

Chonse, a real property lease transaction unique to South Korea

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This article is a tentative analysis of Korean real property lease transaction system, *chonse*, a lease with a large sum of the key money deposit and without monthly rent payments. *Chonse* is the dominant form of lease arrangement used by most middle-class families in Korea without ownership of real property for both principal residences and commercial business places. The author analyzes this unique institution of real estate lease exclusive to South Korea and describes main features and details of it as well as related legal systems. *Chonse* also has the character of a lending system for the real property owners, where the landlord has the same position of borrowing the money from the tenant and the lending term is the same as the lease period. The tenant as a creditor has the leased property at his/her possession for the term and the tenant has the legal interest not only of a usufructuary right but also of a security right of pledge or collateral. After a brief review of the legal characteristics and roles of *chonse* in the modern period of development of South Korea, the author critiques the changing role of the *chonse* system in the modern South Korean society. Continuous economic development, reform of the financial system, globalized lifestyle and home living, and most of all its shrinking and aging population as well as low interest rates and the flourishing of long-term mortgages are all circumstances that need to be taken into account in assessing the implications of the changes taking place with regard to *chonse*.

Keywords: *chonse*, real property lease, registration, priority, real estate finance, real estate transaction.

Introduction

Chonse, also known as *chonsei*, *jeonse* or *jeonsei*, and written as “전세” in Korean as well as “傳賃” in ancient Chinese character, is a legal system of transaction arrangement for house or building lease that is unique to South Korea¹. *Chonse* is the dominant form of lease arrangement used by most middle class families in Korea without ownership of real property for both principal residences and commercial business places. As this unique form of lease transaction system may be unfamiliar to individuals outside of Korea, having a basic understanding of *chonse* is one of the most important steps for foreigners and prospective immigrants and investors who aim to land softly in Korea.

In the *chonse* system, a lessee or tenant is entitled to use the leased house or building by paying some up-front lump sum deposit money to the lessor or landlord, also referred to as the “key money deposit”. The amount of the key money deposit is typically quite large compared with that of an ordinary lease contract, which is called *wolse* (written

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¹ Although the terminology *jeonse* is often used in most news media, this article uses *chonse* according to the English translation version of the Korean Civil Act published by the Korean Legislation Research Institute. *Chonse* is regulated in § 303–319 of the Korean Civil Act. Most of English translation versions of Korean legislations are provided in the Korean Legislation Research Institute web site. The Korean Civil Act is found on: https://elaw.klri.re.kr/kor_service/lawView.do?hseq=45912&lang=ENG. All webpages and websites were last visited and accessed on 15.12.2020.

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as “월세” in Korean and “月賃” in ancient Chinese character). With a large sum of the key money deposit, the tenant has no obligation to pay monthly rents. Although the origin of this system can be traced back to the Middle Ages, *chonse* has become more widely used within the last few centuries, during which time Korea gradually developed into a more industrialized society². As the national economy has been continuously growing and the population of major cities and metropolitan areas has been booming, so did the demands for housing and commercial buildings during the last few decades. Due to the close relationship between economic state and real property, it is often described that the history of the Korean economy cannot be explained without the consideration of the *chonse* system.

Although some claim that the concept of a lump-sum deposit for rent dates back to 1876, when the Joseon Dynasty signed a coercive treaty with Japan³, many factors have influenced the development of the *chonse* system in South Korea, including prolonged high interest rate, rapid uprise of housing prices, the lack of long-term mortgage system for new home buyers, as well as the coexistence of very high demand and short supply of new homes and commercial buildings in modern South Korea, all of which continued on for centuries. However, during the last few decades, the Korean society is experiencing drastic changes to these factors as the country's economy reveals a slight but steady plateauing effect that is heading towards a rather stable society. Some critics note that considering this economic trend, *chonse* is no longer sustainable in the contemporary Korean society and destined to disappear in the very near future. It is undeniable that numerous middle-class families in South Korea will undergo difficulties in family budgeting upon the ceasing of the *chonse* system, as they have been accustomed to a leasing system that does not require monthly rental payment. As such, early discussions on existing policies involving *chonse* and potential strategies on other forms of lease arrangement are warranted.

This article presents the legal structure of *chonse* through some examples and reviews their implications as to how they impact the Korean society and economy. The article also discusses current government policies involving *chonse*, with the author's closing comments on the future directions of this system.

1. Structure and Feature of *chonse*

1.1. Basic Structure of *chonse* Transaction

If a lessor or landlord enters into a *chonse* lease agreement with a lessee or tenant, the tenant is entitled to use the rented house or building by paying an up-front lump sum deposit money to the landlord, for which the amount is agreed by both parties and usually about 40 to 60 % of the market sale value of the leased property. Upon the deposit, the tenant has no obligation to pay any monthly rents to the landlord during the lease term. While the exemption of monthly rents is a huge benefit to the tenant, there are some risks to this system. The landlords keep the received deposit at their disposal. For instance, the landlords could deposit the money into their own savings account in order to receive interest, make an investment on other businesses or projects at their own risk, or even spend it all on miscellaneous expenditures. At the termination of the lease, the landlord returns back to the tenant the nominal value of the deposit without any additional interests or proceeds. Since the landlord has no legal obligation to escrow the deposit safely, the return

² For more discussions on the history of *chonse*, see: *Kwon Y., Lee Y.-S.* Legal analysis of traditional leasehold in Korea (*chonsegwon*) from a comparative legal perspective // *Arizona Journal of International and Comparative Law*. 2012. Vol. 29, no. 2. P. 264–268.

³ *Jeonse*, a keystone of Korea's economic history // *Korea Herald*. February 6, 2015. Available at: <http://www.koreaherald.com/view.php?ud=20150206001042> (accessed: 15.12.2020).

of the deposit is not legally nor financially secured, which means that the default risk of the deposit return by the landlord falls on the tenant. As the deposit is quite a large amount for the tenant⁴, the default of the landlord could endanger the whole social and economic life of the tenant, and as such legal protection of the tenant is strongly warranted.

On the other side, *chonse* has another character as a lending system for the real property owners, where the landlord has the same position of borrowing the money from the tenant. In particular, the amount of the borrowed money is equivalent to the lump sum deposit, the lending term is the same as the lease period, and the interest rate is definitely 0 % from the perspective of the landlord as well. The tenant as a creditor has the leased property at his/her possession for the term, which means the tenant has the legal interest not only of a usufructuary right but also of a security right of pledge or collateral. *Chonse* tenant is entitled to obtain the repayment of deposit money in preference to persons with the junior right or other creditors in the foreclosure process or public auction of leased property⁵. It could be understood that the interest of the borrowed loan is deemed to be set off by the rent of the leased property.

[Example 1] L1 has a condominium unit, for which the market sale price is \$ 600,000. L1 entered into a *chonse* agreement on the condominium unit with T1 as follows:

- (1) *Chonse* deposit shall be \$ 300,000 and
- (2) *Chonse* shall begin 1st of May 2019 and end 30th of April 2021.

After T1 deposits \$ 300,000, T1 can use the unit without monthly rent for the term. L1 receives the deposit \$ 300,000 which is at L1's disposal. After the termination of *chonse*, T1 returns the unit back to L1 and L1 returns \$ 300,000 back to T1 without any additional interests or proceeds.

Even though it is true that *chonse* is extremely dominant in the real property lease market in South Korea, it is also noteworthy that the methods of ordinary lease transactions that involve monthly rent payment are still conducted in the country. The ordinary lease contracts, also known as *wolse*, are often used by the younger population such as students, single residents, foreigners, temporary residents, and other tenants who cannot afford to pay a large amount of lump sum deposit.

If a tenant is confident that he/she can get more income by investing the deposit amount on other projects instead of *chonse* deposit, it is beneficial for him/her to go for an ordinary lease with monthly rents rather than *chonse*. An instance of this would be many commercial property tenants who prefer *wolse* rather than *chonse* as a result of having successful revenue in their business. The preference of *chonse* and *wolse* depends on many factors. Landlords with more opportunities for promising alternative investments would prefer *chonse*, while other landlords who need steady and stable cash income prefer *wolse*. Due to this disparity, there are also many diverse forms of half-*chonse* as well as some hybrid forms of *chonse* and *wolse*, which require both half-reduced lump sum deposit and likewise half-reduced monthly rent payments. As the proportion of deposit

⁴ For example, it was reported that the average lump sum deposit of a *chonse* lease home in Seoul equals to almost \$ 500,000 USD as of August 2020 in the monthly statistics of real estate prices reported by Kookmin Bank (KB).

⁵ Korean Civil Act § 303 (Contents of *Chonse*) (1) Any person having *chonsegwon* is entitled to use it in conformity with its purposes and to take the profits from it, by paying the deposit money and possessing the real property owned by another person. Furthermore, he is also entitled to obtain the repayment of deposit money in preference to persons having the junior right or other creditors, with respect to the whole real property.

(2) Farming land shall not be made the subject matter of *chonsegwon*.

and monthly rent is negotiable between the two parties, the forms and contents of this half-*chonse* are quite diverse and flexible.

[Example 2] L2 entered into a *wolse* agreement on the condominium unit with T2 as follows:

- (1) *Wolse* deposit shall be \$ 9,000 and
- (2) Monthly rent shall be \$ 3,000 and
- (3) *Wolse* shall begin 1st of May 2019 and end 30th of April 2021.

After T2 deposits \$ 9,000, T2 can use the unit with monthly rent of \$ 3,000. After the termination of *wolse*, T2 returns the unit back to L2 and L2 returns \$ 9,000 without any additional interests or proceeds. Usually in this scenario, T2 returns the unit back to L2 without paying the last month rent of \$ 3,000 and L2 returns back \$ 6,000 to T2 after deducting the last month rent.

[Example 3] L3 enters into a half-*chonse* agreement with T3 as follows:

- (1) half-*chonse* deposit shall be \$ 150,000 and
- (2) Monthly rent shall be \$ 1,500 and
- (3) half-*chonse* shall begin 1st of May 2019 and end 30th of April 2021.

After T3 deposits \$ 150,000, T3 can use the unit with monthly rent of \$ 1,500. L3 receives the deposit \$ 150,000 which is at L3's disposal. After the termination of half-*chonse*, T3 returns the unit back to L3 and L3 returns \$ 150,000 without any additional interests or proceeds. Usually in this scenario, T3 returns the unit back to L3 without paying the last month rent of \$ 1,500 and L3 returns back \$ 148,500 to T3 after deducting the last month rent.

Utilities and other cost (water, gas, electricity, cable, phone, internet, security), maintenance fee for the condominium, and contingent cost for necessary minor repairs are regulated by the terms of lease contract, usually paid by the tenant. The default rule of the Korean Civil Act on this matter is that these costs are basically carried by the landlord in case of *chonse*⁶, and in contrast are carried by the tenant in case of *wolse*⁷. The stipulations in the agreement of lease by both parties overwrite these rules because the articles thereof are understood as default rules and optional provisions not as compulsory ones⁸. In rare cases where some major damage has been sustained to the leased property, it has to be fixed before the return of the deposit or the cost for repairs should be deducted from the deposit, which is one of the original functions of the deposits for both *chonse* and *wolse*.

1.2. Distinction of *chonse* and *Wolse* in the Korean Civil Law System

Following a modified pandectist structure of the *Pandekten* system, derived from the ancient Roman law, the Korean Civil Act consists of five main parts, which are (1) general provisions (§ 1–184) (2) real rights (§ 185–372) (3) claims (§ 373–766) (4) relatives

⁶ A *chonse* tenant should maintain the status quo condition of the leased property and perform necessary repairs in the ordinary course of the management thereof. Korean Civil Act § 309 (Duties of *Chonse* Tenant of Maintenance and Repair).

⁷ A *wolse* landlord is bound to maintain conditions necessary for the use and taking profits of the leased property while the lease is in force. Korean Civil Act § 623 (Lessor's Duty). If a lessee has made necessary expenditures relating to the preservation of the leased property he/she may demand reimbursement thereof from the lessor. Korean Civil Act § 626 (1) (Lessee's Right to Demand Reimbursement).

⁸ If any person has declared an intention which differs from any provisions of statutes, which are not concerned with good morals or other social order, such intention shall prevail. Korean Civil Act § 105 (Optional Provisions).

(§ 767–979) (5) inheritance (§ 980–1118)⁹. The first part of general provisions is comprised of regulations that have effect on all the other four parts, such as source of law, personhood, legal capacity, agency, declaration of intent, void and nullification, rescission, and limitation periods. The second part of real rights regulates mainly on the rights regarding real properties and personal properties and transfers thereof, including ownership, possession, servitudes, security interests including mortgage and pledge, and *chonse*. The third part of claim covers torts and unjust enrichment but mainly contracts including sales, lending, hiring, contracting, commission, and lease agreement *wolse*. The fourth and fifth parts are family and succession law, regulating marriage and divorce including marital property schemes, parents and children relation including adoption, guardianship, and succession and distribution of estate and wills.

The clear distinction between real rights and claims is characteristic in the Korean Civil Act as is in most of European continental legal systems like Germany¹⁰ or France¹¹. Although both *chonse* and *wolse* have a common main function which is to use other's real property, the legal characters of the two are definitely different. *Chonse* is categorized as a real right or "right *in rem*" (*Sachenrecht* in German or *droit des biens* in France) when it is registered¹², while *wolse* is categorized as a claim (*Schuldrecht* in German or *droit des obligations* in France). As a real right holder, a tenant of *chonse* is entitled to a secured interest not only against his/her counterpart of the transaction, the landlord, but also against all the third parties¹³, while a tenant of *wolse* has an obligational interest only against the landlord by nature. In addition, *chonse* could be assigned or sub-leased¹⁴, while *wolse* may not be assigned or sub-leased without the approval of the landlord¹⁵.

The up-front large amount of lump sum deposit of *chonse* is secured safely when the leased property is sold or even auctioned as long as the *chonse* is recognized as a real right. An important point here is that a *chonse* needs to be registered on the real estate registration record of the government in order to be recognized as a real right¹⁶. Any real right transaction over a real property including acquisition, alteration, or loss thereof takes legal effect upon its registration according to the Korean Civil Act¹⁷, which is one of the key principles of the Korean real property law. Without a registration, *chonse* is simply recognized as an obligational claim, which means the lump sum deposit is not secured against the third parties including the assignee or successor of the leased property. Even though a *wolse* could be registered on the real estate registration record as well, it is registered as an obligational claim, which makes it a "registered obligational claim", not a real right.

⁹ For details on the Korean Civil Act, also known as Korean Civil Code (KCC): Yang C.-S. Recent preparatory work for the amendment of the Korean Civil Code // Journal of Korean Law. 2004. Vol. 4, no. 1. P.99–101.

¹⁰ Korean Civil Act is especially under strong influence of German Civil Code, *Bürgerliches Gesetzbuch* (BGB), which follows a modified pandectist structure and consists of five main parts as well: (1) general part (*allgemeiner Teil*) (2) law of obligations (*Schuldrecht*) (3) property law (*Sachenrecht*) (4) family law (*Familienrecht*) (5) inheritance law (*Erbrecht*).

¹¹ The Civil Code of the French, *Code civil des Français*, follows the *Institutionen* in the ancient Roman law *Corpus Juris Civilis*, and consists of three main parts: (1) law of persons (*droit des personnes*) (2) law of things (*droit des biens*) (3) law of actions (*droit des obligations et des contrats*).

¹² Kwon Y., Lee Y. -S. Legal analysis of traditional leasehold in Korea (*chonsegwon*) from a comparative legal perspective. P.269.

¹³ If a *chonse* is secured by registration and becomes a right *in rem*, it is then legally described as "*chonse-gwon*" or "*chonsegwon*", which means a right (*gwon*, 권, 權) to *chonse*.

¹⁴ Korean Civil Act § 306 (Assignment and Sub-lease of *Chonse*).

¹⁵ Korean Civil Act § 629 (Restriction on Assignment of Right of Lease and Sub-lease).

¹⁶ Registration of Real Estate Act § 72 (Matters to Be Registered in Rights to Lease on Deposit Basis, etc.). Available at: https://elaw.klri.re.kr/kor_service/lawView.do?hseq=45681&lang=ENG (accessed: 15.12.2020).

¹⁷ Korean Civil Act § 186 (Effect of Changes in Real Rights over Real Properties).

A *wolse* is an obligational claim by nature even after registration¹⁸. The Supreme Court also recognizes that a registered right of lease not only entails a right of use but also serves as security for the claim for return of the lease deposit¹⁹.

The problem is that *chonse* is rarely registered in the real property lease market. While a registration could be completed with written consents of both tenant and landlord, most landlords of *chonse*, not to speak of *wolse*, do not agree to registrations. This practice makes the “non-registered *chonse* tenants” very vulnerable in case of resales or public auctions of the leased properties and/or default of the landlords who are also debtors of the huge lump sum deposits to the *chonse* tenants.

As the national economy and real estate market continues to fluctuate, many *chonse* landlords fail to return the lump sum deposit back to the tenants in a timely manner and some even go through the default, bankruptcy, and/or the foreclosures and compulsory public auctions. Most non-registered *chonse* tenants are widely exposed to the very critical risk of default of the lump sum deposits²⁰, which urges a reform of the Korean lease law system, the legislation of the Housing Lease Protection Act in 1981 and the Commercial Building Lease Protection Act in 2001.

2. Legal Protection of non-registered *chonse* Tenants

2.1. Housing Lease Protection Act

The Housing Lease Protection Act provides a lessee or tenant with a remedy of security. The transferee (including any person who has succeeded to the right to lease) of a leased house is deemed to have succeeded to the status of the lessor²¹. Furthermore, the leasehold takes effect against any third party even though the leasehold is not registered on the real estate registration record, upon the condition that (1) the lessee is provided with possession of the leased house and (2) completes the resident registration²². The resident registration is deemed made at the time of the move-in report to his/her domicile community center according to the Resident Registration Act²³. This is called “opposing power” of the leasehold, which could be understood as a kind of perfection procedure of the leasehold interest, which means that a potential buyer of the property needs to check either there is anyone registered as a resident in the property to be bought and the information on registered residents open for public in South Korea.

The Housing Lease Protection Act also provides remedies to recover the deposits from the landlord, which means that a tenant could be entitled to receive the repayment of the deposit from the converted price proceeds of the leased house at an auction which

¹⁸ Registration of Real Estate Act § 74 (Matters to Be Registered in Leasehold Interests, etc.). If registered, a *wolse* is secured against the third parties but still not assignable without consent of the landlord.

¹⁹ Upon expiration of the lease term, the right of use is extinguished immediately even without cancellation of the registered right of lease. However, the security right is not extinguished immediately, so that the lessee may refuse a request of the lessor to cancel the registration even after expiration of the lease term, until the lessee recovers the lease deposit. Supreme Court 99Da67079, February 26, 2002.

²⁰ It is also unfair that tenants have few difficult options such as a long lasting lawsuit to reduce and get the difference of the deposit back when the prices go down and deposits should be adjusted according to the market prices, while it is very easy for landlords to increase the deposit at the next renewal when the prices go up.

²¹ Housing Lease Protection Act § 3 (4).

²² Housing Lease Protection Act § 3 (1).

²³ Resident Registration Act § 10(1). Available at: https://elaw.klri.re.kr/kor_service/lawView.do?hseq=44509&lang=ENG (accessed: 15.12.2020).

is conducted under the Civil Execution Act²⁴ and a public auction sale under the National Tax Collection Act²⁵. The tenant can receive the repayment above in preference to any junior obligees and other creditors, upon the condition that (1) the tenant meets the requirements for the opposing power above and additionally (2) obtains a “fixed date time stamp” on the lease contract document²⁶. The fixed date time stamp can be obtained at the domicile community center, a notary public office²⁷ or by a clerk of the courts as well²⁸. In addition, the tenant could file an application for auction of the leased property himself/herself based on the final and conclusive judgment on the lawsuit demanding the repayment of deposit²⁹.

[Example 4] L4 entered into a *chonse* agreement with T4 as follows:

(1) *chonse* deposit shall be \$ 300,000 and

(2) *chonse* shall begin 1st of May 2019 and end 30th of April 2021.

As soon as T4 deposits \$ 300,000, T4 shall report residence and get a fixed date time stamp on the *chonse* agreement at the legion community office. This process, which can be conducted by the tenant himself/herself and does not require any consent by the landlord, makes T4’s right legally secured against third parties even without any registration on the real estate record.

Due to the legislation of the Housing Lease Protection Act, most tenants have been relieved of the landlords’ default risks. However, risks still remain for many tenants who are not protected. For one, tenants leading indigent lives without large amount of lump sum deposits cannot afford decent leased homes. They have no other choice but to get very cheap risky rental homes, which are very often already mortgaged near to the maximum of the property value. In this case, tenants are not protected as the other mortgagees have priorities in an auction. As a result, citizens who struggle financially desperately need additional protection, which is also regulated in the Act as the so-called “small amount tenant” protection. These tenants are entitled to receive a partial repayment of a specified amount of the deposit in preference to other persons holding the security rights with priority in the leased house, including prior mortgagees, upon the condition that (1) the tenant satisfies the opposing power requirements above and (2) finishes the move-in report before an application for auction of the leased property³⁰. The scope of this special preferential protection, that is the range of small amount tenants and the secured partial amount, is prescribed by the Enforcement Decree³¹. To get an equitable balance of the interests between small amount tenants and prior mortgagees, the total amount of special preferen-

²⁴ The procedure of compulsory auction as a civil execution is regulated in the Civil Execution Act § 80–162, and the auction as an exercise of security rights is regulated in § 273 (1). Available at: https://elaw.klri.re.kr/kor_service/lawView.do?hseq=41807&lang=ENG (accessed: 15.12.2020).

²⁵ The procedure of public auction sale is regulated in the National Tax Collection Act § 61–79. Available at: https://elaw.klri.re.kr/kor_service/lawView.do?hseq=49349&lang=ENG (accessed: 15.12.2020).

²⁶ Housing Lease Protection Act § 3–2(2).

²⁷ Notary Public Act § 2. Available at: https://elaw.klri.re.kr/kor_service/lawView.do?hseq=46308&lang=ENG (accessed: 15.12.2020).

²⁸ Private documents which contain fixed date stamps by notaries public or clerks of the court have authentic power concerning the date of preparation thereof. Korean Civil Act [Addenda] § 3 (1).

²⁹ Housing Lease Protection Act § 3–2 (1).

³⁰ Housing Lease Protection Act § 8 (1).

³¹ Housing Lease Protection Act § 8 (2). For example, in Seoul Metropolitan City, small tenants with maximum deposit of 110 million won are entitled to the preferential repayment of maximum 37 million won as of 15. Dec. 2020. Enforcement Decree of the Housing Lease Protection Act § 10–11. Available at: https://elaw.klri.re.kr/kor_service/lawView.do?hseq=52144&lang=ENG (accessed: 15.12.2020).

tial protection should not exceed half of the price of the auctioned property in case there are more than one small amount tenant³².

2.2. Commercial Building Lease Protection Act

As the Housing Lease Protection Act has been working more than satisfactorily for middle and under-middle class citizens without their own properties in providing security and stability of the country's residential life, the government expanded this protection system to commercial building lease area. Necessity for the protection of the lump sum deposit of commercial building tenants is not less than that of residential house tenants, which led to the legislation of the Commercial Building Lease Protection Act in 2001³³.

The Commercial Building Lease Protection Act provides almost identical remedies to secure the right of tenants, the opposing power and the remedies related with auctions of the building³⁴. The main difference is that this Act limits the scope of protected leasehold according to the amount of the security deposit³⁵. In case of half-*chonse* or *wolse*, the converted amount of the monthly rent should be added to the deposit, which means the monthly rent is converted to deposit by calculating the interest rate according to the enforcement decree³⁶. Commercial tenants are required to file an application for business registration as an entrepreneur for the leased property with the tax office, in contrast to the residential tenant's move-in report to the domicile community center. Small amount commercial tenants are also additionally protected likewise as is in the housing lease protection system, although the scope is differently regulated by the enforcement decree³⁷.

[Example 5] L5 has a commercial building unit in Seoul, for which the market sale price is \$ 1,000,000. L5 entered into a half-*chonse* agreement with T5 as follows:

Half-*chonse* deposit shall be \$ 300,000 and

Monthly rent shall be \$ 1,800 and

Half-*chonse* shall begin 1st of May 2019 and end 30th of April 2021.

First, it should be determined whether this leasehold is in the scope of protection by calculating the converted deposit amount. The monthly rent of \$ 1,800 is converted to \$ 180,000 ($\$1,800 \times 100 = \$180,000$)³⁸ and then this converted amount is added to the original deposit \$ 300,000, making the total converted deposit \$ 480,000, which is defi-

³² Housing Lease Protection Act § 8 (1). For more discussions on the additional protection of small amount tenants, see: *Son Y.-W.* Study on the "right to claim increases and decreases in rent" and "protection of small deposits" system under the housing lease protection act // *Hanyang Journal of Law*. 2018. Vol. 8, no. 2. 52–58. Available at: http://hylaw.hanyang.ac.kr/html/02-collection/board?tb_name=eng_journal (accessed: 15.12.2020).

³³ Commercial Building Lease Protection Act. URL: https://elaw.klri.re.kr/kor_service/lawView.do?hseq=49069&lang=ENG (accessed: 15.12.2020).

³⁴ Commercial Building Lease Protection Act § 3 (1), § 5 (2).

³⁵ This Act should be applied to any commercial leasehold, the deposit of which is not more than 900 million won in Seoul Metropolitan City area, whereas 690 million won in Busan Metropolitan City area. Enforcement Decree of the Commercial Building Lease Protection Act § 2 (1).

³⁶ The multiplier for the conversion is 1/100 as of 2020. Enforcement Decree of the Commercial Building Lease Protection Act § 2 (3).

³⁷ Commercial Building Lease Protection Act § 14. For example in Seoul Metropolitan City, small commercial tenants with maximum deposit of 65 million won are entitled to the preferential repayment of maximum 22 million won as of 15. Dec. 2020. Enforcement Decree of the Commercial Building Lease Protection Act § 6–7.

³⁸ Commercial Building Lease Protection Act § 2 (2). The multiplier for the conversion is 1/100 as of 2020. Enforcement Decree of the Commercial Building Lease Protection Act § 2 (3). Available at: https://elaw.klri.re.kr/kor_service/lawView.do?hseq=50761&lang=ENG (accessed: 15.12.2020).

nately in the Decree's protection scope of 900 million won³⁹. T5's leasehold could be secured according to the Act, but cannot be additionally protected as a small amount commercial tenant. As soon as T5 deposits \$ 300,000, T5 should file an application for business registration as an entrepreneur for the leased property at the region tax office and get a fixed date time stamp on the *chonse* agreement for perfection.

[Example 6] B5 has a mortgage loan of \$ 800,000 registered on the leased building before T5's *chonse* is perfected as above and the other facts are the same as **[Example 5]**. L5 became insolvent and B5 filed an auction for the leased building, which was sold at \$ 900,000 in the auction procedure. Out of \$ 900,000 the auction court distributes \$ 800,000 to B5 who has priority in time over T5 and the remaining \$ 100,000 is to be distributed to T5. In this case T5 cannot collect the deficit balance of \$ 200,000 from the auction proceeds, which remains as a kind of non-performing loan. T5 is not eligible for the additional protection as a small commercial tenant because T5's converted deposit amount is above the protection scope.

3. Social and Economic Analysis

3.1. Implications of *chonse* to Korean People

A *chonse* tenant can save quite an amount by not being burdened with monthly rent payment, where the amount saved could be used towards down payment to get his/her own property. For instance, T1 of **[Example 1]** does not pay monthly rent as a result of the lump sum deposit of \$ 300,000, while T2 of **[Example 2]** has to pay \$ 3,000 every month, which means T1 can save \$ 36,000 more than T2 each year. On the other hand, L1 needs to get more with the received lump sum *chonse* deposit than the total monthly rent income which L2 receives with *wolse* terms. In other words, it could be stated that the investment opportunities and risks are carried by the landlords, while a certain fixed rate of return is allowed to the tenants in *chonse* transactions. The break-even point depends on the market interest rate or the expected rate of return on alternative investments, which could be assumed around 10–12 % annually in these examples above.

The *chonse* system definitely has been working towards the benefit of many Korean middle class citizens, especially young singles and couples, in their goals of becoming a "home-owner". However, as long as *chonse* system has been flourishing, some of the contemporary advanced financial systems such as small amount financial investment products and long-term mortgage loans have not been established successfully in South Korea. Korean middle class tenants definitely prefer *chonse* as their opportunities and success rate for other investments are limited, while landlords usually have more diverse investment opportunities including purchase of an additional house coming with the assignment of existing *chonse* terms attached. As South Korea's financial institutions have not supplied enough long-term mortgage loans⁴⁰, *chonse* transaction has been working as a tool of leveraged purchases for many prospective new home buyers, both tenants and landlords. It could be understood that a lump sum deposit works as a bridge loan for a new home buyer, while the tenant's lump sum deposit is protected by a kind of "special lien" issued against the property for the amount given subject to the registration or re-

³⁹ Enforcement Decree of the Commercial Building Lease Protection Act § 2 (1). Foreign exchange rate is approximately 1,088 Korean Won vs 1 US \$ as of Dec. 2020, which makes the scope borderline of 900 million won (in Seoul Metropolitan City area) \$ 826,825.

⁴⁰ The short-term mortgages with some annual renewals to the resale of the properties, also known as "balloon payment mortgages", are still common in the mortgage market of South Korea.

port as presented above. This is the primary reason why the Korean Civil Act categorizes *chonse* not only as a usufruct but also a security right.

It is true that *chonse* is an excellent way for new home buyers to finance the purchase of a new home and reap large profits within just a few years, especially between the 1970s and the 2000s during which time real estate prices rapidly and consistently rose⁴¹. *Chonse* transactions grew sharply when the Korean society rapidly transformed into an urban industrialized economy facing two large problems of housing and financing, both of which were elegantly solved by the *chonse* system⁴². It is also pointed out that the *chonse* system is popular for two main reasons, one of which is the financial system of South Korea which has not been so beneficial to the middle class home buyers, and the other reason being the continuous and rapid increase in real estate prices, which is now being concerned as a housing bubble. South Koreans tend to invest the bulk of their savings in real properties especially in residential condominium units⁴³.

3.2. Economic Impact on Real Estate Market and Government Policy

The main factor which has kept the *chonse* system sustainable is the high interest rate or investment return rate of the market. While the annual-return of 10 % could be desirable for landlords, *wolse* is more often used during times of lower interest rates. The prolonged global low interest rate in the last few decades is distracting the landlords from *chonse*. As the economic situation is changing in this direction, the landlords are slowly but continuously heading towards *wolse* or half-*chonse* from *chonse*, as interest rates fell to near-zero, prompting the landlords towards monthly rent income⁴⁴. Another option for landlords might be to raise the amount of lump sum *chonse* deposit as the interest rate goes down. New tenants who are looking for *chonse* are lining up as landlords refrain from leasing their property under the present *chonse* terms. Current *chonse* tenants are compelled to pay additional monthly rents or add some lump sum deposits. These emerging trends indicate a sense of urgency to the Korean middle class *chonse* tenants, as they are not financially ready to pay monthly rent or a higher lump sum deposit, which are usually provided by the tenant loan from the financial institutions with a fairly low rate as the deposit may be taken as collateral⁴⁵.

The other factor is the increasing house prices, which is also slowly plateauing. For decades, landlords continuously and successfully invested in the real estate market using *chonse* lump sum deposit as leverage. Their main source of profit has been one time lump

⁴¹ Kwon Y., Lee Y.-S. Legal analysis of traditional leasehold in Korea (*chonsegwon*) from a comparative legal perspective. P.282.

⁴² It takes \$ 290,000 in cash to rent an apartment in Seoul // Quarts. March 10, 2014. Available at: <https://qz.com/183412/koreas-crazy-system-for-renting-apartments-is-driving-the-country-deeper-into-debt/> (accessed: 15.12.2020).

⁴³ More than W2.1 quadrillion is invested in Korea's real estate market in one way or another, surpassing the country's total GDP of W1.9 quadrillion (Investment in Real Estate Exceeds GDP // The Chosunilbo. October 8, 2020. Available at: <https://english.chosun.com/m/news/article.amp.html?contid=2020100801444> (accessed: 15.12.2020)).

⁴⁴ The Bank of Korea has also kept the benchmark interest rate at a record low of approximately 2 % to grapple with the lingering financial crisis (Poorer Households Face Higher Housing Costs Than the Rich // The Chosunilbo. August 25, 2020. Available at: <https://english.chosun.com/m/news/article.amp.html?contid=2020082502010> (accessed: 15.12.2020)); (Tenants Face Hard Times From Rising Jeonse Payments // Korea Times. July 29, 2009. Available at: https://www.koreatimes.co.kr/www/tech/2022/03/419_49312.html?RD (accessed: 15.12.2020)).

⁴⁵ Outstanding *chonse* loans extended by the country's five major lenders came to 103.3 trillion won (US \$ 94 billion) as of end-November 2020, up nearly 23 trillion won from 2019 (Major banks' home rental loans grow at record pace this year // Yonhap English News. December 3, 2020. Available at: <https://en.yna.co.kr/view/AEN20201203000900320> (accessed: 15.12.2020)).

sum capital gain from resales of the leveraged properties instead of a long term stable rent income. The taxation on the capital gain from the real estate market is one of the most critical and sensitive issues in Korean society, as this “unlabored windfall income” has been criticized as the origin of economic inequality, discord and conflict between social classes, corruption, and many other major social problems in South Korea.

Recently, the Korean government is making every effort to cool down the real estate market. One of the traditional policies is increasing the interest rate, which is impractical under the global low interest rate circumstances. Another orthodox policy is regulating loans. The government has been introducing many strong lending rules capping and regulating mortgage loans, including LTV (Loan to Value ratio), DTI (Debt to Income ratio), and finally DSR (Debt Service Ratio)⁴⁶. Unfortunately, these traditional measures have not been so effective in South Korea, the main reason being that the speculative home buyers are not halted by the loan regulation as they can use *chonse* lump sum deposit as an alternative personal loan, which is not heavily regulated by the existing lending rules.

Moreover, as the interest rate continues to decrease, the amount of *chonse* deposit is rising almost as high as the resale price, which means that speculative buyers such as multiple-home owners could buy an additional home with just a small amount of gap between the deposit used as leverage and the resale price of the home, also known as “gap investment” in South Korea⁴⁷. These speculative transactions are stimulating market prices. The government, foreseeing a speculative bubble, has introduced more measures to cool the market including mortgage ban on properties of specific over-heated regions, increasing property taxes for expensive homes and owners of multiple properties, as well as capital-gains on short-term resales⁴⁸. It is undeniable that the *chonse* system is a significant obstacle to implementing government policies involving the real estate market.

Conclusion

As presented and discussed above on the development and popularity of *chonse* and its historical and institutional settings, the *chonse* system plays an essential role in the housing lifestyle of South Korean families especially in metropolitan areas. *Chonse* has been the most conventional way of savings and investments for property accumulation for many middle class families for centuries. Due to the fact that the South Korea continues to change in economic development, financial system reform, globalized lifestyle and home living, and most of all its population, the difficulty remains in predicting the future trajectory of the *chonse* system. Among these changes, low interest rate and stabilization of the residential real estate prices as well as the flourish of long-term mortgages are gradually and remarkably shrinking the dominant portion of *chonse* coupled with the expansion of ordinary leasehold *wolse*.

The South Korean society is facing more complex public concerns to enhance the welfare of the tenants and to provide safe and profitable ways of savings and investments other than leveraged residential purchase. One of the most urgent projects might be providing a sufficient supply of decent lease and *chonse* homes by public entities including government, municipalities, and other public institutions. Such supplies have been left

⁴⁶ S. Korean banks adopt stricter lending rules for overdraft accounts // Korea Herald. November 20, 2020. Available at: http://news.koreaherald.com/view.php?ud=20201120000694&ACE_SEARCH=1 (accessed: 15.12.2020).

⁴⁷ S. Korea's housing market polarization grows // Korea Herald. November 23, 2020. Available at: http://news.koreaherald.com/view.php?ud=20201123000921&ACE_SEARCH=1 (accessed: 15.12.2020).

⁴⁸ Efforts to rein in house prices are fueling discontent in Seoul // The Economist. August 29, 2020. Available at: <https://www.economist.com/finance-and-economics/2020/08/27/efforts-to-rein-in-house-prices-are-fuelling-discontent-in-seoul> (accessed: 15.12.2020).

mainly to private sectors for centuries in South Korea, unlike many other countries that have more public than private sectors⁴⁹. Balancing the negotiating power of the tenant and landlord is another critical task of leasehold legislation reform, a part of which was done in 2020 but still facing quite a strong resistance from landlords and conservatives⁵⁰.

Although *chonse* is a unique and indigenous market response to economic conditions of South Korea, it is also inevitable for foreign immigrants and investors to understand the main features and trend of the housing market of South Korea⁵¹. Furthermore, this unique South Korean system could be an alternative solution for other societies that are under similar economic environments to relieve the emerging housing problems in the midst of a rapidly expanding economy. Further research and discussions are warranted to reach a final evaluation of this singular legal system for real property leasing.

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⁴⁹ President of South Korea announced that the government will supply "enough" public rental homes, with the goal of providing 2.4 million homes by 2025 (Moon vows more, better public rental homes amid housing market instability // Yonhap English News. December 11, 2020. Available at: <https://en.yna.co.kr/view/AEN20201211005651315> (accessed: 15.12.2020)).

⁵⁰ The three new tenant protection laws authorize house tenants to extend lease period by another two years while imposing a 5 % cap on deposit hikes (Turmoil over 'jeonse' // Korea Times. November 4, 2020. Available at: https://www.koreatimes.co.kr/www/opinion/2020/11/202_298741.html (accessed: 15.12.2020)).

⁵¹ Adventures in Buying Our First Home // Angloinfo. November 4, 2013. Available at: <https://www.angloinfo.com/blogs/south-korea/seoul/bibim-korea/adventures-in-buying-our-first-home/> (accessed: 15.12.2020); Rental agreements: Short and long-term leases in South Korea // Justlanded. Available at: <https://www.justlanded.com/english/South-Korea/South-Korea-Guide/Housing-Rentals/Rental-agreements> (accessed: 15.12.2020); Information on renting accommodation and paying a deposit when renting property in South Korea // Angloinfo. Available at: <https://www.angloinfo.com/how-to/south-korea/housing/renting-accommodation/rent-deposits> (accessed: 15.12.2020).

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Чонсе — уникальный тип аренды недвижимости в Корее

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Чонсе — это форма найма, характерная для Республики Корея, согласно которой наниматель выплачивает наймодателю большую сумму денег в качестве депозита, без внесения ежемесячной платы. При этом чонсе является самой распространенной формой найма среди южнокорейских граждан среднего класса, не имеющих права собственности на недвижимость. Такая форма найма применяется как для жилых домов, так и для коммерческих помещений. Автор иллюстрирует уникальность данного института, подробно анализируя его основные черты и связанные с ним правовые характеристики. Помимо прочего, чонсе имеет функции системы финансирования для собственников недвижимости, поскольку в данном случае собственники сданного в наем имущества уподобляются заемщикам в договоре займа, срок которого совпадает со сроком найма. Наниматель, который на протяжении этого срока владеет объектом чонсе как кредитор, имеет не только usufruct, но и право залога. После короткого обзора правовых особенностей и значения чонсе в истории развития Республики Корея автор дает критическую оценку его меняющейся роли в современном корейском обществе. В частности, такие факторы, как продолжение экономического роста страны, реформы в сфере финансирования, глобализация жизненного стиля корейцев и образа их домашнего проживания, сравнительно низкие ставки, распространение и рост объема долгосрочных ипотек, а также сокращение и старение населения, необходимо учитывать для определения меняющейся роли правового института чонсе в Корее. Современное южнокорейское общество сталкивается с очень сложными общественными проблемами, связанными с повышением благосостояния арендаторов и обеспечением безопасных и прибыльных способов сбережений и инвестиций, отличных от покупки жилья с привлечением заемных средств. Одним из наиболее неотложных проектов может быть обеспечение достаточного предложения

достойного съемного жилья государственными структурами, включая правительство, муниципалитеты и другие государственные институты. Жилые помещения в Южной Корее на протяжении веков предоставлялись в наем в основном частным сектором в отличие от многих других стран, где государственного сектора больше, чем частного. Автор надеется, что данная научная работа поможет иностранцам, малознакомым с правопорядком Республики Корея, лучше понять фундаментальные элементы ее правовых институтов.

Ключевые слова: чонсе, договор найма жилого помещения, регистрация, приоритет, финансирование недвижимости, сделка с недвижимостью.

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