



## Housing Loans Insurance Corporation (Transfer of Pre-transfer Contracts) Bill 2006

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## Housing Loans Insurance Corporation (Transfer of Pre-transfer Contracts) Bill 2006

**Date introduced:** 13 September 2006

**House:** House of Representatives

**Portfolio:** Treasury

**Commencement:** The day after Royal Assent

### Purpose

To enable the Commonwealth to transfer its ownership to another person of the residual mortgage insurance contracts that were written by the Housing Loans Insurance Corporation prior to its restructure and abolition in 1997.

### Background

The Housing Loans Insurance Corporation (HLIC) was established by the government of Sir Robert Menzies in 1965 to provide a government-backed housing loan insurance scheme. The main purpose of this scheme was to assist prospective home purchasers to obtain a loan at a reasonable rate of interest by providing mortgage insurance. Mortgage insurance policies cover the losses suffered by lenders when a borrower defaults on a loan secured by mortgage. Although the HLIC principally insured housing loans, it also insured lenders for loans relating to non-residential buildings. In the mid-1990s, HLIC was the largest mortgage insurer in Australia, having insured more than 1,300,000 loans.<sup>1</sup>

In 1996 Parliament passed the *Housing Loans Insurance Corporation (Transfer of Assets and Abolition) Act 1996* which restructured HLIC into a new government-owned company. Subsequently, HLIC Ltd was sold to the private sector in 1997.<sup>2</sup> Insurance contracts written by the HLIC prior to its restructure, known as ‘pre-transfer contracts’, remain under the Commonwealth’s ownership. The size of the principal amount covered by the Commonwealth’s guarantee and the balances outstanding was estimated in 2005 to be \$5.397 million. This figure is a small increase on the balance outstanding in 2004 which was \$5.087 million, but much less than the \$19.036 million balance outstanding in 2003.<sup>3</sup> There are no figures available for earlier years.<sup>4</sup>

According to the second reading speech, claims against these contracts are managed on behalf of the Commonwealth under a management agreement. No figures are available for the extent of the Government outlays associated with the management of the pre-transfer insurance policies. In 1996, when it took over the pre-transfer contracts, the Government

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estimated its expected budget allocations to cover anticipated home loan defaults in the three years following the restructure of HLIC would be: <sup>5</sup>

1996–97	1997–98	1998–99
\$20m	\$15m	\$8m

### Mortgage default

Recent press reports have indicated a rise in the number of cases lodged in state and territory Supreme Courts to take legal action against borrowers who default on mortgages that are secured by property.<sup>6</sup> For example, the *Age* reported that in Victoria there had been a 58 per cent increase in mortgage repossessions between 2004–05 and 2005–06.<sup>7</sup> In New South Wales, the *Australian Financial Review* reported that there was a 60 per cent jump, up from 3061 in 2005 to 4873 in 2006,<sup>8</sup> while in the ACT, the *Canberra Times* quoted a report by the Consumer Law Centre saying that repossessions in the Territory increased by 39 per cent between 2004 and 2005.<sup>9</sup> However, in Western Australia, the trend is in the opposite direction. According to the *West Australian*, ‘after a rise in the number of home repossessions in 2004–05 to 577, the number of applications dropped to 531 in the past financial year’.<sup>10</sup> It is not known what risk the rise in mortgage defaults poses to the Commonwealth through its ownership of the pre-transfer contracts of the HLIC.

### Possible financial implications

The second reading speech explains that the Government has no desire to continue to be involved in the business of mortgage insurance through its continued ownership of the residual pre-transfer contracts.<sup>11</sup> The Parliamentary Secretary stated that the Commonwealth’s involvement is no longer financially viable and will only become increasingly burdensome to administer over time.<sup>12</sup> The purpose of this Bill is to provide a framework that would allow the Commonwealth to divest its ownership of the remaining mortgage insurance contracts, if it can find someone to take on the residual risk. Depending on the nature of the risk, it is possible that the acquirer may seek consideration for assuming this risk from the Commonwealth. The explanatory memorandum says that this Bill has no financial implications.<sup>13</sup> However, this may be because, at this stage, it is not known if the Minister will succeed in transferring the risk to somebody else or not. Transferring the remaining mortgage insurance contracts to somebody may or may not involve some future compensation. As it is not possible to estimate the amount of such compensation, the Bill provides for any such payment to be made as a special appropriation from the Consolidated Revenue Fund and reported in the Treasury Portfolio Budget Statements and the Treasury Department Annual Report.

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## Implications of a failure to pass this Bill

This Bill is time sensitive because the current management agreement under which the pre-transfer insurance contracts are managed expires on 31 December 2006. Moreover, according to the second reading speech:

the Australian Government Actuary has advised that present market conditions and the current profile of the portfolio provide the Commonwealth with the best opportunity it has had to complete its exit from the lenders mortgage insurance business. Any delay in amending the current legislation may diminish the government's negotiating position in the interests of the Australian public.<sup>14</sup>

## Main provisions

**Proposed section 3** contains definitions of words and terms used in the Bill. One significant definition is 'vesting day' which is the day fixed by the Minister by notice published in the *Gazette*. The 'vesting' refers to the transfer of assets and liabilities owned by the Commonwealth in the form of mortgage insurance contracts to an 'acquirer'. The mortgage insurance contracts had been written by HLIC prior to its restructure and abolition in 1997. These pre-transfer contracts have continued to be owned and guaranteed by the Commonwealth.

**Proposed section 6** is a key provision in the Bill and enables the Commonwealth to wholly divest its interests in the pre-transfer contracts to the acquirer. On the vesting day, the acquirer becomes the successor in law to the pre-transfer contracts, associated documents, rights and liabilities. This is a broad provision, intended to cover any circumstances which might not be covered by the specific vesting provisions in the proposed section. Any rights and liabilities of the Commonwealth under a pre-transfer contract or an associated document become rights and liabilities of the acquirer.

**Proposed section 7** preserves the effect of any pre-transfer contracts and relevant legislative instruments that were in force immediately before the transfer day in 1997 when the HLIC was restructured into a company and the Commonwealth took over ownership of the pre-transfer contracts. Under the current law, references to the 'Corporation' in a pre-transfer contract or a relevant legislative instrument refer to the Commonwealth. The effect of the saving provisions in **proposed section 7** is that, after the vesting day, references to the 'Corporation' in a pre-transfer contract or a relevant legislative instrument will refer to the acquirer. Each pre-transfer contract and each relevant legislative instrument will continue to have effect, according to its terms, after the vesting day.

**Proposed section 8** provides an exemption from stamp duty and other state and territory taxes in relation to the transfer of the pre-transfer contracts to the acquirer pursuant to

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**proposed section 6.** The purpose of this proposed section is to provide certainty to the acquirer.

The Bill provides a framework that enables the Government to commence formal discussions with persons interested in acquiring the pre-transfer contacts. No other Parliamentary approval will be necessary to bring about the transfer of ownership of the pre-transfer contracts to another person. Should the acquirer seek compensation from the Commonwealth for taking on the risk that might exist in the remaining mortgage insurance contracts, then provision is made by **proposed section 9** to pay the acquirer out of the Consolidated Revenue Fund. It is not possible, at this stage, to know if compensation will be required, and if so, how much will be sought. An annual appropriation through the Appropriation Bill would not be practical for this purpose as it requires an accurate estimation of the amount to be paid. The use of a standing appropriation will ensure that public money can be used to support the transfer, if needed. According to the explanatory memorandum, accountability to Parliament will be met through the Treasury Portfolio Budget Statements and the Treasury Department Annual Report.<sup>15</sup>

**Proposed section 10** enables the Minister to delegate his or her powers and functions in declaring the vesting day and acquirer under **proposed section 5**, and certifying matters that are exempt from stamp duty and other state and territory taxes under **proposed section 8**. The delegate is to be either the Secretary of the Department (currently Treasury) or a Senior Executive Service employee in the Department. The delegate is to comply with directions of the Minister.

**Proposed section 11** provides that the Governor-General may make regulations prescribing matters that are required or necessary for carrying out the operation of this Act. This includes matters of a transitional nature, including prescribing any saving or application provisions relating to the enactment of this Act and the repeal of the *Housing Loans Insurance Corporation (Transfer of Assets and Abolition) Act 1996*.

## Concluding comments

This Bill does not commit the Commonwealth to transfer its ownership of the residual mortgage insurance contracts to another person, but would enable any transfer to occur, if desired. In 2005, the principal amount covered by the Commonwealth's guarantee and the balance outstanding was estimated to be \$5.397 million. If the Government can find somebody willing to assume ownership of this risk, then it is possible the acquirer will seek some consideration for assuming this risk from the Commonwealth. This Bill provides that funds may be drawn from the Consolidated Revenue Fund for this purpose. The Government has received advice from the Australian Government Actuary that the present market conditions and the current profile of the portfolio provide the Commonwealth with the best opportunity it has had to complete its exit from the lenders mortgage insurance business.

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## Endnotes

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1. Hon. John Fahey, Sale completed of Housing Loan Insurance Corporation', *Media Release*, 22 December 1997. In the debate on the Housing Loans Insurance Corporation (Transfer of Assets and Abolition) Bill 1995, it was stated that HLIC had insured 94,700 loans in 1994 and a further 84,000 loans in 1995. (Senator C Kernot, Senate, *Hansard*, 31 May 1996, p. 1563).
2. Hon. John Fahey (Minister for Finance and Administration), 'Sale of Housing Loans Insurance Corporation', *Media Release*, 31 October 1997; Hon. John Fahey, Sale completed of Housing Loan Insurance Corporation', *Media Release*, 22 December 1997. HLIC Limited was sold to GE Capital Australia.
3. Treasury, *Annual reports*, 2004-05 p. 196; 2003-04 p. 229; 2002-03 p. 214.
4. For the years 1997-2002, the Treasury reported that 'the principal amount covered by the guarantee and the balances outstanding are unable to be reliably measured', see for example, Treasury, *Annual report 1997-98*, p. 182.
5. *Explanatory memorandum* to the Housing Loans Insurance Corporation (Transfer of Assets and Abolition) Bill 1995, p. 3.
6. Figures of the number of repossession actions are kept by state and territory Supreme Courts.
7. Ben Doherty and Nassim Khadem, 'Hundreds lose homes as rates rise', *The Age*, 2 August 2006, p. 1; Ben Doherty, 'Howard's dream-believers living on hand-outs', *The Age*, 3 August 2006, p. 8. Also, Karen Collier, 'Living on the edge: Victorians risk losing homes', *Herald Sun*, 17 July 2006, p. 1.
8. Fiona Tyndall, 'Housing risk warning', *Australian Financial Review*, 3 February 2006, p. 46. Also, 'Lenders repossessing houses of overextended borrowers', *Canberra Times*, 19 January 2006, p. 6.
9. Paul Malone, 'Rise in home repossessions sparks call to regulate brokers', *Canberra Times*, 14 September 2006, p. 2.
10. Amanda Banks, 'Home owners battle to hold on', *West Australian*, 4 August 2006, p. 4.
11. Hon. C Pearce (Parliamentary Secretary to the Treasurer), 'Second reading speech, Housing Loans Insurance Corporation (Transfer of Pre-transfer Contracts) Bill 2006, House of Representatives, *Debates*, 13 September 2003, p. 3.
12. *ibid.*
13. *Explanatory memorandum*, Housing Loans Insurance Corporation (Transfer of Pre-transfer contracts) Bill 2006, p. 3 and 4.
14. *ibid*, p. 1.
15. *ibid*, p. 11.

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