

# **Submission Booklet**

## **Public consultation on Home Equity Conversion Schemes**

**Office for Senior Citizens,  
Ministry of Social Development**

**GUIDELINES FOR COMPLETION OF THIS SUBMISSION BOOKLET**

Before preparing your submission, we suggest that you read the discussion paper 'Public Consultation on Home Equity Conversion Schemes', as this will provide you with background information that will help you make your submission.

The submission booklet contains all the questions asked in the discussion paper. When you have completed this booklet please return it to the Office for Senior Citizens at the postal address below.

In making your submission you do not need to restrict your views to only those matters raised in the discussion paper. If you consider there are other aspects of Home Equity Conversion Schemes that should be considered, we are interested in hearing about those also.

If you are completing a postal submission and there is not enough room to complete your response, you can attach separate sheets of paper where necessary. Please ensure that additional sheets are firmly attached.

For more information or to obtain a submission booklet, contact the Office for Senior Citizens by:

- Phone (04) 916 3758
- Website [www.osc.govt.nz](http://www.osc.govt.nz) to print out or complete online

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## **RETURNING SUBMISSIONS**

Submissions can be:

Sent to:                   Office for Senior Citizens  
                                  PO Box 1556  
                                  WELLINGTON 6140

or

Completed and submitted online via this website:  
[www.osc.govt.nz](http://www.osc.govt.nz)

Your submission should reach the Office for Senior Citizens by 31<sup>st</sup> March 2007.

## **ADMINISTRATIVE DETAILS**

If your submission is being made as an individual, on behalf of an organisation or a business group we would appreciate it if you could complete the relevant details below. All information provided to us will be kept strictly confidential.

Full name of organisation or individual making submission:

This submission is made by the Rates Postponement Consortium, a group of 14 councils to provide open-ended rates postponement for older people. The councils in the consortium are the Ashburton, Far North, Gisborne, Kapiti Coast, Marlborough, Masterton, Queenstown Lakes, Rodney, Rotorua, South Wairarapa, Thames-Coromandel and Western Bay of Plenty District Councils, the Nelson City Council and Environment Waikato.

The consortium has considerable experience with a somewhat parallel product, indefinite rates postponement. In the course of developing that product, the councils have given a great deal of thought on matters of best practice, duty of care, the trade off between the present future interests of older people and a number of other relevant matters. Their experience is reflected in the submission which follows. \_\_\_\_\_

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Contact person (if different from above):

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**Independent legal and financial advice**

1. Should obtaining independent legal or financial advice before agreeing to a HEC loan, other than from the agent, or the agent's company alone, be made mandatory or remain voluntary?

Yes, it should be made mandatory. Older people are in a particularly vulnerable situation. Normally the equity in their property is the only substantial asset they have. Amongst other things, it represents the resource they will need to turn to in later years if they have health care or other needs which cannot be met by the state. The trade off between the present gratification of "borrow and spend" and future needs may not be well understood (a fit 69-year-old may be reluctant to accept that he or she could become a frail 85 year old). It is crucial that they have independent advice able to work through these sorts of issues with them.

2. Should potential borrowers of HEC schemes be required to certify that they have sought and received advice from an independent adviser?

Yes. It is a necessary part of a process designed to ensure that the borrower has the best possible opportunity of taking a well informed decision. The requirement to certify should focus attention on that.

3. If receiving independent advice is voluntary, should potential borrowers who have not sought this advice be required to sign a waiver to that effect?

Yes. This serves two purposes. First it directs the borrower's attention to the importance of understanding what they are doing. Secondly it provides a protection for other parties. With home equity conversion schemes, there is a real potential for litigation alleging, for example, undue influence. This is likeliest to happen either when the borrower dies and beneficiaries realise the impact of the borrowing, or when the borrower needs to draw down equity for health care or other purposes and finds it has all been used up. Those events will be years away from the time of the transaction itself so that a written record will be critical in establishing what happened.

4. Who should provide this advice for HEC schemes? Please select one option.

- Lawyers
- Financial planners
- Counsellors
- Accountants
- Not sure
- Other (please state).....

.....

A lawyer will be essential because a mortgage is involved and the borrowers will need to understand their legal rights. However this will not be sufficient. The borrower also needs advice on the implications of the transaction from perspectives such as their ability to afford health care or other support in the future, and the impact on family. The rates postponement consortium has found that this type of counselling is best provided by someone who has real experience in family and related matters and is professionally trained in counselling. Accordingly, a professional counsellor, with appropriate qualifications and organisational affiliations should also be involved (the term counsellor covers a very wide range of different backgrounds services and capabilities).

5. Are the costs of independent legal or financial advice likely to deter participation in these schemes?

The costs of independent legal or financial advice, and professional counselling, can collectively be quite substantial. They may have a deterrent impact but it is absolutely essential that people who take on home equity conversion loans do have quality advice covering the financial and non-financial issues involved.

### **No-negative equity**

6. Should a “no-negative” equity guarantee be made compulsory for all HEC schemes?

Yes. This has been accepted as best practice internationally. Home equity conversion lenders are infinitely better placed to insure against the potential for negative equity than are individual borrowers. In practice, the absence of a no negative equity guarantee is going to mean much more than simply a debt in the estate of the borrower when the borrower dies. Almost certainly, it will mean a forced sale by the lender to recover the amount due whilst there is still some equity remaining.

7. If a “no-negative equity” guarantee is not compulsory, should consideration be given to alternative measures to ensure users of HEC loans do not end up owing more than they own?

The issue is not so much ensuring that borrowers do not end up owing more than they own. Rather, it is ensuring that they are not forced out of their property. It is hard to see what alternative measures could be put in place. Negative equity almost invariably results when critical variables (property value, interest rates) change in ways that were not anticipated at the time of the transaction. The best alternative option is probably to impose restrictions on the proportion of the equity which could be drawn down in relation both to the value of the property and the life expectancy of the borrower, with the

proportion determined on a "worst case" scenario.

## **Breach of Terms and Conditions by borrowers**

8. How can the best interests of borrowers be protected when a breach of the terms and conditions of the contract occurs?

The immediate issue is what is the nature of the breach? The likeliest cases, given that the borrower is not required to make any payments to the lender, are failure to insure, to pay rates, and to maintain the property. In respect of the first two breaches, the lender must have the right ultimately to require that the borrower make payment, or go to a mortgagee sale. The third is discussed in the answer to question nine.

The overriding consideration, in any breach, should be ensuring as far as possible that the borrower is able to remain living in their home. This suggests that, even when the borrower is in default of a payment such as insurance or rates, the lender takes enforcement action only if it is genuinely necessary to protect the lender's interests. If there is still adequate equity to cover both the outstanding loan, and the unpaid rates and/or insurance, then those should be added to the mortgage (there may need to be provision for a penalty rate to apply so that borrowers did not have an incentive to let payment fall to the lender). There will be difficult judgements in some of these cases. There may be a case for the equivalent of the banking ombudsman to act as a mediator.

9. Should there be guidelines for a maintenance standard which properties, subject to a HEC loan, are required to meet?

It is standard practice for mortgages to include a maintenance covenant. It would make good sense for the maintenance covenant in a home equity conversion loan to be accompanied by a plain English guide explaining what is required.

10. Should property maintenance requirements be part of the initial disclosure?

Yes. It represents a future liability for the borrower which must be met. The nature of the liability and its potential scope both need to be clear. It is also part of the duty of care responsibility which any lender should have when ensuring that the borrower understands what is being taken on.

## **Protection of spouses' and partners' residency rights**

11. Should spouses or partners of borrowers, who are not the property owner, be afforded the same level of protection for their occupancy as the borrower?

Yes. They almost certainly will have rights, in any event, under matrimonial property legislation. The overriding consideration is that, as a matter of best practice, borrowers should ensure that the loan transaction is set up to cover both the property owner and the property owner's partner. The alternative of the loan being called in when the property owner dies, leaving the partner homeless, is unacceptable.

12. Should any protection be extended to spouses or partners who entered into a relationship after the loan has been taken out?

Ideally Yes. However, that protection should not be available automatically as it could force the lender into a totally unanticipated loss (assume, as a scenario, a couple in their 60s who take out a HEC loan. One dies, the survivor re partners with someone in their 40s, and lives until their late 80s at which stage the new partner is in their 60s. If the lender were required to leave the loan outstanding until the new partner died, that could add an extra 20 years or so to the loan term). The borrower should have the right to require the lender to restate the terms of the loan so that the new partner was included, but only to the extent that the restatement was within the lender's lending criteria.

## **Disclosure**

13. Should the HEC documentation illustrate the potential financial position of the borrower five, ten and fifteen years after taking up the loan?

This is absolutely essential. The borrower should be given scenarios of the likely situation through the term of the loan using high and low assumptions for key variables such as interest rates and property value (this was one of the most important recommendations made by the Auditor-General in his recent review of rates postponement schemes, and is part of the practice followed through the counselling process in the scheme).

14. should there be a standard disclosure template applying to all HEC schemes?

Ideally as a means of ensuring a standard approach to the duty of care in disclosure.

15. If so, what should such a disclosure template include?

It should include at least the following:

- The full costs which the borrower will incur in actually taking out a loan including legal, counselling and valuation costs.
  - The commission payable to any financial adviser, both on the initial transaction and on any future borrowings, including any trailing commissions.
  - The expected outstanding balance under the loan, on a regular basis throughout the expected duration, using high and low assumptions on key variables.
  - The borrower's obligations including insurance, rates and maintenance.
  - The circumstances under which the loan is repayable (crucially this should cover whether the loan is repayable if the borrower ceases to live in the property, for example, because he or she is admitted to a rest home).
  - The borrower's rights to draw down further advances (this raises a separate issue; what are the borrower's rights if the lender is unable to make further advances perhaps because its own funding arrangements have fallen through. For a borrower who has made themselves dependent on the ability to draw down further advances, this could be disastrous. We propose that, if this does happen, the borrower should be able to borrow against the property from another lender in priority to the loan from the defaulting lender).
  - Any early repayment rights, and the penalties associated with exercising them.
  - Whether or not the borrowers have the right to transfer the loan to another property and under what conditions.
16. Should subsequent disclosure be required to outline possible consequences if a HEC borrower takes up further loan amounts against the equity in the home?

If this question means should there be further disclosure if the borrower takes out further loan amounts, then the answer is yes.

17. Should information about HEC schemes include the potential effects on entitlements to benefits or supplementary assistance when equity is released as an income stream rather than as capital?

Yes. At the moment, releasing equity as an "income stream" (technically an incorrect term as equity, however released, is capital) would result in that "income stream" being treated as part of a borrower's income for the purpose of any income tested benefits. That is essential information for the borrower.

### **Cooling off period**

18. Should there be a cooling off period and, if so, how long should the

standard cooling off period be for HEC schemes?

Yes. The recommendation is 10 working days. There are related issues. First, if the borrower elects not to proceed during the cooling off period, should the borrower be liable to meet charges such as valuation? Next, should the borrower have a right of repayment, in whole or in part, during the term of the loan and on what conditions including penalty? The interests of older persons suggest yes and at a minimum penalty.

### **Sales through financial agents and advisers**

19. Are there particular constraints or requirements needed for financial agents and advisers selling HEC schemes?

Yes. Financial agents and advisers should have completed an appropriate training course covering not just the terms of home equity conversion loans themselves, but the issues which they raise for older people.

There is one issue which needs very careful consideration. This is whether it should be lawful for financial agents or advisers to approach their existing clients recommending either that they take out a home equity conversion loan, or that they increase the amount of an existing home equity conversion loan. It is very clear that, as a marketing ploy, advisers and agents are being encouraged to do exactly this in order to increase their commission income. The vulnerability of older people, and the crucial importance of ensuring that their ability to cope in later years is not prejudiced by running down their equity unnecessarily suggests that it should be unlawful for advisors or agents to initiate a transaction in this way.

20. Should disclosure of commissions or brokerage payments to financial agents and advisers be a requirement?

Yes. Commissions paid are substantial. Potential borrowers need to know the extent to which the adviser will benefit from the transaction so that they can understand the vested interest the adviser has in getting them to take out the loan.

21. Should financial advisors and agents have specific training before they can act as an agent selling HEC products?

Yes, as already suggested in the answer to question 19.

### **Relationship to other financial products**

22. Should any protections be put in place to ensure that undue pressure is not placed on consumers to purchase other financial or insurance

products and services?

Yes. Undue pressure should not be placed on any one, in any circumstances, to enter into any transaction. The real issue here, surely, is whether financial advisers should be able to offer other financial insurance products at all in the context of a home equity conversion transaction. There may be cases where it is appropriate, for example, to offer house and contents insurance if the borrowers do not currently have insurance. On the other hand, it is imperative to avoid a situation in which a financial adviser could encourage a borrower to take out a home equity conversion loan in order to invest in another financial product which the adviser was marketing. There should be clear protections against this type of practice. The best guidelines would be to enable a financial adviser to sell complementary products with the proviso that any transaction could be voided, and the financial adviser and the institution, fund or other entity with which the monies were invested, be under a joint and several obligation to refund the cost of the product, if on complaint to (say) an appropriate financial ombudsman, it was determined that the transaction was not in the interests of the borrower.

23. Should there be any restriction on the provision of unreasonably related financial products?

Yes. The scenario already outlined of the adviser encouraging someone to take out a loan in order to invest in a financial product the adviser was marketing is an example. The basic assumption with a home equity conversion loan is that the borrower has no other significant financial assets. For this reason, the provision of unreasonably related financial products would almost certainly represent an investment of the proceeds of the home equity conversion loan. It is difficult to think of circumstances in which it would be in a borrower's interests to take out an expensive loan (the cost of HEC loans is significantly greater than the cost of a conventional mortgage) in order to invest in another financial product.

## **Advertising**

24. Are there particular requirements or standards needed for advertising HEC schemes?

This is a difficult question. In a market economy, it is normally hard to argue that a product should be subject to explicit advertising restrictions tighter than those which apply under the general law such as the fair trading act. On the other hand, where there are particular public policy reasons for taking an interest in the consequences of using a product or service, we have been prepared to require advertisements to contain explicit warnings or descriptions of product content (cigarettes; food labelling requirements). There may be a case for considering whether advertisements for HEC schemes should include a warning about the implications of running down equity on persons' ability to cope in future years.

## **issues identified in international literature RE: families**

There are two important issues to be considered here, a borrower's rights to confidentiality and privacy, and the family's expectation of an inheritance.

25. Please write any comments you may have on this issue.

There is evidence internationally that older persons attitudes towards leaving an estate, and the next generation's expectations of receiving an inheritance, are both changing. The Scottish Local Government Finance Review Committee, which reported in November 2006, notes (drawing on Joseph Rowntree research) that "recent survey evidence indicates that for many people the family home is not simply viewed as an asset which should be passed from one generation to the next. Two thirds of those with the ability to leave a bequest say they will not worry too much about not passing on an asset, while more than half of the population say they are "not at all" or "not very" likely to inherit any property." there is also evidence, in New Zealand, reported by groups such as Age Concern that elder abuse is far more common than generally realised and normally focuses on financial issues. In the context of home equity conversion, this could sometimes be influencing a parent not to take out a loan so as to maximise the value of the estate, alternatively, it could be encouraging a parent to do so in order to give the money to the child. The overriding principles nonetheless seem clear. It is the borrower's property and the borrowers have a right to privacy. From the lender's perspective, given the possibility that a child may react negatively when the estate turns out to have a substantial debt, good practice suggests carefully documenting what happened at the time, including the question of independent advice.

### **Protection for borrowers**

26. Are there any steps that could be taken to protect borrowers who are being pressured into taking up or not taking up HEC loans by family members or others?

Probably not. The practice is deplorable but whether the state can intervene between a potential borrower and other family members (or others) is doubtful at best. Indirect measures, such as raising awareness of elder abuse, and supporting agencies who work on behalf of the elderly in this area, maybe the best approach.

This question does, however, emphasise the importance of properly trained professional counsellors being involved to advise borrowers. They are likely to be better placed than anyone else to deal with the kinds of questions borrowers will have about family attitudes, when to discuss and not to discuss the borrowing, and how to respond to family reactions.

## **Transferability of loans to new homes or to a retirement village**

27. Should borrowers have the ability to transfer their full equity, including HEC charge, to a new home or an owner-occupied retirement village unit?

Yes, provided that the loan on the new home or unit is within the lender's parameters and the borrower meets the lender's reasonable costs in facilitating the transfer. Any other requirements would constitute an unreasonable interference with the lender's security. However, another issue arises. Borrowers should understand what their rights, if any, to transfer are before they take out the original loan.

## **Dispute resolution, sanctions and redress**

28. How should complaints and disputes be managed for HEC schemes?  
Please select one or more option.

- A special voluntary or statutory disputes-resolution body
- Arbitration and mediation
- Borrower to litigate any complaints or disputes
- Not sure
- Other (please state)

The best approach is probably the equivalent of the banking ombudsman, established with the agreement of home equity conversion providers. If this is set up as a voluntary arrangement (which has been the practice) then it will clearly bind only those lenders who agreed to join within the scheme. Whether or not a lender was a party to the ombudsman arrangement should be a matter for disclosure at the time the loan is taken out and the implications should be one of the matters covered both in counselling and by independent legal advice.

29. How should HEC scheme providers be sanctioned or penalised for breaches of standards?

The ombudsman should have the power to fix financial or other penalties and publish those on appropriate websites, including requiring the provider to publish information on any penalties it has incurred prominently on the homepage of its own website.

30. Should HEC schemes be regulated by a specific body responsible for the HEC code of practice and its enforcement?

Yes. The office of the Retirement Commissioner who already has this responsibility for retirement villages would seem appropriate.

### **Changes of ownership of schemes**

31. How should borrowers be informed of change in any matter that might have a material impact upon their occupancy rights, services and facilities under a HEC scheme? Please select one option.

- Via a new disclosure statement
- In writing
- Not sure
- Other (please state).....

The best means seems to be a new disclosure statement although given the nature of a home equity conversion transaction, it is difficult to see how a change of ownership of a provider could have a material impact, other than perhaps a reduction in the ability of the lender to meet its obligations such as the obligation to make further advances.

### **Protection against provider default or insolvency**

32. Where home ownership is transferred to a third party or where a person has drawn funds down as an annuity, should scheme insurance be optional or mandatory for HEC providers of reversion schemes?

Insurance should be mandatory as, without this, there can be no certainty that the borrower's right to continuing payments is adequately protected.

### **Specific HEC regulation**

33. If regulation is needed, what form should it take? Please select one option.

- A voluntary industry code of practice
- A government-led code of practice, for example best practice standards. This option could also involve government endorsement of HEC schemes which comply with the standards
- Greater coverage of HEC schemes within the Credit Contracts and Consumer Finance Act 2003, such as additional requirements for HEC schemes over and above those required of other credit products

- Stand alone legislation for the regulation of HEC schemes
- Other (please state)

Standalone legislation, recognizing both the unique characteristics of HEC schemes and the likelihood that they will increase considerably in magnitude.

34. Should there be a requirement for providers of HEC schemes to be registered?

Yes, with provision for deregulation for providers whose conduct merits that sanction. Note that this would require associated measures to ensure protection of existing borrowers from the provider.

### **Consumer information**

35. To what extent and in what form should a consumer information programme be developed to inform the public about HEC schemes?

The retirement Commissioner is best placed to undertake this role, as the office already does in respect of savings generally. There is a clear need for education which will assist older people in particular understand not only the potential benefits, but the downside. Specifically, how does the fit 69-year-old understand the implications for the frail 85-year-old he or she may become of drawing down the equity that may be required to purchase care in future years?

36. Who should provide information on HEC schemes or other options to release equity?

This also seems an appropriate role for the retirement Commissioner.

37. Any additional comments, questions or issues?

The recent review by the Auditor-General of rates postponement deals with a number of best practice and duty of care matters which could usefully be drawn on for home equity conversion schemes generally.