

# All aspects on the residential rent negotiating process

Mikael Ahlborn, 2011-04-05

## Negotiating process

### The System

The system for rent setting in Sweden is partly based on a negotiation process in which the change in rent is an outcome of annual municipality-wise negotiation between the tenant's association and the municipality owned housing companies. In this negotiation there is an opportunity to let rents develop differently in different neighbourhoods possibly aiming towards better correspondence of rent and tenants conceptions of housing and neighbourhood quality.

The purpose of the Swedish rent-setting system was that the residents' general values to govern the rental structure. In practice, however, rent levels were tied to costs in municipality-owned housing companies. Rent level was governed largely by building age and maintenance costs. As a result of this, interest in quality improvement and adaptation to tenants' preferences were in the background of an intense cost versus price talk.

Utility value rent, the rent setting regulatory systems in use today and that takes account of the building and the apartment's standard equipment in the apartment, and in common areas such as laundry rooms, stairways and courtyards. Proximity to city centre, shops, daycare facilities and good public communication, but also the area's image and reputation are taken into account when the rent is negotiated on behalf of property owners and tenants.

Quality Rental is a development of the utility value system in which additional quality factors are measured and weighed in during the negotiations.

Utility value rent is a price regulation that differs from the market economy laws of supply and demand. This makes it possible for people with lower incomes to live in desirable neighbourhoods. At the same time the level of rent in less

desirable neighbourhoods can be higher than it would have been at market rent. As a result of more people willing and able to live in desirable neighbourhoods, reducing the number of available apartments there and waiting lists arise. The leases may be a de facto value. In 2009, the Competition Authority submitted a report which proposed a ban on communal determination of rent, and a reproachment of the market rent, in accordance with EU legislation. Critics say that although the purpose of the utility value system was that people with lower incomes would have the opportunity to live in desirable neighbourhoods, it has not happened to any great extent. Instead we have a system of housing rebate for high earners.

### **The utility value system**

Utility value system which was introduced in 1968 is about how a possible judicial review of a rent dispute should go about. In order to assess the rent reasonableness, requirements of rent for the apartment in question, compared with the rent for the "usage-value in terms of" equivalent apartments.

The utility value system was developed because, at the rent of regulation elimination, protect the individual's tenure, especially in shortage areas. The object was to enable the transition to a market-development of the rents. Comparison rent would be sought among the highest rents for usage value in terms of equivalent apartments in the resort, isolated peak rents excluded. Average rents would not be sought after, to the effect that this would preserve the rental structure and "counteract the desirable movement of rents". The utility value system as such was not the purpose of reducing rents; its purpose was to secure tenure. However, it had provided to public housing, rent costs determined by these mortgage companies, who were practically the dominant building owners, would be indicative and can therefore act governing and restraining effect on the general level of rents. When the review later revealed that it was doubtful as to whether the right of the application, given the price leaders function as intended, and that according to the Law Committee, considered necessary that barring an undue rise in the general level of rents.

From 1974 were validated because the rental trials in all situations (not only in the absence locations) in the first place would be made by comparing it with municipality- owned housing companies.

## **Developments in the years 1942 - 2009**

The Swedish rental market has been undergoing a gradual process of transformation from an unregulated profit market to an integrated social rental market since the 1940s.

Between 1942-1967: a cost-covering form of rent regulation was in force, to limit the profits of private landlords and prevent rents from being pushed up by housing shortages. During this period a stock of non-profit rental housing was built up, providing a non-profit alternative to the existing privately owned stock. Generous interest subsidized loans were made available for both profit and non-profit new build projects.

Between 1967-1992: rent-regulation was replaced by "negotiated rents", reflecting "utility value" to take better account of consumer demand. Rents in both non-profit and profit housing were to be arrived at via negotiation between the non-profit housing companies and the tenants unions who were to thereby act as cost-watchdogs over the rent setting process. Subsidy levels remained much as before.

In 1992: non-profit housing companies were given more leeway in determining their rent structures, and the role of the tenant unions in the negotiation process was weakened. This phase continues with the process of freeing up the non-profit housing companies by removing their special privileges and subjecting them to the same tax regime as profit housing companies. At the same time, state housing investment subsidies to all forms of housing are being significantly reduced.

More potential for rent-pooling within non-profit rental companies has led to increased market-sensitive rents, in general, higher in more popular older dwellings and lower in less popular, (mostly newer) dwellings.

The last major change in the rent setting rules was made in 2006 during which the rules of the rents of newly built houses were again discussed. It concluded that housing shortages were a fact in most municipalities, and one reason for that was said to be rented translation system. When the rental conditions could change six months after they had been determined, the reasonableness of the rent for a newly built house was to be examined by the rent tribunal six months after occupancy. Many property owners refrained from new construction when there was concern that the negotiated rent for six months would appear to be unreasonable by the rent tribunal. Such a rent reduction would cause the property owner to not obtain coverage for the costs of production and the return they

expected from the building, thus many refrained from dwelling. The government's starting point in the development of the new rules was that the rent for newly built apartments would cover the landlord's expenses while the tenant's interests for a reasonable rent and a secure tenure would be met. The regime finally introduced means that the rent for the planned, initiated and newly built apartments is presumed to be reasonable when it is established in a negotiated agreement with a locally established tenants' organization as a party to the hearing. All apartments in the property shall be subject to negotiation scheme and the agreement must be drafted prior to any lease agreement between landlord and tenant. The presumption exists then for ten years but can be breached in exceptional circumstances. Such exceptional circumstances shall be regarded as very exceptional situations such as that contract is deemed invalid or that the relationship can be reconciled. After the presumption period, the rent will then be established in accordance with the usual use-value system

### **New rules from January 1<sup>st</sup>, 2011**

Parliament has decided that new rules on rent setting will apply from 1<sup>st</sup> January 2011. The rent will be negotiated as before and utility value will remain the basis of the rent.

A change in the review of the rent, that is, when you find out if the rent is reasonable. At those times, one should not only take account of rents for comparable apartments in municipal companies, but also for equivalent apartments in private housing companies. Another change in the municipal housing companies' role, they will still be operated in a non-profit making but also for business principles.

Rents reformed by the municipal housing companies rent normative role, proposed for replacement by the collective negotiated rents instead become normative. This means that both municipal and private landlords may negotiate with the tenants' association on rents. The starting point for negotiations should be the practical value and it also introduced a protection clause against excessive rent increases in order to safeguard tenants' security of tenure.

## **Tangible security requirement**

Tangible security requirement means that when a rent is reviewed by the rent tribunal, a rent is not considered reasonable if it is "significantly higher than the rent for apartments" interchangeable. The motive of letting the rent any more than the municipality company rents was to create opportunity for movement in the price. As tangible security requirement applied in practice, private property owners could expect a premium of approximately five percent of municipality rents in comparison trials. It should be emphasized that tangible security requirement can be applied only in cases when the rent tribunal hearing a rent and then make a direct comparison.

A few words about the process of the rent tribunal in the trial of reasonable rent. It is up to the parties, tenant and landlord, to develop the comparison rents that are claimed. The property owner is trying to get as high rents as possible, while the tenant relies on comparison with lower rents. If the parties do not produce or fail to produce a reference, which is equivalent to the apartment whose rent is reviewed, the Board may make a general assessment of reasonableness of the requested rent in light of their own experience on the rental situation in the area. This is purely a fairness hearing and in this trial tangible security requirement does apply. However, if the parties manage to invoke a reference, which is roughly comparable to redress the apartment, made a direct comparison and rents compared the apartment will be the basis for the trial. It is only in this trial tangible security requirement may apply. The rent review in the test apartment then provides a rent that is not significantly higher than the rent for the apartment comparison, equivalent to about five percent. For direct comparison to be made it is assumed that the apartments should be roughly equal, that they must have about the same size and degree of modernity. In practice, however, the Boards usually exclude direct comparison. Almost all trials today are so-called natural justice, assessments, and then there is no way of using the tangible security requirement.

It must be highlighted that the new rules do not change when the issue of which apartments are "broadly equivalent" to the test apartment, but the same requirement to invoke the equivalent material will apply under the new rules.

## **Malmö model**

The rents in the Malmö model are determined by the two factors standard and location. The location of the apartment is given a large effect on the rent. This can be considered controversial since the location not has previously been given that much of an impact such as in the Malmö model. According to the legal system the rents are supposed to be determined based on the tenants' valuations. Since the tenants, according to presented research, value the location of the apartment higher, there is nothing wrong in letting the location be reflected in the rent. The rents in the Malmö model are in this way adjusted to the market.

## **Summary**

Utility value system has evolved from being a very landlord friendly rent-setting system that certainly lead to more equal partners, but also a much more limited system. The author also questions whether the utility value system is taking care of tenants' interests more in today's utility value system than to the landlord's interest. This is why the relationship between the parties to a certain extent can be said to have fallen upon the tenant's favor. The utility value system can thus no longer be said to be a system that imitates a market-justice system when taking adequate account of changes in the rental market when the new rents shall be set by residential apartments.

# All aspects on the residential rent negotiating process

Mikael Ahlborn, 2011-04-05

## Group Work

### Residential rent negotiating process

As the city manager, you are just in the beginning of the annual residential rent negotiating process. You start to think about what you need to do before the meeting with the Tenants Association.

### Questions

- 1 What do you need to think about before you start the annual rent negotiating process?
- 2 What should you bring with you to the negotiating meeting?