

THE EVOLVING STATUTORY REGULATION OF REVERSE MORTGAGES IN AUSTRALIA'S 'RISK SOCIETY'

FIONA BURNS*

A reverse mortgage is a mortgage 'in reverse'. Under a standard 'forward' mortgage the borrower obtains a loan to acquire a property and eventually attain one hundred per cent equity in that property. Under a reverse mortgage, the borrower releases the equity in the property as cash and uses it for a wide variety of purposes. There are no instalment repayments. Instead the loan (including interest and fees) is generally repaid when the borrower dies or vacates the property. Reverse mortgages are increasingly seen by governments as a legitimate component of retirement planning in the new neo-liberal 'risk society' in which seniors are expected to bear an increasing portion of their retirement expenses. However, governments and their agencies are acutely aware that there are a number of legal and financial problems associated with reverse mortgages. In the Consumer Credit Legislation Amendment (Enhancement) Act 2012 (Cth), the then Labor federal government tackled a number of these problems. It will be argued that such regulation was not incompatible with a neo-liberal perspective and that the regulation of reverse mortgages is still a work in progress.

I INTRODUCTION

When the *Consumer Credit Legislation Amendment (Enhancement) Act 2012* (Cth) ('CCLAA') was debated in the Federal Parliament, the major proportion of the debate was devoted to short-term loan schemes known colloquially as 'pay-day lending'. However, the Bill also contained for the first time significant provisions designed specifically to regulate reverse mortgages. To the extent that reverse mortgages featured in the debate, the general attitude was that reverse mortgages were a helpful financial vehicle for retirement planning, but that limited statutory intervention was necessary.¹ The Bill received assent on 17 September 2012. Some of the provisions of the CCLAA became operative after

* Associate Professor, Sydney Law School, University of Sydney.

¹ See, eg, Commonwealth, *Parliamentary Debates*, House of Representatives, 26 June 2012, 8020 (Bill Shorten, Minister for Financial Services and Superannuation); Commonwealth, *Parliamentary Debates*, House of Representatives, 26 June 2012, 7922–3 (Joe Hockey, Shadow Treasurer); Commonwealth, *Parliamentary Debates*, Senate, 20 August 2012, 5736 (Matt Thistlethwaite).

the day of assent,² while others became operative on 1 March 2013.³ The *CCLAA* made important amendments to the *National Consumer Credit Protection Act 2009* (Cth) ('*NCCPA*') and the *National Credit Code* ('*NCC*').⁴

While reverse mortgages are a relatively new financial vehicle, they became remarkably popular in the first decade of the 21st century. By 31 December 2010, the reverse mortgage market had reached \$3 billion consisting of more than 41 000 reverse mortgage facilities.⁵ Indeed, it is arguable that as the population ages, more Australians may consider taking out a reverse mortgage due to for example, a limited aged pension and the rising cost of living. The rise of the reverse mortgage market reflects new social expectations in regard to retirement planning. It also anticipates the kind of future society that retirees will live in.

While the content, implementation and operation of mortgages generally have been subject to both state and federal legislative oversight,⁶ legislation in the past did not specifically cover reverse mortgages. The purpose of this paper is to discuss and evaluate the evolution of the specific statutory response to reverse mortgages. This article will proceed as follows. First, the article will outline the situation before the passing of the new provisions. In so doing, it will outline the main features of reverse mortgages (in contrast to the ubiquitous 'forward' mortgage) and describe the changed social and financial environment which has spawned the emergence of the reverse mortgage. Second, the article will consider the major financial and legal problems associated with reverse mortgages; and the response of the finance industry and governments to them, prior to the amendments under the *CCLAA*. Third, the article will describe and evaluate the new provisions regulating reverse mortgages. Finally, some comments will be made about the future of reverse mortgages and their management in Australia.

In view of the variety of terms used to label the participants in reverse mortgages and in order to create clarity and consistency, the term 'borrower' will refer to

2 *CCLAA* sch 2 items 1–8 (definitions), item 15 (early payment), item 19 (substitute of heading), item 20 (insertion of a new sub-div B after s 86 of the *NCC* — ending of reverse mortgage by credit provider receiving value of reverse mortgaged property), item 23 (insertion of a new s 93A in the *NCC* — extra requirements for enforcing reverse mortgage if debtor's liability exceeded value of reverse mortgaged property).

3 *CCLAA* sch 2 items 9–14 (provisions applying to licensees and credit providers; provisions for a person other than the debtor to occupy reverse mortgaged property), items 16–18 (provisions concerning contravention and changes to tenancy protection), items 21–2 (enforcement of credit contract and some faults not a basis for a default notice), items 24–6 (provisions relating to a person other than debtor to occupy reverse mortgaged property). See also Australian Securities and Investments Commission, *ASIC Credit Reform Update: Issue 35* (11 February 2013) <<https://www.asic.gov.au/asic/asic.nsf/byheadline/ASIC+Credit+Reform+Update+-+issue+35?openDocument>>.

4 The *NCC* is contained within sch 1 of the *NCCPA*.

5 Deloitte Touche Tohmatsu and SEQUAL, 'Australia's Reverse Mortgage Market Reaches \$3bn at 31 December 2010' (Media Release, 25 May 2011) 1.

6 See, eg, the *Consumer Credit Code* which was contained in the appendix to the *Consumer Credit (Queensland) Act 1994* (Qld) and implemented through uniform state and territory legislation: *Consumer Credit Act 1995* (ACT) s 4; *Consumer Credit (New South Wales) Act 1995* (NSW) s 5; *Consumer Credit (Northern Territory) Act 1995* (NT) s 4; *Consumer Credit (South Australia) Act 1995* (SA) s 5; *Consumer Credit (Tasmania) Act 1996* (Tas) s 5; *Consumer Credit (Victoria) Act 1995* (Vic) s 5; *Consumer Credit (Western Australia) Act 1996* (WA) s 5.

the 'mortgagor', 'consumer' or 'debtor',⁷ and the term 'lender' will refer to the 'mortgagee' or 'credit provider'. The term 'advisor' will be generally used when discussing 'mortgage brokers' and other financial or credit advisors. The term 'senior' will refer to a person who is retired and 60 years or older. The article will refer throughout to 'reverse mortgages' as a product in which the senior releases equity in the home in the form of a loan secured against the family home which does not have to be repaid until the senior dies or vacates the home. Although the use of the term has been circumscribed by the amendments passed in the *CCLAA*,⁸ it has been the most commonly used term to describe the most widespread form of equity release in Australia.⁹

II REVERSE MORTGAGES: CONTEXT, FEATURES AND PROBLEMS

A Basic Features of the Reverse Mortgage

Standard or 'forward' mortgages are ubiquitous and their basic features are well known. A person decides to purchase a property and, in order to do so, borrows money. A typical borrower would be a young person purchasing his or her first home. The lender provides the funds to acquire the property; the borrower simultaneously mortgages the property as security in favour of the lender. The borrower as owner is entitled to reside in the property while repaying the loan over (generally) a long period of time.¹⁰ Assuming that the borrower complies with the repayment plan and all other terms, over a period of time the borrower's interest or equity in the property slowly increases until the borrower finally repays the entire loan and acquires 100 per cent equity in the property.

As the name suggests, the 'reverse mortgage' displays features of the forward mortgage in reverse. Some of the problems associated with reverse mortgages are not unique to them, in the sense that inadequate disclosure mechanisms, dishonest broker advice or poor consumer financial literacy may feature in the creation of forward mortgages. However, problems with information asymmetry and poor consumer understanding are exacerbated in the reverse mortgage context because reverse mortgages are still relatively novel, they have some unique features and some of the potential borrowers are arguably the least equipped to appreciate the consequences of taking out a reverse mortgage. The typical situation is where the borrower is a senior and owns the property — generally the family home —

7 In the *NCCPA* and the *NCC*, potential borrowers are generally referred to as 'consumers' and borrowers are referred to as 'debtors': see *CCLAA* sch 2 item 10, inserting *NCCPA* s 133DB; *CCLAA* sch 2 item 2, inserting *NCC* s 13A.

8 *CCLAA* sch 2 item 10, inserting *NCCPA* s 133DE.

9 ASIC, 'Equity Release Products' (Report 59, November 2005) 4.

10 This will be the case in relation to both old system or common law title (notwithstanding the transfer of the legal estate to the mortgagee) or Torrens title in which the registered proprietor retains the title and the mortgagee acquires a charge over the land: see Peter Butt, *Land Law* (Lawbook, 6th ed, 2010) 581 [18 08], 587 [18 21], 634–7 [18 93]–[18 95].

outright. The lender provides funds to the borrower secured by a mortgage over the home. The borrower draws down the equity in the home and is able to utilise it in a variety of ways, such as: making renovations to the home, purchasing new white goods or paying off debts.¹¹ The borrower is entitled to reside at the property. The interest is 'capitalised' and is secured against the borrower's equity in the property, as the borrower does not make regular repayments. The result is that, instead of gaining equity over the term of the loan, the borrower loses equity in the property. Indeed, if the borrower continues to draw down equity and the interest continues to be 'capitalised', the borrower will have no equity in the property whatsoever. Assuming that the borrower complies with the mortgage terms, it is likely that the mortgage will come to an end when the borrower dies or vacates the property to live in aged-care facilities and the property is sold.¹² However, if the borrower does not comply with the mortgage terms, there is a danger that the lender will be able to take action to enforce the mortgage terms, sell the property prematurely and evict the borrower.

Accordingly, reverse mortgages present three important and special risks. First, reverse mortgages are marketed to seniors who own their own home. This demographic group is a wide one. While there will be a group of seniors who will be capable of managing their financial affairs and understanding the financial implications of reverse mortgages, there will be some who will be unable to do so and could fall prey, for example, to unconscientious conduct by mortgage brokers, lenders and even family members. Second, while there is the danger for all borrowers who mortgage their home that lenders may take action to enforce the mortgage, seniors will be particularly hard hit because they are not likely to be in full employment and therefore their financial capacity to recover from such a disastrous situation is low. Third, one of the major (and attractive) features of reverse mortgages is that there is no need to make capital or interest payments until the borrower dies or vacates the property. Linked to this feature is one of the major dangers associated with reverse mortgages: not only will the senior (or the senior's estate) be left with no equity in the family home, but may owe the lender further funds (beyond the market value of the home) in the form of negative equity. In the event that the mortgage comes to an end during the senior's lifetime, this will mean that he or she will have to make an additional payment to cover the negative equity. This could leave the senior with scarce resources to cover aged-care at the very time that such resources are most necessary.

B The Rise of Reverse Mortgages in a 'Risk Society'

Reverse mortgages have only been available in Australia for the past 10–15 years, although equity release arrangements have been available much earlier in

11 Catherine Bridge et al, 'Reverse Mortgages and Older People: Growth Factors and Implications for Retirement Decisions' (Final Report 146, Australian Housing and Urban Research Institute, May 2010) 14–15 [2.3], 47–8 [3.6]–[3.6.1].

12 See generally ASIC, 'Equity Release Products', above n 9, 16–17; Bridge et al, above n 11, 15–25 [2.4]–[2.4.3].

such countries as the United Kingdom and the United States.¹³ The reasons why reverse mortgages have suddenly become available in Australia and have been taken up by seniors are complex. Nevertheless, there are some important reasons for the rise of the reverse mortgage.

1 The New 'Risk Society'

There has been a significant change in the way that the ownership of property, finance and risk has been viewed in Australia. Some commentators have referred to developments in other Western countries as the 'risk society' in which 'neo-liberal' attitudes towards the role and responsibility of the individual or 'risk subjects' has been increasingly at the forefront of financial regulation and retirement planning.¹⁴ For the purposes of this article, there are six components of the 'neo-liberal' and 'risk society' approach.

First, the role of the state is being transformed from being a paternalistic provider of retirement benefits to one which facilitates and mandates financial facilities for retirement planning, such as superannuation.¹⁵ The state 'is now viewed as an aid in forming the market',¹⁶ such as the market for superannuation. Coupled with the task of 'forming the market', the state is also involved with 'forms of governance that encourage both institutions and individuals to conform to the norms of the market'.¹⁷ As this article demonstrates, the state is becoming an aid to forming the reverse mortgage market.

Second, taking financial risk is increasingly viewed as a normal and expected part of living in a neo-liberal modern society. There has been recognition that there are a variety of risks which citizens face when taking the step to enter the market, such as performance risk (relating to the viability of the investment); prudential risk (pertaining to the viability of financial entities and institutional failure); bad faith risks (such as misrepresentation and unconscionable dealings); and complexity and suitability risk (where the proposed transaction is difficult to understand and/or patently unsuitable for the needs of the citizen).¹⁸ However, 'risk' and 'regulation' are not antithetical, but rather complementary. Unlike the classical liberal approach in which government intervention was inappropriate for a market economy, in neo-liberalism the state remains a central player in the creation and maintenance of 'the conditions where market, freedom and self-

13 ASIC, 'Equity Release Products', above n 9, 22–7.

14 Lorna Fox O'Mahony, *Home Equity and Ageing Owners: Between Risk and Regulation* (Hart Publishing, 2012) 46–9.

15 Superannuation is a complex area which will not be discussed in this article. However, regulatory oversight is performed by three bodies: the Australian Prudential Regulatory Authority, ASIC and the Australian Tax Office. For a helpful discussion of the intricacies of the statutes regulating superannuation, see Gail Pearson, *Financial Services Law and Compliance in Australia* (Cambridge University Press, 2009) ch 11.

16 Ibid 11 [1.3].

17 Wendy Larner, 'Neo-Liberalism: Policy, Ideology, Governmentality' (2000) 63 *Studies in Political Economy* 5, 12.

18 See, eg, Financial Services Authority (UK), *A New Regulator for the New Millennium* (January 2000) 8–9.

interest can be realized'.¹⁹ While it is not possible to remove all financial risks, the state facilitates the market and upholds the risk society by implementing regimes of regulation.

The extent to which intervention and regulation may be tolerated in a neo-liberal context can be seen in the Productivity Commission's articulation of a consumer policy framework,²⁰ which has included the consideration of consumer credit.²¹ The Commission recommended a nationally coherent approach to consumer policy which created a generic framework based on efficiency, fairness and equity,²² but which also allowed for the creation of industry-specific regulation.²³ In relation to the generic framework,²⁴ the Commission emphasised, *inter alia*, the importance of comprehensible, timely and prescriptive disclosure of information to consumers (which ought to address to some degree information asymmetry, bad faith risk, complexity and suitability risk);²⁵ the necessity for there to be protection against unconscionable and deceptive conduct (which ought to redress bad faith risk, complexity and suitability risk);²⁶ and a proactive and protective approach to the vulnerable consumers including aged consumers.²⁷ In relation to industry-specific regulation, the Commission recognised that consumer credit was one area where industry-specific regulation was warranted,²⁸ particularly recommending the introduction of systems of licensing (thereby confronting the problems associated with prudential risk).²⁹ The Commission also observed that, where necessary, government regulation had also proactively protected consumers 'by changing the terms and conditions of transactions'.³⁰ These recommendations have become central issues in consumer credit policy and the successful implementation of subsequent legislation can be measured by the extent the legislation covers these issues and, in a practical sense, deals with them. However, the Commission's recommendations could not be said to have created the prospect that the broad objectives of neo-liberalism would be undermined. The implementation of consumer policy and the regulation of consumer credit transactions would be aimed at creating an orderly and efficient market, avoiding market failure,³¹ making consumers responsible for their actions³² and, as the

19 Steven C Ward, *Neoliberalism and the Global Restructuring of Knowledge and Education* (Routledge, 2012) 190. See also Fox O'Mahony, above 14, 84–5.

20 Productivity Commission, 'Review of Australia's Consumer Policy Framework' (Inquiry Report No 45, April 2008) vol 2.

21 Ibid 98–107 [5.3].

22 Ibid 58–61 [4.2].

23 Ibid xvii (Recommendation 5.1).

24 Ibid xv (Recommendation 3.1).

25 Ibid xxv–xxvi (Recommendation 11.1), 258–69 [11.2].

26 Ibid 147–8.

27 Ibid ch 12. The Commission specifically referred to aged consumers and reverse mortgages: at 295.

28 Ibid 83, 98–108 [5.3].

29 Ibid 83, 107–8.

30 Ibid 2.

31 Pearson, *Financial Services Law and Compliance*, above n 15, 8–9.

32 See also Ward, above n 19, 191; Therese Wilson, 'Vulnerable and Disadvantaged Consumers' in Justin Malbon and Luke Nottage (eds), *Consumer Law & Policy in Australia & New Zealand* (Federation Press, 2013) 288, 305.

Commission observed, 'making consumers more confident about participating in markets'.³³

Fourth, commentators have identified the 'risk subject' or, as Pearson describes, the 'financial citizen' who 'participates in the polity and the market'.³⁴ Indeed, not only must individuals face risks (and, in the context of this article, financial risks), but those risks are 'more individualized'.³⁵ Therefore:

neoliberalism has sometimes ironically set up governing systems whose central activities are not to manage large scale social risk but are, as part of both neoliberalism's moral project and devolving budgets, to 'push risk off' — to actively relocate risk from the state to the individual.³⁶

Accordingly, financial citizens are increasingly expected to take financial risks in order to secure better financial returns and to be less reliant on the public purse. Indeed, it has been suggested that there may be no alternative but to engage with financial risk, particularly in view of the regulatory structures which have been put in place to encourage risk-taking and reduce what are perceived to be inappropriate risks.³⁷ Therefore, for example, under superannuation policy, employees have been transformed into investors.³⁸ This view was articulated in the *National Strategy for an Ageing Australia*, in which it was stated that 'people have a responsibility to make provision for themselves if they are able to and if they expect to have a higher level of income than if they relied on the aged pension alone'.³⁹

Fifth, as well as the 'risk subject', there is the 'risk object'. Property is no longer simply perceived as property to be enjoyed, but as a financial asset which can be utilised in market participation and risk-taking. Superannuation is a prime example of property becoming a financial asset which is invested in the market and subject to risk-taking (as was demonstrated by the global financial crisis).⁴⁰ As will be discussed below, other property such as the family home has become a 'risk object'.⁴¹

Finally, the 'risk subject' needs a 'risk advisor' or financial intermediary who is able to interpret the market and provide advice about increasingly complex financial vehicles. Besides financial planners, there has been the expanding number of mortgage brokers who by 2005 'issued one-third of asset-backed

33 Productivity Commission, above n 20, 2.

34 Pearson, *Financial Services Law and Compliance*, above n 15, 2–3. On the 'risk subject', see Fox O'Mahony, above 14, 61–72.

35 Ward, above n 19, 198.

36 Ibid 199.

37 Fox O'Mahony, above 14, 48; Pearson, *Financial Services Law and Compliance*, above n 15, 7.

38 Pearson, *Financial Services Law and Compliance*, above n 15, 450–2.

39 Bronwyn Bishop, *The National Strategy for an Ageing Australia: Independence and Self Provision* (Discussion Paper, November 1999) 3, quoted with approval in ASIC, 'Equity Release Products', above n 9, 13. See also Bishop, above n 39, 55.

40 Pearson, *Financial Services Law and Compliance*, above n 15, 451–2.

41 See Part II(B)(3).

securities'.⁴² Mortgage brokers have been instrumental in promoting the growth of the reverse mortgage market.⁴³

2 The Ageing Demography

The population is ageing. There are and will be a larger number and proportion of the population both over the age of 65 years and comprising the old 'old' over 85 years of age.⁴⁴ On the other hand, there will be fewer taxpayers as a proportion of the entire population who will be available to meet the costs associated with ageing such as: the aged pension, home-care, aged-care and specialist geriatric care. It has been projected that 'ageing pressures will reduce fiscal sustainability'.⁴⁵ Faced with the increasing costs of ageing, governments have found the prospect of retirees utilising equity release schemes and bearing an increasing cost of their retirement highly attractive.

Therefore, as will be shown below, notwithstanding some of the practical, legal and financial problems which have been customarily associated with reverse mortgages, Australian governments have not taken action to prohibit reverse mortgages.⁴⁶ Instead, they have taken steps, directly and through government instrumentalities to create a financial environment where seniors will be able to seriously consider entering into them without the fear that reverse mortgages are overly risky. This general approach has taken several forms. First, as will be shown below, government instrumentalities have actively intervened in either regulating reverse mortgages when they are empowered to do so, or recommending the further regulation of reverse mortgages.⁴⁷ Second, government instrumentalities have provided information to prospective borrowers about reverse mortgages.⁴⁸ Third, as will be shown below, the former federal government and Treasury determined that industry self-regulation would not be adequate and further supervision of reverse mortgages would be necessary.⁴⁹ The then Federal Minister for Financial Services and Superannuation, Mr Bill Shorten, stated that the amendments to the *CCLAA* would 'maintain public confidence in reverse mortgage providers' and would 'give seniors who are thinking of taking out a reverse mortgage better information to assist them in making such an important financial decision'.⁵⁰

42 Pearson, *Financial Services Law and Compliance*, above n 15, 6.

43 Bridge et al, above n 11, 3, 28–33 [2.6]–[2.7.3].

44 Wayne Swan, 'Australia to 2050: Future Challenges' (Intergenerational Report, Treasury, January 2010) 9 [1.3.2].

45 Ibid 39 [3.3].

46 See Part IV(B).

47 See Parts III(C)(2)–(4).

48 See Part III(B)(2).

49 See Part IV(B)(1).

50 Commonwealth, *Parliamentary Debates*, House of Representatives, 26 June 2012, 8020–1 (Bill Shorten).

3 The Ready-Made Home-Owning Market

The family home has been discovered as another significant financial asset.⁵¹ It has been observed that perceptions of the family home have undergone a significant transformation in recent years. It was not so long ago that the family home was seen as primarily a source of ontological security, the foundation of 'ageing in place' and the cornerstone for inheritance plans.⁵² In the risk society, the family home is considered to be predominantly an investment, which like other investments can and ought to be used for consumption purposes.⁵³ The rise of the reverse mortgage in Australia demonstrates starkly the changed perception of the home. It is no longer considered unusual for seniors to mortgage their home (risking eviction from the home) at a time in life when: they are no longer employed; they are otherwise dependent upon an aged pension or limited savings; and where the precious equity in the home is a finite resource.

There is a ready-made home-owning market as a high proportion of retirees in Australia own their own home.⁵⁴ Retirees are reliant on pensions and investments which may not cover all the costs associated with retirement. Some retirees worked at a time when there was no compulsory superannuation scheme;⁵⁵ and others, particularly women, did not work full-time or undertake any formal employment, preferring to be unpaid homemakers. A reverse mortgage offers the opportunity to acquire goods or services without having to downsize or make immediate repayments of capital and/or interest.⁵⁶

In the 'risk society' it is assumed that seniors ought to be able to exercise their autonomy, bear risks and adverse consequences associated with reverse mortgages. Therefore, the question becomes a regulatory one: to what extent and to what kind of risks ought the senior be exposed?

4 The Attraction of Reverse Mortgages for Lenders

Australia has a wide range of lending bodies including banks, credit unions and building societies, and some of these institutions have been willing to participate in equity release lending. While the global financial crisis led some institutions to abandon equity release lending,⁵⁷ there are still a significant group

51 See generally Rachel Ong, 'Unlocking Housing Equity through Reverse Mortgages: The Case of Elderly Homeowners in Australia' (2008) 8 *European Journal of Housing Policy* 61; Bruce Bradbury, 'Housing Wealth as Retirement Saving: Does the Australian Model Lead to Over-Consumption of Housing?' (Paper presented at the 30th General Conference of the International Association for Research in Income and Wealth, Portoroz, Slovenia, 25 August 2008) <<http://www.iariw.org/papers/2008/bradbury.pdf>>; Richard G Reed, 'The Increasing Use of Reverse Mortgages by Older Households' (Paper presented at the 15th Annual Pacific Rim Real Estate Society Conference, 18–21 January 2009).

52 Fox O'Mahony, above 14, 138–46.

53 Ibid 146–54.

54 ASIC, 'Equity Release Products', above n 9, 13–14.

55 Pearson, *Financial Services Law and Compliance*, above n 15, 450.

56 Bridge et al, above n 11, 47–9 [3.6]–[3.6.3].

57 Ibid 15 [2.4]. Settlements are still to reach pre-global financial crisis rates: Deloitte Touche Tohmatsu and SEQUAL, above n 5, 1.

of lending bodies which find reverse mortgage lending financially attractive and sustainable.⁵⁸

For example, under a forward mortgage, the lender may provide significant purchase capital (which is sometimes almost the entire market value of the property). The lender has effectively had to make a significant investment in the property. However, when lending under a reverse mortgage, the lender does not have to provide purchase capital upfront. Instead, typically the lender lends only a portion of the market value (generally 50 per cent or less) and leaves the compound interest to further and quickly release in its favour the equity in the property.⁵⁹ To put it another way, the lender is able effectively to purchase the equity in the property for a lot less than the market value.⁶⁰ Moreover, if the reverse mortgage continues for many years or decades, it is likely that the lender will also be entitled to a proportion (if not all) of the capital appreciation of the property (due to the ongoing imposition of compound interest on the loan); whereas under a forward mortgage the borrower is likely to benefit from the increase in the market value of the property over time.

From a broad demographic perspective, there is another reason why reverse mortgages have been developed and promoted by financial institutions. As the population ages, there will be more seniors as a proportion of the total population.⁶¹ This will mean that while younger groups will continue to borrow under forward mortgages, it is likely that this portion of the credit market will decrease, while the potential for reverse mortgages will markedly increase. In terms of economic survival and market share, it makes sense for financial institutions to develop equity release products such as the reverse mortgage.

However, financial institutions have not considered all aspects of reverse mortgages as beneficial to them. Reverse mortgages are more open-ended and less predictable than forward mortgages. They lack a timeframe based on a repayment structure. Under a forward mortgage, the parties negotiate a repayment scheme, thereby setting down when the loan ought to be repaid. The lender is able to determine its own borrowing requirements over the period of the loan. In contrast, it is not possible to predict how long the reverse mortgage will last because (assuming that the borrower complies with the mortgage terms) the borrower is not obliged to make any repayments until the mortgage comes to an end. Generally, a reverse mortgage will come to an end when the property is sold after the borrower dies, the property is vacated, or the borrower breaches a fundamental condition of the mortgage.⁶²

58 Bridge et al, above n 11, 16–20 [2.4]–[2.4.1].

59 Ibid 21–2 [2.4.2].

60 See, eg, ASIC, “‘All We Have is This House’: Consumer Experiences with Reverse Mortgages” (Report 109, November 2007) 16, where a participant in a review commented that the debt would be likely to double after 12 years due to the compound interest.

61 Swan, above n 44, 9–11 [1.3.2].

62 ASIC, ‘Equity Release Products’, above n 9, 16.

III THE REVERSE MORTGAGE: THE BORROWERS' RISKS AND THE NEED FOR REGULATION

A Classical Contract and Limited Statutory Oversight

After the introduction of reverse mortgages during the first decade of the 21st century, they were not specifically regulated under statute. Leaving aside the fact that they were new on the market, there were other reasons. Reverse mortgages still represent a small proportion of the mortgage market.⁶³ The complex issues they raise were neither fully identified nor considered to be a major threat to the financial well-being of borrowers generally and there had been little experience in Australia of their potential adverse impact. The considerable evidence from comparator overseas countries that equity release could be fraught with problems was initially ignored.⁶⁴

It is arguable that early reverse mortgage transactions were immediately imbued with the classical liberal interpretation of contract based on autonomy, self interest, rational choice, freedom to negotiate and (subject only to pre-existing statutory regulation) relative freedom from government interference.⁶⁵ Indeed, the early reverse mortgage was in some ways the apotheosis of classical liberal contractualism. Reverse mortgages were advertised as providing a new and exciting opportunity for the exercise of financial freedom and the unlocking of financial wealth in a flexible way.⁶⁶ Many of the novel features of the reverse mortgage were unregulated and left to the negotiation between the parties such as: the inclusion of a No Negative Equity Guarantee (NNEG); a cap on the ratio of the value of the loan to the market value of the property; and what conduct constituted default.

Initially, it was assumed that reverse mortgages were already adequately regulated by general contractual doctrines and state and federal statutes. First, there were several important general common law and equitable doctrines which mandated procedural fairness in relation to the formation of contracts.⁶⁷ In addition, some state legislation dealt with procedural and substantive unfairness, most notably the *Contracts Review Act 1980* (NSW) which allows a court to vary a contract or

63 Ibid 12.

64 ASIC reported that there had been difficulties with equity release in comparator countries such as the United Kingdom and the United States: *ibid* 22–6.

65 See, eg, P S Atiyah, *Essays on Contract* (Clarendon Press, 1990) 10–17.

66 See, eg, the details of a Transcomm Credit Co-operative Ltd advertisement for its reverse mortgage, which were ultimately found by ASIC to be untrue: ASIC, 'ASIC Stops Misleading Reverse Mortgage Advertising' (Media Release, 06–093, 29 March 2006).

67 See, eg, the doctrine of undue influence: *Johnson v Buttress* (1936) 56 CLR 113. See also the doctrine of unconscionable dealing: *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447; *Asia Pacific International Pty Ltd v Dalrymple* [2000] 2 Qd R 229.

declare it as wholly or partly void when the contract is 'unjust in the circumstances relating to the contract at the time it was made'.⁶⁸

Second, many reverse mortgages were likely to have been covered by the then *Consumer Credit Code* ('CCC')⁶⁹ because the definition of 'credit' under the CCC included situations where the payment of a debt owed by one person to another was deferred.⁷⁰ Moreover, the CCC applied to mortgages which were given by natural persons where the credit was wholly or predominantly for personal, domestic or household purposes; and the credit was made available by a credit provider who was in the business of providing credit.⁷¹ A typical reverse mortgage would have fulfilled these criteria. The CCC regulated a diverse range of matters including the form and content of the mortgage;⁷² disclosure requirements such as detailed information about the terms upon which the credit is made,⁷³ such as interest rates; and the provision of the mortgage document to the mortgagor within 14 days.⁷⁴ The CCC also enabled the court to re-open a mortgage which was alleged to be unjust, having regard to whether there had been unfair pressure or undue influence exerted; and if appropriate set aside or modify the mortgage or relieve the mortgagor from paying an amount which was in excess of what the court considered was reasonably payable.⁷⁵

Even if the CCC was not applicable, there were other relevant statutes prescribing and proscribing conduct in relation to the enforcement of mortgages. For example, reverse mortgages were subject to state legislation governing the registration and enforcement of Torrens title mortgages.⁷⁶ Reverse mortgages were also under the jurisdiction of the Australian Securities and Investments Commission (ASIC) to take steps to redress misleading advertising.⁷⁷

However, as will be explained below, such general law and statutory regulation were insufficient to protect all vulnerable borrowers from the stratagems of lenders and mortgage brokers.⁷⁸ It could not be assumed that borrowers acted rationally or in their best interests. As studies in behavioural economics have

68 *Contracts Review Act 1980* (NSW) s 7(1). There are a wide variety of factors to which the court may have regard in order to determine whether the contract is unjust including: the material inequality of the bargaining power between the parties; whether the provisions of the contract were subject to negotiation; whether the contract imposes conditions which are unreasonably difficult to comply with; the parties' relative economic circumstances, educational background and literacy; the intelligibility of the contract; whether independent advice was sought and the commercial or other setting of the contract: at s 9.

69 The CCC, which was contained in the appendix to the *Consumer Credit (Queensland) Act 1994* (Qld), came into operation on 1 November 1996 and was adopted into the laws of each of the states and territories: see, eg, *Consumer Credit (New South Wales) Act 1995* (NSW).

70 CCC s 4(1).

71 Ibid ss 6(1), 8.

72 Ibid ss 38–41.

73 Ibid s 15.

74 Ibid s 39.

75 Ibid s 70.

76 See, eg, *Real Property Act 1900* (NSW) pt 7 div 3.

77 *Australian Securities and Investments Commission Act 2001* (Cth) s 93AA.

78 See Parts III(C)(2)–(3), (D).

demonstrated, people entering into contracts do not necessarily read the contract and may not be equipped to understand fully its terms or the legal and practical ramifications.⁷⁹ Accordingly, authorities began to realise the problems associated with reverse mortgages demanded greater intervention.⁸⁰

B Problems Associated with Reverse Mortgages before Specific Regulatory Intervention

From the perspective of the borrower, the drawbacks could be seen at four levels.

1 General Observation — Findings of ASIC

When reverse mortgages were initially introduced, certain features appealed to the borrowers' self-interest and these were the mainstays of advertising campaigns. For example, the prospect that retirees could have additional cash, without repayments, which may not affect their pension entitlements or their taxation liability, was a kind of financial nirvana.⁸¹

ASIC undertook a groundbreaking investigation into reverse mortgages by conducting detailed interviews with borrowers who had taken out reverse mortgages three years before the study.⁸² The study found that: borrowers did not understand how reverse mortgages worked and how the release of equity could have an adverse effect upon their future retirement planning; there were significant limitations and gaps in the advice that they were given; and the products were not always suitable for the specific needs of the borrower.⁸³ In short, the borrowers did not grasp that in a 'risk' society, financial institutions were also entitled within the law to act in their self-interest; and some borrowers regretted taking out a reverse mortgage.⁸⁴ Some major issues are outlined below.

2 Pre-Contractual Issues

Borrowers suffered from significant disadvantages because of informational deficits.

79 See, eg, Christine Jolls, Cass R Sunstein and Richard Thaler, 'A Behavioral Approach to Law and Economics' (1998) 50 *Stanford Law Review* 1471; Russell B Korobkin and Thomas S Ulen, 'Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics' (2000) 88 *California Law Review* 1051; Justin Malbon, 'Shopping for Credit: An Empirical Study of Consumer Decision-Making' (2001) 29 *Australian Business Law Review* 44.

80 See, eg, Part III(B)(1).

81 ASIC, 'ASIC Stops Misleading Reverse Mortgage Advertising', above n 66.

82 ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 5.

83 Ibid 6–7.

84 Bridge et al, above n 11, 73–4 [4.4.3]; ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 7.

(a) *Lenders Providing Misleading Information*

Lenders misled potential borrowers in a calculated and egregious fashion. For example, a lender advertised that borrowers under their reverse mortgages would be highly protected because the mortgage would never secure more than 50 per cent of the value of the property; the mortgage contained a measure to protect the borrower against negative equity; and the drawdowns under the mortgage would not affect pension entitlements.⁸⁵ None of these claims were true; and ASIC took steps to redress the misleading information.⁸⁶

Another example was when a lender described the mortgage as a 'reverse mortgage' when in fact it required ongoing repayments during the course of the loan. As the borrowers (who were seniors) had not made the requisite repayments, the unfortunate result was that the lender was able to take action to sell the property and evict the borrowers.⁸⁷

(b) *Unregulated Advisors Providing Misleading or Incomplete Information*

Some unregulated advisors such as mortgage brokers acted in their self-interest and displayed a scant concern for the needs of borrowers and in some cases provided misleading or incomplete information.⁸⁸ For example, *Choice* magazine undertook a shadow shopping exercise in which prospective borrowers sought the advice from mortgage brokers about various reverse mortgages on offer. The exercise demonstrated that some mortgage brokers: acted in their self-interest (by recommending the client borrow more than was necessary, thereby increasing the mortgage broker's commission); gave no information about alternative approaches (such as downsizing); gave no information on the impact of the loss of equity and the borrower's inability to use the equity for aged-care in the future; or gave incomplete information about the terms of the mortgage (such as failing to discuss the absence of a NNEG).⁸⁹ One of the major problems was that mortgage brokers were not subject to any formal licensing arrangement or legislative oversight in relation to the advice provided about mortgages generally.⁹⁰

85 In relation to the features of the Transcomm Credit Co-operative Ltd mortgage, see ASIC, 'ASIC Stops Misleading Reverse Mortgage Advertising', above n 66.

86 Ibid.

87 Consumer Credit Legal Centre (NSW) and Consumer Action Law Centre, Submission to NSW Office of Fair Trading, *National Finance Broking Legislation Inquiry*, March 2008, 13.

88 An interesting potential indication of self-interest can be found in Bridge et al, above n 11, 32 [2.7.3], where mortgage brokers suggested what would be appropriate reforms to the reverse mortgage industry. At the top of the list were increases in up-front fees and commissions, followed by changes that would increase the efficiency of the application process and changes that would reduce the time needed to explain the product to clients.

89 Uta Mihm, 'Reverse Mortgage Shadow Shop: Our Shadow Shop Revealed Poor Advice and Information From Reverse Mortgage Sellers', *Choice* (online), 27 February 2007 <<http://www.choice.com.au/reviews-and-tests/money/borrowing/your-mortgage/reverse-mortgage-shadow-shop.aspx>>. Some of the important alternatives to reverse mortgaging a property are listed in ASIC, 'Equity Release Products', above n 9, 30.

90 ASIC, 'Equity Release Products', above n 9, 43–4.

(c) A Lack of Financially and Legally Educated Advisors

One general difficulty was that there were no mandatory standards for the provision of legal or financial advice about reverse mortgages.⁹¹ Even when accountants, lawyers and mortgage brokers were acting disinterestedly, trying to provide relevant and meaningful advice, they were not always equipped to do so. Reverse mortgages are a specialist form of mortgage requiring an understanding of the unique financial consequences of their operation. Borrowers who had researched reverse mortgages complained that they knew as much if not more than the advisor.⁹² Another complaint evident in the ASIC survey was that borrowers were not provided with tailored financial data mapping out the likely course of the reverse mortgage over various stages of the loan,⁹³ for example: the likely depletion rate of their equity in the home; the impact of compound interest; how a variable interest rate could hasten the depletion of their equity in the home; or the ongoing costs for the running of the mortgage such as administrative fees or fees to re-evaluate the value of the property during the course of the mortgage.⁹⁴

3 The Mortgage and Its Terms

Although theoretically, the parties could have negotiated the terms of the contract, lenders produced their own reverse mortgages; modified their own standard mortgages; or relied on an industry-based template.⁹⁵ Therefore, borrowers faced the problem that there may not be any meaningful negotiation process. In addition, borrowers faced the following difficulties.

(a) The Presentation of the Mortgage

There was no standard method of presentation of the reverse mortgage, nor was it necessary to confine the mortgage to one document. Some were lengthy documents, sometimes with conflicting and confusing terminology.⁹⁶

(b) Negative Equity

Upon the introduction of reverse mortgages, one of their most problematical characteristics was the prospect of 'negative equity'. Reverse mortgages involve the depletion of the borrower's equity in the home. Such depletion comprises not only the capital borrowed, but also compound interest and administrative fees. An advantage of a reverse mortgage may be that the borrower is shielded from

91 ASIC expressed the view that overall reverse mortgages would not be subject to the financial services regulatory regime: *ibid* 42–3.

92 Bridge et al, above n 11, 82 [5.3.1].

93 ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 15–16.

94 Bridge et al, above n 11, 73–5 [4.4.3]; ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 23–30.

95 The reverse mortgage developed by ABN AMRO (and offered by the Royal Bank of Scotland) is used by a number of lenders and covers 70 per cent of the reverse mortgage market: Bridge et al, above n 11, 17 [2.4.1].

96 Consumer Affairs Victoria, *Preventing Unfair Terms in Consumer Credit Contracts* (2009) 50.

the depletion of equity by the value of the property rising,⁹⁷ so that the additional capital value hedges the borrower against the cost of the loan. However, property prices may not necessarily rise. Moreover, as there may be no precise date for the mortgage to come to an end, it is possible that in time the debt exceeds the property's market value. Once the borrowing limit has been reached, the ongoing compound interest and fees would send the debt into 'negative equity' whereby part of the debt would not, in practical terms, be secured by the property. Therefore, the term 'negative equity' (which may be seen to be a contradiction in terms) signifies that the debt is secured, but the value of the security is not sufficient to cover the full value of the debt.⁹⁸

The concept of 'negative equity' is not a new one. In Australia, it is recognised that the security afforded by the traditional forward mortgage may not be sufficient to cover the debt owed. Therefore, mortgages contain personal covenants so that the lender can recover any balance outstanding (or 'negative equity') from the borrower if the value of the property does not fully cover the debt.⁹⁹ In view of the usual approach to forward mortgages, it is not surprising that reverse mortgage lenders offered mortgages which did not restrict the borrower's liability to the value of the property; and/or demanded that borrowers be personally liable for any negative equity generated under a reverse mortgage.

However, the context in which reverse mortgages are created is different from forward mortgages because the borrower will be a senior who will have limited opportunity to augment earnings or savings or repay the debt early. Moreover, the compound interest which is imposed on borrowers¹⁰⁰ is likely to have the effect of significantly depleting equity at an accelerating rate. Therefore, following overseas jurisdictions,¹⁰¹ one of the important competitive and preferable features of some reverse mortgages became that the mortgage contained an NNEG clause. Under the guarantee the lender agreed that if upon the sale of the property, the proceeds (after expenses had been deducted) did not cover the value of the debt owed, the lender would not seek to recover the balance from the borrower or the borrower's estate. Thus when discharging the mortgage, the lender would be restricted to the value of the security for the payment of the debt and expenses.

There was also the issue of when the NNEG would not operate due to the adverse conduct of the borrower. Therefore, lenders restricted the NNEG clause when the borrower had committed an act of default such as failing to pay rates and taxes in relation to the property, failing to care for the property or deliberately damaging it.¹⁰²

97 See ASIC, 'Equity Release Products', above n 9, 14.

98 Ibid 34–5.

99 The personal covenant can be relied upon when the lender exercises its power of sale: *Rudge v Richens* (1873) LR 8 CP 358; *Gordon Grant & Co v Boos* [1926] AC 781; *Commonwealth Bank of Australia v Buffett* (1993) 114 ALR 245. However, if the lender forecloses, the lender will be deprived of the right to sue on the personal covenant: see, eg, *Conveyancing Act 1919* (NSW) s 100; *Fink v Robertson* (1907) 4 CLR 864.

100 See Part III(B)(4)(b).

101 ASIC, 'Equity Release Products', above n 9, 35.

102 Ibid.

(c) Conduct Amounting to Default under the Mortgage

One of the major advantages of standard reverse mortgages for borrowers is that repayment is postponed until the borrower dies, or until the borrower vacates the property or sells it. Conversely, one of the dangers facing a borrower is that an event which is deemed to be a default could happen. An early event of default (even one over which the borrower contended he or she had little control) would enable the lender to call in the loan early and take steps to sell the property well before the borrower's death or the borrower's voluntary vacation of the property.

Events of default under reverse mortgages could have three alternative features. First, the mortgage may state that specific conduct or omissions such as vacating the property or failing to maintain the property is a default entitling the lender to bring the mortgage prematurely to an end.¹⁰³ Second, there may be a general default clause which states that a breach of any term will constitute a default entitling the lender to bring the mortgage prematurely to an end. In either case, the default could be relatively minor in practical terms, but it would be enough to empower the lender to exercise its rights.

Third, as noted above, default provisions have been tied to the protection of the NNEG so that the lender is not only entitled to bring the mortgage to an end but is also entitled to seek repayment of the full debt, rendering the NNEG otiose. Indeed, it would be open for lenders to insist that upon any default (however minor or broadly defined) there would be no NNEG protection.¹⁰⁴

(d) Non-Titleholders

One of the rights of a landowner is that he or she may invite anyone she chooses to reside with him or her. The conditions which govern the occupancy would be determined by the parties. When seniors are involved, there may be a non-titleholder such as a spouse, relative or carer residing with the senior. The senior may have obligations to disabled children or grandchildren; and it would not be uncommon for a senior to have a relative living with him or her to assist with day-to-day chores. It has been an important way for seniors to remain in familiar surroundings and 'age in place'.¹⁰⁵

In the reverse mortgage context, the existence of non-titleholders can have undesirable consequences. Lenders may decide that they do not wish to lend to a senior with whom non-titleholders reside for fear that non-titleholders may raise rights against the lender in the future. Alternatively, lenders could insist that the non-titleholder's occupancy of the property without the lender's consent would be an event of default, so that the lender could bring the mortgage to an end and the non-titleholder would have no right to remain in the property. Non-

103 Ibid 37.

104 Ibid 35.

105 For a consideration of the advantages of 'ageing in place', see Fox O'Mahony, above n 14, 125–38.

titleholders who are not party to the mortgage will have no rights in the event that the borrower dies and could face the prospect of eviction.¹⁰⁶

4 Financial Issues

Borrowers have navigated a variety of financial issues governing the mortgage's structure. Such matters would individually and collectively determine the extent to which the equity in the property would be depleted.

(a) The Borrower's Age

Reverse mortgages have been available to seniors who were 55 years of age and older,¹⁰⁷ although it was more likely that seniors in their mid-seventies who had 100 per cent equity in their home would enter into a reverse mortgage.¹⁰⁸

Although the age of a borrower may appear an issue of little relevance, it can be crucial for both the borrower and the lender. Generally speaking, borrowers in their sixties will only be able to release a relatively small amount of the equity in the home. It will be assumed that the borrower will live a decade or more longer than older seniors; and the remaining equity will be necessary to cover the compounding interest and fees. Therefore, for borrowers the optimum equity release opportunity is when they are older because they are able to release more equity in their favour. Their likely remaining life span will be limited, so that the period in which the compounding (and equity depleting) interest runs will be shorter than for younger borrowers.

For lenders also, the age of the borrower presents different advantages. A loan to a 'young' senior means that the lender may acquire a large portion of or even the entire equity in the home on the basis of a loan of relatively small amount, for example 20 per cent of the home's original market value. However, the lender has potentially three problems. One is that lender still has to service the loan from its own borrowings and make a profit. Another is that, assuming that the borrower complies with the terms of the mortgage, it is uncertain how long the mortgage will continue, unless the mortgage is limited to a specified timeframe. Finally, it is possible that when the mortgage comes to an end, the value of the debt exceeds the property's market value. If the mortgage contains a NNEG, then it will be questionable whether the lender will make a sufficient profit on the transaction. Therefore, it is arguable that for lenders, 'older' seniors are preferable borrowers because it is likely that the loan period will be shorter and it is less likely that the ultimate debt will exceed the property's market value.

106 ASIC, 'Equity Release Products', above n 9, 40.

107 Ibid 16.

108 See Deloitte Touche Tohmatsu and SEQUAL, above n 5, 1.

(b) Compound Interest

Reverse mortgages are subject to compound rather than simple interest (and in relation to some mortgages there are ongoing monthly fees).¹⁰⁹ Plainly put, the interest is not only chargeable in respect to the loan, but also in relation to the further interest and fees which accrue (including such matters as re-evaluation fees). Perhaps compound rather than simple interest is charged because arguably from the perspective of the lender, reverse mortgages are high-risk products. Certainly, lenders are aware of the effect of a NNEG and the potential longevity of the borrower.¹¹⁰ However, this appears to overstate the lender's vulnerability, particularly as the borrower already owns the security outright; and the operation of compound interest will accelerate the depletion of the borrower's equity.

(c) Variable or Fixed Interest?

Borrowers have had to determine whether to take out loans subject to fixed or variable interest, although it appears that in most cases borrowers have preferred variable interest rates.¹¹¹ In the event that borrowers have opted for a variable interest rate, the interest rates imposed on reverse mortgages have been higher than that charged in regard to standard forward mortgages.¹¹² The explanation has been that from the lenders perspective reverse mortgages are high-risk products.¹¹³ However, as stated above, this is questionable.

Borrowers have also been subject to the cost of break fees when attempting to convert their fixed term loan to a variable interest mortgage,¹¹⁴ although recent changes have restricted the capacity of lenders to impose substantial break fees.¹¹⁵

(d) Protected Equity in the Home

Sometimes borrowers had the choice of negotiating a protected equity in the property. This means that they retained and quarantined a portion of the equity in the property for themselves during the course of the mortgage.¹¹⁶ The lender can only recover the debt from the unprotected portion of the equity. However, if a borrower was able to avail himself or herself of the protected equity alternative, then it is likely that the value of the original loan as a proportion of the value of the property would be less than if no protected equity had been negotiated.

¹⁰⁹ Bridge et al, above n 11, 20–1 [2.4.2].

¹¹⁰ Ibid 20 [2.4.2].

¹¹¹ Ibid.

¹¹² Ibid.

¹¹³ Ibid.

¹¹⁴ Ibid 21 [2.4.2], 73 [4.4.3].

¹¹⁵ Break fees can be challenged if they are unconscionable and therefore breach *NCC* s 78, or if they are unfair and therefore breach the *Australian Securities and Investments Commission Act 2001* (Cth) which contains unfair contract terms provisions: at pt 2 div 2 sub-div BA. For a helpful discussion of how the legislation can be used in relation to break fees, see generally: ASIC, 'Early Termination Fees for Residential Loans: Unconscionable Fees and Unfair Contract Terms' (Regulatory Guide No 220, November 2010).

¹¹⁶ Bridge et al, above n 11, 22 [2.4.2].

(e) *Loan to Value Ratio (LVR)*

Borrowers also had to consider and negotiate what will be the value of the initial loan and its proportion of the market value of the property at the time the mortgage was created. Lenders offered different loan to value ratios, some as high as 50 per cent.¹¹⁷ However, the effect of the loan to value ratio upon the inevitable depletion of equity cannot be understood in isolation. Rather, it would have to be cojoined with a number of factors including the likely interest rate (if the interest rate were variable) and the age of the borrower.

(f) *Fees*

Borrowers were subject to application fees and administrative fees for the ongoing review and servicing of the loan which were controversial and criticised.¹¹⁸ Some mortgages also provided for re-evaluation fees which permitted the lender to have the property professionally re-valued at the cost of the borrower.¹¹⁹ Some lenders were able to introduce new fees as well as change pre-existing fee structures.¹²⁰ Usually the fees would not be paid upfront by borrowers, but would be secured by the property, subject to compound interest rates and generally payable when the mortgage came to an end.¹²¹

(g) *How the Equity Will be Accessed*

One of the touted advantages of reverse mortgages was (and is) that the equity may be released flexibly. Depending upon the lender, borrowers have had a choice of whether to take a lump sum, drawdown the equity in stages or to have a credit facility readily available to be utilised on a flexible and ad hoc basis.¹²² How the equity is released will determine the extent and rate at which the equity in the property will be depleted; and an early or imprudent release of equity can mean that the borrower is unnecessarily charged interest and loses valuable equity in the property.¹²³

(h) *How the Equity Will be Used*

Equity can be released for a variety of purposes, such as: repairs to the house; purchase of whitegoods; supplemental expenditure for day-to-day necessities; holidays; or financial gifts to relatives.¹²⁴ The use of the equity will have a bearing upon how the equity is released so that, for example the purchase of a car would warrant a lump-sum drawdown, whereas the use of the funds for day-to-day

117 Ibid 21–2 [2.4.2].

118 Ibid 20 [2.4.2], 75 [4.41]; Consumer Affairs Victoria, above n 96, 48.

119 Consumer Affairs Victoria, above n 96, 50.

120 Ibid 48.

121 Bridge et al, above n 11, 21 [2.4.2].

122 ASIC, 'Equity Release Products', above n 9, 14.

123 ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 19–23.

124 ASIC, 'Equity Release Products', above n 9, 14; Bridge et al, above n 11, 47 [3.6].

necessities would require a credit-facility permitting multiple drawdowns. A serious issue for borrowers was (and remains) whether they use the equity released wisely, because in most cases they will not be in a position to repay the lender; and the equity will no longer be available to fund aged-care and accommodation in the future.¹²⁵

C Early Approaches to Reverse Mortgages: Intervention and Regulation

The outline of some of the major pre-contractual issues, legal content and financial features of the reverse mortgage indicates that this was (and is) an unusual and complex financial vehicle which needed to be carefully constructed and appropriately managed. In view of the growing list of problems associated with reverse mortgages, there were some important initiatives and recommendations about how to regulate reverse mortgages.

1 SEQUAL

The first major response to potential problems did not come from government, but from the lenders who provided reverse mortgages. They set up the Senior Australians Equity Release Association of Lenders (SEQUAL) which established the self-regulation of reverse mortgage products as an acceptable method of legitimating reverse mortgages in the market.¹²⁶ SEQUAL was 'committed to the development of an efficient and ethical Seniors Equity Release market in Australia'.¹²⁷ In order to do this, SEQUAL introduced a *Code of Conduct* which required members of SEQUAL to meet certain minimum criteria including: inserting a SEQUAL standard NNEG into their mortgages;¹²⁸ clearly identifying all costs which would be incurred by the borrower;¹²⁹ providing tools about 'the potential effect of future house values, interest rates and the impact of any capitalisation of interest where applicable';¹³⁰ and ensuring borrowers obtained independent legal advice before executing the documentation.¹³¹ SEQUAL also began a program for professional advisors such as lawyers and accountants who would be accredited as appropriate advisors in regard to reverse mortgages.¹³²

125 A risk which has not been sufficiently raised with borrowers: see ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 19.

126 As to the value of self-regulation as a tool, see Pearson, *Financial Services Law and Compliance*, above n 15, 21–2. In 2000, the Commonwealth government set up the Taskforce on Industry Self-Regulation which determined inter alia that self-regulation worked better when there was an active industry organisation leading the regulatory framework: Taskforce on Industry Self-Regulation, 'Industry Self-Regulation in Consumer Markets' (Final Report, August 2000) 48–50. It appears likely that SEQUAL was set up with this aim in mind.

127 SEQUAL, Submission to Treasury, *National Credit Reform Phase 2 — Green Paper*, August 2010, 5.

128 Ibid 6 (*Code of Conduct* cl 3).

129 Ibid (*Code of Conduct* cl 7).

130 Ibid (*Code of Conduct* cl 9).

131 Ibid (*Code of Conduct* cl 6).

132 Ibid 7–8.

There can be no doubt that the creation of SEQUAL had a positive impact upon the reverse mortgage market and the reputation of reverse mortgages amongst the public. In particular, SEQUAL stressed the importance of disclosure, advisor accreditation and the incorporation of a NNEG into reverse mortgages as a defining feature — all matters which would be later dealt with by the *NCCPA*, *NCC* and *CCLAA*. However, SEQUAL'S self-regulation strategy was limited because it targeted only some aspects of reverse mortgages; and there was no requirement that lenders be members of SEQUAL,¹³³ offer mortgages containing any form of NNEG or insist on borrowers obtaining independent advice.

2 ASIC

While at the time ASIC did not have the power to control reverse mortgage lending, it did perform three roles. As noted above, it took action to redress misleading advertising.¹³⁴ ASIC also investigated reverse mortgages empirically and legally, making recommendations for reform.¹³⁵

In regard to the empirical study referred to above,¹³⁶ ASIC recommended reducing the risks associated with reverse mortgage by lenders in a number of ways including: a NNEG in reverse mortgages;¹³⁷ adopting procedures in the event of default which were appropriate for seniors;¹³⁸ facilitating a disciplined use of the equity release funds;¹³⁹ providing borrowers clear information about the borrower's obligations;¹⁴⁰ tailoring personalised projections (covering long-term scenarios) about the effect of reverse mortgage drawdowns;¹⁴¹ and recommending that borrowers seek independent financial advice.¹⁴² ASIC also recommended that lenders and intermediaries develop dispute resolution procedures appropriate to the needs of older borrowers;¹⁴³ and that training ought to be developed to assist financial advisors fully understand the impact of reverse mortgages.¹⁴⁴ In short, ASIC recommended that: the structure and operation of reverse mortgages be tailored to the needs of seniors; more, clearer and relevant information be disclosed to borrowers; and that borrowers ought to have improved access to advice.¹⁴⁵ Although ASIC referred positively to SEQUAL's role,¹⁴⁶ it was evident

133 There are a number of reverse mortgage lenders who are not members of SEQUAL, see Bridge et al, above n 11, 16 [2.4] (Table 1).

134 See Part III(B)(2)(a).

135 ASIC, 'Equity Release Products', above n 9; ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60.

136 See Part III(B)(1). See also ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60.

137 ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 32 (Recommendation 1).

138 Ibid.

139 Ibid 32 (Recommendation 2).

140 Ibid 33 (Recommendations 4–5).

141 Ibid (Recommendation 5).

142 Ibid 34 (Recommendation 8).

143 Ibid 33–4 (Recommendation 6).

144 Ibid 34 (Recommendation 7).

145 Ibid 31–4 (Recommendations 1–10).

146 See ibid 32.

that more was required to deliver a moderated product in regards to which there was an appropriate level of risk for vulnerable seniors.¹⁴⁷

In the review of the legal regulation of reverse mortgages, ASIC highlighted that the CCC was inadequate: it did not mandate disclosure of risk; it did not provide a mechanism to ascertain the full cost of a mortgage (in view of equity release); and it did not apply to funds used for investment purposes.¹⁴⁸ ASIC was concerned that mortgage brokers were insufficiently regulated as there were no training requirements or regulation of the quality of the advice provided by mortgage brokers.¹⁴⁹

Finally, ASIC was so concerned about the vulnerabilities of seniors that it took informal action. It set up a website which provided general advice on reverse mortgages and an equity release calculator so that borrowers could work out the extent of their loss of equity in the family home.¹⁵⁰

3 State Government Entities

There were also increasing concerns about reverse mortgages at state level. Consumer Affairs Victoria (CAV) comprehensively reviewed the terms which regularly occurred in reverse mortgages.¹⁵¹ For example, CAV expressed unease about the conditions modifying NNEG clauses such as when the consumer elected to repay the loan early without selling the property.¹⁵² CAV drew attention to onerous default clauses under which a failure to pay the council or water rates (other than due to physical or mental disability) meant that the lender had the right to evict the borrower and to insist on the full repayment of the loan.¹⁵³ CAV objected to the inadequate and imprecise specification and disclosure of fees, charges and commissions, and to lenders having the unilateral right to introduce new fees and charges and to change existing fees and charges.¹⁵⁴ Some lenders had a broad contractual entitlement to repair and re-value the property which the CAV considered was unwarranted.¹⁵⁵ Overall, the CAV considered that the terms of reverse mortgages were weighted too far in favour of lenders, identifying egregious potential breaches of the CCC.¹⁵⁶

147 See *ibid* 34 (Recommendation 9).

148 ASIC, 'Equity Release Products', above n 9, 46.

149 *Ibid*.

150 See ASIC, *Reverse Mortgage Calculator* (24 January 2014) MoneySmart <<https://www.moneysmart.gov.au/tools-and-resources/calculators-and-tools/reverse-mortgage-calculator>>; ASIC, *Thinking of Using the Equity in Your Home? An Independent Guide to Reverse Mortgages and Other Equity Release Products* (July 2009). See generally ASIC's MoneySmart website: <<https://www.moneysmart.gov.au/>>.

151 See Consumer Affairs Victoria, above n 96, ch 7.

152 *Ibid* 49.

153 *Ibid* 47.

154 *Ibid* 48–9.

155 *Ibid* 50.

156 *Ibid* 47–8.

4 *Mortgage Brokers and the Ministerial Council on Consumer Affairs (MCCA)*

At the time when reverse mortgages were introduced in Australia, the activities of mortgage brokers were essentially unregulated, although the extent to which borrowers were using mortgage brokers was increasing (and has continued to increase, without borrowers necessarily recognising the risks involved).¹⁵⁷ In view of evidence of 'inappropriate and unscrupulous practices in the industry'¹⁵⁸ the MCCA decided that a working group ought to develop proposals to address problems associated with mortgage brokers.¹⁵⁹ While the proposals predominantly dealt with the licensing, obligations and liabilities of mortgage brokers generally,¹⁶⁰ specific recommendations dealt with reverse mortgages. First, there was a proposed definition of a 'reverse mortgage contract'.¹⁶¹ This was important because of the characteristics which were considered to be essential for a reverse mortgage, namely that the debt was secured by a mortgage which would not have to be repaid unless and until the land was sold, the borrowers or the last of them died or the borrowers or the last survivor of them vacated the land.¹⁶² Second, the proposed definition attempted to embed in statutory form a qualified NNEG as an integral characteristic of reverse mortgages.¹⁶³ Third, the recommendations proposed that the mortgage broker would be required to provide a range of estimates to the borrower about how the mortgage would work over different time.¹⁶⁴

D *Comment*

Even though reverse mortgages have been available on the Australian market only for a short time, the problems associated with them became quickly evident. The different entities discussed above responded to these problems in various ways, depending upon their jurisdiction and responsibilities. However, several broad (and sometimes overlapping) concerns are apparent. First, all entities identified that without some form of regulation, reverse mortgages would continue to operate unfairly against borrowers. SEQUAL considered that it was possible for lenders to self-regulate the reverse mortgage market. However, the findings of ASIC, CAV and MCCA indicated that lenders and mortgage brokers acted in their self-interest to the extent that they could not be relied upon to do otherwise.

157 Pearson points out that there can be issues of conflicts of interest (on the part of the mortgage broker) and the cost of the advice: Gail Pearson, 'Financial Literacy, Consumer Banking and Financial Advice' in Justin Malbon and Luke Nottage (eds), *Consumer Law & Policy in Australia & New Zealand* (Federation Press, 2013) 262, 282–3.

158 Ministerial Council on Consumer Affairs, *National Finance Broking Scheme Consultation Package* (November 2007) 1.

159 Ibid.

160 Ibid 3–6.

161 Exposure Draft: Finance Broking Bill 2007 (NSW) s 3.

162 Ibid s 3(b).

163 Ibid s 3(c).

164 See, eg, ibid ss 35, 37.

Second, SEQUAL, ASIC and MCCA emphasised the need for lenders and mortgage brokers to provide clear and relevant information to potential borrowers about the operation of reverse mortgages. Third, all entities (to varying degrees) recognised that an appropriate level of risk could not be achieved for borrowers by only regulating the provision of general information or the pre-contractual processes. For ASIC and MCCA in particular, lenders and mortgage brokers were responsible for creating bespoke transactions in terms of the borrower's needs and financial projections for equity release. Fourth, all entities recognised to varying degrees that it was necessary to regulate not only transactional processes, such as the disclosure of information, but also the substantive content of reverse mortgages, such as the inclusion of a NNEG and its range of operation. Finally, ASIC and MCCA recognised that mortgage brokers were key proponents of reverse mortgages who needed to be regulated carefully.

However, what was absent from the responses of these entities were two interrelated questions: are reverse mortgages suitable retirement planning products; and do the risks associated with reverse mortgages (including the significant depletion of equity) outweigh any benefits to borrowers? All entities assumed that reverse mortgages could be appropriate retirement planning products. This was not surprising in the context of the 'risk society' discussed above.¹⁶⁵ What was significant was the growing realisation that the substantive content of reverse mortgages required scrutiny. This approach would inform the federal government's attitude to reverse mortgages.

IV THE FEDERAL REGULATION OF REVERSE MORTGAGES

In view of the increasing complexity of the Australian finance market and the global financial crisis, the federal government decided that it was necessary to review the supervision of consumer credit including mortgages generally and the newly emerging reverse mortgage sector. The creation of statutory provisions in regard to reverse mortgages was a slow one subject to several phases and revisions.

A The First Phase

1 Financial Services and Credit Reform Green Paper

For some time, there had been concerns that a comprehensive and national consumer credit law including provision for responsible lending was needed.¹⁶⁶ The Treasury's *Green Paper 2008* set the stage for the first phase of statutory

¹⁶⁵ See Part II(B)(1).

¹⁶⁶ For a helpful historical introduction to the *NCCPA*, see Gail Pearson and Richard Batten, *Understanding Australian Consumer Credit Law: A Practical Guide to the National Consumer Credit Reforms* (CCH, 2010) 1–12 [1.1]–[1.4].

regulation.¹⁶⁷ For the purposes of this article, there were three important aspects of the report which pertained to reverse mortgages. One was that the federal government proposed that it would take responsibility for mortgages (including reverse mortgages) as credit contracts including associated advice (in view of, for example, the inappropriate borrowing by borrowers).¹⁶⁸ This was an important shift in the attitude to mortgage regulation as previously mortgages were not considered to be ‘financial products’¹⁶⁹ and although they are still not defined as ‘financial products’ the need for comprehensive regulation of mortgages as financial vehicles was recognised. However, Treasury did not envision that the federal government would take responsibility for all aspects of mortgages. It was implicit in their recommendations that essentially mortgages would also remain regulated by state legislatures in terms of such matters as title by registration under the Torrens system or the exercise of the power of sale.¹⁷⁰ Nevertheless, even under earlier legislation such as the *CCC* there was some further regulation of such matters as the default notice which could be issued for the purpose of exercising the power of sale.¹⁷¹ What the Treasury recommended was that a national approach to mortgages from the perspective of credit regulation would address gaps in regulation and create consistent credit regulation of mortgages across Australia.¹⁷² As will be shown below, some of the amendments in regard to reverse mortgages under the *CCLAA* have not only modified how mortgagees may exercise their powers when the borrower is in default, but also the terms of the reverse mortgages.¹⁷³ Therefore, the state and federal legislation operate simultaneously. Another issue was that Treasury considered that reverse mortgages raised important regulatory concerns, in view of ASIC’s studies which have been discussed above.¹⁷⁴

Finally, Treasury could not ignore that the conduct of some mortgage brokers had been unsatisfactory and that uneven and inadequate licensing regimes did not cover mortgage brokers.¹⁷⁵ Indeed, Pearson has observed that: ‘Concerns about the lack of national consistent regulation of mortgage broking in most Australian jurisdictions is one of the main reasons for the introduction of the [*NCCPA*] regime’.¹⁷⁶ However, significantly, the Treasury shied away from any regulation of fees and charges, contending that these matters were better left to a competitive market.¹⁷⁷ There was industry support for the closer and centralised regulation

167 Treasury, ‘Financial Services and Credit Reform: Improving, Simplifying and Standardising Financial Services and Credit Regulation’ (Green Paper, June 2008) (*‘Green Paper 2008’*).

168 *Ibid* 7, 15.

169 A mortgage that secured obligations under a credit contract, provided that it was not a facility through which a person made a financial investment, was a credit facility: *Corporations Regulations 2001* (Cth) reg 7.1.06(1)(f). A credit facility was not a financial product for the purposes of the *Corporations Act 2001* (Cth) s 765A(1)(h)(i).

170 In relation to title by registration and the exercise of the power of sale, see Butt, above n 10, 750–60 [20 12]–[20 22], 653–9 [18 129]–[18 139].

171 *CCC* s 80.

172 *Green Paper 2008*, above n 167, 9.

173 See Parts IV(B)(1)–(2).

174 *Green Paper 2008*, above n 167, 4–5. See also Parts III(B)(1), (C)(2).

175 *Green Paper 2008*, above n 167, 9–10.

176 Pearson and Batten, above n 166, 283 [9.7].

177 *Green Paper 2008*, above n 167, 15.

of reverse mortgages, including the regulation of appropriate disclosure and the national licensing of advisors.¹⁷⁸

2 National Consumer Credit Protection Act 2009 (Cth)

The federal legislature passed the *NCCPA* which commenced operation on 1 July 2010. The original *NCCPA* was the first phase of federal regulation of reverse mortgages because it set up a framework of control and licensing to which reverse mortgages, as credit contracts, were subject. However, it did not deal with all concerns about reverse mortgages. Although it is not possible to discuss all aspects of the *NCCPA* at length, it is important to be aware of the following, because they have an impact upon the operation and regulation of reverse mortgages.

(a) ASIC

ASIC became responsible for the overall administration of the *NCCPA* (and the *NCC*).¹⁷⁹ Therefore, as the single central administrative authority, ASIC has responsibility for the implementation and enforcement of all aspects of the legislation in regard to mortgages, including reverse mortgages.¹⁸⁰

The legislation covers 'credit' and 'credit activities'.¹⁸¹ The concept of 'credit' to which the *NCCPA* and the *NCC* applies is one where 'the debtor is a natural person or strata corporation'.¹⁸² The credit is inter alia 'provided or intended to be provided wholly or predominantly for personal, domestic or household purposes'.¹⁸³ 'Credit activities' include credit contracts and mortgages (which are a sub-species of credit contract in so far as it secures obligations under a credit contract).¹⁸⁴ The activity of lenders as credit providers includes the creation of mortgages, so that a person who is a mortgagee or performs the obligations or exercises the rights of a mortgagee is engaging in a credit activity.¹⁸⁵ Persons who

178 SEQUAL, Submission to Treasury, *Financial Services and Credit Reform Green Paper*, 1 July 2008, 2–3. It was incumbent on the government to provide to prospective borrowers 'unbiased information ... without scaring them away from using options such as reverse mortgages which can substantially improve many retirees' standards of living': at 3.

179 *NCCPA* s 239. See also Pearson and Batten, above n 166, 236 [8.2].

180 See Paul O'Shea, 'Regulatory Consistency and Powers' in Justin Malbon and Luke Nottage (eds), *Consumer Law & Policy in Australia & New Zealand* (Federation Press, 2013) 366, 379–80.

181 *NCC* s 3(1); *NCCPA* s 6. See also Pearson and Batten, above n 166, 23–37 [2.4].

182 *NCC* s 5(1)(a).

183 *NCC* s 5(1)(b)(i). The section also includes circumstances where the credit is provided or intended to be provided ... to purchase, renovate or improve residential property for investment purposes; or to refinance credit that has been provided wholly or predominantly to purchase, renovate or improve residential property for investment purposes.

Ibid s 5(1)(b)(ii)–(iii).

184 A credit contract is one 'under which credit is or may be provided': *NCCPA* s 5; *NCC* s 4. For mortgages specifically, see *NCC* s 7; Pearson and Batten, above n 166, 44 [2.10].

185 A credit provider 'means a person that provides credit, and includes a prospective credit provider': *NCCPA* s 5 (definition of 'credit provider'); *NCC* s 204 (definition of 'credit provider'). It also includes the assignee of the original credit provider: *NCCPA* s 10. See also Pearson and Batten, above n 166, 44 [2.10].

provide a credit service such as providing credit assistance to a borrower,¹⁸⁶ or acting as an intermediary between the credit provider and the borrower are also engaged in a credit activity.¹⁸⁷ Therefore, mortgage brokers who assist with the provision of credit are covered by the legislation.¹⁸⁸

The *NCCPA* introduced a national system of licensing, registration and regulation of persons who engage in credit activities including those who are credit providers, mortgagees and persons who provide a credit service (such as mortgage brokers).¹⁸⁹ There are a significant number of criteria which ASIC must take into account before issuing a licence¹⁹⁰ including whether the person is a fit and proper person to engage in credit activities.¹⁹¹ It is a criminal offence for a person to engage in a credit activity without an Australian Credit Licence.¹⁹²

(b) Responsible Lending, Disclosure and Misleading Conduct

The *NCCPA* and the *NCC* prescribe obligations to which licensees generally and in particular credit assistance providers (such as mortgage brokers) must adhere.

Lenders and mortgage brokers are required to act responsibly¹⁹³ by meeting certain basic standards of disclosure (including disclosure of fees and commissions)¹⁹⁴ and through assessment of the proposed mortgage including, for example, an evaluation of the suitability or lack of suitability of the credit contract in view of the borrower's circumstances.¹⁹⁵ They are prohibited from suggesting, assisting with or entering into unsuitable credit contracts.¹⁹⁶ For example, in relation to the obligations of lenders, a credit contract will be unsuitable if the borrower would be unable to comply with the financial obligations or could only do so with substantial hardship,¹⁹⁷ if the contract would not meet the borrower's requirements or objectives,¹⁹⁸ or 'if the regulations prescribe circumstances in which a credit contract is unsuitable'.¹⁹⁹ Lenders and mortgage brokers

186 *NCCPA* s 8. See also Pearson and Batten, above n 166, 46–51 [2.14].

187 *NCCPA* s 9. See also Pearson and Batten, above n 166, 51–2 [2.15].

188 See Justin Malbon, 'Responsible Lending, Unjust Terms and Hardship' in Justin Malbon and Luke Nottage (eds), *Consumer Law & Policy in Australia & New Zealand* (Federation Press, 2013) 241, 246.

189 *NCCPA* ch 2. For a helpful discussion of the process for obtaining an Australian Credit Licence, see Pearson and Batten, above n 166, ch 3.

190 *NCCPA* ch 2 pt 2-2.

191 *Ibid* s 37(1)(c). See Pearson and Batten, above n 166, 78–9 [3.10].

192 *NCCPA* s 29.

193 *Ibid* ch 3. For a general overview of the requirements, see ASIC, 'Credit Licensing: Responsible Lending Conduct' (Regulatory Guide No 209, March 2011); Malbon, 'Responsible Lending', above n 188, 246–8; Pearson and Batten, above n 166, ch 5.

194 *NCCPA* ss 113–14. As to the impact of the obligations on mortgage brokers, see Pearson, 'Financial Literacy', above n 157, 279–80, 284–5; Pearson and Batten, above n 166, 283–7 [9.7].

195 *NCCPA* ss 116, 131. For a helpful discussion of the requirements for responsible lending, see ASIC, 'Credit Licensing', above n 193; Pearson and Batten, above n 166, 165–8 [6.2].

196 *NCCPA* ss 123–4, 133.

197 *Ibid* s 131(2)(a). In *Silberman v Citigroup Pty Ltd* [2011] VSC 514 (18 October 2011) [11], the Court held that the term 'substantial hardship' ought to be given its ordinary dictionary meaning.

198 *NCCPA* s 131(2)(b). See also Pearson and Batten, above n 166, 179–80 [6.4].

199 *NCCPA* s 131(2)(c).

must not, in the course of engaging in a credit activity, give information or a document to another person if [they] know, or [are] reckless as to whether, the information or document is false in a material particular or materially misleading.²⁰⁰

The *NCC* sets out important matters in regard to the pre-contractual statement and the credit contract.²⁰¹ The credit contract must be in writing²⁰² and must include such matters as: the amount of credit; the interest rate or rates; the method of calculation of interest charges; the number of repayments; the default rate; commissions and enforcement expenses.²⁰³ Lenders are required to provide a statement of account on a regular basis.²⁰⁴ In the event that the borrower suffers hardship or the transaction is unjust, the *NCC* allows for the alteration of the credit contract.²⁰⁵

(c) *Comment*

The *NCCPA* addressed a variety of risks to which reverse mortgage borrowers were exposed, and placed further obligations on lenders and mortgage brokers. The licensing regime dealt with prudential risks in terms of the suitability and viability of lenders and mortgage brokers to act in regard to credit contracts. The prohibition of misleading information and documentation and the requirement to provide certain documents containing detailed information confronted the possibility of bad faith risks. The problem that borrowers will be faced with complex provisions and the risk that the mortgage is not suitable for their needs was to some extent covered by disclosure requirements and the responsible lending provisions, but the scheme needed specific provisions dealing with reverse mortgages.

B *The Second Phase*

1 *The National Credit Reform Green Paper*

In the second reform phase,²⁰⁶ the Treasury further considered reverse mortgages in the *Green Paper 2010*,²⁰⁷ noting the necessity for 'special enhancements to the regulation and tailored disclosure for reverse mortgage'.²⁰⁸ The Treasury identified three main areas of concern.

200 Ibid s 33(1). Indeed, a person who provides such information or document could face two years imprisonment: at s 33(2).

201 *NCC* s 16(1)(a), referring to s 17.

202 Ibid s 14. In relation to mortgages separate from the credit contract, see ss 42–3.

203 Ibid s 17. See also Pearson and Batten, above n 166, ch 7.

204 *NCC* ss 34–6.

205 See especially *NCC* ss 72, 76. For a helpful discussion of this issue, see Malbon, 'Responsible Lending', above n 188, 250–9; Pearson and Batten, above n 166, 209–10 [7.6].

206 For an overview of this phase, see Pearson and Batten, above n 166, 14–19 [1.6].

207 Treasury, 'National Credit Reform: Enhancing Confidence and Fairness in Australia's Credit Law' (Green Paper, July 2010) ('*Green Paper 2010*').

208 Ibid 33.

First, the Treasury observed that as there was no statutory requirement for lenders to protect borrowers against negative equity, the prospect of negative equity was a danger for borrowers who did not deal with SEQUAL accredited lenders.²⁰⁹ The Treasury suggested that there were two options: maintaining reliance on industry self-regulation, or the introduction of a statutory provision which specified that lenders would not seek to recover any amount in excess of the value of the property subject to some limited exceptions.²¹⁰

Second, the Treasury commented that, notwithstanding the first phase of the *NCCPA*, borrowers may not acquire sufficient information about the special legal and financial implications of reverse mortgages and may be unaware of financial alternatives.²¹¹ Moreover, the Treasury observed that borrowers may not obtain independent advice and, in any event, the independent advisors may not be adequately equipped to provide relevant advice.²¹² The Treasury suggested that there could be a statutory requirement that borrowers obtain independent legal and/or financial advice, or there could be a statutory requirement for improved generic pre-contractual advice by lenders and intermediaries such as mortgage brokers; or a combination of both methods.²¹³ There could also be a requirement for ongoing disclosure, such as the impact of compound interest accumulated on the loan.²¹⁴

Third, the Treasury listed several contentious ‘product features’.²¹⁵ It pointed out that there was no minimum age or any mandatory LVR, both of which would inevitably have an effect on the depletion of equity.²¹⁶ Other significant difficulties were broadly drafted default clauses; the absence of well-defined and appropriate default procedures; and the lack of protection for non-title holding residents.²¹⁷ In relation to default clauses, the Treasury proposed relying on industry based self-regulation or setting up a mandatory and uniform default procedure applicable to all reverse mortgage providers, or a combination of both methods.²¹⁸

2 The Legislative Response

There were a variety of responses to the *Green Paper 2010*, depending upon the experience, responsibilities and philosophical outlook of the respondents. Those respondents who provided reverse mortgage credit or advice tended to emphasise

209 Ibid 37.

210 Ibid 43–4.

211 Ibid 39.

212 Ibid.

213 Ibid 44–6.

214 Ibid 45–6.

215 Ibid 39–41.

216 Ibid 39–40.

217 Ibid 40–41.

218 Ibid 46.

that there ought to be self-regulation (based on SEQUAL's *Code of Conduct*)²¹⁹ or minimal statutory interference,²²⁰ while others who represented seniors and consumers advocated strong and coherent regulation in view of a long list of potential risks.²²¹

The first Exposure Draft of the reverse mortgage provisions was released in 2011 (*First 2011 Version*).²²² This was the first of three drafts, but remained a significant foundation for the amendment of the *NCCPA*. The general tenor of the *First 2011 Version* was to empower the borrower who would be: entitled to financial projections related to the value of the property;²²³ protected by a statutory NNEG;²²⁴ and protected from the powers of lenders to enforce the mortgage and sell the property.²²⁵

The *First 2011 Version* was superseded by a Second Exposure Draft released later in 2011 (*Second 2011 Version*)²²⁶ which maintained most of the *First 2011 Version* except that there were significant changes to the definition of a reverse mortgage,²²⁷ the use of the term 'reverse mortgage',²²⁸ the statutory NNEG²²⁹ and the lender's enforcement of the mortgage.²³⁰ This version formed the basis for the current legislation, subject to a few relatively minor amendments which were the outcome of later recommendations by the Parliamentary Joint Committee on Corporations and Financial Services.²³¹

The reverse mortgage provisions in *CCLAA* will be considered from four perspectives: the creation of a statutory NNEG; disclosure and information;

219 Finance Brokers Association of Australia Ltd, Submission to Treasury, *National Credit Reform Green Paper*, 9 August 2010, 3; Financial Ombudsman Service, Submission to Treasury, *National Credit Reform Green Paper*, 6 August 2010, 10–11; SEQUAL, Submission to Treasury, *National Credit Reform Green Paper*, 6 August 2010, 9–13; Westpac Group, Submission to Treasury, *National Credit Reform Green Paper*, 12 August 2010, 11.

220 For the Mortgage and Finance Association of Australia, the regulation of reverse mortgages ought not 'interfere with the commercial freedom of elderly Australians': Mortgage and Finance Association of Australia, Submission to Treasury, *National Credit Reform Green Paper*, 6 August 2010, 7.

221 Council on the Ageing, Submission to Treasury, *National Credit Reform Green Paper*, 6 August 2010, 3–6; Financial Planning Association of Australia Ltd, Submission to Treasury, *National Credit Reform Green Paper*, 6 August 2010, 3–9; National Legal Aid, Submission to Treasury, *National Credit Reform Green Paper*, 6 August 2010, 17–22; National Information Centre on Retirement Investments Inc, Submission to Treasury, *National Credit Reform Green Paper*, 6 August 2010, 7–13.

222 The reverse mortgage provisions in the *First 2011 Version* Exposure Draft: National Consumer Credit Protection Amendment (Enhancements) Bill 2011 (Cth) were set down to commence operation on 1 July 2012.

223 *First 2011 Version* sch 1 item 8, inserting *NCCPA* ss 133DA–DC.

224 *First 2011 Version* sch 1 item 17, inserting *NCC* s 86A.

225 *First 2011 Version* sch 1 item 18, amending *NCC* ss 88(1)–(2).

226 The reverse mortgage provisions in the *Second 2011 Version* Exposure Draft: Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011 (Cth) were set down to commence on 1 March 2013.

227 *Second 2011 Version* sch 2 item 2, inserting *NCC* s 13A.

228 *Ibid* sch 2 item 10, inserting *NCCPA* ss 133DA, 133DE.

229 *Ibid* sch 2 item 20, inserting *NCC* ss 86A–86F.

230 *Ibid* sch 2 item 23, inserting *NCC* s 93A.

231 Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Inquiry into Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill* (December 2011).

other statutory regulation of features of reverse mortgages; and the subsequent regulations which have been introduced pursuant to the amended *NCCPA*.

(a) *The Creation of a Statutory NNEG*

In order to create a viable statutory NNEG protection, it was necessary to define what kind of mortgage would constitute a 'reverse mortgage' for the purposes of the *NCCPA* and *NCC*. The legislature would mandate that when such a mortgage had been created and the debt exceeded the market value of the property, the lender would only be entitled to the market value of the property.

The *First 2011 Version* provided a definition of 'reverse mortgage'. An arrangement would be a reverse mortgage if certain conditions were met or the arrangement was declared to be a reverse mortgage by ASIC.²³² In relation to the former, one condition was that full repayment of the debt was not due until one of a number of events occurred, including that the borrower died or the debtor permanently vacated the land.²³³ The other condition was that the lender have a policy of only entering into such arrangement with borrowers who were at least 55 years of age.²³⁴

In the *Second 2011 Version*, the statutory definition of a reverse mortgage was radically changed and the earlier version jettisoned. The *Second 2011 Version* became the cornerstone definition of 'reverse mortgage' to which the *NCCPA* and the *NCC* would apply. The first (and arguably major) condition is that the borrower's liability under the mortgage may exceed (to a limited or unlimited extent) the maximum amount of credit that may be provided under the mortgage without the borrower being obliged to reduce the liability to less than the maximum amount of credit.²³⁵ Interest and other fees and charges are not included in the definition of an amount of credit under the *NCCPA*.²³⁶ Therefore, if the borrower is loaned \$50 000 and during the course of the loan the debt exceeds the original amount of credit (due to the accumulation of interest and other charges) and the borrower is not obliged to reduce the amount owing below the amount of credit during the course of the loan, the mortgage is a reverse mortgage.²³⁷ From the perspective of the borrower, the advantage of this provision (in contrast to the earlier version) is that the most important feature of a reverse mortgage is that there is no obligation to make a repayment during the term of the loan. The

232 *First 2011 Version* sch 1 item 2, inserting *NCC* s 13A.

233 *Ibid*, inserting *NCC* s 13A(2)(a), (c). Other events contained in the Exposure Draft were that the dwelling or land was sold, the lender or a person associated with the lender exercised a right of taking possession, a period specified in the contract ended, or the borrower had reached a certain age: see *First 2011 Version* sch 1 item 2, inserting *NCC* s 13A(2).

234 *First 2011 Version* sch 1 item 2, inserting *NCC* ss 13A(2)–(3).

235 Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2012 (Cth) sch 2 item 2, inserting *NCC* s 13A(2).

236 Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011 (Cth) sch 2 item 2, inserting *NCC* s 13A(2). See also the accompanying note to this sub-section which refers to the fact that under *NCC* s 3(2), an 'amount of credit' does not include any interest charge under the contract.

237 Explanatory Memorandum, Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011 (Cth) 36 [3.14].

definition is not circumscribed by either a list of events one of which must occur to bring the mortgage to an end, or the minimum age of the borrower. The statute itself will supply the NNEG protection.

Indeed in this context it ought to be noted that it is not only the traditional family home as a cottage or dwelling which is envisaged in the amendments. The definition of a 'reverse mortgaged property' means a dwelling or land that has been mortgaged to secure the borrower's obligations under the credit contract.²³⁸ Therefore, for example, a senior could own land, live in a caravan on the land and enter into a reverse mortgage in regard to that land.

Once the mortgage falls within the definition of 'reverse mortgage' and the property falls within the definition of 'reverse mortgaged property', the borrower would be entitled to terminate the mortgage and discharge it for less than the accrued debt.²³⁹ The *Second 2011 Version*, which was basically replicated in *CCLAA*, created a full subdivision instituting a statutory NNEG.²⁴⁰ The subdivision applies when the debtor's accrued liability exceeds the market value of the property (calculated in accordance with the relevant regulations).²⁴¹ If the lender receives the market value of the property then the borrower's obligations are discharged.²⁴² If the lender receives an amount in excess of the market value, then the lender is required to pay the excess to the borrower and the lender is not entitled to demand further payments.²⁴³ It also appears that if a reverse mortgage made prior to the implementation of the NNEG provisions did not contain a NNEG itself, the statutory definition will supplement the mortgage, so that the borrower will be entitled to rely on the statutory NNEG.

However, the subdivision provides some balance in favour of the lender (taking into account industry standards) as the statutory negative equity protection would be conditional upon certain events not occurring. The provisions do not apply where the borrower engages in fraud or made a misrepresentation relating to the reverse mortgage before, at or after the time the credit contract was made or where other circumstances prescribed by the regulations exist.²⁴⁴ In the event that the borrower is unable to rely on the statutory NNEG because of the borrower's conduct, the lender is required to indicate in the default notice that an event precluding reliance on the statutory NNEG has occurred.²⁴⁵

(b) *Disclosure and Information*

There are three important features which regulate the information to which the borrower is entitled and control the use of the term 'reverse mortgage' to preclude,

238 *CCLAA* sch 2 item 8, inserting *NCC* s 204(1).

239 In relation to the earlier version see: *First 2011 Version* sch 1, items 17, 20, inserting *NCC* ss 86A, 93A.

240 *Second 2011 Version* sch 2 item 20, inserting *NCC* sub-div B (ss 86A–86F).

241 *CCLAA* sch 2 item 20, inserting *NCC* s 86A.

242 *CCLAA* sch 2 item 20, inserting *NCC* s 86B.

243 *CCLAA* sch 2 item 20, inserting *NCC* ss 86C–D.

244 *CCLAA* sch 2 item 20, inserting *NCC* ss 86E(b)–(c).

245 *CCLAA* sch 2 item 23, inserting *NCC* s 93A(2)(a)(iii).

as much as possible, any misunderstanding by the borrower or misrepresentations by the lender.

(i) Licensees Giving Financial Projections

Licensees such as lenders and mortgage brokers bear further obligations to inform the borrower about the depletion of borrower's equity in the property, and the nature and effect of reverse mortgages generally. They are required to supply projections about how the mortgage would operate in relation to the value of the dwelling or land to be subject to the reverse mortgages before providing credit assistance or entering into a credit contract to which the mortgage relates.²⁴⁶ The projection would have to be made in person with the proposed borrower (or as prescribed by the regulations) and using a website approved by ASIC.²⁴⁷ Licensees must give the borrower a printed copy of the projections and a reverse mortgage information statement in the form prescribed by regulations which would set out generic features of reverse mortgages, and they must also tell the borrower about any matters prescribed by the regulations.²⁴⁸ Failure to comply with these requirements will be an offence attracting a criminal penalty.²⁴⁹ However, a licensee would not have to provide projections or provide a printed copy of them if someone else has already done so.²⁵⁰

(ii) Independent Legal Advice

Notwithstanding the fact that independent legal and financial advice has been considered a vital protection for seniors,²⁵¹ the legislation does not mandate independent legal or financial advice as a pre-cursor to the creation of a reverse mortgage. It leaves open the possibility that regulations may regulate or prohibit a lender entering into a reverse mortgage if the debtor has not obtained independent legal advice, and the regulations can impose offences and civil penalties for contravention.²⁵² There is no provision for mandatory financial advice.

The open-ended approach to independent legal advice may be explained by the expectation that the information provided by licensees will be more than adequate (particularly in view of the responsible lending requirements)²⁵³ and the self-regulation of the reverse mortgage industry by SEQUAL.²⁵⁴ However, this may be unduly optimistic as licensees may understandably be unable to provide the kind of impartial evaluation that third parties may be able to give.

246 *CCLAA* sch 2 item 10, inserting *NCCPA* s 133DB.

247 *CCLAA* sch 2 item 10, inserting *NCCPA* s 133DB(1)(a).

248 *CCLAA* sch 2 item 10, inserting *NCCPA* ss 133DB(1)(b)–(d).

249 *CCLAA* sch 2 item 10, inserting *NCCPA* s 133DB(2).

250 *CCLAA* sch 2 item 10, inserting *NCCPA* s 133DB(3).

251 *Green Paper 2010*, above n 207, 44.

252 *CCLAA* sch 2 item 13, inserting *NCC* s 18C.

253 *NCCPA* ch 3. See especially the provisions relating to licensees providing credit assistance: at ss 116–19. See also the provisions relating to the obligations of credit providers: at ss 129–31, 133.

254 See generally SEQUAL, *National Credit Reform Phase 2*, above n 127.

(iii) The Use of the Term 'Reverse Mortgage'

Lenders and mortgage brokers are prohibited from using the phrase 'reverse mortgage' or another term (whether or not in English) of similar import.²⁵⁵ In both cases, civil penalty units are imposed.²⁵⁶ The inclusion of this provision was a response to the instances where borrowers were lulled into the false sense of security that they were entering a reverse mortgage.²⁵⁷ However, it is a defence that the use of such terms truly represent that the mortgage is a reverse mortgage which conforms to the definition discussed above.²⁵⁸

(c) Other Statutory Features

(i) Third Party Occupants

Non-title residents may have rights in relation to the reverse mortgaged property. When a person other than the borrower occupies the reverse mortgaged property, the mortgage must stipulate that the borrower may at any time nominate or revoke the nomination of a person who would be allowed to occupy the property.²⁵⁹ While the nomination is in force, the nominee is entitled to occupy the property other than in the event of the borrower's death or vacation of the property.²⁶⁰ In the event that the mortgage does not contain such a provision entitling the borrower to nominate a non-title resident, the borrower must be informed that the mortgage did not protect such a person, otherwise the lender or mortgage broker will be subject to a criminal penalty.²⁶¹

(ii) Default Terms Which Must Not be Included

As there had been concerns about the possibility that default proceedings would be commenced on the basis of the borrower's minor breaches of the mortgage, there are events upon which the lender cannot rely to commence default proceedings.²⁶² These events include: the failure of the borrower to inform the lender that another person occupies the property; the borrower leaving the property unoccupied; the borrower failing to pay a cost which the borrower was obligated to pay within three years after the payment became due; the borrower failing to comply with a provision of the credit contract if the contract does not make it clear how the borrower is to comply with the provision; or an event or omission of the borrower

255 CCLAA sch 2 item 10, inserting NCCPA s 133DE.

256 CCLAA sch 2 item 10, inserting NCCPA ss 133DE(1)–(2).

257 These are called 'asset loans' or 'low doc' loans. The loan is made by reference to the valuation of the borrower's asset (which forms the security) rather than the borrower's ability to repay the loan. Sometimes such loans have been held to be unjust by courts: *Perpetual Trustee Co v Khashaba* [2006] NSWCA 41 (20 March 2006) [84]–[85] (Spigelman CJ), [128] (Basten JA); Pearson, *Financial Services Law and Compliance*, above n 15, 443–4. See also *Permanent Trustee Co Ltd v Gillian O'Donnell Permanent Trustee Co Ltd* [2009] NSW 902 (4 September 2009) [5]–[6] (Price J).

258 CCLAA sch 2 item 10, inserting NCCPA s 133DE(3); CCLAA sch 2 item 2, inserting NCC s 13A.

259 CCLAA sch 2 item 12, inserting NCC s 17(15A).

260 CCLAA sch 2 item 12, inserting NCC s 17(15A)(b).

261 CCLAA sch 2 item 13, inserting NCC s 18B.

262 CCLAA sch 2 item 13, inserting NCC s 18A.

prescribed by the regulations.²⁶³ Moreover, the lender must not agree to change or unilaterally change the credit contract so that it provides a basis for commencing proceedings which is prohibited.²⁶⁴

(iii) Enforcement Proceedings

In view of the significant adverse impact upon a senior if enforcement proceedings were commenced, the legislation outlines actions which the lender must take before taking proceedings to enforce the mortgage.²⁶⁵ These requirements largely reflect SEQUAL's mandated practice for its members.²⁶⁶ The lender is unable to take action against the borrower or against the property unless: there is a default; the lender has given notice to the debtor to enable rectification of the default at least 30 days from the date of the notice; and has informed the borrower or the borrower's representative of the consequences of failure to remedy the default or has made reasonable efforts to do so.²⁶⁷

(d) Regulations

In addition to the *CCLAA*, regulations have been implemented pursuant to the new s 86A(2) of the *NCC*.²⁶⁸ The regulations prescribe how an adjusted market value of the property will be determined, in the event that the borrower's debt exceeds the property's sale price and the borrower relies on the statutory NNEG. The adjusted market value will either be determined by an accredited valuer within three months before the lender receives an amount to discharge the mortgage; or the property's sale price.²⁶⁹ However, if the value of the property was reduced by deliberate damage to the property; the sale was not conducted in good faith; or the sale was not conducted on fair and reasonable terms, then the market value of the property will be determined by the valuer at the time of the sale of the property.²⁷⁰ Therefore, while deliberate damage to the property does not constitute an event of default,²⁷¹ if the property is sold having been damaged by the borrower or the occupier, then the borrower will be exposed to a higher valuation than the sale price.

3 Comment and Evaluation

When evaluating the merits of the reverse mortgage reforms implemented by *CCLAA*, it is appropriate to consider the reforms in three ways, namely, how the

263 *CCLAA* sch 2 item 13, inserting *NCC* s 18A(3).

264 *CCLAA* sch 2 item 13, inserting *NCC* s 18A(2).

265 *CCLAA* sch 2 item 21, inserting *NCC* ss 88(1)–(2).

266 See the SEQUAL guideline on the 'Minimum Procedural Requirements on Default' in SEQUAL, *National Credit Reform Phase 2*, above n 127, 15–16.

267 *CCLAA* sch 2 item 21, inserting *NCC* s 88(1).

268 *National Consumer Credit Protection Regulations 2010* (Cth) reg 84A.

269 *Ibid* reg 84A(2).

270 *Ibid* reg 84A(3).

271 Note that such a provision was deleted from *Second 2011 Version* sch 2 item 20, inserting *NCC* s 86E.

reforms fit within the consumer policy framework; how the reforms fit within the neo-liberal regulation context; and whether the provisions adequately cover all potential problems associated with reverse mortgages.

(a) *The Reverse Mortgage Reforms and a Consumer Policy Framework*

As discussed above, there are certain critical features of consumer policy against which legislative reforms may be judged.²⁷² First, the reforms rely on the licensing provisions in the *NCCPA* and *NCC* so that market players providing or advising on reverse mortgage are fit to be market players, must be licensed to do so and must act responsibly when entering into credit contracts such as reverse mortgages, including making a preliminary assessment as to whether the loan is suitable for the borrower.²⁷³ Reliance on the general licensing provisions is appropriate, as the licensing requirements: ensure the ongoing oversight of ASIC;²⁷⁴ impose strict prohibitions;²⁷⁵ and compel lenders and advisors to retain financial records, trust accounts and be audited.²⁷⁶

Second, there is the issue of disclosure of information to consumers in order to address information asymmetry and to ensure as much as possible that consumers are well-informed of the advantageous and disadvantageous features of the consumer credit transaction. The reforms build on the general disclosure provisions in the *NCCPA* and *NCC* which require that lenders and mortgage brokers (who have assessed the borrower's situation and evaluated the suitability of the credit contract)²⁷⁷ provide the borrower with a preliminary assessment of the reverse mortgage.²⁷⁸ However, the reverse mortgage reforms also require that lenders and advisors provide tailored projections about the likely impact of the reverse mortgage on the borrower's equity in the home over time,²⁷⁹ an obligation which ASIC had strongly recommended.²⁸⁰ Therefore, lenders and mortgage brokers can no longer gloss over the impact that the reverse mortgage may have upon the borrower's equity in the property. This is to be welcomed because it reinforces in specific financial terms the potential impact of the proposed mortgage and dispels the illusion that the interest and administrative costs associated with the reverse mortgage are of minor significance. Moreover, lenders and advisors are required to have generic information available about reverse mortgages.²⁸¹ Both requirements fit well into the consumer policy goal of providing relevant information to consumers, redressing information asymmetry and making

272 See Parts II(B)(1), IV(A)(1).

273 See *NCCPA* ch 3, ss 29, 129.

274 See *ibid* ss 49–51.

275 *Ibid* ss 30–3. Two significant prohibitions are against giving misleading information: at s 33; and against suggesting or assisting consumers to enter or increase the credit limit under unsuitable credit contracts: at s 123.

276 *Ibid* pt 2-5 divs 2–4.

277 See *ibid* ss 115–17, 128–30.

278 *Ibid* ss 120, 132.

279 *Ibid* s 133DB.

280 ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 33 (Recommendation 5).

281 *NCCPA* ss 133DC–DD.

borrowers aware of their obligations. It also goes some way to addressing ASIC's desire that borrowers have clear and relevant information.²⁸²

Nevertheless, despite the potentially positive impact of disclosure, it cannot be assumed that all borrowers will take the opportunity to review the information. There could be a problem that a borrower is not fully capable of appreciating the complexity of reverse mortgages (even though there is no suggestion that he or she lacks a general capacity to care for himself or herself on a day-to-day basis).²⁸³ There could be simply an information 'overload' so that the borrower is unable to rationally absorb all that is proffered to him or her. Alternatively, despite the disclosure of the disadvantages associated with reverse mortgages, the borrower may not act to protect himself or herself and make an informed choice because the borrower may consider that in his financial situation, he or she has little option but to enter into the reverse mortgage.²⁸⁴

Third, linked to disclosure another important consumer policy goal is to protect consumers against misleading information. The reverse mortgage reforms confront the glaring problem of misleading information not only by imposing the requirement for written financial projections but by also prohibiting the use of the term 'reverse mortgage' unless the use of the term correctly identifies that the credit contract is or is not a reverse mortgage.²⁸⁵

Finally, the reverse mortgage reforms reflect the desire to protect vulnerable consumers such as seniors. The reforms do not nullify provisions in the *NCCPA* and the *NCC* which address unsuitable contracts and hardship and unjust terms.²⁸⁶ Instead, the reforms are testimony to the realisation that notwithstanding the utility of licensing, disclosure, provisions addressing misleading information and unjust terms (and any associated penalty provisions),²⁸⁷ direct legislative intervention is required in view of the unusual nature of reverse mortgages, the context in which they operate and the potential clientele. The legislation proactively intervenes to change, redirect and standardise terms in reverse mortgages in order to redress concerns that features and terms of reverse mortgages may penalise vulnerable seniors. The amendments remove some matters from what would otherwise be part of the 'negotiation' process between the parties. At the forefront of the legislative intervention is the creation of a statutory NNEG, the definition of an 'adjusted market value' of the property and the regulation of how and when enforcement proceedings may be commenced.

282 ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 31–4.

283 In relation to contractual capacity and seniors, see Fiona Burns, 'Mortgages, Seniors and the Common Law Contractual Doctrine of Mental Incapacity in Australia' (2011) 34 *International Journal of Law and Psychiatry* 79, 81–2.

284 Wilson, above n 32, 305.

285 *NCCPA* s 133DE. Such an example of misleading information was uncovered by ASIC in relation to the description of mortgages to seniors: see ASIC, 'ASIC Stops Misleading Reverse Mortgage Advertising', above n 66.

286 *NCCPA* ss 119, 131; *NCC* s 76.

287 For example, criminal penalties will apply when the lender does not give projections of equity depletion before entering the reverse mortgage: *NCCPA* s 133DB; fails to disclose that the credit contract for the reverse mortgage does not protect the tenancy of third parties occupying the property: *NCC* s 18B; or fails to follow the procedure set down for the enforcement of the reverse mortgage: at ss 88(1)–(2).

It could be argued that such intervention goes beyond the traditional approach to consumer policy and protection based on licensing, disclosure and providing redress for unjust terms. However, the comments of the Productivity Commission in 2008 made it clear that if necessary, legislative regulation could be by way of 'changing the terms and conditions of transactions'.²⁸⁸ Moreover, the Productivity Commission specifically identified that seniors entering reverse mortgages could be vulnerable and may unwittingly sacrifice home equity which ought to be used for aged-care.²⁸⁹ Therefore, although the reforms may move beyond the traditional approach they fit within a modern consumer policy framework.

(b) The Reverse Mortgage Reforms and Neo-Liberalism

When faced (from the perspective of lenders and mortgage brokers) with a 'soft' regulatory option and an onerous one, the federal government sometimes selected an approach which was demanding and likely to better protect the borrower. Several examples illustrate this. Instead of leaving the issue of the NNEG to SEQUAL's self-regulatory regime, the legislation includes a statutory NNEG and the NNEG is not limited by evidence of deliberate damage to the property.²⁹⁰ Lenders are required to provide to borrowers not only generic material about reverse mortgages, but tailored projections about equity release. Events of default have been circumscribed and the lender's obligations in terms of a uniform default procedure have been augmented to ensure that action to remove the borrower from the property only occurs after the borrower is clearly advised that he or she must redress the breach.

In view of the extent and nature of the legislative regulation, it could be argued that the broad thrust of the legislative intervention was not neo-liberal and the government was predominantly interested in limiting the powers of lenders and advisors. However, the reforms were not inconsistent with neo-liberalism. In framing the *CCLAA*, both the government and the finance industry had a common goal which went beyond debates about whether government regulation or industry self-regulation was more appropriate: the future good standing of the reverse mortgage industry, the creation of a reverse mortgage market with some standard features (such as the statutory NNEG) and the minimisation of adverse publicity.²⁹¹ It was a matter of ensuring that perceived weaknesses of reverse mortgages were adequately addressed so that potential borrowers would not be discouraged from taking risks and entering into reverse mortgages in the future. The government would foster a climate in which seniors would take out reverse mortgages and would be less reliant on the public purse, while the finance

288 Productivity Commission, above n 20, 2.

289 Ibid 295.

290 *Second 2011 Version* sch 2 item 20, inserting *NCC* s 86E. See also Parliamentary Joint Committee on Corporations and Financial Services, above n 231, 35 [3.25], 38 [3.36].

291 Indeed, Senator Cormann pointed out that the finance industry supported the legislative amendments in regard to reverse mortgages: Commonwealth, *Parliamentary Debates*, Senate, 20 August 2012, 5721 (Mathias Cormann).

industry would benefit from the creation of a stable, profitable and statutorily endorsed reverse mortgage market.

(c) *Further Potential Problems*

It ought not to be assumed that the legislation completely or even adequately regulates reverse mortgages. Instead, it is arguable that the provisions were a 'trade-off' between the interests of the government and the finance industry on the one hand and the interests of borrowers and consumer advocates on the other. It is true that the legislation has burdened the lender with additional disclosure responsibilities and the borrower is protected by a statutory NNEG and enhanced protections to his or her occupation of the property. Moreover, it is incumbent on all lenders and advisors to evaluate mortgages (including reverse mortgages) from the perspective of the responsible lending provisions.

Nevertheless, there are some matters which await further consideration and possible regulation. One such issue is independent advice. It is surprising that independent advice was not made immediately mandatory. In view of the previous recommendations of ASIC,²⁹² the vulnerability of seniors and the complexity of reverse mortgages, it would have been preferable to have lucid provisions imposing the requirement that the borrower obtain independent financial advice (and setting out the nature and extent of the mandatory advice required) rather than simply relying on the disclosure provisions or the discrete treatment of certain facets of reverse mortgages in the *NCCPA* and the *NCC*.

Moreover, there are a number of important issues which remain completely unregulated particularly in relation to the disciplined use of equity release funds²⁹³ and depletion of the equity in the property: the portion of the equity which can be borrowed or the LVR; the portion (if any) of the equity of the home which can be quarantined from the loan; the kind and amount of the interest rates which can be imposed; the use of the funds; and the minimum age of the borrower.²⁹⁴ These matters may be components of the finance projections which illustrate the proposed mortgage's impact upon the value of the property, the borrower's indebtedness and the borrower's equity in the property. However, the mere inclusion of some of these components in the financial projections may not constitute adequate disclosure, sufficiently highlight them to the borrower or protect the interests of the borrower. These significant financial components require careful thought and so it is strongly arguable that, at the very least, independent financial advice ought to be mandatory. For lenders, the pace of the borrower's equity depletion (and the lender's equity accretion) is central to the viability of a reverse mortgage because the home generally secures the entire debt. It is arguable that the question of the rate of the equity depletion has been left untouched by statutory regulation to ensure that lenders remain in the market.

292 ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 34 (Recommendation 8).

293 See *ibid* 32 (Recommendation 2).

294 The maximum loan to value ratios and the minimum age of the borrower were raised in *Green Paper 2010*, above n 207, 39–41.

This is notwithstanding the fact that there have been well-documented complaints about the nature and rate of equity depletion.²⁹⁵

Finally, it is questionable whether the penalties imposed for breach of the reverse mortgage provisions go far enough to deter lenders and advisors from failing to comply with their obligations. For example, while civil and criminal penalties may be imposed where lenders or advisors fail to provide equity projections, they may not be a sufficient deterrence because it will be necessary for the enforcement provisions under the *NCCPA* to be activated.²⁹⁶ Borrowers may also be able to avail themselves of the licensee's own internal resolution procedure or may be able to have the reverse mortgage re-opened by the court on the basis that it is an unjust transaction.²⁹⁷ However, enforcement proceedings, dispute resolution or review proceedings may be time consuming and expensive. Moreover, unless regulations provide otherwise, the failure to comply with any requirement of the *NCCPA* does not necessarily affect the validity or enforcement of any credit contract.²⁹⁸

Measured against consumer policy goals and neo-liberalism, the reverse mortgage reforms still remain wanting. In relation to the former, the reliance on licensing, disclosure and transactional intervention may not be sufficient to ensure that vulnerable seniors are dealt with fairly by lenders or advisors. In relation to the latter, the reforms may soften the risks that seniors may otherwise suffer and therefore create and enhance a standardised reverse mortgage market. However, there could still be the prospect of damaging adverse publicity (leading to the contraction of the market) arising from such matters as a senior's incomplete understanding of the transaction, the failure of lenders or advisors to comply with the legislation or from a rapid depletion of equity.

V CONCLUSION

The rise of reverse mortgages and the subsequent federal regulation of them has been the result of a number of shifts in thinking about the nature of individual responsibility for retirement planning and the role of government in guiding and encouraging individuals to accept the financial burdens of their retirement.

One general and ongoing shift has been away from the assumption that the public purse will be available to fund retirement. Instead, employees and seniors are increasingly becoming 'risk subjects' or 'financial citizens' who are expected to save for their retirement, participate as investors on the market and utilise all available assets to fund the costs of retirement.²⁹⁹ The family home is no longer

295 ASIC, 'Consumer Experiences with Reverse Mortgages', above n 60, 27–30.

296 See, eg, *NCCPA* s 133DB. Civil proceedings are brought by ASIC: at s 166. A contravention of a civil penalty provision is not an offence: at s 168. Criminal proceedings are brought by ASIC, a delegate of ASIC or a person authorised by the relevant Minister: at s 206(1).

297 Ibid s 47(1)(h); *NCC* s 76.

298 *NCCPA* s 333.

299 See Pearson, *Financial Services Law and Compliance*, above n 15, 450–1.

quarantined from retirement planning considerations. It is no longer sacrosanct. It is progressively viewed as an investment asset like any other in the neo-liberal 'risk society'.

The new reverse mortgage provisions amending the *NCCPA* and the *NCC* ought not be seen as contradicting or counteracting against neo-liberalism and the 'risk society'. Indeed, they can be seen as an expression of the values of the 'risk society' because they are consistent with government's role (from a neo-liberal perspective) to facilitate and create markets and to set reforms in motion which ought to prevent market failure. The provisions were framed in view of the limited parameters set by the *Green Paper 2010*. Neither the *Green Paper 2010* nor the parliamentary debates questioned whether reverse mortgages were appropriate vehicles for retirement planning or whether 55 years of age was too young to take out a reverse mortgage (particularly in view of the potential longevity of seniors and the possibility that the equity in the family home would be required to pay for aged-care later in the senior's life). It was assumed that: seniors ought to be able to act autonomously and avail themselves of the opportunity to release the equity in the family home; reverse mortgages were suitable vehicles for retirement planning; and reverse mortgages would create social and economic benefits for seniors and the government coffers. The reverse mortgage provisions are the result of a process of weighing up the risks which seniors may face when taking out a reverse mortgage; and determining which risks are acceptable and which risks need to be moderated or removed altogether in view of consumer credit policy.

The oversight of reverse mortgages indicates that there have been two further important general and ongoing shifts which pertain to the regulatory approach. One is ASIC's assumption of responsibility for consumer protection, including reverse mortgages. While the *NCCPA* and the *NCC* are still framed from the perspective of consumer protection, ASIC's assumption of responsibility indicates that the financial nature of consumer protection has assumed new significance. In relation to mortgages, including reverse mortgages, the creation of securities over properties and the family home are seen both as consumer and financial transactions. Creating debt is not only becoming a debtor, but acting as a 'risk subject' or a 'financial citizen'.³⁰⁰ The other is that there has been a realisation that regulation may have to perform far more than a licensing or disclosure function. Sometimes the legislature will have to regulate intrusively by 'changing the terms and conditions of transactions'³⁰¹ in order to achieve neo-liberal aspirations.

However, the reverse mortgage is still a work in progress and it is possible that further legislative controls or amendments may be deemed necessary in the future. First, the legislation has left it open for the government or ASIC to create further regulations in regard to some discrete matters such as independent advice. Second, additional problems may be discovered which require legislative

300 Pearson had already presaged this shift in her book, as she included consumer protection law as part of the broad concept of financial services law: *ibid* ch 10.

301 Productivity Commission, above n 20, 2.

intervention in order to ensure that reverse mortgages remain attractive to borrowers. Third, the family home has only been recently 'discovered' as an additional source of retirement income, so that government policy towards the family home and equity release is still developing and dependent upon how the ageing of the population affects economic growth and government finances. In the future, reverse mortgages may be actively encouraged by governments or even become mandatory for retirement planning. Fourth, in contrast to major concessions to the borrower such as the statutory NNEG, other financial aspects of the reverse mortgage are currently subject to market forces, most particularly the nature and rate of equity depletion and how the equity will be used. Although such matters are subject to the additional disclosure provisions, it remains to be seen whether disclosure will adequately deal with such complex matters or whether further statutory intervention will be required, for example, to deal with borrowers' misunderstanding of or concerns about the potential for the rapid depletion of equity.

Finally, in regard to reverse mortgages, there are three stakeholders: the government, the lenders and the borrowers. So far, legislative reforms have concentrated upon moderating the risks of reverse mortgages so as to create and enhance a viable reverse mortgage market and protect the borrower's liability (in the form of the NNEG) or the borrower's occupancy of the family home (by, for example, limiting events of default). The legislation has not prescribed to what extent and for what purposes the equity in the home may be released. It has been assumed that a borrower as a rational and self-interested market player is entitled to use the equity released how he or she wishes because the underlying asset belongs to him or her. For example, at present borrowers at the relatively young age of 55 years may take out a reverse mortgage. So too, borrowers are presently able to utilise the released equity in the home in a wide variety of ways including, for example, paying for holidays and making financial gifts to relatives. Yet it is possible that such borrowers could live for several more decades and require aged-care which could have been financed by either a delayed release of equity or a release directed to the borrower's aged-care needs, rather than holidays or gifts to relatives. If reverse mortgages become increasingly viewed as a realistic or the essential way in which seniors can fund their basic retirement expenses and aged-care without being a burden on the government, then in the future governments may consider that it is necessary to take further steps to regulate the market such as determining: the age when a borrower can take out a reverse mortgage, the rate of equity depletion and how the equity may be spent.