



6 April 2016

By email: yoursay@fairersaferhousing.vic.gov.au

Residential Tenancies Act Review
Consumer Affairs Victoria
GPO Box 123
MELBOURNE VIC 3001

Dear Sir/Madam

Residential Tenancies Act review: Issues Paper 2 – Rent, bonds and other charges

Consumer Action Law Centre (**Consumer Action**) is pleased to comment on *Issues Paper 2—Rent, bonds and other charges* as part of Consumer Affairs Victoria's (**CAV**) review of Victoria's Residential Tenancies Act.

This submission is focused on rent-to-buy schemes in the residential property market, building on our previous submission to this review's *Consultation Paper—Laying the Groundwork*. Consumer Action is also providing comment on rent-to-buy and vendor terms issues to CAV's current review of consumer property laws. There are typically similar risks for buyers and vendors in both of these types of schemes.

Our comments are detailed more fully below.

About Consumer Action

Consumer Action Law Centre is an independent, not-for profit consumer organisation based in Melbourne. We work to advance fairness in consumer markets, particularly for disadvantaged and vulnerable consumers, through financial counselling, legal advice and representation, and policy work and campaigns. Delivering assistance services to Victorian consumers, we have a national reach through our deep expertise in consumer law and policy and direct knowledge of the consumer experience of modern markets.

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Financial risks in rent-to-buy schemes

In rent-to-buy schemes, a tenant (hopeful buyer) pays market rent and an option fee or above-market rent for a property for a specified period of time, with the hope of then qualifying for a bank loan and purchasing the property. Often, but not always, part of the option fee will be credited towards the purchase price of the property.

Our [submission](#) to this review's *Consultation Paper—Laying the Groundwork* (dated 27 July 2015) identified the high risks of rent-to-buy schemes, including that:

- homes are typically sold at hugely inflated prices,
- buyers are required to make weekly payments that are unaffordable for them,
- a buyer's name is not on the property title unless they complete the purchase and the title is transferred,
- it is typically third-party brokers or intermediaries who stand to profit from these deals, and
- the legal nature of the deal is not always understood by buyers entering these deals.

The following case study shows the heavy financial loss and stress suffered by one family who entered into a rent-to-buy agreement in metropolitan Melbourne.

Case study: Will, Mira and Abdi

Will and Mira had 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.

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. The company would arrange finance for Abdi and Will to buy the house, which would be easy with their combined incomes.

The purchase price was \$429,000. Will would need to pay a \$8,000 deposit and sign over his First Home Buyers Grant of \$20,000. He would then make weekly payments of \$670 for three years, totaling 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 \$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.

There was no assessment of Will's suitability to make the rental payments, or to obtain a loan at the end of the three years.

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.

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 that Will would pay \$350 per week.

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 \$8,000 deposit and their First Home Owners Grant. These amounts total over \$80,000.

Option fees

As outlined in our first [submission](#) to CAV's consumer property laws review on 11 March 2016, tenants in rent-to-buy schemes often pay large amounts in option fees to secure the chance to purchase a property in the future.

In lease option deals, typically a tenant (a hopeful buyer) signs:

- a residential tenancy agreement for a set period (for example, three to five years), and
- a separate but related 'option agreement' specifying the terms on which the tenant can buy the property and the 'option fee' payable in order to purchase the property at a specified time. An option fee may consist of ongoing payments as well as a lump sum.

A contract for the sale of land may also be drawn up, although not signed.

Consumer Action has a particular concern with how option fees are treated by third party brokers or vendors in rent-to-buy deals.

Firstly, Consumer Action has seen one failed deal where a tenant paid above market rent and an option fee approximating the rent—in total, this was more than double the market rent. Only a small portion of the option fee (less than 12%) was to be credited towards the agreed purchase price.

Buyers in these deals pay exorbitant amounts purely in the hope of purchasing a property at an inflated price. Not only are some of these deals set up to fail because they are not affordable for the tenant, under option agreements typically none of the option fee is refundable to the tenant if the purchase does not go ahead.

In Consumer Action's view, terms of option agreements which provide for a large option fee that is not fully credited to the purchase price may constitute an unfair term in breach of the

Australian Consumer Law. In our view, while the fee itself might amount to an upfront fee or main subject matter of the contract, a contractual provision that states such a fee is not refundable or credited to the purchase price is not necessary to protect the legitimate interests of the trader.

Secondly, unlike bonds held by the Residential Tenancies Bond Authority, option fees are typically not held securely on behalf of the tenant. This is a critical risk for tenants. While courts and tribunals have treated option fees as rent in advance in some cases, even if a tenant did get a judgment against a broker awarding them an amount, the money may never be recoverable (for example, if the money is no longer sitting with the broker or the broker has gone bankrupt).

It is Consumer Action's view that, as long as rent-to-buy schemes continue in Victoria, anything paid by a buyer aside from market rent, including but not limited to option fees, should be held on trust for the buyer and fully refundable if the buyer does not purchase the property (any bond paid by the tenant would be held by the Residential Tenancies Bond Authority).

Thirdly, there is a real question as to whether options contracts and fees should have a role in the residential market at all. While options contracts have for many centuries been a useful mechanism for sophisticated parties to speculate on changes in market prices, or hedge against changes in market prices, it is difficult to see a rationale for their use in the sale of residential property to people who are excluded from mainstream financial markets. Consumer Action's experience has been that options contracts, when combined with rental contracts in the residential market, are used to circumvent the application of the *National Consumer Credit Protection Act 2009* (Cth) and to exploit the desire of marginalised consumers to buy a home.

Please contact Susan Quinn on 03 9670 5088 or at susan@consumeraction.org.au if you have any questions about this submission.

Yours sincerely,

CONSUMER ACTION LAW CENTRE



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