

Sale and rent back

An OFT market study

October 2008

OFT1018

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1 EXECUTIVE SUMMARY

Background

- 1.1 Sale and rent back is a relatively new type of property transaction whereby firms buy homes from individuals, usually at a discount, and then allow those individuals to stay on in the property as tenants. These deals are often sold to people in financial difficulty and potentially facing repossession. Sale and rent back firms often tell consumers that they will be able to stay in their home for years, but in reality the tenancy is rarely guaranteed for more than six or twelve months.
- 1.2 There is little reliable data available on the size of the industry. The sector appears to be highly fragmented, and mainly served by small firms, including non-professional landlords. It is likely that there are upwards of 1,000 firms, together with an unknown number of non-professional landlords, who have conducted about 50,000 transactions to date.
- 1.3 In the current economic climate, the number of people experiencing mortgage difficulties, and possibly repossession, is rising. This is likely to increase demand for sale and rent back. At the same time, however, tighter lending criteria for buy-to-let mortgages - the main source of finance for sale and rent back firms - is making it more costly for sale and rent back firms to operate. Anecdotal evidence suggests that, as of autumn 2008, the sector is still active, although transaction volumes may have fallen with the reduced availability of buy-to-let mortgages. Higher costs are driving up the discounts at which homes are purchased.
- 1.4 In May 2008, the Office of Fair Trading (OFT) launched this market study in response to widespread concerns raised by Citizens' Advice, Shelter, and the Council of Mortgage Lenders, among others. The main concerns were: first, that homeowners in vulnerable positions were entering into sale and rent back arrangements, erroneously believing that they had secure tenure for the medium to long term; and second, that the worsening economic climate meant there was the potential for the

scale of detriment in this sector to grow very quickly. For this reason the OFT has carried out this short market study on a very tight timescale.

Key findings

- 1.5 A sale and rent back transaction involves the consumer forgoing a significant amount of equity in their property in exchange for the benefit of staying in their own home as a tenant.
- 1.6 Our concerns are twofold. First, we believe that some consumers are entering into sale and rent back transactions when this is not necessarily the best option for them. We have seen examples of sale and rent back tenants being evicted because they cannot afford the rent agreed – staying in the property may not always be a sustainable solution. This problem is exacerbated by the uncertainty many face as to whether they will be eligible for housing benefit following the sale of their home.
- 1.7 Second, the lack of security of tenure means that there is substantial risk involved in the transaction. It is impossible to say how often this risk materialises but we have seen examples of tenants losing their homes, for example because their landlord imposed significant rent increases, after only a short tenancy period. We have also seen examples of tenants losing their homes because the landlord has defaulted on the mortgage and the property has been repossessed by the lender.
- 1.8 Early eviction entails significant financial and psychological detriment to individuals. The consumer may often have been better off proceeding with other alternatives, which would have been less risky or more affordable. These alternatives include negotiation with their current mortgage provider, selling on the open market or – for older homeowners – using a regulated equity release product.
- 1.9 Sale and rent back deals and the alternatives available are complex to evaluate, particularly for consumers already in stressful and difficult financial and emotional situations. Our research indicates that most consumers are not in a position to make a balanced assessment at the point of sale taking into account the real market value of their home, the

price offered, and the cost of renting – in addition to the risks of the firm defaulting on the mortgage, increasing the rent in the future or starting eviction proceedings at the end of the agreed term of the tenancy. We do not believe that many consumers will be aware of, or able to assess, the full costs and risks they face in sale and rent back transactions.

- 1.10 Furthermore, our research indicates that many consumers do not feel able to talk openly to others about their problems and do not shop around. Often, the only discussion about the deal is with the sale and rent back firm, which is motivated to persuade the consumer to accept the transaction. It seems that some consumers place considerable weight on informal assurances that they will not be evicted or face increases in rent.
- 1.11 For some consumers, however, a sale and rent back transaction may be the best way forward – our research suggests that some individuals find the ability to sell and rent back their own home extremely valuable. However, even though some consumers are happy with the arrangement, they currently bear almost all of the risk in the transaction. We are concerned that they may not be fully aware of these risks, and may not be prepared to accept the consequences if the downside risk materialises.

Recommendations

- 1.12 The industry is making efforts to improve standards by developing codes of practice and establishing self-regulatory membership groups. The OFT welcomes these efforts. However, given the high degree of fragmentation in the sector, the vulnerability of consumers and the secrecy of the transactions - and the consequent lack of shopping around - we do not believe that self-regulation can adequately address all the concerns we have identified.
- 1.13 We recommend that sale and rent back transactions be subject to statutory regulation, and that this be carried out by the Financial Services Authority (FSA). We believe that this can be achieved relatively quickly through an amendment to the Regulated Activities Order for the

Financial Services and Markets Act 2000. The FSA already regulates equity release schemes, which have a number of similarities with sale and rent back products.

- 1.14 If the Government accepts the recommendation to regulate, further work will be needed to develop and consult on specific regulatory proposals. Without wishing to presuppose the outcome of that work, we envisage that these might include the following.
- 1.15 We believe that regulated standards of disclosure should be introduced, particularly around the initial valuation and sale price, the term of the tenancy and the rent payable.
- 1.16 Sale and rent back firms should also be obliged to tell consumers about, and allow time for consumers to take advantage of, the existing sources of free, independent advice.
- 1.17 We believe that the tenure of the product should match any assurances given by the sale and rent back firms: firms should be required to provide a tenancy agreement in which the tenant cannot be evicted without cause for a specified period of time, and that period should match any assurances given.
- 1.18 We recognise, however, that it is very difficult to ensure that this type of requirement is actually followed. There is a danger that sale and rent back providers would continue to offer short term tenancies with paperwork to match, but would continue to provide verbal assurances of greater security. For this reason, we believe that it may be appropriate to introduce minimum standards for the sale and rent back product. For example, where the property is sold at a substantial discount to the market value, there could be a requirement for a minimum length of tenure.
- 1.19 Imposing regulation will not be quick. Given the urgency of the problem we recommend a number of more immediate measures, which will be particularly important while the industry remains unregulated.

- 1.20 Self-regulation should be encouraged as it has the potential to raise standards in the industry. It could also play an important role in preparing the sector for regulation.
- 1.21 We recommend that the Government take action – through other ongoing initiatives targeted at homeowners in difficulty – to raise consumer awareness of the risks around sale and rent back and to encourage consumers to seek independent, face to face financial advice.
- 1.22 We also recommend that there be greater clarity around eligibility for housing benefits for sale and rent back tenants.
- 1.23 Finally, in the course of this study, we received some indications that sale and rent back firms may be breaching the Consumer Protection from Unfair Trading Regulations 2008 (CPRs). We will liaise closely with enforcement partners, notably local authority Trading Standards Services, with a view to taking action against sale and rent back firms who may be breaching these regulations to the detriment of consumers. We will also work with these agencies to raise awareness of the issues we have identified in the sale and rent back sector.

Thank you

- 1.24 As part of this study, we have consulted consumer groups, industry professionals, trade associations, advisory centres, Government departments and the devolved administrations, and the FSA. We have heard from a number of sale and rent back firms, as well as many individuals who have been through, or considered, sale and rent back. We are grateful for their contributions and willingness to assist the OFT's team in its work.

2 INTRODUCTION

Background to the report

- 2.1 On 14 May 2008, the OFT launched a market study looking at the sale and rent back sector.¹ This followed previous work by a cross-departmental group,² which led to the Chancellor's announcement in the March 2008 Budget that the OFT would lead a study of the sale and rent back sector, focusing on consumers' experiences.³
- 2.2 Stakeholders, including mortgage industry representatives, consumer groups, Peers and MPs expressed concerns that some consumers entering into sale and rent back arrangements are making misinformed choices or are being exploited. The concerns, which were put to us and are explored in depth in this report, include the following:
- Sellers proceed with the transaction mistaken about the security of tenure they will have in the rented home.
 - Sale and rent back firms may evict tenants after only a very short rental period or may demand large, unexpected, increases in rent.
 - The tenant may have to leave the property if the sale and rent back firm defaults on its mortgage and the lender repossesses.
 - The customer may be told that the value of the house is lower than it in fact is.

¹ Market studies are carried out under section 5 of the Enterprise Act 2002. This gives the OFT a broad power to acquire information about matters relating to the carrying out of any of its functions.

² This involved HM Treasury, the Department for Business, Enterprise and Regulatory Reform, the Department for Communities and Local Government, the Ministry of Justice, the Financial Services Authority and the Office of Fair Trading.

³ Budget 2008, para 5.32, available at www.hm-treasury.gov.uk/media/A/3/bud08_chapter5.pdf

- The tenant may not fully understand the financial implications of the transaction, for example in relation to eligibility for housing benefit, or bankruptcy.
- People in stressful situations may be persuaded to go through with sale and rent back even when there are other options which may be financially more sustainable for them.

Evidence and research

- 2.3 We commissioned an independent research company to examine consumers' experience of sale and rent back transactions. This report is at Annexe A. The researchers conducted 47 interviews with consumers recruited from a number of sources, including sale and rent back firms and people who had spoken to Citizens' Advice and National Debtline about sale and rent back. Due to the small size of the industry, and the private nature of the transaction, it was impossible to identify enough consumers using random techniques. So the experiences of the people interviewed for this research are not necessarily representative of sector as a whole. The main research findings are, therefore, qualitative in nature, providing an insight into individuals' experience of the product.
- 2.4 The interviews with individual consumers were supplemented by a focus group with professional advisers who deal with sale and rent back customers.
- 2.5 Some additional quantitative information was collected by including a small number of questions in an 'omnibus' survey put to a sample of around 8,000 participants.
- 2.6 Shelter gave us a detailed submission based on mystery shopping and case study interviews with people who had contemplated or gone through with sale and rent back. In addition, Citizens' Advice and National Debtline submitted 77 case studies to us demonstrating problems experienced with sale and rent back. Our analysis of these case studies is presented in Annexe C.

- 2.7 The National Association of Sale and Rent Back (NASARB) - a newly established trade association for the sale and rent back sector - conducted a survey of around 200 sale and rent back businesses in February and March 2008, and shared the findings with us.
- 2.8 We also trawled sale and rent back websites, to obtain a snapshot view of how sale and rent back firms advertise their services. The results of this are presented in Annexe D.
- 2.9 We have also benefited from constructive discussions with sale and rent back firms, trade associations, consumer groups, Government departments, and the FSA.

Timescale and scope

- 2.10 Repossession is a major driver of demand for sale and rent back, and repossession rates are rising rapidly. The Council for Mortgage Lenders estimates an increase of almost 50 per cent in 2008 – forecasting 45,000 repossessions compared to 27,000 in 2007. We considered it necessary to look into the industry without undue delay.
- 2.11 Our market study was designed to be quick and tightly focused on the sale and rent back product. We had only a limited time to gather evidence but gathering comprehensive information on the industry would have been extremely difficult in any case, particularly given the speed of developments in the housing and finance sectors. Our view is that it is necessary to make a judgement about the likelihood of detriment arising in this sector based on the evidence now available, and to take action commensurate with the risks identified.
- 2.12 We chose not to widen the scope to include 'quick sale' transactions which have no rent back element. This is because our primary concern was the link between the discounts at which properties are purchased and the promise to consumers that they can stay in their home. However, we note that some of the issues identified in this report may also be relevant to 'quick sale'.

Report structure

- 2.13 Part 1 of this report (covering Chapters 3 to 6) considers the scale and nature of the concerns relating to sale and rent back.
- 2.14 Chapter 3 provides an outline of the sale and rent back industry, summarising what we know about the firms that operate, the products they offer, and the consumers who buy those products. It also outlines what currently exists by way of consumer protection for sale and rent back customers.
- 2.15 Chapter 4 explores the business model for sale and rent back. It looks at whether it is attractive for firms to provide sale and rent back products on a long term basis, and considers the attractiveness of the transaction from the consumer's point of view, in light of the alternatives available. It also looks at how supply and demand for sale and rent back might be affected by current changes in the economic climate.
- 2.16 Chapter 5 analyses the potential for consumer detriment. This is based on our consumer research and the other evidence we have received, as well as on an assessment of the key features of the product and the sector.
- 2.17 Chapter 6 summarises our conclusions on the likely nature and scale of the problems in the sector.
- 2.18 Part 2 of this report (Chapters 7 to 11) considers potential solutions to the problems identified.
- 2.19 Chapter 7 provides an introduction to this part of the report.
- 2.20 Chapter 8 considers whether it is possible to do more within existing frameworks to protect consumers entering into sale and rent back transactions.
- 2.21 Chapter 9 considers the potential for self-regulation to make the sector work better for consumers.

- 2.22 Chapter 10 summarises other developments underway that may offer further protection or assistance to sale and rent back consumers.
- 2.23 Chapter 11 concludes that further measures are needed to address the problems identified, and presents our recommendations to Government.

PART I: DIAGNOSIS

3 THE SALE AND RENT BACK SECTOR IN THE UK

3.1 In this Chapter we summarise what we know about:

- Sale and rent back firms – the size of the sector, the geographic spread, and the business models employed;
- Sale and rent back products – what is currently on offer in terms of the prices at which properties are purchased, the terms on which they are rented back, options to buy back the property, and the advice given by sale and rent back firms;
- Sale and rent back consumers – the circumstances in which people are likely to consider sale and rent back;
- Existing protection for sale and rent back consumers.

Sale and rent back firms

Size of the sector

3.2 There is limited information on the size of the sale and rent back sector. It is new and rapidly growing and, as yet, there is no single source of data or information about the sector.

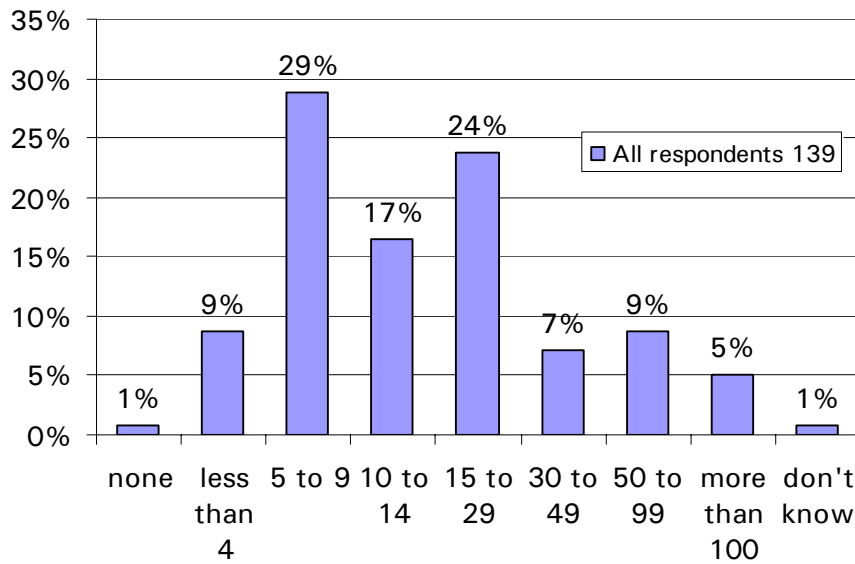
3.3 It is clear that the sector comprises a very large number of small firms, family businesses or individuals together with a few firms which operate on a national basis or regionally on a large scale. Recent research found that 5 per cent of landlords hold at least one sale and rent back property in their portfolio.⁴ Based on an estimate of 750,000 landlords in the UK, this suggests that there are around 37,500 sale and rent back landlords in the UK. Some of these operate individually, while others may be members of a network or franchise operation – the NASARB survey found that nine per cent of its members were part of a franchise

⁴ BDRC research undertaken for The Money Centre, BDRC Landlords Panel Syndicated Research, Fieldwork: June 2008, Wave 7 Subscriber Report, 21 July 2008.

network. Stakeholders we have spoken to provided estimates of the total number of firms active in the sector ranging from 1,000 to 8,000.

- 3.4 There are three industry associations and these have been able to share some data with us. These associations are The National Association of Sale and Rent Back (NASARB), The Property Buyers Association (Probas) and The Rentback Charter Association (RBCA).
- 3.5 NASARB was established in October 2007 by The Money Centre (buy-to-let mortgage brokers). The NASARB committee includes providers, lenders, and mortgage intermediaries. It now operates as an advisory group within the National Landlords Association (NLA). NASARB has over 500 members. It attracts primarily smaller operators – as shown in Figure 3.1, most firms have under 30 properties, though a few have more sizeable portfolios. Together, NASARB registrants hold upwards of 3,000 properties.
- 3.6 Probas was established in 2007 by three of the larger operators (A Quick Sale Limited, UK Property Buyers and North East Property Buyers) and is currently recruiting further members. It believes its members carry out about 3,000 transactions per year.
- 3.7 The RBCA was established in 2008 by a group of property investors. It has 32 full members and 27 who have registered interest, with typical portfolios of 30-50 properties each. In total, these firms have around 750 properties. RBCA is in the process of recruiting further members.

Figure 3.1 Survey of NASARB registrants: Distribution of respondents' portfolio size

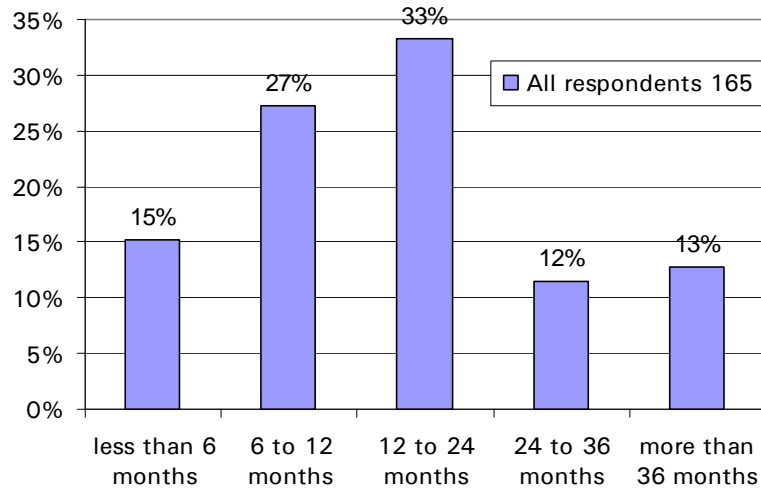


Source: NASARB

3.8 The omnibus survey undertaken as part of our consumer research found that 0.3 per cent of the sample had been through or were going through with sale and rent back. This suggests that, by summer 2008, around 53,000 households might have undertaken sale and rent back transactions.

3.9 Moreover, the sector has grown very fast. The NASARB survey found that around 40 per cent of its respondents had entered the sector in the last year, and a further 33 per cent in the previous year (see Figure 3.2).

Figure 3.2 Length of time in sector, NASARB members

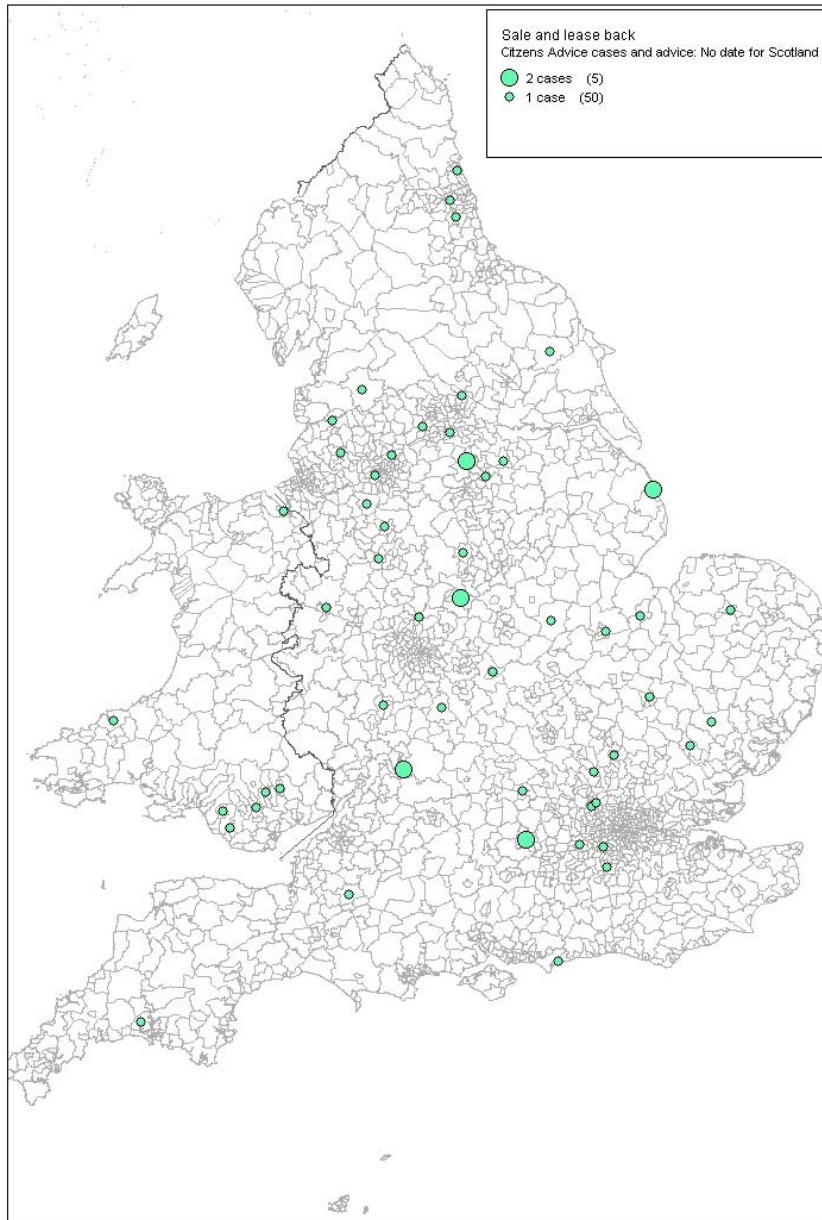


Source: NASARB

Geography

3.10 Sale and rent back firms operate across the UK. Many individual firms often focus on specific regions. Data from national firms indicated they received significant volumes of calls from all regions of the UK. Figure 3.3 shows the locations of the Citizens' Advice Bureaux which have reported concerns about sale and rent back. These are also dispersed across England and, to a lesser extent, Wales. Data for Scotland and Northern Ireland is not available.

Figure 3.3 Locations of CAB complaints



Based on postcode of CAB offices receiving complaints on sale and rent back between June 2006 and May 2008. No data available on Scotland and Northern Ireland.

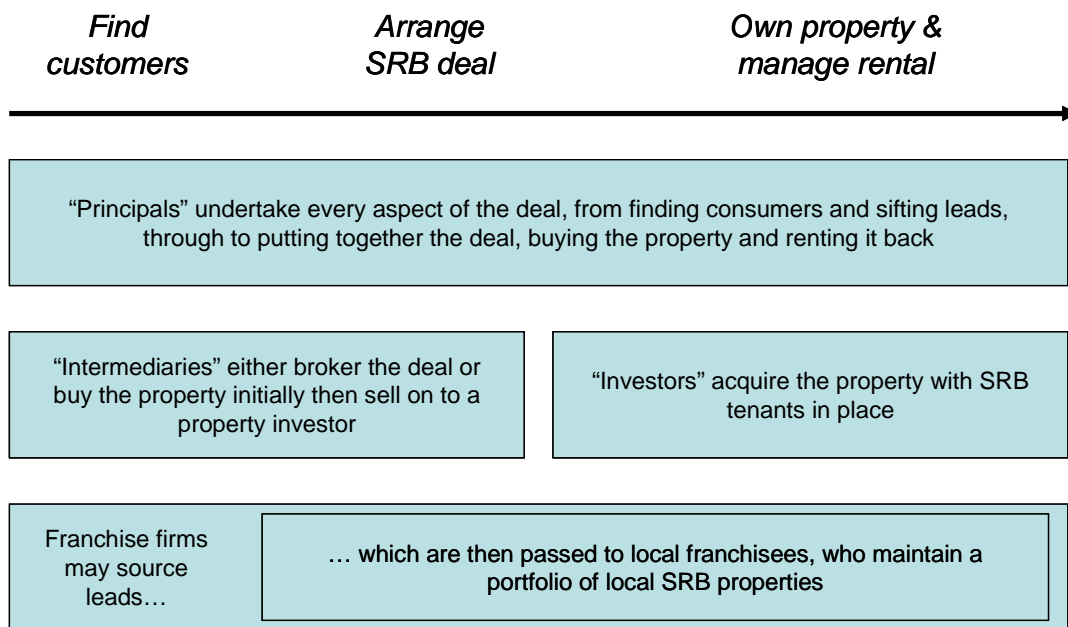
Source: CAB

3.11 Some firms operate internationally, for example A Quick Sale is active in some states of the US.⁵ We believe, however, that most firms are national rather than international firms.

Business model

3.12 Sale and rent back firms operate in different ways. Some business models are summarised in Figure 3.4.

Figure 3.4 Business models for sale and rent back (SRB)



3.13 Firms may also trade leads. For example, firms within a franchise network may sell each other leads that are outside their local area and acquire leads that are within their area.

3.14 Many firms, particularly investors, have a wider portfolio of buy-to-let properties in addition to those acquired through sale and rent back – the NASARB survey found that 92 per cent of respondents had other rental properties. Our website trawl, and conversations with firms, suggested

⁵ Annexe K provides a brief description of the sale and rent back market in the US.

that some companies also offer 'quick sale' transactions as an alternative to sale and rent back. Many firms also refer to 'equity release' on their websites, but use the term very broadly to refer to ways of releasing equity from homes, including sale and rent back, rather than specifically meaning a regulated product. Firms undertaking regulated equity release (that is, lifetime mortgages and home reversions) do not often offer sale and rent back products – they are typically much larger and do not operate as landlords in the ordinary sense. Equity release products are described in Annexe B.

- 3.15 Firms find customers in a number of ways, for example advertising in local or national newspapers, through web pages or by leafleting homes directly. In some cases, customers are referred to them by local authorities or Citizens' Advice Bureaux. Some firms offer inducements to people that recommend the company to a friend. Firms also approach individuals directly, for example after repossession hearings.
- 3.16 Most sale and rent back firms finance their business with buy-to-let mortgages secured on individual properties. A small number have access to commercial finance.
- 3.17 As this industry is still evolving, business models may change over time. It has been suggested to us that at least one firm is considering entering the sector on a very large scale.

Sale and rent back products

- 3.18 A sale and rent back arrangement allows the consumer to sell their house at a discount to the market price in return for the right to remain in the property as a tenant.
- 3.19 Sale and rent back arrangements are often marketed as a quick way of overcoming financial (or other) difficulties. The speed of the transaction is often emphasised – our website trawl suggested that almost all firms stress speed of transaction as one of the benefits of sale and rent back. Some firms say they can complete in 24 to 48 hours. This may be necessary where the consumer faces imminent repossession. However,

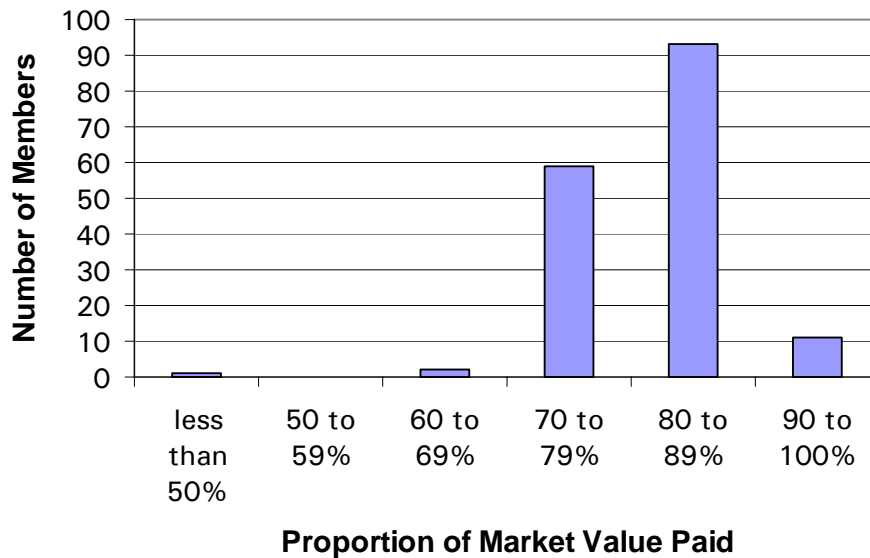
firms told us that it is more usual for transactions to take between two and four weeks.

- 3.20 The exact discount payable and the level of the rent is a matter for negotiation between the sale and rent back firm and client. Most firms appear to offer a bespoke package to each individual, tailored to their financial circumstances, taking into account the amount of the mortgage outstanding, the amount of other debts the consumer has and whether these are also secured on the property, the outgoings they can currently afford, and whether their financial difficulties are expected to be temporary or long-term.
- 3.21 Some firms set these terms out clearly, for example in key facts documents, but in other cases the written agreement is much less clear. Our consumer research found one case where the seller was not given any paper work to retain at all.

Sale price

- 3.22 According to the NASARB survey, most respondents (56 per cent) paid between 80 per cent and 90 per cent of the market value of the home, although a significant proportion (35 per cent) offered between 70 per cent and 80 per cent. This is shown in Figure 3.5. Our website trawl (see Annexe D) suggests that firms advertise in a range of 75-85 per cent.

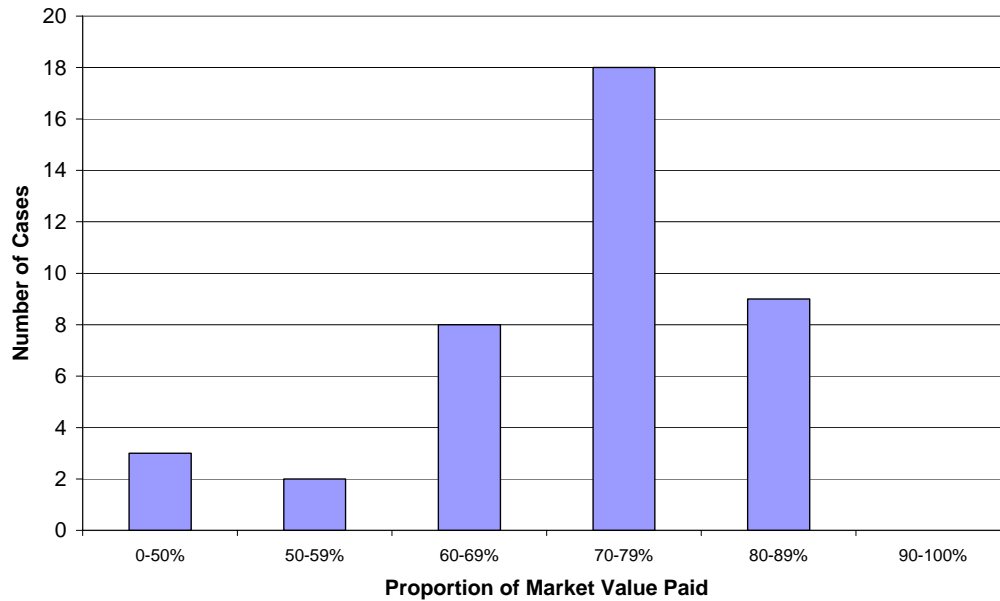
Figure 3.5 Percentage of market value paid, NASARB members



Source: NASARB

3.23 Analysis of the case studies submitted by Citizens' Advice and other organisations (see Annexe C) showed a higher level of discounts. It suggested that offers of between 70 and 80 per cent of the value of the house were common, as shown in Figure 3.6. This difference may be at least in part a reflection of the different sample – the case studies relate to consumers whose problems were deemed sufficiently concerning to be recorded by advisers and filed centrally.

Figure 3.6 Proportion of market value paid, case studies analysis



Source: CAB, National Debtline, Shelter

- 3.24 Firms also told us that, faced with tighter borrowing conditions and falling house prices, they are now offering deeper discounts than they did a year ago.
- 3.25 In some cases, a portion of the consumer's proceeds from the sale is held back by the firm for a period of time. Our consumer research suggested that this could range from a month's rent to tens of thousands of pounds. Firms told us that this helped cover arrears or damage to the property. Our consumer research suggested that in some cases this was unwelcome to customers, but in other cases customers wanted the firm to retain a portion of the proceeds to keep their savings at a level at which they would be entitled to state benefit.
- 3.26 The method by which the property is valued varies. In some cases, firms get the home valued by an independent surveyor. However, in other cases we have been told there is only a 'drive-by' valuation or a valuation conducted by an agent representing the buyer. A surveyor expressed concerns to us that sale and rent back firms were not always

transparent as to the reason for the valuation, and were perhaps requesting mortgage valuations (which would tend to be conservative) but then presenting these to the client as an independent estimate of market value.

- 3.27 Shelter contacted ten firms by phone in a mystery shopping exercise. Of these, four conducted their own valuations, and six said that they would send a RICS surveyor around to view the property and stressed the independence of those valuations as a result. However, only one of the six would let the customer see the report, another would let her see it only if there was a problem and their offer needed to be reduced, and a third suggested that she could use her own surveyor if she paid and that their offer could be based upon this. Two buyers required clients to pay for valuations and one suggested a special offer for a drive by survey.
- 3.28 Our consumer research also suggested that some consumers did not receive a written valuation of their property. Some customers had a good idea of the value of their home, but others only had a hazy idea and believed that the valuer was independent and would provide them with an accurate valuation for their home.
- 3.29 We also have reports of initial valuations subsequently being revised downwards. While 'gazundering' is to some extent to be expected in a falling property market, consumers considering sale and rent back, who may have few options and feel under pressure to act quickly, are particularly vulnerable to this practice. Our consumer research included a number of cases where the sale price was dropped at a crucial stage in the proceedings, such as when the sellers were due in court. Sellers reported that if they were unable to tell the court that the sale was imminent, they were at serious risk of repossession, and were therefore under extreme pressure to accept the reduction. Others were told that the original figure had been incorrect or a misprint.

Rent back

- 3.30 Many firms offer rent at local market rates, but some will offer a higher discount in exchange for rents that are below market value, at least for

an initial period. Market rent may not be transparent to all consumers. Our consumer research suggested that while some sellers were aware of market rent, others were content to be given a figure by the sale and rent back company. In addition, although rent is generally determined in advance of a sale, our research found examples where there was an unexpected increase at the completion of the transaction. Shelter's research also provides some examples where the rent was only agreed after the sale had been completed.

- 3.31 The rental agreement is typically an assured shorthold tenancy (AST). These are standard for the private rented sector. Most ASTs are granted for an initial fixed period of six or 12 months. During the fixed period, the landlord can only recover possession if there is a breach of the tenancy conditions. Once the fixed period of the tenancy has expired, the landlord is able to recover possession at his own initiative. A tenant with an AST may also be forced to leave the property if the sale and rent back firm defaults on the mortgage.
- 3.32 According to the NASARB survey, 95 per cent of firms offer an AST (or the Scottish equivalent) and 80 per cent use contracts with a fixed period of 12 months or less. The remainder of the respondents to the NASARB survey stated that they offered assured tenancies (ATs).
- 3.33 ATs are rarely used in the private rented sector but are widely used for social housing. It is much more difficult for a landlord to evict a tenant under an AT than an AST. A landlord can only seek possession against a tenant with an assured tenancy on a number of specified grounds. The relevant tests require the landlord to prove that it is reasonable to recover possession.
- 3.34 The results from our trawl of websites suggest that firms target consumers who want or need to stay in the property for a long period of time, often mentioning that properties could be rented back 'long-term' or for 'as long as needed'. Some firms warned that they could not guarantee long term tenure, but others did not. Shelter's research also suggested that most schemes are generally advertised – on paper or on

the phone - as providing long-term security and there was very little detail provided on websites as to the nature of the tenure.

- 3.35 Our consumer research indicated that, following their discussion with the sales person, customers were nearly always left with a firm impression that they would be able to remain in their home for as long as they wished. Some were told that there was an AST but this was described as a formality. This security was often a critical factor in proceeding with the transaction.
- 3.36 Firms also told us that they gave verbal guarantees that the tenancy would be rolled over. Others said that they differentiate between an 'intended' period and a 'guaranteed' period of tenancy, offering a rebate if the tenancy is terminated before the intended period is up.
- 3.37 The fact that sale and rent back tenants are offered so little security is at the root of much of the controversy surrounding the sector. Stakeholders (including a number of sale and rent back firms) have told us that there are 'rogue operators' in the sector who lead consumers to believe that they can stay in their home on a long-term basis but then evict tenants after only a short period of time.
- 3.38 Another aspect of the tenancy terms is that consumers may be exposed to unexpected increases in rent. Some firms provide undertakings not to increase rent by more than, for example, RPI plus three per cent annually. Our consumer research, however, found some examples where future rents were not discussed before the consumer signed the contract, or where large increases were demanded when the short fixed term in the AST expired. In some cases, these large increases in rent were unaffordable and led to the consumer having to leave their home. 15 per cent of the case studies provided by advisory bodies (see Annexe C) mention problems around increases in rent or lack of transparency over the rent.
- 3.39 There have also been reports of consumers being evicted following repossession proceedings by mortgage lenders after the landlord defaulted on the mortgage. Our consumer research found examples of

default by the landlord, and 15 per cent of the CAB case studies analysed in Annexe C related to landlords being repossessed. Default by the landlord is a particular risk given that many firms finance the purchase of properties wholly through borrowing and are therefore highly geared – the risks are heightened further when the sale and rent back firm holds back some of the proceeds of the sale against future rent or for other reasons.

- 3.40 The firms we spoke to, however, told us that their business was based on keeping the original occupiers in the property - this is discussed in more detail in the following Chapter - and that they fully intended to keep the tenancy agreement in place for as long as it was working well for both parties. The NASARB survey reported that 86 per cent of respondents had never ended a tenancy agreement, although few of these firms had been in the sector for more than two years so many of these agreements will have been in place for only a short period of time. Of those that had ended a tenancy agreement, 88 per cent said it was because the rent was in arrears and a small number considered the tenants were acting in an anti-social manner. None said they had initiated possession proceedings only in order to sell the property.
- 3.41 Firms told us that they were not able to offer more secure forms of tenure because lenders would only offer buy-to-let mortgages against ASTs with short fixed term periods. Of the firms surveyed by NASARB who said they used Assured Tenancies (ATs), some stated that they did so in contradiction of their lender's terms and conditions. Only a small number said they had access to commercial finance and so were not restricted in this way.
- 3.42 Some lenders we spoke to confirmed that they had a firm policy not to lend against ATs, while others did not appear to have considered the issue. Generally, lenders seemed more concerned about the reputational risk from sale and rent back firms evicting tenants and the difficulty in identifying when mortgages were being used to fund sale and rent back purchases. One lender we spoke to chose to avoid lending to sale and rent back firms at all by including a term specifying that the home could not be rented back to the former owner. Those lenders who were, in

principle, open to lending to sale and rent back firms said they had not developed a way to finance more secure tenancy arrangements.

- 3.43 Some firms have developed ways of enhancing the security of tenure under an AST by giving written undertakings that the tenancy will be rolled over (provided there is no breach of the tenancy) and that the customer will be allowed to stay in the property for a longer period of time, in some cases as long as they wish. For example, one firm we spoke to supplies a 'trust deed' with an undertaking not to evict anyone from the property without cause. Another offers an agreement that if the tenancy is terminated without cause during a specified period (for example five years), the customer will get a pro rata refund of the discount to market at which the property was purchased. Other firms include terms within the AST itself which give the tenant a right to renew the tenancy with rent increases in line with a prearranged schedule.
- 3.44 The robustness of such agreements in terms of protecting tenants are, as far as we are aware, largely untested. Nonetheless, they may provide some additional security should the landlord seek to increase the rent or seek repossession in breach of the terms of the agreement. A tenant who has relied on a clear promise of the landlord not to enforce the right to repossession may be able to argue successfully before a court that it would be unfair to grant possession in the face of such a promise. Each case would, however, need to be considered on its merits. However, such agreements may provide no protection if the landlord defaults on the mortgage and the lender seeks repossession.
- 3.45 The industry associations are working to find ways of reducing the risk to consumers. For example, they are developing the idea of a 'lifeboat' scheme, whereby when a member gets into difficulty with a mortgage on a sale and rent back property (or on a portfolio of properties) the lender grants a grace period during which the property can be sold to another investor, with the tenants in situ. We understand that there has been at least one instance when such a transfer has been successfully achieved.

Buy-back

- 3.46 Some sale and rent back firms give consumers the option to buy back the property in future, should their financial circumstances improve. According to the NASARB survey, a buy-back option is offered by around 75 per cent of firms. However, firms told us that many consumers do not even take-up this option and of those that do few, if any, have exercised it to date.

Advice

- 3.47 Some firms told us that they offer advisory services as part of the package. Our website trawl confirmed this (see Annexe D) These services may include legal services, advice on the consumer's financial situation, support in stopping repossession and advice on matters such as housing benefit (in addition some firms may pay for a valuation, as discussed above). Our consumer research suggested that this may be welcomed as many consumers did not have enough money to pay for their own advisers upfront.
- 3.48 However, this also raises questions about the quality and independence of advice. For example, our consumer research found that solicitors provided by the sale and rent back company to provide advice to the seller were sometimes suspected to be acting for sale and rent back company as well. In other cases, however, customers were invited to choose their own solicitor, usually from a provided list of available legal advisers.
- 3.49 Our consumer research also found instances where firms provided financial advice and debt counselling and were supposed to settle debts for customers as part of the sale and rent back deal, but continued to demand further money after the transaction. Where firms do engage in debt counselling they will need to apply for a credit licence. We checked the names of 149 sale and rent back companies against the OFT's database of credit licences and found 17 matches. This indicates that perhaps 10 to 15 per cent of sale and rent back companies regard

themselves as undertaking activities that are subject to the CCA. We do not know if these correspond to the firms that offer advice.

- 3.50 Some firms provide information on benefits, particularly housing benefit. In some cases, firms will approach housing benefit officers on behalf of prospective tenants to discuss eligibility since whether or not tenants are able to pay the rent may depend on housing benefit. The eligibility of sale and rent back tenants for housing benefit is not straightforward. While each case is assessed individually, in principle, tenants will not be eligible if the tenancy is deemed to have been created to take advantage of housing benefit. They may also be ineligible if capital was released from the sale, or if capital would have been released from the sale had it taken place at full market value. Further detail on state assistance with housing costs is given in Annexe E.
- 3.51 It appears that firms may not always give good advice about benefits - our consumer research suggested that advice around state benefit was a particular source of concern and the case studies from advisory bodies (see Annexe C) suggest that advice from sale and rent back providers on benefits has been a common cause for complaint.
- 3.52 Consumers may also be unaware that the sale and rent back transaction may be relevant in a subsequent application for bankruptcy. This is because the sale of the property in a sale and rent back transaction may be deemed to be a sale of assets at less than their value. If so, and if the sale and rent back transaction is found to have been entered into dishonestly or in a blameworthy manner, the customer may face a Bankruptcy Restriction Order which imposes restrictions on the individual for up to 15 years.
- 3.53 Some firms refer customers to independent financial and legal advice, or recommend a debt counsellor. However some firms told us that they find that many customers do not go ahead with this.

Sale and rent back consumers

- 3.54 Of the consumers who took part in our consumer research, at the time leading up to the sale and rent back transaction, many were out of work and living on benefits; the remainder were in relatively low paid jobs.
- 3.55 In line with the indications from our consumer research, firms told us that properties are generally small houses or flats and are seldom valued at more than £200,000. The analysis of the case studies from advisory bodies (see Annexe C) was also consistent with this, with the average value of the property in those case studies being around £158,000.
- 3.56 Our consumer research also suggests that the majority of sale and rent back consumers were in debt at the time of the transaction – most often they had mortgage arrears but many had other creditors such as loan, credit card and utility companies. Again this was consistent with the CAB case studies in Annexe C, in which over 50 per cent of cases mentioned debts prior to the transaction. Our consumer research indicates that in some cases debt builds up over a long period, but more often it was the result of some event such as ill health or redundancy. Some who took part in our research who were considering or going through with sale and rent back were not yet in debt but expected that forthcoming mortgage changes would leave them unable to pay in the future.
- 3.57 Our consumer research indicates that, while the level of debt varied from a few thousand pounds to six figure sums, a common feature was that the individual felt the situation was out of control and that he or she could not pay off their debts from income. Some were in imminent danger of repossession. This is consistent with the analysis of data from advisory bodies which suggested that 60 per cent faced repossession. Firms we spoke to also confirmed that many of the consumers they deal with are in financial difficulties, and may be facing repossession. Firms also told us that the customers are often sub-prime borrowers with multiple debts.

- 3.58 For sale and rent back to be feasible, the consumer must have a sufficient portion of equity in the home. People facing difficulties with high loan-to-value mortgages taken out in recent years are unlikely to be offered the option of sale and rent back. Several firms told us that a typical client was someone who had exercised a 'right to buy' their property from their local authority. The discount at which they bought the property and/or the subsequent rise in property prices meant they now had equity in the home. There is also some market research available which suggests that many property owners on low incomes do have a large amount of equity in their property.⁶
- 3.59 Not all consumers entering into sale and rent back agreements are in financial difficulties. Some firms told us that they specifically targeted people approaching retirement. Firms also told us that some consumers wanted to release the equity in their home for personal reasons (such as relationship breakdown) but to remain living in it for the time being. Others customers are looking to facilitate relocation, or 'chain breaking' – someone who wants to move can sell their property, stay in it short term, and be a cash buyer. Our website trawl confirmed that some firms do target such consumers (see Annexe D).
- 3.60 It is very difficult to estimate the proportion of consumers entering into sale and rent back for each of the possible reasons, and in many cases the reasons may not be discrete – for example, those facing retirement or divorce may also be in financial difficulty. One firm estimated that only half of its customers were in financial difficulty. Another stated that it actively avoided customers with financial difficulties but instead targeted customers planning for retirement. However, our consumer research found only a small number were exploring sale and rent back as a means of equity release for retirement planning. Certainly, a scan of sale and rent back websites and adverts in local newspapers suggests that financial difficulty and repossession in particular are major drivers in this sector.

⁶ Mintel 'Equity Release, Financial Intelligence' May 2008, page 79-80.

Existing consumer protection

3.61 The sale and rent back sector is largely unregulated. There is no regulation specific to sale and rent back (in contrast to regulated equity release). However, there are sector-specific regulations that apply to any debt advice and estate agency activities undertaken by sale and rent back providers. General consumer protection legislation also applies, and housing law provides some additional protection. The relevant consumer protection measures are described in detail in Annexe F and are summarised in Table 3.7 below. Details of the regulatory regime for equity release are provided in Annexe B.

Table 3.7: Summary of relevant consumer protection regulation

Regulation	When does it apply?	Application to sale and rent back (SRB)	What does it provide for?
OFT sector specific regulation			
Consumer Credit Act 1974 (CCA)	Applies to many forms of consumer credit transactions including 'ancillary credit business' such as debt-adjusting or debt-counselling.	Will apply to sale and rent back where debt advice on loans or other debts (excluding primary – 'first charge' – mortgages) is given.	Debt-adjusting or debt-counselling requires a licence from the OFT. To gain a licence, the firm must satisfy fitness requirements. OFT can revoke the licence. Agreements made without a licence are likely to be unenforceable but there is no direct form of redress under the CCA in relation to losses incurred.
Estate Agents Act 1979 (EAA)	Applies to those engaged in 'estate agency work', essentially those who receive instructions to introduce buyers and sellers of a property in order to secure its sale.	Will apply to sale and rent back providers that sell property on.	OFT can prohibit sale and rent back providers from carrying out estate agency work if they are satisfied that the person is unfit. From 1 October 2008, estate agents have been required to belong to a redress scheme.

Regulation	When does it apply?	Application to sale and rent back (SRB)	What does it provide for?
General consumer protection regulation			
Consumer Protection from Unfair Trading Regulations 2008 (CPRs)	Applies to unfair commercial practices by traders, including those which are misleading (by action or omission) or aggressive and which cause the consumer to take a transactional decision he would not otherwise have taken, or which are included in a list of specific commercial practices which are unfair in all circumstances and prohibited.	Will apply to sale and rent back firms that provide false or deceptive information, or engage in pressure selling or in a prohibited practice, such as falsely claiming to be a signatory to a code of conduct.	A range of enforcement action, including criminal and civil proceedings, may be taken against those who breach the Regulations. Consumers may not seek redress themselves under the Regulations but may seek compensation under the general law.
Advertising regulations	Complaints about misleading advertising can be made to Advertising Standards Authority ('ASA') under voluntary codes.	Will apply to sale and rent back firms that provide false or deceptive marketing communications.	Provider to amend/withdraw unlawful marketing communications. If they fail to do so, sanctions are applied on the business. Non-complying parties may be subject to enforcement action, for example under the CPRs (see above).

Regulation	When does it apply?	Application to sale and rent back (SRB)	What does it provide for?
Unfair Terms in Consumer Contracts Regulations (UTCCRs) 1999	A contractual term is unfair if it has not been individually negotiated and if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations under the contract, to the detriment of the consumer. The fairness test does not apply to terms which define the main subject matter of the contract which are expressed in plain intelligible language.	Will apply to sale and rent back where contract is not individually negotiated. Additionally, the price payable and rent charged or length of the agreement may form the main subject matter of contract and therefore not subject to the unfairness test.	An unfair term of a supplier is not binding on the consumer and a consumer could rely on this in defence to any claim for breach of contract.
Doorstep Selling Regulations	The Regulations apply when consumers buy goods or services from a trader on the doorstep or in their home (or in someone else's home), at their place of work, or when they buy from a trader on an excursion the trader has arranged away from its business premises.	An agreement by a consumer to sell his home to the SRB provider (or to a third party) would fall outside the scope of the Regulations.	Contracts for goods or services with a value over £35 are unenforceable against the consumer unless the trader has delivered to the consumer notice in writing indicating the right of the consumer to cancel the contract within seven days.

Regulation	When does it apply?	Application to sale and rent back (SRB)	What does it provide for?
General law	General application.	SRB providers who have breached contracts or have made misrepresentations causing loss may be liable for damages. SRB providers who seek to increase rent or repossess contrary to assurances may be prevented from doing so by the court.	Consumers may apply to the court for damages, or may defend proceedings in reliance on general principles of law.
Housing legislation			
Mortgages and Home Finance: Conduct of Business Sourcebook (MCOB)	Rule 13 of MCOB concerns arrears and repossessions and requires firms to deal fairly with customers who are in arrears, including using efforts to reach an agreement and providing current FSA information sheet on mortgage arrears.	Grants consumers in financial difficulty an opportunity to resolve their financial difficulties and to obtain information as to sources of independent advice prior to entering into SRB agreement.	If lender has not complied with MCOB, customer can complain and, if necessary apply to the financial ombudsman to resolve complaint. If possession proceedings are commenced, the Court can exercise discretion to suspend possession in some circumstances.
Housing Act 1988	AST or AT rental agreements.	Applies to sale and rent back tenants with a periodic AST (or AT) tenancy agreement.	Landlords are prevented from increasing rent more than once every 12 months, unless provision is made for this in the tenancy agreement. A tenant may also apply to a tribunal if the rent is above market rates.

OFT sector specific regulations

- 3.62 The licensing regime under the Consumer Credit Act 1974 may apply to the sale and rent back sector in limited circumstances. Specifically, those sale and rent back providers who advise individuals on how to discharge debts such as additional secured loans or unsecured loans need to hold a credit licence. Consumers dealing with licensed firms have access to the Financial Ombudsman Service.
- 3.63 The Estate Agents Act will also apply to those sale and rent back firms which act as intermediaries, that is, who introduce individuals wishing to sell and rent back their property to firms looking to buy such properties. The OFT has the power to ban such firms from estate agency work if they deem the provider unfit. In addition, as of October 2008, estate agents have been obliged to join an approved redress scheme.
- 3.64 These sector specific regulations therefore have some application to the sale and rent back sector. However, the protection is somewhat limited, particularly as not all sale and rent back firms provide debt advice or act as intermediaries. The regulations therefore only cover a portion of the sale and rent back sector.

General consumer protection regulations

- 3.65 Sale and rent back consumers also benefit from general consumer protection regulations. The Consumer Protection for Unfair Trading Regulations (CPRs) may have particular relevance. For example, misleading statements about the security of tenure may contravene the CPRs. Consumers can also complain to the Advertising Standards Authority about misleading advertising. However this regime does not provide for direct redress for consumers who have been misled.
- 3.66 Other forms of consumer protection regulations such as the Doorstep Selling Regulations and Unfair Terms in Consumer Contracts Regulations (UTCCRs) and are likely to provide less protection to sale and rent back consumers. Doorstep Selling Regulations provide protection for sales which take place in the home. However, there are exemptions to the

regulations which mean that sale and rent back contracts are not covered. UTCCRs will not apply to sale and rent back agreements which are individually negotiated. Nor do they provide protection for the main subject matter of the contract, or its price.

- 3.67 Consumers may rely on other, general, laws to seek redress from sale and rent back providers, for example for breach of contract or misrepresentation. However, damages may not be recoverable if the sale and rent back provider cannot be traced or is insolvent, and may involve court proceedings if a negotiated settlement cannot be reached. Further steps may need to be taken to enforce any judgment. In certain circumstances, tenants may be able to argue before a court that sale and rent back providers are prevented from imposing rent increases or seeking possession under the terms of the tenancy agreement under the principle of estoppel or, possibly, breach of trust.⁷ However, the outcome may be uncertain and will depend on the particular circumstances of the case.

Housing protection

- 3.68 We note that the FSA's mortgage regime provides some protection to consumers in arrears or facing repossession, and that consumers should be aware of their rights in these circumstances before considering sale and rent back. The FSA's regime does not apply to sale and rent back itself however.
- 3.69 Housing law also provides some protection against unfair practices by landlords, including increases in rent beyond market rates.

Conclusion on existing protection

- 3.70 In summary, although general consumer protection measures apply in this sector, there is limited specific regulation that goes beyond this. In particular, those consumers who may receive informal assurances that

⁷ Further details are contained in Annexe F.

they can stay in their property for a long period of time but are subsequently forced to leave their homes have limited avenues of redress.

4 IS SALE AND RENT BACK SUSTAINABLE?

4.1 In this Chapter we discuss the business model for sale and rent back. We look at whether it is attractive for firms to provide sale and rent back on a long term basis, and then go on to consider the attractiveness of the transaction from the consumer's point of view, in light of the alternatives available. We then look at how supply and demand for sale and rent back might be affected by current changes in the economic climate.

The proposition to the firm

4.2 A number of stakeholders expressed concern that the sale and rent back business model is predicated on gains derived from buying a property at a discount and, once the initial term of the tenancy has expired, evicting the tenants and selling it on at the full market value. Doubts were expressed about whether it could be financially sustainable to rent the home back to the consumer at a rate that was lower than their original mortgage payments for a long period of time, and whether this would be more profitable than evicting the tenant quickly and selling the property on the open market.

4.3 Firms assured us that there was a viable long term business model in sale and rent back. They told us that the capital gain from selling the property is part of rationale for the deal, but that as property investors they were looking at the long-term appreciation of the value of the property, as well as the discount at the time of purchase. The impact of the recent falls in house prices is discussed below.

4.4 Firms also told us that it was sustainable for them to offer rents that were lower than the customers' original mortgage and debt payments. This is because many consumers borrow at high interest rates on their mortgages, as many customers have sub-prime loans, and also pay high interest rates on debt such as second charge loans or credit cards. The sale and rent back transaction allows the consumer to pay off this expensive debt, and leaves the firm with a cheaper buy-to-let mortgage. Because the cost of this debt is lower, firms can cover their interest

costs by offering rent which is less than the customers' original debt payments, even allowing for a 'rent cushion' over and above the mortgage interest.

- 4.5 Firms also told us that renting to former owners is preferable in some ways to renting out on the open market, because they tend to take better care of the property, and are less likely to leave the property which reduces the landlord's exposure to 'void' periods when the rental property is empty. In addition, the market rent for the property would often be low if the houses are in poor condition, and substantial refurbishment would be necessary to rent the property on the open market. It was also suggested, however, that landlords had an obligation to refurbish properties in poor condition, even under sale and rent back agreements. We questioned whether sale and rent back tenants were a riskier proposition in terms of being able to meet rent payments but firms told us that, provided the deal was affordable, their tenants tended to be reliable.
- 4.6 Some consumers may be attracted by sale and rent back agreements even where rents are not significantly lower than their initial mortgage and debt payments, for example, because they believe they would be eligible for more state support with housing costs as tenants than they had been as owner-occupiers.
- 4.7 Nevertheless, firms told us that in many cases they cannot find an agreement which will work financially for both the firm and the consumer and therefore turn away some prospective customers. Our consumer research also suggested that people who reject sale and rent back may do so because either the amount offered for the house would not cover all of their debts or the amount asked for the rent was too high – often at a similar level or higher than the consumer's own mortgage and debt payments.
- 4.8 We consider that the available evidence points towards the conclusion that, in principle, there is a viable business model in which a firm can purchase a consumer's home and rent it back to them on a long term

basis, potentially lowering the consumers' overall outgoings. However, a sustainable deal can be reached only in limited circumstances.

The proposition to the customer

- 4.9 This section considers whether, and how, sale and rent back makes sense from the consumer's point of view. At first glance, consumers appear to be giving up significant amounts in terms of equity in their homes in exchange for being able to continue living there. Is this necessarily the best option for them?

- 4.10 There are a number of courses of action which may be open to people in situations where they would consider sale and rent back. Table 4.1 summarises the main advantages and disadvantages of each.

Table 4.1 Comparison of alternative courses of action

	Advantages	Disadvantages
Sale and rent back	Release equity from home Stay in own home Speed Low transaction costs May increase eligibility for benefit	Lack of security of tenure Don't receive full market value of home Require sufficient equity in home May not significantly lower outgoings Potential implications on bankruptcy
Negotiation with Lender (or remortgage)	Stay in own home May reduce mortgage payments (eg by switching to an interest only deal).	Workable alternative may not be found Remortgaging may entail upfront costs and may be difficult if have a bad credit history
Downsizing – sale on open market	Release equity from home Get full market value Find more affordable solution	Lose home Possible difficulties finding alternative accommodation Costs of relocation May take time
Downsizing – quick sale	Release equity from home Find more affordable solution Speed	Lose home Costs of relocation Possible difficulties finding alternative accommodation Don't receive full market value of home
Equity release	Remain in own home Security of tenure Fully regulated	Age limit Expensive/may not release sufficient capital Require considerable equity in home
Social Mortgage Rescue Schemes	Stay in own home Release equity from home May receive full market value Security of tenure	Eligibility requirements apply
Repossession, bankruptcy, IVA	Freedom from debts Fresh start following discharge	Lose home if repossessed and possibly under bankruptcy/IVA Consequences for credit ratings

4.11 As the table shows, sale and rent back does offer benefits over other options. In particular, it enables the consumer to release equity in their home, while continuing to live in it, possibly with reduced outgoings. In addition, the transaction can be very quick and low cost (for example, with no estate agent's fees) and is less restrictive than regulated equity release.

- 4.12 Our consumer research suggested, unsurprisingly, that the ability to remain in the home was considered an overwhelming advantage. This was often for emotional reasons – many individuals had a strong attachment to their home. Some were also concerned that having to move home would expose their financial difficulties to friends and family. Others had more practical reasons for wanting to stay – for example, in some cases occupiers were too ill to move, had children in a local school, or feared that they would be unable to move pets into rented accommodation.
- 4.13 It seems, from the examples we have, that in many cases customers went through with sale and rent back as they perceived that they would have more access to state support. Where the person becomes eligible for housing benefit as a tenant this can make the transaction attractive even where the rent is no lower than the initial mortgage payments or where other types of sale would generate higher proceeds. To date, support for owner occupiers to meet mortgage payments has been more limited than support for tenants, and there have been longer waiting periods for claims (although as discussed in paragraph 4.24 below, and in Annexe E, the Government is now planning to extend the availability of income support for mortgage interest).
- 4.14 Some customers specifically asked the sale and rent back firm to withhold some of the proceeds of the sale of the property so that their level of capital stayed below the relevant eligibility threshold for state benefit. Others expected to be rehoused by their local authority eventually (for example, on retirement) and were therefore only looking for a solution to tide them over until that time.
- 4.15 In reality, however, the state benefit rules in relation to sale and rent back tenants are not straightforward, and the benefit advice from sale and rent back providers has been a common cause for complaint (see Annexe C). Some customers taking part in our research only discovered that they would not be eligible for housing benefit after selling their property.

- 4.16 Table 4.1 also summarises the serious disadvantages of sale and rent back as an option for consumers. In particular the lack of security of tenure means there is a risk the consumer may lose their home just a short period after entering into the deal. In addition, the rental value of the property may not be significantly below previous mortgage and debt repayments bringing into question the long term affordability of staying in their home. The analysis of case studies from advisers in Annexe C suggests that in over half of the instances, consumers had problems meeting rent payments or other debt even after going through with sale and rent back. For these consumers, undertaking sale and rent back may simply have delayed the inevitable loss of their home, while in effect stripping them of a portion of the equity they had built up in it.
- 4.17 Consumers should therefore consider sale and rent back carefully, weighing it up against the possible alternatives, before entering into it. However, only a few of the consumers participating in our consumer research had considered any other options in any more than a cursory manner. Most felt that they had no way out of their financial dilemma before learning of sale and rent back. Those who rejected sale and rent back generally did so because sale and rent back itself was not affordable, rather than because they had found a preferable alternative. Such individuals generally sold their homes on the open market and moved into private rented accommodation. Others had turned instead to further borrowing.
- 4.18 Those that had considered alternatives mentioned various difficulties:
- Only a few of the consumers our researchers spoke to had approached their mortgage lender. Very few had been able to negotiate repayment options and, in the small number of cases where this had been done, it had failed to resolve the situation because their overall financial situation was too grave for rescheduling to be a viable option.
 - Sale on the open market was rejected by some on the grounds that they would not have enough savings for a rental deposit to a private landlord, and the council would not offer them social housing.

Another concern about sale on the open market was that the property required renovation, and it would be difficult to find buyers for the property in its current condition.

- A 'quick sale' transaction was only considered by one person interviewed, and had been rejected because of the low price offered.
- Where equity release was considered, it was often rejected as it did not provide sufficient capital. Our website trawl (Annexe D) confirmed that sale and rent back is sometimes marketed as a cheaper, quicker and simpler alternative to regulated equity release products.
- Social mortgage rescue schemes were not often mentioned, perhaps because, at the time, schemes were still limited in availability.
- Repossession or bankruptcy were often felt to be the only alternatives, and sale and rent back was considered preferable as it would allow the consumer to stay in their own home. However, during the focus group discussions undertaken as part of the consumer research, professional advisers suggested that bankruptcy may often be the best course of action where debts are insurmountable.

4.19 It seems that consumers choose sale and rent back over other options for a variety of reasons, some more compelling than others. It appears that sale and rent back can in principle make good sense for someone when it lowers their monthly outgoings and allows them to stay in their own home.

4.20 However there are other circumstances in which sale and rent back is unlikely to be a good choice, for example:

- When the affordability depends on the award of housing benefit and there is significant uncertainty over whether this will come through.

- When the rent is not affordable on a long-term basis, for example because the person is out of work for prolonged periods due to ill health.
- When consumers do not have compelling reasons to stay in their own home and they would be better off cashing in the equity they have in the home by selling on the open market and moving on.

4.21 Furthermore, even for those for whom selling and renting back their own home could be a good option in principle, the risks involved in sale and rent back as it stands are considerable. We discuss consumers' ability to take account of these risks in making their decision in the following Chapter.

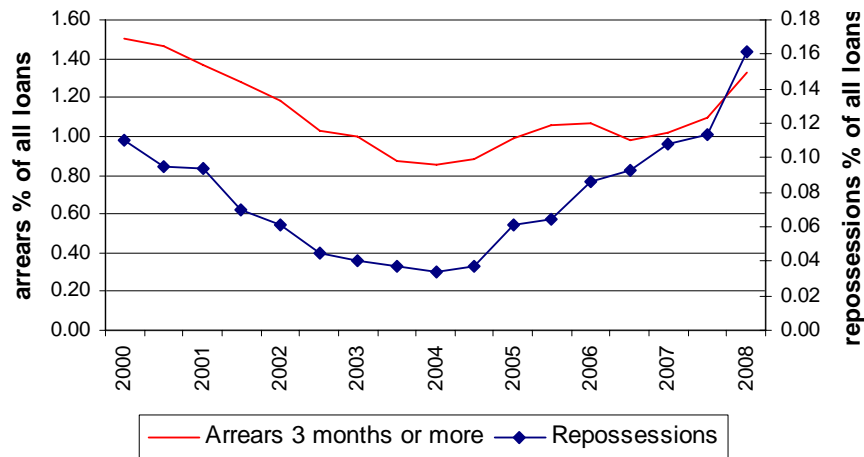
Prospects for the industry

4.22 Ongoing developments in the housing and financial markets will have a significant bearing on both the demand for and supply of sale and rent back deals.

Demand-side factors

4.23 As discussed earlier, difficulties meeting mortgage payments and the threat of repossession are common reasons for considering sale and rent back. Rising arrears and repossessions, illustrated in Figure 4.2, may therefore significantly increase demand for sale and rent back. Most commentators expect the upward trend in arrears and repossessions to continue; indeed they are still low in comparison to historic highs, such as the early 1990s when repossessions were more than double the current level.

Figure 4.2: Arrears and repossessions, 2000-2008



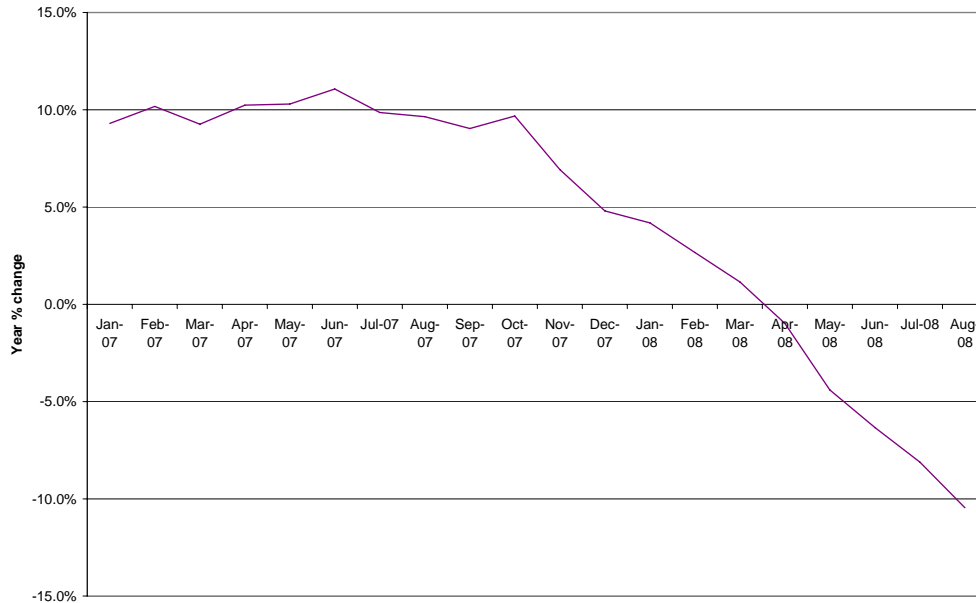
Source: CML: Notes: 1) Mortgages in arrears at half-year end – Repossession per half year. 2) Figures are estimates of arrears on all first charge loans held by CML members, both regulated and unregulated and include buy-to-let. 3) In H1 2008 CML members accounted for 95 per cent of first charge mortgages.

- 4.24 The Government has recently announced a number of measures to help those facing the threat of repossession. This includes significantly expanding funding for social mortgage rescue schemes, which it believes will prevent 6,000 repossessions. (These schemes are described in more detail in Annexe H.) It also announced reforms to income support for mortgage interest, which it estimates will prevent 10,000 repossessions. (These reforms are described in more detail in Annexe E.)
- 4.25 Nevertheless, many people facing repossessions will not be eligible for either form of extended Government support. The Council of Mortgage Lenders (CML) forecasts 45,000 repossessions in 2008, up from 27,000 in 2007 (and others suggest repossessions in 2008 will be even higher – the Royal Institute of Chartered Surveyors puts the figure at 53,000). The estimated 16,000 households which stand to benefit from the increased Government assistance will represent a significant portion of the increment in repossessions over the last year. However, if repossessions increase further in 2009 demand for sale and rent back may increase further.

Supply-side factors

- 4.26 Although changes in the economic climate may increase demand, they negatively affect the supply of sale and rent back.
- 4.27 It seems very likely that the increasing restrictions on borrowing must be severely hampering landlords' ability to acquire new properties. The CML stated that buy-to-let loans in the first half of 2008 came down to 44,600 from 176,500 in the second half of 2007. Bradford and Bingley was one of the major lenders to buy-to-let investors generally and we were told that many sale and rent back firms used Bradford and Bingley's 'Mortgage Express' product until this was taken off the market earlier this year.
- 4.28 Added to this, after a sustained period of increase, house prices are now falling. This is illustrated in Figure 4.3. Expectations are that house prices will continue to decline – the CML expects house prices to be about seven per cent lower in the fourth quarter of 2008 compared to the fourth quarter of 2007. Landlords may therefore expect lower capital gain from the transactions.

Figure 4.3: Nationwide house price index, Jan 07 – Aug 08



Source: Nationwide

- 4.29 The fall in house prices will also mean that homeowners' equity will decrease. This will mean that sale and rent back will be viable in fewer cases, as homeowners have less equity in their homes.
- 4.30 A number of operators have confirmed that the current conditions are restricting growth in the sector. One large firm estimated that as many as half of the players in the sector have disappeared in the last nine months. However, other firms have told us that they will continue to make transactions, but that they require deeper discounts to make them work. One industry body told us they expect that many small, non-professional investors will leave the sector but that the larger operators will continue to invest, albeit more slowly.

Conclusions on prospects for the industry

- 4.31 In summary, the number of consumers considering sale and rent back may be increasing due to homeowners' worsening financial situations. At the same time, the fall in house prices means that the amount of

equity in their homes is decreasing making sale and rent back less viable. Moreover, credit restrictions and house price falls are making it significantly more difficult and costly for firms to supply, leading firms to exit the market.

- 4.32 The complex inter-relationships and uncertainty in the macro economy mean that the prospects for sale and rent back are difficult to predict. However, it seems likely that fewer transactions will be made, although those that do happen will involve higher discounts and/or increased rents for consumers.

Conclusions on sale and rent back business model

- 4.33 Our conclusion is that sale and rent back is potentially a viable proposition in the sense that it can be profitable for the firm to supply at the same time as delivering the benefits consumers expect. However, at present consumers bear a great deal of risk - and we return to this subject in the next Chapter.
- 4.34 However, many consumers also have other ways of releasing equity from their home, such as coming to an arrangement with their lender, selling on the open market and downsizing, or buying regulated equity release products. There is evidence that, despite the risks involved in sale and rent back transactions, consumers do not always give full consideration to these options.
- 4.35 The market for sale and rent back will clearly be affected by the increase in consumers facing financial difficulties, the restricted availability of credit, falling house prices, as well as recently announced Government initiatives on social mortgage rescue and income support for mortgage interest. The net effect of these factors is difficult to predict. It seems likely that growth in the sector will be restricted but that opportunities will remain. Those transactions that are made are likely to involve a greater discount to market value.

5 ANALYSIS OF DETRIMENT

5.1 It is clear that many consumers have found the ability to rent back their own home extremely valuable, and that sale and rent back transactions can in principle benefit consumers, in some cases significantly. Our researchers interviewed a number of customers whose deals had – so far – proceeded as they had expected. These individuals believed that the transaction had been the right thing to do, even though they were not always aware of the total cost of it. Some described it as a 'life saver'. Although none of the consumers interviewed had been renting back for a very long period of time (reflecting the fact that the market is new) some had continued to rent back past the initial term of the tenancy and had experienced only modest rent increases, and some were very content with the fact that they had improvements made to their home.

5.2 However, in other cases sale and rent back transactions have created significant problems for consumers. The research we commissioned and the case studies submitted by other organisations have shown instances of, among other things:

- Sale and rent back landlords defaulting on the mortgage, leading to repossession by the lender and tenants losing their home. In some cases tenants also lost money that the landlord had retained as a deposit or pre-paid rent.
- Sale and rent back landlords suddenly and significantly increasing the rent, forcing the tenants to leave the home.
- People being persuaded to enter into sale and rent back when this was unlikely to be a sustainable solution for them.
- People entering into sale and rent back on the basis that they would receive housing benefit, then discovering that they were not eligible.
- Exploitation of people in difficult situations, for example sale and rent back firms dropping the purchase price just before sellers were due in court for repossession hearings.

- Sale and rent back firms levying unexpected charges at a late stage in the process.
- 5.3 We include a few examples of case studies to illustrate the nature of the detriment – both financial and psychological – when consumers have experienced problems with sale and rent back in Annexe L.
- 5.4 Such evidence is anecdotal in nature and it is hard to judge from a collection of reported incidents whether the problems in this sector are widespread. However, certain characteristics of the product, the industry, and the consumers who are likely to consider sale and rent back give us reason to expect that the types of problem listed above are likely to be recurrent in this sector.
- 5.5 In the following sections we discuss a number of inter-related features of this sector that suggest it is not working well for consumers. These features are:
- There are significant risks inherent in sale and rent back transactions. Consumers are not well placed to assess these risks, and do not appear to take account of the potential downside outcomes in making their decisions.
 - Many consumers do not shop around, which means that the market mechanisms (price competition, reputational effects) that deliver good outcomes for consumers in many markets are weak or absent.
 - Consumers are often in pressured situations and do not appear to be making balanced and informed choices about sale and rent back compared to other options. They may be open to persuasion by sales people even where sale and rent back is not in their best interests.
 - Sale and rent back is for most people a one-off transaction, which means there is little scope for learning effects. Furthermore the detriment to individuals can be severe.
- 5.6 We then go on to discuss what the extent of detriment in the sector might be.

Assessment of risk

- 5.7 At a high level, sale and rent back involves a consumer foregoing a significant amount of equity in the home (perhaps tens of thousands of pounds) in exchange for a promise that they will be allowed to stay there. There is an inherent tension in this proposition in the sense that, once the buyer owns the property, their incentive to deliver on that promise is greatly reduced. Even firms which are well intentioned at the time of entering into the deal may find, for example, that their financial circumstances change and they may have strong incentives to act in a manner that is contrary to the consumer's interest later on.
- 5.8 This tension is common to many products, particularly in the financial sector (for example savings and investments) where an upfront sum is given over in exchange for a promise of future benefits. Many such products are, however, tightly regulated and/or covered by comprehensive compensation arrangements, so that consumers' exposure to the risk is greatly reduced.
- 5.9 In the case of sale and rent back, the risks include:
- The risk of eviction if the landlord defaults on the mortgage, perhaps together with the loss of money held by the landlord as deposit or pre-paid rent.
 - The risk of eviction if the landlord chooses to regain possession of the property after expiry of the fixed term of the AST.
 - The risk of unexpected increases in rents after expiry of the fixed term of the AST.
- 5.10 It seems clear that these risks are not always disclosed to, or understood by, consumers. Most consumers interviewed by our researchers were left with the firm impression that their tenancy would be unlimited. Furthermore, consumers did not necessarily realise that the buyer was not purchasing for cash and that the property would be mortgaged and therefore capable of being repossessed by a lender.

- 5.11 However, even where consumers are made aware of the short-term nature of the tenancy agreement, we believe that they are not always well placed to take account of these risks.
- 5.12 Some customers may back away from sale and rent back because of these risks. However others do proceed, and we do not believe that they do so having taken full account of the risks. Our research indicates that, where the short-term nature of the tenancy was disclosed, people tended to regard it as a 'formality'.
- 5.13 With reputational effects weak in this sector - as discussed below - it is not obvious how consumers could be expected to assess the risk that a sale and rent back firm or landlord may go bust, or tell the difference between firms which are well intentioned and 'rogues'.
- 5.14 Furthermore, there is a significant body of research which confirms that consumers have difficulty understanding and assessing risks in relation to financial products generally. For example, FSA research shows that people often have misconceptions when it comes to financial products, citing for example that 40 per cent of people who own an equity ISA are not aware that its value fluctuates with stock market performance.⁸ Other research found that sub-prime mortgage customers tended to focus on how much they could afford rather than taking account of risk factors such as interest rate rises or unemployment.⁹ Our consumer research suggests that some sale and rent back consumers do not attempt to compute even the basic aspects of the transaction – quite a few had decided to go ahead with sale and rent back without looking at the sums involved.
- 5.15 In summary, the sale and rent back proposition involves risks that are in many ways analogous to those in other financial products, only without the regulatory safeguards that have been put in place for other products.

⁸ FSA, Financial capability in the UK: Delivering Change, 2006

⁹ FSA, Mortgage Effectiveness Review: sub prime and lifetime findings – research report, March 2008.

We believe that many consumers cannot and do not take full account of those risks when entering into sale and rent back transactions.

Shopping around

- 5.16 Our research supports what a number of firms had told us – that some consumers shop around when considering sale and rent back but that many do not. Of the people our researchers spoke to, although some customers contacted two or three firms, most only called one company. In some cases they had previously compared websites but these provided only limited information.
- 5.17 The lack of shopping around may be, in part, due to the time pressure under which many consumers investigate sale and rent back. Also some consumers may in reality have little choice – some of those interviewed had to contact several firms in order to find one which could make them an offer. However, even under less pressurised circumstances, consumers do not always shop around for financial products. For example, the FSA found that 33 per cent of people, who hold no more complex products than general insurance, bought their policy without comparing it to even one other product.¹⁰
- 5.18 The lack of shopping around has important implications for this sector. Where consumers do not shop around, we would not necessarily expect price competition to be effective. In other words, consumers might be receiving less for the purchase of their property, or paying more to rent it back, than should be the case in a competitive market.
- 5.19 Furthermore, sale and rent back firms told us that those consumers who do shop around do not necessarily do so on the basis of price but instead look for an adviser with whom they feel comfortable. While this is entirely rational in one sense – in an unregulated market it is crucial to deal with someone apparently trustworthy – it does mean, again, that there may be less competitive pressure on prices.

¹⁰ For example, 'Financial capability in the UK: Delivering Change', Financial Services Authority, 2006, page 1, ISBN 1-84518-418-1.

- 5.20 Lack of price competition means that some consumers may sell their property more cheaply than they need to. Given the sums involved, this is potentially a significant source of detriment. In a sense it is surprising that the sale price should be problematic – people sell homes all the time and the market in second-hand homes is generally competitive. Our research found that some consumers had a fairly good idea of the value of their property and did back away from sale and rent back firms when their offer price was too low. However, others had only a hazy idea of their property's value and were willing to take the word of the valuer supplied by the sale and rent back firm.
- 5.21 There may be a couple of factors behind this lack of focus on the purchase price. Sale and rent back consumers have other aspects of the transaction to consider - for example, whether they can afford the rent and the implications in terms of benefits - and may also be preoccupied with other concerns - such as dealing with existing debts or finding a way to remain in their own home - so may not focus to the same extent on the price offered. Also for many consumers interviewed by our researchers, the property in question was the only one they had ever owned. In cases where the property had been purchased from the Local Authority under Right to Buy they would not have bought it on the open market, so would have little experience of property market transactions.
- 5.22 The lack of shopping around also has implications for reputational effects in this sector. We believe there are some reputational effects - firms told us that they received a certain amount of business through referrals from existing customers, for example. However, it seems likely that reputational discipline is limited by the lack of shopping around, the fact that many consumers prefer not to discuss their situation with others and may be reluctant to disclose when things go wrong, as well as the fragmentation in the sector. In other words, we do not believe that reputation is sufficiently important in this sector to prevent firms from renegeing on aspects of their promises on occasion, or from otherwise exploiting vulnerable consumers.

Psychological aspects

- 5.23 The circumstances in which sale and rent back transactions take place mean that consumers do not necessarily consider the sale and rent back proposition dispassionately, or make a balanced and informed assessment of sale and rent back against other alternatives.
- 5.24 It appears that sale and rent back consumers may often be making a trade-off between the short run benefit of clearing their debts and the long run implications of the transaction. Generally, there is a well-documented tendency for consumers to be 'myopic', that is focused on short run gains rather than long run effects.¹¹ Research undertaken by the FSA suggested that sub-prime mortgage customers displayed this characteristic – though stating that although they were aware of risks, they did not appear consider longer-term issues.¹²
- 5.25 The failure to address the long term implications may lead consumers to enter into sale and rent back when it is not a sustainable solution for them, for example because they cannot really afford the rent. The analysis presented in Annexe C suggests that in half of the cases studies submitted by Citizens' Advice and other advice providers, consumers had problems making ends meet even after the transaction had been completed. Our consumer research also suggests that many consumers went ahead with sale and rent back arrangements even though the rent was higher than their mortgage payments, on the basis that their outstanding debts would be paid and they would worry about the rent later.
- 5.26 Consumers are often in difficult financial and/or emotional situations. This will further impair their ability to impartially and accurately assess the transaction against the alternatives. Our consumer research suggested that several respondents had noted that the depression or

¹¹ See, for example, Chapter 6 of Camerer, Loewenstein and Rabin, *Advances in Behavioural Economics*, Princeton University Press, 2004.

¹² FSA, *Mortgage Effectiveness Review Stage 2 Report*, March 2008.

anxiety that accompanied their financial problems made it difficult to think clearly or to evaluate possible solutions.

- 5.27 The majority of the negotiations take place with professional sales people and the more unscrupulous have the potential to play on the emotional or psychological aspects of the deal. For example, sales people may focus on what will happen if the consumer does not enter into the transaction and loses their home, and the limited availability of the deal. This aspect of regret can be very powerful, particularly when transactions are made in peoples home, where they are more vulnerable to persuasion.¹³ Our consumer research indicates that sale and rent back representatives may, typically, be very persuasive. In other cases, sales people put considerable pressure on customers, in one case threatening legal action when a customer wanted to pull out of a verbal agreement after a drop in the purchase price.
- 5.28 Deals can also take place very quickly and, in exceptional circumstances, the entire deal can be completed and signed at the first home visit.
- 5.29 In addition, there is some evidence to suggest that consumers do not always take good advice on the merits of the transaction. Our research also suggests that few consumers took independent professional advice. Consumers may also be reluctant to seek advice from friends and family. One of the attractions, to some consumers, of sale and rent back seems to be that it disguises the fact that they are in financial difficulty. Many people who spoke to our researchers said they were reluctant to talk about their difficulties, even to their friends and family, and tried to deal with the situation on their own. Of the respondents to the omnibus survey who had made enquiries about sale and rent back, over a third did not take advice from anyone, including friends and family.

¹³See, for example, 'Psychology of buying and selling in the home' Prepared for the Office of Fair Trading by the University of Sussex at Brighton, May 2004 (OFT716f), produced as Annexe F of 'Doorstep Selling', OFT, May 2004 (OFT716).

Learning effects

- 5.30 For the vast majority of consumers, sale and rent back will be a one-off transaction. Consumers are unlikely to have had previous experience of sale and rent back and may not know anyone else who has - or at least who is willing to talk about it - although increasingly it is possible that they may have been exposed to some media coverage about sale and rent back. This means that there is limited opportunity for learning effects in this sector – that is, consumers cannot be expected to learn from their mistakes, or the mistakes of others, and avoid making the same mistakes in the future.
- 5.31 Furthermore, the detriment when things do go wrong is potentially severe and may run to tens of thousands of pounds. As things stand, consumers have limited access to redress when this happens. The cost of 'mistakes' can be extremely high.

Extent of consumer detriment

- 5.32 This section considers the extent of the detriment in the sale and rent back market. In principle, this depends on the overall size of the sector, the detriment to individuals where transactions go wrong, and the proportion of transactions which do go wrong.
- 5.33 The size of sector is fairly small. We estimate that perhaps 50,000 transactions have been undertaken in total to date. Although we believe that the number of transactions is probably falling, we note that the sector is nonetheless likely to remain a comparable size to other regulated markets. As discussed in Annexe B, when home reversion plans were brought into regulation, only 1,500 transactions were made a year. Equity release in total (that is, including lifetime mortgages) accounts for around 30,000 transactions per year.
- 5.34 Moreover, where things do go wrong, the detriment to individuals can be severe. Although the number of transactions may decline going forward, the depth of the discounts, and therefore the potential severity of detriment, seems likely to increase.

- 5.35 Unfortunately it is almost impossible to assess how often transactions do go wrong. Clearly stakeholders such as Citizens' Advice and Shelter are concerned about the level of problems experienced, based in part on the number of the complaints they receive in relation to sale and rent back. And, based on the above assessment of the characteristics of the sector, our view is that this is a market in which problems can certainly be expected.
- 5.36 However there is very little quantitative evidence. We were unable to obtain a random sample of consumers to interview in depth about their experiences, so we cannot use the interview results to draw inferences about the frequency of particular problems experienced in the general population.
- 5.37 The omnibus survey did question a random sample of the population about sale and rent back. Of the 8,000 people questioned, only 24 had completed a sale and rent back transaction. Of these, 30 per cent were dissatisfied or very dissatisfied with their decision. However, this sample is too small for this to be taken as representative of the sector as a whole.

Conclusion

- 5.38 On the basis of the evidence we have found and for the reasons discussed above, we do not believe that the sale and rent back sector is working well for consumers. While we are not able to quantify the scale of the detriment in the sector, we believe most indicators point towards the conclusion that there is a material risk of severe detriment to a significant number of consumers.

6 CONCLUSIONS FROM PART 1: NATURE AND SCALE OF THE PROBLEM

- 6.1 The sale and rent back sector has evolved rapidly in recent years. It is difficult to collect evidence on the size of the industry, but it appears that some tens of thousands of transactions may have been undertaken to date. It is clear that the industry is highly fragmented, with individual traders participating as well as small and medium-sized firms.
- 6.2 Sale and rent back is developing in a variety of forms but usually involves giving up a significant amount of equity in exchange for a tenancy with limited security of tenure. There is a large amount of risk involved in these deals. They are often sold to vulnerable consumers in pressurised circumstances.
- 6.3 There are serious risks to consumers entering into sale and rent back transactions. These risks relate in part to unscrupulous or 'rogue' operators, who may be exploiting consumers in difficult situations in a largely unregulated sector. There are also firms which offer sale and rent back in good faith and supply consumers with a service which some find extremely valuable. Nevertheless, the current model requires the consumer to bear a large amount of risk, even where the firm is operating honestly and good faith.
- 6.4 In particular we have the following concerns:
- **Transparency:** Consumers may be misled about the sale and rent back deal. In particular, they may be given the impression that the tenure is more secure than it is. Consumers may also be misled about the market value of their home and the level of market rent.
 - **Suitability:** Even where there has been full and honest disclosure, consumers may be persuaded to enter into sale and rent back when it is not the most suitable option. They may be unaware of - or unable to make a good assessment of - the other options available to them, or vulnerable to high pressure sales tactics.

- **Product quality:** Even for those consumers for whom a product of this nature is appropriate in principle, current sale and rent back offerings place a high burden of risk on the consumer. The consumer is at risk of being evicted from the property after an unexpectedly short time period, either because the sale and rent back provider reneges on an understanding (whether explicit or implicit) that the consumer will be allowed to stay in the property for longer, or because the sale and rent back provider defaults on the mortgage and the property is repossessed by the lender. Our research indicates that consumers are ill placed to assess these risks – typically they are not financially sophisticated, may be reluctant to discuss the transaction with anyone other than the sales person, and may be under extreme financial and psychological pressure.

6.5 It is hard to gather quantitative evidence on the extent of the potential detriment – we do not know how many transactions are occurring, or what proportion may be problematic. However, the qualitative evidence we have gathered of consumer experiences in this sector, as well as the characteristics of the deals offered and of the industry, suggests that there is a material risk of detriment. Even if the number of transactions resulting in detriment is relatively small, the severity of the detriment in individual cases, both financial and psychological, can be very severe indeed.

6.6 Going forward, the sector will clearly be affected by the restrictions on lending, falls in house prices, and recent government initiatives to help consumers facing repossessions. It is not yet clear what impact these will have. It seems likely that fewer transactions will be conducted, but that those that do go ahead will involve deeper discounts or higher rents, leading to greater scope for consumer detriment for the individuals involved.

PART 2: SOLUTIONS

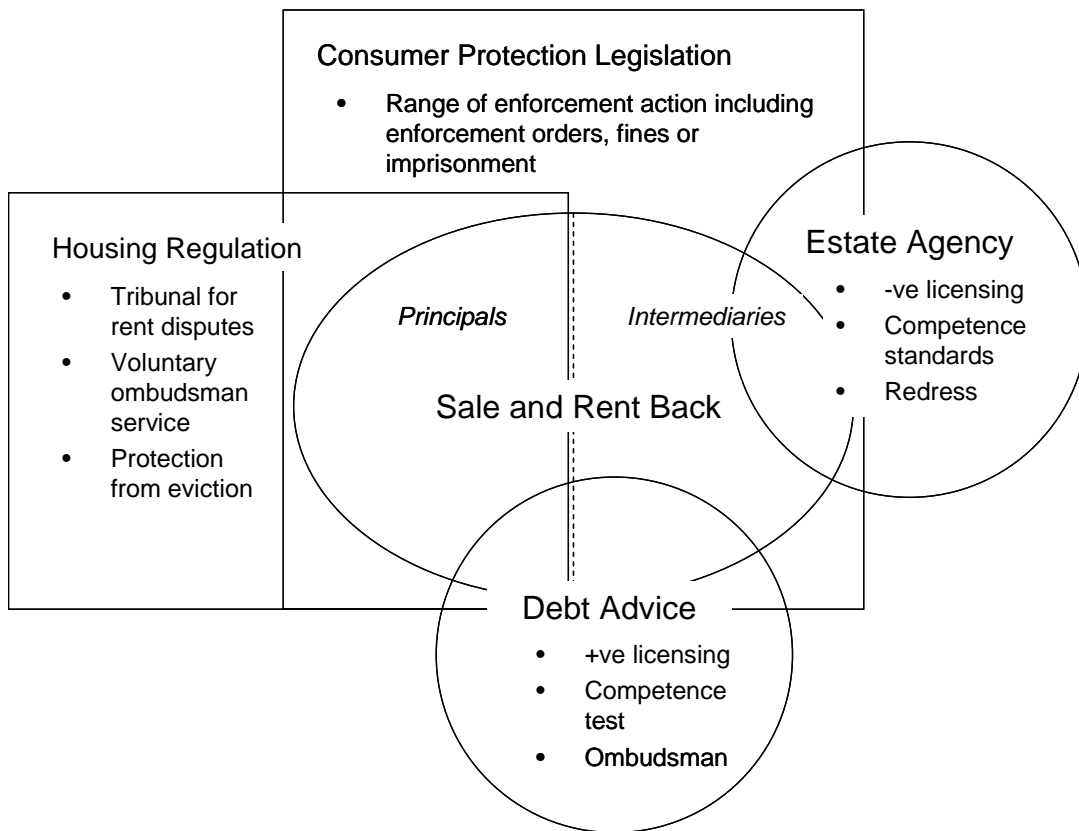
7 INTRODUCTION

- 7.1 Part 2 of this report considers potential solutions to the problems identified in Part 1.
- 7.2 Chapter 8 considers whether it is possible to do more within existing regulatory frameworks to protect consumers considering or entering into sale and rent back transactions.
- 7.3 Chapter 9 considers the potential for self-regulation to make this sector work better for consumers.
- 7.4 Chapter 10 summarises other developments underway that may offer further protection or assistance to sale and rent back consumers.
- 7.5 Chapter 11 presents our recommendations for further measures to address the problems identified.

8 SCOPE FOR FURTHER ACTION WITHIN EXISTING FRAMEWORKS

8.1 As explained in Chapter 3 (and Annexe F), there is, at present, no specific regulation of the sale and rent back sector. However, general consumer protection legislation applies, and there are sector-specific regulations that apply to any debt advice and estate agency activities undertaken by sale and rent back providers. Housing law also provides some protection against unfair practices by landlords, including increases in rent beyond market levels. Figure 8.1 illustrates the coverage of these frameworks.

Figure 8.1: Coverage of existing regulatory frameworks



8.2 In this Chapter we assess whether more could be done within these frameworks to address concerns over sale and rent back, and identify the gaps that remain.

Consumer Protection from Unfair Trading Regulations (CPRs)

- 8.3 As indicated above, the sales and marketing practices of traders offering sale and rent back fall within the ambit of the Consumer Protection from Unfair Trading Regulations (CPRs). The CPR regime provides for a number of bodies - including the OFT, Local Authority Trading Standards Services (LATSSs), and sector regulators such as the FSA - to take enforcement action against firms that breach the CPRs, for example by providing false or deceptive information to consumers.
- 8.4 A number of the practices of concern in the sale and rent back sector could breach the CPRs, for example statements misleading consumers as to the security of tenure offered under the rent back arrangement.
- 8.5 The OFT is reviewing the evidence that has come to light in the course of the market study, and will liaise closely with enforcement partners with a view to taking action against sale and rent back firms who may be breaching these regulations to the detriment of consumers - a successful enforcement action may be effective in sending a signal to all sale and rent back firms about unacceptable standards of commercial practice in the sector.
- 8.6 Nonetheless, we believe that there are limitations in terms of how far enforcement action under the CPRs can address the detriment identified in the sale and rent back sector:
- The CPRs offer some protection from misleading sales. However, they do not address the issues around the suitability of the product for individuals, or the risks inherent in the product as it stands. We have concerns about sale and rent back, even where it is honestly sold.
 - The CPRs do not provide for any rights for consumers to address specific problems in this sector - for example, pre-contractual disclosure of important information.
 - The CPRs allow for a court order to be obtained stopping the unfair practice or, if criminal action is taken, for firms to be fined but are

not designed to provide for individual or collective redress for consumers. We note, however, that the Regulatory Enforcement and Sanctions Act will make a wider range of sanctions available to those enforcement agencies who are deemed to be compliant with the Hampton better regulation agenda, which, in due course, could allow for restorative justice as an alternative to prosecution.

- The industry is very fragmented, and consumers may be reluctant to complain about a bad experience, which reduces the likelihood of finding sufficient evidence to support action against any one firm. Furthermore, firms who breach the CPRs may not stay in business for long, making successful prosecution more difficult.

Consumer Credit Act 1979

- 8.7 The Consumer Credit Act 1974 (CCA) requires most businesses that offer credit, lend money, or provide debt advice to consumers to be licensed by the OFT. The granting of a licence by the OFT indicates that the OFT is satisfied that the applicant is a fit person to engage in the activities covered by the licence. For further details, see Annexe F.
- 8.8 In terms of the activities that sale and rent back firms might be engaged in, the CCA covers debt adjusting and debt counselling. Where the debts arise under consumer credit or hire agreements:
- Helping people with their debt problems by taking over their debt or negotiating on their behalf is likely to fall into the definition of debt adjusting.
 - Providing advice to individuals about how to discharge specific debts is likely to be considered debt counselling.
- 8.9 The CCA does not apply to first charge mortgage contracts on residential property, which are regulated by the FSA. In other words, where sale and rent back firms are helping consumers discharge a first charge mortgage, they are unlikely to be subject to the CCA. However, where they help consumers discharge other debt, the CCA may apply.

- 8.10 Where a sale and rent back firm holds a licence, and gives poor debt advice, the consumer may have access to redress via the Financial Ombudsman Service.
- 8.11 We checked the names of 149 sale and rent back companies against the OFT's database of credit licences and found 17 matches. This indicates that perhaps 10-15 per cent of sale and rent back companies regard themselves as undertaking activities that are subject to the CCA.
- 8.12 On the basis of conversations with firms, we believe that other firms might be offering debt counselling without being aware of the requirements of the CCA. We intend to undertake some work to raise awareness among sale and rent back firms of the requirements of the CCA.
- 8.13 However, it is likely that many firms do not offer debt advice. It is also possible that others may choose to stop offering debt advice rather than apply for a credit licence. Even where sale and rent back firms do hold licences, the problems observed in the sector go wider than issues around debt advice. For this reason we believe there is very limited potential to address the problems in the sale and rent back sector through the CCA.

Estate Agents Act

- 8.14 The Estate Agents Act 1979 (EAA) applies to 'estate agency work'.¹⁴ Estate agency work is broadly defined as 'things done' in the course of a business following instructions from a potential buyer or seller of land (the client) (a) to introduce the client to a seller or buyer, and (b) after such introduction, to secure the sale or purchase of the land.
- 8.15 From the information we have seen it is possible that some sale and rent back businesses, those who operate as an intermediary between the seller and a buyer, may be engaging in estate agency work. However,

¹⁴ EAA, section 1.

since the EAA does not require those engaging in estate agency work to hold a licence, it is not straightforward to check whether sale and rent back intermediaries regard themselves as engaging in estate agency.

- 8.16 The EAA provides safeguards for members of the public buying and selling property. For example, those engaging in estate agency work must tell clients about fees and charges in writing and disclose any personal interest that they may have in the sale of a property on their books.
- 8.17 Where an estate agent breaches certain provisions of the EAA they can be banned by the OFT from doing estate agency work. Further to this under the Enterprise Act 2002, the OFT and its other enforcement partners such as Local Authority Trading Standards Services are also able to take action by means of court orders against estate agents who breach the EAA and harm the collective interests of consumers. Furthermore, as of 1 October 2008 all those engaging in residential estate agency work must belong to an approved redress scheme which will have the power to make a range of awards, including requiring a member to pay compensation up to £25,000.
- 8.18 We intend to undertake some work to raise awareness among sale and rent back firms of the requirements of the EAA. However, many in the sale and rent back sector are clearly not acting as estate agents and therefore the EAA does not regulate the sector.
- 8.19 It is possible that some intermediary firms may choose to avoid engaging in estate agency rather than join an approved redress scheme. Even where sale and rent back firms do regard their activities as covered by the EAA, the problems observed in the sector go wider than issues around intermediation. For this reason we believe there is very limited potential to address the problems in the sale and rent back sector through the EAA.

Housing law

8.20 Housing law may provide some protection against above-market rent increases (see Chapter 3 and Annexe F). However, the extent of the protection is limited – it applies only to the rental aspect, and affords sale and rent back tenants only the same level of protection as ordinary private tenants. In particular, there is no protection against unsuitable sales and neither is there any protection in cases where landlords default on their mortgage. Therefore we do not believe that housing law in itself is capable of fully addressing the problems identified.

Conclusions and recommendations

8.21 The CPRs, the CCA and the EAA all have some application to sale and rent back products. Housing law may also provide some protection.

8.22 However, the CCA and the EAA provide very limited protection as they only apply to a subset of sale and rent back operators and transactions, and are not specifically designed to address the concerns in the sale and rent back industry.

8.23 The CPRs and housing law do cover the whole industry, and are designed to address some of the conduct which has been identified as a concern in this sector, such as pressure selling and misleading statements on the security of tenure, or unfair increases in rent.

8.24 There is some potential for enforcement action under the CPRs to send a clear signal about unacceptable practices and to have a deterrent effect on such conduct. The OFT will investigate and take appropriate action where it has evidence that a firm is breaching these regulations to the detriment of consumers. We will also work with other enforcement agencies, notably local authority Trading Standards Services, to raise awareness of the issues we have identified in the sale and rent back sector and to encourage them to take appropriate action in local markets.

- 8.25 However, we do not believe that, even following successful enforcement action, the deterrent effect of the CPRs and the protection afforded by housing law would be sufficient to prevent potentially extensive consumer detriment in the sale and rent back sector. The fragmentation of the industry limits the effectiveness of ex-post enforcement action as a deterrent. We have also identified other concerns in the sector, such as the suitability of the product and the high level of risk it poses to sale and rent back consumers, which are not obviously covered by this legislation. Furthermore, even where firms have breached the CPRs, the regime as yet offers no redress to consumers, who may have suffered severe financial or psychological detriment.
- 8.26 For these reasons we believe the risk of extensive consumer detriment associated with sale and rent back would be more appropriately addressed by introducing a sector-specific regulatory framework, than by action under general consumer protection law, or piecemeal action under the CCA or EAA. We discuss the possibility of sector-specific regulation in more detail in Chapter 11.
- 8.27 Nonetheless, there are a number of actions that the OFT is taking, or intends to take, under the existing regulatory frameworks:
- The OFT is currently reviewing the evidence that has come to light in the course of the market study and considering whether any of this evidence is strong enough to form the basis for enforcement action.
 - The OFT will work with other agencies that enforce the Enterprise Act (notably LATSS) to ensure that they are aware of our concerns around the sale and rent back sector, and of the potential for taking action under the CPRs against sale and rent back operators.
 - The OFT will raise awareness among sale and rent back firms of the requirements of the CCA and EAA and look to take action as necessary where we find evidence that firms are failing to comply with these requirements.

9 SELF-REGULATION OF SALE AND RENT BACK

9.1 Many sale and rent back operators are concerned about standards in the sector, and about the reputational effects on the sector of the activities of rogue or unethical operators.

9.2 In recent months, a number of self-regulation initiatives have emerged, introduced by the trade associations described in Chapter 2:

- In August 2008 the NLA launched a consultation on a code of practice for the rent back sector, to be operated by NASARB.
- PROBAS has developed a code of conduct and standardised offer document. It also requires its members to post a bond against future compensation claims.
- The RBCA has published a code of conduct, membership agreement and standardised certificate of terms.

9.3 We estimate that the members of these organisations account for perhaps 20 per cent of the estimated 50,000 sale and rent back transactions to date.

9.4 These initiatives are all relatively new, and to varying degrees still in development. It remains to be seen how self-regulation will move towards a steady state for membership and possibly consolidation of industry groups, and how the substance of the proposals will develop.

9.5 In principle, however, we welcome these initiatives and look to self-regulation to provide industry-driven solutions to some of the difficulties facing this sector. In particular, we believe that self-regulation could achieve significant improvements in the following areas:

- Transparency, for example by developing minimum standards for documentation, or pro forma documents, that set out the terms of a sale and rent back agreement clearly, to help consumers understand the offer being made to them, and to provide a record of that deal. PROBAS and RBCA have already developed documentation along

these lines. We anticipate that such 'key facts' documents might cover, at a minimum:

- the valuation of the property
 - the offer price and discount
 - the rent payable, and how subsequent rent increases will be determined
 - the terms and conditions of the tenancy
 - any fees payable
 - any retentions or deposits
 - the identity of the landlord, and
 - the risks to the consumer's security of tenure
- Independence of professional advice, for example a commitment to advise consumers to seek independent legal and debt advice and an independent valuation, or where these services are provided to do so on an independent basis.
 - Reducing the risks in the product, for example by requiring member firms to enter into a binding commitment not to terminate the tenancy at no fault to the tenant.
 - Complaints procedure, for example a role for the industry association in resolving complaints that have not been resolved by member firms, and associated disciplinary procedure.
 - Development of 'lifeboat' schemes to facilitate the sale of property in the event that a landlord gets into financial difficulty, allowing the tenants to remain in place. We understand that there has been at least one case where the properties of a failing sale and rent back firm were sold on with the tenants in place.

- 9.6 However, we believe there are limitations to what self-regulation can achieve in this sector, particularly with regard to coverage and enforcement.
- 9.7 It is unlikely that reputational effects are strong in this sector. Our research suggests that, while some consumers do shop around, it is more common for consumers to talk to just one company, or perhaps to approach a second only if negotiations fail with the first. In other cases people are approached by sale and rent back firms rather than seeking out the service.
- 9.8 Furthermore, many consumers prefer not to discuss their situation with neighbours, friends or even family, as evidenced by the references to privacy and discretion in the marketing materials of sale and rent back firms, as well as by our consumer research.
- 9.9 One of the main differences between much of the sale and rent back sector and regulated equity release products is the circumstance in which consumers make their decision. Where consumers are taking a planning decision (as with regulated equity release) reputational effects can be powerful and self-regulation may achieve a high rate of coverage and impose a strong discipline on the sector. Where consumers are taking decisions in a crisis situation, however (as with many sale and rent back transactions) we believe reputational effects to be much less strong.
- 9.10 Given the lack of shopping around, the potentially secretive nature of the transaction, and the pressure under which decisions are taken, we believe that many prospective sale and rent back consumers will not look for a badge of quality, such as membership of a reputable industry association. Firms are therefore less likely to join such an association, and those that do may have a weaker incentive to abide by their rules, as both the cost of being expelled and the benefit from being a member are lower. Incentives to abide by rules will be further weakened as trade associations find it hard to police the rules in a fragmented industry, where many transactions are conducted face-to-face.

- 9.11 For these reasons, while welcome, we believe that that self-regulation will be limited in terms of achieving wide coverage or a strong disciplinary effect on the sector.
- 9.12 Furthermore, the initiatives emerging do not as yet adequately address the risks to consumers in our view. While we welcome 'lifeboat' schemes as a pragmatic way to deal with the consequences of failing sale and rent back landlords while continuing to serve their tenants, we do not believe that these will be workable in all circumstances. It may be difficult to sell on properties where sale and rent back tenants are paying below market rent, for example. Also, such schemes may run into difficulties if there is a common shock across the sector, such as a sharp increase in interest rates, that causes many landlords to get into difficulties at the same time.
- 9.13 With the exception of PROBAS, which represents the larger players, the self-regulation initiatives so far emerging do not require member firms to pre-fund redress or compensation arrangements to any significant degree, on the grounds that member firms are small and cannot be expected to bear such costs. Our view is that the industry must bear some additional cost to provide better protection for consumers, and we believe this requires compulsory measures.
- 9.14 In conclusion, the nascent self-regulatory efforts in the sale and rent back industry should play an important role in developing industry-led solutions to some of the problems experienced by sale and rent back consumers. However, we are sceptical about both the extent of coverage and the degree of discipline imposed by voluntary self-regulation in this sector, and concerned about the lack of redress and compensation. We believe that, to properly address the risks to consumers, compulsory measures are needed.
- 9.15 This view is shared by some in the industry - we note that PROBAS has been calling for FSA regulation of the sector, and that the NLA recently said that self-regulation could be a staging post en route to regulation.

10 OTHER INITIATIVES

10.1 There are various other initiatives underway across Government, regulators, and the voluntary sector that may offer further protection and/or assistance to consumers considering sale and rent back.

Initiatives on repossessions

10.2 The Government has recently launched a series of initiatives designed to help consumers who are in financial difficulty and facing repossession.

10.3 The Government recently announced a package of measures to address challenges in the housing market.¹⁵ This includes measures to help reduce the number of repossessions, such as:

- reforms to income support for mortgage interest (SMI) – by reducing the waiting period for SMI, and extending its availability, the Government hopes to prevent 10,000 repossessions (for further detail see Annexe E)
- funding for social mortgage rescue schemes – the Government hopes this measure will prevent a further 6,000 repossessions (for further detail see Annexe H).

10.4 In April 2008, the Chancellor and the Housing Minister met with the Council of Mortgage Lenders (CML) and the Finance and Leasing Association (FLA).¹⁶ The industry agreed to review its voluntary arrangements for supporting borrowers facing difficulties, including such steps as restructuring payments in the short term where appropriate, pro-actively identifying at-risk borrowers facing repayment problems, and strengthening links with debt advisers. The CML and FLA are preparing best practice guidance for lenders later this year.

¹⁵ www.communities.gov.uk/news/corporate/950558

¹⁶ www.hm-treasury.gov.uk/newsroom_and_speeches/press/2008/press_44_08.cfm

- 10.5 In May this year, the Government announced a £10 million package of measures to support home owners who may be facing difficulties with their mortgage including:¹⁷
- Strengthening the capacity and expertise of the National Homelessness Advice Service.
 - New arrangements with the Ministry of Justice to ensure that households at risk of repossession have access to free legal advice and representation at county courts throughout England.
 - More specialised training for CAB staff and local authorities, to provide tailored, comprehensive financial advice for consumers.
- 10.6 In August this year, FSA warned it would take action against lenders who were too aggressive to customers in arrears. This followed findings in a 'thematic review' that concluded that some specialist lenders were not complying with FSA requirements in such circumstances.
- 10.7 The OFT is part of a working group with BERR, HM Treasury, FSA, DCLG and MoJ set up in May 2008 to investigate the issues and drivers of poor outcomes (often repossession) for second charge mortgage holders who are over-committed.
- 10.8 The Civil Justice Council is also working on a pre-action protocol for mortgage possession cases, to help to ensure that all reasonable steps are taken to avoid court proceedings.

Initiatives on financial capability

- 10.9 In addition, Government and the FSA are working to improve levels of financial capability in the UK. The FSA leads the National Strategy for Financial Capability and aims to reach 10 million people by 2010/11. The Government and the FSA have taken a number of steps towards increasing general financial capability.

¹⁷ www.hm-treasury.gov.uk/newsroom_and_speeches/press/2008/press_44_08.cfm

10.10 In March 2008, the Thoresen Review, an independent feasibility study commissioned by HM Treasury to research and design a national approach to generic financial advice, published its final report. This set out a high-level blueprint for a national Money Guidance service, accessible via the telephone, internet and face-to-face. The Government accepted the central recommendation for a pilot or 'pathfinder' of the Money Guidance. This is being jointly funded and delivered by HM Treasury and the FSA. In July, Government and the FSA announced that the pathfinder would launch in the North West and North East of England from early 2009.

10.11 'Helping you make the most of your money – an action plan for financial capability', published in July this year, also set out measures from Government, the FSA and its partners to help people to better manage their finances. In addition to plans for the Money Guidance pathfinder, the key initiatives outlined in the plan include:

- A one-stop-shop for impartial information and support on money matters, based around the FSA's Moneymadeclear website and consumer helpline, to be promoted widely this October.
- Support for delivering personal finance education in schools, through the FSA's £16m Learning Money Matters programme and the Government's new £11.5m programme, called My Money.
- A range of programmes to support people in dealing with their finances at key stages or events in their lives, plus work targeted at hard-to-reach or vulnerable groups.

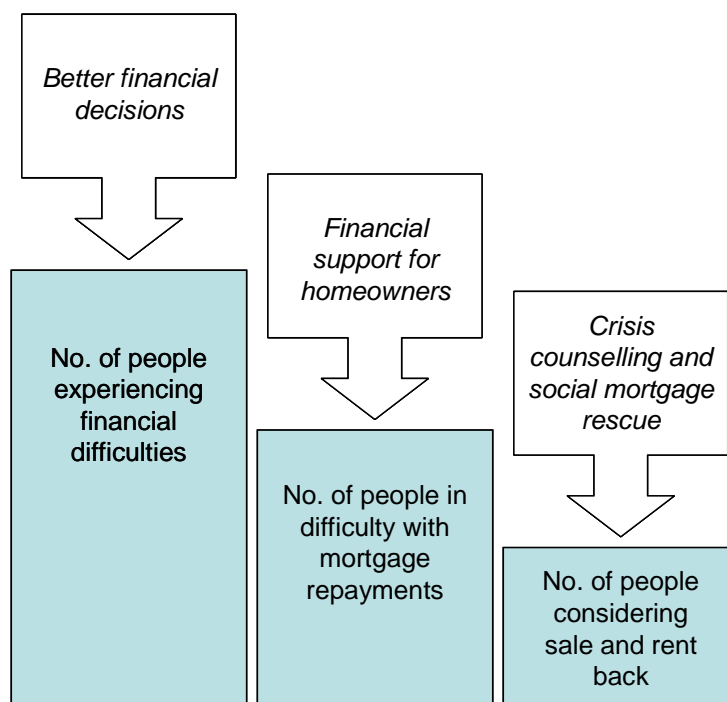
10.12 The National Housing Advisory Service will shortly publish a new advice leaflet for home owners, pulling together the contact details of major national money, debt and legal advice agencies into one document. The leaflet will be distributed by local authorities, CAB, Shelter, and money advisers.¹⁸

¹⁸ www.communities.gov.uk/news/housing/895029

Conclusions

10.13 The effect of these initiatives should be to drive down the number of people who get into a position where they would consider sale and rent back, as illustrated in Figure 10.1.

Figure 10.1: Effect of initiatives on repossessions and financial capability



10.14 This is by far the best way to address concerns about sale and rent back – by preventing people from getting into stressful and pressured financial situations in the first place. We therefore welcome these measures to help people find timely solutions to financial problems.

10.15 We expect that these initiatives, particularly the measures designed to prevent repossession, will have a significant impact on demand for sale and rent back. However, these initiatives will erode but not eliminate that demand. In particular, we do not expect provision of social mortgage rescue on the scale envisaged to completely (or even largely) crowd out private sector sale and rent back offerings.

10.16 Increasing access to crisis counselling should help people take better decisions when in financial distress. However, it is possible that still more needs to be done to encourage those considering sale and rent back to take advice.

11 RECOMMENDATIONS

11.1 The research and analysis presented in the preceding chapters lead us to conclude that the potential for severe consumer detriment in connection with sale and rent back is unlikely to be adequately addressed through existing consumer protection, broader Government initiatives, or voluntary self-regulation of sale and rent back. In this Chapter we set out our recommendations for further action to address potential consumer detriment in this sector. We recommend:

- Compulsory regulation as the primary means of addressing the potential detriment in the sector.
- Increasing consumer awareness of the risks around sale and rent back, particularly in the short-term before regulation comes into place.
- Greater clarity around the eligibility of sale and rent back consumers for housing benefit.

Regulation

11.2 As described in Part 1 of this report, we believe that consumers in this sector are at risk of entering into sale and rent back when this is not a suitable long term solution for them. Our research confirms that they are not typically well placed to make a balanced assessment of the risks associated with sale and rent back and the other options open to them. This difficulty is often compounded by a lack of transparency in relation to the sale and rent back agreement being offered.

11.3 However, we also believe that there are some consumers for whom a product of this nature is potentially a good option, but that the current offerings entail unacceptable levels of risk for those consumers. We find the risks to be unacceptable in terms of most consumers' ability to take account of those risks at the time of purchase - as indicated by our research but also by comparison with the levels of risk associated with other regulated products. For example, insurance contracts are regulated

even for those products where the potential detriment to the consumer may be relatively small. The potential detriment to a sale and rent back customer could be tens of thousands of pounds.

- 11.4 We believe that compulsory regulation is warranted, to ensure that consumers are not sold products with such high levels of risk without any controls on suppliers, or proper access to redress.
- 11.5 In this Chapter we set out how we envisage that regulation might address the problems we have identified in the sector. At a very high level, we believe that regulation could:
- provide some direct protection to consumers, for example by ensuring they have access to redress
 - raise standards across the industry, through a combination of vetting suppliers, and setting minimum standards for dealing with customers, and
 - Have a positive reputational effect that would give both consumers and other businesses (for example lenders and financial intermediaries) more confidence in dealing with the sector.
- 11.6 Another argument in favour of compulsory regulation for sale and rent back is that there are obvious parallels with equity release products, in particular home reversion schemes, which are already regulated by the FSA. Although there are important differences between the markets for sale and rent back and for regulated equity release, the risks associated with the two types of product and the potential severity of detriment are very similar.
- 11.7 Furthermore, our research suggests that some consumers are considering sale and rent back as an alternative to regulated equity release. For example, one person said 'I could go to an equity release company... but they only release 15 per cent or 20 per cent. I'd rather release the lot and put the money in the bank'. Some websites suggest that sale and rent back is a simpler or cheaper alternative to regulated equity release (see Annexe D). To the extent that there is an overlap in

potential demand, regulation would level the playing field in terms of competition between sale and rent back and equity release providers.

- 11.8 Box 11.1 summarises the background to regulation of equity release products. While we recognise that there are important differences between the sectors, we believe that there is potential for regulation to have a similarly positive impact on sale and rent back.

Box 11.1 Regulation of equity release products¹⁹

Equity release products are bought by those who, in planning for their retirement, wish to access the equity they have built up in their home, while continuing to occupy it. There are two main types of equity release – lifetime mortgages and home reversions.

In the early 1990s there was a misselling scandal around the generation of equity release products sold at that time, as both house prices and stock markets fell and elderly homeowners found themselves in negative equity. The self-regulatory body SHIP was founded in response to that crisis, with a 'no negative equity' guarantee as a core requirement for members.

Lifetime mortgages came under FSA regulation in 2004, and home reversions were regulated in 2007. Among the risks identified at this time were vulnerable consumers, mis-buying and mis-selling, security of tenure, and access to redress.

A recent market research report on equity release noted that 'While the time and cost of new regulations may result in a short-term disruption in business for some providers of reversion schemes, having a fully regulated market will undoubtedly have positive long-term implications. By helping to boost the public image and integrity of equity release schemes, there will be more confidence among consumers and advisors alike.'

More detail on the regulation of equity release products is provided in Annexe B.

- 11.9 If the Government accepts the recommendation to regulate, further work will be needed to develop and consult on specific regulatory proposals, and we do not wish to presuppose the outcome of that work in any way. Nonetheless, it is important that we set out in a broad sense how we believe regulatory measures can address the problems we have identified, and the following sections present our view.

¹⁹ Mintel, Equity Release, Finance Intelligence, May 2008.

Transparency and suitability

11.10 It is evident from our research and wider anecdotal evidence that standards of disclosure are inconsistent across the sector and in some cases inadequate. For example, the research identified some cases where fees and charges were not adequately disclosed, where customers did not get to see the contract in advance of being asked to sign, or where valuations or rental quotes received verbally were later discovered to be different from those in the documentation.

11.11 We believe that regulated standards of disclosure should be introduced. For example, firms could be required to provide a 'key facts' document setting out:

- the valuation of the property
- the offer price and discount
- the rent payable, and how subsequent rent increases will be determined
- the terms and conditions of the tenancy
- any fees and charges payable
- any retentions or deposits
- the identity of the landlord, and
- the risks to the consumer's security of tenure.

11.12 Similar measures have been introduced in relation to equity release products (see Annexe B), as well as many other products that the FSA regulates.

11.13 Improved disclosure should help some consumers better understand what they are signing up to, and should mean that consumers have a better record of the main features of the offer. However, we recognise

the limitations of mandatory disclosure as a tool for helping consumers make good decisions. For example, recent FSA research on consumer experiences in the sub-prime and lifetime mortgage sectors found that consumers saw the 'Key Facts Illustration' as a simple and easy to read record, but that it did not affect their purchasing decision.²⁰ We also recognise the dangers of providing consumers with too much information,²¹ but judge that at present most sale and rent back consumers are receiving too little rather than too much.

11.14 We remain concerned that consumers are vulnerable to being persuaded to undertake sale and rent back without full consideration of the other options available. For example, some consumers may decide to take a sale and rent back offer because they cannot face losing their home despite the fact that the rental payments are not really affordable on a long term basis and the right option would be moving to a more affordable property.

11.15 Chapter 5 presents evidence both from the consumer research we commissioned, and from academic literature, of the difficulties sale and rent back consumers are likely to have in making informed, balanced assessments of the options available to them and the associated risks. There are several well documented cognitive biases that are likely to come into play, for example myopia or hyperbolic discounting, whereby consumers fail to take adequate account of long term costs and benefits.²² Other features that give us particular cause for concern in this sector are the fact that consumers may be under significant pressure at

²⁰ FSA, second stage of the Mortgage Effectiveness Review, available at www.fsa.gov.uk/pages/Library/Communication/PR/2008/030.shtml

²¹ Better Regulation Executive and National Consumer Council, Warning: too much information can harm, November 2007.

²² Irlenbusch, Diane Reynier, LSE, '*Financial Capability: A Behavioural Economics Perspective*' Prepared for the Financial Services Authority, July 2008; and Camerer, Loewenstein and Rabin, *Advances in Behavioural Economics*, Princeton University Press, 2004.

the time of sale, and the fact that sales take place in the consumers' own home which typically adds to the pressure on the consumer.²³

- 11.16 Research suggests that crisis counselling can help consumers with financial decision-making, and that the best form of help is free and independent face to face counselling.²⁴ In addition to efforts to raise consumer awareness about sources and benefits of advice (discussed below), regulated firms could be obliged to set out clearly a recommendation that consumers take advice, and point to suitable sources of such advice. They could also be required to allow consumers sufficient time to obtain advice between making the offer and closing the deal.
- 11.17 We recognise, however, that persuading consumers to take up advice when they need it can be extremely difficult. Some of the firms we spoke to said that they already recommended that consumers take advice before proceeding with the transaction – some even put them in touch with a debt counsellor – but that many consumers did not take this up even when thus prompted.
- 11.18 An alternative approach would be to require sale and rent back providers to assess suitability at the point of sale, and not to proceed with the transaction where it is not in the customer's best interests (as is the case for regulated equity release). However, there are incentive problems with requiring a sales person to provide impartial advice, and there are

²³ See, for example, 'Psychology of buying and selling in the home' Prepared for the Office of Fair Trading by the University of Sussex at Brighton, May 2004 (OFT716f), produced as Annexe F of 'Doorstep Selling', OFT, May 2004 (OFT716).

²⁴ See for example information on the Face-to-Face Debt Advice Project, BERR, quoted at www.berr.gov.uk/consumers/consumer-finance/over-indebtedness/debt-advice/index.html and 'Evaluation of the Financial Inclusion Fund Face-to-Face Debt Advice Project, Final report for the stage one evaluation', Opinion Leader, June 2007. See also David de Meza, Bernd Irlenbusch, Diane Reynier, LSE, 'Financial Capability: A Behavioural Economics Perspective' Prepared for the Financial Services Authority July 2008.

calls for clearer separation between sales and advice roles in the financial services industry more generally.²⁵

- 11.19 Moreover, it would be extremely difficult to define objective criteria for suitability in this situation, against which firms could be held to account. Our consumer research confirms that people have a range of reasons for wanting to stay in their own home, from the practical to the purely emotional. Determining whether sale and rent back is 'suitable' for someone may, in many cases, be a highly subjective matter.
- 11.20 Since free, independent advice is available for consumers in financial difficulty from a range of sources such as Citizens' Advice, Shelter and the Money Advice Trust, and we understand that these organisations have the capacity and expertise to offer the right kind of advice to people considering sale and rent back, our view is that steering consumers towards such advice is likely to be a better option. We recognise, however, that encouraging uptake of advice will be difficult - we return to this subject below.

Reducing risk to consumers

- 11.21 We also believe that the risk for consumers entering into sale and rent back should be significantly reduced.
- 11.22 We believe regulation should require that the product offering be strictly in line with any assurances that firms give about security of tenure. Firms should not be permitted to offer consumers the right to stay in their homes 'indefinitely' or 'for as long as you need', unless they offer a product that actually confers this right, either through a secure tenancy agreement, or through guaranteed access to compensation if the tenancy is terminated at the landlord's initiative (through no fault of the tenant), including in the event that the firm is no longer trading. Similarly firms should not be permitted to distinguish between 'intended period of tenancy' and 'guaranteed period of tenancy' – if they offer to let people stay in their home for, say, five years, they should offer a tenancy

²⁵ FSA, Retail Distribution Review – Interim Report, April 2008.

agreement with a minimum secure period of five years, or guaranteed access to compensation for this time.

- 11.23 At present, most sale and rent back purchases are financed by standard buy-to-let mortgages, for which six or twelve month ASTs are standard. Some sale and rent back firms and lenders recognise that this is a problem for the sale and rent back sector but so far they have not developed a more tailored form of finance for the sector that would support a more secure offering. This is in part because, without regulation, they have not needed to do so. But also lenders have been unwilling to engage actively with sale and rent back, due to the reputational risk of dealing with an unregulated sector that has attracted considerable negative publicity.
- 11.24 Introducing regulation might push the sale and rent back industry and its lenders to develop a more appropriate financing model, capable of supporting both short term and long term tenancies. It should give lenders greater confidence in dealing with the sector.
- 11.25 In terms of what more secure tenancy agreements might look like, we can envisage a couple of options, though there may be other possibilities. Firms could offer assured tenancies (ATs), like social landlords and local authorities do. Alternatively, firms could offer an AST with a longer minimum period, such as five years, during which the tenancy could not be terminated without cause.
- 11.26 However, failing the emergence of finance for more secure forms of tenancy, regulation could provide other safeguards, notably ensuring that consumers have access to compensation in the event that they lose their home through no fault of their own:
- Firms could be required to offer redress if they do not deliver what was agreed to in terms of intended duration of tenancy and basis for rent increases. The transparency requirements should ensure that these terms are clearly set out.
 - To address the risk that the landlord defaults on the mortgage:

- sale and rent back providers could be required to obtain the agreement of their lender that in the event of default by the landlord at no fault of the tenant, they will sell the property on with the tenants in place, rather than repossess the property (a 'lifeboat' scheme), or
- firms could be required to join a scheme that pays out to compensate the consumer if the firm is unable to provide redress.

11.27 We recognise that any offering that gives more security to consumers is likely to be more expensive to provide. For this reason it will be very difficult to ensure that a requirement on firms to offer terms that match their promises - or alternatively to limit their promises to the terms they offer - is followed. It would be difficult to prevent operators offering six or twelve month tenancies, with paperwork to show that the consumer had signed up for this, yet where the consumer was assured verbally that the tenancy would be rolled over indefinitely.

11.28 For this reason we believe that it may be necessary to introduce a minimum standard for the product. For example, where the property is sold at a substantial discount (say, more than 10 per cent of the market value as assessed by a RICS surveyor), there could be a minimum period (say, five years) during which the consumer is automatically protected if the tenancy is terminated without fault, or if the landlord defaults on the mortgage. Echoing the discussion above, this could be achieved either through a minimum period for tenancy agreements, or through a minimum period during which regulatory safeguards would apply.

11.29 We recognise that a minimum standard would restrict the offerings available in a sector that currently serves people in a wide range of circumstances. However, shorter arrangements could still be offered where properties were purchased nearer market value - it is the depth of the discounts being offered in many cases that lead us to propose a minimum period during which the consumer would automatically be protected from the risk of eviction through no fault of their own.

Consultation would be needed to establish an appropriate calibration for the minimum standard.

- 11.30 We also recognise that any requirement which shifts some of the risks currently borne by consumers back onto sale and rent back providers and their lenders will increase the costs of providing the product, perhaps significantly.
- 11.31 The likely costs of regulation of sale and rent back can only be estimated when specific proposals are under consideration. However, by way of comparison, the FSA estimated that the incremental costs associated with regulating home reversion schemes would be fairly significant. Depending on the type of firm, estimates of the one-off costs ranged from £8,000 to £115,000 per firm, while ongoing costs ranged from £2,000 to £13,000 per firm per year. However, for other products the FSA has used lower cost approaches – its estimate of the incremental cost of regulation of Home Purchase Plans was £32 per product sold. (We discuss the relevance of these cost estimates in more detail in Annexe I.)
- 11.32 It is unclear whether the sale and rent back business model would be able to bear significantly higher costs in its present form – the firms are typically small and thinly capitalised. Our view is, however, that if sale and rent back is not viable when it offers a product that matches consumers' needs and their expectations (based on what they are told by salespeople), then it is not properly viable at all.
- 11.33 Moreover, it is likely that regulation would change the industry landscape, perhaps prompting some consolidation and the development of more extensive franchise or network operations (whereby member firms purchase compliance and other services from umbrella organisations). We consider that some professionalisation of the sector is desirable.
- 11.34 Annexe I discusses the likely impact of our recommendations in more detail.

Who should regulate?

- 11.35 To implement compulsory regulation, the Government could either amend the secondary legislation to FSMA to allow the FSA to regulate sale and rent back, or pass new primary legislation to establish a regulatory framework which could be implemented by a different, or a new, regulatory body.
- 11.36 We recommend that the Government amend the secondary legislation to FSMA to enable the FSA to regulate sale and rent back. The key advantage of this is the speed with which the change can be made. Changes to secondary legislation are generally quicker than new primary legislation. More importantly, the FSA already has regulatory frameworks in place for other products, with many of the components we propose for sale and rent back, for example disclosure regimes, redress and compensation requirements. It also has expertise in protecting consumers entering into complex financial transactions.
- 11.37 Furthermore, as discussed previously, the FSA already regulates equity release schemes, including home reversions, which have a number of similarities with sale and rent products. Although regulated equity release products are typically sold in different circumstances (for retirement planning rather than in financial crisis) our research indicates that the markets do overlap to some degree. There may, therefore, be advantages to a joined up approach that levelled the playing field between sale and rent back and equity release.

Consumer awareness

- 11.38 We believe there is limited scope to improve outcomes in this sector through educating consumers. Research on financial capability suggests that initiatives to inform and educate are likely to have a positive but modest impact, and that institutional design and regulation that takes account of consumers' psychology may be more effective in improving

financial decision making.²⁶ This is likely to be particularly true for people considering sale and rent back, who may be taking decisions very quickly and under great pressure. We therefore do not believe that measures to educate and inform consumers alone will be adequate to address the detriment in this sector.

11.39 Nonetheless, in the short term before regulation takes effect we believe there may be scope to raise awareness among prospective consumers of the risks around sale and rent back. Given the size of the potential detriment to each individual consumer (up to tens of thousands of pounds), an awareness effort that deterred even a limited number of unsuitable sale and rent back transactions could be worthwhile.

11.40 There is a large amount of research that indicates the best means of assisting customers in who are already in severe financial difficulty is through free face to face debt advice. Other forms of assistance (including telephone advice or self-help and education) are likely to have a much more limited effect.²⁷

11.41 We believe, therefore, that the key message to consumers considering sale and rent back should be that it is a risky product and that those considering it should seek advice. Attempts to provide detailed information on the risks of sale and rent back, and the alternatives people should consider, are likely to be much less effective.

11.42 We do not believe, however, that it is necessary to launch a standalone consumer awareness campaign on sale and rent back. The prospective sale and rent back consumers most at risk (for example, those in imminent danger of repossession) are typically hard to reach.

²⁶ David de Meza, Bernd Irlenbusch, Diane Reynier, LSE, '*Financial Capability: A Behavioural Economics Perspective*' Prepared for the Financial Services Authority July 2008.

²⁷ See for example information on the Face-to-Face Debt Advice Project, BERR, quoted at www.berr.gov.uk/consumers/consumer-finance/over-indebtedness/debt-advice/index.html and 'Evaluation of the Financial Inclusion Fund Face-to-Face Debt Advice Project, Final report for the stage one evaluation', Opinion Leader, June 2007. See also David de Meza, Bernd Irlenbusch, Diane Reynier, LSE, '*Financial Capability: A Behavioural Economics Perspective*' Prepared for the Financial Services Authority July 2008.

Nonetheless, efforts to reach them are already being made on a number of fronts by Government departments and voluntary organisations seeking to provide assistance and advice to people in difficulties with their money or their housing or both. For example, the FSA requires lenders to distribute an information sheet to customers as soon as they fall into mortgage arrears. This and other channels are described in more detail in Annexe J. It would seem feasible to incorporate the message on sale and rent back within these efforts.

- 11.43 We therefore recommend that Government ensure that it sends a clear and consistent message on sale and rent back through the various channels it has open to people facing housing and/or financial difficulties. The message should be that sale and rent back is a risky product and that those considering it should seek advice.
- 11.44 Annexe J describes in more detail the sort of awareness efforts we envisage.

Housing benefit guidance

- 11.45 As noted in Chapter 5, the issue of eligibility for housing benefit following sale and rent back arose in both the research we commissioned, and in a significant proportion of the case studies submitted by other organisations. We understand that the Department for Work and Pensions (DWP) is receiving a growing number of queries from local authorities on this issue. Problems arise when consumers undertake sale and rent back, having assessed the affordability of the rent on the assumption that they will receive housing benefit but, following the transaction, find they are not eligible. They may then be unable to afford their rental payments, and consequently face eviction.
- 11.46 The reforms to state support for mortgage interest (SMI) recently announced by the Government will, from April 2009, reduce the differential between the support available to homeowners on low incomes, and that available to tenants. (Details of the reform are provided in Annexe E). This is a temporary measure to be kept under review. While it is in place, it may reduce the number of transactions

predicated on the receipt of housing benefit. However, we do not expect this to resolve the issue entirely.

11.47 Eligibility for housing benefit is determined by the local authority based on individual facts and evidence, and on guidance issued by DWP. There is considerable complexity in the rules on eligibility for housing benefit where people have recently sold a property - details are given in Annex E - and local authorities are required to exercise a great deal of judgement in assessing such situations. Inevitably, this creates uncertainty for housing benefit applicants.

11.48 We recognise that this is a very difficult area for housing benefit guidance and for local authorities in making such assessments. We also recognise that local authorities cannot give any guarantees as to the outcome of a housing benefit application, before a sale and rent back transaction is undertaken. Nonetheless, we believe there may be scope to provide greater clarity as regards the eligibility of sale and rent back tenants for housing benefit.

11.49 We therefore recommend that DWP issue guidance concerning sale and rent back tenants' eligibility for housing benefit. This could, for example, involve specifying some 'safe haven' situations and/or some situations in which tenants would not be eligible.

11.50 We recommend that this guidance, in whatever form it takes, be disseminated to the sale and rent back industry and to advisers such as CAB and Shelter, as well as to local authorities.

Summary of recommendations

11.51 Our main recommendations are, therefore, as follows:

- The sale and rent back sector should be regulated by the FSA.
Regulation should cover:
 - Transparency – there should be clear disclosure of the basis for the valuation for sale, how rent is to be set, and the security of tenure.

- Advice – there should be a requirement to make consumers aware of sources of independent advice, and to allow time for advice to be taken.
- Reducing the risks to consumers – either by ensuring that firms offer more secure forms of tenancy, or providing regulatory safeguards such as guaranteed access to compensation.
- In the short term, Government programmes targeted at people experiencing financial difficulty over housing should include efforts to raise awareness of sale and rent back, with the key message being that it is a risky product and that those considering it should seek independent advice.
- DWP should provide greater clarity on the eligibility of sale and rent back tenants for housing benefit.

11.52 In addition, the OFT will work with the sale and rent back industry, local authority trading standards, and other stakeholders to raise awareness of the implications for sale and rent back firms of:

- The Consumer Protection Regulations
- The Consumer Credit Act, and
- The Estate Agents Act.