SUBMISSION TO THE JOINT PARLIAMENTARY COMMITTEE ON LEGAL AND CONSTITUTIONAL AFFAIRS

1. SUMMARY

1.1 The self-care retirement village industry is in desperate need of restructure and reform. It is an industry that began with the charitable work of organisations such as the churches that recognised within the elderly some who were lonely, insecure, often poor and no longer physically capable of attending to many of the essentials of daily living. To-day the elderly are a "demographic" studied by the financial managers and recognised as the most wealthy group within the community. They have become the target whose wealth is to be tapped and one of the routes for this is through retirement villages.

1.2 Power and control is the key to an operator's successful operation of a retirement village. Ownership carries with it power, so actual ownership of and control by residents by means of registered freehold title to the property in which they live in a village is rare. Even so, in strata titled villages subsidiary contracts transfer much power from the resident proprietors to the operators or managers. The trend is towards the retention of ownership, and thus power and control, in the hands of the operator, with premises being leased or licenced to the residents.

1.3 The Retirement Villages Act 1999 was introduced by the New South Wales government to modify the excesses of some operators. The government makes no attempt to control prices charged by operators. It is argued that market forces should be the determinant of the prices. However, market forces operate only in a climate where there is perfect knowledge, a far cry from conditions in the retirement village market. Considerable deception is employed by the operators. Many residents entering villages have only a vague understanding of the contracts which they have negotiated or of the conditions they have agreed to accept.

1.4 The value of the legislation in protecting residents from exploitation has to be measured by the extent to which the operators are prepared to observe the law; the awareness of residents that the legislation exists; and, if they are aware, the courage the residents have to challenge, in the available Tribunal, an operator not believed to be observing the law.

2. INTRODUCTION

2.1 The resident-funded retirement village industry is a multi-billion dollar industry operating throughout Australia and forms a significant section of the economy generally and of the housing section in particular. In this paper only the situation in the State of New South Wales will be covered although many of the operators within the industry function throughout the whole of Australia. With differences between the States mainly arising from the legislation introduced in States, it is reasonable to assume that, to a large extent, the same situation being described for New South Wales applies in all States.

2.2 As will be demonstrated in this submission, the industry is causing a massive redistribution of wealth from the thousands of retirement village residents and their ultimate beneficiaries to the small and decreasing number of persons operating retirement villages. The wealth is mainly in the form of profits generated and of the property that is being accumulated by these operators as a consequence of the transfer of funds and considerable loss of equity of the retirees taking up accommodation in the villages. I submitted an economic analysis of loan/licence agreements to the Office of Fair Trading during the year 2005.

2.3 This transfer of wealth has a serious detrimental effect upon the retirees. Upon entry into a retirement village their capital begins to erode to the point where they are unable to afford, unless they have considerable additional financial resources, to leave the village. They may be motivated to leave the village because they are unhappy there and wish to find alternative accommodation either in another village or in the open housing market. More importantly, their health may have deteriorated, giving rise to the need for aged care but they are unable to afford to pay for accommodation in an aged-care facility. That some residents may be forced to apply for a government subsidy to allow them to make such a move is an indictment of the financial arrangements in retirement villages.

2.4 A considerable amount of misinformation and even deception is used by the industry to attract residents. Prospective residents have been conditioned by the rules applying to the acquisition of property in the open market and are ill prepared to deal with the complex legal arrangements for acquisition that apply in the retirement village situation. The arrangements and contracts in villages are so complicated that, frequently, an understanding of the legal and financial significance is not gained by residents until they have signed contracts, lived in the complexes and are too deeply committed to withdraw from the contract. Unfortunately, not all legal practitioners seem able to grasp the disadvantageous financial position in which potential residents will place themselves upon entry into a village. Provisions in legislation which require disclosure of financial aspects before entry are simply not working. Probably the greatest cost to residents under loan/licence arrangements is the cost of foregoing interest on the unsecured, interest-free loans residents are required to make to operators to gain entry into a village. No attempt is made in any literature issued on the subject to reveal to prospective residents the extent of this cost. For other types of villages, the capital losses incurred by residents are by virtue of the sizeable deferred payments or departure fees they are required to pay when they vacate the premises.

2.5 Who are the retirement village operators? Most churches operate retirement villages. There is a group of operators that defines the operation as "not for profit". Some of these operators have gained the status of a benevolent society and thereby sometimes receive relief from governmental and semi-governmental taxes, fees and charges. There are also private operators who operate specifically to gain a profit. Some operators, and they must be very few, actually operate a retirement village on a strictly charitable basis, providing accommodation for the truly needy. Apart from the latter category of operator, all of the operators are gaining considerable wealth from the operation of a retirement village, to the financial detriment of residents.

2.6 The majority of residents of retirement villages are female. It is reasonable to assume that the majority of them have had no business experience and have little or no ability to understand the complex contracts covering entry into a village. With control of the operation increasingly in the hands of the management and the naivety or disinterest of the majority of residents in the financial management of the village, there is considerable scope for dishonest practices to be introduced by management to enhance its income. So well hidden are the costs of living in a village that the residents may never become aware of the actual cost to them of this chosen life-style.

2.7 Unbelievably, there exists no system for the registration or licensing of retirement villages in New South Wales. Even the Office of Fair Trading, responsible for regulation of the industry is unable to provide accurate figures of prices being paid by residents to enter villages, of the number of villages that exist in the State or of the number of residents living in these villages.

3. DEFINITIONS

3.1 To better facilitate discussion of the various arrangements and contracts, in which a great variety of names and descriptions are used to describe virtually the same thing, definitions used in the New South Wales Retirement Villages Act 1999 No.81 will be used. Additional definitions are provided which are specific to this submission alone.

A **retirement village** is a complex containing residential premises that are predominantly or exclusively occupied, or intended to be predominantly or exclusively occupied, by retired persons who have entered into village contracts with an operator of the complex. The definition does not refer to complexes providing residential or respite care under the Aged Care Act 1997 of the Commonwealth or the Nursing Homes Act 1988.

A **resident-funded** retirement village is an entire complex or a section of a multi-use complex which is occupied by retirees who have made payments to the operator which are sufficiently large to cover the purchase of the land, buildings and infrastructure and, usually, to cover all of the day to day or recurrent costs which arise in the operation of the village. The operator receives no governmental or semi-governmental subsidies other than possibly relief from taxes, rates and charges. The residents receive no financial support from the government but some may be in receipt of an aged pension.

An **operator** of a retirement village means the person who manages or controls the retirement village and includes a person who owns the land upon which the village stands.

An **ingoing contribution** is any money payable to the operator under a residence contract. It is not the purchase price of the premises where the resident has title to his or her residential premises.

A **departure fee** is any amount of money payable under a village contract by a former occupant of a retirement village that is calculated in relation to the period, or part of

the period, during which the former occupant has or had a residence right in the village.

A person **owns** residential premises in a retirement village if the person is the registered proprietor of the premises. (This is not the definition used in the Retirement Villages Act).

In the Retirement Villages Act, a **recurrent charge** is defined as meaning any amount (including rent) payable under a village contract, on a recurrent basis, by a resident of a retirement village

A **residence contract** means a contract that gives rise to a residence right

The **retirement village industry** to which this submission refers is the industry which provides accommodation principally for retirees aged 55 years or more on a **self-care** basis but does not include villages, mainly occupied by retirees aged 55 years or more who occupy the premises under the provisions of the Landlord and Tenants Act. Some services may be provided by the operator but they will be on an individual, fee for service basis.

In the case where premises are vacated as a consequence of the death of the resident, reference in this submission to a resident should be understood to be a reference to the **legal representative of the deceased resident**.

4. BENEFITS TO RESIDENTS OF LIFE IN A RETIREMENT VILLAGE

4.1 The residents of retirement villages are elderly but still capable of caring for themselves with, perhaps, some services for which they must pay a fee. They have reached a stage in life when their physical and mental capabilities are beginning to diminish. It should not, however, be assumed that they have all ceased to be mentally competent.

4.2 Retirement villages provide a type of accommodation for the elderly which is greatly appreciated by those who live alone or who feel no longer able to perform the many physical duties required of householders. One considerable benefit is that the responsibility for day-to-day maintenance of the residence is lifted from the shoulders of the resident. All those niggling little jobs that need special tools or special skills are undertaken by caretakers. When a retiree is no longer able to perform these jobs in his or her own home, the assistance of younger people or tradesmen must be sought. It is difficult for the elderly to find a reliable, honest and trustworthy odd-jobs man or woman who will travel some distance to attend to a job worth only a small amount of money.

4.3 Security is another benefit. This varies from village to village but by being able to fall back on neighbours or the staff is a great relief. Units are usually fitted with emergency call buttons so help is usually close at hand.

4.4 The social interaction with others is also of considerable benefit to some. Residents may participate in any group activities to whatever degree they choose.

Social committees are sometimes elected in villages and can organise outings and other functions. At the same time, there is absolutely no obligation for a resident to join in. The privacy of a resident is strictly honoured.

4.5 The larger villages generally have recreational facilities for the benefit of residents. They can have community rooms, community halls, bowling greens, golf putting greens, swimming pools, well equipped gymnasiums, village buses and games rooms. The costs of all of these facilities, however, are borne by all of the residents whether or not they make use of them

5. BROAD DESCRIPTION OF THE VARIOUS ACCOMMODATION ARRANGEMENTS

5.1 General Comment

Within the resident-funded retirement village industry, a residency right can be created by means of a variety of contracts including contracts under a Company Title, a Community Land Title, a Strata Title, a Long-term Lease or under a Loan/licence arrangement. Registration of a complex purporting to be a retirement village is not required under the Retirement Villages Act but may be required for a different purpose under other legislation.

Local government authorities are responsible for approval of the construction of retirement villages. Villages may exist which are unknown to the Office of Fair Trading, the department responsible for the administration of retirement villages, or to the Retirement Village Residents Association Inc., a voluntary association representing residents in New South Wales. The residents in those villages may not be familiar with the Retirement Villages Act 1999 and be unaware of support they may be able to receive when disputes arise.

The purpose of the Government in introducing the Retirement Villages Act 1999, it is assumed, was to establish a standard under which all retirement villages are to be operated but there may well be limits to the reach of this legislation. The descriptions below of various contractual arrangements have been prepared from data gained from limited enquiries made within the industry and are illustrative only. There is no standardisation within the industry and contracts vary between villages as well as between residents in the same village.

5.2 Company Title

A company may be formed for the purpose of developing a retirement village,. It will need to be registered under the Companies Act or the Cooperation Act. The rules adopted by the company will determine the scope of its operation. If the property is subdivided into residential lots the overall plan needs to be registered with the Office of the Registrar General under the Real Property Act. The right of occupancy is gained when the prospective resident acquires a shareholding in the company.

5.3 Community Land Title

A Community Land Scheme developed as a retirement village, under the Real Property Act, must be registered with the Office of the Registrar General. A prospective resident would gain the right of occupancy with the purchase of a lot in such a scheme.

No examples of contracts under either of the above arrangements has been found in any research so far undertaken.

5.4 Strata Title

5.4.1 On the open market, a Strata Plan must, under the Strata Titles Act, be registered in the Office of the Registrar General. Unitholders, under this arrangement, gain a title in fee simple to the unit to be occupied A unitholder is an owner as a tenant-in-common with all other unitholders of the entire common property. Every unitholder is a member of the body corporate and elects a committee of management. The body corporate frequently employs a manager to undertake the administration of the village. As an owner, every unitholder is responsible, on a shared basis, to meet all of the expenses in running and maintaining the property. Levies to be paid by each unitholder are struck by the body corporate for this purpose. When the unitholder vacates the unit, he or she is able to sell it and receive the full market value for it which usually means the receipt of a capital gain.

5.4.2 There is a difference between open market strata schemes and retirement village strata schemes. Prices for retirement village strata title units tend to be equivalent to those for strata title units on the open market. Ownership and operation of a Strata Scheme retirement village are subject to all of the provisions of the Strata Schemes Act. However, it is the practice of developers to include in the contracts special conditions which include the following, with one, a number or all of them applying:-.

1. the resident is to share with the developer, on a specified proportional basis, any capital gain, an unknown amount at the time the contract of sale is signed, upon the resale of the unit;
2. the resident is to pay to the developer as a departure fee a specified proportion of the original purchase price (or perhaps, even, the then unknown resale price), calculated on the length of time the resident lives in the village, and/or
3. the developer is to be given the role of managing the village on behalf of the body corporate. (Quite often, the operator maintains an interest in a small part of the complex and thus remains a member of the body corporate)

It could be argued that by the inclusion of a condition in the contract giving the operator a share of future capital gains, the real price of a unit is set, not at current market prices, but at a price which will apply at some time in the future. It appears that a condition in the contract of sale which obliges the unitholders to appoint the developer as the manager of the village creates a commercially tradable "right of management". Such rights are being bought and sold in the market at the present time and the bodies corporate appear not to exercise their power to prevent it. At least one corporation at present purchasing long-term lease and licence retirement

villages is also purchasing management rights in strata title villages. It is a stated intention of the representative of the corporation that the units will be purchased over time from vacating unitholders and the premises will be either leased under long-term leases to incoming residents or offered under loan/licence conditions.

5.4.3 The argument given by the operators supporting these extra charges and conditions is that "it enables them to keep in touch with the village" or that it compensates them for the cost of the provision of part of the complex. The resident is tied into the payment of the extra funds by means of a registered charge attached to the title to the unit. It frequently happens that residents have failed to understand that there is a charge on the title or the purpose for it. At the time the unit is vacated and sold, the resident or his or her representative receives quite a shock to learn that a large sum of money is to be deducted from the sale proceeds and paid to the operator. These additional demands for payment, surely, cannot be justified. If these additional payments are genuinely needed as reimbursement for the cost of development of the village, they should be included in the price initially quoted to the purchasers.

5.4.4 Under this system the developer initially sells the units in the complex and with the proceeds discharges all debts incurred in its development and construction. If the developer retains an interest in the management and control of the complex, the extent of that control depends upon the competence and strength of the managing committee of the body corporate. In any strata scheme suitable, competent committee members are often difficult to recruit but in a retirement village this is even more difficult when the body corporate members are elderly and sometimes in poor health. In some villages the committee seems to have surrendered control entirely to the manager. The power exercised by the manager is out of proportion in the legal relationship of the body corporate (the owner and employer) to the manager (the employed).

5.4.5 Some operators of strata title villages include in the contract an option clause whereby it is given the first option to purchase back a unit being vacated. The Retirement Villages Act, at section 167, requires, in these circumstances, that the operator gives the resident written notification of its decision whether or not to exercise the option within 28 days after the premises are vacated. By repurchasing vacated units the operator is able to determine or at least control, to a considerable degree, the price received by the departing resident and is able, then, if the market conditions are favourable, to resell the unit at a higher resale price. More importantly, the operator is able to include in the contract all the conditions included in the original sale contract, to its considerable and continuing financial benefit. Residents may gain some security from the existence of the options clause, being willing to accept a lower price for the sake of release from the anxiety of finding a purchaser for the unit.

5.4.6 New residents entering a village after purchasing a unit from a vacating resident can be persuaded to enter into a second contract, agreeing to make a sizeable deferred payment upon resale to the manager who, at that stage, is not even a party to the sale. This seems to occur when the sale is handled by an on-site agent who is also an employee of the manager.

5.4.7 Not all managers of strata title retirement villages disregard the rights of the residents. An example is that of Berkeley Village, at Berkeley Vale on the Central

Coast. As the number of unitholders willing to serve on the management committee often exceeds the number of vacancies on the committee, elections are held to fill the positions. Minutes of meetings are distributed to all members of the body corporate. The Manager is answerable to the management committee. This is a village of 220 units. Recreation facilities include a community hall, games room, library, village bus, swimming pool, concert hall and two bowling greens, one synthetic, the other natural grass. The original purchasers of units in the village agreed to make deferred payments amounting to 35% of capital gains but no charge for such payments have been attached to subsequent sales of the units.

5.4.8 A complaint that is raised by operators of strata title retirement villages is that they are required to comply with two pieces of legislation, the Strata Schemes Management Act and the Retirement Villages Act. This is a spurious complaint. Most people, in their daily activities, are subject to a number of Acts.

5.4.9 The advantage to a strata title retirement village resident is that he or she holds a registered freehold title to the property, the extent of which is clearly defined in the Strata Titles Act.

5.4.10 The main objections to the initial arrangements are:-

1. they contravene the requirement in contract law that the full price be known by each party at the time of entry into the contract. Both parties to the contract are aware of the initial price or consideration set for the transfer of title, but they can only make an estimate of the deferred payment which will have to be made when the purchaser actual resells the property. The contract price is, therefore, open ended
2. the failure of the operator to nominate the "real" price (the initial price plus the deferred payment) rather than the initial price at the time of the unitholder's purchase of the property represents deceptive behaviour on the part of the operator. The majority of purchasers tend only to concentrate upon the initial price.
3. if the developer, under a contractual condition, retains the role of manager of the village, the unitholders are deprived of the right, as owners, to dismiss an unsatisfactory manager and appoint a replacement.

5.5 Long-term Leases

5.5.1 The term of long-term leases is usually set at 99 years but can vary between 49 years or 199 years. In earlier leases, a trust deed is often attached to each lease document. The lease price for each of the residential units is set at a level which enables the developer to recover the cost of development of the complex when all units are initially sold as described in the case [Poignand v NZI Securities Australia Ltd and others (1994)120 ARL 237].

5.5.2 With the sale of each long-term lease, a Memorandum of Lease is registered in the Office of the Registrar General giving the lessee an indefeasible interest in the premises to be occupied. (This has to be qualified to the extent of the operation of Part 9 of the Retirement Villages Act which allows an operator to apply to the Tribunal to remove a lessee from the premises.) The result of the registration of a

lease has been demonstrated in the Woolcott Court retirement village situation. Although the village had been registered as a strata scheme, the residents held long-term leases to their premises but not, apparently, to the common property. Some residents failed to register their leases. The operator became bankrupt. The residents with registered leases retained the right to occupy their premises, while those unregistered were evicted. As a bankrupt, the operator was unable to repay the money paid to it by the residents.

5.5.3 It is not the general case that long-term lease villages have been subdivided into lots, with each lot registered on a folio by the Registrar General. In a lease reviewed for the purposes of this submission, the "premises" leased were defined as the area contained within the inner surface of walls, windows and external doors, the upper surface of floors and the under-surface of ceilings, that is the air space contained within the physical structure. U der the terms of the lease, the lessee is given the right to use and enjoy, on a shared basis with the lessor, persons authorised by the lessor and other residents, the common areas of the village including passageways, halls, grounds, gardens, parking spaces, storage areas and other common facilities. The terms of the lease place responsibility upon the lessees to meet all outgoings related to the operation of the complex, including, mainly, the common areas owned by the lessor.

5.5.4 In another lease, the definition of the demised premises is found by searching through the definitions given in a complexity of documents. The demised premises comprise a self-care apartment which is shown as a specified lot on an annexed plan. Although it is not clearly stated in the documents, it has to be implied that the "demised premises" do not include the land upon which they stand. The money paid for the lease is secured at the expense of the operator, by a first mortgage over the complex to the Trustee.

5.5.5 In reality, the resident lessees have few more rights than a tenant of the premises, although their financial responsibilities, in terms of the contracts, are much greater. The extent of these responsibilities may be tempered by the provisions in Part 7 of the Retirement Villages Act although this remains to be tested in the judicial system. Residents, under the existing Act, are not responsible for the costs of capital replacement, apart from specified exceptions.

5.5.6 Each lessee is required under the terms of the contract to make sizeable payment to the lessor at the time of vacation of the premises. This payment may take the form of a lump sum payment calculated on the basis of the period of occupancy, a proportion of any capital gain or it may represent a proportion of the resale price gained when the lease is resold. In one of the leases, the statement is made that the value of the freehold real estate is discounted for the lessee at the time of entering into the lease in return for these deferred payments. The amount of this "discount" is not disclosed to the resident at the time of purchase. The statement lacks credibility when the deferred payments are based upon the value of the real estate (the capital gain) at the time it is being sold, not at the time of purchase, or upon the period of occupancy.

5.5.7 Before a clear understanding of the harshness of many of the clauses included in these long-term leases can be gained, a careful reading of the documents is required. Many of them are excessively long. Most contain a requirement that a penalty

interest be paid on any outstanding debt of the resident. This provision has application, mainly, when the resident dies and the estate has to be wound up by the executor. All the assets of the estate could be contained in the value of the lease itself and no income is available to pay the regular recurrent charges which have to be paid until the lease is sold or repurchased by the lessor after a specified time has elapsed. Non-payment of the recurrent charges amounts to a fast-building debt upon which the penalty interest is imposed. As to a time specified when the recurrent charges will cease, the lease sometimes allows the lessor to re-purchase the lease from the resident but with the unconscionable condition that the price is determined by the operator(lessor), not an independent valuer.

5.5.8 The lack of standardisation of lease contracts creates comparison difficulties for prospective residents. In the disclosure statement all operators are required by law to issue to prospective residents, no clear legal definition is given as to what is being offered for lease. Recognition is given to the commitment of residents to make deferred payments upon surrender of the lease but no clear explanation of the reason or justification for these payments is given. The actual contract document must be viewed to provide a prospective resident with essential information for proper comparisons to be made between villages. The following table illustrates the differences the formulas for deferred payments can make to final payouts to residents. As many residents look upon the retirement village as their last home, and frequently die there, it is the residents' representatives who have to settle with the operator. They seldom have legal representation at this time, are usually ignorant of the rights of the former resident and are vulnerable to being deceived.

Comparison of Formulas for Calculating Payouts at the Time a Unit is Surrendered

Assume that in each of the three villages the lease price is $500,000, with different formulas to determine the amount of the deferred payment. The results from three actual villages are:

	Village A	Village B	Village C
Assume residency of 10 years with an increase in value at 5% per annum – capital gain is $314,500. Resident to receive	$532,250	$610,875	$610,875
Assume residency of 10 years with a decrease in capital value Capital loss is $50,000 Resident to receive	$325,000	$450,000	$337,500

In reality, the lease prices at the three villages are not the same. It is likely that prospective residents make the choice of village on the basis of its attractiveness, the recreational facilities available and the lease price being demanded. Whether the additional difference – the formula effect of the deferred payment – is taken into account is unknown.

5.5.9 In summary, the payments made by residents cover the development costs of the complex, all outgoings related to its day-to-day operation and administration, the

lessor's legal costs and the fees and costs of the Trustee. The resident also makes an additional payment upon vacation of the premises. Hence, the statement in a prospectus inviting investment in the development of an extension to an existing village, as follows:

"THE ATTRACTIVENESS IS NOT JUST THE DEVELOPMENT PROFIT BUT THE UNIQUE SITUATION WHERE THE OWNER CONTINUES TO RECEIVE BOTH INCOME AND CAPITAL GROWTH ON THE UNITS AFTER THEY HAVE BEEN "SOLD". "

5.5.10 The same principles are adopted in each lease studied for the purposes of this submission, although there is considerable variation in the language used. The language, in fact, is quite creative and tends to be rather deceptive. The consideration is paid by the lessee and the lease is registered by the Registrar General. But contained in some of the contract documents is a clause requiring the lessee to agree that the payment was an interest-free loan. For example, in the lease discussed in the next paragraph the consideration paid by the lessee to the Trustee is referred to in the Trust Deed as a "loan", diluting the sense of the lessee having purchased an interest in the leased property.

5.5.11 Of the lease involved in the case *Murphy v Overton Investments Pty Limited [2001] FCA 500* at paragraph 101, Gyles J., in the transcript, wrote:

"In my opinion, the transaction entered into by the appellants cannot be viewed simply as the sale and purchase of property. The parties were involved in much more than a normal vendor and purchaser transaction. The property in question was a leasehold interest of a very particular kind in a retirement village. The combined effect of the instruments identified below as the Lease, Memorandum of Lease and an incorporated Trust Deed was to put the respondent in the position where it was lessor to the appellants (and others) of units in, and was the manager of, the Heritage Village with very considerable powers and discretions. "

5.5.12 A source of frequent dispute between some residents and the operators is the extent of application of Part 7, the financial management sections of the Retirement Villages Act 1999, to the financial provisions in the lease. The operators' legal representatives tend to argue that the provisions of the Act do not over-ride the provisions of the leases, while the contrary view is held by residents. Legislation is failing to achieve its purpose if its application to any particular issue is unclear. Resort to a Tribunal is a traumatic experience for an elderly resident and, to a higher Court, extremely expensive as well, if a resident is forced to resort to this approach to clarify an issue. Residents tend to buckle under demands of an operator rather than face the worry and expense involved in a Tribunal challenge.

5.5.13 The terms and conditions of the leases result in unfair financial benefits to the lessors. .They are harsh and unconscionable because the power and the bargaining position of the operator far exceed those of the resident.

5.5.14 The main objections to these lease arrangements are:-

1. when the contract is signed, there is no certainty as to total or "real"price, which is ascertained only when the lease is re-assigned.
2. the failure of the operator to highlight the "real" price rather than the up-front price at the time of the sale represents deceptive behaviour on the part of the operator. Some lessees tend not to be mindful that deferred payments are part of the overall price they pay for the lease
3. there is, in some leases, a lack of clarity as to the extent of the "interest" being leased
4. the language used in some of the leases is ambiguous and appears a deliberate attempt to confuse the relationship between lessee and lessor
5 although the statement is made in the documents that the trustee has been appointed in the interests of the lessees, an analysis of the role of the trustee reveals that the purpose of the trustee is mainly to benefit the lessor. This a serious deception exercised on the part of the lessor.
6 the lease and trust deed are so complex that it is unlikely the lessees have read them, let alone understood them
7 lack of standardisation of the contracts within the sector adds greatly to the confusion faced by prospective residents when choosing accommodation in a village
8 the application of provisions of the Retirement Villages Act to provisions in the leases has not been tested in the Courts and lack of certainty leads to disputes between the lessor and the lessee on financial management of the village

5.6 Loan/Licence Arrangement

5.6.1 For the right to occupy a unit under a loan/licence arrangement, a resident pays the operator a sum of money which is in the form of an unsecured, interest-free loan. When the village is first opened to residents, the price for each unit is set at a level which will ensure that, when all units are occupied, the operator will be reimbursed for the cost of development . Thereafter, with the turnover of residents, the price is increased in line with general increases in housing in the open market. Under a loan/licence arrangement the resident receives no proprietorial rights to the property. If additions or improvements are made to the premises, they are usually at the resident's cost .....

5.6.2 When the resident vacates the unit, the operator repays the loan, less a departure fee, usually based upon the length of occupancy. The departure fee is frequently 20%-25% of the loan amount but can be anything up to 100%. Residents who entered a village prior to 1st July, 2000, can be required by the operator to make an additional payment of an amount not expressly stated in the contract but which is, at the time, determined by the operator, to cover the refurbishment of the unit. Section 164 of the Retirement Villages Act 1999 which commenced on 1 July 2000 prohibits this payment for residents who entered a village after the commencement of the Act. By virtue of section 165 of the Act, there is an attempt to involve the earlier residents, or their representatives, in the determination of the refurbishment cost, although section 165(3) provides an escape clause for the operator. As a consequence the refurbishment work is undertaken by the operator who, without check, determines the cost to be met by the former resident. This is an unconscionable position supported by legislation. Unfortunately, residents and their representatives are often

unaware of the existence of these provisions and make no use of them. The amount, whether determined entirely by the operator or as a result of negotiations, is deducted from the loan before any repayment is made. Refurbishment usually means renewing the fixtures and fittings and furnishings and repainting the inside of the unit. Although, in the Act, an allowance is required to be made for "fair wear and tear", it is questionable whether it is done.

5.6.3 While occupying the unit, the resident is charged a levy called a recurrent charge which is to cover running expenses of the village. This is generally increased each year. Some villages increase it under a fixed formula – say the same increase as the increase in the CPI – but others have no restriction upon the amount by which the charges are raised. On the basis that all payments of this levy, including administrative costs, received from residents are absorbed in the running costs of the village, operators hold themselves out to be "not-for-profit" organisations, a false claim in the light of the considerable extra payments received by the operators.

5.6.4 An idea can be obtained of the "real" weekly payment met by a resident for the right to occupy a unit by considering, on an annual basis and then dividing by 52 to get the weekly figure, the estimated value of interest foregone by the licensee in favour of the operator in addition to the recurrent charges payable. At the current official Reserve Bank interest rate of 6.25%, the benefit to an operator for each $100,000 of ingoing contributions received from a resident is $6,250 per annum or $120 per week. If an operator holds, say, $5,000,000 in ingoing contributions, the value of the notional interest is $312,500 per annum. The average housing interest rate is much higher than the official Reserve Bank rate so adoption of the latter rate in this estimate is very conservative.

5.6.5 With respect to the use to which the unsecured, interest free loans paid to the operator are put, the operator is not accountable to the resident (the lender) in any way. Operators argue that this information is "commercial in confidence" even though each loan is an asset of the resident and the transaction is between the operator and the resident only. Residents are unable to satisfy themselves as to how their asset is being applied so that they can feel reasonably assured the loan will be repaid at the termination of the residency.

5.6.6 When residents vacate the premises and new residents enter the village, the loan payable by the new resident is increased in line with the increase in value of properties on the open market and that increase in value is retained by the operator. In other words, the operator is liquidating the increased value of the property on an ongoing basis without actually selling the property. With every change of resident, this increased loan can be utilised by the operator for its own purposes.

5.6.7 Research into public information with respect to a recently completed complex suggests that the initial ingoing contributions, that is the aggregate of unsecured, interest-free loans, made by residents is sufficient to cover the costs of the establishment of the complex. Residents have no equity in the property even though, through their unsecured loans, they are financing its purchase for the operator. By foregoing interest and paying departure fees, the residents' own capital is depreciating dramatically. Increases in property prices in the open market make it very costly if

not impossible for them to afford other accommodation and to contemplate moving out of the village.

5.6.8 The levies payable by residents provide another source of constant concern to residents. Part 7 of the Retirement Villages Act deals with the financial management of retirement villages and is purported to give residents some control over expenditure. Operators are required under the Act to provide residents, at the end of one financial year, with a statement of proposed expenditure for the coming year (a budget) which residents may accept or reject. Some operators appear to take queries raised by residents into account. If residents object to any items in this budget, the operator may apply to the Tribunal to have it approved. The possibility of having to support their opposition to the expenditure before a Tribunal is generally enough to frighten the residents into accepting the budget.

5.6.9 Operators are also required by the Act to provide to residents, each quarter, a copy of the accounts. This provision is by no means observed as it should be. To gain real value from this, the residents need to possess adequate accounting experience to pursue the issues through the accounting processes. In other words, the operator determines how, what, where and when expenditure is incurred; the residents have to meet the costs. This is a highly unsatisfactory situation. The extent of the bargaining power of residents in this situation is minimal. Many operators resent any questioning by residents who at times are quite intimidated by the attitude of the operator.

5.6.10 Few residents have the confidence and are prepared to attempt appeal to a Tribunal made available to them under the Retirement Villages Act. They fear that if such an appeal is successful, the operator has the financial resources, unavailable to the resident of course, to lodge an appeal with the Supreme Court against the decision. Many residents feel too nervous or intimidated to complain. Ample oral evidence is available to this effect. These issues have even been the subject of speeches in the Parliaments of New South Wales and Queensland. While provisions in the Retirement Villages Act appear to be weighted in favour of the residents, in reality they do not work that way.

5.6.11 Part 9 of the Retirement Villages Act – the provisions covering termination of residence contracts – deals with the security of tenure for residents under loan/licence arrangements and seems to be operating for the benefit of residents.

5.6.12 The paying of an ingoing contribution is not an investment. Using the Oxford Dictionary definition, a resident can be described as a tenant of premises in a retirement village. A comparison can be made between a resident of a village and a tenant under the Landlord and Tenants legislation. Upon entry to rental premises, a tenant pays a bond equal to four weeks' rent. The bond is refunded upon vacation of premises, subject to there being no excessive wear and tear and damages. The tenant is obliged to pay a regular, fixed rent during occupancy, although the rent may be adjusted over time. On the other hand, upon entry to retirement village premises, a resident of a retirement village pays an ingoing contribution (a loan), the size of which depends upon the age and location of the village. Under most contracts, only a proportion of this amount is refunded upon vacation of the premises. A resident, therefore, is obliged to make a number of payments which are:

a) the foregoing of interest on the loan in favour of the operator, for the entire period of occupancy,
b) a departure fee which is a proportion of the original loan,
c) regular levies which are expected to meet all costs and charges covering the day to day operation of the village, and
d) in some instances, a refurbishment charge for the refurbishment of the vacated premises

When all of these payments are taken into account, the "bond" or ingoing contribution and the weekly equivalent payment made by a resident are generally much higher than that of a tenant in equivalent rental premises on the open market.

5.6.13 Loan/licence arrangements, generally, are for residents the most costly. The majority of residents are passive; they take little interest in the finances and running of the complex. Many believe they have actually purchased the premises. They are unaware of the real costs involved in the entry into a retirement village and are very content in the village environment. Few are aware of the existence of the Retirement Villages Act. The costs, therefore, represent extreme exploitation of a vulnerable group of people. For most residents of a retirement village, it is exhausting to contemplate challenging the behaviour of the operator if they are dissatisfied. They are often afraid of adverse repercussions if they do. They have moved into a village to seek comfort and freedom from financial worries but are often worried that they will be unable to afford the recurrent charges as they continue to increase.

5.6.14 The main objections to these arrangements are:-

1. the actual financial cost to the resident of the "interest-free" component of the loan, the most costly component in the "real" cost, is seldom, if ever, discussed in negotiations for entry into a village and is, therefore, not generally understood by the resident. It cannot be argued that the contract price is known to the resident, one of the two parties to the contract. These contracts should be void. The conditions are harsh and unconscionable. Residents should not be bound by contracts they do not, and never did, understand
2. the failure of the operator to discuss the real cost at the time of the resident's entry into the village represents deceptive behaviour on the part of the operator
3 the substantial loan made upon entry is not secured and the operator is not accountable to the resident as to how the money is used
4. the uncertainty associated with the definition of a recurrent charge places the resident in a vulnerable position and emphasises the uneven balance of power between the operator and resident when the charges are being negotiated. The majority of residents are afraid to question charges for fear of adverse treatment – they do not wish to upset the operator
5. the failure of some operators to make available to residents copies of accounts is contrary to the requirements included in the Retirement Villages Act and denies the basic rights of residents to knowledge of the costs they are incurring
6. the sense for some residents of being trapped in the village because their capital has been dramatically eroded and they are unable to find the funds necessary to enable them to move into other accommodation. They deal with this situation by becoming resigned to a situation they are unable to change

6. CURRENT TRENDS IN THE INDUSTRY

6.1 The take-over of numbers of villages by large corporations

6.1.1 Large corporations are now taking over self-care retirement villages originally established by independent operators. Many villages are thus being merged under the control of an ever decreasing number of extremely large corporations operating throughout Australia and internationally. Some corporations are purchasing contracts for the management of villages rather than the villages themselves. Anecdotal advice received from a financial manager once engaged in assessing businesses for take-over by clients is that the income stream of a village is first assessed. If this is expected to be large enough to service the debt from borrowings and to pay dividends to shareholders, the take-over will proceed. In the **Sydney Morning Herald** Business Section of July 5, 2006 under the heading *Turning grey power into profits* the argument was presented about corporations taking over retirement villages that–

"*High returns come from keeping costs down and pulling productivity levels right up, as much as possible. These people might be able to get economies of scale and bring in new technology that delivers that*"

The pressure to increase profits for the operators and their financiers is intense, overwhelming any of the sentimental drive of early developers to provide a social service for the elderly.

6.1.2 The extent to which this current trend will eventually change the industry is not yet known but changes becoming obvious include –

(a) inclusion of expenditure on payroll tax in recurrent charges residents are required to pay
(b) in strata title villages, managers are purchasing individual units as they are vacated by residents and converting the occupancies into long-term leaseholds of the premises only

6.1.3 Payroll Tax becomes payable by a corporation when the salaries and wages of employees passes the threshold of $600,000 and is currently rated at 6% (Office of State Revenue). In the case *Milstern Retirement Services P/L v Lindfield Manor Retirement Village* (2005) NSWCTTT 749 (9 November 2005) the report reads -

> "*the Tribunal accepts that the Act entitles an operator to aggregate its accounts. Nevertheless, the Tribunal is not satisfied that it is reasonable for the village to bear a proportion of the payroll tax which is solely a consequence of the size of the operator's business. In isolation, the operation of this retirement village would not attract a liability for payroll tax. Accordingly, this is not an expense reasonably incurred in operating the village in the 2004 year*"

Decisions of the Tribunal do not create a precedent. Many villages included in this year's budget an amount to cover expenditure on payroll tax. Operator's claimed to have received legal advice that it was payable by residents. They virtually threatened residents that even if the residents submitted the budget to the Tribunal and won their argument of have payroll tax excluded, the operators would fight the decision in

higher courts. Under such threats (or duress) residents in most villages accepted the budget.

6.1.4 For the purchasers of strata title village complexes, it is not a case of the operator wanting to resell units. The units will be converted to leasehold. **The Australian** on 12 July 2006 in its article *Sharing in the baby boomer bonanza* commented on the trend

> *"It's a case of retaining control of the village and building a sustainable book of deferred management fees"*

Rather than being the employer of the management team, the former body corporate of the strata title village will gradually be stripped of control and become subservient to the manager..

6.1.5 To purchase a string of retirement villages the large corporations acquire equity by heavy borrowings. There is a serious danger that in an economic downturn, if units in villages become difficult to sell and prices fall considerably, over-committed operators will be unable to achieve the necessary income from the villages to meet their liabilities. Business collapses in the industry could present governments with insoluble problems.

6.2 Proposed new legislation in New South Wales

6.2.1 A Consultation Draft of a Bill to amend the Retirement Villages Act was tabled in the New South Wales Parliament in November 2006. There are, for residents, some alarming features in this proposed legislation. The combined affects of amendments to the financial management divisions will be to increase the amount of contributions to be made by residents and to strip away more of their rights.

6.2.2 Under the present provisions of the Retirement Villages Act 1999, residents are required to fund capital maintenance costs out of recurrent charges. The operator must fund all capital replacement, with some specified exceptions. The Bill proposes dramatic changes to this situation. An operator will be able to fund capital replacement as well as capital maintenance out of recurrent charges. Section 92(3) of the Bill is intended to provide that these replacement and maintenance costs will in future be shared on a 50/50 basis between the operator and the residents. It is reasonable to argue that capital maintenance costs will always be much lower than capital replacement costs. Operators, by sharing the much lesser cost of capital maintenance will be able to demand the sharing by residents of the much greater cost of capital replacement. For some, if not all residents, the recurrent charges can be expected to increase considerably.

6.2.3 This change to funding arrangements should be considered alongside the affects of proposed section 112(7) and (8). Residents, by special resolution, can under the proposed provisions "*consent to NOT have a proposed annual budget provided*". Operators are known to be able to manipulate residents. Only those residents who are alert and active and have the support of a majority of other residents will be in a position to preserve their right to have some input into the manner in which the operator spends their money. In addition to changes to section 112, the proposed section 114(8) provides that residents will be taken to have consented to a budget if "*There has not been a significant change in the services that are proposed to*

be provided..... " or if the budget increase is in accordance with a fixed formula or does not exceed the increase in the Consumer Price Index. This means that residents interested in the financial arrangements within a village can lose all right to negotiate the various budget items with an operator and so attempt to protect their own financial interests. There is worse to come. Section 119B almost ensures that an operator can be relieved of having to provide quarterly accounts for checking by residents. A resident will have no way of determining if any items are of a questionable, illegal or dishonest nature. Disputation before the Tribunal, or even the Office of Fair Trading itself, will become impossible because residents will be denied access to basic and important information.

6.2.4 Another aspect of these changes to the financial management of a village is that it introduces discrimination between operators and between inter-generations of residents. Where increases in recurrent charges are not subject to a fixed formula increase, the operator will be in a position to increase recurrent charges to cover expenditure on capital replacement. Even when residents have to pay only half of these costs, they can, at times, be expected to be significant. Where fixed formula increases apply, the operator is unable to increase recurrent charges to cover major items of capital replacement expenditure. This represents discrimination between villages. As far as discrimination between residents, it will be the unfortunate residents who happen to occupy premises at the time of the capital replacement who will have to meet the heavy extra costs. Operators can create capital works funds to offset this effect, but there is no obligation upon them to do so.

6.2.5 A 90-day settling-in period is proposed under an insertion to Part 5, Division 2 of the Act. In accordance with section 44B(a), if a contract is terminated within the 90-day period, the former occupant is liable to pay a fair market rent for the period, if any, that the former occupant occupied the residential premises. It is assumed that the operator will determine what constitutes "a fair market rent" at the time the former occupant vacates. To avoid the possibility of exploitation, every resident, before entering into the contract, should be advised in the general disclosure provisions, what the "fair market rent" will be in the event of his/her exercising the right to terminate the contract within the 90 days. This is another unconscionable provision actually included in the Act, giving the operator the right to fix a price after the resident has committed to the contract.

6.2.6 Section 44C(a) applies to a registered proprietor of a lot in a strata plan or an owner of shares in a company title scheme, as covered in section 7(1)(a) and (b). If a village contract is terminated, under the settling-in provisions, by one these types of resident, the operator is to pay the former occupant the proceeds from the sale of the residential premises. In other words, the conditions applying to the resident are the same whether the termination occurs within or outside the settling-in period. In both cases, the residential premises will have to be sold before the resident is able to recover his money. It is difficult to see what this provision achieves.

6.2.7 Another new insertion into the Act relates to the expenses of administration. In the event of the financial collapse of a village, the expenses incurred by an Administrator exercising the functions of the operator, are to be paid from recurrent charges and such other funds as would be available to the operator. What sections 87A and 87B mean is that, when the operator becomes bankrupt, the residents of the

village will be held responsible for payment of the Administrator's expenses. Recurrent charges will have to be increased significantly because the fees of an Administrator can be expected to be much higher than the salary of the operator. If residents occupy premises under a loan/licence, the loans they made to the operator are unlikely to be repaid. This could constitute the life savings of the residents – and they are to be additionally burdened with the expenses of the Administrator. While it is acknowledged that the Administrator's expenses have to be met, this proposal seems to be very unfair to the residents. They are the victims; the operator is the offender. What a heartless government. Situations like this are rare but cause enormous hardship to residents when they occur. A far fairer approach would be to require the operators throughout the industry to subscribe to a fidelity insurance scheme such as those applying within the legal and real estate industries to protect clients. If this approach were to be adopted, operators should be prohibited from passing on the cost of the fidelity insurance to the residents.

6.2.8 Within the definition of a "registered interest holder" the Act includes, under section 7(1)(c), a registered long-term lessee whose contract entitles him/her to retain 50% or more of any capital gains from the sale of the lease. For the purposes of the definition, a registered long-term lease is only considered to be such if it is for a term of at least 50 years. The proposed legislation is virtually stating that a registered long-term lessee is deemed not to be a registered interest holder if the registered long-term lease contract –

- is for a term less than 50 years;
- includes provision for the resident to make a deferred payment to the operator of more than 50% of capital gain
- .includes provision for the lessee to make a deferred payment to the operator which is calculated by some means other than as a proportion of capital gain

By tracing the application of section 7(1)(c) through the draft Bill it can be seen that the provision clearly discriminates between different types of leases. . The rationale is difficult to understand. In fact, these provisions are almost a re-write of section 150 of the present Act.

6.2.8 If the provisions in 6.2.8 are applied literally, section 181(2)(f) of the present Act will have application to all leases other than those defined in section 7(1)(c) of the Bill or in Part 10 of the present Act. An operator under section 181(2)(f) must, on a date which is 6 months after the date on which the former occupant delivered up vacant possession of the premises to the operator, make any refund of the former occupant's ingoing contribution that is required, under a village contract, to be made. There exists no formula in any of the leases or in the proposed legislation to allow an amount that is to be paid under this provision to be calculated. Leases usually provide for the lessee to receive payment when the lease is sold to a new resident and until that occurs, the capital gain or the proportion of the sale price to be paid to the operator cannot be calculated. I am unaware of any attempt by a lessee to apply for a refund from an operator under section 181(2)(f). As the provision is discriminatory and seems incapable of application there is some question as to why it is included in the legislation.

7. CONCLUSION

7.1 In the self-care retirement village industry, residence contracts of all types contain unfair, harsh and even unconscionable provisions.

7.2 Residents of retirement villages are old and, generally, lack the physical and mental capacity and energy to protect themselves against exploitation by operators. They may, once, have held responsible positions or achieved much in their working life but those times have past. The industry needs to be completely restructured to free residents from financial concerns and provide them with the security and comfort they seek. Retirement villages should not be seen as a source for easy profits for the developers.

7.3 The government must encourage operators to develop retirement villages for the elderly, but it should ensure that the regulatory legislation it passes is fair to both operators and residents.

7.4 A better structure within the industry might be the provision of two types of village. One type could provide the opportunity for some retirees to purchase a unit, with full title to it and the power to appoint managers for the complex. Another type could provide accommodation on a rental basis, with the opportunity for a resident to invest in the complex and earn interest and a modest income from it. In both types, funds would be available to developers to cover development costs. Where the establishment of a village is to provide accommodation for the less well off, perhaps taxation incentives could be provided to aid the development.

Joan Adams

31 July 2007

From: Joan Adams [

Sent: Thursday, 2 August 2007 8:45 AM

To: Committee, LACA (REPS)

Subject: Retirement Villages in New South Wales

Secretariat
Legal and Constitutional Affairs Committee,
CANBERRA

Dear Sir,

I made a lengthy submission to you on the legal aspects of law and contracts relating to retirement villages in this State. Unfortunately, I omitted another issue which I should have covered.

In my submission, I made reference to section 164 of the New Soputh Wales Retirement Villages Act 1999 which prohibits retirement village operators from collecting refurbishment fees from vacating residents when those residents entered village premises after 1 July 2000. A new trend in lease contracts in this State is to include with the purchase price of the lease an amount which covers the purchase of all fixtures, fittings and furnishings. For example, in a lease I viewed recently, the purchase price was stated to be $715,000, from which $50,000 was to be deducted for the purchase of the fixtures, fittings and furnishings in the unit leased. The lessee is responsible for the maintenance and replacement of all these items. I interpret this new practice as a method by which the operators are circumventing section 164 of the Act. The only refurbishment an operator is required to make after a resident vacates is the repainting of the internal walls of the unit. Another method used to offset the effects of section 164 was for operators, with all residents entering the village after 1 July 2000, to raise the amount of departure fees to be deducted from the loan repayment when a resident vacated the premises.

I apologise for this omission from my submission but I hope my comments will be taken into account.

Yours faithfully,
Joan Adams