Submission to the Financial System Inquiry

March 2014



Contents

Executive Summary	3
Recommendations	
Comments on the financial system and developments since Wallis	10
The Yellow Brick Road Financial Services Five Point Plan – Overview	
Discussion	13
1. More help for Australians to master their personal finances	
Improve financial 'know how' - a system for consumers, not just financial insiders	13
Mortgages should become truly portable and discharged within 14 days – banning exit fees is insufficient	16
Improve access to financial advice – introduce tax-deductibility for financial advice that is means-tested	17
2. Transparency in interest rate advertising	
Mandate true rate disclosure in advertising financial products	18
3. Require real banking competition and encourage consumer mobility	20
Remove moral hazard - introduce the bank levy	20
Promote competition from smaller players – support the RMBS market	22
Revise ASIC's mandate to include a competition brief	
4. Supporting the life dream of a house and a comfortable retirement Make the two great Australian dreams a seamless reality — support a new 'lifecycle' retirement savings asset class	25 25
5. Create a fairer system for the outsiders - women, small business, young people	32
Conclusion	33

Executive Summary

Yellow Brick Road strongly supports this inquiry into the financial services system and is grateful for the opportunity to provide input into the reform process.

The Australian Government has an opportunity with this inquiry to stand back, analyse and then reform some of the financial services settings that are inconsistent with the needs and interests of the vast majority of Australians. In our view, it provides a chance to properly assess progress in financial services reform insofar as it impacts on the wellbeing of ordinary Australians. We believe it also provides an opportunity to revisit and potentially debunk some entrenched myths.

Yellow Brick Road

advocates building a competitive financial system that serves all Australians, not just the financial system 'insiders'.

Yellow Brick Road advocates building a competitive financial system that serves all Australians, not just the financial system 'insiders'. Most Australians have two dreams – to own their own home and to retire comfortably. They hope to have the opportunity to knuckle down, to work hard and to provide for their families. They want to give their children a better life than they had themselves. And then, after their children have grown up and been able to afford to move out of the family home, they hope to retire and spend the next 20-30 years of their lives enjoying everything that they have built for themselves.

This is the dream, but unfortunately for many, it's not a reality. Australians are working as hard as ever, so they should be able to achieve the financial independence that the generations before them have enjoyed. Yet with cost of living, housing, transportation and education pressures, the hope of a comfortable retirement seems more a fortuitous pipedream than an achievable goal.

Currently, financial independence is realisable for a minority of Australians. These are the insiders, the people that can afford to obtain the right advice to help

them make informed decisions about their future. There are the vast majority of Australians, the 'outsiders', the people who are working just to make ends meet. The young people graduating from university who are searching for their first job amidst rising unemployment rates, and the couples who are struggling to get that deposit together for their first house. The young parents who want to give their kids the best education possible in an environment where they are juggling cash flow to cover basic household necessities. The empty nesters that dream of retirement but have to delay it for another five to ten years just to ensure that they won't become a financial burden on their adult children. These people make up the majority of our country. And the current financial system is not adequately geared towards serving them.

Nor is our system keeping up with societal changes. In twenty years' time, the typical consumer won't be who they are today. We are currently experiencing a generational shift where traditional employment takes a backseat to a more mobile, dynamic and evolving workforce. People are less likely to stay at the same job for 30 years and employment may be more insecure. Many young people will enter the workforce with high levels of HECS-HELP debt. People are settling down later in life, and they'll wait to have children and put off purchasing their first home. With rising house prices this means that people will have larger debt that they'll have to pay off for longer periods of time, possibly into retirement age when debt should be non-existent. The trend will be towards longer, later and larger mortgages. So if we continue to operate as we are today, ignoring the majority and favouring the insiders, we'll create a generation that becomes even more dependent on the government to get by.

One of the objectives of financial reform should be to improve the engagement in retirement planning and general financial management for the outsiders who have similar issues in accumulating savings and getting access to affordable lending. Many of the outsiders are women, small businesses, and young people, but they are certainly not confined to those categories.



Five steps to a more competitive, fairer financial services system

There are some simple, but critical reforms that Yellow Brick Road believes are vital to creating a fairer system for all of us, not just a system for a select few.

Without intending to limit the scope of solutions or decry other worthy considerations, Yellow Brick Road advocates the following five point plan for reform that is aimed at delivering for Australian consumers:

- More help for Australians to master their personal finances
- More transparency in interest rate advertising
- Require real banking competition for real consumer choice
- Supporting the life dream of a house and a comfortable retirement
- Create a fairer system for the outsiders women, small business, young people

There are a number of issues that sit under these broader five points that are addressed in the body of this submission. The balance of this executive summary deals briefly with the key themes.

First, the Australian Government needs to encourage more financial literacy and more access to financial advice, particularly for low-to-middle income earners. That is why we are advocating expanding the national education curriculum and making financial advice tax-deductible for people earning under \$75,000, which is roughly the average wage. Only an informed consumer will avoid 'too-good-to-be-true' schemes and only an informed consumer will drive a truly competitive market.

The Australian Government must empower consumers to be able to make choices if we want a competitive financial services system. There are simple legislative changes that can be made – for

example, mandating 'true rate' advertising – which will drive more transparency from some of the industry players and help consumers make better informed choices that meet their interests.

Superannuation must be reformed to address the ageing population, access to it needs to be more flexible to meet the life-cycle needs of Australians, and superannuation regulations need to better address the gender gap in retirement savings driven by decisions to care for a family.

Regrettably, financial services reforms tend to deal with the quite separate silos of retirement savings on the one hand and home lending on the other. But for most middle income Australians, the two issues are inextricably linked with home ownership being as influential on retirement lifestyle as the size of the retirement nest egg. Indeed, increasingly, retiring Australians are utilising lump sum retirement income to service or repay ever increasing mortgages. So while the superannuation sector sticks to the myth that super savings should be for retirement rather than housing, increasingly Australians are using substantial lumps of their accumulated savings for the family home - but after the banks have profited from years of compounded interest charges. We need to reconsider better linkages between savings for a home and savings for retirement.

We are for a system where competition is real – not feigned. We are for a system that delivers a level playing field. We agree with the head of the ACCC, Rod Sims that:

Normally four players in a market should lead to a lot of competitive activity. In the banking sector it seems to need more because even though there are four of them there is a lack of full and effective competition.¹

Normally four players in a market should lead to a lot of competitive activity. In the banking sector it seems to need more because even though there are four of them there is a lack of full and effective competition. – Rod Sims



Australia has four oligopolistic banks that control around 80 – 90 per cent of all financial transactions executed across the country.

Australia has four oligopolistic banks that control around 80 – 90 per cent of all financial transactions executed across the country. And during the GFC, the unprecedented introduction of government guarantees furnished the "big four" banks with a further comparative advantage, leaving us with a highly concentrated banking sector that Australians pay for dearly. These four banks, together with AMP, also dominate wealth management services, retail distribution and life insurance.

Unfortunately policy-makers have embraced in the past a fallacious dichotomy that trades off 'competition' as the perceived enemy of 'financial stability'. It is not only a flawed assumption, it is risky. It favours a more concentrated industry where players have high levels of market power; it has contributed to the injection of moral hazard into the system; and it fails to take into account the importance of competition to the health of the sector and to meet the best interests of consumers. Australia can build a stable and competitive sector – they are not mutually exclusive values.

The big banks try to argue that size equals safety – another fallacy. We learnt from the US experience with Frannie Mae, Freddie Mac and AIG that there is a threshold beyond which size becomes a massive 'contingent liability' for taxpayers because they are 'too big to fail'. Fannie Mae and Freddie Mac were the two giant mortgage guarantors that had to be bailed out by the US Government in late 2008.

Like the major banks, Fannie Mae and Freddie Mac could raise money more cheaply than their competition because investors believed they were government-backed. And they were right. Both institutions are now owned by US taxpayers. The learning from this is that we need to remove the regulatory incentives that actively promote size of the too-big-to-fail variety.

That is why Yellow Brick Road is advocating not only the introduction of a bank deposit levy that requires private banks to pay an insurance premium for a taxpayer funded guarantee, but we encourage a Return-on-Equity (ROE) pricing model. The bigger you get, the higher the fee – which would nevertheless still be a trivial amount to pay as a price for insurance and stability. At present, in many ways, the system is stacked in the opposite direction – as a bank's size increases, its costs dramatically fall. This further stymies competition and consumer choice.

In conclusion, the need to act to improve consumer outcomes from our banking and retirement savings industry is compelling as the following 'ugly' truths of financial services outcomes demonstrate. And while the causal factors for these facts are more complex than financial services alone – we must not miss this opportunity to take some simple and practical steps that specifically address the problems.

Yellow Brick Road's Five Point Plan is the only submission - that we are aware of - that has gone to the Australian people for comment. We have listened carefully to make sure that this submission reflects the needs of Australians before it was finalised. The Five Point Plan received overwhelming public support.

The unpleasant facts

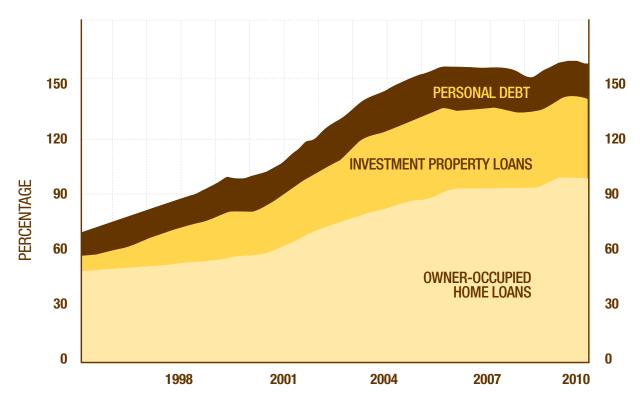
The Global Financial Crisis was caused by the big players that taxpayers in the US then had to bail out because they were 'too big to fail'. Size does not equal safety. Good regulation leads to safety.

- The Global Financial Crisis was caused by the big players that taxpayers in the US then had to bail out because they were 'too big to fail'. Size does not equal safety. Good regulation leads to safety.
- The big four banks (CBA, Westpac, ANZ and NAB) dominate the banking sector. They control 90 per cent of mortgages and hold 80 per cent of banking assets.² Their share of the financial system is 90 per cent, up from 50 per cent in the early 80's.³
- O Together with AMP, these big four dominate the funds management sector, controlling 80.9 per cent of all retail funds under administration.⁴

 These five companies also control almost two thirds of advisers (65.4 per cent)⁵, which facilitates control not only of product but also distribution.
- O The big four are all amongst the biggest 20 banks in the world and in 2012-13 made \$27.4 billion in profit. According to the IMF, they are four of the eight most profitable banks in the world and their high profits have been ascribed to a lack of competition in the market. This is clearly out of proportion with the relative size of the Australian economy and given the very high proportion of their operations are within Australia.

- In 2000, the difference between the superannuation balances of male and female employees increased with age to the point where male employees of retirement age (55-64 years) had more than twice the amount of superannuation of female employees (\$44,700 compared with \$19,800). Lower average wages and women leaving work, or working part-time, to care for children are likely to be contributing factors to this pattern.⁹
- O Most people that retire will need a lump sum balance in their superannuation of around \$1 million per couple (assuming they own their own house).¹⁰ Of concern is the fact that around 31.6 per cent of males and 38.5 per cent of women reported having no superannuation at all in 2011.¹¹
- Over the past decade, the debt of the household sector has increased at an average annual rate of 14 per cent, which is well in excess of the growth of household income. As a result, the ratio of household debt to household disposable income in Australia has risen from a level that was low by international standards to one that is in the upper end of the range of other industrial countries. 12

HOUSEHOLD DEBTPer cent of household disposable income*



^{*} Before the deduction of interest payments **Sources:** ABS;RBA

Recommendations

RECOMMENDATION 1: An informed and educated population is crucial to the operation of a good financial system. If we expect Australians to build sufficient wealth to retire comfortably in their own home, then we have to ensure that people know how to make the right decisions to get them there. The Australian Government should work with the States and Territories to amend the national education curriculum to include financial literacy skills. This will help our youth understand the fundamentals of financial management from budgeting to savings and borrowing to superannuation.

RECOMMENDATION 2: Financial services legislation needs to be simplified, internally consistent and address the needs of consumers, rather than regulators or financial service providers. Advice to clients currently crosses regulatory channels, which adds expense for the client and adds excessive paperwork, making it difficult and confusing for the consumer to absorb. Regulation should be simplified to make it more consumerfriendly; in particular, processes and requirements for advice delivery across the basic needs of savings, superannuation, risk and mortgages should be simplified for those under 45 and below certain income thresholds. Overly complex regulation adds to cost of delivering advice, reducing access for Australians.

RECOMMENDATION 3: In the event of refinancing, the Australian Government should require through legislation the timely discharge of a mortgage by a lender within 14 days in order to allow Australians to exercise their consumer choice rights efficiently.

RECOMMENDATION 4: The Australian

Government should amend taxation laws to allow financial advice from a registered financial adviser to be tax-deductible for people earning up to \$75,000 up to a value of \$1500 per annum. This will empower all Australians to be able to manage their finances and protect them and the government from negative consequences of financial decisions.

RECOMMENDATION 5: Mandate true rate advertising for financial products by amending comparison rate legislation to reflect a true average mortgage of \$300,000 and amend the Trade Practices Act 1974 to require the standardised, annualised interest rate to be prominently displayed and communicated pre-contractually, to avoid confusion over compounding and other gradual rises. Discount advertising should be banned because of its high potential for confusing customers into buying inappropriate products.

RECOMMENDATION 6: Introduce a bank levy to price the taxpayer guarantee of deposits of up to \$250,000 to provide Australians with a return on their investment and compensate for the risk shifted to the taxpayer.

RECOMMENDATION 7: The Australian

Government should invest the proceeds of the banking levy into a fund that invests in securitisation of home loans through the Australian Office of Financial Management, thereby providing smaller and non-bank lenders with the ability to compete with the four major banks, which currently benefit unfairly from a Government guarantee on deposits but also dominate the market for deposits (and therefore access to funding).

RECOMMENDATION 8: The Australian

Government should amend the Australian Securities and Investments Commission Act 2001, to change ASIC's mandate to include promoting competition in the financial services system.

RECOMMENDATION 9: The Australian

Government should incentivise saving across a person's lifecycle, recognising that younger people are focused on securing a home before they can turn their mind to saving for retirement. But the two goals are not mutually exclusive - owning a home is an indicator of a comfortable retirement. There are a range of options for the Government to consider, including shared equity schemes for people to be able to enter the housing market earlier and start paying off a home, or a new 'Savings for Life' product where additional contributions to the mortgage sit in an account linked to the mortgage for their place of residence and those payments are treated preferentially under the tax system just as superannuation contributions are. This will help to address insecure housing, encourage a pattern of savings and address the perverse outcome where superannuation is used to pay off housing debt upon retirement - after the banks have already profited from their longer, later, larger mortgage.

RECOMMENDATION 10: To address the inequality in superannuation in the system, the Australian Government should amend contribution limit rules to average up to a cumulative five year period and allow pooling of contributions with a spouse. This will particularly assist women, small businesses and other Australians that have variable incomes.

Comments on the financial system and developments since Wallis

The world has certainly changed since the Wallis inquiry into the financial system in 1997.

Technology has delivered new 'disruptions' to the system and new international regulations have created a very different environment in which we operate.

Superannuation – barely mentioned in the Wallis inquiry as it was a relatively recent phenomenon – now dominates funds managed in Australia, overtaking the value of deposits in recent years.

Most significantly, the global financial crisis of 2008 – and our policymakers' response to it – also shed light on some vulnerabilities in the Australian financial system.

Prior to the global financial crisis, Australia had a diverse and highly competitive financial system. The four major banks competed directly with the likes of St. George, Bankwest, Wizard, Aussie, RAMS, and Challenger. Today every single one of these entities has disappeared as a genuinely independent entity, and have been wholly or partly acquired by the majors, or merged with one another.

Prior to the crisis, Australia's private banks were not explicitly government-backed. Australian taxpayers had never guaranteed bank deposits before – nor had they conceived of providing such guarantees for free as they currently do – nor had they ever guaranteed the banks' institutional debts.

The taxpayer-owned central bank, the Reserve Bank of Australia (RBA), had also never lent to

the banks on the much longer-dated and more flexible terms that it offered as the financial markets meltdown started to gather momentum, and continues to offer.

During the GFC, the major banks were delivered a windfall that exacerbated their market concentration and power through the Government's wholesale funding guarantee that came with an inequitable fee structure. The fee for the major banks was 70 basis points – compared to more than double that (150 basis points) for most other Australian Deposit-Taking Institutions (ADIs). The RBA has since confirmed that the differential in the fee structure was "relatively large by international standards" and that the fee paid by the major banks (AA-rated institutions) was "at the low end of the international range". 13

A more subtle example of how the system encourages extreme size is the terms on which the banks borrow from the RBA. When doing so, banks have to pledge an asset as collateral to obtain RBA funding. Included in the list of "eligible" assets the RBA will accept as collateral is any senior debt issued by an Australian bank. However, historically that debt had to have a credit rating - of A- or higher - which excluded the debts issued by smaller regional banks and building societies. Since the major banks were amongst the few that qualified for the RBA's funding, this helped further support investor demand for their bonds, and thus lowered their cost. On top of that, the majors have artificial fund-raising advantages through their credit ratings and new devices like covered bonds.

Competition, as Treasury and indeed our Parliament has noted on many occasions, is a fundamental prerequisite to an efficient financial system that benefits consumers.

It is questionable that Stan Wallis and the Campbell Committee intended the introduction of moral hazard into the banking system by these events. Wallis had explicitly recommended against such a guarantee for that reason.

The competitive playing field has changed dramatically as a result and this submission proposes options to deal with the inequities created. Competition, as Treasury and indeed our Parliament has noted on many occasions¹⁴, is a fundamental prerequisite to an efficient financial system that benefits consumers. It was also one of the core aims of the reforms proposed by the Campbell and Wallis inquiries.

Furthermore, the regulatory structure for financial services is complex, costly and byzantine for both advisers and consumers to navigate and understand. Reforms to the financial system – including the Future of Financial Advice (FOFA) reforms introduced in 2012 – have been designed for the purpose of legislative and regulatory oversight. The regulatory system needs to be streamlined and simplified so that it is focused on consumers' needs, rather than regulators' needs. This will reduce costs for Australians attempting to access financial advice and help to make the system more accessible and fair.

The Yellow Brick Road Financial Services Five Point Plan – Overview

More help for Australians to master their personal finances

- O Include the practice of financial literacy in the national curriculum
- O Remove impediments to consumer mobility let consumers vote with their feet
- O Help reduce costs of financial advice by removing unnecessary red tape
- O Improve financial 'know how' a system for consumers, not just financial insiders
- Make basic financial advice tax affordable through tax deductibility

More transparency in interest rate advertising

O Mandate true rate advertising and amendment comparison rate legislation

Require real banking competition for real consumer choice

- Reduce moral hazard through the bank levy
- Foster genuine competition from mutuals and non-bank lenders through RMBS investment
- Give ASIC a competition mandate

4 Supporting the life dream of a house and a comfortable retirement

- Make the two Australian dreams a reality again recognise the reality that home ownership is the greatest factor that helps with a comfortable retirement
- Tackle the superannuation shortfall by encouraging life-long savings

Create a fairer system for the outsiders - women, small business, young people

- O Address continuity gaps for women, small business
- Make superannuation relevant to young people recognise different savings needs at different stages of the life-cycle



Discussion

1. More help for Australians to master their personal finances

Improve financial 'know how'
- a system for consumers, not just financial insiders.

Government regulation plays an important role in protecting consumers from scams and from misleading and deceptive conduct that may influence them into making poor decisions.

But there is no adequate replacement for a population having some general smarts about them when it comes to making financial decisions. Education costs money, but then so too does ignorance. It impacts the extent to which we can fund retirement and the overall wealth of the nation.

Governments can't do everything and it's highly problematic to expect that they can or should. We should never underestimate the role for the individual to play in doing what they can to secure their financial future.

Yellow Brick Road submits to the inquiry that for any package of reforms aimed at generating a more competitive, fairer financial system to be truly successful, a better financial education needs to be part of the policy solution mix.

And the earlier we teach financial life skills, the better. We believe that the national school curriculum needs to include financial literacy so that all Australians can benefit.

All Australians are investors and financial planners now, thanks to compulsory superannuation. And that's before we get into mortgages, credit cards, insurance, managed funds and store finance. We live in a financial context and the quality of our education informs the quality of our decisions. That education process therefore should not end once schooling years are over. It is incumbent on financial service providers to educate their customers.

As Treasury commented in the review of banking competition conducted by the Senate in 2010-11:

If we are looking at competitive and sustainable banking, a major thrust is to better inform customers as to the nature of the banking system and how they should invest their money – to empower them to increase their financial literacy.¹⁵

The Senate Standing Committee on Economics also commented in its report that committee members support more attention being paid to financial literacy, which "is an important part of a more competitive financial system".¹⁶

Too many Australians lack basic financial management skills and this can be remedied.

Yellow Brick Road is aimed at helping all Australians – not just the affluent – understand financial planning and get access to competitively priced loans and other financial products. We support measures that assist Australians to better plan for their future, avoid financial hardship, and make informed choices about choosing between competitors.

Most households today need to use a wide variety of financial services. A typical household, for example, will have a mortgage, home contents insurance, car insurance, various forms of superannuation accounts, life insurance (usually by default through superannuation and not tailored to a person's needs), several credit cards and a savings account.

Financial literacy skills and the ability to access affordable financial advice are critical to assisting people to navigate these big decisions skillfully.



RECOMMENDATION 1

An informed and educated population is crucial to the operation of a good financial system. If we expect Australians to build sufficient wealth to retire comfortably in their own home, then we have to ensure that people know how to make the right decisions to get them there. **The Australian Government** should work with the States and Territories to amend the national education curriculum to include financial literacy skills. This will help our youth understand the fundamentals of financial management from budgeting to savings and borrowing to superannuation.

AUSTRALIANS HAVE THEIR SAY

"I agree with all 5 points but what resonates most is that of financial understanding and how to make better short, medium and long term decisions about money. I work hard for a reasonable day's pay and never seem to get ahead and this is where the financial intelligence will help to build a better country for our children."

- Daniel

Help reduce consumer costs of financial advice by reforming financial services regulations to reduce unnecessary red-tape

The complexity and volume of regulation in the financial services sector is serving to exclude people from the financial system.

The extent of regulation adds significantly to the cost of providing services, making it unaffordable for financial services to provide simple advice that many consumers need.

For example, take the situation of a person who has four superannuation accounts that seeks advice as to which account to choose. The cost to the adviser of providing the advice may amount to around \$900. Yet research conducted by ASIC has indicated that consumers prefer simple rather than comprehensive advise and around 75 per cent of people canvassed were not willing to pay more than \$250.17 The result is twofold – some financial service advisers may avoid offering the advice; and consumers avoid seeking it.

This militates against better financial literacy amongst the community and can promote poor decisionmaking in the absence of expert advice.

Yellow Brick Road supports the proper, effective regulation of the financial services sector and supports Government efforts to crack down on fraud, to set minimum standards across the industry and to promote freedom of choice for consumers.

The core design of the regulatory system encourages artificial silos.

The different application of regulation to different products, service and advice means that advisers are less able to meet the complex needs of their clients. How various products – superannuation, mortgage, personal loan, financial advice – operate in combination can be crucial to a household's financial success and budget. There are trade-offs between short-term needs and those that are more long-term that can be complex to navigate without financial advice.



Historically, regulation has been shaped heavily by the assumption that there is a financial adviser involved, which normally adds costs. This has unintended consequences for delivering affordable and comprehensive advice and services to the majority of whom are still in 'accumulation' mode and working with low levels of savings and high debt.

It would be preferable if limits and variable depths of regulatory requirement could be imposed as floors or ceilings around investment size, for example, or total amount of revenue or financial risk incurred by the consumer, as opposed to product type. Consumers and service providers could then choose how and who to deliver and promote services to and under what means of distribution/engagement.

A siloed approach to regulation makes advice provided narrow and more expensive – and this is not usually in the interests of most working Australians needing financial advice. Most households need access to holistic, affordable and easy-to-use services.

The FOFA legislation should be combined with other legislation in a way that simplifies regulations, reduces duplication and inconsistency, and is developed in a way that is consumer-centric, not sector-centric. Legislation regarding advice delivery and compliance should be written from the 'household view' – so there is one lot of documents, training, supervision and so on for delivering services to an accumulated housing earning under a combined income of \$120,000.

Simplification will lower costs, facilitate better and more appropriate services for the majority of Australians and open up new forms of distribution – thus building innovation and competition in the system. The result is that the outsiders are able to get better access to financial advice. Now the system only favours those – the insiders – that are able to pay for such complicated financial advice.

RECOMMENDATION 2

Financial services legislation needs to be simplified, internally consistent and address the needs of consumers, rather than regulators or financial service providers. Advice to clients currently crosses regulatory channels, which adds expense for the client and adds excessive paperwork, making it difficult and confusing for the consumer to absorb. Regulation should be simplified to make it more consumerfriendly; in particular, processes and requirements for advice delivery across the basic needs of savings, superannuation, risk and mortgages should be simplified for those under 45 and below certain income thresholds. Overly complex regulation adds to cost of delivering advice, reducing access for Australians.

AUSTRALIANS HAVE THEIR SAY

"I have two children that recently left high school and have absolutely no understanding of the financial system, debt, credit cards and creating wealth. Financial education should be an imperative part of the national curriculum in every school. Too many people learn the financial lessons the hard way."

- Ren



Mortgages should become truly portable and discharged within 14 days – banning exit fees is insufficient

While the ban on exit fees for mortgages is a step in the right direction, it is insufficient to promote full mobility for consumers.

Mortgage discharges need to also be completed in a timely manner – within fourteen days. This is consistent with recently introduced legislation requiring superannuation funds to action a redemption within three days. The current lack of regulation with respect to mortgage discharge allows lenders to hold onto a mortgage for a lengthy amount of time, despite the customer switching mortgage providers. This is contrary to the wishes of the customer and legislation should be introduced to better regulate this conduct.

As was canvassed in the Senate's inquiry into banking competition, delays in lenders effecting transfers of mortgages is of concern to consumers. As one of the private submissions to the inquiry noted:

Banks are able to settle properties for purchase readily in normal commercial time, but when they are receiving the settlement from outgoing customer this becomes in the main a painful exercise for the customer.

It should be regulated that a bank is required to settle the transfer of a mortgage from one bank to another, within a maximum of 21 days of the date notified by the customer that they are transferring to another bank.

There is no system impediment to this occurring.

Mostly titles for properties exist both electronically and on paper and the existing customer bank holding the title should be readily able to produce the physical title document, match it with the transfer signed by the customer, and transfer the title to the new lender within this period.

If the bank cannot produce the title within 21 days and affect the transfer for the customer a penalty of perhaps one month's interest expense for each day's delay by the bank be paid to the customer as compensation.¹⁸

Yellow Brick Road believes 14 days is sufficient time for lenders to be able to arrange transfer of the mortgage in accordance with the customer's desires. A standardised form should be used and a process established by regulation.

RECOMMENDATION 3

In the event of refinancing, the Australian Government should require through legislation the timely discharge of a mortgage by a lender within 14 days in order to allow Australians to exercise their consumer choice rights efficiently.



Improve access to financial advice – introduce tax-deductibility for financial advice that is means-tested

Financial advice should be more accessible. Only one in five Australians seeks financial guidance from a professional¹⁹ and that is partly because it is perceived as a luxury service for the wealthy. But it is the Australians in the lower to middle income brackets that are in great need of support in terms of managing their finances to meet financial challenges.

This is why Yellow Brick Road supports making financial advice tax-deductible – or alternatively supplying a Government rebate – for people that earn below \$75,000 per year up to a value of \$1500 per year. It is Australians impacted by high cost of living pressures, housing stress and lack of sound financial knowledge that need the support and the confidence to prepare themselves for retirement. In the long run, an Australian population that is better able to manage its finances is better able to save (and thereby increase national savings) and are less likely to need to rely on the welfare system for support into retirement.

This policy would also be of great assistance to small business owners. There are around two million²⁰ small businesses in Australia and they employ almost five million Australians. Their entrepreneurial spirit is vital to our economic growth.

Yet so many businesses fail because they don't have access to the right support. It has been reported that only 15 per cent of businesses seek financial advice and three quarters of small businesses do not set an annual budget.²¹ Yet proper financial planning is a critical factor that can make the difference between surviving and thriving as a small business, and business failure.

Small businesses need honest advice to ensure they are not over-estimating cash flow streams, they need assistance as to what risk-management strategies they need in place and they need someone to ask them the tough questions.

RECOMMENDATION 4

The Australian Government should amend taxation laws to allow financial advice from a registered financial adviser to be tax-deductible for people earning up to \$75,000 up to a value of \$1500 per annum. This will empower all Australians to be able to manage their finances and protect them and the government from negative consequences of financial decisions.



2. Transparency in interest rate advertising

Mandate true rate disclosure in advertising financial products

While arguably the notion of true rate advertising could easily fall under the broader heading of 'improving competition' by better empowering consumers to make informed choices, Yellow Brick Road believes it is an important enough issue about the integrity of the financial services system and consumer protection to stand alone as a discrete issue.

It is ironic that consumers get better information about the contents of their Vegemite jar than they do about the composition of their home loan or savings account.

It is ironic that consumers get better information about the contents of their Vegemite jar than they do about the composition of their home loan or savings account. It is true that consumers are entitled to (and lenders obliged to provide) extensive disclosure documentation. These documents are often indecipherable, bulky and designed as much to deter the average consumer from reading them let alone absorbing them. It is notable that despite the pro-disclosure regime the most basic piece of information available – the advertised interest rate – is not obliged to genuinely reflect the true cost of the mortgage or the effective interest rate applicable to deposit accounts.

Amendments to the comparison rate legislation are required to remedy these issues.

First, the comparison rate legislation should also be amended to reflect the cost of a true average mortgage to provide a more realistic comparison rate for consumers. In 2003, the average loan size for first home buyers was \$160,500 according to the Australian Bureau of Statistics. The average loan size today has jumped to around \$311,100.²²

Secondly, comparison rate legislation came into effect ten years ago, whereby any interest rate advertisement had to be accompanied by a comparison rate and the appropriate warning.

At the time, honeymoon rate products – along with substantial early exit fees – were popular, so the intent of the legislation was to allow consumers to get a better understanding of the true cost of a loan prior to committing to a decision.

The requirement for the disclaimer effectively ended interest rate advertising on radio and made it more difficult to advertise on TV and in newspapers. A popular alternative has become to advertise just the discount off the standard variable rate. Advertising an interest rate discount off the standard variable rate is beyond the reach of current comparison rate legislation as no actual rate is disclosed.

In the area of deposits, consumers are regularly drawn in by ADI's advertisements of a rate paid on a savings account but in the finer print (if it is available at all in the advertisement) the consumer would be surprised to see their rate drop after three months to a rate that is uncompetitive. The advertised rate – usually in bold and enlarged – is the 'hook' that disadvantages the consumer within a short period of time.

We are seeing a move in the financial services sector away from ensuring that we have an informed consumer by advertising rates and offers that do not state the underlying rate. For example much advertising today is highlighting the discount off the variable rate, rather than the rate itself. Discounted rate advertisements should therefore be banned as they serve only to confuse the consumer.

This provides consumers with very little information to compare loans, and post GFC as standard variable rates are now significantly varied between lenders, the discount (which is often accompanied with a large annual fee) cannot demonstrate the relative competitiveness of the loan.

Yellow Brick Road has sought to address this and that is why we have pioneered the concept of 'true rate' advertising – to ensure that we have an informed consumer. Yellow Brick Road believes such disclosure should not be the exception and a matter of individual company choice – it should be the standard in a system that aspires to be consumer rather than insider-orientated.

The Australian Government should therefore mandate 'true rate' disclosure in advertising of financial products to better protect consumers from the hazards of comparing complex effective interest rates.

The 'true rate' would comprise standardised, annualised interest rates to be prominently displayed and communicated pre-contractually, to avoid confusion over compounding and other gradual rises.

There needs to be transparency in how banks advertise their mortgage rates and other rates for financial products and that is why this loophole needs to be closed. Australians are confused by the honeymoon and discount rates being advertised and it is extremely laborious for them to work out the true rate.

RECOMMENDATION 5

Mandate true rate advertising for financial products by amending comparison rate legislation to reflect a true average mortgage of \$300,000 and amend the Trade **Practices Act 1974 to** require the standardised, annualised interest rate to be prominently displayed and communicated pre-contractually, to avoid confusion over compounding and other gradual rises. Discount advertising should be banned because of its high potential for confusing customers into buying inappropriate products.

AUSTRALIANS HAVE THEIR SAY

"As a small business owner and a father of 4 children with a mortgage, I fully support the 5 point plan, especially the clarity around interest rate advertising as it can make it difficult for people to really know what rate they are being charged."

- Sam



3. Require *real banking* competition and encourage consumer mobility

Remove moral hazard - introduce the bank levy

The introduction of a permanent guarantee of deposits from 1 February 2012, following the Government's introduction of a guarantee on deposits and wholesale funding under the Financial Claims Scheme during the GFC²³, exacerbated moral hazard in the Australian banking system in an unprecedented way.

This is the concern that once you start insuring away a private company's risk of failure, you remove the critical disciplining influence of free markets. Bank executives therefore, over time, start behaving less responsibly, and expose taxpayers to even greater risk of loss. In the long-run, this makes them weaker institutions and our financial system depends on the stability of the banking sector.

It was also an international anomaly and it produced competitive distortions, because the ratings agencies' methodology (e.g. Standard & Poor's) assumed that only the major banks will receive a government bailout as they are 'too big to fail' – resulting in cheaper credit for the bigger banks. Similarly, the Government's guarantee for retail deposits held by Australian Deposittaking Institutions (ADIs) during the GFC reduced funding for retail mortgage investment schemes by increasing their relative risk profile, compared with bank or mutual deposits.

Consequently, Yellow Brick Road believes the proposed deposit levy should be implemented. The levy – which Canada has provided an effective model as a precedent to study – would appropriately require banks to pay a fair return for the taxpayer-funded subsidy the banking system receives through the Government's guarantee of deposits up to \$250,000.

It is effectively an insurance premium – or a fair price – for taxpayers guaranteeing the value of deposits under the Financial Claims Scheme. If Australians have to pay for their own insurance, so should the banks – it's as simple as that.

If Australians have to pay for their own insurance, so should the banks – it's as simple as that.

If it is priced correctly, competition will be enhanced because smaller banks – which normally have lower credit ratings and higher funding costs as a result – will be able to access credit more affordably.

On the issue of pricing – of both the RBA's liquidity facilities and the price of government guarantees - it should be set on either a Return-on-Equity (ROE) basis or a flat fee, irrespective of the size of the institution. This is because all APRA-regulated institutions are - and should be - exposed to the active regulation of APRA. Since the government licences the banks, controls their risk management, and can directly remedy any issues it identifies, the government should be willing to rely on itself when determining the price of taxpayer support. The Government should have confidence in its agencies' ability to regulate the sector's capital requirements and risk management. The price should not be based on Standard and Poor's credit rating, which merely promotes size begetting greater size.

Yellow Brick Road has previously proposed a standard rate of half to one basis point, payable per annum on total assets, by ADIs. For the banks with a ROE of greater than 20 per cent, a two basis points per annum fee on total assets would be applied.

The proposed rate is a miniscule price to pay in exchange for taxpayers' guarantees of banks' solvency and stability, particularly given their highly leveraged business models. Modeling by the Australian Financial Review has illustrated that major banks are leveraged 62 to 86 times across their home loans and that allegedly riskier non-major banks carry around half this leverage (approximately 31 times). Furthermore, when one of the big four provide a home loan, they are able to hold less than half the capital to protect against losses on that asset as the smaller banks. It is able to therefore earn twice the returns – with over twice the leverage – as non-major banks.



The big banks also earn a high return on equity – the big four averaged an ROE of 15.9 per cent for the 2013 financial year. For such high ROE rates, they bear relatively little risk because of the implied guarantee that they are too big to fail, and therefore have implicit government support. They also are more profitable, have wider interest margins than banks in most comparable countries and these net interest margins have increased since the GFC. Their profitability and market power has continued to rise during the GFC, partly as a result of this government guarantee. Pricing this guarantee is therefore important.

There is no doubt that banks perform a vital social function – they take short-term savings and use it to fund long-term loans that enable our economy to grow and businesses to innovate at a much faster rate than they might otherwise. Due to the mismatch between the term of funding from deposits and the length of the loans they provide to businesses and households, banks risk insolvency if there is a run on the banks. That is why the RBA provides short-term loans to banks to cover this risk through the committed liquidity facility and the banking regulator, APRA, ensures that banks hold sufficient capital to cover liquidity shocks.

On this latter note, Yellow Brick Road supports the new liquidity coverage ratio (LCR) rules that have resulted from the Basel III global banking rules that are designed to ensure banks maintain an adequate level of high-quality liquid assets to meet its needs for 30 days under a severe shock scenario. As the IMF recently warned, if one of the big four banks ran into significant difficulty, this would "have severe repercussions for the entire financial system, and, in turn, the real economy."

RECOMMENDATION 6

Introduce a bank levy to price the taxpayer guarantee of deposits of up to \$250,000 to provide Australians with a return on their investment and compensate for the risk shifted to the taxpayer.

Promote competition from smaller players – support the RMBS market

To promote competition, wholesale funding access should be developed into a more level playing field. Revenue from the bank levy should be used to support the residential mortgage-backed securities (RMBS) market to enable competitors to the big four banks to source money on similar terms to those big four.

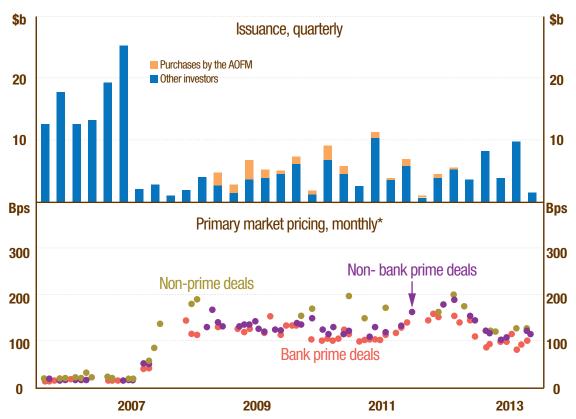
In the 1990's, new challengers to the big banks, such as Wizard, Aussie Home Loans, and RAMS, were able to compete because they utilised wholesale funding through securitisation. As the Senate Committee on banking competition in 2011 noted: "This (securitisation) increased competition in the housing loan market markedly." The GFC

inflicted the RMBS market severely and it has never recovered. As Mr Glenn Stevens, Governor of the Reserve Bank of Australia said (13 December 2010):

...as an asset class globally, mortgage backed securities have had a severe reputational hit. It is certainly true that the ones sold in this country are of fabulous quality but, as an asset class as a whole, unfortunately there has been a reputational hit which will take time to be worked off.²⁷

In the past, the Government's support for securitisation has provided a key source of funding to enhance competition, particularly through the Australian Office of Financial Management (AOFM), however this support has been relatively inadequate compared to the extent of the decline in the securitisation market that resulted during the GFC.

AUSTRALIAN RMBS



*Face value weighted monthly average of the primary market spread to bank bill rate **Source:** RBA



Inadequacies in liquidity in the wholesale Australian Residential Mortgage Securities – traditionally an important source of funding for smaller and non-bank lenders – were brought about by the various preferences for being a creditor to the big four banks stacked in the system.

Yellow Brick Road recommends that the Government supports securitisation of Australian home loans through direct investment – using the banking levy – and facilitated by the AOFM. Issuers would be required to maintain equity in the issued securities on its balance sheet – similar to the Canadian model – to ensure that risk is not offloaded and remains with the issuer.

AUSTRALIANS HAVE THEIR SAY

"Many people don't realise that they actually can negotiate with a lender, just like you can if you were to buy a new TV... Banks should have to compete for our business, and people should feel like they have the power to have those conversations."

- Joanna

RECOMMENDATION 7

The Australian Government should invest the proceeds of the banking levy into a fund that invests in securitisation of home loans through the Australian Office of Financial Management, thereby providing smaller and non-bank lenders with the ability to compete with the four major banks, which currently benefit unfairly from a Government quarantee on deposits but also dominate the market for deposits (and therefore access to funding).



Revise ASIC's mandate to include a competition brief

The Australian Securities and Investments
Commission (ASIC) is one of the main agencies
responsible for regulating the financial services sector.
Under the Australian Securities and Investments
Commission Act 2001, its mandate is to maintain,
facilitate and improve the performance of the financial
system and the entities operating in it.²⁸ However,
there is no clear mandate with respect to ensuring this
occurs with promoting competition as an objective.

The Australian Prudential Regulatory Authority (APRA), for example, "is required to promote financial stability in Australia while balancing its objectives of financial safety and efficiency, competition, contestability and competitive neutrality."²⁹

While it is clear that the Australian Consumer and Competition Commission (ACCC) is the main competition regulator under the Trade Practices Act and has specific powers – for example, with respect to regulating mergers – ASIC should have the mandate to consider factors affecting competition, which should be considered a measure of the effectiveness of the financial system.

There are numerous examples in both existing and proposed legislation and regulations that promote a bias to large product issuers that stifle both competition and innovation. An example is the regulation proposed regarding the supervision of Managed Discretionary Accounts, which are emerging as a competitor to managed funds, with the aid of technological development.

The requirements favour the existing, large-scale retail Funds Under Management (FUM) and platform providers that ironically have little commercial imperative to adopt this consumer-friendly investment vehicle and indeed are incentivised to retain the Unit Trust structure of Managed Investment

Schemes for most savings. The smaller providers, on the other hand, do not necessarily have the resources or capital to meet these requirements.

It is the emerging, smaller industry players that drive industry innovation and change for the benefit of Australians. Consolidation and the lack of a competition mandate for ASIC has all but removed genuine innovation and a better deal for consumers.

RECOMMENDATION 8

The Australian Government should amend the Australian Securities and Investments Commission Act 2001, to change ASIC's mandate to include promoting competition in the financial services system.



4. Supporting both life dreams of a house and a comfortable retirement

Make the two great Australian dreams a seamless reality – encourage lifecycle savings.

Yellow Brick Road believes that both owning your own home and having a comfortable retirement should be attainable aspirations for all Australians.

We believe the financial system should genuinely support both objectives. Unfortunately, the current system treats savings for housing and savings for retirement as competing goals. We need to recognise that they are in fact complimentary.

The Government has already noted this – the Harmer review, for example, previously noted that a person's ownership of their home had a strong impact on their ability to retire comfortably.³⁰

For many Australians, though, there are major challenges to the realisation of these two dreams.

We are seeing a shift to bigger mortgages that take longer to pay off. Whereas 30 years ago, 15-20 year mortgages were common, we are now seeing mortgage terms offered for 30, even 40 years.

Some key facts:

- Nationwide, the average mortgage size is 4.5 times higher than it was in 1990 it is \$305,000 compared to \$69,100 back then.³¹ The graph on the next page illustrates the steep rise in the average mortgage size.
- In Sydney and Melbourne, the average home costs nine times and 8.4 times the median income respectively,³² whereas between the 1960's and the 1990's, it was three to four times

- the average income.³³ The table on the next page graphically illustrates the rising dwelling price-to-income ratio.
- The value of an average home in Australia grew by almost 10 per cent in 2013 to a record of \$615,000.³⁴
- In NSW, the average mortgage grew by \$56,000 in 2013 to more than \$529,000.35
- It is estimated that 620,000 people fell out of home ownership between 2001 and 2010 and were not able to get back into home ownership at the end of 2010.³⁶
- The rate of home purchasing among 25 to 44 year olds has declined 15 per cent in the last 20 years.³⁷
- O The average age of first home buyers has risen from 25 in the 1970's to 31 in 2011, 38
- O The average amount borrowed by First Home Buyers was \$275,000 in 2009-10, up 127 per cent since 1993.³⁹
- O The number of people renting in Australia has doubled since 1981 and about a third of the 1.8 million households renting have done so for more than a decade. The proportion of families with dependent children renting has also increased over this time period. This phenomenon is 'Generation Rent' 40, according to some commentators, and feedback received by Yellow Brick Road shows that doubts about being able to enter home ownership is of concern to many people.
- O At the other end of the spectrum, an increasing number of Australians continue to have mortgage debt aged 55 64 and 65 and older. The proportion of people in those demographic groups has been increasing steadily since 2002.⁴¹ They are then likely to use their superannuation to pay off the mortgage when they hit retirement age and many then go onto the age pension.⁴²

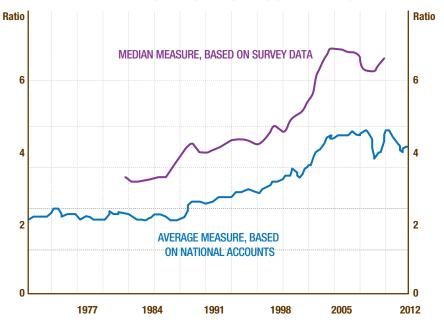
AUSTRALIANS HAVE THEIR SAY

"My kids are struggling to pay rent let alone save money for a home. After child care, rent and food on the table, there is nothing left for savings for a home. This is going to have a huge impact on them in the future. They are typical Aussie kids, they work hard to pay their bills and need a break."

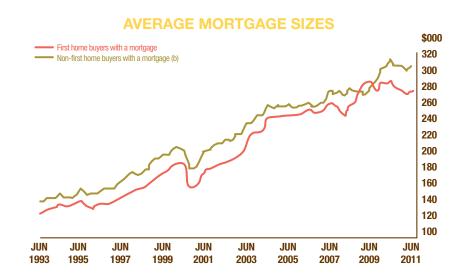
- lan



DWELLING PRICE-TO-INCOME RATIO



Sources: Abelson and Chung 2005, ABS, APM, ATO, CBA/HIA, RBA, REIA, RP DATA RISMARK



(a) In 2009-10 dollars. Adjusted for changes in the Consumer Price Index. (b) Excludes refinancing

Sources: Housing Finance, Australia (cat. no. 5609.0)

While it may sound appealing to have a lengthier mortgage over 40 years – to meet lower monthly repayments – this trend creates its own problems. As mortgages become larger and terms longer, the interest paid increases dramatically, severely cutting into a person's ability to save for retirement.

For example, a \$400,000 loan paid over 40 years (at 7 per cent interest) would cost \$235,000 in additional interest than if they paid it back over a 30 year period. 43 The loan then starts to span (and in some cases exceed) a person's working life.

And now there is speculation that 50 year loans – already offered in other countries like the US – could be offered in Australia.⁴⁴

A recent study has found that people are increasingly accessing their superannuation at retirement and using part of the money to pay off housing debt.⁴⁵ This makes retiring comfortably more difficult.

So working Australians are living on a wing and a prayer. They're hoping that they'll be able to both pay off a home and also save for a comfortable retirement. Those dreams are becoming less and less achievable.



REPAYMENTS FOR \$250,000 MORTGAGE (8% PA INTEREST)	LOAN TERM (YEARS)				
	10	20	30	40	50
Minimum monthly repayments (\$)	3033	2091	1834	1738	1698
Total repayments (\$)	363,983	501,864	660,388	834,374	1,018,911
Total interest (included in total repayment, \$)	113,983	251,864	410,388	584,374	768,911

TOTAL REPAYMENTS ARE BASED ON A MINIMUM MONTHLY REPAYMENT; LOAN FEES AREN'T TAKEN INTO ACCOUNT.

Source: Choice, 'Risky Home Loans - What to Avoid', 2008

Working Australians are living on a wing and a prayer. They're hoping that they'll be able to both pay off a home and also save for a comfortable retirement. Those dreams are becoming less and less achievable.

What's the solution?

There are several options that have been floated to encourage people to better manage lifetime savings throughout their working career: (1) access to superannuation to provide a deposit for a house; (2) introducing a shared ownership scheme for housing; and (3) introducing a new savings account that is attached to a mortgage and that receives favourable tax treatment like superannuation.

The first option – being able to access superannuation savings for the purpose of a deposit on a home – has been proposed by several members of the public through our public consultation process with the draft submission.

This proposal, which would require legislative change, involves a person being able to draw down on their superannuation balance to access the capital to pay for a housing deposit. It is used in countries like Singapore to assist with access to the housing market.

The issue with this approach is that it may assist with entering the housing market, but already the adequacy of retirement savings is a concern for Australians and the Australian Government.

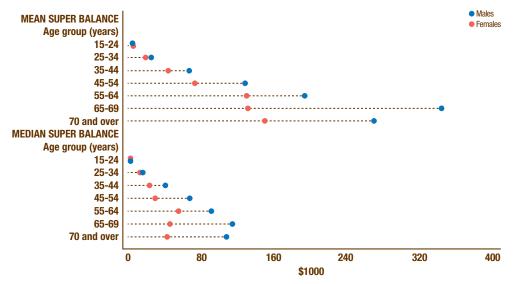
Furthermore, according to ABS figures, 42 per cent of men and 44 per cent of women in the 15-24 age group had no superannuation coverage at all. And the average super balance for 30 year old men is, according to research, \$22,239 and for women is \$20,177.⁴⁶ The ABS figures from 2007 similarly show low balances for people aged 25-34.

From the mid-twenties onwards, superannuation savings start to accelerate and there are likely to be concerns about cannabalising already low superannuation savings before they have a chance to grow.

Yellow Brick Road's view is that Australians need to be able to achieve both goals – home ownership and a comfortable retirement – rather than one goal at the expense of the other. To that end, this proposal has some challenges that need to be carefully considered.



MEAN AND MEDIAN SUPPERANATION BALANCES (A) (B), BY AGE, 2007

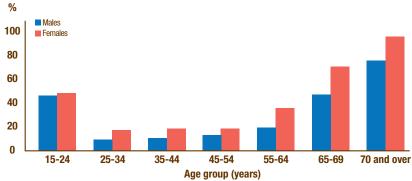


(a) For yp to three superannuation accounts in accumulation phase.

(b) Means and medians are calculated using known values (i.e missing values and excluded).

Sources: ABS data available on request, Survey of Employment Arrangements, Retirement and Superannuation 2007.

NO SUPERANNUATION COVERAGE, BY AGE 2007



Sources: ABS Employment Arrangements, Retirement and Superannuation, Australia 2007 (cat. no. 6361.0)

A second possible solution is to move to a model that has been adopted by the UK and US Governments whereby the consumer purchases part of the house and private investors purchase the other part – possibly through superannuation funds if that is attractive to them and also possibly with the addition of a means-tested Government subsidy.

Known as a 'shared equity scheme' or 'shared ownership scheme', it has assisted people to partly buy their property – with a smaller deposit and smaller repayments – while paying a small amount of rent at the same time on the part that they don't own.

It's a creative combination or an amalgam of being both an owner and a renter and has been popular in the UK. Many shared owners aim to buy out the private investor's ownership to eventually move into full ownership. However, there have been reports in the UK that the odds are not high – with only one in four expanding their share of ownership over time.⁴⁷

There are versions of this scheme already on offer by some State Governments, particularly WA and the ACT, as an alternative to social housing, which is severely overburdened. It's a scheme that has some attraction in a country like ours where housing prices are growing so strongly, making it difficult for aspiring first home buyers to enter the housing market.



AUSTRALIANS HAVE THEIR SAY

"I so agree. I have often wondered why we can't have a similar system to the 401k system where I can borrow money from my super account and at agreed value fixed term so my super account gets the interest rather than a bank. My wife and I are in our mid 30's and collectively our super balance is enough to pay out our home loans. Why I can't borrow some of that, not all, giving money to my pocket not the banks... means loans paid off quicker and I can invest more of the excess cash into building this country."

- Name withheld

If it is correctly designed, and Australians entering into the arrangement are fully informed of any possible risks, this model could assist thousands of Australians to achieve their dreams of home ownership.

The third option is to move towards a lifecycle saving product that helps people pay off their home loan more quickly and set them up for a pattern of saving that lasts a lifetime.

We know that the average couple needs a million dollars to retire comfortably – but what too many people are facing at retirement age is lingering mortgage debt.

Yellow Brick Road proposes that the Government could apply the same tax preferred settings that apply to superannuation to a new form of savings – where these savings are additional contributions to a mortgage for the principal place of residence above and beyond the minimum repayments.

These payments would be paid into a 'Savings for Life' account that sits as an offset account to the mortgage and attracts the same preferred tax rate that additional superannuation contributions attract.

This addresses the problems Australians are facing with longer, later, larger mortgages eating into their ability to save for retirement. It encourages accelerated payment of a home and frees up income later in a person's lifecycle that would otherwise have been used to pay for the accumulated compound interest during that time.

Too many Australians are using their superannuation at retirement not to fund their costs of living but to pay off their mortgage debt and then collect the age pension. And this is after the banks have already profited from compounded interest over the longer, later, larger mortgage.

For example, a young woman, Wendy Smith, takes out a \$300,000 mortgage on a 25 year term and we assume she pays a six per cent interest rate. She receives a pay rise at work so she decides to put an additional \$150 into the mortgage each month (around \$5 a day). This would:

- Reduce the total amount paid by Wendy over the life of the loan by over \$48,000.
- Result in the loan being paid back almost four years earlier (45 months), freeing up Wendy to start saving for retirement.
- O Achieve a tax savings of \$315 a year*.

*If this savings proposal is taken up, there would be savings on tax because, within the contribution limit, the tax rate is 15 per cent as opposed to the normal income tax rate. So for people earning between \$37,001 and \$80,000, the rate is 32.5 per cent for each dollar above \$37,001⁴⁸, which would be a savings of \$315 a year in tax.

This way, this saving offset account acts in a complementary way to superannuation. Rather than allowing longer, later, larger mortgages to stunt retirement savings, this encourages a pattern of savings and earlier finalisation of mortgage debt.

Once Wendy has paid off her loan, she has created a habit of saving. If she then continues to put the same monthly payments into her superannuation account for another five years, she will end up with an additional \$24,995 in her superannuation each year, or an additional \$124,975 at the end of the five years.



The possible characteristics of such a 'Savings for Life' account might be:

- People opt in to a lifecycle product that covers one principal place of residence;
- The preferred tax benefit for housing repayments is limited to "additional" payments only that cannot be redrawn (except in extreme circumstances, which are covered under existing superannuation laws);
- The home payment offset account is time limited (until a threshold age for example – say 50 or 10 years to the minimum retirement age of 60) or tapered out from 40 onwards – although there are varied views on whether this is fair on older mortgagors;
- There could be a cap applied to the value of additional payments to the mortgage permitted to make the 15 per cent tax deductions affordable for the Government's budget;
- It could be potentially tied to shorter mortgage payment periods to encourage early repayment; and/or
- An increased contribution requirement (being a portion of the foregone mortgage repayment amount) potentially being tapered in from 40 onwards to bulk up retirement savings.

Yellow Brick Road is agnostic regarding the means to achieve more national savings for the purpose of retirement. We do note that several countries including Canada, Singapore, South Africa, France and New Zealand have linked their superannuation systems with their housing system in various ways, recognising that they are intertwined in terms of outcomes.

Savings are savings and they should be rewarded because they set Australians up for retirement. There is little point lecturing young Australians on the need to save for retirement if they are hard-pressed trying to juggle a family, work and a mortgage.

During the earlier stages of life, meeting rent and or making home loan repayments will take a higher priority than making additional retirement savings. While many baby boomers are currently using their post mortgage and post family period to bulk up superannuation savings, current trends mean that

more people are still facing significant mortgages later in life.

The Savings for Life option is an innovative policy proposal that encourages people to attain both Australian dreams – secure housing and a comfortable retirement. It's not one Australian dream or the other – it's both that we need to recognise as fundamental to financial security.

AUSTRALIANS HAVE THEIR SAY

"I am a woman, 59 next month, who works full time and still has a mortgage. I have been through split ups and property settlements, so I have been scrambling for years to try and work towards a secure old age. I took out a mortgage only 6 years ago; yes, I had monies from a property settlement which I used as my deposit for my current home. I have thrown as much money as I can into this mortgage and had to stop making extra payments in my super, I just could not afford to do both. I have recently had to cut down on how much I pay each fortnight on the mortgage as I could not afford food! Just the thought of a tax break for extra payments on my mortgage has me thinking and working out how much more I could put into my super. As you say, I too am looking at using my super to pay out my mortgage when I retire. When I do this, I will be back to living on the age pension, which is not something I ever planned to do. What an excellent idea, tax breaks on extra payments on the mortgage."

- Chrissy



AUSTRALIANS HAVE THEIR SAY

"Whilst I totally agree with this concept I do have one exception. Having it time limited or tied to aged 50 is really disadvantaging the older home loan [borrowers]. Not everyone starts a home loan in the early years and some people for various reasons start home loans in their 40's. Why not give them the same opportunity, as most of them will be struggling towards the end of their working life to pay off the loan also? These people actually might struggle more than the younger home loan holders."

- Tony

RECOMMENDATION 9

The Australian Government should incentivise saving across a person's lifecycle, recognising that younger people are focused on securing a home before they can turn their mind to saving for retirement. But the two goals are not mutually exclusive owning a home is an indicator of a comfortable retirement. There are a range of options for the Government to consider, including shared equity schemes for people to be able to enter the housing market earlier and start paying off a home, or a new 'Savings for Life' product where additional contributions to the mortgage sit in an account linked to the mortgage for their place of residence and those payments are treated preferentially under the tax system just as superannuation contributions are. This will help to address insecure housing, encourage a pattern of savings and address the perverse outcome where superannuation is used to pay off housing debt upon retirement - after the banks have already profited from their longer, later, larger mortgage.

5. Create a fairer system for the outsiders - women, small business, young people

Many Australians that are retiring have insufficient funds to be able to retire without experiencing financial stress. Empirical evidence overwhelmingly points to a severe underfunding of at least the next two generations heading towards retirement at the same time as the tax base shrinks from a demographic bulge that cannot be bridged.

In some respects, improving financial literacy assists by educating younger generations to manage money and save for their retirement. But half our population are women, and many of them struggle to retire because of abysmal superannuation savings. Women tend to work in lower paying positions, or are getting paid less than their male counterparts to fulfil the same roles. Many women also miss out on accumulating superannuation savings while they are out of the workforce raising their children. If we're not supporting women and giving them the same opportunities as men, we alienate half the population and it just so happens to be the half that lives longer and needs more superannuation savings, not less.

This puts enormous stress on women and their families. It is estimated that the financial disadvantage women will have at retirement will be as high as \$1 million in the course of a lifetime due to their disjointed career trajectory and the fact that they earn an average 17 per cent less than men.⁴⁹

Small business owners also find it extremely difficult to prioritise retirement savings because of the need to ensure that free cash is available for the small business to survive and grow. Managing cash flow is critical and that's why we support making advice more affordable to small businesses by allowing tax deductibility for people earning up to \$75,000 and by simplifying the regulations so that costs for small business seeking professional financial advice are lowered.

Yellow Brick Road applauds the Federal Government's paid parental leave policy, which is both pro-women and pro-small business. The policy will enable small businesses to attract and retain women in the workforce, rather than lose them to big businesses that can afford to have extensive paid parental leave policies.

However, more needs to be done to ensure that women, small businesses, and other people that have highly variable incomes are able to save enough for retirement. One possible option may be to open up contribution limits where an averaging up to a cumulative five year period can be grossed up and made in a shorter time period. This should be adopted regardless of gender, given it addresses the reality that many people are unable to save fully and consistently every year. Another option would be to allow a couple to pool their contribution limits, so that the gender gap can be bridged through combined earnings.

RECOMMENDATION 10

To address the inequality in superannuation in the system, the Australian Government should amend contribution limit rules to average up to a cumulative five year period and allow pooling of contributions with a spouse. This will particularly assist women, small businesses and other Australians that have variable incomes.

AUSTRALIANS HAVE THEIR SAY

"I agree with all, especially the part about helping people who have bumpy incomes. I am self-employed and my super is non-existent because other things come first. I'm hoping my business will be my retirement savings but there are no guarantees. If something was done to look out for self-employed people, I think that would really help."

- James



Conclusion

If the Campbell inquiry was about efficiency, and Wallis was about 'regulation', this inquiry should be about competition and giving the outsiders to the financial system a fair break and opportunity to participate.

There are economic and social costs of the lack of competition in the financial services market.

The bias towards the 'insiders' – the 'insider' banks and the 'insider' consumers – needs to be rectified in the interest of fairness.

Our financial services system should be rebalanced to serve the national interest and the interests of the vast majority of Australians.

We need to encourage a system that teaches people how to structure themselves financially so they can have knowledge and information to make financial decisions in their interests.

We need to ensure competition and transparency – to ensure that consumers have a real choice.

We need to look at cutting red tape to ensure equal opportunities for all people, irrespective of their socioeconomic status. We need to make the great Australian dreams of owning a home and having a comfortable retirement a reality for all people, not just the insiders and the privileged few.

That's why Yellow Brick Road is endorsing the following five point plan for the panel and the Government's consideration:

- More help for Australians to master their personal finances
- More transparency in interest rate advertising
- Require real banking competition for real consumer choice
- Supporting the life dream of a house and a comfortable retirement
- Create a fairer system for the outsiders women, small business, young people

Yellow Brick Road appreciates this opportunity to make a submission and we would welcome any further discussion and debate to ensure that Australian consumers get a better deal out of the financial system.



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