Review of the Retirement Villages Act 1986
Submission by Les Scobie, retirement village resident since 2007

Before moving to examine the Victorian Retirement Villages Act 1986 it is important that all parties are aware of the following primary facts when it comes to Retirement Villages.

1. **72% of retirement villages are owned by 'for-profit' operators. The days of the 'benevolent' operator discounting the entry cost by the amount of the 'deferred fee' are well past.**

2. **74% of retirement village residents do not occupy their units on a freehold basis, merely granted a lease or licence to occupy.**

3. **Retirees often pay a price commensurate with an outright purchase price for a similar unit within the general community without ever gaining ownership.**

4. **Contracturally residents have all the financial responsibilities of 'property ownership' like maintenance costs, renovation costs, selling costs, administration costs.**

5. **Contracturally in the order of only 1 in 2 residents have the financial rewards of 'property ownership' such as capital gain. Where granted however the retiree may not be entitled to 100% of any capital gain, it may be shared with the operator. The retiree also becomes proportionally responsible for any capital loss.**

6. **Contracturally residents can lose up to 45% of their in-going payment in a so named 'deferred fee' without ever gaining ownership.**

The following statement by [redacted], the then president of the NSW Retirement Village Residents Association, sums up the entire retirement village industry. It amplifies the financial impact on the capital base of both the occupants and subsequently their families.

“Families need to be aware that what we are talking about here is the transfer of inter-generational wealth, not to families, but into the pockets of large multinationals. Shame about elderly people not having enough money for aged care”

Respected journalist [redacted] also provided clarity as to the reality of the retirement village industry with his article 'Retirement villages: how grandma and grandpa become corporate financiers'.

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

My Part 2 submission to the Financial models and the deferred management fee sector of the Retirement Villages Act 1986 review -

Les Scobie.

Review of the *Retirement Villages Act 1986*
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The regulatory and policy framework (Part 2)
Application and scope of the *Retirement Villages Act 1986*

Financial models and the deferred management fee – 14, 15, 16. (Part 2)

Under 3.4.2 in the Issues Paper is the following statement on the Deferred Management Fee (DMF).

"Despite its name, the DMF is not a fee related to management services and could be more properly characterised as deferred rent. As indicated above, the deferral of this payment leaves residents with more funds for living expenses."

' the deferral of this payment leaves residents with more funds for living expenses'

This is a concept that -

1. Believes the entry cost is discounted to reflect the Deferred Management Fee (DMF) to be paid on departure. The days of the benevolent operator are gone and replaced by 'for-profit' commercially based operators (74% of the market place). Retirees today are paying entry prices often commensurate with a 'buy' price of a similar property within the general community.

2. Believes the occupant is actually living for 'free' in the village until a deferred management fee is extracted from their in-going payment to produce the refundable amount. A concept promoted by the industry by dividing the DMF by the number of months of occupation and presenting this as the monthly 'cost of living in the village'.

This concept is of course a nonsense and difficult to believe Consumer Affairs Victoria subscribe to it. The true cost to the retiree of living in a loan / lease retirement village (74% of villages) is -

- A Deferred Management Fee (DMF).
- Maintenance costs on a property they do not own.
- Administration costs on a property they do not own.
- Selling costs on a property they do not own.
- Refurbishment costs on a property they do not own.
- Providing the operator with working capital at 0% cost. (the refundable amount)
- Loss of earnings on the interest free loan to the operator. (the refundable amount)
- Suffering an inflationary devaluation of their refundable amount over the occupancy period.
- 41% of retirees are not granted access to any capital gains.
- Where granted a share of any capital gain may vary from 100% down to 25%.
- Where granted access to any capital gain retirees are also proportionally responsible for any capital losses.

For example if $800,000 was the in-going amount with a 40% DMF being $320,000 then according to the industry the cost to a retiree of living in that village over the industry average occupancy period of 7 years would be $320,000 / 7yrs / 52wks = $879 per week. A return to the operator in the order of 5% on an $800,000 property the cost of which is fully or near fully funded by the occupant for free, a 5% return on minimal or no long term capital investment cost. In addition the occupant pays all maintenance, administration, refurbishment, and selling costs on the property owned by the operator.

With the increasing value of the property some of which may be shared with the occupants, 41% of the industry do not, the return to the operator will increase each time the unit is sold for an increased price generating a higher deferred management fee. For example on the second sale of the property at say $1.2m and a DMF of 40% the return would be $480,000 / 7yrs / 52wks = $1,318 per week as opposed to the initial $879.

It is interesting at this point to observe that a private property investor would anticipate a return of about 5% on an investment property of $800,000, say $800 per week. The private investor however needs to supply 100% of the purchase capital needed at commercial rates. The retirement village operator gains 100% or near 100% of the capital requirement at zero cost from the occupant as is required by Victorian law. *The granting of a lease or licence to occupy on the mandatory payment of an in-going amount.*

RETIREMENT VILLAGES ACT 1986 - SECT 3
***retirement village** means a community—*

(b) at least one of whom, before or upon becoming a member of the community, pays or is required to pay an in-going contribution;

The operator gains much much more than just the quoted $879 per week of course. The retiree as well as paying a DMF of $320.000.00 ($879 per week) also has to pay -

- Maintenance costs on a property they do not own only occupy.
- Administration costs on a property they do not own only occupy.
- Selling costs on a property they do not own only occupy .
- Refurbishment costs on a property they do not own only occupy.
- Suffers an inflationary devaluation of their refundable amount over the occupancy period.
- May or not be granted access to any capital gains.
- Where granted this share of any capital gain may vary from 100% down to 25%.
- Where granted access to any capital gain retirees are also proportionally responsible for any capital losses.

The following graphic displays two cost components 1. The 'residential tenancy' value eg. $879 per week and 2. a cost specific to residential accommodation living in a retirement village.

Initially when the industry was more on a not-for-profit basis this in-going amount paid was discounted to the value of a similar property within the general community in the order of the deferred management fee amount. This enabled people who had some funds but not sufficient funds to obtain retirement living residential accommodation. As the industry has moved to a more commercial for-profit basis this concept of 'discount' has slowly disappeared with retirees now paying in-going prices commensurate with a 'buy' price yet still paying a deferred management fee often in the order of 40% of the in-going amount on departure.

This can be put into monetary terms –

- Table 1 shows the cost of living in a metropolitan retirement village with an entry price of $800,000. It examines a loan / lease village both with and without any share of capital gain.

- Table 2 displays this cost in direct comparison to remaining in the family home or retaining the capital amount and executing a standard residential tenancy.

- Table 3 shows the reduction in capital value of a retiree over the industry average occupancy period in a village with an entry price of $245,000.

Parameters used -

- Entry price paid $800,000.00.
- Deferred Management Fee at 36%, one example with DMF calculated on the entry fee, one with the DMF calculated on the unit exit value following 2.5%pa capital gain.
- Inflationary devaluation at 2.5%pa on the refundable amount.
- Initial weekly maintenance fees of $150pw plus 2.5% CPI annual increases.
- Initial refurbishment cost of $50,000.00 plus 2.5% CPI annual increases.
- Initial sell costs at $10,000 plus 2.5% CPI annual increases.
- No allowance for lost earnings on the interest free loan to the operator. (the refundable amount)
- Family Home - 2.5%pa capital gain compounded.
- Residential Tenancy - 2.5%pa return flat on retained $800,000 capital, 5%pa flat rental return to landlord.

Table 1

Own Home		**Residential Tenancy**		**Retirement Village 1 – 36% Deferred Management Fee on Exit Price – Capital Gain to Resident**		**Retirement Village 2 – 36% Deferred Management Fee on Entry Price – Capital Gain to Operator**	
Ingoing	$800,000	Ingoing	$800,000	Ingoing	$800,000.00	Ingoing	$800,000
Capital Gain @ 2,5%pa	$140,000	Capital Gain	$0	Capital Gain	$150,949	Capital Gain	$0
Sub-total	$940,000	*Sub-total*	$800,000	*Sub-total*	$950,949	*Sub-total*	$800,000
		Deferred Fee	$0	Deferred Fee	$342,341	Deferred Fee	$288,000
		Sub-total	$800,000	*Sub-total*	$608,607	*Sub-total*	$512,000
		Earnings @ 2.5%pa	$140,000	Weekly Fees	$58,870	Weekly Fees	$58,870
		Sub-total	$940,000	Refurbishment $	$57,985	Refurbishment $	$57,985
		Weekly Rent @ 5%pa	$280,000	Selling/Admin $	$11,597	Selling/Admin $	$11,597
$ After 7 Years	$940,000	$ After 7 Years	$660,000	$ After 7 Years	$480,156	$ After 7 Years	$383,548
				CPI Devaluation	$106,506	CPI Devaluation	$89,600
				Value of Capital after 7 years	$373,649	*Value of Capital after 7 years*	$293,948

What is striking in Chart 1 and Chart 2 is -

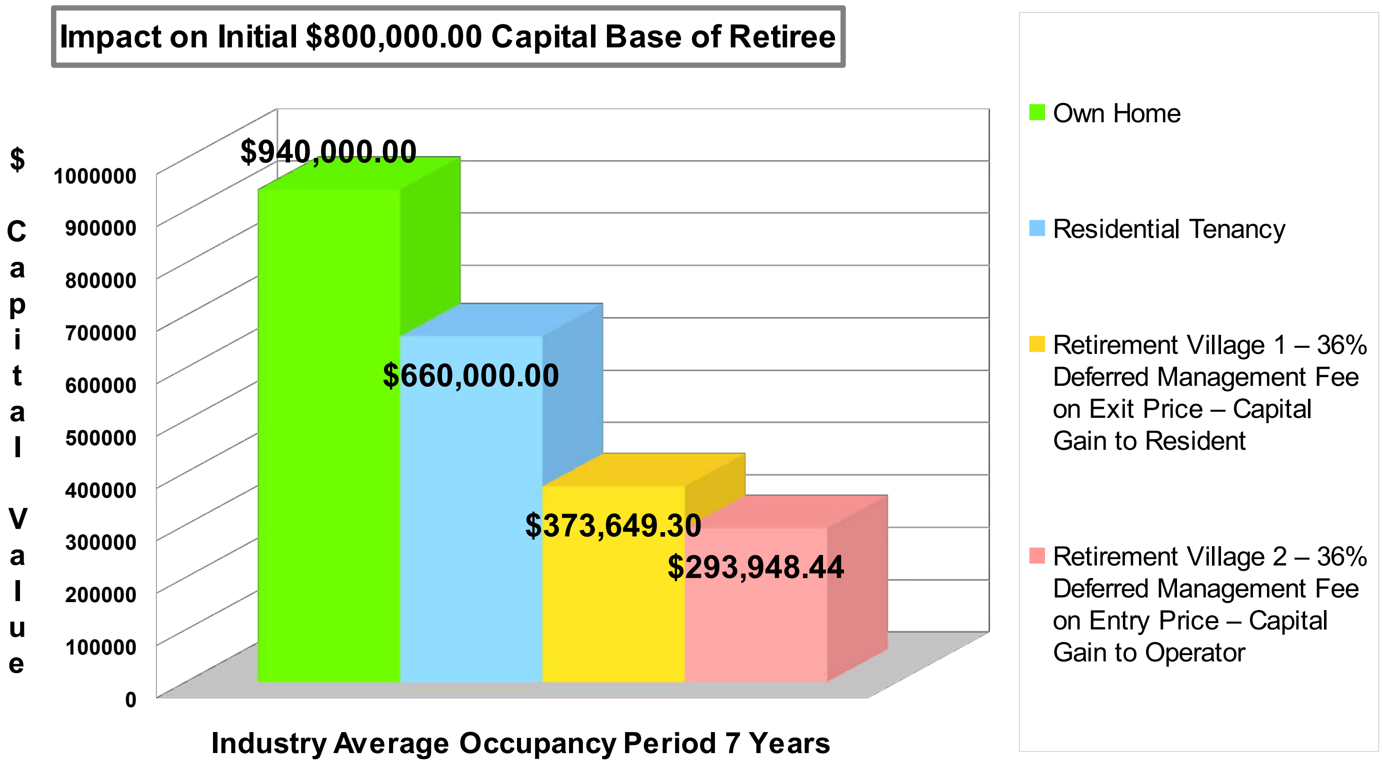
- In Retirement Village 1 where the resident received the value of the capital gain the reduction in the initial capital value of $800,000 was $426,351.00. Over the 7 year occupancy this equates to an actual weekly accommodation cost to the retiree of $1171 per week as opposed to $941 (unit exit value $954,949 x DMF 40% = $342,341 / 7 / 52) that the industry would promote.

- In Retirement Village 2 where the resident DID NOT receive the value of any capital gain the reduction in the initial capital value of $800,000 was $506,052.00. Over the 7 year occupancy this equates to an actual weekly accommodation cost to the retiree of $1390 per week as opposed to the $879 (unit entry value $800,000 x DMF 40% = $342,341 / 7 / 52) that the industry would promote.

- A retiree who sold the family home but secured residential accommodation by way of a residential tenancy agreement and retained their capital base of $800,000 for investment, would have suffered a reduction in capital value in the order of $140,000 at the rate of only $384.61 per week over the 7 years.

- A retiree who stayed in the family home the value of their capital base would have increased by $140,000 over the same period as opposed to the reduction in capital values particularly from the two retirement village options..

Table 2



The following chart shows the financial cost of living in a rural retirement village.
It examines a loan / lease village within the 41% of the market place without access to any share of capital gain.

The parameters used are -

- Entry price paid $240,000.00.
- Deferred Management Fee 25% of in-going cost. 5%pa over the first 5 years.
- Zero access to any capital gain.
- Inflationary devaluation at 2.5%pa on the refundable amount of $180,000.00.
- Initial weekly maintenance fees of $90pw plus 2.5%pa CPI annual increases.
- Initial refurbishment cost of $20,000.00 plus 2.5%pa CPI annual increase.
- No allowance for lost earnings on the interest free loan to the operator. (the refundable amount)

The industry average occupancy period is between 7 to 10 years, note the poor 'financial position of the retiree after 7 years of occupancy. At 16 years the initial capital value of the retiree is totally wiped out.

Table 3

It is beyond argument, the cost to a retiree of living in a Retirement Village is greater than simply just the Deferred Management Fee.

Submission by -

Les Scobie,

Personal details 'not for publication'.

[redacted]