FINANCIAL PLANNING
ASSOCIATION *of* AUSTRALIA

4 August 2017

Manager
Accumulation and Savings Unit
Retirement Income Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: superannuation@treasury.gov.au

Dear Sir / Madam

Treasury Laws Amendment (Reducing Pressure on Housing Affordability) Bill 2017

The Financial Planning Association of Australia (FPA) welcomes the opportunity to provide feedback on the draft legislation to implement the Government's First Home Super Saver Scheme (FHSS) and contributing the proceeds of downsizing to superannuation measures.

The FPA would welcome the opportunity to discuss with you the issues raised in our submission.

If you have any questions, please contact me directly on heather.mcevoy@fpa.com.au or 02 9220 4500.

Yours sincerely

Heather McEvoy
Policy Manager
Financial Planning Association of Australia[1]

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[1] The Financial Planning Association (FPA) has more than 12,000 members and affiliates of whom 10,000 are practising financial planners and 5,600 CFP professionals. The FPA has taken a leadership role in the financial planning profession in Australia and globally:

- Our first "policy pillar" is to act in the public interest at all times.
- In 2009 we announced a remuneration policy banning all commissions and conflicted remuneration on investments and super for our members – years ahead of FOFA.
- An independent conduct review panel, Chaired by Graham McDonald, deals with investigations and complaints against our members for breaches of our professional rules.
- The first financial planning professional body in the world to have a full suite of professional regulations incorporating a set of ethical principles, practice standards and professional conduct rules required of professional financial planning practices. This is being exported to 24 member countries and 150,000 CFP practitioners of the FPSB.
- We established the Financial Planning Education Council in 2011 as an independent body chartered with raising the standard of financial planning education. The FPEC has built a curriculum with 17 Australian Universities for Bachelor and Master degrees in financial planning We have built a curriculum with 17 Australian Universities for degrees in financial planning. Since 1st July 2013 all new members of the FPA have been required to hold, as a minimum, an approved undergraduate degree.
- We are the only professional body in Australia licensed to provide the CFP® certification program. CFP certification is the pre-eminent certification in financial planning globally. The educational requirements and standards to attain CFP standing are equal to other professional designations, such as the Chartered Accountant designation of the Chartered Accountants Australia and New Zealand (CA).
- We are recognised as a professional body by the Tax Practitioners Board

TREASURY LAWS AMENDEMENT (REDUCING PRESSURE ON HOUSING AFFORDABILITY) BILL 2017

Exposure Draft and Exposure Draft Explanatory Materials

FPA submission to

Treasury

4 August 2017

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Introduction

Housing affordability in Australia is a significant and complex issue that impacts on people's wellbeing in a variety of ways and to different extremes. It requires a number of multi-faceted solutions to support the diverse needs of the Australian community. Any measures to increase demand need to be finely balanced with policies to increase supply in order to control prices; and supported by appropriate local infrastructure.

The FPA provides the following comments based on feedback from our financial planner members and the impact the draft legislation will have on their clients.

First Home Super Saver Scheme

The FPA is concerned that allowing people to access their superannuation accounts for a deposit will have consequences on both the housing market and the retirement income system, ultimately increasing house prices and the strain on the age pension.

While the proposed FHSS is based on the release of voluntary contributions, as discussed below these FHSS funds are not quarantined from superannuation balances, meaning the proposal will still have consequences for the retirement savings of many Australians who use the scheme.

The investment earnings in super usually represent a larger component of an individual's superannuation balance at retirement than the voluntary contributions an individual makes. Any income earned by assets sitting in super gets reinvested to buy more assets, over years and years. A key attribute of the superannuation system is the use of compound interest to improve the growth of retirement savings. Removing money from super early dramatically cuts its growth potential.

For example, a 30 year old with an average balance of $30,000[2] compounding at a rate of 7.5 per cent annually, that $30,000 investment alone becomes:

- after 20 years (age 50) = $127,436
- after 40 years (70) = $541,327

The longer the funds remain in super, the greater the consumer nest egg in retirement. The early release of funds presents long-term implications for the superannuation system as consumers lose the impact of compound earnings over several decades, leaving Government to fund the resulting shortfall in retirement savings.

Using the superannuation accounts to fund housing will reduce the retirement savings of future retirees, putting extra pressure on the age pension.

As evidenced with the first homeowner grants, incentives for housing usually push up house prices. Such schemes commonly result in a condensed influx of people being able to afford to buy with more money up front to spend on a house, driving more demand for properties and

[2] Superannuation account balances by age and gender, Ross Clare, Director of Research ASFA Research and Resource Centre, December 2015

artificially inflating house prices to match the availability of funds. Housing markets then adjust accordingly to the influx of funds, further disadvantaging home buyers.

This ignores the cyclical nature of markets. Encouraging people to buy property at what may be the peak of the cycle in some cities will not grow wealth, rather it will only lead to an increase in household debt.

Finally we would note that while not legislated, the First Home Super Saves Scheme does not meet the Objectives of Superannuation contained in the Superannuation (Objective) Act 2016 nor the secondary obligations contained in the draft Superannuation (Objective) Regulation 2016 which we note the Government is looking to implement.

Recommendation

The FPA does not support the use of superannuation savings as a housing deposit for first home buyers.

FPA feedback on draft legislation

No separation of funds

The draft legislation does not quarantine the contributions made for the purposes of the FHSS from the member's superannuation funds. This creates a significant risk that the member's superannuation savings, including the superannuation guarantee, will be released for a housing deposit, eroding their superannuation balance and the benefits of long term compounded interest on their retirement savings.

Impact of volatility on positive deemed earnings and superannuation balance

The maximum amount that could be released under s138-20 reflects contributions and deemed earnings (s138-35) in respect of those contributions. However, there is no requirement for the trustee to quarantine these contributions in a cash option, instead the contributions would be invested as normal in the member's default or choice investment option. In periods of volatility, negative earnings would reduce the balance, however the amount that could be released under the FHSS proposed legislation would still reflect the value of the initial contributions and positive deemed earnings. Therefore in periods of volatility, the amount withdrawn would be funded from those contributions plus the existing balance to make up the deemed earnings shortfall. This scheme provides a risk free return for housing deposits, at the expense and risk of the remaining superannuation balance.

This would result in the release of FHSS funds also taking funds contributed for the purposes of superannuation including the superannuation guarantee, in order to ensure the FHSS deemed earnings remained positive. The FHSS could have a significant impact on the remaining superannuation balance, particularly during periods of prolonged volatility such as the GFC.

1.127 of the Explanatory Memorandum states that associated earnings are calculated ….*ending on the day that the Commissioner makes the determination is necessary to crystallise the FHSS maximum release amount*. However, with contributions mostly invested in non-cash assets under the superannuation investment options, this will also crystallise potential investment losses.

We would further note that even superannuation cash options are often not "cash" in most superannuation funds. All super investment options are designed for the liquidity profile of a superannuation fund and its members. This is generally a significantly longer time frame than a first home saver will be looking to invest. The liquidity profile and therefore the investment mix for MySuper and choice investment options will only exacerbate this issue further. Using super in this manner will potentially impact the long-term attributes and performance of the entire investment pool of a superannuation fund, impacting on all members retirement balances and leading to further strain on the social security system.

Previous interest held in real estate

To be eligible for the FHSS, proposed subsection 138-5(2)(a) states "*you have never held an interest in a CGT asset that is taxable Australian real property*".

This could unfairly disqualify a first home buyer if they held any interest (legal, beneficial or otherwise) of any amount in taxable Australian real property. This proposed wording would potentially and unintentionally disqualify genuine first home buyers such as a lessee for example.

The FPA suggests consideration be given to the inclusion of a carve out to provide greater certainty as to the type of interest held in the taxable Australian real property. For example, subsection 86(2)(a) of the Duties Act 2001 (QLD) which relates to a duties exemption for first home buyers, carves out "*an interest other than – (i) as trustee for another person; or (ii) as lessee: or (iii) as the holder of a security interest*".

Recommendations

Voluntary contributions made for the purposes of accessing the FHSS should be quarantined from superannuation funds (compulsory and voluntary).

Consideration should be given to the appropriate investment options and risks for FHSS funds, given the emphasis on positive deemed earnings. Superannuation funds should not be used to cover negative deemed earning on FHSS contributions.

138-5(2)(a) should clearly exclude certain type of "interest held in the taxable Australian real property" to ensure genuine first home buyers are not inadvertently ineligible for the FHSS scheme.

Reducing barriers to downsizing

The FPA supports public policy that ensures senior Australians have housing choice and can downsize at low cost if they choose to. While the proposed measure may assist some retirees, it does not address the following cost and social inhibitors to downsizing for many older people:

- the high cost of stamp duty
- the impact of selling a home on the means test for Age Pension recipients
- the availability of appropriate housing for seniors in their local community so vital access to local services and community connections can be maintained if desired.

FPA feedback on draft legislation

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Indexation

There is no indexation on the cap of up to $300,000 for downsizing contributions into superannuation. It would be appropriate for the contribution cap to be indexed to keep pace with ongoing rising house prices and the inflationary cost of living, and would be consistent with indexation applied on other caps within the superannuation system.

The $300,000 downsizing contribution cap could be indexed to three times the annual non-concessional contributions cap, AWOTE, or CPI, for example.

Contributions when spouse is under 65 years

292-102(1)(a) requires an individual to be 65 years or over to be eligible to make a downsizer contribution to their complying superannuation plan.

This creates an unfavourable position where there is a large age gap between two members of the couple and one spouse is under 65 years of age. While the government recognises that in this case, the under 65 year old spouse would contribute to superannuation under the usual non-concessional contributions cap and rules, given the 1 July 2017 changes, the under 65 year old spouse may not be able to contribute to super for example, if their total superannuation balance exceeds $1.6 million or they have already fully used the non-concessional contributions cap.

The Government permits a spouse that is not on the title of the main residence to be eligible to use this measure. We suggest the Government employ this same type of flexibility and permit the younger spouse of an individual who is 65 years or older, to be eligible to make a downsizing contribution.

Transfer downsizing contributions to pension phase

As stated in the draft Explanatory Material, the Government's intent of the downsizing contributions measure is to permit older Australians to invest the proceeds of selling their home into superannuation to encourage them to downsize, to free up larger homes for younger, growing families (paragraph 2.5 - 2.7).

Many Australians who are 65 years and older have entered the pension phase of the superannuation system. We therefore suggest it would be appropriate and in line with the Government's policy intent, to allow the downsizing contributions to be transferred to individual's pension account, even if the person has fully used the transfer balance cap.

CGT main residence exemption

The criteria for the downsizer contribution set in 292-102 of the draft legislation requires that the dwelling must be eligible in part or full for the main residence exemption in 118-B of the Incomes Tax Assessment Act. We note that this includes specific rules for partial exemptions if the dwelling has been used to produce assessable income (paragraph 2.24 of the draft Explanatory Material).

However, we seek clarity regarding the eligibility for this measure under draft s292-102(1)(d) of an asset that is predominantly used for running a business but includes a main residence. For example, a farm, motel with a manager's residence, bed and breakfast, all of which may be

eligible for a 15 year small business CGT exemption (or any other small business CGT concession), and used partly as a main residence.

Notification

Draft s292-102(8) requires the Commissioner to notify a superannuation provider if all, or a specific part, of a contribution made by an individual does not meet the downsizer contributions criteria. This draft section also suggests the Commissioner provide a copy of the notification to APRA.

However, neither the draft legislation nor the draft Explanatory Material require the Commissioner to provide a copy of its assessment that a contribution does not meet the downsizer criteria, to the individual who made the contribution. We suggest this should be a responsibility of the Commissioner, not the provider, so if the individual is dissatisfied with the Commissioner's decision they should have the ability request a review of the decision.

Recommendations

Legislation for the contributing the proceeds of downsizing to superannuation measure should:

- include indexation in the monetary caps
- permit the younger spouse of an individual who is 65 years or older and meets the criteria, to be eligible to make a downsizing contribution
- allow the downsizing contributions to be transferred to individual's pension account, even if the person has fully used the transfer balance cap
- permit an asset that is predominantly used for running a business but includes a main residence. For example, a farm, motel with a manager's residence, bed and breakfast, etc.
- require the Commissioner to provide a copy of its assessment that a contribution does not meet the downsizer criteria, to the individual who made the contribution. An individual should be permitted to request a review of the Commissioner's assessment.