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House of Representatives Standing Committee on Economics, Finance & Public Administration

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SUBMISSION 54

SUBMISSION TO EFPA:

SUPERANNUATION SAVINGS OF YOUNG HOUSEHOLDS

REVERSE MORTGAGES
HOUSING IS SUPERANNUATION

A. Some background

Generational balance in Australia has been disturbed by house prices doubling in the past decade or so. A sensible commitment to home ownership among young households inevitably means that paying off mortgages on overpriced houses leaves little scope to put more into superannuation, over and above the (admittedly inadequate) compulsory 9 per cent levy on employment income.

Mature (and wealthy) households -- primarily the boomer generation – who owned most of the housing stock at the outset were handed a massive windfall gain just as they are coming to the retirement altar with hands poised to take an age pension and ancillary benefits from the public plate. As things stand young households will be paying (unnecessary) taxes to fund a growing burden of social security payments to their well-heeled parent's generation – taxes, their money, which could be better used to fund a needed increase in the compulsory superannuation levy on their employment earnings.

This socially divisive scenario is worrying and it is difficult to accept that it is coming like a train on time without any apparent sense of urgency to get off the present wrong track and put in place policy reforms likely to be as essential as they may be unpopular. In particular it is now essential, and fair, to propose removing the standing exemption of retirees' homes from the means-test constraining access to the age pension.

The essential equivalence of all assets available to retirees seems to have eluded those so far making submissions to this inquiry. Instead, invitations to make submissions have, as usual, elicited many typically self-serving proposals -- especially from those already milking the superannuation savings of the community, young and old, by taking excessive commissions and fees.

B. Reverse mortgages: the concept

This submission brings together elements of two articles published in CFO magazine, and available at cfoweb.com.au, and another from the online newsletter *EUREKA Report* (eureka report.com.au)*: the central theme of these articles is the likely implications of reverse mortgages for retirees and government policy.

* ***Keep an open mind*** (CFO July 2005); ***Storm the castle*** (CFO October 2005) and ***How to buy a mansion with your super and win*** (EUREKA Report 28 October 2005)

Reverse mortgages are being advertised and most seniors have a passing familiarity with the general idea. Background on reverse mortgage products is available at sequal.com.au, the website of an association of lenders offering equity release loans to senior Australians.

At a conceptual level, resources available in retirement comprise all accumulated assets, and typically a home and superannuation savings dominate the portfolios of retirees. At a very practical level, for most pending 'boomer' retirees it is likely that the value of their home exceeds their superannuation savings – indeed for most the increase in their net worth over the past decade was mainly due to the increased sale-value of their home.

As noted elsewhere, it makes good sense for many retirees to have access to some of the equity in their home without selling it outright, and continuing to live in it 'forever' in retirement. Using such no-repayment, lifetime loans, repayable only when the property is finally sold, retirees will be able to draw a regular income in the form of additional cash advances. Using home equity as a de facto super fund is comparable to drawing down an allocated pension from superannuation savings and probably more attractive because the 'income' won't be taxed and the 'asset', being exempt from the means-test, will not prevent retirees receiving the age pension.

It will make a substantial difference to retirees' financial flexibility and standard of living if they can draw on the equity in their home -- for living expenses or to help their families – and reverse mortgages facilitate that. At a broader level the scope for reverse-mortgages to release equity from the homes of retirees, has important implications for retirement-incomes policy generally.

C. Policy implications

The personal and public policy implications of reverse mortgages are wide ranging, not least for government retirement-incomes policy covering social security pensions and superannuation.

-- some basics

- first and foremost it is entirely beneficial that retirees who are asset rich and income poor can boost their disposable income from 'savings' tied up in a home much as others draw income from superannuation savings; and

- second, abandoning sharp distinctions between 'superannuation savings' and 'savings used to buy a home' vindicates young households typically well advised to pay off their housing loan quickly rather than putting more into superannuation -- being 'in debt' can loom large even when locked-away superannuation investments prospectively have a higher rate of appreciation than house prices.

-- some complexities

- excluding the 'family home' from the age-pension means test underscores a sharp but artificial and unhelpful distinction between assets nominally in separate 'superannuation' and 'housing' buckets;

- this contrived distinction opens an opportunity for retirees (and pending retirees) to exploit the age pension arrangements and, more generally, it more or less ensures that the stock of housing in Australia will continue to be used inefficiently: retirees, often single retirees living alone, will continue to occupy valuable residential real estate that they would not continue to want to own if the asset was embraced by the age-pension means test; and

- perversely, one prospect that then emerges is for some retirees, well capable of self-funding their own retirement, to substitute more-expensive, 'exempt' housing assets for means-tested assets tied up in superannuation. Again as noted elsewhere, for those contemplating turning their home into a de-facto super fund which 'pays' reverse mortgage installments, the consequent eligibility for the age pension is a big attraction: at some $400,000 for a couple, the present value of an entitlement to the age pension for life far exceeds the tax likely to be payable when cashing out the superannuation that denies access to the age pension. Retirees who swap their 'super' for 'more expensive housing' would most likely have higher total disposable cash income than those that don't.

C. Some policy implications

- **means test madness**

The 'compulsory' super savings of most boomers fall well short of their retirement needs and they will be positioning themselves to be eligible for the age-pension: retirees may be 'old' but they are not silly and they quickly ferret out holes in the public purse.

Australian retirees also have a lingering sense of entitlement to the age pension irrespective of their personal financial circumstances. Contending that "we all paid our taxes, so we are all entitled to the age pension" many retirees feel aggrieved if, by virtue of prior prudence or success, they are means-tested out of pension benefits readily available to others of more modest means (and possibly less virtuous). Finding holes in the public purse is considered fair game.

Remarkably, the circumstances unfolding will allow wealthy retirees to become eligible for the full age pension. Remarkably because, with an ageing population, the policy imperative is to the contrary: ideally, the dependence of the retiring boomer generation on public funding needs to be reined in. 'Remarkably' again because many consider it imperative also that policy restores a sense of proportion to housing prices: the circumstances unfolding actually risk another blow-out of housing prices as competition for expensive residences for retirees is fuelled by the prospect of a $400,000 subsidy from the government.

In short, there is some means-test madness afoot – and apart from ensuring the means test works effectively (and not perversely) more needs to be done to encourage well-off retirees to accept the sense of means tests as a fair way of limiting social security payments to the truly needy.

- **home ownership: virtue or vice**

Australian's much-praised attachment to owning a family home is predictably taking on a different colour. Some sense of this virtue becoming a dangerous vice-like addiction was starkly illustrated as housing prices doubled in the space of a few years recently, following a rush to so called investment housing mainly driven by inappropriate tax breaks overlaid on a climate too conducive to housing investment anyway.

A transitory saving 'grace' for Australia is our financial planning profession: venally addicted to advising clients to hold superannuation investments that leave a trail of lucrative commissions for themselves, planners would get no joy advising clients to get out of super to buy a more expensive home. However, even this questionable mercy will evaporate once 'planners' add a commission-taking, mortgage-broking arrow to their quiver and start putting retired clients into hock with a reverse mortgage on their homes.

Australia has some serious soul searching to do about housing policy because the addiction, to 'home ownership' and its accumulated raft of attendant political pressures, risks running the economy aground. Embracing the homes of retirees in the age-pension means test would be a very useful start towards bringing housing markets into line for the long haul.

- **superannuation: under done**

The converse, obviously, of an unhealthy national preoccupation with accumulating 'housing' assets is a similarly unhealthy underinvestment in superannuation. Superannuation 'under done' is not characteristic of young households alone – if anything it is the older community, retiring boomers basking in the glow of 'my house is worth double', that is the real offender.

This Committee may have been given a special focus on 'superannuation and young households' but it is the essential substitutability of 'housing' and 'superannuation' across the board, and across all generations, that is a more relevant focus. Again, from another angle, one likely effective step towards everyone sensibly rebalancing their 'housing' and 'superannuation' priorities would entail embracing retirees' homes in the age pension means test -- it is important to protect a sense of balance when choices between 'housing' and 'superannuation' are being made by everyone, young and old.

D. End piece

This Committee would now seem to be facing a substantial test of its mettle.

What apparently seemed to most making submissions -- a simple exercise in 'encouragement' for young households to contribute more to superannuation -- is perhaps better seen as embracing issues which go to the very heart of some deeply held Australian traditions – the unalloyed virtue of home-ownership and the associated exemption of retirees' homes from the means test restricting access to the age-pension, a prized entitlement.

The tide has turned for both these shibboleths of Australian economic and social policy and I would like this Committee to say so in its report. Reforms on both fronts would do more to underwrite the proper provision of young households for their retirement than any tinkering on the edges.

Peter Mair
31 October 2005