about deciding and raising rents but the German Government enforces a strong regulatory policies because the share of the private rental market is relatively large.

Rent control in Germany started from freezing rents of housing that is built before 1917 with the level of 1914 or before by the National Rental Housing Act(1992). This lasted until the Allied occupation(1945-1949) through the Nazi Germany. Rent regulation was implemented through a “protected residential lease contract law(for promotion law enacted in 1971)” and a “rent increase regulations” but the unification of the regulatory framework was made since rent regulation is incorporated in 2001 as the “German Civil Code”.

2) Purpose

Comparative rent scheme in Germany is applied to the general housing rather than social housing. The comparative rent scheme aims to prevent excessive rent increases by making the rent hike similar to the market rent hike and to provide a legal status for a rent increase.

The Rent Standard Table(Mietspiegel) formulates the upper and lower limits for rent with cooperation of public and private and provides an average residential housing rental prices by residential levels to both the landlord and tenant groups. Tenants could assess the fair value of the rent with this table.

3) Calculation Method

Housing rents in Germany is estimated for free at the first time according to the system of rent stabilization policies but housing rents could be raised when there is no variation in the rent for 15 months in accordance with comparative rents(Ortsübliche Vergleichsmiete).

Comparative rent is calculated by municipalities based on rental prices of past four years by types, scales, facilities, location and status of housing.

Rent standard table plays a role of the basis of comparative rents and it is filled with from 2/3 to 3/4 of regional rents with cooperation of tenant and landlord representatives and the local government. At this time, housing status is divided by a residential area, the area of housing, a building year and the presence of bathroom and central heating.

Through the process of creating the rent standard table, the landlord and tenant groups mutually agree and municipalities coordinate to share thoughts about whether the fair rent prices are appropriate with a role of coordinator.

4) Renewal and Rise limit

The rent standard table is renewed every two years. In order to raise the rent, the household should provide the rent standard table, the data of rent information bank, expert appraisal, and at least three rents of similar types housing as evidence. Also, it is not possible to raise the rent of the house beyond the comparative rent, the rent is able to get raised after one year once it is set, and the rent cannot be raised over 20 percent for three years.

5) Meaning

Comparative rents and the rent standard table functions as a guideline for rent adjustment and certain rent increase. Also, the rent standard table is created through mutual agreement so it is highly reliable in that there is only few legal disputes regarding housing rents.

D. France

1) Background

In France, rent control went into effect after the outbreak of the First World War as a temporary emergency measure but the rent control policy reduced the motivation for investment in rental housing and occurred problems such as neglected maintenance and repair of the existing houses. Thus, the French Government introduced a Housing Allowance System in 1948 to promote investment in the housing sector and ease rent controls.

Since the late 1950s, a large supply of a lease type social housing, or public rental housing, is promoted in earnest. In the 1970s when the absolute lack of housing was solved, the national economy was damaged because of oil shocks and other economic circumstances. Eventually, the French government carried out a reform in 1977 and focused on rental assistance rather than supply-oriented housing policy. The rents that are first registered were defined freely by the parties at the first time

but since the ruling of Socialist regime a new legislation has also regulated the initial rents.

2) Purpose

To introduce IRL(Rent Reference Index) for adjusting rents links the increase level of rents with an objective index. Introducing IRL reflects the inflation rate, so reduces risks of volatility and makes it possible to keep increase rate of rents lower in case of inflation. Disputes relating to the lease is prevented and the landlord may consider the economic benefits thanks to IRL.

3) Calculation Method

Rents can be divided into two types; one is set when moving in for the first time and the other is adjusted after moving in.

The initial rent of public rental housing(HLM) is determined in consideration of the financing methods and costs applied to the supply of HLM with the cap set by regulation rather than the local non-regulated market environment. The initial rents are determined by taking into account technical characteristics such as price, operating funds and the landlord's administrative status by the balanced rent method. At this time, the rent cannot exceed the maximum rent by rule. That is, in theory, the landlord can raise the rent freely if it is lower than the maximum rent by rule but, in reality, most of the rentals have been formulated in conjunction with the maximum value from the beginning. Thus, rents are adjusted linked with IRL[5].

If households want to raise the rent after moving in to the same tenant, rents are set on the basis of the IRL. IRL is calculated by adding Customer Price Index(CPI, excluding rents and tobacco) 60% and ICC(Construction Costs Index) 20% to IPEA(Index of the cost of maintenance and renovation works) 20%.

4) Renewal and Rise limit

The National Institute of Statistics and Economic Studies(INSEE) announces quarterly statistics of IRL. Housing rentals can be revised annually by the lead of the landlord on the day indicated in the lease agreement or on the day of one year after the contract. Maximum rent is annually adjusted based on IRL Index so the rent markups due to renewal of rents cannot exceed the IRL.

5) Meaning

The balanced rent method and the maximum rent are used to set the initial rent. In addition, IRL Index adjusts the maximum rent if the rent is updated.

IV. COMPARATIVE ANALYSIS

A. Case Summary and Comparison

The calculation methods for fair rents vary substantially from applying 40 or 50 percentile by standard-quality rental housing to setting criteria based on the market rent and supply costs to calculating considering characteristics of the house.

In Anglo-American countries, fair rent is calculated by considering the characteristics and quality of housing at the first time but the method is simplified in a way to set 30~50 percentile of local market rents in order to reduce time and cost for calculating and to consider regional market environment. Thus, the fair rent system is changing into a way based on market rents rather than estimating the fair rent additionally, and also, into a way to lessen burden for rents with housing or construction cost assistance and tax benefits.

TABLE II
CASE SUMMARY AND COMPARISON

	England	USA	Germany	France
Name of System	Fair Rent	Fair Market Rent (FMR)	Comparative Rent (Ortsübliche Vergleichsmiete)	The Balanced Rent Method And IRL
Calculating Method	Rent officers determine the fair rent considering years elapsed from construction, characteristics, location, quality of maintenance, the number and status of furniture, utility fees	40 or 50 percentile of the local market rent for the standard-quality rental housing of each region	Municipalities calculate the comparative rent based on rental prices of past four years by types, scales, facilities, location and status of housing	The initial rent is determined between the balanced rent that is calculated in consideration of price, operating funds and the landlord's administrative status and the maximum rent The maximum rent is adjusted by IRL Index
Renewal Frequency	Every 2 years	Annually	Every 2 years	Annually
Limits on Rent Increase	Linked with CPI	Linked with CPI	The rent cannot be raised over 20% for 3 years	Linked with IRL (CPI 60% + ICC 20% + IPEA 20%)
Meaning	Used to calculate rent assistance	Used to determine Housing Benefits	A role of guideline to adjust rents	Used to determine the initial rent and adjust the maximum rent

B. Implications for Housing Market of Korea

1) Expected Effects

If the standard rent is introduced to Korean rental housing market, the tenants will be able to enjoy more financially stable life. To this day, they have had no choice but to pay the rental fee beyond the fair rents because of insufficient information

provided. This causes unstable residential real estate market and increase in Chonseil prices which lead to aggravate housing cost burden of the working classes. However, it is possible to get enough information about appropriate level of the rental price if the standard rent is presented in the rental housing market. Also, the cap system that will be applied with the standard rent is expected to lessen burden of housing cost. It represents much to

formation and maintenance of local community because the occasion of residents' moving out of the region due to increasing housing cost will grow down. Finally, it may be said that decline in proportion of housing cost to household income will contribute to encouraging consumer spending and, furthermore, economic stabilization and development.

2) Risks and Challenges for Introducing

First, it is essential to build base data to calculate the standard rent. The statistics such as how much is the monthly rent and the conversion rate for Chonsei-to-Monthly Rent are now need to be gathered and organized. This would take a great deal of time considering the present condition of related infrastructure. What have to be done first is to make the registration of contracted rental price mandatory in order to understand the current situation since the rental price comes in a broad range depending on the type, location and size of housing.

Second, it is necessary to accompany cap system with the standard rent and to establish detailed criteria for the standard rent and the cap. If a markup on rental price is way too high so that tenants cannot afford, they cannot help but moving into the region with lower rental price. Considering that the purpose of the standard rent is to support long-term lease for resident stability, this requirement is essential.

Third, the objectivity of the procedure should be ensured for the settlement of the standard rent. If the rental housing market recognizes the standard rent as a regulation and the consumers have no confidence in the price itself and the procedure the standard rent is calculated through, it would rather constrict the private rental housing market and deepen the current rent crisis. According to foreign cases of controlling over rental prices, excessively tight regulations result in a downturn in trade and market distortion. Therefore, the standard rent is recommendable only if it is utilized as the norm not as the compulsory criterion. Also, the role of the Committee on Rental Price Coordination to deduce agreement between tenants and landlords is important.

V. CONCLUSION

This study intended to examine the standard rent system the Seoul government plan on introducing as a solution to the Chonsei crisis. To be specific, the study verified cases in England, USA, Germany, and France where the standard rent system have already been utilized. And based on this, the direction to be followed to draw appropriate model for Korean rental housing market was suggested. As results, the housing cost burden on the tenants is expected to be reduced as per proposing fair level of rental price. It is more likely to be a logical conclusion especially in the Korean rental housing market situation because Korean housing market have been faced the problems of sudden increase in housing expenses and downward residential level due to the growth of households paying monthly rents and their movement to suburbs. However, there is demand for the cautious introduction of the standard rent system. If the standard rent is regarded as restrictions on the market, housing transaction can be daunted. Thus, the realization of residential rights is fully expected when constructing base data and putting the caps over the increasing

rate of the rental price are coincided with the standard rent system.

REFERENCES

- [1] E. H. Lee, "Study on the rent regulation in England and Wales", *Korean Journal of Civil Law*, Vol.34, 2006, pp.513-563.
- [2] HUD, "Final Fair Market Rents for the Housing Choice Voucher Program and Moderate Rehabilitation Single Room Occupancy Program Fiscal Year 2014", Oct. 2013.
- [3] Korea Appraisal Board, "February 2015, Total Housing Chonsei to Monthly Payment Conversion Rate of 7.7%", Press Release, Apr. 2015.
- [4] Listokin, D., "Federal Housing Policy and Preservation; Historical Evolution, Patterns, and Implications", *Housing Policy Debate*, Vol.2, Issue 2, 1989, pp.157-185.
- [5] Ministry of Land, Infrastructure and Transport, "Case Studies of International Housing Welfare Policy", 2012.
- [6] M. S. Park, "Fair Rent system of England and the Implications", *The Korea Spatial Planning Review*, Vol.357, Jul. 2011, pp.97.
- [7] National Assembly Research Service, "National and International Trends and Implications Related to Rent Regulations", 2011.
- [8] N. G. Kim, "Introducing Methods and International Cases of Fair(Standard) Rent System", Press Release, Apr 2015.
- [9] Office of Policy Development & Research, Fair Market Rents For The Section 8 Housing Assistance Payments Program, HUD, July 2007(rev.)
- [10] Seoul Development Institute, "A Study on Rent Subsidy Program of Seoul Metropolitan Government", 2011.
- [11] Seoul Development Institute, "Introduction to the Fair Rent System for Private Cooperative Housing in Seoul", 2012.
- [12] S.H. Kim, J. A. Park, "Section 8 Housing Choice Voucher Program for Low-Income Families in U.S.A: Focused on Columbia City, Missouri State", *Housing Studies Review* Vol.17, No.3, 2009, pp.05-34.
- [13] Y. S. Kim, S. J. Lee, "The Computing Standards of Fair Rent and the Tenure Security Program", *Construction and Economy Research Institute of Korea*, 2001, pp.1-132.
- [14] Y. T. Kim, "Lessons of French Housing Welfare Policy for 100 years", SERI, 2006.
- [15] Y. T. Kim, "Housing Welfare Policy of France", *Welfare Trends*, Nov. 2006.