RETIREMENT VILLAGE DEFERRED MANAGEMENT FEES: YOUR QUESTIONS ANSWERED

Despite having been the mainstay of Australia's retirement village industry for decades, deferred management fees remain a poorly understood and confusing concept for many consumers.

In fact, the first time that most consumers hear about deferred management fees is when they consider moving into a retirement village.

You won't be charged a deferred management fee when you buy a general apartment or a house - but you will more than likely be charged such a fee by a retirement village.

Deferred management fees come in many shapes and sizes.

The advantage of this situation is that consumers can shop around for the best deal, and work with an operator to create a pricing model which suits their needs.

The downside, however, is that there can be an overwhelming number of choices and options.

However, fear not.

Downsizing.com.au has put together the ultimate dummy's guide to deferred management fees (also known as exit fees or deferred fees).

What are deferred management fees?

A deferred management fee is a fee you need to pay a retirement living operator when you leave the village.

Deferred management fees represent an operator's return (potentially including profit) from the villages they develop and run.

Why do village operators charge deferred management fees?

Deferred management fees are not well-understood, typically because they are such a different pricing model compared to general housing projects.

For instance, a typical apartment developer would seek to recover its profit as a percentage of the value of the apartment, when selling it for the first time. The developer then exits the project and allows the apartment owners to manage the complex.

However, this scenario is not really suitable when applied to retirement villages, which have a vastly different operating model.

This is because:

- Charging a set percentage of the dwelling price when a resident moves into a retirement village (using the above model) may be unfair if the resident only stays in the village for a very short time, such as a year or so
- State legislation can be quite strict about how operators charge monthly fees, with the aim that they recoup their costs but don't extract a profit. As a result, the deferred management fee model has been developed by the industry to get a return on the project, because they can't get this through monthly fees
- Unlike the apartment developer example above, retirement village operators both develop the project and then continue to manage the project, which means an apartment style upfront 'set and forget' pricing structure may not work.

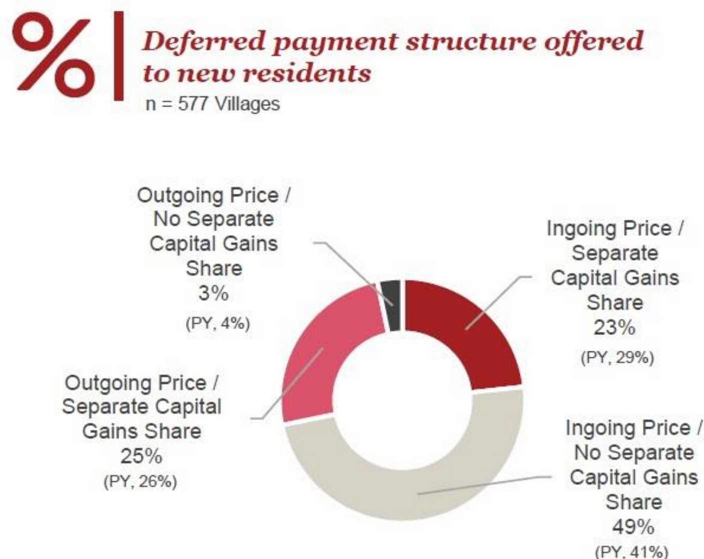
As a result of the above, the industry has developed the idea of the deferred management fee.

The fee is linked to the length of time that the resident stays in the dwelling, which in essence is a fair and reasonable concept.

What are the different types of deferred management fees?

Unfortunately, not only are deferred management fees a niche and poorly understood feature of the retirement village industry, consumers also need to learn about the many different ways that they are charged.

The chart below (from the Property Council of Australia 2019 Retirement Living Census) shows the different ways that operators seek to charge fees, including on either the incoming or outgoing price of the dwelling, and sometimes a portion of capital gain (or loss).



As you can see from the chart, the most popular way that a deferred management fee is charged is on the incoming contribution, with no percentage charged on the capital gain of the dwelling while the resident has been living there.

Some people argue this option provides the greatest certainty, because it means that a person will know the fee they are going to pay when they sign on the dotted line. This is not possible if the fee is charged on the outgoing price, given this is a future variable.

Consumers are also well-advised to carefully read their contract, and shop around, if the operator is proposing to extract part of the fee from the village unit's capital gain.

Although it doesn't often happen, some contracts have been known to state that the consumer will both pay a portion of the capital gain if the price of the dwelling goes up, but also have to pay a fee to compensate the operator if the value of the dwelling falls. In other words, the consumer pays both ways - no matter what the outcome.

There are two schools of thought in relation to operators linking the fee to capital gain.

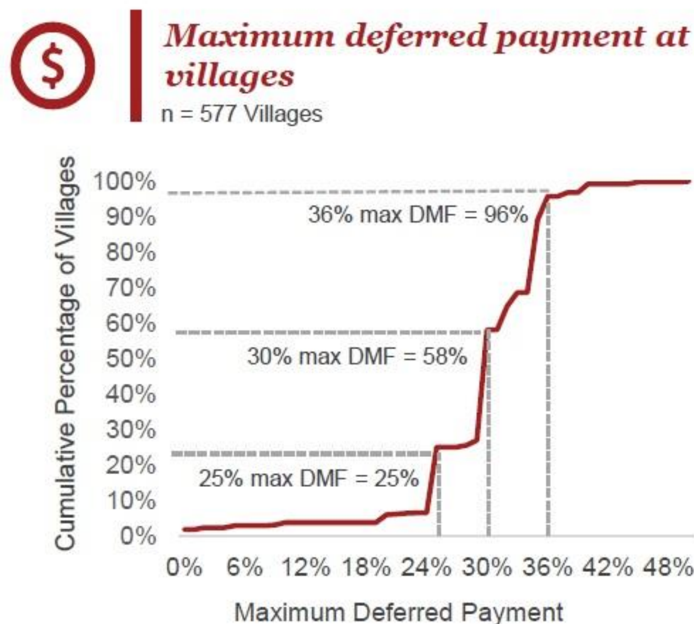
Some consumers, understandably, think they should wholly benefit from any capital gain, just as they would if their family home value increased.

In contrast, some operators argue it is actually in the interests of both the consumer and the operator for the fee to apply on capital gain.

According to this argument, a fee linked to capital gain ensures that both the resident and the operator are motivated to keep the dwelling and village well-maintained, so the dwelling appreciates in value over time.

What is the average cost of deferred management fees?

As the chart from the Property Council 2019 Retirement Living Census below shows, there are a wide range of deferred management costs.



The maximum fee level typically ranges between 25 and 36 per cent of your home value (noting the different pricing models explained above). So it pays to shop around.

What's more, operators apply this maximum fee in different timeframes.

Around half of all villages reach the maximum fee level within six years (noting that the average stay in a retirement village is around 8-9 years). Around one in five however reach the fee within just four years.

Obviously, you are more likely to pay more if you sign-up with an operator with a higher fee which applies in a shorter time frame.

How do I know what fee option is best for me?

Not only do you need to understand what the operator is offering, and shop around, you also need to consider your own financial circumstances.

Operators are likely to be willing to reduce the deferred management fee amount, if you pay a higher entry price when you sell your family home and downsize into a retirement village dwelling.

This is because they will make money by earning interest when they invest this higher amount, and therefore are willing to forgo a higher fee.

The potential advantage of this approach is that, by paying a higher amount, you also won't have too much spare cash lying around and breach the pension assets threshold (and therefore lose all or part access to the pension).

A good financial advisor should be able to help with calculating this.

Separately, for some people, an option where they pay a very high fee - in some cases well over 50 per cent - but also a much lower incoming price, is preferable.

This is because, without this lower entry price, the residents wouldn't have been able to move into the village at all. In other words, the deferred management fee is simply a formula - and can be pushed and squeezed in a way which best suits your needs and financial situation.

How can I compare and contrast different offers?

Fortunately, the Macquarie University has developed a Retirement Village Calculator, which seeks to boil all the above options (and the monthly service charge) into a simple monthly cost. This allows you to compare and contrast different operators and scenarios.

In addition, some operators have done away with deferred management fees altogether - see the stories below for more information:

- "Largest in Australia": $270m Canberra care-centered vIllage accepts its first residents (2020 story)
- Big changes in retirement living (2018 story)

Also check out this expert analysis of different sort of legal titles and fee pricing models in NSW retirement villages.