

Jack D. Tavinor

5 December 2019

The Hon. Marlene Kairouz,
Minister for Consumer Affairs, Gaming and Liquor Regulation
Minister for Suburban Development.
Level 26, 121 Exhibition Street, Melbourne, VIC 3000

By email: marlene.kairouz@parliament.vic.gov.au

Dear Minister,

Re: Why does CAV not recognise that the Retirement Villages Act promotes operator complacency?

On 28 October 2019, you released the Issues Paper kicking off the Review of the Retirement Villages Act.

The Issues Paper reveals significant misunderstandings of retirement villages. I am concerned about one misunderstanding in particular – the Financial Model.

From time to time, the operator of my village reminds residents that ‘the Village must be self-sustaining’. What this means is:

- Residents must provide the funds required to run the village (our Maintenance Fee) to cover categories of expense which include General and Administrative Expenses, Property Repairs and Maintenance (including the contribution to the Long Term Maintenance Fund (aka Sinking Fund), Occupancy Expense, Utilities and Wages. On top of the maintenance fee we must make a substantial payment at the end of our stay in the form of a Deferred Management Fee PLUS a contribution to the Village Capital Fund.
- The operator manages the village on a cost-recovery basis, not for profit. If prices of the goods, services and wages that it takes to run the village go up, we must contribute more money to maintain the service level. Our contract does not adequately define what the service level is.
- In spite of the Village showing a surplus of Income over Expenditure for the past 5 years there is an entrenched attitude to increase Maintenance Fees year on year when, in my opinion, there is opportunity for CPI increases to be absorbed thereby offering relief (if only token relief) to cash-strapped residents
- Surplus funds at year end have been added to the Long Term Maintenance Fund and while this provides a safety net for possible future events that are extraordinary in nature the fact remains that the fund does not belong to the Residents but to the operator and the existence of the fund and its healthy balance enhances the value of the Village and directly affects the Deferred Maintenance Fee / Capital Fund contribution when it is paid on sale of Units

If our operator does a good job, the company profit does not go up because it earns its profit from other sources. Why would it bother to do a good job? If the operator does a poor job, its profit does

not go down, at least in short to medium term. The business of managing a retirement village is not an ordinary business.

What can we do if our operator does a poor job of running our village? Go elsewhere? Hardly. If we move out, we have to pay a substantial fee, a Deferred Management Fee plus a Capital Contribution Fee, to the operator. After paying this fee, we are unlikely to have enough money left to pay for another Unit of similar size, standard and location, particularly in a rising market. We are locked in. We can't punish poor management in the same way we can punish a restaurant that serves mediocre food.

The Retirement Villages Act S36 makes provision for a Village to elect a Residents' Committee and thereafter somewhat loosely defines the very limited role and responsibility of such a committee. It does not define any authority that the committee has, particularly in relation to the Financial Management of the Village.

It fails to acknowledge that the Village is our home and that we should, through our Residents' Committee or a sub-committee thereof, have the right of input into all aspects of its Financial (and other) Management and for such input to be heeded.

Under the existing legislation a Residents Committee in a non-Strata Title Village is, effectively, a 'Toothless Tiger' – it can roar all it likes but at the end of the day the operator can choose to ignore it completely.

We have seen instances in other Villages where frustrated residents have taken complaints to the media because their concerns are not being properly addressed by the operator. There is no mechanism to have concerns addressed in a fair, timely and authoritative manner – e.g. an Ombudsman. Taking issues to the media is an action most residents would shy from because of the sensationalist approach the media is apt to take and the adverse reflection such an approach has on the saleability of units as a consequence – a case of 'giving a dog a bad name'.

As mentioned above we contribute, through our Maintenance Fee, to the Long Term Maintenance Fund (aka Sinking Fund) which, in our particular Residence Agreement, is defined as being '...a fund established to cover minor repairs, minor renovations, minor replacements and minor maintenance of the Communal Facilities and the Village, not including the interior or rear garden of the residences or the Fixtures and Fittings in residences'.

Unfortunately there is no clear definition of minor repairs, renovations, replacements etc. and one would be justified in assuming that such items should be covered by the Maintenance Fee contributions. The Long Term Maintenance / Sinking Fund would be better defined as 'a fund to meet maintenance (as opposed to Capital) costs of an unexpected or extraordinary nature such that they could not be forecast or otherwise provided or for which provision (accumulation of funds) has been made over time'.

To the best of my knowledge there is no legislated requirement governing

- The purpose of the Long Term Maintenance / Sinking Fund
- Any limitation on the annual contribution to the fund or the maximum total amount that can be reserved in such fund or any formula to determine these matters

Based on experience (over five years) in my own Village, at the end of each Financial Year there have been funds in excess of the budgeted result. The operator is able to divert these, subject to minimal restriction, in whole or part, to the Long Term Maintenance / Sinking Fund or alternatively to hold funds as Retained Earnings. I have seen examples where surplus funds have been directed to increased rental charges or contributions to wages at the end of the financial year when those items have not previously reflected in the budget for the Village.

In making these comments I would make the following points

- For the last 5 years I have been directly involved in providing Financial Management support to the manager of my Retirement Village in the areas of Budgeting and Performance Monitoring
- The activities undertaken by myself have been acknowledged and supported by the Chairman of the operating company as well as key executives
- All activities have been directed to achieving the best possible outcome for all stakeholders – owner, residents, Village Manager
- Financial management and outcomes have exceeded expectations in all respects

What are the issues?

1. Residents (through their Residents' Committee) have little to no control of the operator's spending but bear the cost of the operator's complacency and / or inefficiency.
2. The lack of normal commercial pressures to perform, resulting in poor service and financial inefficiency. There is a propensity for funds to be wasted through frivolous, unnecessary and profligate spending where there is no robust governance in place to control such issues.
3. Lack of involvement of the Residents' Committee / Sub-Committee in the development of Annual Budgets promotes a sense of mistrust that the best interests of Residents are being represented
4. Lack of detailed monthly interim financial reporting to the Residents' Committee (such as Forecast vs Actual and appropriate variance analysis) further promotes the mistrust and an atmosphere of doubt that can undermine a sense of security so essential to our residents
5. The Retirement Villages Act is not specific enough regarding the presentation of Annual Budgets to the Residents' Committee and the Residents in terms of timing or content nor does it make any provision for a budget to be rejected, by either body, in whole or part
6. The Retirement Villages Act is not specific about when the Statutory Annual Meeting of the Village is to be conducted. This should be stated categorically e.g. within 90 days of the end of the Financial Year with appropriate penalties for non-compliance.
7. The Retirement Villages Act fails to specify the level of information required to be disclosed with the Annual Financial Reports such as the break-down of items included in the larger expense categories of the Village
8. Auditor certification relative to Annual Financial Reports should contain specific reference that issues such as segregation of duties, three way matching and conflict of interest (to name but a few) have all been addressed as part of the audit process as a step to mitigating the chance of serious financial mismanagement and providing some protection to Village staff responsible for financial management

I believe that these issues should be included in the Issues Paper instead of some of the trivial ones that are there? It is my opinion that the paper would have been more relevant had CAV widely consulted residents before preparing it.

Yours faithfully

