22/07/2019

Kevin Anderson MP
Minister for Better Regulation and Innovation

Sir,

Retirement Villages - Exit Entitlements and Recurrent Charges Cap

Thank you for the opportunity to comment on the examination of A reform to ensure payment of exit entitlements within set time frames and A reform to limit recurrent charges.

I would like to make some primary points at the start for they are pivotal to the examination of the proposals -

1. EXIT ENTITLEMENTS - The village operator is not being asked to pay out his own money or money he does not have. He was given this money within the in-going payment by the occupant prior to a grant of occupancy. The operator is merely being asked to repay this loan/refundable amount earlier.

   In a loan/lease village with 150 units, a unit value of $983,899.00 and a deferred management fee of 36%, this pool of interest free money held by the operator would be an amount in the order of $76.8 million dollars. The operator being well placed to return the refundable amount earlier.

2. RECURRENT CHARGES – The village operator is being asked to pay a small contribution to maintenance/management costs of their own property

3. PROPERTY OWNERSHIP – An important determining factor is who is the 'owner' of the property. Currently these costs are being transferred from a commercially driven property owner to the elderly occupants. This transfer of cost being enshrined in statute.

Important to understand which of the parties approaches these reform proposals from a position of financial strength or financial weakness. I am focusing on the capacity of the property owner to meet the cost of these modest proposals and the diminishing capital base of the retiree over the period of their occupancy.

In a Loan/lease - Loan/licence retirement village the following components are the 'true' cost to a retiree of living in a village. This 'true' cost not identified by many retirees in their initial decision making.

In a loan/lease retirement village the occupant -

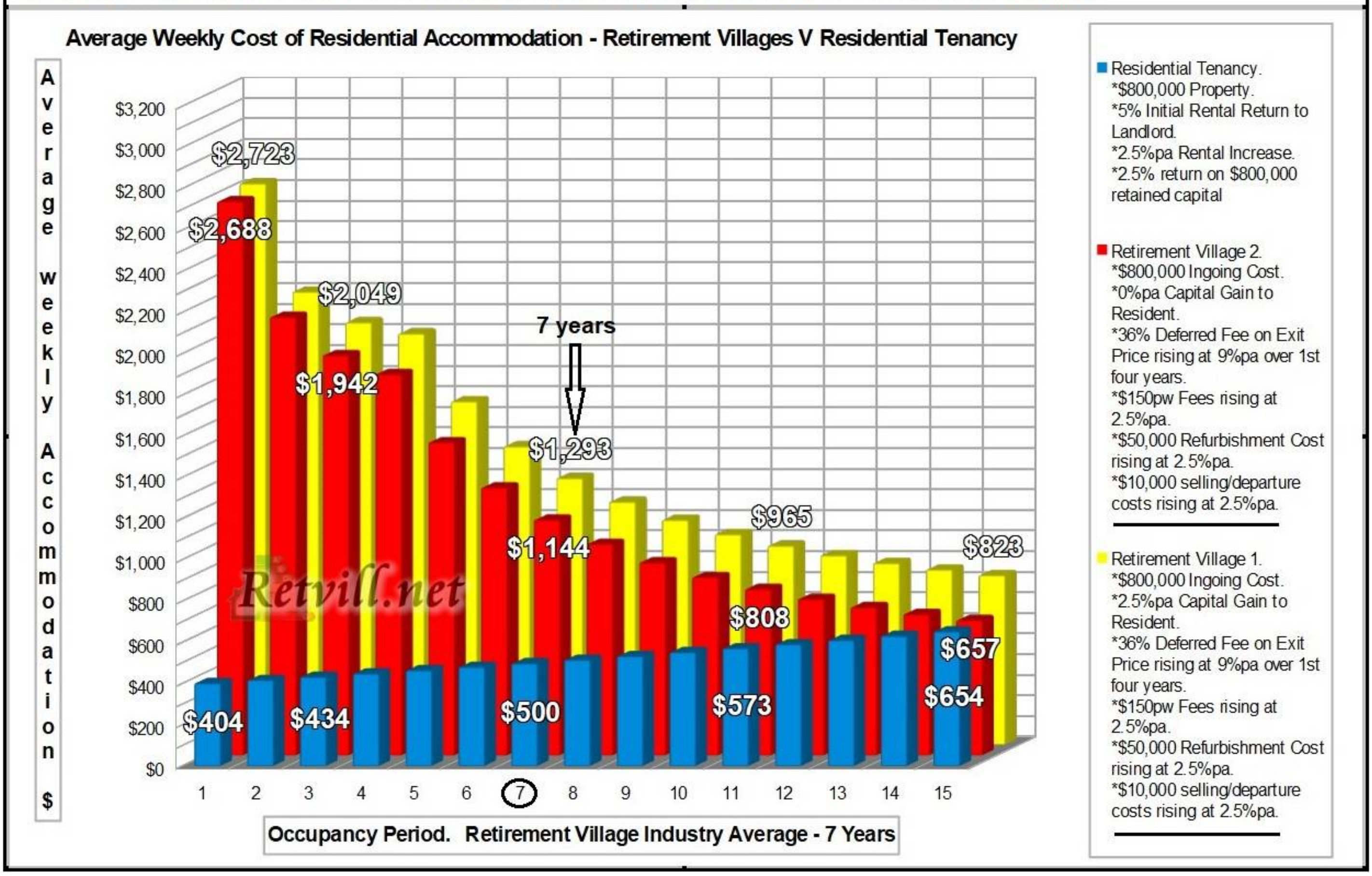
1. Pays an in-going amount not to obtain ownership simply a conditional right to occupy. This in-going amount can often be commensurate with an actual 'buy' price for a similar standard property.
2. Pays a so named 'Deferred Management Fee' upwards to 40% of this in-going payment. *Claimed by the industry to compensate the operator for discounting the entry cost. Factual?*
3. Loans the refundable amount *(in-going payment minus the deferred management fee)* to the village owner at 0% interest for the duration of their occupancy.
4. Suffers a loss-of-earnings on this refundable amount over the period of occupancy.
5. Suffers an inflationary devaluation of this refundable amount over the period of occupancy.
6. May or may not be granted access to any capital appreciation in the value of the unit occupied. Where granted access to any capital gain the occupant will be responsible for any capital loss.
7. Pays to fully maintain an asset not owned by the retiree.
8. Pays to fully operate/manage an asset, not owned by the retiree.
9. Pays to fully refurbish an asset, not owned by the retiree.
10. Pays the selling costs of an asset, not owned by the retiree.
11. Pays a diminishing but nevertheless substantial 'lifestyle' premium above the net market value of the residential accommodation.

1. Examination of the actual full underlying cost to a retiree of living in a retirement village.

The following chart examines the financial position of a retiree by calculating the full weekly financial cost to the retiree of living in a retirement village. A village where ownership of the unit is not transferred, where the resident is only granted a conditional right to occupy.

The most direct comparison for this type of lease/tenancy residential accommodation is to compare it with the market driven cost of a traditional residential tenancy. Comparing a retiree with $800,00.00 capital who pays an in-going amount to enter a retirement village, with that of a retiree who retains their $800,000.00 capital base for investment and takes a traditional residential tenancy.

Loan/Lease, Loan/Licence Village - The following chart shows the average weekly cost of living in a retirement village compared to a standard residential tenancy. ***No allowance has been made for the annual CPI devaluation of the Loan amount (Ingoing Amount Paid minus the Deferred Management Fee) held by the operator at 0% cost and due for repayment to the outgoing resident on their departure from the village.***



The chart shows that the full financial cost to the retiree of living in Retirement Village 1 is -

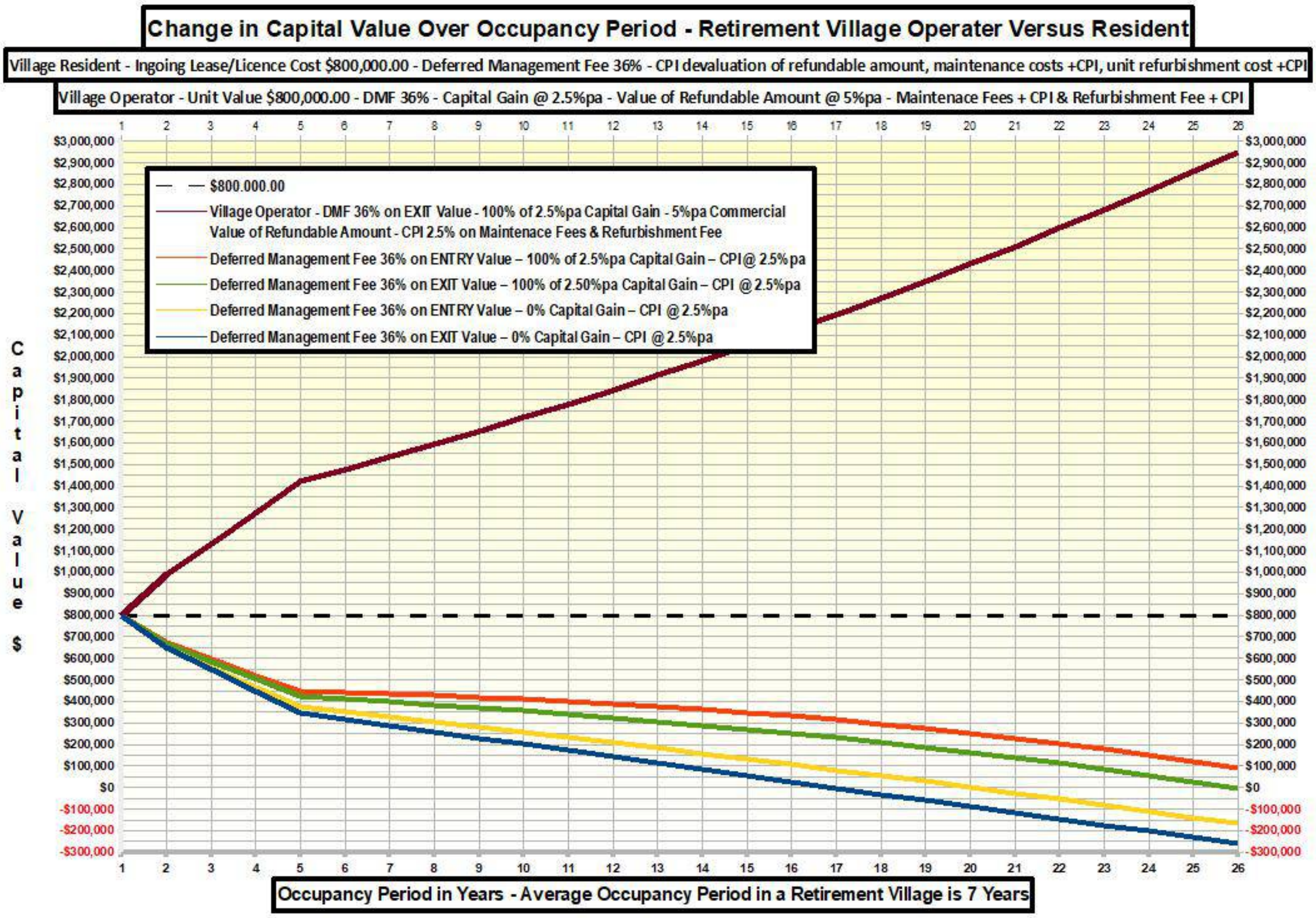
- In Year 1 - 6.74 times that of a traditional residential tenancy.
- In Year 3 - 4.72 times that of a traditional residential tenancy.
- In Year 7 - 2.58 times that of a traditional residential tenancy.
- In Year 11 – 1.68 times that of a traditional residential tenancy.
- In Year 15 – 1.26 times of that of a traditional residential tenancy.

Summation - The chart clearly shows that retirees living in a retirement village to be in a vastly inferior financial position to retirees retaining their original capital base and executing a traditional residential tenancy.

Conclusion – Given that the average occupancy period in a retirement village is only 7 - 10 years, retirees living in a retirement village are poorly placed financially, and deserve respite from, these financial imposts under review.

2. Examination of the change in capital values for both the village occupant and the operator.

The following chart displays the change in Capital Value for a loan/lease retirement village operator as compared to a retirement village resident, based on the initial $800,000.00 in-going payment.



Summary - The chart dramatically shows that **t**he long term financial position of the village operator becomes vastly superior to that of a resident over the period of occupancy. Only strong capital gains can stave off destruction and in some cases complete destruction of the original capital base of the retiree.

The chart shows that in fact the matter under consideration should be -

Where an outgoing village resident is not the 'owner' of the property, but simply the lessee/tenant, the complete removal of any exit entitlement waiting period.

Conclusion – Given the diverse financial strengths of the two parties, the village operator is well placed to absorb any minor financial impost from the proposals.

'Greatest untouched consumer protection issue'

https://www.smh.com.au/business/banking-and-finance/calls-for-federal-inquiry-into-retirement-villages-amid-aveo-scandal-20170627-gwz8nb.html

Professor Fels described the retirement village rort as the greatest untouched consumer protection issue of this century and called for urgent enforcement action from governments and regulators.

"These days we talk of vulnerable and disadvantaged consumers but the aged are possibly the most important category," Prof Fels said.

3. The accumulating change in the respective capital values of the village occupant and the village operator.

The following chart shows the accumulating change in total capital value for the resident and the operator measured over 7 year periods for a loan/lease retirement village. These figures are for just one village of 150 units, one has to consider what the industry wide figures for New South Wales would be.

After just 7 years the residents will have suffered a reduction in capital value of $43.2M dollars, whilst at the same time the village operator has had an increase in capital value of $70.7M dollars. The total amounts after 28 years of operation are, the operator plus $396.5M whilst the residents minus $242.0M. The other number of note is the size of the pool of interest free money held by the operator – At year 7, $76.8m. At year 14, $94.4m. At year 21, $116.1m. At year 28, $142.8m.

Accumulating Change in Capital Wealth – Retirement Village Operator Versus Residents

Measured at 7 Yearly Intervals	Year 0	At Year 7	At Year 14	At Year 21	Year At 28
Ingoing Payment by New Resident per Unit	$800,000.00	$983,899.09	$1,210,071.78	$1,488,235.66	$1,830,342.14
Value of the 150 Units	$120,000,000.00	$147,584,863.85	$181,510,766.98	$223,235,348.61	$274,551,321.09
Property Capital Gain Paid to Operator – 3%pa compounded		**$27,584,863.85**	**$33,925,903.13**	**$41,724,581.62**	**$51,315,972.48**
Deferred Management Fees Paid @ 36%		**$43,200,000.00**	**$53,130,550.99**	**$65,343,876.11**	**$80,364,725.50**
Accumulating Change – Operator	*Increase*	$70,784,863.85	$157,841,317.97	$264,909,775.71	$396,590,473.69
Accumulating Change – Residents	***Decrease*	*$43,200,000.00*	*$96,330,550.99*	*$161,674,427.10*	*$242,039,152.60*
Operator	***Increase***	**+$70.7M**	**+$157.8m**	**+$264.9M**	**+$396.5m**
Residents	*****Decrease***	**-$43.2M**	**-$96.3M**	**-$161.6M**	**-$242.0M**
Total Refundable Amounts Held by Operator at 0% cost		**$76,800,000.00**	**$94,454,312.86**	**$116,166,890.87**	**$142,870,623.11**
Ingoing Payment by New Resident @ Year 0		$800,000.00			
Deferred Management Fee Rate 36%		36.00%			
Deferred Management Fee Period in Years		4			
Capital Gain 3% pa compounded		3.00%			
Number of Units in Village		**150**			
Industry Average Occupancy Period in Years		7			
**Note:- Calculations do not include Maintenance Fees, Management Fees, Refurbishment Costs, Selling Costs, all paid on a property never owned by the retiree.*					
**Note:- Calculations do not include the CPI devaluation of the refundable amount payable on departure to the retiree held by the operator at 0% cost to the operator.*					

Summary. - The chart clearly shows that **t**he long term financial position of the village operator is vastly superior to that of the resident/s.

Note:- The chart does not include -

- *Maintenance/administration fees, refurbishment costs, selling costs paid by the occupant/tenant on a property not owned by themselves, but owned by the operator.*
- *A CPI devaluation of the refundable amount suffered by the occupant/s over the period of their occupancy.*

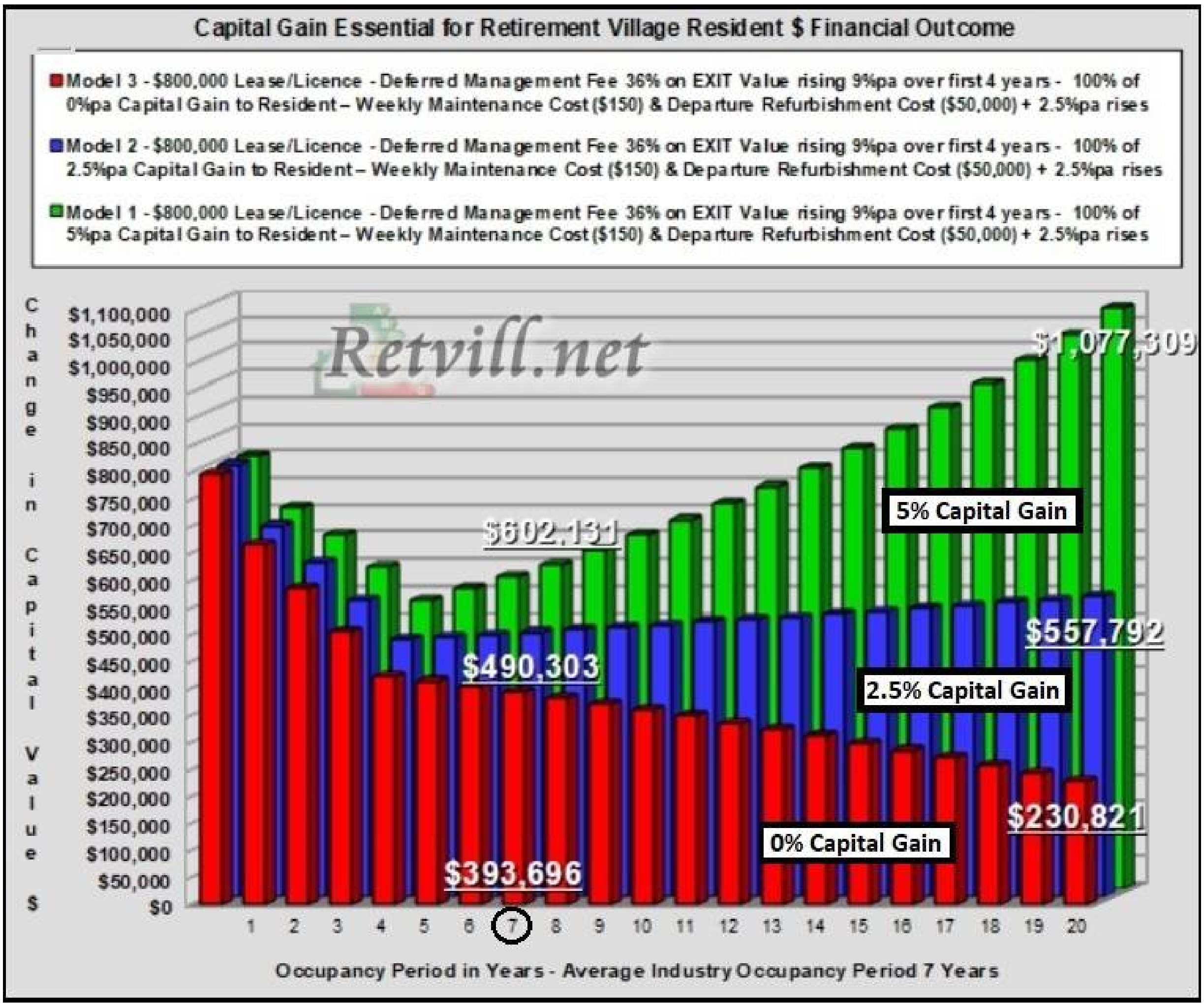
Conclusion - The village operator would be well placed to absorb any financial impost from the proposals. This substantial pool of 0% money held by the operator for repayment of the refundable amounts shows that an operator should be in a position to repay on the day of departure, let alone 6 months after departure.

"It would be interesting to know just how many retirees know, when they finally alight upon a leafy retirement village to while away their twilight years, that they are using their nest eggs to make a large, unsecured, interest free loan to a property developer"

Michael West - https://www.michaelwest.com.au

4. The impact of capital gain on the financial outcome for exiting retirement village residents.

The following chart displays the differing impacts of access to capital gain on the financial position of a resident departing a village. Strong rises in property values over past years have masked the negative financial impacts of retirement village living, see model 1 (green). Will those heady property years return and what is the impact if they don't. And what of retirees who are never granted access to any capital gain through their contractural arrangements. See model 2 (blue) and particularly model 3 (red).



Summary. - The chart clearly shows that having access to any increase in the value of the unit being occupied has a dramatic impact on the financial position of the retiree on departure from the village.

NOTE:- Any resident/tenant that has been granted access by contract to capital gain also carries the financial responsibility of any capital loss. A clear danger to retirees in the current residential property market and any longer term falling or flat property market.

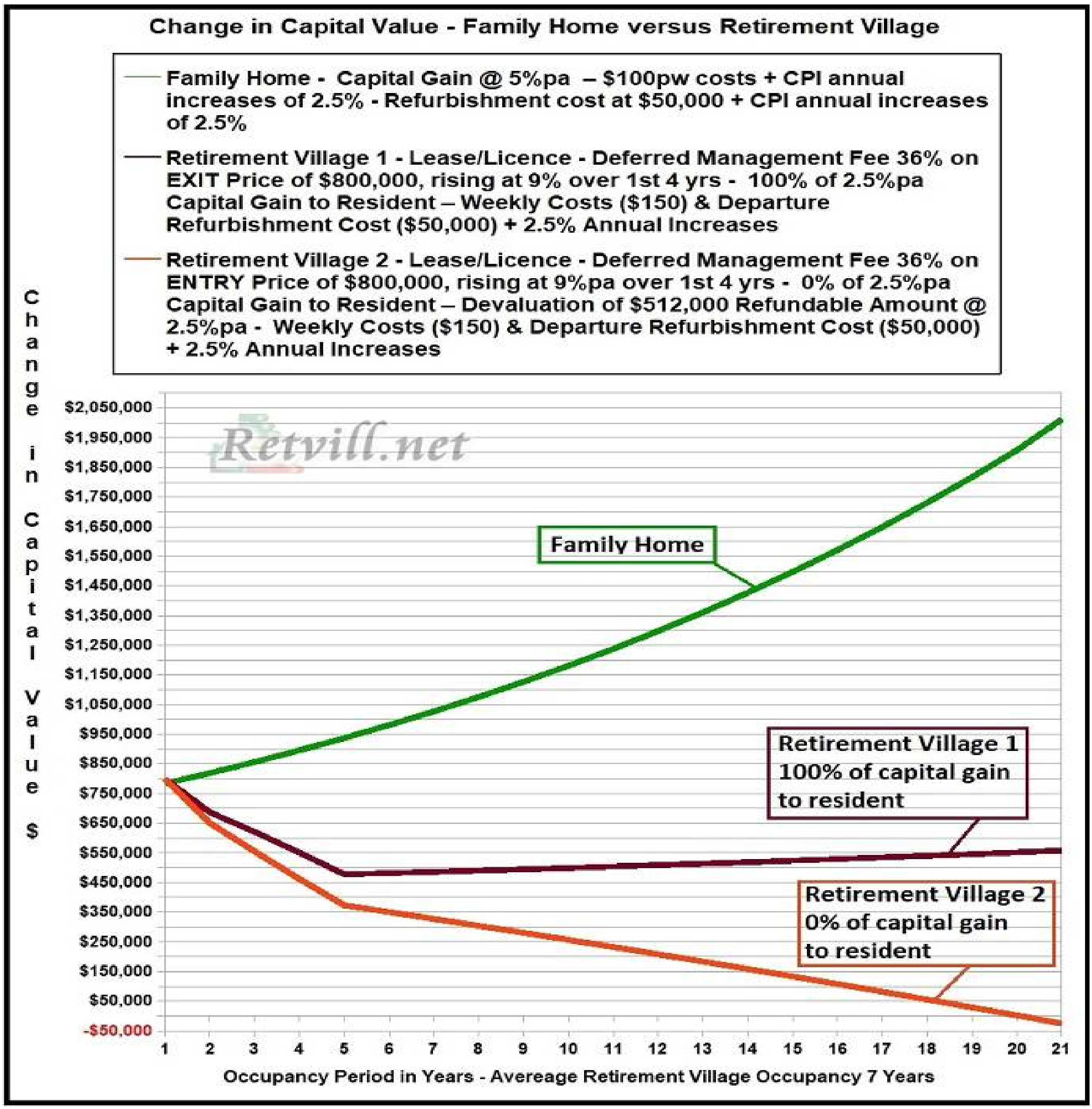
Conclusion - The heady days of continuous substantial rises in property values appear gone, the financial position of many retirees on leaving a retirement village will be dramatically worse than those of times past. Outgoing residents are less likely in the future to be able to absorb the costs of the current statutory period for the delay in repayment of the refundable amount and the current ongoing period of payment of recurrent charges.

5. SOCIAL PUBLIC COST - "This could in turn affect the availability of housing stock for younger people in the general housing market, as retirees decide to remain in their current premises longer."

The chart below displays differing impacts on the capital base of a retiree following a decision to either remain in the family home or 'downsize' as encouraged by governments into residential accommodation such as a retirement village.

Note the following -

- Any capital improvement in the value of the family home (green) is lost to the retiree.
- On entering a retirement village the capital value of the retiree will suffer a reduction as in the case of retirement village 1 and a significant reduction as in the case of retirement village 2. Both these impacts will have a dramatic negative impact on the financial capacity of the retiree to change direction either by choice or by circumstance or to help fund their aged pension, home care or residential aged care costs.



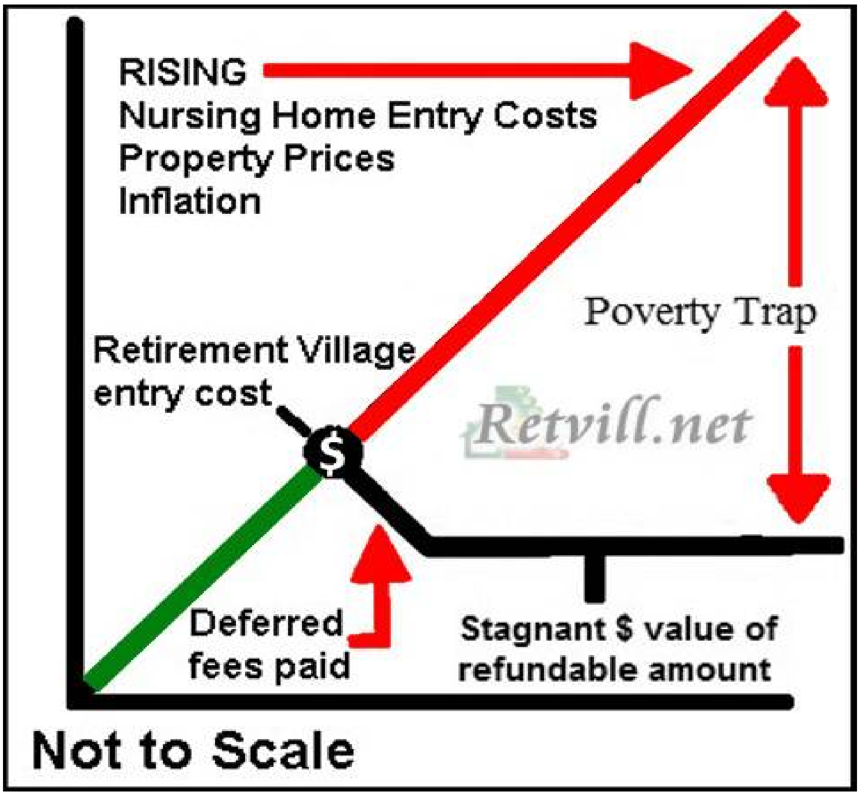
Summary - The encouragement by governments to retirees to surrender their capital wealth through the sale of the family home described as, to enable younger Australians access to the property market, is in my view self-defeating and -

1. In a time where the heady days of continuous substantial rises in property values appear gone, the financial position of many retirees on leaving a retirement village will be dramatically worse than those of times past.

2. These same retirees will come back after their so called 'party' years to these same 'younger Australians' seeking increased funding assistance for their aged pension, home care or residential aged care costs.

3. A 'downsize' move into a retirement village sends many retirees on a journey of destruction of their capital worth. Many residents already report being financially trapped and unable to move on with a different phase of their life, forced either by choice or circumstance.

4. In the future an increased number of retirees, having downsized from the family home, will find themselves in the so named 'poverty' or 'financial' trap of retirement villages such is the financial impact on their original capital base.



Conclusion – The data indicates that the best financial outcome for a retiree is to remain in the family home. Before moving into a retirement village retirees should have a full understanding of potential financial outcomes, sadly many do not.

6. The differentiation between rural and city villages.

As to the matter of differentiation between a metropolitan (6 months) and a rural (12 months) retirement village when it comes to the maximum period a refundable amount can be held by the operator/landlord, I feel this is to clearly discriminate against rural retirees, asking rural retirees to accept more of the cost of statutory delay periods for the payment of refundable amounts and recurrent charges than their city equivalent. This on a property not actually owned by the retiree but by a village operator seeking all the commercial rewards yet happy to deflect some commercial risk toward the occupants. Some of this deflection enshrined in legislation by government, surely just a financial 'free kick' to the operators.

To Conclude -

1. Would any state government consider introducing a law where in a standard residential tenancy a tenant on leaving the premises has to continue paying rent until the landlord has installed a new paying tenant.

2. Would any state government consider introducing a law where in a standard residential tenancy a tenant on leaving the premises the bond cannot be released until the landlord has installed a new paying tenant and received a new bond.

I think not although the many private property investors around Australia would love it to be so, yet this is the very scenario faced and for much more sizeable sums of money by outgoing residents of retirement villages.

Liquidity – ability to pay exit entitlements before sale.

Statement - "many operators would be unlikely to have sufficient liquidity to fund a multiple exit entitlement payments within a very short period."

Why? They already have the money to repay, they received the money within the in-going amount paid to obtain occupancy. The money was always due for repayment to the outgoing resident on their departure.

Statement - "Where insufficient liquid funds exist, operators would need to source the finance from a parent company or financial institution (loan)."

Why? They already have the money to repay, they received the money within the in-going amount paid to obtain occupancy. The money was always due for repayment to the outgoing resident on their departure.

There may be a small fall in income in the short term resulting from the holding of more shorter term working capital, but given the previous example of just 1 village with 150 x $983,899.00 units and holding a pool of $76.8m dollars of refundable money at zero cost, an increase of just 1% in interest rate returns increases the total return to the operator by $768,000.00 per annum.

The previous Minister for Better Regulation and Innovation Mr. Kean is reported as saying that he liked retirement villages because they came at no cost to government. It is a fact however that they come, as can be seen from the charts presented, at a significant capital cost to New South Wales retirees with long term financial and social consequences for these retirees.

Commercial operators come to the retirement village market place seeking the substantial commercial rewards available, yet they also seek and have been granted financial concessions by governments for some of the commercial risk. The cost of these concessions transferred directly to New South Wales retirees or their families. The benevolent provision of retirement housing for the older residents of New South Wales is no longer a dominant driving force behind the industry.

I see no increase in commercial risk for the village operators in these proposals, they simply involve an adjustment to the allocation of working capital and a minor increase in financial responsibility for the maintenance / management costs of their own asset. These proposals are a small, modest adjustment to the financial equilibrium between occupants and operators of retirement villages, currently heavily weighted in favour of the operators.

Thank you again for the opportunity to make a submission.

Yours faithfully,

Les Scobie.