

Housing Policy and Housing Defect Warranty System in Japan

Ken Takizawa

Director of Housing Warranty Office, Housing Bureau
Ministry of Land, Infrastructure, Transport and Tourism
2-1-3 Kasumigaseki Chiyoda-ku Tokyo 100-8918
takizawa-k2yk@mlit.go.jp

Abstract

Starting with the general information on Japanese housing situation and policy, I will introduce the current housing defect warranty liability system, which became legislated as a result from the scandal of false earthquake resistance data for condominiums and hotels revealed in 2005. Specifically, I will describe the outline of related laws, history and background of establishment of the warranty/insurance programs, characteristics thereof compared to other countries. The course of action toward even better operations considering the social and economic situations is stated from the policy maker's viewpoint.

1. Housing situation and housing policy in Japan

1) Basic information on Japan

Japan is an island country (four big islands) located in the Pacific Ocean in North East Asia. Most of the country belongs to the temperate zone with clear four seasons due to the monsoon.

The total land area of Japan is 370,000 km², which is almost the same as the land area of Germany, although Japan does not have much flat land. The population is approximately 126 million, which is the 10th most populated country in the world. The population is concentrating in big cities, and especially Tokyo, the capital, which has approximately 10% of the whole population (12 million).

The changing demographic structure in Japan gives an impact larger than any other economic or social factors to the future housing and housing policy. The population in Japan has been declining since 2010, and the rate of aging is expected to rise up to 41.1% in 2060 from 22.8% in 2010. This is a striking figure compared to other countries. The number of households with only old people is also growing every year.

In Japan, the proportion of non-regular employees and the unemployment rate are both on

the upward trend, which leads to reduce the average annual income of working people. In particular, the average annual income of people in their 30's, who are the majority of first-time housing purchasers, has significantly decreased.

2) *Housing and housing policy in Japan*

In Japan, owner-occupied detached houses account for half of the total existing houses. Including the apartment houses, some 60% of existing houses are owner-occupied. The rest of existing houses are rented houses, which are characterized by much smaller area/space compared to the owner-occupied houses.

The percentage of newly built houses is high in the housing market, and the share of the existing houses is only 13.5%. The average life of houses is 27 years, which is quite short compared to other countries.

According to “Better Life Index” issued by OECD, the quality of life in Japan is ranked relatively low. Specifically categories of “housing” and “work-life balance” are not highly evaluated.

Housing starts in Japan have been decreasing since late 1980s. Due to economic downturn precipitated by the Lehman Brothers bankruptcy in 2008, the number dropped down to 790,000. Since then, there is sign of recovery and the number is getting close to 1 million housing starts per year.

Japanese housing policy can be classified according to its aims under the following periods after World War II:

1st period	1945~1975	Solution of housing shortage
2nd period	1976~2000	From quantity to quality
3rd period	2000~2006	Promotion of market function and housing stock
4th period	2006~	Realization of an affluent living

In 2006, the Basic Act for Housing was enforced aiming to provide an affluent living for people.

The Basic Act for Housing stipulates, among others, its basic principle and framework of the “Basic Plan of Housing” that sets forth a purpose of housing policy for every 10-year

period and the specific measures thereof.

The current “Basic Plan of Housing” set forth is for the period of FY2011 to FY2020.

The application of housing defect warranty liability insurance is expected to be one of the policy measures used to activate an existing house market and to develop a housing renovation market in the ongoing “Basic Plan of Housing.”

2. History of establishment of Housing Defect Warranty Liability System in Japan

As stated above, the target of housing policy in Japan changed from "securement of quantity" to “improvement of quality." Today, the Japanese Government puts much importance on realizing affluent living.

At the end of the 20th century, when the need to improve the quality of housing markedly increased, the Housing Quality Assurance Act (HQA Act) was enacted (effective from 2000). The purpose of the enactment of the HQA Act was to create a framework to provide housing of sufficient quality to consumers throughout the process from the production of housing to after-sales service.

Concrete measures taken in the HQA Act are as follows:

- i) Introduction of Housing Performance Indications System (HPIS)
A system for displaying and evaluating the performance of the housing to be conducted by a third party (not the builder) was introduced. The aim of this system is to make it possible for a consumer to understand the performance of the house which they intend to purchase and to compare the performance with others.
- ii) Establishment of an ADR system
In order to strive to settle a dispute over the performance of housing quickly and inexpensively, an Alternative Dispute Resolution (ADR) system specializing in disputes regarding HPIS was introduced.
- iii) Special provisions for Defect Warranty Liability of newly built houses
Special provisions concerning the Civil Code for Defect Warranty Liability of newly built houses were introduced. By these provisions, builders or realtors of new housing are liable for a 10-year period for defects of major structural elements necessary for structural strength and parts preventing rainwater ingress.

In 2005, a scandal “Forgery of structural calculations” occurred which was a great shock to housing construction industry in Japan.

In this scandal, it was discovered that a number of condominiums were built based on false structural calculation statements by some architects. As a result, rebuilding or large-scale repair work became necessary.

The developer of these condominiums should have fulfilled their Housing Defect Warranty Liability based on HQA Act. However, as there were too many defective condominiums, the developer went bankrupt. The buyers of these condominiums (consumers) could not claim repair or compensation to anybody.

The scandal “Forgery of structural calculations” revealed the extreme vulnerability of HQA Act, which is the fact that if housing suppliers do not have sufficient financial means to fix a defect found in a new house, there were no measures to cover the cost and protect consumers.

On the basis of this experience, several committees established in the Ministry of Land, Infrastructure, Transport and Tourism (MLITT) examined how to design the new system in order to strengthen consumer protection. MLITT concluded that it was necessary for builders and realtors supplying newly built houses to secure financial resources in order to fulfil their Defect Warranty Liability.

3. Overview of Act for Execution of Defect Warranty Liability under Housing Quality Assurance Act

[Key points of the Act]

The Act for Execution of Defect Warranty Liability under Housing Quality Assurance Act (EDWL) was promulgated in 2007 and became completely effective in October 2009.

The following are the key points of EDWL:

- Compulsory Funding Scheme to Ensure Fulfillment of Defect Liability for Newly built houses;
- Consolidated Insurance Underwriting; (Specific Housing Insurance Corporations)
- Improved ADR System

Act for Execution of Defect Warranty Liability under HQA Act (Overview)

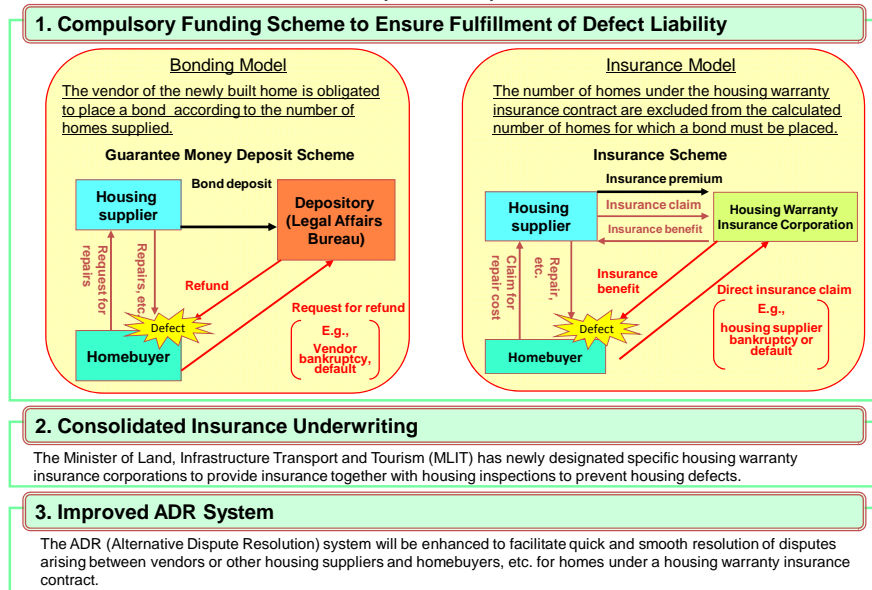


Figure 1.

4. Characteristics of the Housing Defect Warranty Liability System in Japan

1) *Compulsory funding scheme to ensure fulfillment of defect liability for newly built houses*

The Japanese Civil Code sets provisions that contractor of a building has defect warranty liability for a certain period of time. For example, in the case of a wooden building, the defect warranty liability lasts five years. (The period of this liability can be shortened by a special agreement.)

Concerning newly built houses, the HQA Act has provisions which require defect warranty liability for 10 years regarding major structural elements necessary for structural strength and parts preventing rainwater ingress. These provisions are mandatory and the duration of the liability cannot be shortened.

In order to ensure the fulfillment of the defect warranty liability for new houses, EDWL Act requires financial resources as stated below to builders and realtors supplying newly built houses.

The aim of this requirement is to make builders and realtors ensure the fulfillment of the defect warranty liability by making them prepare financial resources which are necessary for the payment of damages or the implementation of repairing when there is a defect in new houses. Therefore, it is builders and realtors that are obligated to meet this requirement.

However, taking out Housing Defect Warranty Insurance (HDWI) is not the only way to fulfill the requirement concerning financial resources. It is also possible to deposit Guarantee Money (GM) to the Local Legal Affairs Bureau. One of the features of the Japanese system is that builders and realtors can choose HDWI, GM or mixture of the two.

99% of businesses (builders and realtors) select HDWI. However, since most of the businesses which select GM are large companies, the ratio to the total number of construction of new houses is almost equivalent. (HDWI: 52%, GM: 48%)

2) Consolidated Insurance Underwriting (Specific Housing Insurance Corporations)

In order to appropriately manage the HDWI system, it is necessary to not only design and sell insurance products, but to also conduct accurate on-site inspections of houses for insurance underwriting. In Japan, there exists Housing Defect Warranty Insurance Corporations (HDWIC) which specialize in providing HDWI. At present, five HDWICs are designated by the Minister of Land, Infrastructure and Transport.

It is the MLIT which is in charge of housing administration regulations and supervises the HDWICs.

3) Improved ADR System

Regarding houses which are covered by HDWI, the EDWL Act enabled builders or realtors and consumers to utilize the ADR (Alternative Dispute Resolution) System which was established by HQA Act:

- Housing Dispute Examination Committee (HDEC, *1) conducts mediations, conciliations and arbitrations regarding disputes about the contract of construction or sale of new houses.
- Housing Dispute Settlement Support Centre (in Tokyo) is in charge of maintaining the

ADR system as a whole. (Ex. Subsidies to HDEC, training for lawyers who are in charge of ADR cases, telephone counseling for consumers etc.)

- (*1) HDEC is organized in Designated Housing Dispute Settlement Bodies (DHDSB). DHDSBs are established nationwide by Japan's 52 bar associations.

4) Others

In Japan, the fulfillment of Housing Defect Warranty Liability by builders and realtors is thought to be very important from the point of view of consumer protection on housing.

HDWI not only is based on the EDWL Act, but also has been constructed by the close cooperation between the public and private sectors to protect consumer on housing. (Ex. relief fund by the central government, re-insurance pool)

To prepare for risks of defects of existing houses or renovations, HDWICs provide several kinds of non-mandatory insurance.

The total number of issuing insurance policies of these non-mandatory insurance is about 30,000; it is only about 1% of that of mandatory insurance for new houses.

5. Housing Trend and Review of Secure Execution of Specified Defect Warranty Liability system

It is required to review EDWL after five years from its enforcement and to revise the system if necessary.

The fifth year falls this year, and a working committee composed of professionals has been holding discussions.

6. Change of society and economic situations that influences the demand of housing

As described previously, new houses are a major share of the market compared to existing houses in Japan. However, the number of families with children has been decreasing due to declining birth rates on a consistent basis since 1950s, and the new housing market is expected to shrink further.

Another negative factor that is making housing purchase difficult includes the average annual income of the people in their 30's has been decreasing because of irregular

employment and an increased jobless rate.

Due to de-population, relocation of elderly people to retirement houses and deaths, there are abundant vacant existing houses. Also the cost to obtain an existing house, including necessary renovation work on it, is less compared to buying a new house. Considering these facts, policy makers should work on a housing policy that will make existing houses a practical solution to meet the consumers’ various demands.

On the other hand, it is a fact that there are a certain number of existing houses with inadequate quality. For example, houses are supposed to be designed with some anti-seismic measures in Japan, although approximately 20% of those houses do not conform to the present earthquake resistance standards.

Defect insurance plans for existing houses and housing renovation works are very important in light of securing the quality of existing housing stock and activating the market for existing housing stock.

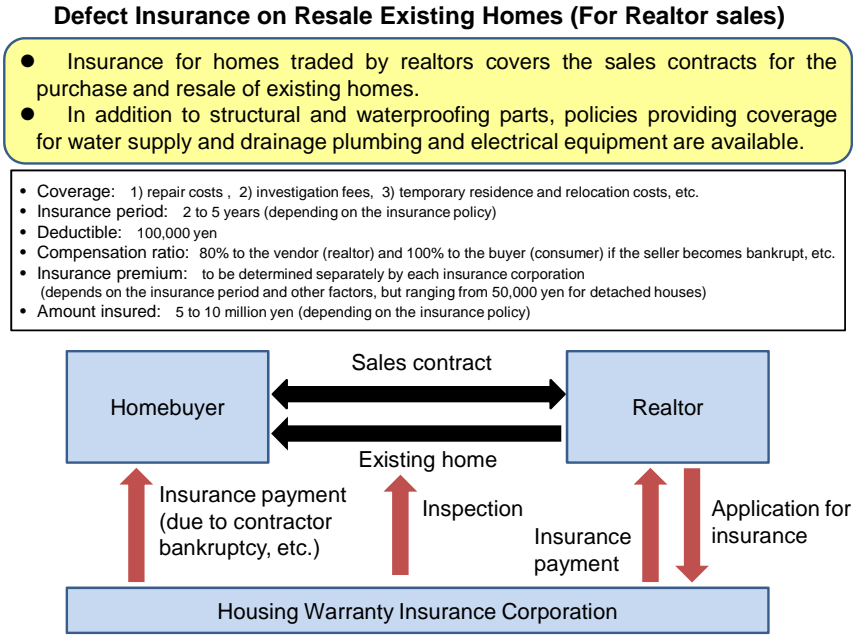


Figure 2.

Remodeling Defect Insurance

- Remodeling defect insurance covers the insured for remodeling contracts.
- Coverage is available for all parts of the remodeling work.

- Coverage: 1) repair costs, 2) investigation fees, 3) temporary residence and relocation costs, etc.
- Insurance period: 1 to 10 years (depending on the insurance policy)
- Deductible: 100,000 yen
- Compensation ratio:
80% to the contractor (remodeling contractor) and 100% to the client (consumer) if contractor becomes bankrupt, etc.
- Insurance premium:
to be determined separately by each insurance corporation
(around 30,000 yen for renovations contracted at 4 million yen).
- Amount insured: 1 million to 20 million yen (depending on the contract amount, etc.)

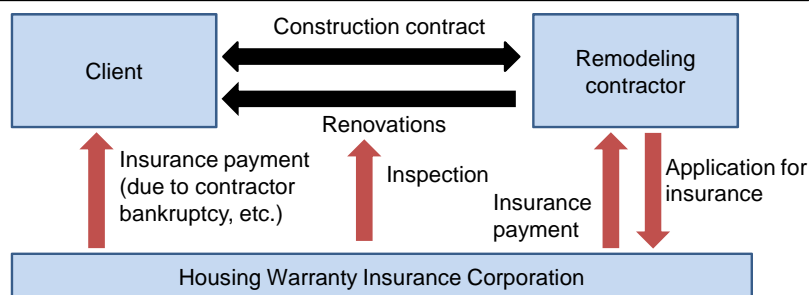


Figure 3.

Housing warranty/insurance plans in other countries seem to be mostly for new houses, and the development and diffusion of insurance products to cover existing houses and renovation work should advance global efforts. We will pursue this challenge which should enrich consumer protection policies.

One of the important conditions for promoting the existing house market is to ensure a consumer has enough information about the house before making a purchase. However, the “inspection” that a professional should carry out to check the current state of the house prior to the maintenance/renovation work or purchase has not been well established nor well spread. MLITT released a guideline for the implementation of inspections for existing houses in May 2013, which we believe will make the inspections of existing houses widely familiar.

Conclusion

It is common knowledge around the world that purchasing a house is not an everyday occurrence and consumers have a strong desire to obtain a house with an equal or even better value than the money they pay. From the point of view of consumer protection, housing warranty and insurance systems are playing an important role.

As the Ministry of Land, Infrastructure, Transport, and Tourism, we are determined to contribute to the diffusion and development of housing warranty and insurance systems on a global basis through the of exchange opinions/information and close cooperation with the participants in this conference.