

Consumer protection for buyers of newly built tenant-owned apartments

Summary and recommendations

In most cases, a consumer who purchases a product or service is covered by special consumer protection legislation. Purchase of newly built tenant-owned apartments is not covered by this legislation. Instead, it takes place as part of an association formation process regulated by the Swedish Tenant Ownership Act. Normally, the tenant-owned apartment is purchased by entering into a binding advance agreement with a tenant-owners association, formed by a housing developer, for which it has appointed a construction board. Initially, the buyer is not a member of the tenant-owner association and therefore has neither insight into nor influence on the construction process. The buyer is often bound by the advance agreement for more than two years before taking possession of the apartment.

Since the Tenant Ownership Act took its current form in 1991, the market for newly built tenant-owned apartments has changed. Housing prices have risen sharply, while today, the buyer finances a large part of the construction cost through their invested capital. When prices fell in autumn 2017, it was noted that some buyers had trouble completing their purchases. Along with other indications of risks for the buyers, the Swedish NAO has found reason to examine consumer protection relating to purchase of newly built tenant-owned apartments.

Purpose and audit questions

The purpose is to examine whether the Government and the government agencies have done enough to safeguard the interests of buyers in conjunction with the purchase of newly built tenant-owned apartments. The audit comprises the following questions:

1. Do current regulations for purchase of newly built tenant-owned apartments ensure fit-for-purpose protection against material risks for the buyers?
2. Do buyers receive adequate, customised information about material risks and other conditions before their purchase?

3. Have the Government and the relevant agencies overall made appropriate efforts to safeguard buyers' interests when they purchase newly built tenant-owned apartments?

Audit findings

The Swedish NAO's overall conclusion is that the Government has not done enough to safeguard the interests of buyers in conjunction with the purchase of newly built tenant-owned apartments. The audit shows that the protection for buyers of newly built tenant-owned apartments has fundamental deficiencies compared to protection in other consumer markets. In addition, the buyer does not receive sufficient information about risks, nor the level of consumer protection that, for example, consumer-oriented supervision provides in other markets.

Buyers of new apartments lack fit-for-purpose protection

In the opinion of the Swedish NAO, the buyer's position is particularly weak in this area since the construction board appointed by the housing developer provides the developer with a large amount of influence to the detriment of the buyer.

The reason for the buyer's weak position is that the opposite contracting party is the tenant-owner association, not the business operator, that is, the housing developer which is running the construction project. Thus, the principle in the tenant-ownership legislation applies whereby the interests of the individual member must be weighed against the interests of the association (that is, all the members). This is a well-justified principle when the tenant-owner association consists of the members who are living there and is run by a board consisting of members. However, the Swedish NAO believes that this principle does not work satisfactorily when a tenant-owner association formed by the builder sells newly built tenant-owned apartments. In practice, the construction board can act based on the interests of the housing developer rather than those of the association. Nor can the buyer demand what normally applies in a consumer relationship.

The principle of association interest also means that the construction board has the right to make decisions about changes in the design of the dwelling and the finances of the tenant-owner association. The buyers, who are the future members, have no opportunity to influence the decisions and have limited opportunities to demand redress. If the buyer wishes to pursue a legal process to revoke the advance agreement and loses the case, this may entail large legal costs for the buyer. In addition, the buyer has neither influence on nor insight into the construction contract entered into between the construction board and the construction company regarding construction of the building. This means that the buyers do not know what the association has actually ordered from the construction company until afterwards. Nor is it certain when the members take

over the work of the board that, for example, plans and agreements with the construction company have been documented.

The Swedish NAO also considers that the complexity of the process to form the association reinforces the buyer's inferior position in terms of knowledge. For both the buyer and some estate agents, it is, for example, difficult to understand what the advance agreements and the grant of usage agreements entail. It is also the construction board that engages estate agents, certifiers and inspectors who have various information and control assignments during the construction process. This further strengthens the construction board's position relative to the buyer.

During the process, the buyer takes personal financial risks that are not protected in the same way as similar risks in the financial markets, for example. Buyers who sign an advance agreement bear a large personal financial risk in the event of price drops in the housing market, which in the worst case can result in personal bankruptcy. Since the credit agreement is normally signed long after the advance agreement, the 15 percent cash down-payment that means that buyers in the ordinary housing market have a margin for coping with a price decline is not secured. There is also no common view on what constitutes sustainable finances for the association. This gives scope for variation and in a review of a large number of financial plans, the Swedish NAO has noted significantly varying financial conditions. Some buyers therefore run a higher risk of being hit by large increases in the association's fees, which may significantly reduce the value of the buyer's apartment.

No clear information about the risks

The Swedish NAO's conclusion is that buyers do not receive adequate, customised information about material risks and other conditions before their purchase. There is no information requirement in the tenant ownership legislation. The Swedish NAO's review of sales material prior to purchase shows that it focuses on lifestyle and rarely provides information about risks associated with the advance agreement or the association's finances.

The Swedish NAO also considers that information measures cannot address the fundamental deficiencies in consumer protection which are the result of the legislation.

The Government has not done enough to improve consumer protection

The Swedish NAO's conclusion is that the Government has not made appropriate efforts to safeguard buyers' interests when they purchase newly built tenant-owned apartments. The question of consumer protection in the market for tenant-owned apartments was investigated in 2015–2017 at the initiative of the

Government. The inquiry has not prompted the Government to submit any proposals to the Riksdag.

Recommendation

The Swedish NAO notes that there are deficiencies in the protection of buyers of newly built tenant-owned apartments. The Swedish NAO therefore makes the following recommendation to the Government:

- Review the provisions of the Tenant Ownership Act and other relevant regulations to ensure that buyers of newly built tenant-owned apartments are covered by fit-for-purpose consumer protection, in line with other consumer markets. The protection should mean that the housing developer is responsible for delivery of the product to the buyer. This review should also take into account:
 - the need to clarify the estate agent’s role and information responsibility in negotiating newly built tenant-owned apartments
 - the need to limit buyers’ personal financial risk after signing an advance agreement, for example, in the event of price drops
 - the need for regulations defining what constitutes sustainable finances for a tenant-owned association formed by a housing developer
 - the need to introduce regulations so that the buyer is informed about risks before buying a newly built tenant-owned apartment.