



SEQUAL Guideline

No Negative Equity Guarantee and Default Conditions

August 2007

1. Background

The SEQUAL Code of Conduct requires all SEQUAL Members to offer a No Negative Equity Guarantee (NNEG). The NNEG provides that the borrower shall never owe more than the value of the property provided they comply with the terms of the contract.

Following the CHOICE reports in 2006 and 2007, and the inevitable and continued focus on the terms and conditions in Reverse Mortgage lenders contracts, it is necessary that the SEQUAL Code of Conduct be enhanced such that a No Negative Equity Guarantee must be in force without reference to whether the customer is in default. This issue is considered threshold to the credibility of SEQUAL. It is also necessary to limit the effect of default clauses on consumers by ensuring proper process is followed.

In addition, there has been some comment on the ability of lenders to apply penalties or require repayment if the borrower is in default of the conditions of the loan. For this reason, a minimum process needs to be specified.

This Guideline sets out the general conditions which must be contained in contracts as a minimum as well as the minimum process required in the instance of defaults.

This Guideline is considered mandatory for all SEQUAL Members as part of their compliance with the SEQUAL Code of Conduct, and is deemed for this purpose to be part of that Code of Conduct.

2. Minimum Contract Requirements – No Negative Equity Guarantee

It is required that the terms of the contract with the borrower must be in the following general terms:

- The NNEG must apply in any situations where a repayment trigger event occurs under the contract
- The NNEG must guarantee that the lender will not have recourse to recover amounts in excess of the net sales proceeds of the property (ie after reasonable sales costs including any government taxes) from the borrower or their estate or any other person in any circumstance other than those specified below
- When the repayment trigger is a sale of the property, it is acceptable that the contract specifies that it must be sold at arms-length and only following express permission of the lender prior to the sale, and that non-compliance with this requirement will invalidate the NNEG
- The only other situations in which the NNEG can be invalidated where it would otherwise apply is where there has been fraud by the borrower or willful damage to the security property by the borrower which has resulted in the shortfall.
- If the borrower is in default under the loan for any other reason, the lender cannot use this as a reason to invalidate the NNEG.

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3. *Minimum Procedural requirements on Default*

- Where there are default conditions in the loan contract, these must be fair and reasonable.
- Where there is a serious default under the contract, it is permissible that the lender can require the loan to be repayable immediately or apply a default rate of interest.
- Except in a situation where there is an immediate threat to the value of the underlying security, the lender must act in accordance with the Uniform Consumer Credit Code as regards notice and follow the process outlined below prior to moving to require the loan to be repaid or applying a default rate of interest:
 - Send the borrower a written notice of default specifying a period for rectification of the default (such period being reasonable taking into account the particular circumstances of the default).
 - The Lender (or their representative) must personally contact (or make a reasonable attempt to contact) the borrower (or their legal personal representative) prior to the expiry date of the notice to ensure that they have received the notice and understand the consequences of not rectifying the default
 - If the borrower remains in default after the period of notice has expired, the lender may commence action for the loan to be repaid in full at that point. Alternatively, it is permitted that the lender can, in these circumstances, choose to charge a higher default rate of interest until the default is rectified, as long as the default rate is reasonable in the circumstances having regard to the nature or cost of the default to the lender.

4. *Date of Operation*

This Guideline comes into operation from 1 January 2008 at the latest and applies to all contracts issued on or after that date or the date of amendment of the standard contract to comply with this Guideline, whichever is the earliest.

All contracts must be reviewed by SEQUAL by or on 1 January 2008, whenever they are amended, and at least annually to ensure compliance with this requirement. SEQUAL will keep a list of complying members, which will be available to interested parties as required.