

# Fringe dwellings

The vendor finance and rent-to-buy housing black market



October 2016



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# Disclaimer

This report was funded by the Victorian Legal Services Board's 2015 Grants Round. The program provides funding to projects that aim to improve the administration of laws, increase access to justice, improve legal services and inform and educate the wider community about legal services.

Legal information contained in this report does not constitute legal advice.

The case studies cited in this report do not represent a statistically significant number. They are, however, the lived experience of consumers who have approached Consumer Action or other legal services for assistance. The case studies represent a range of vulnerable and disadvantaged consumers across different geographic areas. Names of individuals and businesses and some minor details have been changed to protect privacy.

The views expressed in this report are those of Consumer Action.

To the best of our knowledge, the information in this report is current as at 12 September 2016.

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The contributions to this report have assisted in shaping its content and recommendations. However, the views expressed in this report are those of Consumer Action and do not necessarily reflect the views of particular persons or organisations who have contributed.

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# Executive summary

Vendor finance and rent-to-buy schemes promise the Australian dream of owning your own home—without a bank loan.

However, these deals typically do not result in successful home ownership and in some cases financially destroy hopeful buyers. Instead, they exploit people who have a desire for home ownership but are 'locked out' of the property market.

The legal status of these schemes is extremely complex and it is often unclear which laws apply. Vulnerable buyers, and some vendors, can suffer significant detriment yet have limited avenues for redress.

## **The housing black market**

Chapter 1 details the vendor finance industry and schemes. These schemes are varied and evolving, but generally fall into two categories.

In *rent-to-buy schemes*, a buyer agrees to an inflated property price then pays market rent (or above), an 'option fee' to purchase the property in several years' time, and in some cases a deposit and outgoings. The option fees are at least partly credited to the purchase price. A buyer must refinance with a mainstream lender to buy the home by the time the rent-to-buy deal expires.

People who have signed up to rent-to-buy deals because they could not obtain a mainstream mortgage will find it virtually impossible to refinance. This is particularly the case because they gamble on what a property will be worth in several years, and in many cases it is far less than they expected.

Consumer Action has seen no examples of successful rent-to-buy deals. These schemes do not enable people who could otherwise not buy a property to achieve home ownership. They are extremely financially risky and the legal protections for buyers are grossly inadequate.



In *vendor finance schemes*, a buyer agrees to an inflated property price, then pays a deposit, instalments, outgoings and in some cases their First Home Owners Grant. Vendor finance agreements are typically for between two and 30 years. However, a buyer will often need to refinance within several years, and will face the same obstacles as those seen in rent-to-buy deals.

Consumer Action has seen multiple examples of failed vendor finance deals. Many buyers have paid significant amounts towards what they hope will be their home, only to find that they cannot complete the purchase and will lose everything.

### **The risks**

These deals are often brokered by intermediaries who do not invest their own money and are driven by the opportunity to make significant profits.

Buyers are often highly vulnerable and have the most to lose. The most significant risks faced by buyers include:

- the buyer is not the legal owner of the property until the buyer pays the purchase price and the vendor transfers the property title—in many cases this never happens,
- many deals are destined to fail from the start because they are unaffordable for the buyer,
- the buyer often faces unknown costs, such as built-in interest rate increases and the cost of property repairs and maintenance, despite not being a home owner,
- a buyer may not be able to refinance due to the buyer's inadequate financial situation and the property price being above market value,
- a buyer who misses a payment often faces significant penalties under the contract and stands to lose the home and everything paid towards it, and

- a buyer is also at risk of losing everything if the vendor has a debt problem and loses possession of the property.

Some vendors enlist a broker to sell their properties as an investment strategy. However, many vendors are property owners in financial distress who need quick money. The risks faced by vendors include:

- losing control of the property to an intermediary broker,
- not getting the fast sale of the property that the broker promised,
- receiving less money than expected, and
- potentially being responsible for unlawful conduct by the intermediary broker.

Problems with the conduct of intermediary brokers include:

- misleading advertising and representations to buyers and vendors, and not explaining the arrangements and risks,
- seeking high profits which reduce the affordability for buyers and profitability for vendors—these deals are rarely both fair and profitable,
- failing to disclose the likelihood of whether the buyer will be able to refinance at the end of the agreement,
- encouraging buyers and vendors to get legal advice from a lawyer who the broker knows is unlikely to be negative about the arrangements, and
- breaching the law, either intentionally or due to lack of knowledge, and
- in some cases, ‘disappearing’ when things go wrong, or becoming insolvent when a buyer or vendor are seeking redress for a failed deal.

As the case studies in Chapter 2 of this report show, these schemes and the conduct of brokers have caused significant financial and personal harm to property owners and hopeful buyers.

# Recommendations

Regulation in this area requires an overarching approach to prevent harmful industry conduct and schemes. As the analysis in Chapter 3 shows, the law frequently does not provide meaningful redress for vulnerable buyers and vendors caught up in these black market housing schemes.

This report recommends legislative changes aimed at curbing the significant detriment caused by problematic vendor finance and rent-to-buy deals.

## Specific recommendations

### *Prohibit residential lease-options (p 90)*

Residential rent-to-buy or lease-option agreements are high risk and have no discernible benefit for consumers. They should be prohibited in the residential property market.

### *Strengthen regulation of vendor terms contracts (p 83-4)*

If vendor terms contracts continue in Victoria, particularly those brokered by intermediaries for profit, the law should be amended to ensure that:

- the National Credit Code (**NCC**) applies, so that the transactions operate in an established credit framework and buyers have access to affordable dispute resolution options, and
- certain money paid by the buyer is held securely on behalf of the buyer until settlement, so that a buyer can recover any amount they are entitled to if a deal is not completed.

### *Prohibit mortgage 'wrapping' (p 81)*

Vendor finance and rent-to-buy transactions, if not prohibited per se, should be prohibited for properties which are sold subject to a mortgage or other encumbrance.

### *Restrict access to the First Home Owners Grant (p 98)*

The First Home Owners Grant should only be paid on final settlement of a vendor terms contract, or where the buyer is in a genuine position to own the home. This would better reflect the purpose of the First Home Owners Grant, remove the immediate profit incentive for brokers and ensure that public money is not lost to failed deals.

### **Broader recommendations**

#### *Extend the National Credit Code to include private lending (p 105)*

The NCC should be extended to cover private lending, to protect buyers where a deal is not considered to be a transaction in the course of a business of providing credit. This would close a significant gap in the NCC's coverage, as well as having broader benefits (for example, in new disruptive business models like peer-to-peer lending).

#### *Prohibit unfair trading (p 116)*

The prohibition on unconscionable conduct under the Australian Consumer Law (**ACL**) and *Australian Securities and Investments Commission Act 2001* (Cth) (**ASIC Act**) requires a very high threshold of wrongdoing, and is not well adapted to deal with unfair business models such as problematic vendor finance and rent-to-buy schemes. A broader prohibition on unfair trading would enable regulators to more proactively impede unfair business models.

#### *Federally regulate property investment advice as financial advice (p 119)*

Property spruikers who promote vendor finance and rent-to-buy schemes to hopeful property investors should be subject to the same requirements as financial advisers under the *Corporations Act 2001* (Cth) (**Corporations Act**) and ASIC Act. Brokers who provide property investment advice by promoting these deals should also be subject to the same laws.



# 1. The housing black market

## Key points

- Vendor finance and rent-to-buy schemes are pitched as a way to buy your own home without a bank loan.
- Aspiring property investors learn to broker these deals at property investment seminars.
- The types of transactions and structures used vary and have changed over time.
- Intermediary brokers target disadvantaged hopeful homeowners who would otherwise never own a home and property owners in financial distress.
- These deals can be extremely risky, particularly for buyers.

## **What are vendor finance and rent-to-buy schemes?**

Vendor finance and rent-to-buy schemes promise the Australian dream of owning your own home—without a bank loan.

Typically under these schemes, people who cannot get a mainstream mortgage because of their low income, lack of savings or poor credit history are sold the hope of a secure place to call their own.

While details of these schemes vary, typically a buyer pays a deposit and regular payments towards the purchase of a home. Often the buyer must refinance in several years through a mainstream lender.

A buyer does not legally own the property until all payments are made. The legal rights of the buyer and vendor are often very unclear and/or limited (see Chapter 3). Consumer Action, other legal services and consumer regulators across Australia have seen numerous risky deals fail. These have resulted in financial ruin for buyers and significant losses for some vulnerable vendors (see Chapter 2).

## **History of vendor finance and rent-to-buy**

Vendor terms contracts date back to the early 1900s in Australia, but experienced a resurgence in the early 2000s.

After World War II, vendor terms contracts were a common method of selling cheap inner-city housing to recent migrants.<sup>1</sup> Because vendor terms contracts were long-term, buyers could only sell by entering into vendor terms contracts with subsequent buyers, creating a 'chain' of buyers who relied on those earlier in the chain, and ultimately the property owner, maintaining their contracts and payments.

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<sup>1</sup> Consumer Action Law Centre, *Vendor Terms: Rhetoric & reality*, February 2007, pp 41-45.

Lawyer Russell Cocks has stated that these arrangements 'undermine' the established system of property ownership.<sup>2</sup> New migrants with limited finances and/or English language skills were vulnerable to 'persuasive land salesmen' and entered into vendor finance deals without legal advice or an understanding of the risks involved.<sup>3</sup> In the United States in the mid-1900s, land instalment contracts were similarly targeted at African Americans, who were excluded from the mainstream housing market.<sup>4</sup>

In Victoria, the *Sale of Land Act 1962* (Vic) was introduced to address the concerns about 'chains' of vendor terms contracts, requiring notice to be given to buyers of any mortgage over the property. This reform may have caused 'much angst' among lawyers and the real estate industry, but it meant that the problems caused by chains of contracts were overcome.<sup>5</sup>

Vendor finance had a renaissance in the early 2000s, in the form of single transactions rather than chains of contracts. One media report at the time suggested hundreds of brokers were offering thousands of mortgaged homes to vendor finance buyers on 1% to 2% more than the standard variable interest rate.<sup>6</sup> Rent-to-buy schemes appear to have emerged after the introduction of responsible lending laws, which apply to certain 'terms sale of land contracts' but not rent-to-buy housing.<sup>7</sup>

The renewed popularity of vendor finance came after the introduction of the First Home Owners Grant in 1998. In Consumer Action's 2007 report, every case study involved the First Home Owners Grant. Many of the case studies in this report also share this common factor.

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<sup>2</sup> R Cocks, 'A study in consumer protection: A historical analysis of *The Sale of Land Act* (Vic) 1962' (2004) 11 APLJ 44, p 45, cited in Consumer Action Law Centre, *Vendor Terms: Rhetoric & reality*, February 2007, p 42.

<sup>3</sup> Justice Adam in R Cocks, note 2, p 45.

<sup>4</sup> National Consumer Law Center, *Toxic Transactions: How Land Installment Contracts Once Again Threaten Communities of Color*, July 2016, p 3.

<sup>5</sup> R Cocks, note 2, p 45.

<sup>6</sup> B Brown, 'Vendor Finance—Housing Under Wraps', *The Australian*, 23 April 2003.

<sup>7</sup> See the discussion of consumer credit laws at pp 100-108.

## How widespread are these schemes?

A key challenge in understanding vendor finance and rent-to-buy schemes is the lack of independent information and data available.

The Australian Census question on household tenure type previously included the option of 'being purchased under a rent/buy scheme'. In Consumer Action's view, this referred to the state government shared equity schemes which were being developed at the time. The question was revised in the 2016 Census to 'being purchased under a shared equity scheme'.<sup>8</sup> Because the question covers arrangements outside the scope of this report, the Census statistics have not been considered in this report. Consumer Action was also unable to find useable data from other government agencies, such as Consumer Affairs Victoria, LANDATA (land titles) and the State Revenue Office.

Between January 2011 and March 2015, Rick Otton's *We Buy Houses Pty Ltd*, the biggest vendor finance and rent-to-buy promoter in Australia, ran seminars attended by approximately 3,400 people, 'boot camps' attended by 2,000 and mentoring programs involving 700 people.<sup>9</sup> Students go through these training schemes with the aim of becoming intermediary brokers, although only a very small portion actually become active operators.

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<sup>8</sup> Australian Bureau of Statistics, *2011 Census and 2016 Census*, question 56. See Australia Bureau of Statistics, *2008.0—Census of Population and Housing: Nature and Content, Australia, 2016: Tenure Type*, <http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/by%20Subject/2008.0~2016~Main%20Features~Tenure%20type~133>. This issue is detailed in The Naysayer (blog), *Acceptance of rent-to-buy—the Census question*, 24 February 2014, updated August 2016, <https://thenaysayer.net/2014/02/24/acceptance-of-rent-to-buy-the-census-question/>.

<sup>9</sup> *Australian Competition and Consumer Commission and another v We Buy Houses Pty Ltd ACN 094 068 023 and another*, ACCC Statement of Claim, Federal Court of Australia, File Number NSD170/2015, 2 March 2015, para 7. There may be some duplication in these numbers (that is, some individuals may have participated in multiple offerings). We Buy Houses had a turnover of \$20 million between January 2011 and June 2014: ACCC Statement of Claim, para 6.



Buyers generally do not record a caveat to register their interest in the property title or, if they do, the reason for the caveat may be unclear. If a transaction completes, the underlying vendor finance or rent-to-buy agreement still may not be recorded anywhere.

While there is a lack of quantitative data, Consumer Action is aware of three other legal services in Victoria and nine elsewhere in Australia which have assisted clients in vendor terms or rent-to-buy arrangements in recent years. Chapter 2 of this report examines ten such cases, which show the close similarities between the schemes across Australia.

### **Where is it happening?**

The 'hotspot' areas and types of housing sold in these schemes have shifted over the past decade.

In 2007, Consumer Action observed low-value, run-down housing in regional and remote areas of Victoria sold for inflated prices. The First Home Owners Grant was often the sole source of the buyer's deposit.<sup>10</sup>

In 2016, the market appears to have shifted to growth areas of outer metropolitan Melbourne. Consumer Action has seen examples of 'clusters' of problematic deals involving multiple buyers in these areas. There have been similar experiences in rural and regional NSW.

The deals Consumer Action has seen in recent years generally share two key features:

- they are typically in areas where property value growth is not keeping pace with state or national averages,<sup>11</sup> and
- they involve new housing, for which home buyers may be eligible for the First Home Owners Grant.

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<sup>10</sup> Consumer Action Law Centre, note 1, pp 9-10.

<sup>11</sup> The Naysayer (blog), *One more 'rent-to-buy' risk—property values*, 8 April 2016, <https://thenaysayer.net/2016/04/08/one-more-rent-to-buy-risk-property-values/>.

While the brokers may be relatively small in number, the more active among them have well-established businesses, and some operate across state borders.

## The industry landscape

Australia's vendor terms and rent-to-buy industry appears to be significantly driven by lead promoter Rick Otton and his *We Buy Houses* business. At the time of writing this report, a claim by the Australian Competition and Consumer Commission (**ACCC**) for misleading and deceptive conduct by Otton and *We Buy Houses* had been heard by the Federal Court of Australia, with judgment reserved.<sup>12</sup> This ACCC action related to claims made by Otton and *We Buy Houses* in marketing materials, seminars and a book. Otton was promoting boot camps in the United Kingdom until mid-2016, but at the time of this report was instead promoting community meet ups.<sup>13</sup>

Key industry promoters were originally trained by Otton<sup>14</sup> and now promote their own products and services, including coaching, books, template legal documents, legal compliance guides, software applications and management and advertising services. One promoter previously

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<sup>12</sup> *Australian Competition and Consumer Commission and another v We Buy Houses Pty Ltd CAN 094 068 023 and another*, note 9. Hearing scheduled 29 August to 7 September 2016.

<sup>13</sup> We Buy Houses Community Meet Ups, <http://webuyhouses.co.uk/rick-otton-meetups/>.

<sup>14</sup> Rob Hardy, who was associated with the Vendor Finance Institute (<https://vendorfinanceinstitute.com.au/>), David and Karen Siacci of the Siacci System for Vendor Finance Real Estate (<http://siaccisystem.com.au/>) and Stephen Donaldson of Creative Property/Fast Property Doctor Pty Ltd (<http://creativeproperty.com.au/>) in the past gave positive testimonials for Otton as his former students: see *Australian Competition and Consumer Commission and another v We Buy Houses Pty Ltd CAN 094 068 023 and another*, note 9, Annexures (various Otton marketing materials). Consumer Action does not suggest any connection between the conduct of Otton's students and the ACCC action against Otton.

offered its Australian Credit Licence to vendor finance brokers (as credit representatives) for a fee, but stopped this after a 'risk/reward analysis'.<sup>15</sup>

The vendor finance industry is small and opaque, operating outside the mainstream real estate industry. Small companies and individual operators broker private transactions. Based on Consumer Action's casework and research, there appears to be a handful of brokers operating through specialist companies. In some cases, multiple companies are controlled by the same people. In Victoria, Consumer Action has seen recent vendor terms contracts and particularly risky 'intention to purchase' off-the-plan deals.<sup>16</sup> Activity in other states differs. For example, while problematic deals continue in NSW, disputes and complaints against brokers in WA have reduced, following high-profile and targeted enforcement action by Consumer Protection WA.<sup>17</sup>

Brokers and promoters continue to have a strong online presence, including their own websites<sup>18</sup> and Facebook groups.<sup>19</sup> Social media, particularly LinkedIn, is also used to network with related professionals, connect brokers with each other and advertise to potential vendors and buyers.

While in the past the industry operated outside of any licensing regime, recent regulatory action has led to an increased number of brokers holding estate agent licences and/or Australian Credit Licences. One

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<sup>15</sup> Vendor Finance Institute, *A New Path To Credit Representative Status*, 24 September 2014, <https://vendorfinanceinstitute.com.au/a-new-path-to-credit-representative-status/>.

<sup>16</sup> See for example case study 1, p 41.

<sup>17</sup> See the examples in chapter 3, pp 111-112.

<sup>18</sup> See for example the Vendor Finance Institute <https://vendorfinanceinstitute.com.au/> and Creative Property/Fast Property Doctor <http://creativeproperty.com.au/>.

<sup>19</sup> See for example the Vendor Finance Institute <https://www.facebook.com/vendorfinanceinstitute/> and the Vendor Finance Association Australia <https://www.facebook.com/VendorFinanceAssociation/>.

industry body, the Vendor Finance Institute, has associated itself with the Finance Brokers Association of Australia.<sup>20</sup>

## Related professionals

Several lawyers and mortgage brokers are closely connected with the vendor finance industry. They attend industry events and promote their services and expertise in the area to brokers and property investors.

Generally a broker suggests to the vendor a specialist lawyer, or several lawyers, with whom the broker has an ongoing professional relationship. These lawyers prepare documents and act on behalf of the vendors. This arrangement could potentially create a conflict between the lawyer's duty to act in the best interests of a vendor, and the incentive to maintain a positive ongoing relationship with the broker who is providing referrals.<sup>21</sup>

Consumer Action has significant concerns that some lawyers may not be acting in the best interests of buyers and vendors in vendor finance and rent-to-buy deals.

A Victorian solicitor was fined in 2014 for 'reckless dishonesty' in acting for a vendor with no authority to do so.<sup>22</sup> In a recent NSW Supreme Court case, a broker recommended a lawyer to the buyers. The broker and lawyer then pressured the buyers to see the lawyer quickly and pay on the day to receive a discounted fee. One of the buyers was concerned that the arrangement was a rent-to-buy scheme, however the lawyer told her it was like a bank mortgage.<sup>23</sup>

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<sup>20</sup> Finance Brokers Association of Australia, *New vendor finance committee formed by FBAA*, 29 May 2014, <https://www.fbaa.com.au/new-vendor-finance-committee-formed-by-fbaa/>.

<sup>21</sup> See further on lawyers' referral conflicts Consumer Action Law Centre, *Lawyers and Referrer Conflict—an underrated risk*, 30 May 2016, <http://consumeraction.org.au/lawyers-referrer-conflict-underrated-risk/>.

<sup>22</sup> Victorian Legal Services Board and Commissioner, *Lawyer fined \$25,000 for "reckless dishonesty" in property transaction*, 13 August 2014, <http://lsbc.vic.gov.au/?p=3998>.

<sup>23</sup> *Evolution Lifestyles Pty Ltd v Clarke (No 3)* [2016] NSWSC 1237, paras 26, 53-56.

In the case studies in this report, some buyers were given information by lawyers connected to the brokers. However, none were made aware of the risks of the deal.

### **Vendor terms and rent-to-buy players**

As noted above, Australia's **lead promoter**, Rick Otton, has taught vendor finance, rent-to-buy and related strategies to thousands of people through his seminars, boot camps, coaching and products.<sup>24</sup> Several other operators who went through Otton's training are now **promoters** themselves.

**Brokers** of these deals are typically trained by one or more promoters. They aspire to build their personal wealth as property investors.

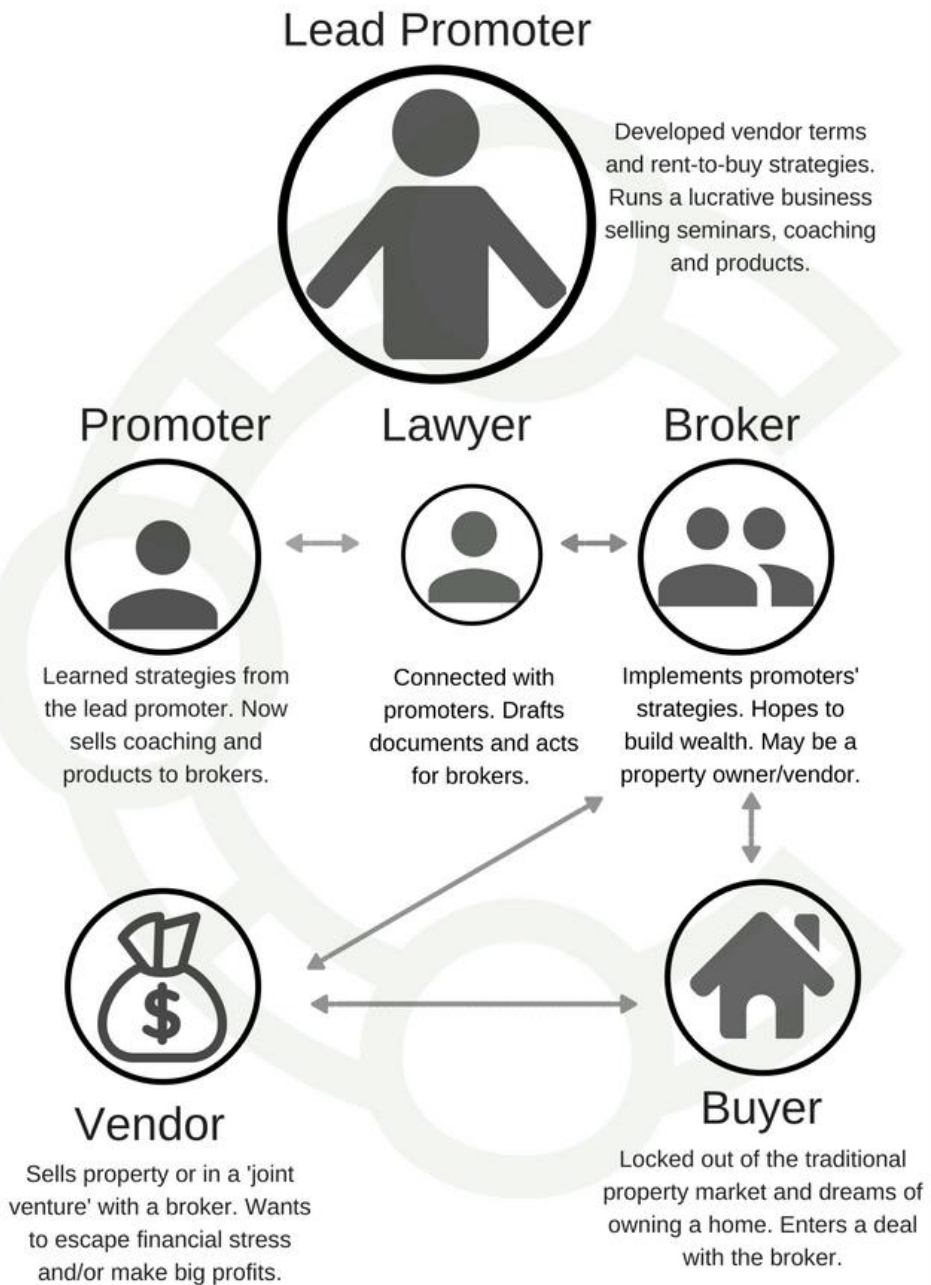
Brokers typically target potential **vendors** who are desperate to escape financial stress (for example, because they are facing foreclosure by their lender) and/or looking to make big financial returns on their property. Consumer Action has also seen deals where the vendor has been knowledgeable about the scheme, or has brokered a deal themselves, using the same tactics as brokers.

Brokers target **buyers** who are locked out of the home market due to their income, savings and/or credit history.

Specialist **lawyers** act on behalf of promoters, brokers, vendors and sometimes buyers. Other industry players such as mortgage brokers can become involved when a buyer is trying to refinance.

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<sup>24</sup> *Australian Competition and Consumer Commission and another v We Buy Houses Pty Ltd* CAN 094 068 023 and another, note 9, para 7.



*Graphic: Players in vendor finance and rent-to-buy schemes*

## Types of deals

There are two main types of residential property transactions examined in this report: rent-to-buy deals and vendor terms contracts. Despite differences in terminology, processes and documentation, the schemes seen by Consumer Action have largely been variations of one of these two types. However, more recently some deals in NSW have involved a 'licence' agreement, and Victoria has seen off-the-plan sales similar to vendor terms contracts.

The evolution in the structures used appears to follow changes in the industry's understanding of property and consumer laws and the regulatory environment.

### Rent-to-buy

Rent-to-buy schemes are also referred to as *lease-options* or *rent-to-own*. Generally in these deals:

- the buyer and vendor sign a residential tenancy agreement and an option agreement,
- the option agreement gives the buyer the option to purchase the property for a specific price after an agreed period, generally two to five years,
- the buyer pays a deposit, rent and option fees and may pay outgoings, and
- typically some (but not all) of the option fees will be credited to the buyer's deposit on the property.

The documents will specify what will happen if a buyer does not make all payments required, which can include the charging of default interest, fees and legal costs, and eviction. The broker's or vendor's lawyers also prepare a contract for sale with an inflated purchase price at the time the rent-to-buy deal is arranged.

The legal status of rent-to-buy transactions is unclear, and these deals lack key consumer protections, such as coverage by the National Credit Code (**NCC**).<sup>25</sup>

Rent-to-buy and vendor finance deals typically involve a property on which the vendor already has a mortgage. This poses a significant risk to buyers, particularly where a vendor is facing financial distress, because if a vendor cannot maintain their mortgage payments, a lender may take possession of the property.

There may also be more complex 'sandwich lease' arrangements, where a broker enters a rent-to-buy agreement with a vendor, then a rent-to-buy sublease with a buyer on terms that are profitable for the broker.

A number of submissions to Consumer Affairs of Victoria's 2016 review of Victoria's property laws agreed that rent-to-buy schemes need tighter regulation<sup>26</sup> and/or may not have a role in the residential property market.<sup>27</sup> The vendor finance industry itself has stated that rent-to-buy schemes are higher-risk than vendor finance arrangements and that the majority of rent-to-buy deals do not end in a successful sale.<sup>28</sup>

### Vendor terms contracts

Vendor finance is also referred to as *terms contracts*, *instalment contracts* and *instalment sales*.

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<sup>25</sup> See p 100.

<sup>26</sup> Law Institute of Victoria, *Consumer Property Acts Review Issues Paper No. 3: Sale of land and business*, 17 May 2016, p 15.

<sup>27</sup> See for example Victorian Civil and Administrative Tribunal, *Consumer Property Law Review—Sale of Land and Business Issues paper No 3—Tribunal Submission*, 30 May 2016, p 4; Real Estate Institute of Victoria, *Submission: Consumer Property Acts Review Issues Paper No 3: Sale of Land and Business*, May 2016, p 12; Consumer Action Law Centre, *Consumer property law review: Issue Paper 3: Sale of land and business*, 2 June 2016, p 14.

<sup>28</sup> Finance Brokers Association of Australia (representing Vendor Finance Institute), *Response to the Consumer Property Acts Review Issues Paper No 3*, 13 May 2016, p 8.



Vendor finance transactions typically involve:

- a contract for sale between the buyer and vendor, usually in a standard form with extra terms,
- a settlement period of anywhere between two and 30 years,
- an inflated purchase price,
- payment by the buyer of a deposit, in some cases the First Home Owners Grant, ongoing instalments and outgoings such as rates, insurance and maintenance, and
- interest on the instalments that is at least 1% to 2% above the interest rate paid on the vendor's mortgage.

As with rent-to-buy deals, the contract will specify what happens if a buyer does not make all payments required.

While a contract may belong-term, there are often practical reasons that buyers attempt to refinance with a mainstream lender within several years. As one vendor finance promoter has said:

*Our [instalment contracts] are written up over 30 years but most refinance somewhere in the 2 to 5 year range. We declare up front to our buyers that their interest rate will increase over the first few years, to encourage them to refinance. Yes, we do "vet" our buyers closely but, with the interest rate increases I mentioned, if they did stay for the long term, we'd be happy, as the monthly cash flow would be very attractive.<sup>29</sup>*

As with rent-to-buy deals, vendor terms deals typically involve a property that is already mortgaged. This is referred to as mortgage 'wrapping' (that is, the mortgage is 'wrapped' in a vendor finance arrangement). For the reasons noted above, 'wrapping' poses significant risks to buyers.

There are variations on vendor finance arrangements, such as the 'some now, some later' scheme, where a property is partly paid for through a bank loan upfront and the remainder paid via vendor finance instalments.

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<sup>29</sup> P Dobson (Vendor Finance Institute), 'David and Julie Siacci', *Somersoft Property Investors Forum*, 8 October 2010, 3:36pm, <http://somersoft.com/forums/showthread.php?t=60274&page=3>.

### Licence to occupy

Under licence to occupy schemes, the property is sold with an inflated purchase price, with either the full purchase price or a deposit payable in instalments over a number of years. During that time, the buyer also pays a 'licence' or 'occupation' fee to live in the property. The buyer will additionally pay a deposit and outgoing, and may be liable for land tax and stamp duty.<sup>30</sup> A buyer must pay fees and instalments until either the purchase price is paid in full, or the deposit is paid and the buyer has obtained finance for the remainder of the purchase price.

This transaction type has been promoted by one NSW lawyer as one which does not involve 'credit', and therefore avoids consumer credit laws, and does not involve a lease agreement, so falls outside residential tenancy laws.<sup>31</sup> However, in September 2016, the Supreme Court of NSW found that one of these arrangements did in fact fall under the NCC.<sup>32</sup>

### Off-the-plan

In recent years, Consumer Action has seen a number of off-the-plan sales which resemble vendor terms sales. Typically a buyer is required under 'letter of intent' to pay a non-refundable administrative fee, a deposit and instalments over a long period (for example, 25 years).

These arrangements are stated to be conditional on, among other things, approval of the buyer's solicitor, a credit check, and settlement by the vendor. However, buyers have paid significant amounts towards these deals without a contract in place and therefore without any clear legal rights or protections. These are among the most legally and financially risky transactions for buyers.

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<sup>30</sup> See the discussion of liability for taxes and duties at pp 95-100.

<sup>31</sup> T Cordato, *What is a Deposit Builder?*, 27 January 2014, <http://buywithoutabank.com.au/deposit-builder/>.

<sup>32</sup> *Evolution Lifestyles Pty Ltd v Clarke (No 3)* [2016] NSWSC 1237.

## Lifecycle of a deal

The typical vendor finance or rent-to-buy deal follows a similar pattern.

### *1. Promoter spruiks the strategies*

Promoters typically attract aspiring property investors with the promise of profits with no upfront investment. These investors typically get involved after attending a free introductory seminar.

### *2. Broker learns the strategies*

After the initial free seminar, hopeful investors pay thousands of dollars for boot camps, personal coaching and products.<sup>33</sup> This coaching appears to focus on how to find vendors and buyers, sales tactics, and the key features of transactions.<sup>34</sup>

### *3. Broker finds a vendor*

Vendors are often in a vulnerable position from the beginning of their dealings with brokers, because brokers target property owners in financial distress. However, in some cases property investors attend training and broker their own deals without an intermediary broker.

Some methods that brokers and sophisticated vendors have used to find vendors include:

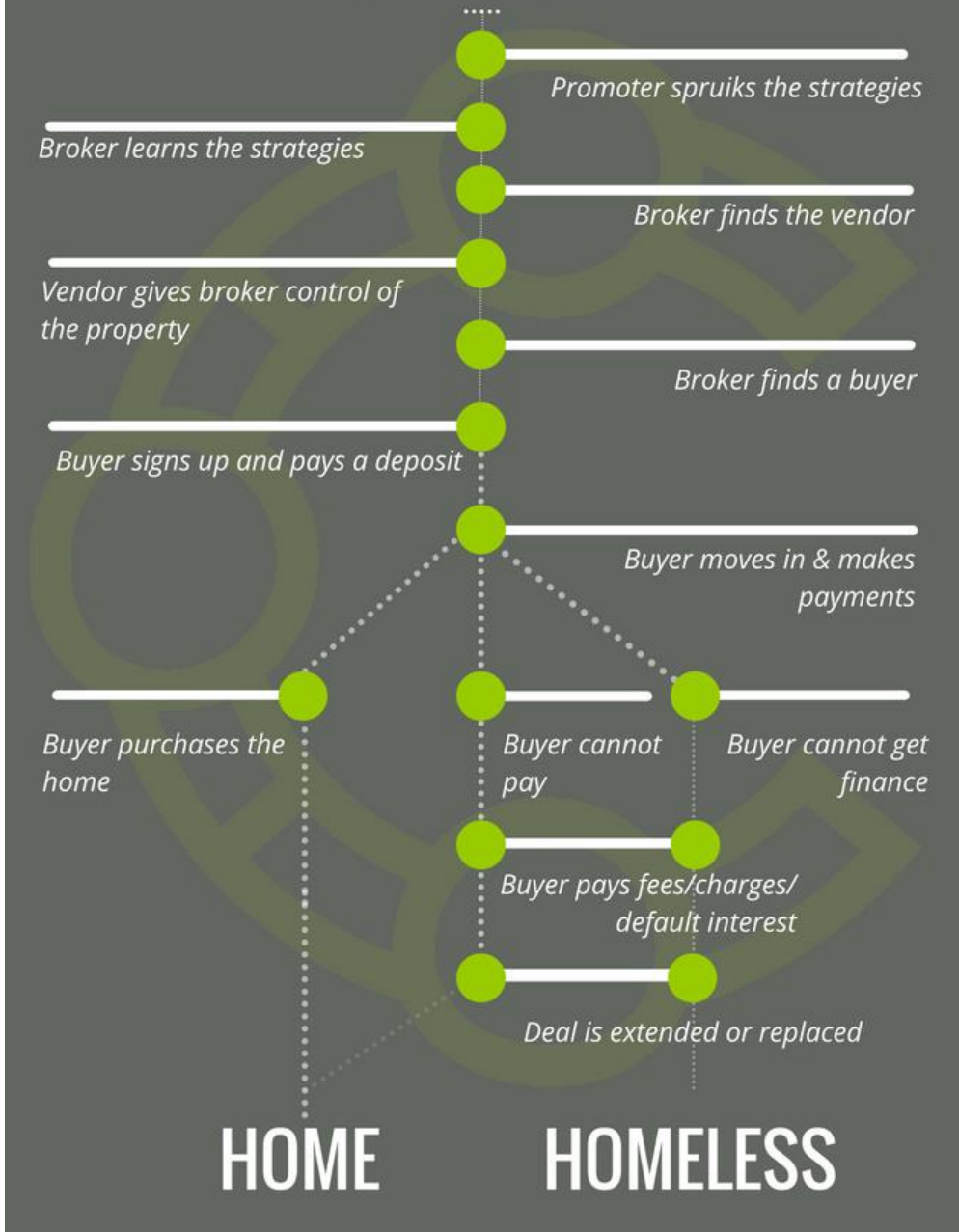
- searching court lists for mortgagee-initiated proceedings and contacting property owners who are facing foreclosure, offering to sell their houses fast or to generate quick income,
- placing hand-written street signs in targeted areas with slogans such as 'We buy houses fast',
- approaching property owners who are having trouble selling properties, and

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<sup>33</sup> For example, brokers Patricia and Bryan Susilo paid \$20,000 to attend a four-day boot camp and \$1,000 per month for ongoing mentoring, having first attended a free seminar: *Commissioner for Consumer Protection v Susilo* [2014] WASC 50 (27 February 2014), paras 79-81.

<sup>34</sup> Based on a review of the lead promoter's marketing materials and the casework of Consumer Action and other legal services.

# LIFE CYCLE OF A DEAL



Graphic: Typical stages in a vendor finance or rent-to-buy deal

- advertising in local newspapers, and on Gumtree, Facebook, specialist real estate websites and their own websites.

#### *4. Vendor gives broker control of the property*

The arrangement between a broker and vendor is often called a 'joint venture' agreement. Typically, the vendor gives the broker control of the property through a power of attorney, and the broker agrees to prepare documents, sell the property (often on any terms) and manage ongoing payments.

The broker may be entitled to all or part of the buyer's deposit and First Home Owners Grant (if available) and the broker and vendor may split the ongoing payments. The broker may charge fees for managing the property. There also may be an agreed minimum sale price, and if the property is sold for more than that, the broker is entitled to all of the proceeds above that amount.

The amount paid on to the vendor often depends on the sophistication of the vendor—a vendor who is a seasoned investor will receive more than a desperate vendor in financial trouble.

These agreements can give a broker complete control of a vendor's property and pose significant risks to the vendor's financial position. In some cases, vendors fully understand the arrangement. However, a significant number of vendors have not understood these agreements. Case study 9 is one such case.<sup>35</sup>

#### *5. Broker finds a buyer*

Brokers attract buyers by advertising in local newspapers, online and on street signs. They aim to engage buyers locked out of the traditional home loan market due to low income, lack of savings or credit history. A broker's pitch is along the lines of 'Buy without a bank', 'Why rent? Buy now' and 'Bank says no? We can help'.

Buyers have reported finding online advertisements while specifically searching for rent-to-buy properties but also when looking for regular

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<sup>35</sup> See p 69.

rental properties. Consumer Action is also aware of a number of cases within a close community where people referred their friends to a broker.

While vendor terms, rent-to-buy and similar deals are structured differently, the processes used to attract and sign up buyers are almost indistinguishable. In particular, many buyers believe they have found a chance to achieve home ownership, which they had thought was out of their reach. They hope to turn around their financial situation and refinance with a traditional lender within several years, often on the basis of what the broker told them during the sales process.

#### *6. Buyer signs up and pays a deposit*

A buyer typically signs the documents quickly and pays the broker a deposit and various fees. Consumer Action has not seen any buyers who received independent legal advice before signing up or fully understood the legal status of the deal. Several buyers spoke with a lawyer connected with the broker but were not made aware of their rights and liabilities.

#### *7. Buyer moves in and makes payments*

Vendor terms and rent-to-buy deals seek to set themselves apart from traditional property sales by being quick transactions. Consumer Action has seen instances of buyers moving into a home less than a week after first contacting a broker. Once in the property, a buyer begins to make regular payments and pay any outgoings.

#### *8. The deal ends*

A vendor finance or rent-to-buy deal will end one of three ways.

##### 1. The buyer purchases the home as planned

The vendor will transfer title to the buyer if the buyer pays all agreed amounts. Consumer Action has seen several examples of vendor finance arrangements which ended this way, albeit at a huge cost to the buyer. However, we have seen no examples of rent-to-buy deals that have ended with the hopeful buyer achieving ownership of the property.

Rent-to-buy deals usually range from two to five year-terms. In theory, a vendor finance buyer may pay the house off over a long period (for example, 25 years) and take ownership. However, often a buyer will try to refinance with a lender in several years, because the interest rate is high and increases annually.

In both cases, the buyer's financial situation must improve significantly and the property's value must increase substantially, which is made more difficult when the property is overpriced in the first place.

## 2. The deal is extended or replaced

If the buyer cannot obtain finance, the broker or vendor might extend the deal or make a new deal with the buyer. However, many contracts do not give the buyer a right to extend the contract.

An extended deal might adjust the regular payments up or down, depending on the agreement and circumstances, and give the buyer additional time to obtain finance. Alternatively, a new deal may replace the previous deal and potentially eliminate any equity the buyer built up in the property. Some buyers continue to live in properties (for example as tenants) with no prospect of ever buying the home.

## 3. The buyer moves out

Buyers have moved out of or been evicted from properties because they cannot afford the high ongoing payments and costs. Typically a buyer who moves out loses everything paid towards the property, including the deposit, First Home Owners Grant and any equity built up through regular payments.

## **The risks of vendor finance and rent-to-buy**

There are significant risks inherent in vendor terms and rent-to-buy schemes. The examination of the relevant law and how it has been applied in Chapter 3 shows that the patchwork of laws can cause or exacerbate consumer detriment, particularly for buyers. The case studies in Chapter 2 show how these risks have materialised and the outcome.

### The business model is broken

At the heart of the problem with these schemes is the business model, which is weighted heavily in favour of intermediary brokers and investor vendors. This works to the detriment of vulnerable buyers and some vendors.

It does not appear to be possible, other than in rare cases, for these deals to be both affordable for buyers and profitable for brokers and vendors. This is particularly true where a broker is aiming to maximise their own profits and has minimal or no financial stake in the deal and bears minimal risks. These schemes are far from the win-win-win that the marketing claims.

### Risks for buyers

#### *The buyer is not the legal owner*

The vendor remains the property owner until the buyer has paid the total purchase price and registered the title.

Because buyers do not seek independent legal advice, they do not understand this significant legal risk. A vendor terms buyer may be able to register a caveat on the property, however Consumer Action has not seen cases where buyers have done this. A caveat also does not definitively secure a buyer's financial interest in the property, particularly where, for example, a lender has a mortgage over the property.



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- Do you have a small deposit?
- Or no deposit?
- Are you self-employed?
- Do you have credit issues from your past?
- Are you paying too much dead rent which is making it hard to save for a deposit?
- Do you have a lack of savings history
- Is your age a problem (too young too old)?
- Are you new to Australia?
- Does your religion not allow you to get a a loan from a bank?

## We can help YOU!



**At Last, There is a way to own a  
Home Quickly and Easily with  
No Banks & No Hassles**



*Graphic: Excerpts from marketing material aimed at hopeful home buyers, 2016*

### *Deals are unaffordable from the beginning*

The vast majority of the deals seen by Consumer Action were destined to fail from the start because they were simply unaffordable for the buyer.

The case studies show multiple instances of buyers being signed up to deals that stretch them beyond their financial limits. Buyers are typically on low incomes, often reliant on Centrelink payments, and may have significant debts. Many buyers who do not qualify for mainstream finance cannot afford an overpriced property at a high interest rate plus outgoings. Even if the buyer can afford the payments and outgoings, there is still the risk that after several years they will be in no better position to refinance.<sup>36</sup>

### *Refinancing is often impossible*

A buyer often needs to refinance within several years. This is either because the agreement is short-term, or costs under the contract, such as the interest rate, increase as time goes on. However, a buyer often cannot refinance because:

- The buyer has not built up enough equity in the overpriced property. A lender will assess a loan application based on the market value of a property, rather than the agreed purchase price. If the purchase price is higher than the market value at the time the buyer tries to refinance, the buyer may not have built up the deposit required by a lender, and will not get a mortgage.<sup>37</sup>
- The buyer's financial situation has not improved sufficiently. A buyer who originally could not get a mainstream mortgage must significantly improve that financial situation in a relatively short time. In case study 2, the buyer was assured by the broker that he would qualify for a bank loan in three years, even though he would still have had a debt

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<sup>36</sup> See further the discussion of responsible lending laws at pp 105-106.

<sup>37</sup> These deals have taken place in areas where increases in property values have not kept pace with average prices rises across Victoria: see The Naysayer (blog), *One more 'rent-to-buy' risk—property values*, 8 April 2016, <https://thenaysayer.net/2016/04/08/one-more-rent-to-buy-risk-property-values/>.

agreement (which is a form of insolvency regulated under bankruptcy laws) in place at the time the loan was needed, and therefore had virtually no chance of being approved.<sup>38</sup>

### *There may be hidden costs*

There are often significant costs that buyers are not fully aware of when signing up to a deal, for example, repairs and maintenance. Consumer Action has seen one buyer move into a house where the water heater had to be immediately replaced at the buyer's expense.

Tax implications are an added complexity. Vendors may need to pay capital gains tax during the deal and rent-to-buy buyers may need to pay stamp duty, even if they never successfully buy the home.<sup>39</sup>

### *Missing a payment risks everything*

The consequences of late or missed payments can be significant. Agreements commonly require buyers to pay a higher interest rate, late fees and the legal costs of recovering the overdue amount. In case study 3,<sup>40</sup> these costs increased the total amount that the buyer owed beyond the amount she had agreed to pay for the property, leaving her with no stake in the property and a large debt.

If a buyer has problems making payments, the usual protections that come with a mainstream mortgage (such as hardship)<sup>41</sup> or under residential tenancies laws (such as eviction procedures)<sup>42</sup> may not apply.

One promoter has stated that under some vendor finance arrangements 'there is a mechanism for buyers to access their equity build up'.<sup>43</sup> However, Consumer Action has repeatedly seen brokers and vendors

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<sup>38</sup> See p 44.

<sup>39</sup> See the discussion of taxes and duties at pp 95-100.

<sup>40</sup> See p 47.

<sup>41</sup> Under s 72 of the NCC.

<sup>42</sup> For example, under the *Residential Tenancies Act 1997* (Vic) Pt 6 Div 1 and Pt 7.

<sup>43</sup> P Dobson (Vendor Finance Institute), 'David and Julie Siacci', *Somersoft*

*Property Investors Forum*, 9 October 2010, 12:17am,

<http://somersoft.com/forums/showthread.php?t=60274&page=3>.

deny a buyer's request to refund part of their payments. This has forced buyers to take legal action to recover any money owed.

Critically to a buyer, where a deal fails and the buyer is legally entitled to recover an amount from the broker, there may not be any money to access. In some cases, a broker's company has gone into liquidation and a buyer has struggled to recover any money owed. This would not be the case if certain payments were required to be held on trust for a buyer (as with deposits in traditional property sales) or with a government authority (as with residential tenancy bonds).<sup>44</sup>

### Risks for vendors

#### *Losing control of the property*

A 'joint venture' agreement is inherently risky for a vendor. It can give a broker complete control over a vendor's property. This means the vendor can be committed to a long-term arrangement with unknown financial returns and no say in who the buyer is, the terms of the deal and the likelihood of the buyer being able to maintain payments.

Additionally, the vendor cannot control who moves into the home, and the broker generally does not oversee the property in the way a property manager would. There have been reported cases of buyers dealing drugs from and even setting up a drug lab in a property. A rent-to-buy arrangement may have been attractive to these 'buyers' because of the lower level of oversight.<sup>45</sup>

#### *Not getting the expected returns*

Depending on the vendor's agreement with the broker, the broker may be able to sell the property at any price and take fees or other proceeds from the deal. The vendor could end up with much less money than expected.

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<sup>44</sup> See the discussion of how a buyer's money could be better protected at pp 83-84, 90.

<sup>45</sup> Vendor Finance Institute, *Drug Labs*, 12 August [year unknown], <https://vendorfinanceinstitute.com.au/drug-labs/>.



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terms, we can assist you in solving your property problems!

*Graphic: Excerpts from marketing material aimed at desperate property owners, 2016  
and Facebook testimonial*

Consumer Action has seen cases where the vendor knew nothing of the broker's arrangement with the buyer and was receiving a very small amount from the deal. A vendor in a desperate financial situation who needs money fast will get a worse deal than a sophisticated, knowledgeable vendor.

#### *Not getting the expected returns*

Depending on the vendor's agreement with the broker, the broker may be able to sell the property at any price and take fees or other proceeds from the deal. The vendor could end up with much less money than expected. Consumer Action has seen cases where the vendor knew nothing of the broker's arrangement with the buyer and was receiving a very small amount from the deal. A vendor in a desperate financial situation who needs money fast will get a worse deal than a sophisticated, knowledgeable vendor.

#### *Inadvertently breaching the law*

A vendor is potentially liable for a broker's actions if the broker is considered a legal agent of the vendor. This could expose the vendor to legal liability for the conduct of a broker towards a buyer, despite the vendor having little or no personal involvement.

A vendor can also be vulnerable when acting on the advice of a broker. In one case seen by Consumer Action, the vendor may have breached sale of land legislation after following the broker's advice. A vendor in this type of situation could be at risk of prosecution and penalties.

### Risks for brokers

#### *Legal compliance*

Brokers face complex legal requirements when advertising and dealing with vendors and buyers. This includes liability for certain conduct and representations under the Australian Consumer Law (**ACL**) and obligations under sale of land and residential tenancies laws. They must also comply with the requirements of the NCC and licensing requirements



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“ Loads of lightbulb moments today which I'll use eg "show people don't tell people". easy ways to explain options to people in language they understand and how to spot trust questions when they come up. Rick's teaching follows my own values driven approach to using what are basically tools to help people. ”

*Graphic: Excerpts from marketing material aimed at property investors, 2016*

under estate agent laws and the *National Consumer Credit Protection Act 2009* (Cth) (**NCCP Act**).

Several brokers have fallen foul of the law in recent years. Chapter 3 details some of the enforcement action taken by regulators against these brokers.

### *Financial liability*

A broker often does not invest any money in a transaction, but faces significant financial risks if engaging in unlawful conduct. A broker may have to repay certain amounts to the buyer, compensate the vendor for financial loss and pay penalties for breaching the law.

### **Affordable home ownership models**

A lack of affordable housing drives the demand for vendor finance and rent-to-buy schemes. These schemes target people for whom home ownership is otherwise not an option. However, as the case studies in Chapter 2 show, they are not a fair, safe or realistic way to enable people otherwise locked out of purchasing a home to own a place of their own.

While Consumer Action does not endorse any particular model of affordable home ownership, there are more genuine attempts to open home ownership to people who cannot access traditional home finance.

### **Government schemes**

Some government schemes enable community or public housing tenants to buy the properties they are living in.<sup>46</sup>

There are other examples of government initiatives. For example, the Affordable Homes SA scheme offers homes for sale to first home buyers earning below a certain income for a limited period before they're offered

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<sup>46</sup> See *Buying your public housing property*, <https://www.sa.gov.au/topics/housing-property-and-land/housing/public-and-community-housing/tenants/buying-your-public-housing-property>.



to other buyers. These are newly built houses, house-and-land packages, and former public housing properties valued at under \$350,000.<sup>47</sup> The government-initiated HomeStart SA provides lower cost home loans and was created in response to high interest rates and unaffordable home finance options.<sup>48</sup>

Overseas, the UK government expanded a different type of rent-to-buy program in 2014, with significant funding.<sup>49</sup> This program provides support to housing associations and others to build houses, requiring the provider to lease the property at below market rent for a minimum of seven years. It is proposed that renters can save for a deposit during this time.

### Community schemes

Habitat for Humanity is a not-for-profit organisation that provides affordable housing for low-income families across the world, including more than 50 to date in Victoria. Their model uses skilled and unskilled volunteers and corporate partners and sponsors to fund and build new homes. Families spend 500 hours helping to build their homes, pay a deposit of \$1,000 and purchase the home at 95% of market value, on a no-interest loan with repayments capped at 25% of the family's income.<sup>50</sup>

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<sup>47</sup> Affordable Homes SA, <http://affordablehomes.sa.gov.au/>.

<sup>48</sup> HomeStart, <http://www.homestart.com.au>.

<sup>49</sup> Department for Communities and Local Government and The Rt Hon Sir Eric Pickles MP, *New 'Rent to Buy' scheme to help young people save and move up housing ladder*, 26 September 2014, <https://www.gov.uk/government/news/new-rent-to-buy-scheme-to-help-young-people-save-and-move-up-housing-ladder>.

<sup>50</sup> Habitat for Humanity Australia, *Home Building Program*, <http://habitat.org.au/our-work-in-australia/home-building-program/>.



## 2. When the deal fails: Case studies

### Key points

- Vendor finance and rent-to-buy deals carry very significant risks and there are multiple ways that the risks can materialise
- Buyers are the most vulnerable party when deals go wrong.
- The case studies show similar problems with these deals throughout Australia.

These case studies show the experiences of people who Consumer Action and other legal services have assisted. Names of individuals and businesses and some minor details have been changed to protect privacy.

“Nina has paid approximately \$57,000 to NFH Trust. She just wants her money back.”

## Case study 1: Nina, Victoria

### The buyer

Nina arrived in Australia as a refugee from East Africa in 2005. She became a single mother to six children when her marriage ended in late-2014. She lived in government housing in inner Melbourne and earned approximately \$2,500 per fortnight running her own family day care business from home.

### The deal

Nina was looking for a bigger property to rent but a friend put her in contact with a man who would help her design and build a new home for her family. In about July 2014 she visited the offices of a representative of New Family Homes Trust (NFH Trust). Andrew at NFH Trust said that the company could design and build a house for Nina after she paid a deposit, then she would need to make regular payments while it was being built. Nina understood that she would be purchasing the home by paying weekly amounts for a long time.

Nina chose a piece of land in western Melbourne and worked with NFH Trust to design the house. Approximately two weeks later, at a meeting which lasted approximately 20 minutes, she signed a Letter of Intent, which was conditional on, among other things, a formal Contract of Sale and Section 32 Statement being prepared by NFH Trust’s solicitor. The

Letter of Intent was entered into with NFH Trust, which Nina thought was the owner of the property. Andrew told Nina that the house would be built in 34 weeks, so she could move in and continue her day care business.

Nina paid NFH Trust a \$40,000 deposit, which was her life savings, then another \$9,000 and \$1,300 for legal fees and drawing up the contract. Andrew told Nina that \$10,000 would be obtained from the government by NFH Trust as a First Home Owners Grant. She also began paying \$600 per fortnight by direct debit. Nina was happy that she could buy a home for her family on a similar basis as renting.

### **What went wrong**

About six months after signing the Letter of Intent, and with no progress having been made on the construction work, Nina became concerned. She attempted to contact Andrew on numerous occasions but he evaded her or gave excuses for why the project was delayed. He promised that it would start soon. The construction work was not completed within 34 weeks as promised. Nina ended up losing her business, as she wasn't allowed to run a day care centre from her house.

In mid-2015, Nina decided that she didn't want to proceed with the project and stopped her direct debit payments. She requested a refund of the money she had paid to NFH Trust. Several months later, Nina was still waiting for her money to be repaid. She drove past the property and saw a 'For Sale' sign out the front.

Nina discovered that the property had been mortgaged to a bank, by a different company which was the legal owner of the land - the New Family Homes Pty Ltd, a few months after she had signed the documents and paid the deposit. It appears that NFH Trust was not the legal owner of the property that it purported to sell Nina. Caveats on the property had also been registered during July and August 2015 by other parties, some associated with Andrew.

An external controller was appointed on behalf of the bank to sell the land and to recover the amount owed to the bank. The bank alleges that they

had no knowledge of Nina’s agreement to purchase the property prior to the property being mortgaged.

## Outcome

Nina and her children are now living in a rental home in inner Melbourne. She is unable to run her business from her current home and is receiving Centrelink payments.

The legal status of the documents that Nina signed with NFH Trust is unclear and her legal claim in relation to the property is uncertain.

Nina has paid approximately \$57,000 to NFH Trust. She just wants her money back.



“Mike told them that if they entered into a ‘rent-to-buy’ agreement they could own the house in three years.”

## Case study 2: Will and Mara, Victoria

### The buyers

Will and Mara have three children. Will worked as a salesman and earned \$30,000 to \$35,000 per annum. Mira received parenting payments from Centrelink. Will had two adverse credit listings on his credit report and was paying back several debts. Will decided to try to buy a family home with his friend Abdi.

### The deal

Will and Abdi found a 'rent-to-buy' agent online. They met with Mike, a director of the rent-to-buy agency, who showed them a few houses. Mike represented the owner of the property. Mike told them that if they entered into a 'rent-to-buy' agreement they could own the house in three years. Mike's company would arrange finance for Abdi and Will to buy the house, which would be easy with their combined incomes.

Will signed up for a vendor terms contract. The purchase price was \$429,000. Will would need to pay an \$8,000 deposit and sign over his First Home Owners Grant of \$20,000. He would then make weekly payments of \$670 for three years, totalling around \$104,000. Will and Abdi would need to obtain a loan to make a final payment of \$404,000.

Will would end up paying approximately \$536,000 to the vendor, including the deposit, rent and the \$404,000 purchase price. If he bought the house, Will would then be paying interest on the \$404,000 bank loan.

Will was concerned that in three years they would need a loan for \$404,000, which was more than the value of the house. Mike said that the house was expected to increase in value to \$429,000 by then. Because of Mike's advice, Will agreed to buy the house. Abdi was not on the paperwork.

Neither Will nor Abdi spoke to a lawyer, and Will never met the vendor—they only met with Mike. Will and Mira paid the deposit of \$8,000 and signed over their rights to the First Home Owners Grant. Will, Mira, their children and Abdi moved into the house. For almost three years they made the payments.

### **What went wrong**

Towards the end of the three years Abdi moved out of the property and decided he no longer wanted to rent to buy. Will asked Mike to arrange the \$404,000 loan. Mike could not. Will believed that this was for two reasons:

- the property value had not increased as they were told it would, and in fact it may only be \$360,000, and
- Will still had credit defaults, and his income at that time was \$60,000 per annum.

Mike and other people at his company started avoiding Will.

Will and Mira then started to make weekly payments of only \$450. Almost one year later, Will tried to end the contract and get a refund. Mike told him it was not possible. They agreed to reduce the payments to \$350 per week.

## **Outcome**

Will and Mira are still in the house, paying \$350 per week. They have paid more than \$137,000 to Mike's company.

They want a refund of what they paid above market rent, the deposit and their First Home Owners Grant. These amounts total over \$80,000.



“By early 2011, Carla was paying 14% interest”

## Case study 3: Carla, Victoria

### The buyer

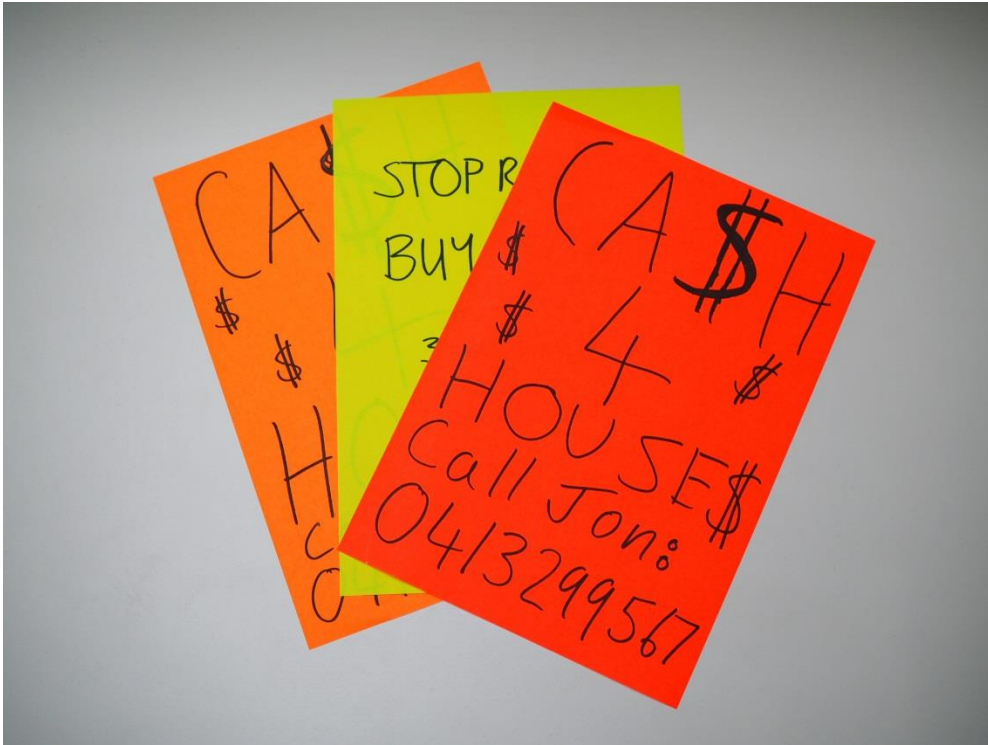
Carla was a single parent and lived in the Geelong area. She was not working and received Newstart allowance. She had bipolar disorder.

### The deal

In 2005, Carla was looking for a new home and saw an advertisement for an older house in outer Geelong that was available on vendor finance. She contacted Rob, the owner of the property.

Carla signed a vendor terms contract to buy the house for \$175,000 over 30 years. Rob actually valued the property at \$136,000. Carla was required to pay a \$1,500 deposit and signed her First Home Owners Grant of \$12,000 over to Rob. She then needed to pay \$280 per week in 'rent' and \$10 per week in rates. She would pay 1,520 of these weekly instalments, then a final payment of \$5,110.

Rob provided finance to Carla with an interest rate of 1.46% over what Rob was being charged on his own mortgage. If Carla did not make all of her payments, a default interest rate of 5% above the current interest rate was payable.



Carla moved into the house with her daughter. It was an older property and not in good condition.

The interest rate Carla was paying was variable. She was paying between 8% and 14% over the course of the agreement. Between January 2006 and June 2012, Carla was paying an average interest rate of 9.99%.

### **What went wrong**

By early 2011, Carla was paying 14% interest. She made her regular payments until May 2011, when she was hospitalised for approximately two months. While she was in hospital, Carla stopped paying the instalments. She was sent a default notice and given 30 days to pay all costs. Because she was in hospital, Carla did not get the notice or pay the outstanding amount. She was then given 14 days' notice to vacate the property. Penalty interest was charged from the time of default, on both the rental arrears and associated legal costs.

Carla did not receive the notices until she was home from hospital. She paid off the arrears within a few months but did not pay the legal fees. The penalty interest continued to accumulate on the legal fees. By mid-2011 Carla owed approximately \$184,000, which was more than she had agreed to pay for the house.

By June 2011, Carla was more than \$9,000 in arrears, of which more than \$8,000 was enforcement costs. By 2012, Carla was \$13,000 in arrears, including more than \$12,000 in enforcement costs.

Carla was undertaking some renovation work on the property in 2011 and 2012. However, in 2012, Carla's financial situation changed due to family reasons and she could no longer make the payments. Carla told Rob that she needed to sell the house urgently, then sought help from a lawyer to represent her as she sold the house. Carla felt she was no longer able to afford to make mortgage payments and stood to lose everything.

## **Outcome**

Because Rob held a credit licence, Carla's lawyer made a complaint to the Credit Ombudsman Service Ltd (**COSL**). Rob's internal dispute resolution system did not meet Australian Securities and Investments Commission (**ASIC**) requirements—in particular, Rob had passed on his internal dispute resolution costs to Carla. After the COSL complaint, Rob reduced the amount in enforcement costs and legal expenses that he was pursuing.

Carla found out that the actual market value of the house was closer to \$108,000. A lawyer acted for Carla as she sold the property and negotiated for Rob to pay her a final amount. Carla sold the house and received the payment from Rob after settlement. Carla's payment was enough for her to move into housing she could afford and restart her life.

“Sarah and Rohan quickly found it very difficult to make the payments on the house. The payments took up all of Rohan’s pay”

## Case study 4: Sara and Rohan, Victoria

### **The buyers**

Sara and Rohan lived in a rented house in Melbourne's north with their two young children. Rohan worked part-time and had multiple illnesses and injuries. He received his wage, WorkCover and a carer's allowance for their disabled son. Sara earned approximately \$100 per week working casually and received Centrelink payments. They had \$20,000 in savings and dreamed of owning their own home. They applied for a bank loan but could not get approved.

### **The deal**

In mid-2013, Sara found a four-bedroom house in their local area advertised on Gumtree. The advertisement said you could own the home for \$570 per week with no deposit. Sara called the number in the advertisement and spoke with Felix. Felix, a director of the company advertising the house, said that they helped people who could not get a home loan to own their own home.

Sara filled out a 'pre-qualification form'. The next day Fiona, an employee of the company, told Sara that she had 'qualified'. Sara and Rohan

inspected the house with Felix and were keen on it. They gave Felix their application and a \$750 refundable application fee on the spot. Felix requested more documents, and soon told them that they were formally approved.

Sara and Rohan agreed to buy the house under a five-year vendor terms contract for \$365,000. They would pay a \$20,000 deposit and the \$7,000 First Home Owners Grant, then \$2,393 per month (\$570 per week), which was 8.5% interest only for the first three years. Felix said that they would be the owners of the house and would pay a monthly rent amount and insurance. He also said they could renovate the house. Felix's company arranged for the First Home Owners Grant to be paid to his company direct. At the end of the five years, Felix and his company would help them get a bank loan and buy the house for \$338,000.

Sara and Rohan paid the deposit. A week later, Fiona sent Sara a contract of sale and notes for the solicitor who would 'assess' the contract. After they signed the contract, Sara and Rohan had a brief meeting with the solicitor who Fiona recommended to them. The documents only included the name of the property owner, and did not mention Felix's company.

After signing the documents, Sara asked Fiona how much of the monthly 'rent' would come off the loan at the end. Fiona said the rent would pay the loan interest only, but that they could make lump sum payments towards the purchase price at any time. Fiona said that if after three years the property value had increased to \$420,000, Sara and Rohan would have an 80% loan to value ratio and would not likely need to pay a further deposit.

In June 2013, three weeks after Sara first spoke with Felix, Sara and Rohan moved into the house. Sara and Rohan only ever met Felix or Fiona at the house, not at an office. Sara and Rohan only met the property owner once, when she was dropping off a few squares of spare carpet, shortly after they moved in.

## What went wrong?

Sara and Rohan quickly found it very difficult to make the payments on the house. The payments took up all of Rohan's pay, and for four months they were still paying rent on their old house. They found it hard to get enough money for food and fell behind on many of their bills. They resorted to a lot of credit and Rohan borrowed money from colleagues.

Sara and Rohan realised that their repayments were expensive. Their neighbours were paying \$325 per week rent. The median rent for a four-bedroom house in their area was \$360 per week. At their previous rental property they had been paying \$330 per week for a similar house with a bigger backyard.

In October, Sara and Rohan could only pay part of their monthly payment. In November, their third child was born. There were complications during the birth and Rohan had to take time off work. From November onwards, they made whatever payments they could but never the full amounts. Sara received emails requesting she catch up on payments from Fiona and the real estate agent taking the payments. Fiona told Sara to contact her if she was experiencing financial difficulties.

By February 2014, Rohan was very sick and needed surgery. Fiona arranged for Sara and Rohan to make payments by direct debit. Sara wanted to make lower payments over a longer time. In April, Sara and Fiona agreed on monthly payments of \$2,000 for six months, and for the remaining amounts to be added to the purchase price. They signed new documents. Sara noticed that the direct debit payments were now being taken by a different company.

In August 2014, Fiona emailed Sara saying that the lower payment would revert to the higher amount in October. Sara said they would do their best but that they were struggling and borrowing money from Rohan's parents. Sara and Rohan continued to pay what they could but decided to sell the house. Sara told Fiona that they would move into another rental property as soon as possible and would make fortnightly payments and pay the arrears when the property was sold. Fiona said they must

continue to make the monthly payments and that the owner of the house might want to sell it herself.

Sara and Rohan eventually found a rental property and moved out of the house. Fiona said that repairs and professional cleaning must be done at Sara and Rohan's expense as soon as possible, because there was already another buyer for the house.

Sara and Rohan were in a bad way. Rohan's dad helped them with the cleaning, repairs and finances. He arranged with Fiona to pay the final arrears of \$4,700 by Christmas 2014.

### **Outcome**

Sara and Rohan paid \$62,541, not including incidental costs such as rates, for the house over approximately 18 months. They are considering their legal options.

“Davina and the lawyer both told Anna that it was like a mortgage”

## Case study 5: Anna, NSW

### The buyer

Anna lived in a rental home in regional NSW with her partner Rob and their children. Rob had just started a new job. Anna had left school in year eight. She stayed at home with the children and received Centrelink benefits. She was a victim of family violence.

### The deal

Rob saw a 'For Sale' sign outside a house in their local area. Rob called the number on the sign and spoke with Davina. Davina was the sole director of Don't Wait Buy Now (DWBN), a trustee company of a property trust that owned the property. She said DWBN's aim was to 'help people with financial difficulties purchase their own home'.

Rob and Anna inspected the property. Anna did not want to buy a home at the time but Rob insisted. Rob was being violent towards Anna at the time and she felt intimidated.

Rob had debts and credit defaults, and told Davina that he knew he would not be able to get a mortgage because of his credit problems. Davina said



Rob and Anna would need to be joint purchasers, even though Anna had no income other than her Centrelink payments.

Anna and Rob moved into the property and soon after signed a contract to buy the house for \$349,000. They paid a \$34,000 deposit, including the \$14,000 First Home Owners Grant. The remaining \$315,000 was to be paid by 780 fortnightly instalments of approximately \$1,200 per fortnight, covering the purchase price and interest. The interest was at a reference rate with a premium on top.

Anna and Rob also had to pay for outgoings and insurance for the property. The contract allowed them to renovate the property at their own expense or on-sell the property. If Anna and Rob defaulted on the contract, by not keeping up with their payments, they could be evicted and charged additional amounts for the arrears.

Davina recommended a lawyer for Anna and Rob to see before they signed the contract. Anna asked Davina and the lawyer whether the contract was a rent-to-buy contract. They both told her that it was like a mortgage. Davina said it would help to improve Anna and Rob's credit rating. Anna felt pressured by Davina but particularly Rob to sign everything in the lawyer's office on the day, to get a discount on the legal fees. Anna says she did not understand the documents when she signed them and Rob did not read them.

Over six years, Anna and Rob paid \$238,000 in instalments, plus rates and insurance, and made more than \$20,000 worth of improvements.

### **What went wrong**

After six years in the house, Anna and Rob decided to divorce. Rob moved out and Anna stayed in the house. Anna contacted Davina to talk about selling the property. Anna says that Rob agreed that he would keep up the payments to the house, but the following month he stopped making payments.

Davina began to send default notices to Anna and Rob. A few months later, Anna engaged a real estate agent to sell the house. Anna struggled to sell the house because it was in a mess and she was having trouble coping with the sales process. Anna got an offer to buy the house for \$315,000 but she thought that price was too low.

Nine months after Anna and Rob stopped paying, Davina got a court judgment against them, requiring them to pay Davina \$27,000. A subsequent court order overturned that judgment, ordered Anna to pay \$150 per week rent and expedited a hearing in the Supreme Court of NSW.

### **Outcome**

The Supreme Court found in Anna's favour. The judge held that the agreement Anna and Rob had entered into was unjust, and that the notices of default that Davina issued were not valid under the NCC.

Davina was ordered to repay everything that Anna and Rob had paid towards the property, aside from the equivalent of market rent. This amount totalled almost \$115,000. Anna had to move out within 30 days.<sup>51</sup>

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<sup>51</sup> The summary of the legal proceedings in this case is current as at 12 September 2016. The decision of the NSW Supreme Court is detailed at p 107.

“We thought that Ernie and Gloria were giving us a break”

## Case study 6: Joe and Kate, New South Wales

### **The buyers**

Joe was in his early 40s. He grew up in public housing in a rural area and left school in year 10. He describes himself as not being good at school. He has no formal qualifications and has worked in a range of jobs, including driving trucks. Kate left school at 14 years old and has worked in various jobs, mainly cleaning. Kate and Joe were both in debt agreements, which are a form of insolvency regulated under bankruptcy laws. They lived in rental accommodation in regional NSW.

### **The deal**

In mid-2012, Kate and Joe saw an advertisement in a newspaper for vendor finance through Your Home Now (YHN). They called the phone number in the advertisement and spoke with Ernie. Ernie told Kate and Joe that the rent they paid for a house would be used as a deposit, and the extra money they put in as an option fee was like a bank account—at the end of the agreement they could use that money to prove to a bank that they could regularly make repayments. Ernie told Kate and Joe that he would help them get a loan.

Ernie asked Kate and Joe to fill out an application with their financial details, rental history, outstanding debts and income. Kate and Joe both told YHN that they were in debt agreements. Kate and Joe also signed a form stating that they were offered the chance to seek legal advice. Joe spoke to Ernie's wife Gloria about this over the phone. Gloria said that 'any legal people will tell you the same as what we're telling you so save your money'.

Kate and Joe were quickly approved. Ernie told them to drive around the area and look at properties that were for sale, then give him a list of six properties that they liked. Kate and Joe understood that Ernie and Gloria would purchase a property on their behalf, then in three years the house would be theirs with a bank loan that YHN would arrange. Kate and Joe believed that in that first three years they and Ernie and Gloria would own the house.

Kate and Joe say:

*We were very happy about having been accepted and that we were finally going to get ahead in life. We thought that Ernie and Gloria were giving us a break.*

Kate and Joe found a three-bedroom house that they liked. Ernie told them that they could buy it for \$336,000. Ernie and Gloria wanted \$3,000 upfront from Kate and Joe. However, as the time to sign the contract got closer, that amount increased to \$10,000. By then, Kate and Joe were very excited. They borrowed money from family and paid all that they could, which was \$8,000 upfront.

Kate and Joe signed a three-year residential tenancy agreement and option agreement with YHN. Under the lease, the rent was \$381 a week for the first year, then increased by 4% each year. Under the option agreement, they paid the initial \$8,000 deposit then option fees of \$381 per week for the first year, \$403 per week for the second year and \$427 per week for the third year. Only the deposit and \$41 per week of the option fee would be credited to the purchase price of the property, totalling \$14,396 over the three years. After three years, they could

exercise the option and buy the house. If Kate and Joe did not buy the house after three years, all option fees were kept by YHN. At the same time, YHN gave them an unsigned contract for the sale of land with the agreed price of \$336,000.

All of their dealings were done over the phone and by post. Kate and Joe never met Ernie and did not meet Gloria until 2015.

### **What went wrong**

Two months after signing the agreements, Kate and Joe moved into the house. Gloria and Ernie sent them a letter a couple of months later 'to CONGRATULATE you on the purchase of your family home'. After Kate and Joe moved in, they were under huge stress and worked extra hours to make the repayments. To them it seemed like 'the deal of a lifetime' and they needed to make it work. There were times when Joe felt suicidal.

About 18 months into the agreement, Joe called Gloria because he was worried he might not be able to get a bank loan at the end of the three-year period. Gloria called him back a week later and told him not to worry, his credit report was good and he was on track to get a home loan with a bank.

Toward the end of the three years, Joe called Gloria again to start the process of getting a bank loan. Gloria told him that there was no chance of him getting a bank loan until his debt agreement was paid out, and that he would need a 20% deposit on the property. After three years, Kate and Joe were unable to buy the house. They did not have any money for a deposit (except the small amount from the option fees) and could not get a bank loan.

By that time, Joe was not getting overtime at work anymore. He could not afford a deposit on a rental property and the debt agreement made finding rental accommodation difficult. He and Kate asked Gloria if they could rent the property. Gloria said they could enter a six-month lease then go back into the option agreement with no penalties. Kate and Joe

met Gloria and signed the lease. They also signed another document but they do not know what that was. It was the only time they ever met Gloria in person. She said she would send them a copy of the lease and other document but they never received it.

Kate and Joe were misled from the outset, particularly into believing that the arrangement would lead to them getting a bank loan and owning the property. This was because:

- the agreed price of \$336,000 was inflated. Eighteen months after they signed up to the deal, the property was valued by a real estate agent at \$290,000 to \$300,000,
- Kate and Joe were paying considerably more than market rent. Three years after they entered the agreement, a similar house on the same street was advertised at \$330 per week rent. They paid over \$62,000 rent in three years,
- the option fees totaled \$71,032 over three years but only \$14,396 of this was credited to the deposit on the property. This was only a 4.3% deposit on the inflated purchase price,
- the high rent and option fees meant that Kate and Joe could not save any more money toward the deposit, and
- Joe's debt agreement was still in place at the time the option to purchase would have arisen and Kate's would have recently ended but still have been listed on her credit report. It would have been almost impossible for them to get approved for a bank loan.

## **Outcome**

Kate and Joe decided not to take legal action. They wanted to remain in the house and did not think that they could find alternative rental accommodation. They were also worried about upsetting the landlord or Gloria. They are still paying rent and have paid over \$68,000 in option fees for an option they were never going to be able to exercise, as well as above-market rent. This deal has been devastating for Kate and Joe.

YHN's website appears to have been taken down. There is now no record of them anywhere.

“By the time Jane and Ian got the letter they only had six days to move out.”

## Case study 7: Jane and Ian, New South Wales

### The buyers

Jane and Ian lived with their children in regional NSW. Ian worked and had become bankrupt. Jane received parenting payments from Centrelink.

### The deal

Ian found a house in the local area advertised on Gumtree and showed it to Jane. Jane knew the house and thought it looked 'alright'. They contacted the advertiser through the email address in the advertisement. They got a call from Rose. Rose was not the owner of the house but acted for the owner.

Rose asked what their annual income was and quickly said they were eligible. She then asked them to fill in application forms and arranged for them to look at the house. They were keen and Rose sent them the paperwork to buy the house. This all happened within a few days.

Jane and Ian decided to buy the house for \$269,000 in a rent-to-buy deal. They signed a two-year residential tenancy agreement and an option agreement with the property owner, although they never met him. Rose was not mentioned in any of the paperwork.

Under the tenancy agreement, Jane and Ian were required to pay \$304 per week rent. Under the option agreement, they were required to pay an upfront fee of \$8,000 within three months of signing. Then they were required to pay a weekly option fee of \$304 per week for the first year and \$328 per week for the second year. It also allowed Jane and Ian to request a 12-month extension. If they did so, they had to pay \$2,900 then \$350 per week in option fees. There was nothing in the agreement about extending it beyond three years. If Jane and Ian did not exercise the option to purchase, the option fees would not be refunded. The unsigned contract for sale required a deposit of approximately \$15,000, which would come from the money Jane and Ian paid plus a \$7,000 First Home Owners Grant.

Jane remembers Rose saying that she was 'registered with the bar of solicitors' and there was no need for them to get legal advice. Rose said she could explain the documents, which would save them paying \$1,200 to get their own solicitor. They had not met Rose but were keen to meet later to discuss the details, especially because they had heard about the First Home Owners Grant ending soon.

Jane and Ian signed the agreements and paid \$5,000 of the deposit. They moved into the house. It needed a lot of repairs, including a new hot water system. Rose encouraged Jane and Ian to do any renovations and repairs, at their own cost.

### **What went wrong**

Jane and Ian were going to pay the remaining \$3,000 when they got a cheque they were owed. Because it was delayed, Rose asked Jane to pay an extra \$100 per fortnight. Jane agreed. A few weeks later, Jane remembers Rose asking for 'another \$50 but weekly instead of fortnightly'. Although Jane told Rose they could not afford it, eventually Jane and Ian were paying \$750 per week.



After living in the house for four months, Jane and Ian were under massive financial and personal stress. They were struggling to find money to feed their children.

Jane also became suspicious about the extra payments Rose was asking for. She went to see a lawyer. Jane discovered that they were not eligible for the First Home Owners Grant. They also asked a local real estate agent for an estimate of the house's value. He gave an estimate of \$195,000 to \$205,000, meaning the agreed sale price may have been around 35% higher than the market value.

Jane and Ian stopped making payments under the agreements because they realised that they were actually just renting and were ahead with their rent. Their lawyer wrote to the owner telling him that the option agreement was terminated because it relied on the First Home Owners Grant, which would not be available. Within two weeks of the letter, Rose's lawyer sent Jane and Ian a notice of termination of the tenancy agreement. The letter said that Jane and Ian had to either pay the rental arrears or move out within 14 days.

By the time Jane and Ian got the letter, they only had six days to move out. Their lawyer said this was not legally enough notice and that they could go to the Consumer, Trader and Tenancy Tribunal.

## **Outcome**

Rose took Jane and Ian to the tribunal to get them evicted. The tribunal found that the tenancy and options agreements were essentially one agreement. The option fees that Jane and Ian had paid were treated as rent in advance, therefore they had already paid their rent for almost a year. The tribunal did not consider whether the rent was market rent.

The tribunal could not rule on the \$5,000 deposit as it was linked to the contract for sale rather than the lease or option agreement.

Jane and Ian were able to stay in the house for another two months. When they moved out, the owner had to pay them over \$800 in advance rent payments and other costs.

Jane and Ian were in the house for less than one year. They decided not to pursue the \$5,000 deposit because of the stress and cost of taking legal action.

Under the agreements, they would have paid a total of almost \$64,000 in rent and options fees over two years, but only \$15,000 would go towards a deposit to buy the house. Even with the \$15,000 deposit, they would have needed a bank loan of \$254,000 to buy a house valued at approximately \$200,000.

Rose continued to pursue Jane and Ian for money for repairs and other costs for almost a year after they moved out.

Jane and Ian separated because of the stress they were going through, but they are now back together and living with family.

“James harassed and frightened Michelle, hoping she would vacate. He disconnected the gas and electricity and entered the property several times”

## Case study 8: Michelle, South Australia

### The buyer

Michelle was on a disability support pension and had a mental illness. She had left a violent relationship and moved from regional South Australia to Adelaide with her two sons. Michelle was living in temporary accommodation at a friend's place when she first moved to Adelaide. She had \$20,000 from a property settlement relating to her family home.

### The deal

In early 2007, Michelle was urgently looking for accommodation when she came across an advertisement for a rent-to-buy property in the newspaper. She called the number in the advertisement and spoke with James. She inspected the property with James and got the impression that he was the owner. The house was quite run down.

James called a few days later to negotiate a sale price. Michelle wanted to negotiate at their next face-to-face meeting. The following day, James called to negotiate a deposit. He told Michelle to draw a cheque in his name for \$20,000 and confirmed that this would be the deposit for the purchase of the property. James also said that he required \$1,680 cash, being four weeks bond and two weeks rent in advance (\$280 per week).

James told Michelle that she had to pay \$1,500 per quarter into his bank account and \$200 towards the cost for a lawyer to draw up a contract of sale. Michelle paid James the deposit, bond and two weeks' rent that day.

The next day, James told Michelle to go to a lawyer's office to sign the contract. She thought she was going to see a lawyer but was taken to a Justice of the Peace. James was in fact not the owner of the property. He was instead assigning to Michelle a rent-to-buy agreement that he had with Tina, the property owner. Michelle was given a four-page document purporting to assign James' interest in the rent-to-buy agreement to her. She did not have an opportunity to read the papers and she signed the papers with the belief that the rent-to-buy contract was being drawn up by a lawyer and that there were further legal processes. Michelle never got any legal advice on the contract.

Three days later, on a Friday, Michelle moved into the property. She contacted Centrelink about her pension and was asked to provide documentation about the rental agreement.

### **What went wrong**

Over the weekend, Michelle suspected that something was wrong. On Monday morning she went to her bank to try to stop the cheque payment for the deposit. She went to the police station, Land Titles Office, Legal Services Commission (LSC), Real Estate Institute SA and Residential Tenancies Tribunal (RTT) for assistance. The RTT told Michelle that it was a civil matter and they could not assist. Michelle went to the address that James used as his address on the contract but discovered that he did not live there.

The LSC helped Michelle to draft a letter requesting receipts for all of the money she had paid, confirmation that the bond had been registered with the RTT, and evidence that James was authorised to act on behalf of Tina. It also raised doubts about the legality of the option transaction. After he received the letter, James went to Michelle's home and told her that he had paid Tina \$10,000 and that he paid \$1,000 for that contract.

The LSC referred Michelle to a community legal centre. Her lawyer at the legal centre sent a letter to James stating that there was no legal contract for the sale of the house and that the \$20,000 must be returned immediately. A couple of weeks later, James went to Michelle's home again and tried to encourage her to go to a finance company to obtain a loan. When Michelle said she was no longer interested in purchasing the property, James threatened that she was at risk of losing her \$20,000 deposit. Michelle's lawyer referred her matter to the regulator (now Consumer Business Services).

Michelle could not afford her rent and did not pay any more rent. She refused to vacate until her money was returned. James harassed and frightened Michelle, hoping she would vacate. He disconnected the gas and electricity and entered the property several times. Michelle got a restraining order against James. However, the next day, James assaulted Michelle and her son with a screw driver.

Michelle was served with a breach of agreement notice and required to attend a RTT hearing to have her evicted.

At the RTT, Michelle found out that there was a rent-to-buy agreement between James and Tina, and that James was attempting to assign his interest to Michelle. Tina lived in Queensland and her husband had negotiated the rent-to-buy agreement with James. Tina said she signed the contract without reading or understanding it, because she was told to by her husband, who negotiated the agreement with James (Tina's husband was deceased by the time Michelle moved in).

Tina said that she received \$8,000 from James and was supposed to receive \$2,000 per year rent for what she thought was three years. She later learned the agreement was for five years. James and Tina used the same solicitor, who did not identify that the purchase and sale contract were void in South Australia. Tina claimed that James had never been honest with her.

## Outcome

Michelle was evicted from the property by the RTT order. She sued James in the Magistrates Court for the return of the \$20,000 deposit. Approximately 18 months after Michelle signed the rent-to-buy contract with James, the court ordered James to pay her \$20,000, as the agreement was voidable under s 6 of the *Land and Business (Sale and Conveyancing) Act 1994* (SA). However, despite successfully obtaining judgment against James and going through some enforcement processes, Michelle never recovered her deposit from him. Michelle obtained victims of crime compensation for the injuries suffered during the assault by James.

James claimed that he was homeless. He was arrested under a warrant because of his failure to attend investigation hearings. He had no assets to seize or sell to pay the debt to Michelle.

The RTT found that the agreement between James and Tina was not a residential tenancy agreement and therefore the RTT had no jurisdiction to hear the matter. Tina took court action against James. Michelle's lawyers do not know what happened in this action.

“They did not know that the option agreement was void and the lease agreement was voidable under South Australian law.”

## Case study 9: Alice, South Australia

### The vendor

Alice was a widow in her 60s. She was illiterate and depended on her children to manage her financial affairs. Alice was suffering from severe arthritis. She owned a house in the northern suburbs of Adelaide. She was concerned about maintenance of her property with her deteriorating arthritic condition.

### The deal

One of Alice's sons, Nick, who had limited commercial experience, saw an advertisement by The Property Company (TPC) in the local council newspaper. Nick contacted TPC then Alice spoke with Jim, the director of TPC. Jim had attended property investment seminars to learn techniques to make money from property. Jim proposed that Alice enter into a Power of Attorney with TPC to sell and transfer the title of her home. TPC also arranged for Alice to sign a letter appointing a conveyancer and giving directions to that conveyancer to follow Jim's advice and pay the proceeds of the sale of Alice's home to TPC to 'enable the execution of other agreements we have between ourselves'.

Jim used the equity of approximately \$200,000 from the sale of Alice's home to buy two options to purchase other properties in the same

suburb. Each option cost approximately \$100,000. One option was in Nick's name, so Alice effectively gifted half of the equity in her home to Nick. The other option was in Alice's name. The market value of the houses was approximately \$175,000 and \$350,000.

Alice and Nick each signed five-year option agreements and lease agreements for the new houses, with an amount for rent and an amount for the option fees. Between one-half and one-third of the rent was to be applied towards reducing the agreed purchase price at the end of the five year period. The option fees paid would be credited to the purchase if the options were exercised. Jim told Alice and Nick that the option fees and the part of the rent that would be credited to the purchase price would be kept in a trust account. The lease agreements were never registered with the regulator, Consumer and Business Services SA.

Alice and Nick did not seek any legal or financial advice before signing the documents. Alice could not read the documents. The documents suggested that, by entering the rent-to-buy arrangements, Alice and Nick would save thousands compared with a bank loan.

### **What went wrong**

Alice and Nick were both paying significantly above market rent. Alice could not afford to pay the rent so it was arranged for Nick to pay approximately 80% of the rents combined. After several years, Nick was unable to work, and he could no longer pay the rent for the two properties.

After Nick could no longer afford to pay, Alice and Nick were evicted. Alice and Nick then saw a solicitor and found out that there were multiple problems with the agreements they'd made. These included that:

- because Alice and Nick did not get legal advice before signing the documents, they did not know that the option agreement was void and the lease agreement was voidable under South Australian law. The only public warnings about this are on the Consumer and Business Services SA website, but Alice is illiterate and does not use the internet,



- Alice gave TPC the Power of Attorney over her home without understanding what it was, therefore there was an issue with her legal capacity to do this,
- the Power of Attorney was invalid because the witness was not qualified to witness the execution of it, and
- although Jim told Alice that the option fees and rent money that would be credited to the purchase price would be kept in a trust account, they were not.

Jim said that TPC did not have sufficient money to pay back the option fees and the rent above market rent paid by Alice and Nick. There is concern that TPC will go into liquidation or that Jim will transfer money out of TPC now because he knows about the protections in place in South Australia.

## **Outcome**

The future for Alice is unknown at this stage. The home that she sold to TPC has been rented to another family under a rent-to-buy arrangement. She has put a caveat on it.

It is likely that if TPC goes into voluntary administration or liquidation that Alice will not recover all of the money that she is legally entitled to. She will then have to see if she can recover money from Jim personally for breach of his director duties or to examine whether Jim has tried to move money out TPC.

“Keith and Julia have paid a total of approximately \$134,500 in rent and \$85,500 in ongoing option fees”

## Case study 10: Keith and Julia, Western Australia

### The buyers

Keith and Julia lived in regional Western Australia. In 2009, they wanted to move to Perth to be closer to their children and grandchildren. Julia had owned a small business before moving to Perth. When they moved to Perth, Julia worked at a bank in the city, while Keith worked fly-in-fly-out at the mines. Keith cannot read well and has difficulty understanding documents at times. He is also partially deaf and has attention deficient disorder.

### The deal

In 2009, Julia started researching ways that she and Keith could purchase a home. Julia had default listings on her credit file from the time that she owned the small business, and this meant that she and Keith would have needed to pay a 20% deposit and take out lender’s mortgagee insurance to obtain a home loan. Julia started looking at alternative options.

Julia started researching other options online to buy a property. She found Own Your Home, No Loan Pty Ltd (OYHNL). Her contact for OYHNL was Toby. After doing some online research about OYHNL, Keith and Julia

decided to give this option a go and filled out some online application forms in late 2009.

In early 2010, Julia and her daughter met Toby at a local café to discuss the agreement with OYHNL. Keith was not involved in this process as he was away working at the time.

During the course of the meeting, Julia understood that the agreement with OYHNL meant that:

- Keith and Julia would be renting a property through an arrangement set up by OYHNL,
- during the course of the rental agreement, they would pay an ongoing option fee in addition to their rent payments, which would provide them with the option of purchasing the property at the end of their rental agreement. When the time came, this additional fee would come off the purchase price of the property,
- an upfront option fee was payable and would be used to help with future settlement costs,
- the option to buy would be valid for five years,
- once Julia and Keith were in a position to purchase the property, a statutory declaration would be signed by the property owner to state that a certain amount of money had been received, and so would be deducted from the purchase price, and
- Keith and Julia would be part-owners of the property and could make improvements to the property as they liked.

Julia also asked Toby what had happened in previous circumstances where prospective buyers had eventually been unable to buy the house. Toby said that in these circumstances, the money was refunded.

At the end of the meeting, Julia signed an option to buy contract. The contract actually stated, among other things, that:

- the sale price of the property was \$526,000,
- the upfront option fee was \$17,500, to be applied in full towards the purchase price and deposit at settlement, or to be forfeited to the vendor if the option lapsed or was terminated,

- the ongoing option fee would be payable as a weekly fee of \$295 for four years,
- for one year only, each time the \$295 per week ongoing option fee was paid on time, Julia and Keith would receive a credit of \$200 per week towards the purchase price and deposit at settlement, a total amount of \$10,400,
- the balance price of the property at the end of the agreement would be \$498,000, and
- the option expired after four years.

Julia signed the option to buy contract at the meeting and took a copy home for Keith to sign, even though Toby said that Keith did not need to sign. A few days later, Keith signed the contract and posted it to Toby. Keith and Julia did not keep a copy of the contract for themselves.

Keith and Julia did not speak to a solicitor, or seek independent advice on the contract, at any point.

After signing the contract, Keith and Julia paid a \$17,500 'upfront option fee' into the OYHNL nominated bank account. This was paid from money they had saved. This was the last time they dealt with Toby and OYHNL.

Keith and Julia moved into the property in mid-2010. They were greeted by the property owners, Bill and Rebecca, and were handed the keys.

Keith and Julia dealt with Bill via email or phone to sort out administrative matters, such as rent payments.

Keith and Julia paid Bill and Rebecca \$450 per week for rent and \$295 per week as an 'ongoing option fee'. They did not enter into a separate lease. Keith and Julia also believed that they were part-owners of the property and could make improvements to it as they wished. They estimate that they have spent more than \$14,000 on home improvements and maintenance. They did not ask Bill and Rebecca to pay these costs.

For four years, Keith and Julia paid \$2,380 per year to Bill and Rebecca to cover shire rates and water usage.

### **What went wrong**

Keith and Julia originally entered into the agreement fully intending on purchasing the property, but encountered some financial challenges stemming from various changes in their work and family circumstances.

Keith and Julia stopped paying the weekly option fee in late 2015. In early 2016, Keith emailed Bill to say that they were no longer in a position to buy the property, contrary to their original intentions. Keith asked if Bill could refund the option fee. Bill replied that according to the option agreement, the buyer forfeits the option fees paid to the vendor if the option expires or ends. Bill told Keith and Julia that he intended to sell the house and he asked them to enter into a periodic lease and pay a bond. Bill stated that he was prepared to consider a partial refund when the house was sold.

The company OYHNL has been wound up and Toby has absconded.

### **Outcome**

Keith and Julia's likely outcome is still uncertain.

They are currently living in Bill and Rebecca's property and paying \$450 per week rent. Since they moved there in 2010, Keith and Julia have paid a total of approximately \$134,500 in rent and \$85,500 in ongoing option fees. They want to try to get back some of the money they paid in option fees, shire rates, water usage, improvements and maintenance.



### 3. The law

#### Key points

- Vendor finance and rent-to-buy schemes sit in grey areas of the law, with 'gaps' in regulation creating significant risks.
- Legal requirements and protections for people involved differ between jurisdictions and depending on the type of transaction.
- The nature of vendor finance arrangements makes the application of the National Credit Code (**NCC**) uncertain.
- The First Home Owners Grant can be accessed in vendor finance deals without a buyer ever having legal ownership.
- Taxes and duties can apply to these schemes even if there is not a successful home purchase.
- When these schemes fail, the dispute resolution options are often inappropriate and inaccessible, particularly for vulnerable people.

## Summary

This chapter examines the legal frameworks in which vendor finance and rent-to-buy schemes operate across Australia. It also examines enforcement action by regulators and decisions of the courts.

The laws relevant to these schemes include:

- sale of land laws, which regulate both vendor finance and rent-to-buy schemes,
- residential tenancies laws, which regulate some elements of rent-to-buy arrangements,
- estate agent licensing and conduct regimes, which can apply to brokers and vendors,
- the *National Consumer Credit Protection Act 2009* (Cth) (**NCCP Act**) and the NCC, which regulate certain vendor finance arrangements,
- consumer protections under the Australian Consumer Law (**ACL**) and *Australian Securities and Investment Commission Act 2001* (Cth) (**ASIC Act**), which apply to brokers and in some cases vendors,
- First Home Owners Grant schemes, and
- stamp duty, land tax and capital gains tax arrangements.

Overlapping laws can make legal requirements and obligations unclear. Gaps in the law can leave people with limited or no legal protections if things go wrong. The effectiveness of legal protections varies depending on the people involved and the nature of the transaction.

This legal uncertainty, coupled with a lack of independent legal advice, is why the risks of these schemes are so significant, particularly for buyers.

## Vendor terms contracts

A vendor finance agreement is called a 'terms contract' in Victoria, WA and NT and an 'instalment contract' in NSW and Queensland. In South Australia, it is a sale where part of the purchase price (aside from the

deposit) is payable before settlement.<sup>52</sup> Legislation in Tasmania and the ACT does not specifically deal with vendor terms contracts.

Laws in each jurisdiction aim to protect the interests of vendor finance buyers by:

- restricting the use of vendor terms contracts,
- allowing the buyer to require a transfer of title with mortgage-back,
- restricting the vendor from selling or mortgaging the property during the term of the agreement, and/or
- restricting the vendor's right to end the agreement.

## Victoria

*What is a vendor terms contract?*

The *Sale of Land Act 1962* (Vic) (**SLA**) defines a terms contract as:

[A]n executory contract for the sale and purchase of any land under which the purchaser is—

(a) obliged to make 2 or more payments (other than a deposit or final payment) to the vendor after the execution of the contract and before the purchaser is entitled to a conveyance or transfer of the land; or

(b) entitled to possession of the land or to the receipt of rents and profits before the purchaser becomes entitled to a conveyance or transfer of the land.<sup>53</sup>

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<sup>52</sup> Land and Business (Sale and Conveyancing) Act 1994 (SA) s 6.

<sup>53</sup> SLA s 29A. This definition was amended in 2008 (by the *Consumer Credit (Victoria) and Other Acts Amendment Act 2008* (Vic)) and again in 2015, to address uncertainty stemming from the 2008 amendments (by the *Veterans and Other Acts Amendment Act 2015* (Vic)). For the uncertainty of the pre-2015 definition see *Ottedin Investments Pty Ltd v Portbury Property Developments Co Pty Ltd* [2011] VSC 222 paras 43-51 and *Landmark Property Enterprise Pty Ltd v Monash Property Developments Pty Ltd* [2015] VSC 266, paras 36-51 (the case turned on the interpretation of 'deposit').



A 'deposit' is part of the purchase price, paid in one or more payments, with 60 days of the contract being signed by both parties.

A terms contract can only be entered into where the person selling the land is the registered proprietor, entitled to become the registered proprietor or empowered by statute to transfer the land.<sup>54</sup>

Because under the SLA definition a terms contract exists where certain payments are required *or* the buyer is entitled to early possession, a relatively broad range of transactions may be regulated as terms contracts under the SLA.

#### *Pre-contractual disclosure*

While the SLA covers a broad range of vendor finance arrangements, it also restricts how a terms contract can be entered into.<sup>55</sup>

Firstly, there are pre-contractual disclosure requirements in the SLA which aim to ensure that a buyer has sufficient information about a terms contract before they enter into it. Under these requirements, a vendor must tell a buyer:

- details of the vendor finance agreement and information about certain financial matters related to the property, including rates, taxes and other outgoings,<sup>56</sup> and
- whether the property is mortgaged and, if it is sold subject to a mortgage, certain details about the mortgage balance, current interest rate and instalments.<sup>57</sup>

A breach of the vendor disclosure requirements is an offence and the buyer can end the contract before settlement.<sup>58</sup> However, despite the pre-contractual protections in place, Consumer Action continues to see vulnerable buyers enter deals that are unaffordable and high risk. In the

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<sup>54</sup> SLA s 29B.

<sup>55</sup> Part 1, Div 4, ss 29A to 29W.

<sup>56</sup> SLA s 32A and Sch 2.

<sup>57</sup> SLA s 29M and Sch 1.

<sup>58</sup> SLA s 29N.

case studies in Chapter 2 of this report, none of the buyers obtained independent legal or financial advice prior to signing the contract. Buyers have signed documents that they did not fully understand, even if they met the SLA disclosure requirements.

Intermediary brokers have often played a significant part in convincing buyers to agree to vendor finance deals, despite a lack of knowledge of what they are signing.<sup>59</sup> The SLA disclosure requirements, while important to retain, do not in themselves deter vulnerable buyers from entering high-risk vendor terms contracts.

#### *Restrictions in relation to mortgages*

Under the SLA, a vendor must either discharge the mortgage over a property before a terms contract is entered into, or disclose certain details of the mortgage before the contract is entered into (see above).<sup>60</sup>

It is also an offence for a property owner to enter into a vendor terms contract where there is a mortgage over the property which also relates to one or more other properties.<sup>61</sup> If this occurs, the buyer can end the contract before settlement.

Once a vendor terms contract is in place, a vendor must not take out a mortgage on the property in question.<sup>62</sup> If a vendor does this, the contract can be ended and the vendor is guilty of an offence. In addition, if the mortgagee had notice of the buyer's interest, it cannot enforce its rights as mortgagee.<sup>63</sup>

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<sup>59</sup> The conduct of brokers and vendors is covered further in chapter 1 and in the discussion of the ACL at pp 108-116.

<sup>60</sup> SLA ss 29M and 29O.

<sup>61</sup> SLA s 29M(a).

<sup>62</sup> SLA s 29P.

<sup>63</sup> SLA s 29S(1). If a lender had notice of a buyer's interest under a terms contract, the lender must discharge the mortgage. A lender can also recover any money paid to the vendor under the mortgage.

A buyer may not be able to end a terms contract if a vendor acted 'honestly and reasonably and ought fairly to be excused for the contravention' and the buyer is 'substantially in as good a position as if all the relevant provisions' had been complied with.<sup>64</sup>

While the SLA does mitigate buyer risks where there is a mortgage over the property, a vulnerable vendor facing the loss of their property could still comply with these requirements while creating a high-risk situation for a buyer. This is particularly true where the vendor enters the deal without independent legal and financial advice.

Without an outright prohibition on vendor terms contracts being entered into in relation to a property which is mortgaged, vendor terms buyers will continue to be at risk of losing their home and money if a vendor's financial situation deteriorates.

Recommendation: Prohibit mortgage 'wrapping'

Vendor finance and rent-to-buy transactions, if not prohibited per se, should be prohibited for properties which are sold subject to a mortgage or other encumbrance.

*Protection of a buyer's legal interests*

The SLA seeks to address the critical risk of a buyer not having legal ownership of the property during the period of a vendor terms contract. It does this by giving the buyer a right to require the legal ownership of the property to be transferred to the buyer, with a 'mortgage-back' to the vendor.<sup>65</sup> If the property is mortgaged, it can be transferred subject to that mortgage only if the terms of the mortgage are not more onerous than the terms of the terms contract.<sup>66</sup> In Consumer Action's experience,

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<sup>64</sup> SLA s 32K(4)

<sup>65</sup> SLA s 29H.

<sup>66</sup> SLA s 29H(5).

the vendor's mortgage is not more onerous than the vendor terms contract, otherwise the vendor terms deal would not be profitable for the vendor and broker. It is an offence for a vendor to not comply with a buyer's request for a transfer with mortgage-back, and the buyer can seek civil remedies.<sup>67</sup>

The transfer with mortgage-back requirement has the potential to secure a buyer's stake in the property where the buyer is an equal party to a transaction and has independent legal advice. However, Consumer Action is not aware of any cases where a disadvantaged or vulnerable buyer has used this provision. There would be significant hurdles for disadvantaged and vulnerable buyers using a 'transfer with mortgage-back', including that:

- a buyer must proactively require the vendor to transfer the property—this would require complex legal advice, which disadvantaged buyers typically do not seek or cannot afford,
- a buyer would have to pay for the documentation, transfer and any other costs, as well as continuing instalment payments and outgoings—this would be prohibitively expensive for the buyers we have seen.

In addition to this, a vendor's financial situation and/or own mortgage may force the vendor to breach the SLA and face penalties, for example:

- a vulnerable vendor in financial stress may not be able to discharge the mortgage if required,
- the terms of a vendor's mortgage may restrict the vendor's ability to transfer the property, and
- a lender will most likely need to consent to the transfer, responsible lending obligations under the NCC will come into play, and other lender requirements may prevent the vendor from transferring the property to the buyer.

These factors make the transfer with mortgage-back protection under the SLA complex. This legislative protection is unlikely to assist disadvantaged

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<sup>67</sup> SLA s 29J.

buyers and could present a significant risk to vulnerable vendors. The buyer's lack of legal ownership in a vendor terms arrangement therefore remains a significant legal risk.

#### *Protection of a buyer's financial interests*

A buyer's lack of ownership rights in a vendor terms arrangement creates a major financial risk—the prospect of losing all of the money paid towards the home if the deal fails.

Under the SLA, any money paid by a buyer prior to possession is considered 'deposit monies' and must be paid into a conveyancer's, solicitor's or estate agent's trust account, or a special purpose account in both the vendor's and buyer's names.<sup>68</sup> However, Consumer Action has not seen any transactions involving vulnerable buyers where the deposit was held securely on behalf of the buyer. There appears to be widespread non-compliance with, or avoidance of, this requirement. In addition, because buyers often move in quickly and take possession of the property, the large amounts paid after a buyer moves in are not required to be held securely.

When a deal fails, a buyer can struggle to recover any money owed, even if there is an order for the return of some of the money paid. This is a critical risk for buyers which is not adequately addressed under the SLA.

#### Recommendation: Strengthen regulation of vendor terms contracts

If vendor terms contracts continue in Victoria, particularly those brokered by intermediaries for profit, the law should be amended to ensure that:

- the National Credit Code (**NCC**) applies, so that the transactions operate in an established credit framework and buyers have access to affordable dispute resolution options, and

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<sup>68</sup> SLA ss 23 and 25.

- certain money paid by the buyer is held securely on behalf of the buyer until settlement, so that a buyer can recover any amount they are entitled to if a deal is not completed.

## Other jurisdictions

### *What is a vendor terms contract?*

Legislation across Australia regulates different types of arrangements. In general, whether or not a particular transaction is a vendor terms contract depends on the number of instalments payable and what is considered the deposit.<sup>69</sup> For example, a terms contract in Queensland and the NT can involve just one payment between the deposit and final payment.<sup>70</sup> In Victoria, there must be at least two payments.<sup>71</sup> However, taking early possession will in itself create a terms contract in Victoria and WA.<sup>72</sup>

In NSW, an 'instalment contract' can only be entered into in relation to certain subdivision lots and where four or more part payments are made.<sup>73</sup> However, this more restrictive legislation has not prevented harmful property deals taking place in NSW. It appears that different transaction types are used or that the NSW laws have been contravened.

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<sup>69</sup> Aside from in Victoria and WA, the date on which the buyer takes possession is not relevant to whether a contract is a vendor terms contract.

<sup>70</sup> *Law of Property Act 2000* (NT) s 73 and *Property Law Act 1973* (Qld) s 71. In *Watpac Developments Pty Ltd v Latrobe King Commercial Pty Ltd* [2011] QSC 392, a deposit paid in instalments was still a 'deposit' under s 71 of the Queensland legislation and did not create an instalment contract.

<sup>71</sup> See SLA s 29A. This also includes an option to purchase under the same conditions.

<sup>72</sup> SLA s 29A(1)(b) and *Sale of Land Act 1970* (WA) s 5.

<sup>73</sup> *Land Sales Act 1964* (NSW) s 2. The subdivision must meet certain requirements, including the necessary approvals and a trust established in connection with it: ss 4 and 7.

South Australia has the most stringent regulation of vendor terms contracts in Australia. In SA, contracts that provide for payment of part of the purchase price (except the deposit)<sup>74</sup> before settlement have been void since 1973.<sup>75</sup> Any money paid by a buyer under a vendor terms contract can be recovered by the buyer.<sup>76</sup> This prohibition arose from a recognition of the particular vulnerability of a buyer under terms contract arrangements.<sup>77</sup> Consumer Action is not aware of any vendor terms deals in SA, however there have been harmful rent-to-buy arrangements in recent years.<sup>78</sup>

### *Buyer protections*

Property which is already mortgaged can be sold on vendor terms in all parts of Australia where terms contracts are permitted. For example, the NSW, Queensland and WA laws require a vendor to disclose any mortgage, among other things, before entering into a vendor terms contract.<sup>79</sup>

However, the Victorian ban on a mortgage being taken out in relation to a property that is already subject to a terms contract<sup>80</sup> is not replicated across Australia. In Queensland and NT, a vendor under a terms contract can sell or mortgage the property with the buyer's consent.<sup>81</sup> In WA, the property can be mortgaged with either the buyer's consent or permission from a court.<sup>82</sup> In NSW a vendor must give a buyer notice of the intention

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<sup>74</sup> The deposit is an amount paid in not more than three instalments before the date of settlement: *Land and Business (Sale and Conveyancing Act) 1994 (SA)* s 6(3).

<sup>75</sup> *Land and Business Agents Act 1973 (SA)* s 89. Instalment contracts are now void under s 6 of the *Land and Business (Sale and Conveyancing Act) 1994 (SA)*.

<sup>76</sup> *Land and Business (Sale and Conveyancing Act) 1994 (SA)* s 6(2).

<sup>77</sup> Bradbrook et al, *Australian Real Property Law*, 5th ed, Thomson Reuters, Sydney, 2011, p 471, para 8.340.

<sup>78</sup> See case studies 8 and 9, pp 65, 69.

<sup>79</sup> *Conveyancing Act 1919 (NSW)* s 52A(2); *Land Sales Act 1984 (Qld)* s 9(1); *Sale of Land Act 1970 (WA)* s 7.

<sup>80</sup> SLA s 29P.

<sup>81</sup> *Property Law Act 1973 (Qld)* s 73 and *Law of Property Act 2000 (NT)* s 75.

<sup>82</sup> *Sale of Land Act 1970 (WA)* s 8.

to mortgage the property, and the buyer can require a transfer with a mortgage-back.<sup>83</sup>

In relation to transfer with mortgage-back arrangements, in WA a buyer does not have this option. However, it is available in NSW and Queensland. In NSW, at least 15% of the purchase price must have been paid,<sup>84</sup> and in Queensland at least one-third of the purchase price must have been paid.<sup>85</sup> This contrasts with the equivalent Victorian provision, which does not require the buyer to have built up any minimum equity in the property before requiring a transfer with mortgage-back.

In terms of protecting a buyer's funds, in NSW at least 15% of the purchase price must be paid to the trustee of the relevant subdivision.<sup>86</sup> This provides more protection for a buyer's funds than the Victorian legislation, albeit in the more limited types of contracts regulated in NSW.

Specific notice periods and penalties apply for default under terms contracts in some parts of Australia. For example, in WA a buyer has 28 days, or what is reasonable in the circumstances, to remedy a payment default.<sup>87</sup> In Queensland and NT, the relevant period is 30 days.<sup>88</sup> These are stronger buyer protections than the general 14-day notice period and penalties in Victoria.<sup>89</sup>

A vendor terms buyer can lodge a caveat to claim an interest in the property in question in all parts of Australia. This is an express right under some legislation, or a right which stems from a buyer's equitable interest under the vendor terms contract.

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<sup>83</sup> *Land Sales Act 1964* (NSW) s 14.

<sup>84</sup> *Land Sales Act 1964* (NSW) s 13.

<sup>85</sup> *Property Law Act 1974* (Qld) s 75(1).

<sup>86</sup> *Land Sales Act 1964* (NSW) Pt 3. This can be released if certain conditions are satisfied: ss 7(d) and 12.

<sup>87</sup> *Sale of Land Act 1970* (WA) s 6.

<sup>88</sup> *Property Law Act 1973* (Qld) s 72(1) and *Law of Property Act 2000* (NT) s 74(1).

<sup>89</sup> *Estate Agents (Contracts) Regulations 2008* (Vic) Sch 1, Forms 1 and 2, General Condition 27.



## Rent-to-buy schemes

Rent-to-buy schemes do not have the same long history of use that vendor terms contracts have in Victoria. As outlined in Chapter 1, a rent-to-buy deal generally involves a residential tenancy agreement and a separate 'option to purchase' agreement. While they are regulated under both residential tenancies legislation and sale of land legislation, there are similar risks for buyers to terms contracts.

### Victoria

Rent-to-buy schemes were brought under the *Residential Tenancies Act 1997 (Vic) (RTA)* in 2008.<sup>90</sup> The RTA was extended to cover residential tenancy agreements regardless of the length of their term, if a tenant had a right or option to purchase the property.<sup>91</sup> The purpose of the 2008 amendments was to amend the RTA so that:

*[P]eople who are buying their homes through rent-to-buy arrangements are covered in the same way as other residential tenants—so they will be protected against unreasonable rent increases, so they will have the right to have the premises that they are renting repaired and so they can have limits placed on owners entering the property that they are renting. The amendments also provide access to dispute resolution at VCAT (Victorian Civil and Administrative Tribunal) to individuals who are buying their homes through a rent-to-buy arrangement.*

Rent-to-buy schemes sit in a very different regulatory space to vendor terms contracts under Victorian laws. The legal status of an option agreement in a rent-to-buy arrangement is unclear, as are the rights and obligations of people who enter into them.

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<sup>90</sup> Section 6 of the RTA was amended by the *Consumer Credit (Victoria) and Other Acts Amendment Act 2008 (Vic)*.

<sup>91</sup> The right or option can be under the tenancy agreement or another agreement (s 6) but the RTA does not apply to a tenancy agreement created accordance with a term of a contract for sale or mortgage (s 13).

An option agreement may be considered part of a tenancy agreement under the RTA, depending on the degree of connection between the option agreement and residential tenancy agreement, and the structure of the agreement as a whole. If an option agreement is part of a tenancy agreement under the RTA, it may mean that:

- a term of an option agreement is invalid if it excludes, restricts or modifies the application of the RTA, or the exercise of a right under the RTA,<sup>92</sup>
- a term of agreement is invalid if it is harsh or unconscionable,<sup>93</sup>
- certain charges payable by the buyer (such as a fee for preparing the contract) may be prohibited under the RTA,<sup>94</sup> and
- a penalty may apply to the vendor and/or buyer for preparing a written tenancy agreement that is not in the standard form.<sup>95</sup>

If the RTA does apply, some of the essential terms of an option agreement, such as the requirement to pay option fees, could be invalid.

The legal status of an option agreement is further complicated by it also being considered a 'sale' under the SLA.<sup>96</sup> This means that general buyer protections under the SLA apply. For example, a vendor must provide the buyer with a 'vendor's statement', disclosing certain details about the property, before the option agreement is signed.<sup>97</sup> A buyer can end the contract if the vendor breaches the agreement or the law.<sup>98</sup> However, this requires the buyer to be proactive and have the resources to sustain legal action. In addition, if a vendor has acted 'honestly and reasonably and ought fairly to be excused for the contravention' and the buyer is 'substantially in as good a position as if all the relevant provisions' had been complied with, the buyer may not be able to end the contract.<sup>99</sup> This

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<sup>92</sup> RTA s 27.

<sup>93</sup> RTA s 28.

<sup>94</sup> RTA s 51.

<sup>95</sup> RTA s 26(2).

<sup>96</sup> Under s 2 of the *Sale of Land Act 1962* (Vic).

<sup>97</sup> SLA s 32.

<sup>98</sup> SLA s 32K.

<sup>99</sup> SLA s 32K(4)

may be the case where a vulnerable vendor has been taken advantage of by a broker.

*McOrmond v Bass Valley Constructions Pty Ltd [2015] VCAT 18*

The buyer and vendor entered into a rent-to-buy arrangement where the buyer paid an upfront option fee, a weekly option fee and a weekly amount to cover market rent and build up 'rent credit'. The option fees and rent credit were to go towards the purchase price. When the buyer exercised his option to purchase, the vendor failed to prepare the contract for sale as required.

The tribunal found that the buyer owed the purchase price and outgoings paid by the vendor after the option date, minus the option fees, rent credits and interest on the rent credits that the buyer had paid. The decision put the buyer in the position he would have been in had the vendor prepared the contract.

The Tribunal Member also noted that the option contract would be regulated under the SLA. The Member observed that the option agreement could arguably be illegal given that it was a 'sale' under the SLA and no vendor's statement (required under s 32 of the SLA) was provided. However, the decision did not turn on this issue.

The dual application of the SLA and potentially the RTA to option agreements presents a significant uncertainty in this area of law. The risks this creates for buyers are exacerbated by rent-to-buy arrangements not being expressly regulated under the NCC.<sup>100</sup>

The unclear legal status of rent-to-buy agreements creates significant financial risks. Typically, a buyer will lose all money they have paid towards a property if the deal fails, for example, because the deal is unaffordable and they fall behind on payments. Even where a buyer complies with a rent-to-buy arrangement, if something goes wrong there is no clear cause of action or avenue to recover the money paid.

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<sup>100</sup> See p 100-101.

One way of addressing this financial risk could be to introduce a legal requirement to hold all buyer payments aside from market rent securely on behalf of the buyer. For example, buyer payments could be held in:

- a solicitor's, estate agent's or conveyancer's trust account, similarly to the deposit in a traditional home purchase, or
- in a statutory account, for example with the Residential Tenancy Bond Authority in Victoria.

The funds could then be required to either be applied to the purchase price if the sale is completed, or be refunded to the buyer if the deal ends. However, the legal structure of rent-to-buy schemes would still be inherently risky.

Lease-options in the residential property market appear to be limited to the high risk model involving vulnerable buyers which are examined in this report. This contrasts with vendor terms contracts, which may have other limited uses in the property market that do not give rise to the same concerns.

In light of the demonstrated consumer harm involved, there is no legitimate place for rent-to-buy arrangements in Victoria's residential property market.

#### Recommendation: Prohibit residential lease-options

Residential rent-to-buy or lease-option agreements are high risk and have no discernible benefit for consumers. They should be prohibited in the residential property market.

#### Other jurisdictions

Residential tenancies legislation across Australia appears to cover at least the residential lease in a rent-to-buy agreement. Provisions of the legislation in each jurisdiction operate to prohibit certain payments, such as bonuses, commissions or similar payments to make, continue or

renew leases. For example, under some legislation a landlord can only require rent and a security bond, and the amount of rent charged in advance is also restricted.<sup>101</sup> Certain payments aside from rent are also specifically banned.<sup>102</sup>

Legislation which permits and prohibits certain payments appears to be limited to payments under a tenancy agreement or for the tenant's right to occupy the property. Because an option agreement gives the right to purchase the property in the future, not the right to occupy it, the legal status of option agreements in other parts of Australia appears to be similar to that in Victoria. That is, if the option agreement is found to form part of the lease agreement, its contents may constitute invalid terms of the lease.

*Milsom Ardle v Hooi Kiang Kho, NSWCTTT, 18 April 2013*

The parties were in a rent-to-buy arrangement under a residential tenancy agreement and option agreement. The buyer fell behind on payments and the vendor moved to evict the buyer.

The NSW Consumer, Trader and Tenancy Tribunal found that, because signing the option agreement was a precondition of signing the tenancy agreement, the two contracts formed one agreement. The requirement to make payments under the option agreement was void, because s 21 of the *Residential Tenancies Act 2010* (NSW) prohibits lease terms that are inconsistent with or prohibited under that Act.<sup>103</sup> The money paid under the option agreement was refundable to the buyer.

Given the similarities between the equivalent provisions in the NSW and Victorian legislation, there is potential for a similar outcome in Victoria.

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<sup>101</sup> See for example *Residential Tenancies Act 1995* (SA) s 54 and *Residential Tenancies and Rooming Accommodation Act 2008* (Qld) s 87.

<sup>102</sup> See for example *Residential Tenancies Act 1997* (Vic) s 51 and *Residential Tenancies and Rooming Accommodation Act 2008* (Qld) s 163.

<sup>103</sup> *Residential Tenancies Act 2010* (NSW) s 21.

In SA, agreements where a buyer has a right or an option to purchase a property and pays rent to occupy the property for six months or more before exercising that option are voidable by the buyer.<sup>104</sup> This has been the case since 2008, following the decision in *Johnstone v Poralka Investments* (see below). Any money paid by a buyer in excess of fair market rent can be recovered by the buyer.<sup>105</sup> Despite this, a number of failed deals have been seen in South Australia (see case studies 8 and 9 in this report).

*Johnstone v Poralka Investments Pty Ltd [2008] SADC 87*

This case applied the *Land and Business (Sale and Conveyancing) Act 1994 (SA)* before the 2008 amendments which made rent-to-buy contracts voidable.

The buyer and vendor entered into a rent-to-buy deal with a two-year lease agreement and an option agreement. For the buyer to purchase the property at the end of the fixed term, the vendor needed to adjust the property boundaries on the title, although this was not in the documents. The vendor refused to realign the boundaries and the purchase could not go ahead. Instead of telling the buyer this, the vendor tried to impose a new deal under which the buyer could buy the whole property or move out.

The court found that the agreements together constituted a vendor terms contract that was void under the SA legislation. The two agreements were linked and could not stand alone or exist without the other, and the option gave the buyer an equitable interest in the land.

The rent and option fees were refundable to the buyer. The buyer was also entitled to relief due to the vendor's misleading and deceptive conduct. The vendor was entitled to compensation for the buyer's use of the land.

There may be limited application of *Johnstone v Poralka* now, due to the 2008 amendments making rent-to-buy arrangements voidable instead of

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<sup>104</sup> *Land and Business (Sale and Conveyancing) Act 1994 (SA)* s 6(2a).

<sup>105</sup> *Land and Business (Sale and Conveyancing) Act 1994 (SA)* s 6(2c).

void. However, it shows the potentially broad scope of the SA prohibition on vendor terms contracts.

The same uncertainties with rent-to-buy in Victoria are seen in other parts of Australia. Expressly prohibiting rent-to-buy arrangements in residential property markets in other jurisdictions would be of significant benefit to consumers.

## **Estate agents regulation**

The *Estate Agents Act 1980* (Vic) and equivalent legislation in other jurisdictions specifies who must hold an estate agent's licence and regulates the conduct of licensed estate agents. In Victoria, a person must hold an estate agent licence to carry on, advertise or notify that they are willing to undertake the business of selling, buying, exchanging, letting, leasing, negotiating terms of sale or collecting rent for any real estate on behalf of another person.<sup>106</sup>

In recent years, regulators have made it clear that brokers of vendor terms and rent-to-buy deals must be licensed estate agents and operate in accordance with state and territory estate agents regimes (see the case studies following). Some segments of the industry have acknowledged this.<sup>107</sup> However, from Consumer Action's review of online advertising, there are signs that brokers may be continuing to promote themselves as 'private investors' or home owners.

### *Ban for Victorian agent assisting unlicensed broker to advertise properties*

In April 2015, Consumer Affairs Victoria entered into an enforceable undertaking with an estate agent who was involved in vendor finance and rent-

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<sup>106</sup> *Estate Agents Act 1980* (Vic) s 4.

<sup>107</sup> See for example Vendor Finance Institute, *Should All Home Buyers Get 'National Credit Code' Protection?*, 5 May 2016, <https://vendorfinanceinstitute.com.au/should-all-home-buyers-get-national-credit-code-protection/>.

to-buy property deals. The agent admitted to breaches of the *Estate Agents Act 1980* (Vic).

The agent admitted to:

- aiding and abetting a company that was an unlicensed estate agent, by allowing property advertisements to be listed on the company's behalf on the realestate.com.au website, and
- refusing or failing to answer an inspector's questions and produce documents.

The agent agreed to surrender his estate agent's licence and not apply for a licence for three years. He also agreed to not work as an agent's representative for 12 months or help anyone that is not a licensed agent to carry on a business as a licensed agent. He paid \$1,000 to the Victorian Property Fund.<sup>108</sup>

The unlicensed broker associated with this agent was found to have engaged in false and misleading conduct (see below).

#### *False and misleading conduct by an unlicensed broker, Victoria*

In October 2015, the Melbourne Magistrates Court found that a broker of vendor terms and rent-to-buy deals had operated as a real estate agent without a licence and engaged in false and misleading conduct, after a CAV investigation. (This broker was associated with the licensed agent above.)

The court found that the broker (through two of his companies) had engaged in estate agent activities without being licensed to do so, by advertising properties for sale online and negotiating the sale of real estate.

The court also found that the broker (through two of his companies) had engaged in false and misleading conduct by:

- falsely representing that he had a licence to sell property, and
- falsely describing the nature of the:
  - 'joint venture agreement' and 'power of attorney' documents to a consumer (a vendor), and
  - terms of sale of a property in an advertisement.

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<sup>108</sup> Consumer Affairs Victoria, *James Allan Monaghan—Enforceable undertaking*, 10 April 2015, <https://www.consumer.vic.gov.au/news-and-events/news-updates/james-allan-monaghan-enforceable-undertaking>.



There was no financial penalty for the broker's false and misleading conduct but he was banned from acting as a real estate agent or dealing with property while unlicensed. He was ordered to submit certain documents relating to his deals to CAV and to pay costs of over \$6,000.<sup>109</sup>

Estate agent licensing ensures that brokers have some minimum level of education and skill, that they must operate within a mainstream regulatory regime and that there are remedies and penalties if their conduct falls outside that regime. All vendor terms and rent-to-buy intermediary brokers should be licensed estate agents, to establish appropriate legal requirements for brokers conduct, however this is not in itself the answer to regulating brokers.

## First Home Owners Grant, taxes and duties

### First Home Owners Grant

In vendor terms sales in most parts of Australia, a buyer's First Home Owners Grant (**FHOG**) can be accessed prior to the buyer legally owning a property. The FHOG is not available in rent-to-buy arrangements unless the buyer exercises their option to purchase at the end of the rent-to-buy period and a contract for sale is entered into.

The FHOG scheme has operated Australia-wide since 2000 and is administered by the states and territories under their own legislation. The grant amounts and eligibility criteria have varied since the introduction of the scheme. In Victoria currently, the FHOG is available for newly built homes below a specified value.

As some of the case studies demonstrate, the FHOG is being paid into arrangements that do not appear to be genuine home purchases. In these cases, the vendor and/or broker benefit, rather than the buyer. It

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<sup>109</sup> Consumer Affairs Victoria, *Benjamin David Chislett—Court action*, 28 October 2015, <https://www.consumer.vic.gov.au/news-and-events/news-updates/benjamin-david-chislett-court-action>.

also appears that vendor terms brokers may have followed FHOG availability. In Consumer Action's 2007 report, the FHOG was involved in all 12 case studies. With the FHOG now only available for new builds, the industry appears to have changed its approach to fit FHOG eligibility.

### *Victoria*

In Victoria, the FHOG can be accessed relatively early in a vendor finance deal.

In Victoria, as well as in NSW, the FHOG is payable on 'completion' of the eligible transaction,<sup>110</sup> which includes when the buyer is entitled to possession in the case of a terms contract<sup>111</sup>. Therefore, the grant may be used as a deposit or in the early stages of the transaction for homes purchased under terms contracts in Victoria and NSW.

Tighter requirements for payment of the FHOG would reflect the purpose of the FHOG scheme. One measure which would reduce the risk of buyers of losing their FHOG, and which may remove the incentive for vendors to structure contracts with this type of upfront payment, is to make the FHOG payable only at or after the final settlement.

### *Other jurisdictions*

In Queensland, Tasmania, the ACT, and the Northern Territory the transaction is 'completed' when both possession *and* registration (or the necessary steps taken to achieve registration) of the buyer on title have occurred.<sup>112</sup> However, the grant may be paid prior to completion of the contract (that is, prior to settlement and registration) subject to conditions being satisfied. In these jurisdictions certain minimum

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<sup>110</sup> *First Home Owners Grant Act 2000* (Vic) s 7(1) and *First Home Owner Grant (New Homes) Act 2000* (NSW) s 7(1)(b)(ii).

<sup>111</sup> *First Home Owners Grant Act 2000* (Vic) s 13(5)(a)(i) and *First Home Owner Grant (New Homes) Act 2000* (NSW) s 13(5)(a)(i).

<sup>112</sup> *First Home Owner Grant Act 2000* (Qld) s 10, Dictionary; *First Home Owner Grant Act 2000* (Tas) ss 7, 13(5)(a); *First Home Owner Grant Act 2000* (ACT) ss 7(1)(b)(ii), 13(4)(a); *First Home Owner Grant Act 2000* (NT) ss 7(1)(b)(ii) and 13(6)(a).

financial contributions must have been made by the buyers for them to be eligible, and in Queensland and Tasmania the buyer must have been in possession for at least one year.<sup>113</sup> Other conditions also apply which generally go to the viability and nature of the transaction as a genuine purchase of a residence.

The Queensland model requires that:

- the contract has been in existence for at least one year,
- the buyer is not in default under the contract so that the vendor has no right to cancel the contract,
- the buyer has occupied the home as their principal place of residence under the contract, and
- the buyer has paid the vendor an amount not less than the FHOG or at least 10% of the purchase price, whichever is the greater. This would include the deposit, interest and other amounts that are deducted from the purchase price.

In Western Australia 'completion' requires possession and registration as owner (for new homes being purchased)<sup>114</sup> or that the building is ready for occupation (for new builds). However, the commissioner may pay the grant early if there is a 'good reason' and the commissioner is otherwise satisfied of certain things. Theoretically, the grant may be paid early and used as a deposit in Western Australia.

In South Australia (where terms contracts are for all intents and purposes prohibited in any event), the FHOG will be paid at or after registration has occurred or the necessary steps have been taken to achieve registration.<sup>115</sup> The grant may be paid prior to completion if there are 'good reasons' and the state will be adequately protected.<sup>116</sup>

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<sup>113</sup> See Office of State Revenue Queensland, *Public Ruling FHOGA019.1.2— Instalment contracts*, 12 September 2012 and State Revenue Office Tasmania, *Public Revenue Ruling PUB-FG-2007-5*, 24 December 2007.

<sup>114</sup> *First Home Owner Grant Act 2000* (WA) ss 8(1)(b)(ii), 14AA(2)(a).

<sup>115</sup> *First Home And Housing Construction Grants Act 2000* (SA) ss 7(1)(b)(ii), 13(5)(a).

<sup>116</sup> *First Home And Housing Construction Grants Act 2000* (SA) s 17.

The applicable criteria, or the relevant legislation, prevent the grant from being available to be used as a deposit in all jurisdictions other than WA. However, this has not prevented ongoing harm. Victoria's FHOG scheme could be significantly enhanced by making the grant available only where the transaction will genuinely result in legal ownership of the home.

#### Recommendation: Restrict access to the First Home Owners Grant

The First Home Owners Grant should only be paid on final settlement of a vendor terms contract, or where the buyer is in a genuine position to own the home. This would better reflect the purpose of the First Home Owners Grant, remove the immediate profit incentive for brokers and ensure that public money is not lost to failed deals.

#### Stamp duty

While a buyer in a vendor terms deal will not have to pay stamp duty until successful completion of the deal, in rent-to-buy deals a buyer may be liable for stamp duty during the deal, irrespective of whether they ever buy the property. This is another unexpected cost that a disadvantaged buyer without a full understanding of the deal may face.

Under the *Duties Act 2000* (Vic) (**Duties Act**), stamp duty is payable by the buyer within 30 days of the property being transferred.<sup>117</sup> In vendor terms deals, this would only happen where a buyer requires a transfer with mortgage-back to the vendor or where the deal is successfully completed.<sup>118</sup>

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<sup>117</sup> Duties Act s 16.

<sup>118</sup> The Victorian State Revenue Office provides guidance on the topic: *Transfer of Land Pursuant to a Terms Contract—Duties Act Bulletin D5/05*, August 2005.

This contrasts with Queensland, where a buyer in a vendor terms deals is liable for stamp duty when the terms contract is entered into.<sup>119</sup> The situation is similar in the ACT and NSW.<sup>120</sup>

The stamp duty implications of rent-to-buy deals are different. Since 2009,<sup>121</sup> stamp duty has been payable on any lease where there is a right or option to purchase the land and for which anything other than 'rent reserved' (amounts 'paid or payable for the right to use the land under the lease')<sup>122</sup> is payable.<sup>123</sup> This does not appear to include option fees.<sup>124</sup> These reforms were purportedly designed to prevent stamp duty avoidance by those entering complex long-term leases. However, there has been concern with the ambiguity of these reforms and they have been described as going beyond closing the loophole.<sup>125</sup>

If rent-to-buy deals are dutiable in Victoria, stamp duty will be payable by the buyer on the full value of the property. This liability arises at the time the lease is granted,<sup>126</sup> and the duty must be paid within 30 days.<sup>127</sup>

### Capital gains tax

A vendor who does not have sufficient knowledge or advice on a transaction may face unexpected capital gains tax (**CGT**) liabilities on a vendor terms deal. This is likely to occur where a broker sets up a deal

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<sup>119</sup> *Duties Act 2001* (Qld) ss 9(1)(b) and 16 and Sch 2.

<sup>120</sup> See *Duties Act 1999* (ACT) s 7(1)(b)(i); *Duties Act 1997* (NSW) s 8(1)(b)(i); *Duties Act 2008* (WA) s 11(1)(b).

<sup>121</sup> Under the *Duties Amendment Act 2009* (Vic).

<sup>122</sup> *Duties Act* s 3(1).

<sup>123</sup> *Duties Act* s 7.

<sup>124</sup> *Duties Act* s 3(1).

<sup>125</sup> Law Institute of Victoria *Duties Act 2000* (Vic)—*Lease Provisions and the Rule of Law—Submission to the Hon Robert Clark MP Attorney General and Minister for Finance, Parliament of Victoria*, 22 December 2011; Parliament of Victoria *Hansard: Second Reading Speech, Duties Amendment Bill 2009*, 26 February 2009. See for example the comments of the Member for Scoresby (Mr Wells). See also Law Institute of Victoria *Duties Amendment Act 2009* (Vic) *Supplementary Submission*, 10 December 2009.

<sup>126</sup> *Duties Act* s 11.

<sup>127</sup> *Duties Act* s 16.

with a vulnerable vendor, and will reduce the profits the vendor expects from the deal. Incurring an unexpected taxation liability of this type may also contribute to any financial stress the vendor might already be experiencing, which could have flow on effects for the buyer if this leads to a mortgagee resorting to their remedies against the property.

Under a vendor terms contract, the vendor will be liable for CGT in the financial year in which the contract is entered into, even though the bulk of the purchase price will not be received for years after that. In a rent-to-buy agreement, a vendor may have to pay CGT on any amount that the buyer pays in excess of rent (such as option fees).

### **Consumer credit laws**

The NCCP Act, which includes the NCC, regulates consumer credit, including home loans. The NCCP Act and the NCC constitute a mature regulatory regime that has developed over many decades of scrutiny and consultation. Under this regime, parties involved in the provision of regulated credit are obliged to, amongst many things, hold a licence administered by ASIC. Before providing credit, a credit provider must comply with responsible lending obligations and ensure that a loan is not unsuitable having regard to the borrowers financial position and requirements and objectives.<sup>128</sup> Credit providers and intermediaries must also be members of an industry external dispute resolution (ombudsman) scheme.

The NCC expressly covers certain sales of land by instalments.<sup>129</sup> The definition of these instalment sales is different to but not inconsistent with the SLA definition of a terms contract.

However, for the NCC to cover a transaction, the relevant credit provider must be in the business of providing credit.<sup>130</sup> A vendor terms vendor, as the credit provider, may not be 'in the business of providing credit', particularly if the vendor is a distressed property owner drawn into the

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<sup>128</sup> NCCP Act Ch 3.

<sup>129</sup> NCC s 10.

<sup>130</sup> NCC s 5.

deal by a broker. A terms contract may therefore be valid under the SLA but not be covered by the NCC. This is a significant and possibly unintended gap in buyer protections.

The NCC will generally not apply to rent-to-buy arrangements. This is because these arrangements do not involve the provision of credit and are not otherwise expressly brought within the ambit of the NCC. The NCC covers leases of goods where the lessee has an option to purchase the goods, but this does not extend to land or buildings.

Credit laws have also shown the risks that arise when a vendor enters into a vendor terms deal because of financial difficulties, without the consent of the lender with a mortgage on the house.

*Financial Ombudsman Service Determination 354321*

The parties entered into a three-year vendor terms contract. Within months of the deal, the vendor had financial difficulties and sought hardship from the lender. The lender gave the vendor a seven month moratorium to allow the vendor to sell the house. However, the vendor wanted three years to enable the vendor terms contract to be finalised. FOS determined that the lender had assisted with the vendor's financial difficulties and it would not change the terms of the mortgage to allow the vendor terms contract to be completed.

### Coverage of vendor terms contracts

Within the last decade, terms contracts where the vendor is 'in the business of providing credit' have been brought under consumer credit codes, initially the *Uniform Consumer Credit Code (UCCC)* and now the NCC. First, in early 2008, the case of *Geeveekay* (below) clarified the position under the UCCC, and afterwards in the same year the UCCC was amended to specifically cover terms contracts (and other similar credit-like arrangements).

The Explanatory Memorandum of the amending legislation noted that the intention was to ensure that consumers of 'terms sale of land contracts'

have protection under the UCCC.<sup>131</sup> In supporting the move to a national consumer credit regulatory framework in the same year, the Productivity Commission stated that 'product/service coverage [should be] comprehensive such that there are no gaps that can be exploited by unscrupulous providers', including vendor financing.<sup>132</sup>

A vendor terms contract will be covered by the NCC where the relevant criteria are satisfied. Section 10 provides that the NCC applies where:

- (a) under the contract, the purchaser:
  - (i) is entitled to enter into possession of the land before becoming entitled to receive a conveyance or transfer of the land; and
  - (ii) is bound to make a payment or payments (other than a deposit or rent payment) to, or in accordance with the instructions of, the vendor without becoming entitled to receive a conveyance or transfer of the land in exchange for the payment or payments; and
- (b) the amount payable to purchase the land under the contract exceeds the cash price of the land.

Section 10(2) specifies that the vendor is the credit provider under the contract. This is significant where the vendor is not in the business of providing credit and therefore may claim to fall outside the coverage of the NCC (see below).

This case illustrates the limited recourse and control a buyer under a terms contract may have in circumstances where they are relying on a vendor to ensure that repairs are completed.

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<sup>131</sup> *Justice Legislation Amendment Bill 2008*, Explanatory Notes, p 3.

<sup>132</sup> Productivity Commission, *Inquiry Report: Review of Australia's Consumer Policy Framework: Volume 2—Chapters and Appendices*, Report No 45, 30 April 2008, p 99, <http://www.pc.gov.au/inquiries/completed/consumer-policy/report/consumer2.pdf>.



*Geeveekay Pty Ltd v Director of Consumer Affairs Victoria (2008) 19 VR 512*

In this appeal from a trial decision, the court found that the vendor terms contract fell under the predecessor to the NCC, the UCCC. The relevant section was read broadly. The UCCC was later amended. The decision of *Lewis v Ormes* [2005] NSWCTTT 481 had similarly found that a terms contract fell within the UCCC and that the vendors were unconscionable under s 70 of the UCCC.

*Financial Ombudsman Service Determination 302744*

This determination concerned a vendor terms deal where the NCC did apply. The property was damaged by a cyclone. The vendor made an insurance claim for the damage but applied part of the proceeds towards the balance due under the contract, not to repairs.

The vendor had discretion as to how to apply an insurance payment under the contract and did not inform the buyer that the insurance would not be applied to the repairs for 12 months. When the buyer discovered this was not the case he paid for the repairs.

FOS found that the buyer had not suffered financial loss but had suffered stress and inconvenience and awarded him \$2,000.

### Business of providing credit

The NCC applies to the provision of credit where the credit contract fits the prescribed criteria.<sup>133</sup> Irrespective of whether a credit provider is required to hold a licence under the NCCP Act, the NCC may still apply. This will be the case if credit is provided 'in the course of a business of providing credit'.<sup>134</sup> This is one of the most significant issues for buyers in vendor terms and rent-to-buy schemes.

*Weerasinghe v Jamaly [2015] VSC 45*

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<sup>133</sup> NCC s 5.

<sup>134</sup> NCC s 5.

The buyers defaulted on a vendor terms contract and the vendor successfully obtained an order for possession of the property to force the buyers to leave. The buyers then applied to set aside the order, arguing that the contract fell within the NCC, and that the vendor had engaged in unlicensed credit activity. The court found that the buyer's argument was 'elaborate and unpersuasive' and held that the NCC:

[D]oes not extend to a private treaty, involving the sale of land by vendors who were not in the business of providing credit, or where the provision of `credit was incidental to some other business.

*Gray v Latter [2014] NSWSC 122*

The vendors were trusted by the buyers, had sold them a house on vendor terms for almost \$100,000 more than its market value, and did not consider the buyers' ability to get a loan to complete the deal.

The buyers did not have recourse under the NCC or ACL because the vendor was not in the business of providing credit.

The issue of whether a vendor is in the business of providing credit has been significant in vendor terms disputes.

Despite the NCC expressly covering terms contracts, where vendor finance deals have failed, brokers and vendors have denied liability under the NCC on the basis that the vendor, as the credit provider, was not in the business of providing credit, and therefore not providing the type of credit regulated under the NCC.

An extension of the NCC to private lending would remove this gap in the NCC's coverage, as well as having broader benefits beyond this issue (for example, new disruptive business models like peer-to-peer lending). It is noted that exposure draft legislation designed to achieve this in 2012 was not passed before the end of the 43rd Parliament.<sup>135</sup>

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<sup>135</sup> *National Consumer Credit Protection Amendment (Credit Reform Phase 2) Bill 2012 (Cth)*.

### Recommendation: Extend the National Credit Code to include private lending

The NCC should be extended to cover private lending, to protect buyers where a deal is not considered to be a transaction in the course of a business of providing credit. This would close a significant gap in the NCC's coverage, as well as having broader benefits (for example, in new disruptive business models like peer-to-peer lending).

### Responsible lending

Chapter 3 of the NCCP Act places 'responsible lending' obligations on licensees that are credit providers<sup>136</sup> or that provide credit assistance in relation to credit contracts.<sup>137</sup> These requirements are 'aimed at better informing consumers and preventing them from being in unsuitable credit contracts'.<sup>138</sup>

The responsible lending obligations are designed to ensure that credit licensees do not suggest, or assist a consumer to apply for or enter into a credit contract that would be 'unsuitable' for the consumer. A contract is unsuitable if it is likely that the consumer would not be able to repay the loan without substantial hardship, or that the contract would not meet the consumer's requirements or objectives.

To make the assessment, the credit licensee must make reasonable inquiries about the consumer's objectives and requirements and financial situation, and take reasonable steps to verify the consumer's financial situation.<sup>139</sup>

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<sup>136</sup> NCCP Act Ch 3 Pt 3-2.

<sup>137</sup> NCCP Act Ch 3 Pt 3-1.

<sup>138</sup> NCCP Act ss 111 and 125.

<sup>139</sup> ASIC *Regulatory Guide 209: Credit licensing: Responsible lending* conduct, Chapters C and D set out how a licensee should determine whether a credit product is 'not unsuitable' for a consumer.

As the case studies in this report show, many brokers have clearly not complied with responsible lending requirements when signing up buyers to deals. There are particular areas where this proves significant for buyers:

- **Short-term contracts which require refinancing**: Consumer Action has seen arrangements which are too short for refinancing to be a feasible option at their conclusion. This is in contrast to the original structure and purpose of terms contracts.
- **Significant increases in instalment payments**: Even where contracts are longer-term, they may involve built-in instalment or interest rate rises which increase financial stress and may aim to push buyers to refinance.
- **Balloon payments**: ASIC's Responsible Lending Guidelines require lenders to specifically consider whether a consumer understands and can make a large 'balloon' payment at the end of a loan.<sup>140</sup> Short term contracts by nature involve balloon payments, which is the point at which buyers may discover they cannot refinance.

### Unjustness

Under the NCC, a court may reopen a contract if it is considered to be unjust.<sup>141</sup> A consumer also has similar recourse for unconscionability and misleading and deceptive conduct under the ACL<sup>142</sup> and ASIC Act.

In September 2016, the NSW Supreme Court found a long-term licence agreement to be unjust under the NCC.

*Evolution Lifestyles Pty Ltd v Clarke (No 3) [2016] NSWSC 1237*

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<sup>140</sup> ASIC *Regulatory Guide 209: Credit licensing: Responsible lending conduct*, para RG 209.127.

<sup>141</sup> NCC s 76.

<sup>142</sup> ACL Ch 2 Pts 2-1 and 2-2.

Under a 30 year licence/vendor finance-type agreement, the buyers paid 'occupation' fees, instalments and interest. After six years, the buyers wanted to sell the property. They stopped making payments and the vendor sought to remove them from the house and claim the unpaid instalments.

The Supreme Court of NSW found that the arrangement was unjust because:

- any default over 30 years would have dire consequences for the buyers,
- the vendor knew of the defendant's limited capacity to meet the obligations under the contract,
- the vendor should have known that the contract was not appropriate for the buyers because the buyers could not obtain finance through a bank and would not authorise credit checks,
- the vendor had placed undue pressure on the buyers to choose a lawyer selected by the vendor, meaning the buyers did not have independent legal advice,
- one buyer did not have any real understanding of the deal and said that she felt rushed into signing the contract, and
- the vendor told the buyers that the contract was 'basically a mortgage' when it did not give the buyers any legal or equitable interest in the property until the last payment.

The Court set aside the agreement. The vendor was ordered to repay all of the buyer's payments including the occupation fees, instalment payments, improvements to the property, fees and charges, minus rent that the vendor would have received. The buyer's deposit was returned under s 55(2A) of the *Conveyancing Act 1919* (NSW) and the buyer was required to move out within 30 days. The Court also found that the vendor had not complied with the notice requirements under s 88 of the NCC.<sup>143</sup>

#### *Credit Ombudsman Service Limited decision 5 February 2013*

A buyer entered a vendor terms contract and fell behind with payments. She was given a notice to vacate and made a complaint to the ombudsman, claiming that the reason she could not make payments was that she had a mental health issue, which she had prior to entering into the deal.

The ombudsman determined that there was no unjustness under the NCC as the financial services provider had complied with its own responsible lending

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<sup>143</sup> The facts of this case are detailed in case study 5, p 54.

requirements. It was found that the buyer's mental health issue did not prevent her from understanding the agreement. The issues that caused the buyer to default were not reasonably foreseeable when the deal was made.

This decision also considered unconscionable conduct under the ASIC Act (see below) and found the relevant conduct to not be unconscionable.

## Consumer and financial services laws

Broker and vendor conduct may be regulated under the ACL<sup>144</sup> and ASIC Act,<sup>145</sup> which protect consumers from, among other things, unconscionable conduct and misleading and deceptive conduct.

These laws are particularly relevant in a broker's sales tactics and pre-contractual representations to buyers. They also cover a promoter's dealings with hopeful property investors/brokers. In addition to the general requirements discussed below, brokers may be specifically liable for false or misleading representations in relation to land, including the nature of the interest in the land and the price payable.<sup>146</sup>

Regulators across Australia took part in a co-ordinated action on property spruiking in 2014-15. This resulted in legal action against 10 traders and legally-enforceable undertakings with a further seven.<sup>147</sup>

### Misleading and deceptive conduct

Section 18 of the ACL provides that a person must not engage in misleading or deceptive conduct. There has been regulatory action for

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<sup>144</sup> *Competition and Consumer Act 2010* (Cth) Sch 2. The ACL applies in Victoria by force of the *Australian Consumer Law and Fair Trading Act 2012* (Vic).

<sup>145</sup> Sections 12CA to 12CC of the ASIC Act substantially mirror ss 20 to 22 of the ACL in relation to unconscionable conduct.

<sup>146</sup> ACL s 30.

<sup>147</sup> NSW Fair Trading, *Media release: Property Spruikers Put On Notice by Regulators*, 30 July 2015, <https://www.finance.nsw.gov.au/about-us/media-releases/property-spruikers-put-notice-regulators>.

misleading and deceptive conduct under the ACL in relation to both buyers and people who have gone through training in vendor finance and rent-to-buy strategies.

*ACCC Federal Court action for misleading and deceptive conduct*

At the time of this report, the Federal Court of Australia had heard a claim by the Australian Competition and Consumer Commission (**ACCC**) against Rick Otton, the lead promoter of vendor terms and rent-to-buy strategies, and his *We Buy Houses* business for alleged breaches of the ACL.<sup>148</sup>

The ACCC took the action over alleged representations by Otton and *We Buy Houses* in published materials and at events, including that people who used certain property techniques could buy a house for \$1 or build property portfolios without their own money and without new bank loans.

The ACCC alleged that the strategies did not enable brokers to buy a house for \$1, but rather involved them acting as middlemen to facilitate property transactions between third-party vendors and third-party buyers.

At the time the action commenced, ACCC Chairman Rod Sims said that the ACCC was:

[C]oncerned that the strategies ... target vulnerable consumers who don't qualify for bank loans or who are having difficulties meeting their mortgage repayments.<sup>149</sup>

The ACCC action also involved ASIC (as some matters could fall within its financial consumer protection jurisdiction), NSW Fair Trading and Consumer Protection WA.

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<sup>148</sup> For the status of this matter, see

<https://www.comcourts.gov.au/file/Federal/P/NSD170/2015/actions>.

<sup>149</sup> ACCC, *Media release: Coordinated investigation results in ACCC taking action against We Buy Houses and Rick Otton regarding property strategies*, 3 March 2015, <https://www.accc.gov.au/media-release/coordinated-investigation-results-in-accc-taking-action-against-we-buy-houses-and-rick-otton-regarding-property-strategies>.

The ACCC is seeking declarations, pecuniary penalties, permanent injunctions, corrective advertising, costs and a disqualification order.<sup>150</sup>

The Court's judgment is reserved and no wrongdoing has been found on the part of Otton at the time of this report.

#### *Lead promoter's enforceable undertaking in WA*

In September 2013, Rick Otton entered into an enforceable undertaking not to conduct seminars, distribute promotional material or promote his real estate business in WA for two years. The action was in relation to rent-to-buy schemes that he promoted.

Otton undertook to make it clear to prospective buyers that:

- the purchase price for a property must be paid before they own it,
- the one dollar payment for the option to buy is only the initial step towards owning the property,
- they may not necessarily satisfy a bank's lending requirements to exercise the option to buy, as payment of instalments may not prove their creditworthiness, and
- legal advice should be obtained before being involved in a rent-to-buy property scheme.

The WA Commissioner for Consumer Protection said at the time that WA consumers were being misled in the marketing of this scheme, with statements such as 'buy a house for one dollar' and 'profit without initial investment'. The Commissioner was also concerned that:

These types of seminars highlight to potential investors the benefits of securing their financial future by investing in property, while downgrading the risks. They also appear to exaggerate the potential gains from property and other investments by following the promoter's programs.

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<sup>150</sup> ACCC, note 149.



Additional information that Otton agreed to provide overcame concerns raised by the Commissioner.<sup>151</sup>

*Unlicensed brokers banned and fined for misleading and deceptive conduct, WA*

In February 2014, Patricia and Bryan Susilo, two young siblings brokering rent-to-buy deals in WA between 2010 and 2013 admitted to misleading and deceptive conduct. The sister also admitted to operating as a real estate agent without a licence.

The Supreme Court of WA found that the duo made false, deceptive or misleading statements. These included:

- 'Own my home', which gave prospective buyers the wrong impression that they would get either sole or joint ownership of a home after signing the contract, and misrepresented to buyers that they were the owners of the properties,
- 'No banks needed' and 'Stuff the banks—move in today', which suggested buyers could buy a home without a bank loan, when the brokers had no reasonable grounds to make these statements,
- 'We buy houses', which suggested that the brokers could buy properties immediately, which they could not,
- 'We do not charge commission or fees', which was misleading because the brokers derived revenue from the arrangement,
- 'We are part of a group of real estate investors', which was false, and
- information on the weekly cost to prospective buyers, which did not accurately reflect the true total cost of eventually owning the property.

The court made a three-year injunction banning the duo from engaging in rent to buy real estate transactions without a licence, or without working for a licensee.

The court also ordered the brother and sister:

- not to represent that they buy houses, unless they intend to acquire the freehold title,

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<sup>151</sup> Consumer Protection WA, *WA ban for property investment promoter (We Buy Houses Pty Ltd / Rick Otton)*, 10 September 2013, <https://www.commerce.wa.gov.au/announcements/wa-ban-property-investment-promoter-we-buy-houses-pty-ltd-rick-otton>. No wrongdoing by Otton was found by the regulator.

- not to represent that they are the owners of properties they are selling unless they are in fact the owners,
- not to represent to potential buyers that they can purchase a house without a bank loan unless there are reasonable grounds for that representation,
- provide an accurate and complete statement of money payable by prospective buyers in a proposed arrangement,
- disclose that a rent-to-buy arrangement is not an immediate sale of property, and
- disclose what revenue they would derive from an arrangement.

The court ordered the brokers to pay \$17,500 and \$12,000 respectively and total costs of \$8,000. The Commissioner for Consumer Protection said at the time:

It would appear from our investigations into these rent to buy property schemes that the prospective buyers are at great risk of losing their money and sellers are locked into a fixed sale price for the duration of the contract...

The schemes target people who are desperate and find it difficult to get finance to purchase a home as well as vendors who are having difficulty selling their homes.<sup>152</sup>

#### *Enforceable undertaking and fines for promoter, Queensland*

In April 2015, a Queensland-based promoter agreed in an enforceable undertaking with the Queensland Office of Fair Trading not to engage in conduct liable to mislead consumers, and to make a \$15,000 payment. Her promotions company also entered into an enforceable undertaking with the regulator and made a \$20,000 payment.<sup>153</sup>

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<sup>152</sup> Consumer Protection WA, *Penalty and injunctions for rent to buy property promoters (Patricia and Bryan Susilo)*, <https://www.commerce.wa.gov.au/announcements/penalty-and-injunctions-rent-buy-property-promoters-patricia-and-bryan-susilo>.

<sup>153</sup> 'Fair Trading crackdown in Queensland', *The Real Estate Conversation*, 31 July 2015, <http://www.therealestateconversation.com.au/news/2015/07/31/fair-trading-crackdown-queensland/1438347600>.

The regulator at the time said that consumers had been promised financial benefits that promoters could not deliver, misled about their cooling-off period rights and pressured into buying at 'free' seminars.

### Unconscionable conduct

The ACL and ASIC Act prohibit unconscionable conduct.<sup>154</sup> This protects consumers against conduct that is particularly harsh or oppressive, and more than simply unfair, unjust, wrong or unreasonable. The conduct must be against conscience and demonstrate 'moral obloquy'.

The courts, regulators and ombudsman have considered unconscionable conduct in a number of disputes involving vendor finance or rent-to-buy deals. In particular, in 2013 the Victorian Supreme Court examined a vendor finance broker's conduct and interpreted unconscionability under the former *Fair Trading Act 1999* (Vic)<sup>155</sup> narrowly.

#### *Director of Consumer Affairs Victoria v Scully [2013] VSCA 292*

The broker was employed by a company that promoted and managed complex vendor finance and rent-to-buy schemes. He knew that the buyer could not afford a particular deal and manipulated information in a 'budget planner' spreadsheet to make it appear that the buyer could afford it.

The trial judge held that the broker had 'made a conscious decision' not to explain the arrangements underpinning the scheme to the buyers, and that those arrangements benefited the company but posed significant risks to buyers. His conduct was immoral and deserving of the 'opprobrium of a finding of unconscionability', but his employer company was not found to have authorised the broker's conduct.

The personal conduct of one director and one employee who were directly involved in brokering deals was unconscionable but there was no unconscionability on the part of another director of the company who did not authorise the employee's conduct. In effect, the company was not found to

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<sup>154</sup> ACL ss 20 and 21 and ASIC Act ss 12CA to 12CC.

<sup>155</sup> The equivalent to s 21 of the ACL.

have engaged in unconscionable conduct, leaving the regulator and people caught in the schemes with limited recourse.

An appeal against the decision on the company confirmed that the relevant conduct must include a significant element of moral obloquy. It is not enough that the conduct is objectively unfair, unjust, wrong or unreasonable—there must be some 'moral taint'.

#### *ASIC enforceable undertaking to compensate buyers*

In April 2011, ASIC entered into an enforceable undertaking with a regional NSW-based property developer and his company after an investigation into alleged unconscionable conduct in his lending practices. The developer was the sole director of the company, which had operated a residential property development business since 1997.

From 2004 until late 2009, the company offered vendor finance to people who purchased property from it and associated entities. The developer made verbal inquiries about the prospective buyers' income, assets, and liabilities but did not take steps to independently verify the information about their financial situations. Many of the buyers were from non-English speaking backgrounds.

ASIC's investigation found concerns with his conduct including:

- whether adequate inquiries were made as to a borrower's or any guarantor's financial situation,
- reliance on a borrower's assertions as to their financial situation and failure to test or independently verify the borrowers' assertions,
- whether borrowers sufficiently understood the terms and conditions of the vendor finance loan, considering the developer knew or ought to have known that some borrowers had a poor understanding of English and/or little financial acuity,
- the offer of vendor finance to some borrowers who were receiving Centrelink benefits, and
- the offer of vendor finance on promotional terms, including capped repayments, contributions to the borrower's first mortgage loan and lump sum cash rebates.

The developer agreed to write to clients and provide them with an opportunity to seek compensation if they believed they were victims of unconscionable conduct. He was also required to appoint an independent person—to be approved by ASIC—to consider any compensation claims that UPG has rejected.

ASIC accepted the enforceable undertaking as an alternative to commencing court proceedings.<sup>156</sup>

*Credit Ombudsman Service Limited decision, 5 February 2013*

The buyer entered a vendor terms contract and fell behind with payments. She was given a notice to vacate and made a complaint to the ombudsman, claiming that the reason she could not make payments was that she had a mental health condition, which she had prior to entering into the deal. The ombudsman, looking at unconscionable conduct under the ASIC Act (as at 2005), found that the elements of unconscionable conduct were not made out, and that there was no 'moral obloquy' on the part of the financial services provider. This decision also considered unjustness under the NCC (see above).

## Unfair trading

Because there is no specific legal prohibition on 'unfair' trading or conduct, aggressive sales and marketing practices short of coercion, which tends to target disadvantaged or vulnerable consumers, fall outside the ACL and ASIC Act. In *Scully* (above), the requirement of 'moral obloquy' meant that only an individual broker and not the employer company was held liable for the broker's conduct.

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<sup>156</sup> ASIC, *Media release: 11-81MR Property developer enters into enforceable undertaking providing compensation for vendor finance borrowers*, 14 April 2011, <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2011-releases/11-81mr-property-developer-enters-into-enforceable-undertaking-providing-compensation-for-vendor-finance-borrowers/>.

There has been consideration in recent years, including by the Productivity Commission<sup>157</sup> and consumer affairs ministers, of a general prohibition on unfair conduct in Australia, similar to the European Union's 2005 Unfair Commercial Practices Directive.

As *Scully* shows, broader prohibition on unfair trading would enable regulators to more proactively impede unfair business models. Reform along these lines could improve the ability of regulators to identify and address particular unfair practices, including those seen in vendor terms and rent-to-buy deals, and better reflect community expectations. Consumer Action continues to advocate for this reform to effect broader-reaching change to benefit consumers.<sup>158</sup>

#### Recommendation: Prohibit unfair trading

The prohibition on unconscionable conduct under the ACL and ASIC Act requires a very high threshold of wrongdoing, and is not well adapted to deal with unfair business models, such as problematic vendor finance and rent-to-buy schemes. A broader prohibition on unfair trading would enable regulators to more proactively impede unfair business models.

#### Dispute resolution

External dispute resolution (**EDR**) or industry ombudsman schemes are established under the *Corporations Act 2001* (Cth) (**Corporations Act**) and

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<sup>157</sup> Productivity Commission, *Inquiry Report No. 45: Review of Australia's Consumer Policy Framework, Volume 2—Chapters and Appendixes*, chapter 7, 30 April 2008, <http://www.pc.gov.au/inquiries/completed/consumer-policy/report/consumer2.pdf>.

<sup>158</sup> See Consumer Action Law Centre, *Discussion Paper: Unfair trading and Australia's consumer protection laws*, July 2015, <http://consumeraction.org.au/wp-content/uploads/2015/07/Unfair-Trading-Consumer-Action-2015-Online.pdf>.

membership is mandatory for certain financial services providers under the Corporations Act and NCCP Act.<sup>159</sup> EDR can provide more accessible and less expensive dispute resolution than courts or tribunals do.

However, many vendor finance disputes cannot be heard by EDR schemes because the vendor does not fall within the NCC.<sup>160</sup> Consumer Action is aware of multiple cases where EDR schemes have found that vendor finance disputes were not within their remit.

The legal reforms to credit and consumer laws recommended in this report would go some way to enabling resolution of vendor finance disputes through EDR schemes.

### Property investment advice

The regime for regulation of financial advice under the Corporations Act and ASIC Act does not regulate property investment advice in the same way that advice on financial products such as securities, superannuation or credit facilities is regulated.<sup>161</sup> Because of this, spruikers or brokers of vendor terms or rent-to-buy deals are not required to hold a financial services licence and are generally not liable for the advice they provide in the way that a financial adviser is liable.

This gap in the regulatory regime has been acknowledged numerous times. In 1999, ASIC reported that although there were differences between property and securities as products, the financial considerations for both were similar and they were interchangeable as investment alternatives.<sup>162</sup> In 2005, a Parliamentary Joint Committee on Corporations and Financial Services report recommended that property investment advice be regulated with the same licensing and conduct requirements as

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<sup>159</sup> Corporations Act Ch 7 and NCCP Act Ch 2.

<sup>160</sup> See further pp 103-105.

<sup>161</sup> Property is not a financial product under s 12BAA of the ASIC Act.

<sup>162</sup> ASIC, *Report 05: Review of the financial advising activities of real estate agents—interim report*, July 1999, <http://download.asic.gov.au/media/1340000/irfin.pdf>.

financial advice.<sup>163</sup> A Victorian Parliamentary Inquiry in 2008 also recommended that property investment advice be regulated at the federal level and that consumers be warned about property marketeers.<sup>164</sup> While the 2014 Murray Financial System Inquiry did not recommend changing the scope of financial advice,<sup>165</sup> the Senate Economics References Committee's Scrutiny of Financial Advice Inquiry reported on land banking in early 2016 and recommended inclusion of a definition of 'property investment advice' in the relevant federal legislation.<sup>166</sup>

Property spruikers who promote vendor finance and rent-to-buy schemes to hopeful property investors as an investment technique should be subject to the same laws and licensing regime as those who provide financial advice. Brokers who provide property investment advice by promoting these deals to vendors or buyers should also be subject to the same laws.

There is currently regulation of residential property 'marketeers' under the *Residential Occupations Act 2014* (Qld), which may be effective in regulating any person promoting property for sale or providing a service in that state. However, with financial advice federally regulated, and consumer detriment through vendor terms, rent-to-buy and other

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<sup>163</sup> Parliamentary Joint Committee on Corporations and Financial Services, *Property Investment Advice—Safe as Houses?*, June 2005, [http://www.aph.gov.au/Parliamentary\\_Business/Committees/Joint/Corporations\\_and\\_Financial\\_Services/Completed\\_inquiries/2004-07/investment/report/index](http://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/Completed_inquiries/2004-07/investment/report/index).

<sup>164</sup> Parliament of Victoria Law Reform Committee, *Final Report: Inquiry into Property Investment Advisers and Marketeers*, April 2008, [http://www.parliament.vic.gov.au/images/stories/committees/lawreform/property\\_investment/final\\_report.pdf](http://www.parliament.vic.gov.au/images/stories/committees/lawreform/property_investment/final_report.pdf).

<sup>165</sup> *Financial System Inquiry: Final Report*, November 2014, [http://fsi.gov.au/files/2014/12/FSI\\_Final\\_Report\\_Consolidated20141210.pdf](http://fsi.gov.au/files/2014/12/FSI_Final_Report_Consolidated20141210.pdf).

<sup>166</sup> Senate Economics References Committee, *Scrutiny of Financial Advice Part I—Land banking: a ticking time bomb*, February 2016, [http://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Economics/Scrutiny\\_of\\_Financial\\_Advice/Report](http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Scrutiny_of_Financial_Advice/Report).



property schemes such as land banking persisting across Australia, a national approach is the obvious preferred option for reform in this area.

Recommendation: Federally regulate property investment advice as financial advice

Property spruikers who promote vendor finance and rent-to-buy schemes to hopeful property investors should be subject to the same requirements as financial advisers under the Corporations Act and ASIC Act. Brokers who provide property investment advice by promoting these deals should also be subject to the same laws.



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