Reform of the Reform – ways to reduce poverty in old age and supplement retirement Incomes

A Report of the European Project Proceedings:

towards informing Irish and European policy engagement

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Editors

John Maher, Sebastien Clerc-Renaud, Doris Neuberger, Martina Eckardt,

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Executive Summary

In 2015, DG Employment and Social Affairs commissioned a research project to examine the potential for housing assets to augment retirement income in the European Union. This is against a backdrop of increased longevity, higher costs associated with pension provision, lower dependency rates, declining income replacement rates on retirement and fiscal pressures arising with respect to public pension provision. This conference held in May 2017 in Hamburg Germany provided a platform for presenting preliminary findings from research covering retirement provision, housing, demographics and policy options, primarily focusing on six countries in the EU. This two year research project is conducted by iff-Hamburg (lead partner), Waterford Institute of Technology, Queen's University Belfast, University of Rostock, Technological University Delft, Andrássy University-Budapest and LUMSA-Rome.

The conference involved academics, advocates and practitioners familiar with the project domains and also included representatives of commercial firms with experience of the market in several countries. The presentations dealt with issues of market attractiveness, potential household appetite for solutions, suitable consumer protection, conceptual awareness among all stakeholders, product development, provision of capital, market evolution, and regulatory matters. Contrasting perspectives were offered and cultural preferences were highlighted with respect to the provision of housing (renting/owning), mobility (staying/moving), equity release (selling/leveraging), and inter-generational disposals (lifetime, on death, in full, partial, not at all). Participants recognised the changing nature of housing needs over a lifetime, the nature and location of housing within a community, the size of the available housing equity and the associated release mechanisms as complementary factors, all having significance in personal financial planning for retirement.

Building on the insights shared at this conference, the research partners next will engage with stakeholder in their respective countries and each will also conduct one further national consumer focus group. A synthesis report will then be prepared and submitted to the Commission. Following due consideration, it will be published and made available electronically to all stakeholders.

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Panel 1 Synopsis

Real estate a good idea for old-age provision? Equity release schemes as a way out.

Speakers: Mr Ettore Marchetti (European Commission); Dr. Peter Hennecke (Univ. Rostock); Dr. Jörg Dötsch (Univ. Andrássy); Sebastien Clerc-Renaud (iff), Dr. Declan French (Queen's Univ. Belfast); Mr Friedrich Thiele (Dt. Leibrenten AG);

Moderation : Prof Dr Doris Neuberger (University of Rostock & iff-Hamburg)

This panel focused on the potential of Equity Release Schemes (ERS) to provide additional income in old-age. Ettore Marchetti (European Commission) started with a presentation of pension adequacy and need for private pensions in the EU. The latest Pension Adequacy Report from 2015 projected lower pensions, in spite of longer careers. Deep adequacy issues may develop in several countries and within certain groups of people, mainly women, the less-educated, and migrants. Although old-age poverty in the EU decreased, still 14% of people aged 65+ were at-risk-of-poverty in 2015. Pensions are key to reducing old-age poverty and ensuring that income is maintained after retirement. The share of pensions in household income is highest for elderly singles (mainly women). Due to an ageing population, public pension costs are rising. Whereas personal pensions are becoming more widespread, only a small fraction of the population is affiliated, and very few contribute substantial amounts. Saving for one's home remains by far the major way Europeans set aside for old age. Some ¾ of older Europeans own the home they live in and ownership is higher in poorer countries; however, within countries, poverty rates among older tenants are twice as high as among older people who own their dwelling. This means that the poor have fewer opportunities to increase their incomes using their properties. Nevertheless, there is some scope for reducing old-age poverty through schemes that allow turning one's home into income. In addition, for many middle-class people, reverse mortgages can help sustain income and consumption in old ages. There is risk, however, that supplementing state pensions with personal savings (pension, housing, including reverse mortgages) will increase old-age inequality. Moreover, we need to work towards making the schemes safe and affordable.

Sebastien Clerc-Renaud (iff) explained what an ERS is and how it differs from other ways of extracting equity, i.e. remortgaging and downsizing. These alternatives tend to be associated with high social and possibly financial costs. According to iff, ERS must be a financial service, a source of liquidity for the future (lump sum or regular payments), contain a strong entitlement to remain in occupation of the property, and rely solely on the sale of the property for (re-)payment of the funds released to be used as a retirement pension. There are primarily two forms of ERS: the Loan Model ERS (reverse mortgage, lifetime mortgage) and the Sales Model

ERS (home reversion). The loan model ERS enables homeowners to borrow money against the value of their property, without losing their ownership. In this form, the amount lent is recovered through the sale proceeds of the house. The sale model involves immediate selling of the house. Homeowners convert their house to cash by selling a part of or the entire property to the ERS provider, while retaining their rights to live in the house.

Peter Hennecke (University of Rostock) presented research he conducted with Pierluigi Murro, Doris Neuberger and Flaviana Palmisano on market conditions for ERS in the EU member states. They used statistical data to measure the growing need for additional old age income as a proxy for potential ERS demand and the feasibility of ERS based on the availability of debt-free houses and the development of the housing and mortgage markets as a proxy for potential ERS supply. The results show that there is considerable heterogeneity between EU member states. For instance, while a comparatively high need in Germany is not met by an equally high feasibility, the market conditions are more favourable in the Netherlands and the UK. In any case, ERS can only be part of the solution as they are only of interest to a rather small part of the population, i.e. the cash poor but house rich with no bequest motive. Unfortunately, for those in most need of additional income, i.e. low income households with subsequently even lower pensions, ERS is usually not applicable as these households generally do not possess high real estate equity that could be released.

Jörg Dötsch (Andrássy University Budapest) provided an overview of public policy options which affect people's decision to invest in private pensions and home ownership. The main fiscal incentives to increase private pension savings result from how taxation relates (1) to contributions to such schemes, (2) to the returns on investment and the accumulated funds and (3) to the benefits from these pension plans. In addition, personal pension schemes might also be (4) subject to social security contributions. Finally, (5) subsidies might be available to incentivize contribution in private pension savings. Furthermore there are wide ranging state interventions on the closely interconnected housing and mortgage markets as e.g. subsidization of the acquisition of new homes. There is an extremely wide variety of policy interventions across Europe. Regarding private pension schemes, for the six countries covered by the research project, there is quite a lot of variation in regard to tax treatment, with no two countries applying the same overall design. Housing policies among the six member states vary with respect to the importance attached to it by policy-makers, the division of responsibilities, and the focus on social problems. Overall, regarding design and use of policy instruments, member states cannot be compiled into homogeneous groups. One may condense – at the most – two groups: countries using policies that actively stimulate the mortgage markets and countries relying on rather conservative policies.

Due to these differences in both market conditions and policy frameworks, also the use of ERS differs considerably across EU member states. As an example of a developed ERS market, Declan French (Queen's University Belfast) presented the UK case. The equity release market in UK being dominated by the loan model (lifetime mortgages), is one of the most developed ones across Europe. Homeowners demand such products primarily to finance home or garden improvements (63%), followed by to pay debts (31%) and go on holidays (29%). Only 13% of customers need the funds to help with regular bills. However, the mandatory 'No Negative Equity Guarantee' reduces the loan-to-value ratio or the liquidity released. There is a need for better coordination across government with regards to policies on equity release. To ensure that those implementing policy changes have considered the impact on equity release, government and consumers, it is important for a department of the government to take a leading role in this area. Policymakers will have better insight on the use of equity release in fulfilling policy aims such as increasing retirement income or paying for social care if more efforts are spent on understanding the sector. Not many people in UK understand equity release completely or are aware of this financial product. Equity release schemes can become a regular source of income for people in retirement if there is more transparency about the mechanisms and tax implications of taking out ERS.

Finally, Friedrich Thiele (Deutsche Leibrenten AG) presented the German case as an example of a less developed ERS market. As provider of home reversion products, which dominate the small ERS market in Germany, he stressed the advantages of the Sales Model over the Loan Model ERS. First, a home reversion product completely covers the beneficiary for the economic risk of a prolonged lifespan, while in the case of a reverse mortgage this risk is not covered without additional insurance products. Therefore, the provision of lifetime mortgages is not attractive for banks. Secondly, since the beneficiary of a home reversion product is acting as the seller of the asset, there are no additional costs driving down the value of the annuity, which arise from uncertainty about the future property value faced by a reverse mortgage provider. In the early days of the last century, home reversion products in Germany were often used only in rural regions, when family-owned farms were passed on to the next generation or by selling the property to the church. Deutsche Leibrenten Grundbesitz AG, a real estate stock corporation, offers an institutional solution. As a first nationwide home reversion plan provider it uses the potential of widely diversified real estate portfolios.

Following this, the profitability and risks of the sale model were discussed. Since the Deutsche Leibrenten AG is owned by venture capital funds, their requirements on return on equity, which covers the customers' longevity risk, have to be met. Consumers have to be protected against the providers' default risk and the risk of living shorter than expected.

Panel 2 Synopsis

Theme : Equity Release – A tale of Five Countries , role models for a safe old age provision

Speakers: Dr. Carmen Friedrich (Chemnitz University of Technology), Dr. Joris Hoekstra (Delft University of Technology), Mr John Maher (Waterford Institute of Technology), Prof. Pierluigi Murro (LUMSA University of Rome), Mr Nigel Waterson (Equity Release Council)

Moderation: Prof. Dr. Martina Eckardt (Andrássy University Budapest)

The focus of this panel was on consumer attractiveness and demand for Equity Release Schemes (ERS) as well as on consumer protection. ERS are very complex financial products which demand a rather high standard of financial literacy from consumers. In this panel Joris Hoekstra (Delft University of Technology, Netherlands) presented the main findings regarding attitudes to homeownership and ERS as a way of equity extraction. These are based on 12 focus group interviews with consumers from six EU member states (Germany, the United Kingdom, Italy, The Netherlands, Hungary and Ireland) carried out by the researchers of the project 'Integrating Residential Property with Private Pensions'. The findings of these focus groups obviously differ between the various national contexts. Nevertheless, four main trends could be discerned. (1) growing awareness of the potential of, and the need for, releasing housing equity; (2) strategies to release housing equity are context-dependent; (3) the personal situation determines if, when and how much housing equity is released; (4) there is a need for more transparent and objective information on ERS.

Following this, safeguards and safety features from a consumer protection point of view were discussed. These were illustrated by reference to the experiences with consumer protection provisions in place in different EU member states, thus accounting for the differences in the market for ERS schemes as well as for differences in consumer protection in EU member states.

John Maher (Waterford Institute of Technology, Ireland) outlined the main differences between Loan and Sale Model ERS from a demand side perspective. Loan Model ERS, which are prevalent in Ireland, involves an individual or couple drawing down a loan which is secured on the property until the demise of one or both owners, typically after between 15 and 20 years. By retaining ownership, a consumer continues to enjoy a psychological benefit, not felt to the same extent under the Sale Model ERS. That involves ownership passing at the outset of the contract to a financial institution. The amount obtained by the consumer is principally a function of interest rates, the occupants' age and health, and the determinants of the value of the property (condition, quality of title and location, etc.). Consumers in Ireland must be supplied with financial services which meet their needs and are suitable for their circumstances. Since 2008, ERS products have been brought under the Central Bank's Consumer Protection Code and consumers must be advised of the consequences of equity release products and of the total costs including interest. Suppliers must make their clients aware of the importance of taking independent legal advice and explicitly warn the customers that there may be a negative impact on funding future needs. Issues which could give rise to consumer tension include family members receiving diminished bequests, interest roll up not being properly understood and the possibility of negative equity giving rise to a claim against other assets on death.

Pierluigi Murro (LUMSA University of Rome, Italy) explained that in Italy only one type of a Loan Model ERS is currently available. Providers are banks, credit institutions or financial institutions under the supervision of the Italian Banking Law. A recently introduced law in Italy about ERS, which resulted from joint cooperation of the Association of Italian Banks and Consumer Associations, includes the following regulations: prospectus of the maturation of interests, co-header of house for the spouse, period of reflection for heirs, agreement at the time of sale of the house, etc. What is still lacking is the right of ERS consumers to smooth the bank payment during their life, if necessary. In addition Consumer Associations in Italy stress the importance of financial education for the diffusion of these products and for consumer protection. This seems the more important as recent surveys document that in Italy levels of financial culture are among the lowest reported in the advanced economies both for adults and students.

Although the market is very small with only a few number of providers active, in Germany Sales Model ERS products are the preferred ERS as Carmen Friedrich (Chemnitz University of Technology, Germany) showed. The underlying legal arrangements are based on well-established rules of the German private law, like life annuity and charge on real property including life estate (Leibrente/Reallast mit Wohnrecht) and usufruct (Nießbrauch) and charge on real property (Reallast) which are combined. Neither banks nor insurance companies are in this market, which is dominated by private stock companies or foundations. These are not subject to special regulations or supervision by the German financial authorities, like the Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht). According to Dr. Friedrich, lack of transparency and safeguards in regard to payment default and insolvency of the provider are the main problems from a consumer protection point of view.

Finally, Nigel Waterson (Equity Release Council, UK) presented the evolution of ERS consumer protection in the UK, where there is the best developed ERS market so far in the EU. In contrast to Germany, the main focus there is on Loan Model ERS. In the UK, the guarantee of non-negative equity in Loan Model ERS is a most important feature of the product design to mitigate consumers' risks. However, this benefit comes at the cost that only a rather small amount of the value of a property can be retrieved in this way, making it not suited for providing a larger share of old-age income. Following some misselling scandals in the 1980s and 1990s, consumer protection regarding ERS has been substantially reformed in the UK. The Equity Release Council is a voluntary provider association, organizing most of the British ERS providers. It requires its members to adhere to additional product standards for selling ERS products, making sure consumers which are usually 55+ of age really do understand the complex products. In addition, before contract conclusion, advice by an independent financial adviser who is certificated for ERS products must be given.

Following a lively discussion, this panel showed that ERS are very complex financial products, with consumers in different member states preferring different types of ERS. In addition, financial consumer protection provisions not only differ significantly between the member states, but are of high complexity even within single member states. Following from this the following conclusions can be drawn:

- For ERS products to become more widespread, **providers have to develop innovative ERS products** which are much better comprehensible for the target group of older consumers.
- To increase consumer awareness, much **more public initiative is necessary to substantially increase financial literacy**, in particular tailored to the needs of elderly people.
- In the near future **neither a single market of ERS products** in the EU might arise **nor will substantial cross-border business** take place given the diversity of consumer preferences for ERS products and of consumer protection mechanisms in the EU member states.

Panel 3 Synopsis

Theme : Equity release schemes: characteristics of a good product?

Speakers : Prof. Donal McKillop (Queen's Univ. Belfast); Prof. Udo Reifner (iff); Mr Lennart Grabe (Hypotekspension Sweden); Mr John Moriarty (Seniors Money Ireland)

Moderation : Mr John Maher (Waterford Institute of Technology)

This panel dealt with the market structures and products and which currently exist or could be offered prospectively as a policy support to the goal of securing additional retirement income for individuals and households. Because household financial planning exists within a lifecycle that for many includes periods of family formation, employment or self-employment, raising children who later leave the family home, retirement and perhaps periods of social care, it is necessary to consider the affordability of different forms of housing and pension provision over that lifecycle. At present equity release schemes involve treating of households who have already accumulated equity in their homes who wish to release cash. A further cohort of the population consists of those individuals and households who have not commenced the process of pension provision nor committed themselves to the purchase of a home. This population segment might be served well by financial solutions which would afford them the possibility of providing both housing and a retirement income savings vehicle over their lifecycle.

John Maher (WIT) indicated that the search for solutions meant striking a balance between the mix of benefits sought by consumers, the returns sought by financial providers, the safety and soundness of the market sought by regulators and the socioeconomic policy goals sought by governments individually, and collectively through the European Union. Security of tenure in all cases is a fundamental benefit that consumers require.

He observed that due regard must be had to cultural factors as these represent strong forces regarding household purchasing behaviour of both housing and pensions. In order for suppliers to become involved in the market, there needs to be a level of latent demand and satisfying it should be economically feasible by (i) being affordable by customers, (ii) on a scale worthy of policy intervention and supplier engagement and (iii) capable of attracting capital. The State plays a role through a range of interventions including tax relief and other subsidies of payments made by individuals and households when paying for housing and saving for retirement and obtaining financial returns on such savings.

He also outlined a possible solution for individuals engaged in household formation typically in the 25-35 age cohort that would see them obtain a lifetime right to occupancy of a property while also contributing to an individual pension. This would represent a bundled product offering, and the payment to the supplying financial service provider would involve both rent and pension contributions. Rent levels would be lower than short term rentals based on the elimination of vacant periods, improved maintenance and more assured income levels associated with long term occupancy. Such a product would be attractive for individuals and households who otherwise have to forfeit the possibility of pension savings due to the high cost of property relative to modal incomes in society and the impact of macro-prudential considerations with respect to mortgage lending. From a supplier perspective, this offering would involve significant capital funding for example compatible with a pooled or collective investment governed by a residential property asset mandate.

Donal McKillop (QUB) reviewed the growth in equity release in the UK market as indicated, volume, number of suppliers and number of products. He examined the motives and choices households have in obtaining cash from residential property equity and the factors reported as influencing their decisions. He discussed two possible solutions that could contribute to retirement income provision linked to residential property. The first involves tax relief on housing acquisition being provided by way a contribution to a pension. This offering would also be aimed at the population segment which is buying residential property as part of the household formation process.

The second involves linking the loan liability on an equity release product to a regional house price index, thereby obtaining a desired *no negative equity* outcome. This option deploys a derivative contract and takes into account the regional nature of house price movements evident in residential property markets in the UK and elsewhere. This solution could mirror the higher level of equity release that is obtained in US markets and thus have the effect of altering the value proposition for consumers insofar as a more material enhancement of retirement income would be possible. There exists in the market a minimum equity release advance which suppliers believe is necessary to justify the costs and provide an adequate return. A higher proportionate release in turn could increase the number of properties across the valuation spectrum to which equity release might be applied.

Udo Reifner (iff-Hamburg) examined more a creative approach to obtaining the use of property assets through a collective ownership structure. This would allow an accordion like approach to expanding and contracting ownership through a unitised approach to the residential property assets. He questioned the policy emphasis placed on the outright ownership which exists in some countries, highlighting the empirical evidence offered by others such as Germany and Switzerland where household rental is a widespread phenomenon, and does not serve as an obstacle to prosperity and social cohesion.

It was acknowledged that mortgage credit does fill the role of inter temporal consumption transformation. However this possibility is not accessible to some medium and lower income groups as they cannot buy property using conventional mortgage finance. Thus a gap exists which policy development could address through reimagining the possibilities for retirement income and housing supply while retaining the intergenerational transmission that conventional ownership and inheritance offers.

John Moriarty (Seniors Money) reflected on experience obtained from over a decade of trading activity in equity release markets in Ireland Spain, New Zealand and Australia. Demand exists, particularly with a growing, ageing, and property owning population segment. In recent years, the supply of capital has shifted from bank and securitised sources to insurance providers who can match a long term investment with long term liabilities. Effective matching does depend also on a suitable prudential framework such as that which has evolved in the UK. There, market development has been facilitated by such treatment. A similar coordinated approach in Europe could contribute to market progression. The US policy approach to public assistance in mitigating negative equity risk has also proved beneficial and is worth examination, and perhaps replication. Overall market conditions are now seen as more favourable than any time since the financial crisis and renewed trading activity should follow as a result.

Lennart Grabe (Svenskhypotekspension AB) spoke about the development of the equity release concept in the Swedish market with initial offerings being guided by the SHIP framework originating in the UK. Consumer dissatisfaction with this basic model transpired. Now his company offers a product very much based on a UK equivalent with similar protections offered to customers as are provided by the UK Equity release standards and guidelines. Conceptually he views equity release essentially as an agreement to share the proceeds of a residence in return for a release either of a lump sum or a periodic payment. A no negative equity guarantee was viewed as a *sine qua non* of such a product offering.

Viewing equity release in terms of a conventional mortgage is damaging to suppliers as it distorts capital requirements, suggests a need for asset amortization, and triggers otherwise inapplicable borrowing considerations.

In the subsequent discussion, attendees encouraged the Panel to continue their work in examining proposals and expressed appreciation for the possibilities now presented. They supported the dialogue between participants coming from different discipline and different jurisdictions. In order to inform the empirical and conceptual dimensions of the project, the attendees were invited to communicate further reflections and observations to the research consortium, either to iff-Hamburg or to other consortium members

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Panel 1 : Thursday, 11 May 2017, 11:30-13:00h

Theme : Real estate a good idea for old age provision? Equity Release schemes as a way out.

Speakers: Mr Ettore Marchetti (European Commission); Dr. Peter Hennecke (Univ. Rostock); Dr. Jörg Dötsch (Univ. Andrássy); Sebastien Clerc-Renaud (iff), Dr. Declan French (Queen's Univ. Belfast); Mr Friedrich Thiele (Dt. Leibrenten AG);

Moderator Prof Doris Neuberger (University of Rostock and iff-Hamburg)

Demographic change and the growing problems of traditional old-age security systems have increased the need for additional private savings for old-age. However, this might be in conflict with private savings for homeownership. One way of mitigating this potential conflict could be to release the liquidity of the wealth incorporated in one's housing assets during old-age by so-called Equity Release Schemes (ERS). A homeowner may thus access the wealth accumulated in the form of his or her home, while being able to continue to live in it.

In this panel, we will aim to cover the potential of such products to provide additional income in old-age. We will start with a presentation of the EU pension adequacy and need for private pensions and an overview of ERS need and feasibility in different EU Member States. After a short overview of public policy options for private pensions and homeownership, and of what ERS is, we will look at the existing ERS markets in the EU. The UK case will be presented as an example of a developed ERS market, and the German case as an example of a less developed one.

The workshop will seek to answer the following questions:

- Do the EU pension systems provide adequate security for old age?
- What are the conditions for ERS in the EU Member States, measured by the need for complementary private pensions provided by ERS, and the feasibility of ERS given the current market situation?
- What are the public policy options which affect people's decision to invest in private pensions and home ownership?
- What is an ERS and how does it differ from other ways of extracting equity?
- How large are the existing ERS markets in the EU?
- What are the main features of the ERS markets in the UK and Germany and how do these differ?

Dr Peter Hennecke, University of Rostock

Abstract

The pension systems of EU member states are under increasing demographic pressure. Later retirements ages and lower replacement rates are inevitable to prevent (pay-as-you-go) pension systems from collapsing. Thus, the need to acquire additional old age income is high. Equity Release Schemes (ERS) might contribute to close the widening pension gap. ERS transform illiquid assets in the form of owner-occupied homes into liquid assets such as a lump sum payment or a regular income stream. The advantage of ERS in comparison to other ways of accessing the value of one's home, e.g. selling and moving out, is that it allows residents to stay in their home and area. Peter Hennecke presents research he conducted with Pierluigi Murro, Doris Neuberger and Flaviana Palmisano on market conditions for ERS in the EU member states. They used statistical data to measure the growing need for additional old age income as a proxy for potential ERS demand and the feasibility of ERS based on the availability of debt-free houses and the development of the housing and mortgage markets as a proxy for potential ERS supply. Their research shows that there is considerable heterogeneity between EU member states. For instance, while a comparatively high need in Germany is not met by an equally high feasibility, the market conditions are more favourable in the Netherlands and the UK. In any case, ERS can only be part of the solution as they are only of interest to a rather small part of the population, i.e. the cash poor but house rich with no bequest motive. Unfortunately, for those in most need of additional income, i.e. low income households with subsequently even lower pensions, ERS is usually not applicable as these households generally do not possess high real estate equity that could be released.

Dr Jörg Dötsch, Andrássy University Budapest

Abstract

What are the public policy options (fiscal incentives etc.) which affect people's decision to invest in private pensions and home ownership?

A decisive starting point of people's decision to invest in private pensions and home ownership is first and foremost the pension system, which differ considerably. Recently voluntary personal pension schemes play only a rather minor role in regard to coverage, which should be below 10% for most EU member states.

The main fiscal incentives to increase private pension savings result from how taxation relates (1) to contributions to such schemes, (2) to the returns on investment and the accumulated funds and (3) to the benefits from these pension plans. In addition, personal pension schemes might also be (4) subject to social security contributions. Finally, (5) subsidies might be available to incentivize contribution in private pension savings.

Furthermore there are wide ranging state interventions on the closely interconnected housing and mortgage markets as e.g. subsidization the acquisition of new homes or for renovating and enlarging private property or for adopting energy-efficient construction. There are different "Bauspar" schemes, subsidized mortgages, tax advantages for mortgage holders or, as in Germany, subsidies for personal "Riester pensions". Some states foster investment in private pensions and home ownership by providing financial advice or assistance and expanding forms of consumer protection by e.g. mortgage rescue schemes.

What are the key differences and similarities of these policies across EU member states (with focus on Germany, Hungary, Ireland, Italy, Netherlands, UK)?

There is an extremely wide variety of policy interventions across Europe. Regarding *private pension schemes*, for the six countries covered by the research project, there is quite a lot of variation in regard to tax treatment, with no two countries applying the same overall design. *Housing policies* among the six member states vary with respect to the importance attached to it by policy-makers, the division of responsibilities, and the focus on social problems.

Tax exemptions on housing-related investment or subsidies for housing-related activities vary. Overall, the countries covered pursue different aims, follow different traditions and apply different instruments and reveal more differences than similarities. A common reference point is the turbulent years of 2007/2008 which entailed similar macro-prudential measures such as bands for LTV ratios to lower the risk of mortgage lending. In almost every country there is a tightening of the regulation of mortgage lending. There are considerable differences between developed and dynamic mortgage markets on the one side, and more 'conservative' and less dynamic mortgage markets on the other side. Overall, regarding design and use of policy instruments, member states cannot be compiled into homogeneous groups. One may condense – at the most – two groups: countries using policies that actively stimulate the mortgage markets and countries relying on rather conservative policies.

Mr Ettore Marchetti, DG Employment & Social Affairs, European Commission

Abstract

The Ageing Report (2015) illustrates that recent pension reforms stabilised pension expenditure in the next decades. This financial stability was achieved through reducing coverage and benefits and increasing labour participation. The Pension Adequacy Report also monitors pension adequacy. The latest, also from 2015, projected lower pensions, in spite of longer careers. Moreover, there deep adequacy issues may develop in several countries and within certain groups of people, women, the less-educated, migrants.

The European Commission's objectives are

1. Reduce old-age poverty
2. Ensure that income is maintained after retirement

Pensions are key to both objectives. Although incomes drop after retirement, poverty decreases, thanks to pension's progressive nature that ensures lower inequality than among working-age people.

In addition to ageing, people are becoming more mobile. As young Europeans become more mobile, they may opt more easily for "portable" types of savings, such as personal pensions. The European Commission is also working towards making such pensions more secure and portable across countries. Self-employed people and workers on non-standard contracts would also need to develop supplementary pension savings. The European Commission is also working on extending social protection to all workers, with an eye to granting sickness and unemployment benefits and access to labour market measures, but also, in the longer term, pensions.

Now, whereas personal pensions are becoming more widespread, only a small fraction of the population is affiliated and very few contribute substantial amounts. Saving for one's home remains by far the major way Europeans set aside for old age.

The ECB households' finances and consumption survey revealed that a large proportion of people's net wealth is in property and often much of it is one's home. Some ¾ of older Europeans own the home they live in and ownership is higher in poorer countries; however, within countries, poverty rates among older tenants are twice as high as among older people who own their

dwelling. This means that the poor have fewer opportunities to increase their incomes using their properties. Nevertheless, there is some scope for reducing old-age poverty through schemes that allow turning one's home into income. In addition, for many middle-class people, reverse–mortgages can help sustain income and consumption in old ages.

There is risk, however, that supplementing state pensions with personal savings (pension, housing, including reverse mortgages) will increase old-age inequality. Moreover, we need to work towards making the schemes safe and affordable. All this, while pursuing our main policy goal of extending working lives to afford adequate statutory pensions for all.

Dr Declan French, Queens University Belfast

Abstract

Recent reforms to pensions have been motivated by a perception that current levels of pension saving are inadequate due to increased longevity and public expectations about living standards in retirement. Additionally, the UK government desires to reduce budget deficits. This has motivated the introduction of auto-enrolment of employees into occupational schemes or group personal pensions thereby increasing the numbers of those saving for retirement. Reforms to the level of the state pension from April 2016 are intended to reduce inequalities as well as to simplify the current complex means-tested system thus facilitating pension planning. However, commentators argue that most retirees with the exception of the low-paid and the self-employed will be worse off as a result.

Future legislation is likely to reduce tax reliefs enjoyed by higher rate taxpayers. Such a change would make accumulating pension wealth through housing more attractive at least for these individuals as the fiscal treatment of pensions would then be similar to the fiscal treatment of housing equity i.e. 'Taxed-exempt-taxed'.

High UK house prices (particularly in South East) and the high level of homeownership are conducive to the development of the ERS market. First-time buyers are finding it more difficult to get on to the property ladder but homeownership is still an aspiration for the majority of people. Government policy has focused on increasing demand but has done little to address planning restrictions on housing supply. Homeownership levels are thus expected to continue to decline. Any reduction in Stamp duty, Capital Gains Tax or Inheritance Tax would make saving for retirement by means of housing more attractive.

The equity release market in UK is one of the most developed ones across Europe. Equity release has great potential to take care of people's need in retirement. There is a need for better coordination across government with regards to policies on equity release. To ensure that those implementing policy changes have considered the impact on equity release, government and consumers, it is important for a department of the government to take a leading role in this area. Policymakers will have better insight on the use of equity release in fulfilling policy aims such as increasing retirement income or paying for social care if more efforts are spent on understanding the sector.

Not many people in UK understand equity release completely or are aware of this financial product. Equity release schemes can become a regular source of income for people in retirement if there is more transparency about the mechanisms and tax implications of taking out ERS.

Mr Friedrich Thiele, Dt Leibrenten AG

Abstract

When people discuss the proper measures for providing for their retirement years, it is well known that state pension schemes alone can no longer finance one's old-age requirements. In the end, the general public knows that private provisions are a must, in addition to state pension schemes. People are aware of this, whether or not they can actually finance such additional provisions with their private incomes. It is accepted both politically and socially, that for this additional provision, owner-occupied residential property is outstandingly suitable. Currently in Germany, significantly more than fifty percent of the population above the age of sixty-five owns residential real estate. Many retirees, however, are finding that their residential properties alone cannot close the gap between their inadequate state pension schemes and their daily cost-of-living expenses, even though they do not have to pay any cold rent costs. The reasons for this funding gap are, on the one hand, that the mortgage for the property did not leave any breathing room for building further liquid assets, such as life insurance or bond funds; and, on the other hand, that the property has very likely "aged", as well, and might, therefore, require some repair and/or renovation investment, meaning that the asset's recoverability cannot always be taken for granted. A third reason is that people often underestimate the cost of their old age needs. Aside from maintaining their accustomed standard of living, there are, inevitably, expenses for nursing services, property maintenance services, and/or senior-friendly property modifications. Most

property owners must bear these additional financial burdens on their own, because social benefits are not granted until the property assets are depleted. Therefore, for residential property owners, equity release products provide these owners their only chance to continue living in their familiar environment, as well as providing them with a comfortable economic status in their golden years. These equity release products also satisfy the issue of the owners' social relationships, as ninety-eight percent of residential property owners don't want to relocate in their later years, but prefer, instead, to continue living in their usual autonomous fashion, within their own residential properties.

In such cases, a home reversion product has some major advantages over a reverse mortgage. First and foremost, it completely covers the beneficiary for the economic risk of a prolonged lifespan. Secondly, the entire property asset is at the beneficiary's disposal, and since the beneficiary is acting as the seller of the asset, there are no additional negative costs driving down the value of the annuity. A reverse mortgage, on the other hand, has some significant disadvantages. A pension is based only on a low hypothecated value, and the risk of a longer-than-expected lifespan is not covered without additional products, such as payments into bond funds or life insurance in cases of early redemption. And a reverse mortgage is on the other hand simply a non-performing loan for the financing bank.

Now is the perfect time, therefore, to rediscover the German home reversion. In the early days of the last century, home reversions in Germany were often used only in rural regions, when family-owned farms were passed on to the next generation or by selling the property to the church. But there was never an institutional corporation using, as a real estate company, the potential of home reversion for retirement provisions, setting up interesting and widely diversified real estate portfolios. Deutsche Leibrenten Grundbesitz AG wants to open this market as "*first mover".* Close attention by politics and science to the home reversion´s potential for retirement financing will lead to higher transparency and acceptance of the product and to its developing its own market. An owner-occupied residential property can offer so much more than just "rent-free" living

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Panel 2 Thursday, 11 May 2017, 14:00-15:30h

Theme : Equity Release : A tale of five countries, role models for a safe old age-provision

Speakers: Dr. Carmen Friedrich (Chemnitz University of Technology), Dr. Joris Hoekstra (Delft University of Technology), Mr John Maher (Waterford Institute of Technology), Prof. Pierluigi Murro (LUMSA University of Rome), Mr Nigel Waterson (Equity Release Council)

Moderator : Prof Dr Martina Eckhardt, (Andrássy University, Budapest)

Aim & Structure

Panel D1.1 of the iff conference discusses the potential of Equity Release Schemes as an additional means to provide income in old-age by releasing illiquid wealth from home-ownership. That panel presents and discusses the current state of Equity Release Schemes.

In this panel, the focus is on consumer attractiveness and demand for Equity Release Schemes (ERS) as well as on consumer protection. ERS are very complex financial products which demand a rather high standard of financial literacy from consumers. In this panel we present the main findings regarding attitudes to homeownership and ERS as a way of equity extraction based on 12 focus group interviews with consumers from six EU member states. Next, the main differences between Sale and Loan Model ERS are outlined from a demand side perspective, before we turn to safeguards and safety features from a consumer protection point of view. This will be illustrated by reference to the experiences with consumer protection provisions in place in the United Kingdom, Italy and Germany.

Questions

The workshop will seek to answer the following questions by looking at experiences in different EU member states:

- Is releasing equity from home ownership an attractive means for additional old-age income for the elderly?
- What are consumers’ perceptions of ERS models?
- What are the main features of Loan and Sales Model ERS that are most relevant from a consumer’s point of view?
- What are the prevalent consumer protection regulations in place for ERS?
- What are the experiences with consumer protection in place regarding ERS?
- Are additional regulations for ERS necessary? If so, what form should they take?

- Do different types of consumers need different types of protection?
- Do different types of ERS providers (banks vs. insurance companies, for example) pose different challenges from a consumer protection point of view?
- What kind of consumer protection mechanism is best for ensuring trust in ERS?
- What role can consumer associations play in this respect? What advantage(s) might trade association have?

Mr John Maher, Waterford Institute of Technology

Abstract

In Ireland, aspirations relating to residential property have deep roots with individuals and families seeking to acquire and own their own homes during their working lives. However with the collapse in the supply of new homes since 2009, considerable growth occurred in the private rental sector. In addition the emergence of a sizeable mortgage arrears problem in the economic downturn led to reduced mortgage lending. This was coupled with the State largely exiting from the provision of new social housing due to budgetary constraints. More recently, house prices have recovered from the nadir experienced in 2009 and the negative equity experienced by some mortgage holders is steadily being mitigated. In addition, those who own their properties without any outstanding debt are once again being sensitised regarding the extraction of capital or income from their homes to augment their incomes. This situation exists in parallel to the pensions' scenario where less than half private sector workers have any private pension other than the *de minimis* amount provided by State social security. Thus many young adults which comprise the largest new household formation cohort face critical choices regarding paying for housing in the immediate future and making some provision for retirement. Early pension savings can benefit from compound returns over their working lives.

From a consumer perspective therefore, the opportunity for developing solutions which might offer acceptable outcomes for young and old exists. These would involve striking a balance between the elements which influence household resource allocation such as costs, tax treatment, value provided, risk, sustainability, housing tenure, and flexibility in changing circumstances. Meanwhile financial institutions and associated intermediaries can respond to market demand where acceptable returns can be obtained on capital, the new business acquisition costs and

servicing costs are predictable and affordable within a pricing structure that would deliver growing sales volumes. Strategic considerations also influence such firms in terms of market positioning, fit with organisational mission, compatibility with core competences and expertise, and contribution to the overall product portfolio. Lastly, State authorities can use fiscal policy to provide signals to the consumers and financial institutions regarding public preferences for initiatives in pension and housing markets. Policy can frame new incentives or restructure existing ones to stimulate effective use of finance by parties on the demand and supply side of these markets.

The current research project led by iff-Hamburg and involving researchers in Germany, UK, Italy, Netherland Hungary and Ireland represents an exploration of the financial, social, structural and behavioural space within which the design of such policy solutions can be undertaken.

Dr Carmen Friedrich (TU Chemnitz)

Abstract

Discussion of the following ideas.

"In the foreseeable future, there is hardly any potential for the German market

Equity release. There is a need for more potential security. "

In the first quarter of 2017 the current poverty and wealth report of the Federal Government was published. According to this, the poverty rate in 2015 is 15.7 percent. Poverty is particularly hard hit by pensioners. Here, the poverty rate rose by 49 percent between 2005 and 2015. The President of the Federation of National Solidarity in the relevant press conference predicts that: *"If we do nothing, the pension will have lost more than a fifth of its value by 2045!* The fact that the reforms so far, such as the Riester pension or the raising of the retirement age to 67, have flopped, is obvious. No one makes private pension provision. The second and third pillars of old-age insurance therefore are hardly relevant. "

Against this background, the question arises, whether the financial situation in old age can be improved by real estate capital release for consumption, at least for the property owning segment of the population,. According to the report on poverty and wealth, about 50 percent of private households owned residential property continuously since 2010. For more than 10 years, this supposedly great potential has been the target of credit institutions, insurance companies and

private sector companies to place products for real estate consumption. The development on the market shows, however, that over six banks and insurance companies have now ceased their business and only around 10 product providers are currently active on the market.

The active providers generally provide two kinds of products to people own their homes: the first is so-called reverse mortgage. In these cases, the owner of the property obtains a real-estate loan. The interest is deferred and the entire residual debt is, in principle, repaid with the sale of the property at the end of the contract. In the case of the second type of product, the "sales model", the property is transferred to a third party at the beginning of the contractual relationship, and the right to reside, the payments for more liquidity and other benefits for the former owner are secured on the title of the property.

The target group for these products are in particular retirees. In the last ten years and even today, this group consists of people born at the end of the Second World War or belonging to the first post-war generation. They are characterized by a particular economic orientation. They feel a desire epitomised as follows: "*Our children and grandchildren should obtain a better life"* and this affects their behaviour. They consider that the hard-earned property should be neither to be burdened by debt nor "*consumed*" and that "*No debts are to be passed on to the next generation.*" According to the author, this is the main reason for the fact that, in particular, the Reverse Mortgage portfolio has not yet caught on in the market as perhaps hoped. Only with a generation change does a change appear possible here.

This is different with products of the "sales model". Germany has tried and tested instruments that are well suited to "sales models": usufruct, lifelong property rights, real lasts secured as collateral, or claim to care for the elderly. These instruments are used to this day, especially in the countryside. For example, farms are overwritten on their own children, and the parents ensure their livelihood through usufruct, housing rights and a service charge on property. In the cities, for example, in patchwork families as well as in the management of inheritances, properties of the self-employed are increasingly being transferred to children and/or other heirs during the original owner’s lifetime and are burdened with the above-mentioned obligations.

A potential market segment for the consumption of real estate other than by family transmission consists of those people who do not wish to leave an inheritance to their heirs or have no heirs. For this target group, the author contends that there would be demand for products which not only guarantee lifelong living, regular payments and the maintenance of the property by third parties but also, in particular, the possibility to be provided in a senior or nursing home if necessary. "Sales models" with or without additional services are offered, among other things, by private corporations and foundations. As a matter of principle, these products also raise the question of price and performance ratios for consumers as well as sufficient and transparent information to compare products on the market. The suppliers of these products are not subject to approval or supervision by BaFin (the German Financial Regulator). This is why the answer to the question of consumer protection is at least as important as the level of demand.

Dr Joris Hoekstra Delft (University of Technology, Delft)

Abstract

In order to get a better insight into the attitudes and preferences of consumers towards releasing housing equity, the researchers of the project 'Integrating Residential Property with Private Pensions' have carried out focus groups in six EU-countries: Germany, the United Kingdom, Italy, The Netherlands, Hungary and Ireland. The findings of these focus groups obviously differ between the various national contexts. Nevertheless, the following four main trends can be discerned.

1. ***Growing awareness of the potential of, and the need for, releasing housing equity***

At many places in Europe, pension incomes are decreasing and care systems are getting less inclusive. As a result of this, more and more older people have problems to make ends meet. In these circumstances, releasing housing equity is increasingly seen as a viable option to increase the retirement income.

2. ***Strategies to release housing equity are context-dependent***

Older home owners can extract their housing equity in various ways: selling the house and moving to a smaller home ownership dwelling, selling and moving to a rental dwelling, letting out part of the dwelling, engaging in a sale-and-lease back construction or using a so-called equity release scheme (e.g. a reversed mortgage). The option that is preferred largely depends on the context: the housing market situation, the attachment to the current home, the quality of the current home, the health situation and the availability of suitable financial products.

3. ***The personal situation determines if, when and how much housing equity is released***

In addition to the contextual factors mentioned above, the personal situation of the older home owning household determines to a large extent if, when and to what extent this household is interested in releasing housing equity. For example, many older home owners do not want to extract all their housing equity. They want to keep a buffer in order to remain financially independent of their family and the state's safety net. In a similar vein, some older home owners with children want to pass on (some of) their housing equity to their children after they have died, thus limiting the extent of housing equity that can be released. Finally, there are older home owner that want to release housing equity in order to be able to help their children settling down and acquiring a home ownership dwelling (advanced inheritance). .

4. There is a need for more transparent and objective information on ERS

Older home owners generally don't have a good overview of the Equity Release Schemes (ERS) that are on offer on the market. The available products are seen as complicated, not very transparent and offering insufficient value for money. This is related to the fact that the providers of financial products are often not trusted. According to the consumers, a better government regulation of the ERS market is required. Moreover, there is a need for more objective and transparent information on ERS.

Prof. Pierluigi Murro, (LUMSA, Rome)

Abstract

Only one type of ERS is currently available in Italy: the presitito vitalizio ipotecario, which is qualified as a Loan Model. This product is a lifetime mortgages, a financing secured by mortgage of residential property that enables the owner to convert into liquidity part of the economic value of the property. It is structured as a medium or long loan contract between individuals aged 60 or older and banks, credit institutions or financial institutions under the supervision of the Italian Banking Law secured by first rank mortgage on residential property. According to this financial product, credit can be granted with annual capitalization of interests and costs, and reimbursement in a lump sum at the end of the contract. As such, this financial product is regulated by legislation (See Law of 2nd Dec. 2005, no. 248; Law of 2nd Apr. 2015, no. 44). The subscriber will not pay any costs during the contract period and the interests will be capitalized together with the capital. At the death of the subscriber either principal and capitalized interests

will be paid back to the bank by the heirs or the bank will proceed by selling the house that has been mortgaged by the bank.

What are the experiences with consumer protection in place regarding ERS? Are additional regulations for ERS necessary?

The recent law in Italy about ERS was the result of a joint job of ABI (Association of Italian Banks) and Consumer Associations. This is an example of good interaction among different associations and between these associations and politics.

This process of formation of the law directly impacts the consumer protection. All the observations of Consumer Associations are now in the law: prospectus of the maturation of interests, co-header of house for the spouse, period of reflection for heirs, agreement at the time of sale of the house, etc. For the next steps, the principal point that is not in the law is to give the possibility to smooth the bank payment during the life of the elder.

Finally, Consumer Associations suggest the importance of financial education for the diffusion of these products and for consumer protection. Over the last decade Italy too has witnessed the development of financial education initiatives by numerous public institutions and private entities. The absence of a national framework that cohesively denes training gaps, priorities and criteria for intervention has nonetheless limited coordination of the various initiatives and the exploitation of synergies. The increasingly complex financial choices that citizens must make in the course of their lives require levels of financial literacy that are often higher than those currently recorded among large swathes of the population. Recent surveys document how levels of financial culture in Italy are among the lowest reported in the advanced economies for adults and students. The aim of financial education is to help people enhance their financial competency.

Mr Nigel Waterson, (Equity Release Council-UK)

Abstract

About the Equity Release Council

The Equity Release Council is the industry body for the UK equity release sector, representing over

500 members, including providers, qualified financial advisers, solicitors, surveyors and other industry professionals. The Council is currently celebrating the 25th anniversary of when its Industry Standards were first introduced to establish a safe and reliable market for consumers aged 55 and over.

Recent trends

2016 saw the UK equity release sector reach a new landmark with annual lending surpassing £2bn for the first time.

The sector's rate of growth also more than doubled from 16 per cent in 2015 to 34 per cent last year.

In terms of customer numbers, equity release is currently the fastest growing mortgage market in the UK.

Equity Release in the UK

Equity release plans fall into two categories:

i. **lifetime mortgage** – the consumer retains ownership of the home while extracting funds either in a single lump sum, or in periodic smaller amounts up to the maximum limit agreed. Interest on the loan can be fixed or rolled-up.

ii. **home reversion plan** – the consumer can sell all or part of the value of the property in return for a cash lump sum and/or regular income, while retaining the right to remain in the property, rent free, for the rest of their life.

Products

Of the £2bn lending, this was made up of £1.23bn of drawdown products, £918.86m of lump sum mortgages and £3.43m of home reversion plans.

In 2016, lump sum mortgages increased their market share – accounting for 35% of the market, up from 29% in 2012.

However, drawdown products remain most popular: there were 17,882 taken out in 2016, a 19% increase from 2015.

Consumer protection

With its Statement of Principles and product standards, consumer protection is at the heart of the

Equity Release Council's operations, promoting high standards of conduct and practice in the provision of and advice on equity release.

For example, all Council members adhere to the requirement for all customers to receive independent financial and legal advice when taking out an equity release product. Product safeguards include: No Negative Equity Guarantee; the right to remain in the property for life or until the consumer needs to move into long-term care; right to port to another suitable property; and fixed or capped rate of interest for lifetime mortgages.

Extract from the Equity Release Council's consumer protection Standards put in place:

Statement of Principles

The Equity Release Council exists to promote high standards of conduct and practice in the provision of and advice on equity release.

Our members will –

- Ensure that all their actions promote public confidence in equity release as a potential retirement solution
- Act at all times in utmost good faith
- Communicate high expectations for equity release outcomes in all their dealings
- Ensure conflicts of interest are managed fairly and reduced to the lowest practical level
- Exercise due skill, care and diligence in all that they do and uphold the standards set out by their professional bodies at all times
- Always act with the best interests of their clients being paramount, treating customers fairly in all their actions.

Our provider and adviser members comply with the Financial Conduct Authority's (FCA's) rules governing the sale of equity release products. These rules include the requirement that all customers who buy equity release plans are fully advised by a qualified adviser.

In addition, our members have voluntarily adopted further safeguards. These are set out in our Rules & Guidance (www.equityreleasecouncil.com/standards/rules-and-guidance/) and are designed to give you confidence in our members and their products and services. These further safeguards include product standards and a requirement for all customers to receive independent legal advice when taking out an equity release product.

Product standards

Our product standards are set out below. Our members are only allowed to tell you that a product meets these product standards if it meets **all** of them. If you are offered or are considering a product that does not meet all of the standards, the product literature must explain which standards are not met, and give an illustration of the types of risk that this might pose for you.

Our product standards are as follows:

- For lifetime mortgages, interest rates must be fixed or, if they are variable, there must be a “cap” (upper limit) which is fixed for the life of the loan
- You must have the right to remain in your property for life or until you need to move into long-term care, provided the property remains your main residence and you abide by the terms and conditions of your contract
- You have the right to move to another property subject to the new property being acceptable to your product provider as continuing security for your equity release loan
- The product must have a “no negative equity guarantee”. This means that when your property is sold, and agents’ and solicitors’ fees have been paid, even if the amount left is not enough to repay the outstanding loan to your provider, neither you nor your estate will be liable to pay any more.

Independent legal advice

You may choose your own solicitor to carry out the legal work in connection with your plan. Before the plan is completed, your solicitor will be provided with full details of the plan, including the rights and obligations of both parties (you and your product provider) under the contract, should you choose to go ahead. Both you and your solicitor will be required to sign a certificate confirming that these rights and obligations have been explained to you and that you wish to enter into the plan.

Information about and explanation of your equity release plan

You will be provided with a fair, simple and complete presentation and explanation of your equity release plan. The benefits and limitations of the plan will be clearly set out, together with your obligations under the terms of the contract. You will be given information about:

- all the costs that you will have to bear in setting up the plan;
- the tax implications;
- what will happen if you wish to move to another property; and
- how changes in house values may affect your plan.

Approved November 2014

From the website: http://www.equityreleasecouncil.com/standards/

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Panel 3 Thursday, 11 May 2017, 16:00-17:30h

Speakers : Prof. Donal McKillop (Queen's Univ. Belfast); Prof. Udo Reifner (iff); Mr Lennart Grabe (Hypotekspension Sweden); Mr John Moriarty (Seniors Money Ireland), Mr John Maher (Waterford Institute of Technology)

Theme : Equity release schemes : Characteristics of a good product

Moderator: Mr John Maher (Waterford Institute of Technology)

Household formation and financial planning exists within a lifecycle of dependency/full time education, adulthood and full potential labour market participation, and retirement with non, limited or indeed continued full labour market participation. Equity release requires a convergence of pricing, value, risk, taxation, distribution, regulation, and an attractive benefit proposition relative to alternatives. Longer life expectancy, lower interest rates, house price inflation and fiscal pressures have rendered the objective of comfortable retirement income and consumption more problematic. Thus a search for fresh policy choices exists in Europe and elsewhere as society seeks solutions which could offer satisfactory outcomes in terms of savings accumulation, housing consumption, and capital decumulation over the lives of individuals and their households.

Aim & ***Structure***

In this panel we will discuss the parameters and variables which are critical for the development of such choices and explore some examples of emerging possibilities for market solutions and policy development. We will start with a presentation which sets household financial decision making in the context of lifecycle frame and positions market behaviour in the context of need fulfilment over the lifecycle.

Current market practice will be examined and pathways identified for further evolution. The pooling dimension of risk will be addressed and the mechanisms for sharing and bearing the risk will be investigated. Regulatory aspects of product provision will also be considered from customer and supplier perspectives, having regard to critical turning points in market progression.

Questions

- What are the financial elements involved in leveraging capital from an individual’s or household’s residential property?
- How could households provide for housing and retirement income in a complementary

manner?

- What risks must financiers and households manage in relation to housing capital accumulation or release?
- Is there a role for the State in contributing to risk management in this context?
- Is there a portfolio of solutions depending on when in the lifecycle, households decide on an approach to a synthesis between meeting housing needs and preparing for consumption in retirement?
- What are the critical regulatory issues and principles for current and prospective market development?
- Who could supply capital to this market and what does such supply now command?
- What are the salient features of an attractive market segment that would motivate entrants and competition?

John Maher (Waterford Institute of Technology)

Abstract

Views on residential property and retirement income from an Irish context

In Ireland, aspirations relating to residential property have deep roots with individuals and families seeking to acquire and own their own homes during their working lives. However with the collapse in the supply of new homes since 2009, considerable growth occurred in the private rental sector. In addition the emergence of a sizeable mortgage arrears problem in the economic downturn led to reduced mortgage lending. This was coupled with the State largely exiting from the provision of new social housing due to budgetary constraints. More recently, house prices have recovered from the nadir experienced in 2009 and the negative equity experienced by some mortgage holders is steadily being mitigated. In addition, those who own their properties without any outstanding debt are once again being sensitised regarding the extraction of capital or income from their homes to augment their incomes. This situation exists in parallel to the pensions' scenario where less than half private sector workers have any private pension other than the *de minimis* amount provided by State social security. Thus many young adults which comprise the largest new household formation cohort face critical choices regarding paying for housing in the immediate future and making some provision for retirement. Early pension savings can benefit from compound returns over their working lives.

From a consumer perspective therefore, the opportunity for developing solutions which might offer acceptable outcomes for young and old exists. These would involve striking a balance between the elements which influence household resource allocation such as costs, tax treatment, value provided, risk, sustainability, housing tenure, and flexibility in changing circumstances. Meanwhile financial institutions and associated intermediaries can respond to market demand where acceptable returns can be obtained on capital, the new business acquisition costs and servicing costs are predictable and affordable within a pricing structure that would deliver growing sales volumes. Strategic considerations also influence such firms in terms of market positioning, fit with organisational mission, compatibility with core competences and expertise, and contribution to the overall product portfolio. Lastly, State authorities can use fiscal policy to provide signals to the consumers and financial institutions regarding public preferences for initiatives in pension and housing markets. Policy can frame new incentives or restructure existing ones to stimulate effective use of finance by parties on the demand and supply side of these markets.

The current research project led by iff-Hamburg and involving researchers in Germany, UK, Italy, Netherland Hungary and Ireland represents an exploration of the financial, social, structural and behavioural space within which the design of such policy solutions can be undertaken.

Prof Donal McKillop (Queen's University Belfast)

Abstract

Globally by 2050 there will be 2 billion people over the age of 60. Given increases in life expectancy it is anticipated that in many countries there will be more people beyond the state pension age, claiming pension benefits than the number of taxpayers. To ensure adequacy of retirement incomes many Governments, including the UK Government, are promoting private pension schemes and encouraging people to save more.[1] Running alongside this there is a debate about the use of housing as a source of retirement funding particularly for those who may be income poor but housing asset rich. Housing can be used to generate funding through downsizing, re-

[1] It is expected that the cost of providing state pension to UK pensioners will grow more than four times in the next fifty years from its current level of £121 billion. The gap in the funding for social care will also rise and is expected to be £2.9 billion by 2020. It is estimated that the average cost of long-term residential care is £28,367 per year, with provisions made by old people standing at approximately £16,027. ERC (2015) calculates there to be a shortfall of 44% between the funds estimated and actual provisions towards the true cost of care.

mortgaging or by purchasing an equity release product. This raises two basic questions. First, can we identify the characteristics of those households that opt for different means of housing equity withdrawal? Second, can we gain insight as to why households might choose one form of housing equity withdrawal over another? Academic research, both empirical and theoretical, can offer insights to both questions with the answers couched variously in terms of, lifecycle considerations, household demographics, consumption smoothing, precautionary savings motives, transaction costs and taxation, and bequest motives and emotional attachment.

The Research Team at Queen's have built on this literature, and using the UK Wealth and Asset Survey 2006 to 2014 as the test-bed, have sought to empirically determine, in a probabilistic sense, the characteristics of those who chose different forms of housing equity withdrawal and the factors important in determining the choice of one form over another. In terms of the purchase of an equity release product we conclude that demographics such as age and marital status are important as are liquidity constraint variables such as, household debt to income and loan to value ratios. While in the decision of whether to purchase an equity release product rather than for example downsize the factors of influence include age, marital status and the liquidity constraint variable, loan to value.

Moneyfacts (2016) estimates that for the UK, lending through equity release will reach £1.93bn in 2016, up 20% from £1.61bn in 2015. Moneyfacts (2016) notes that the range of equity release products has more than doubled compared with three years ago. This increase is due to new product providers and product innovation. The latter includes products which permit a percentage of repayments to be made without an early repayment charge as well as products which offer downsizing protection. Accepting that innovations are now occurring, the Research Team at Queen's has examined ways to enhance the attractiveness of equity release products.

Model One combines tax relief on a lifetime mortgage payment in conjunction with a lifetime mortgage product. It assumes that individuals receive tax relief on their initial mortgage payments. This relief accumulates to a pot of money, as in a standard pension system, which can be drawn from, either as a lump sum or as an annuity once the person reaches his/her normal pension age. In addition, the model allows individuals to withdraw home equity through equity release schemes once they reach their normal retirement age. This is similar to a standard lump sum mortgage product. The individual could make provisions for an amount equal to a proportion of the original mortgage amount released.

Model Two focuses on the No Negative Equity Guarantee (NNEG) offered by UK providers of equity release products. This model attempts to estimate the value of NNEG under current market practices drawing on the framework suggested by Andrews and Oberoi (2014). In our proposed structure, the NNEG risk could be covered through an agency in the form of a Public-Private Partnership. In simulation exercises the covering of the NNEG is found on average to double the percentage of the house value that the equity release provides can offer.

Prof Udo Reifner (Hamburg University & iff-Hamburg)

Abstract

Equity release for Pensions

Equity release is the attempt to transform individual property into a liquid asset which can be used for old age pensions. It tries to harmonise three elements of modern housing policies: (1) individual homeownership, (2) increased financing of house purchase and (3) the financialisation of care for the elderly. While there are no alternatives to the last two elements, the idea that the use of houses or flats for living has to be provided in an illiquid form is neither general nor coercive. Historically, renting a flat was a productive alternative to owning it, which is a choice through which large sums of money have to be advanced and kept illiquid until death. With extremely low homeownership rates, wealthy countries like Germany and Switzerland show that this alternative housing tenure should not be seen as outdated. This is why, within the European Commission funded project "Integrating residential property with private pensions in the EU", a proposal led by our Irish partners which seeks to integrate renting and old age saving (model 3 in the project thinking) is an interesting path that should be kept in mind in discussions about the development of Equity release schemes (ERS). However, most countries join a different ideology. Homeownership is seen as the better form of living. "*My home is my castle*" prohibits the flexibility to move whenever you want to take up a new job opportunity, change property for a more adequate home when children leave the parental nest, look for calm more rural areas in old age etc. The permanent and flexible alignment of the offer of housing to its needs is excluded by forms of property which in the shift to an economy of users seems increasingly anachronistic. (see

Subprime crisis, price bubbles, unaffordable living in urban areas). ERS provides a way out: “rent” your flat from a bank in the form of a mortgage.

But the existing techniques of lending still subscribe to the purpose of financing to acquire debt free property in the end. Own capital, large repayment instalments, and credit restrictions are seen as a foundation of a safe financial system. Another model being considered by the project (our second model) questions these assumptions. Financing can separate from life time and form a unit between heirs and legators. Ownership can remain with the users, but credit provides the flexibility. Nevertheless, such amelioration will only help the better off, those households who can at least combine a minimum of savings into one’s home and savings for old age at the same time, although much more could be “released” if heirs would be integrated into the solution. A true step forward should question the adequacy of the legal forms of homeownership today. The alternative of being either owner or tenant is outdated. Industry has shown that transferring inflexible property rights to legal entities that can be governed through share and participation provides enormous flexibility. Our third model has been developed in this realm under the title “*Tenants buy their homes*”. Those who can only afford to become tenants do not have to refrain from property rights. Tenants can buy and sell square meters of their flats, be tenants and owners at the same time and experience their rights as a true equivalent to personal property. Such solutions may contribute to ERS as well.

Mr Lennart Grabe (Svenskhypotekspension AB)

Abstract

Observations about Equity Release (ER) from a Swedish perspective.

Svensk Hypotekspension AB introduced ER in Sweden 2005. At that time in the market, some banks had a product for seniors called “seniorlån”, which was a regular mortgage and on top of that a credit facility from which the interest due on the mortgage was regularly paid. When the extra credit was used up, typically after ten years, inherently the property was supposed to be sold to repay the arrangement. Also products where sold with a regular mortgage with the capital placed in a ten year annuity insurance, in turn placing the money in risky share-funds. Now all those banks have stopped supplying these products after a lot of criticism from a consumer protection perspective and some terrible mishaps with the insurance solution. Only our product, which was based on the 2005 British *SHIP*-code (Safe Home Income Plan, now succeeded by the

Equity Release Council's rules) with a lifetime commitment and a no-negative-equity-guarantee, prevails. The market in Sweden for funding via a warehouse bank facility during the build of loan stocks, subsequently repaid via the issuing of ABS-bonds in the fixed income market, is functioning. We have completed two rounds of this, and are now using our third warehouse facility for the lending. Next securitization is planned for 2020.

I find it important that ER always is defined and presented in accordance with the EU-directives wording: "*certain credit agreements where the creditor contributes a lump sum, periodic payments or other forms of credit disbursement in return for a sum deriving from the sale of an immovable property and whose primary objective is to facilitate consumption"… An assessment of the consumer's creditworthiness… is irrelevant since the payments are made from the creditor to the consumer rather than the other way round... other products, such as home reversions… have comparable functions to reverse mortgages or lifetime mortgages.*"

My point is that ER must not be seen and presented as a loan in the normal sense. It is a way of selling a property, like in home reversion schemes. It is an agreement between a creditor and a homeowner to share the proceeds from the future sale of the home. The creditor gives the homeowner an advance of the future proceeds. Of course, the creditor wants to have some return on the advance, which it gets in the form of a gradually increasing share of the future proceeds, computed in the form of an accumulating interest to be added to portion represented by the advance. In accordance with this concept, it goes by itself that the share cannot become larger than 100 %. The presence of what is generally called the "no-negative -equity-guarantee" (NNEG) is a matter of course, and the concept thereby should not reasonably be at risk for having consumer protection measurements against over-indebtedness applied upon it. If you introduce a product without *NNEG,* you, in my opinion, corrupt the concept of ER and must accept to be subject to restrictions applied on normal indebtedness.
The problem experienced in Sweden is that the above way of understanding ER has not yet been accepted by Swedish authorities. They tend to look upon it as a regular mortgage, since it legally and formally is shaped in the form of a mortgage credit, which then automatically falls under the rules and regulations for regular mortgages where the borrower has to pay interest and amortizations. (This also lends itself to erroneous price comparisons between ER credits and regular mortgages.) The Swedish FCA is of the opinion that the ER should be mandatory amortized

by 1% yearly as soon as the total debt exceeds 50% of the value of the home, as for other mortgage loans. In addition It has recently been suggested that also ER credits should be subject to restrictions against over-indebtedness, like limitations of the allowed lending to e.g. a certain times net income, which is directly in contrast to the wording in the directive. I am presently using most of my time trying to change all this.

The matter will be decided in new legislation, which will be presented to the parliament this fall. This might be the end of ER in Sweden. Hopefully I succeed in "selling" the above right way of looking upon ER to the politicians to save the business.

Mr John Moriarty (Seniors Money)

Abstract

Perspective on Equity Release

Frame of reference

My perspective on the equity release space is framed by over ten years' experience of working in the industry for a lender - Seniors Money International (SMI). SMI was founded in New Zealand in 2003 to offer Lifetime Loans (equity release mortgages) to over 60s, and entered the Australian market shortly thereafter. I joined the northern hemisphere management team in 2005 with responsibility for Finance and Operations. We launched operations in Ireland and Spain in 2006 and in Canada in 2007. Following the onset of the global financial crises, the group focused its funding capacity on Ireland, New Zealand and Australia. We sold the Canadian business in 2010 and the Australasian businesses in 2014, so today the group comprises the Irish and Spanish operations and portfolios.

SMI remains the only specialist equity release provider in the world to enter multiple country markets. I have been involved in every aspect of developing and managing ER lending operations across these markets and am currently Group CFO.

Observations – past and emerging

Over the past decade I have experienced the industry cycling from boom to bust and, potentially, now being on the cusp of re-emerging in terms of new business growth. The over-riding observation is that, whilst the demand-side is in rude good health (as populations age and face ever-growing challenges to fund retirements), the supply-side has been broken for a number of years: The old bank-funded model, of warehouse funding refinanced by securitisation, was hit hard by the banking crisis whilst the insurance industry, which ought to be the obvious candidate to match long-dated ERMs to their long dated liabilities, has struggled to work out how to do this under Solvency II. The UK regulator has been at the forefront in putting an SII framework in place for ER assets, so it is perhaps no surprise that the UK market has experienced a record-breaking year for new business, largely funded by insurance funders. This has not been the case in other EU markets.

Public policy and regulations

The legislative and regulatory frameworks that cover ER vary greatly between countries – specific laws and regulations in some countries and none in others. Given its nascent nature and small size, the industry is easily overlooked when both prudential and conduct of business regulations are formulated – witness SII. Rigorous prudential and conduct of business rules are very desirable, but need to be framed within a wider public policy recognition of the vital social need that ER can fulfil. The industry needs to be promoted, not just regulated. In the short run, initiatives to clarify the capital requirements for ER assets (there is little transparency from Central Banks on this) would stimulate investment in the assets. Noting the federal support for the US reverse mortgage industry (via HUD programmes to insure certain lending risks), similar state- or EU-level support should be in place to provide (or at least enable the provision of) insurance to cover NNEG risk.

Aspirations for the future

When the global financial crisis hit in 2008 SMI rescaled its business to meet the new environment and, supported by its shareholders and bankers, adopted a strategy of retaining the key personnel, IP and market presence to be in a position to return to a growth strategy once favourable conditions returned. SMI aspires to the resumption of new lending in the near-term, initially in Ireland, followed by a return to the strategy of entering a number of selected international markets.

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Appendix 1

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- The Revenue Commissioners
- The Departmentment of Finance
- Seniors Money
- Chartered Accountants Ireland
- Probus
- Consumer Association of Ireland
- Waterford Institute of Technology

Appendix 2

Consortium Research Teams

Team Number	Institution	Researchers
1	**Iff-Hamburg**	Mr Sebastien Clerc Renaud Dr Dirk Ulbricht Prof Udo Reifner
2	**Waterford Institute of Technology**	Mr John Maher Dr Richard Burke Dr Sean Byrne Mr Yogesh Jaiyawala
3	**Queen's University Belfast**	Prof Donal Mckillop Dr Declan French Ms Tripti Sharma
4	**University of Rostock**	Prof Doris Neuberger Dr Peter Hennecke
5	**Technological University Delft**	Prof Marja Elsinga Dr Jorg Hoekstra Dr Marietta Hafner
6	**Andrassy University Budapest**	Prof Martina Eckardt Dr Jörg Dötsch Dr Stefan Okruch
7	**LUMSA Rome (**Libera Università degli Studi Maria Ss. Assunta di Roma**)**	Prof Pierluigi Murro Dr Flaviana Palmisano Dr Francesca Lipari