



Australian Council of Social Service

'Surviving, not living'

**Submission to Senate Employment
Committee on the adequacy of
'allowance' payments**

ACOSS Paper 192

August, 2012

First published in 2012 by the Australian Council of Social Service

The Australian Council of Social Service is the peak body of the community services and welfare sector and the national voice for people affected by poverty and inequality. ACOSS' vision is for a fair, inclusive and sustainable Australia where all individuals and communities can participate in and benefit from social and economic life.

Locked Bag 4777
Strawberry Hills, NSW, 2012 Australia
Email: info@acoss.org.au
Website: www.acoss.org.au

ISSN: 1326 7124
ISBN: 978 0 85871 055 9

© Australian Council of Social Service

This publication is copyright. Apart from fair dealing for the purpose of private study, research, criticism, or review, as permitted under the Copyright Act, no part may be reproduced by any process without written permission. Enquiries should be addressed to the Publications Officer, Australian Council of Social Service. Copies are available from the address above.

CONTENTS

Summary	5
Living standards.....	6
Work incentives	7
Employment services	8
Future reform.....	8
Recommendations for the 2013 Budget:.....	10
Recommendations for future reform:.....	11
I Reliance on working age income support payments and rates and payment	13
1.0 Income support payments.....	13
1.1 The changing profile of people of working-age on social security payments	15
1.2 Current rates of payment	17
2 Policy history	19
3 The adequacy of allowance payments	23
3.0 Poverty lines.....	24
3.1 Budget standards.....	26
3.2 Deprivation.....	28
3.3 Financial stress	31
3.4 Allowance payments compared to wages	33
3.5 Single Allowance rates and inflation.....	34
3.6 The assets of pensioners and allowees	35
3.7 Post-secondary student payments.....	38
3.8 Conclusions on the adequacy of allowance payments.....	41
3.9 Recommendations to improve the adequacy of allowance payments in the short term.....	42
4 Paid work incentives	44
4.0 Incentives to move into fulltime employment.....	44
4.1 Incentives to undertake part time and casual employment.....	48
4.2 Recommendations to improve incentives to undertake part time and casual employment.....	52
5 Necessary improvements to employment services	53
5.0 Choice of provider	55
5.1 Investment in people unemployed long term	55
5.2 Wage subsidies	57
5.3 Recommendation for the 2014 Budget:.....	57

6	Future reforms of the support system for people of working age	58
6.0	Policy development.....	58
6.1	Recommendations for policy development.....	60
6.2	The pension-allowance system	61
6.3	Pressures for change	62
6.4	A framework for reform	65
6.5	The UK experience with income support reform.....	69
6.6	Recommendations for future income support reform.....	71

Summary

This inquiry is examining:

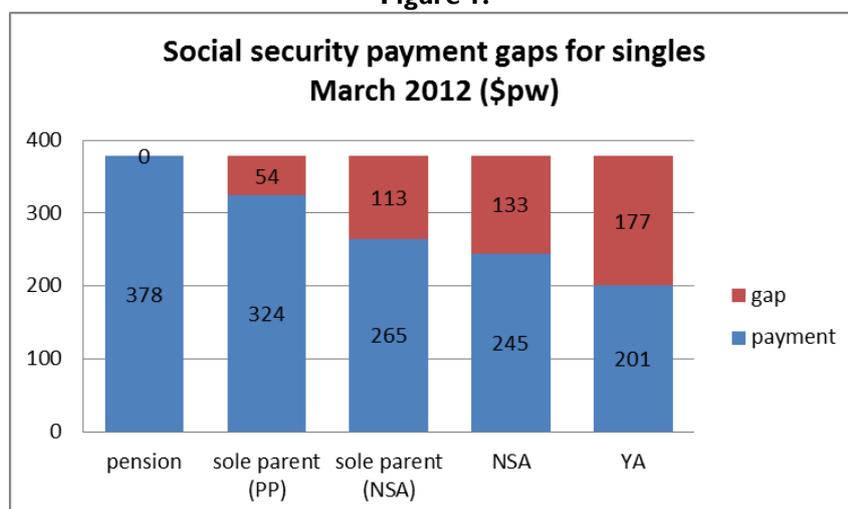
'The adequacy of the allowance payment system for jobseekers and others, the appropriateness of the allowance payment system as a support into work and the impact of the changing nature of the labour market.'

The Inquiry is timely because it deals with unfinished business from the Harmer and Henry reviews three years ago. It is important because it assesses payments for those living in the deepest poverty.

The system of income support payments for people of working age¹ is divided into three tiers: pensions such as Disability Support Pension (DSP), Allowance payments for people participating in the labour market including Newstart Allowance (NSA) and Youth Allowance (Other - YAO), and student allowances including Youth Allowance (student- YAS) and Austudy Payment. Compared to pension payments, Allowances are lower, have tighter income tests, and have activity requirements such as job search or study.

In March 2012, the maximum single rate for NSA was \$245 per week or \$35 a day. This is \$133 per week less than pension payments such as age and disability pensions. Further, student payments such as YAS for single people living independently of their parents are currently \$210, which is \$44 per week less than NSA. The rate of NSA for sole parents is \$59 less than the Parenting Payment Single (PPS) payment for sole parents, which in turn is \$54 less than other pensions (figure 1).

Figure 1:



In 2008 the Harmer Review examined the adequacy of pension payments and recommended a substantial increase in single rates of payment to bring their average living standards up to that of partnered pensioners. In 2009, the Government legislated a \$32 per week real increase (now significantly greater due to indexation) for single pensioners, to 66.3% of the combined married pension rate. Allowance

¹ Payments for adults aged 18 to 64 years.

payments were excluded from that review, along with one pension payment (PPS) and those people missed out on the increases.

Due to the different indexation arrangements for pensions and allowances, the gap between the single pension and Newstart Allowance payments rose from \$55 per week in September 2008 to \$133 per week today. On current trends, by 2040 the single Newstart rate will be just half that of the pension.

The Henry Report on the tax-transfer system acknowledged that Allowance payments were inadequate, at least for single people, and that the growing gap between pensions and allowances was inequitable and counterproductive in encouraging people on income support payments to seek employment. It recommended that the formula applied by the Harmer Report to pensions – a single rate equal to 66.3% of the combined partnered rate – should also apply to Allowance payments. Currently, that would require an increase of approximately \$50 per week in the single rate of the relevant Allowance payments. It also recommended that allowance payments should be indexed to a measure of wages as well as the CPI, to prevent the gaps between pension and allowance payments from growing.

Living standards

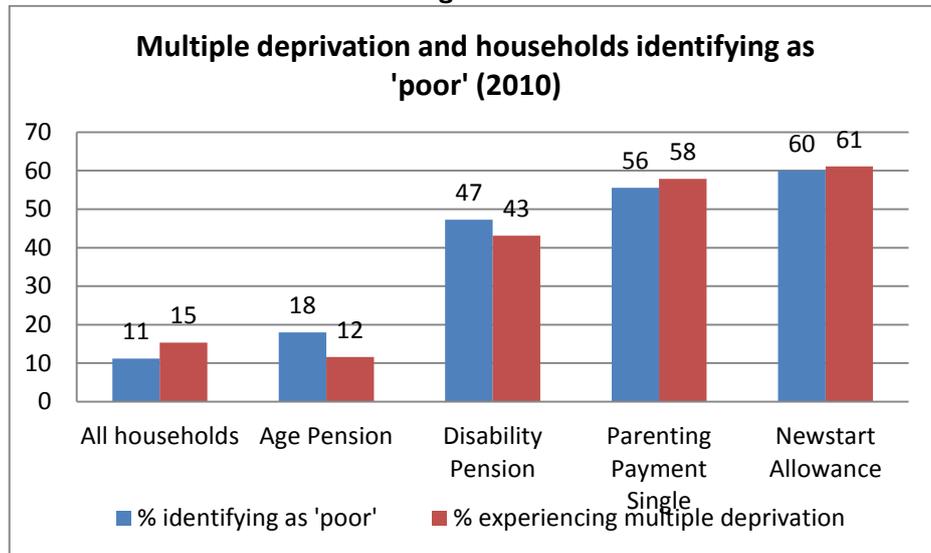
There are 800,000 people receiving employment related allowance payments such as NSA and YAO, and another 400,000 receive student payments (YA, Abstudy and Austudy Payment). Most are living in poverty, especially single people on the \$35 a day NSA (which has not been increased in real terms since 1994) or \$29 a day student payments. Their living standards are still frozen at a point in time when the internet was in its infancy.

Since 1994, the single rate of NSA has fallen from 92% to 72% of the poverty line and from 26% to 21% of the fulltime median wage. Its purchasing power has declined by \$8 a week since the cost of essential goods and services such as rent and utilities has risen more quickly than the CPI.

The single rate of Age Pension (AP) is a very frugal payment and ACOSS welcomed the increase granted in 2009. The evidence shows that people of working age on social security payments, many of whom missed out on that payment increase, face deeper financial hardship:

- Among people receiving NSA, PP or DSP, at least a third lacked \$500 in emergency savings compared with 21% of all households;
- 40% of people on NSA could not afford to pay a utility bill on time in the past year, compared with 12% of all households;
- One fifth of children in families receiving NSA or PP lacked up to date school uniforms and books;
- Between 47% and 60% of people receiving NSA, PPS and DSP identified their household as 'poor' compared with 11% of all households (figure 2).

Figure 2:



Source: Social Policy Research Centre, "Multiple deprivation" refers to % of households lacking 3 or more of 24 essential items.

People receiving allowance payments have few resources to fall back on if they cannot meet their basic needs on \$35 a day. In our rigorously targeted social security system a single person cannot receive any NSA payment if they earn more than \$455 a week or have more than \$2,500 in the bank.

Only 18% of people on NSA own or are purchasing their home. Half rent privately and they have faced sharp increases in rents over the last five years. A single person on NSA receives up to \$60 a week in Rent Allowance, or \$71 per week if they have children, but this covers only a fraction of market rents. For example, the median rent for a two bedroom flat in Sydney is \$450 and that in Melbourne is \$295.

Work incentives

There is scope to increase the single rate of NSA substantially without undermining work incentives. A single adult on NSA more than doubles their after tax income if they obtain a fulltime job paid at the minimum wage.

The single rate of NSA has fallen in proportion to the minimum wage (after tax) from 52% to 45% since 1994 when it was last increased. An increase of \$40 per week would merely restore the payment's former value relative to minimum wages.

Compared to wages, the single rate of NSA is the lowest unemployment payment in the OECD, at just 40% of a low fulltime wage after tax (two thirds of the average wage), including Rent Assistance.

Families with children keep all of their Family Tax Benefit (FTB) when a parent moves from income support to the fulltime minimum wage, a fact that is often

neglected when assessing work incentives for unemployed families. The OECD calculates that the income of an unemployed couple with two children is equal to 70% of that of the same family on two thirds of average earnings.

The NSA income test *does* discourage *part time and casual employment* because people can only earn \$31 per week before payments are reduced by 50 cents in the dollar or more, and they can only earn about a week's minimum wages in a casual job every six months before the 'earnings credit' runs out.

Employment services

Reliance on income support payments among people of working age has fallen substantially in the last decade, from 18% of all people of working age in 1999 to 14% in 2011. But as unemployment falls, those on income support are increasingly drawn from groups disadvantaged in the labour market.

Of the people who received unemployment allowances in 2010, one in six had a disability ('partial work capacity'), one in three was over 44 years old, one in ten was Indigenous, and roughly half had less than Year 12 qualifications.

In March 2012, 62% of people receiving unemployment allowances were on income support for more than 12 months. It can no longer be claimed that allowances are short term payments to tide people between jobs. Even though a substantial group of people on NSA cycle on and off the payment within a given year, the vast majority of the funds spent on NSA are supporting long-term recipients whose chances of securing employment within the next 12 months are only about 50:50.

Employment services such as the Job Services Australia system can make a difference to their employment prospects, but JSA providers are currently only funded to interview people unemployed long-term once every two months together with \$500 in an Employment Pathway Fund to invest in work experience and training. This is clearly inadequate to overcome the hurdles to employment this group faces. Last year's Budget invested in 10,000 wage subsidies to give people unemployed 'very long term' (24 months) a chance for 6 months of paid work experience in a regular job. Well targeted wage subsidy schemes work and this one should be expanded.

Future reform

It is over a decade since the system of income and employment supports for people of working age on income support was reviewed, in the 'McClure review'. Given the changing profile of those who receive these payments, the opportunity to end their labour market exclusion if population ageing gives rise to labour shortages, and the unfinished business of reform of social security and employment services, it is time for a thorough reassessment of the system.

The McClure Report recommended structural reform of the system of working age payments: to replace the current three tier system of pension, employment allowances, and student payments with a much simpler system based on a common minimum rate of payment with supplements for additional costs such as the costs of disability, raising a child alone, caring, and rent.

A social security system based on need rather than out-dated judgements about 'ability to work' would be fairer. It would also strengthen workforce participation since people would no longer face the risk of transfer to a lower payment as they seek employment (as people on the DSP payment do now) and activity requirements could take better account of the diversity of people's circumstances. The social security system could devote its energies to alleviating poverty and helping people secure employment instead of sorting them into an ever more complex array of payment categories.

A restructure of income support broadly along these lines is under way in the United Kingdom, where simplifying the system to improve workforce participation is a bipartisan commitment. Structural reform to make the social security system simpler and fairer deserves wide support and careful consideration in Australia.

In this submission we argue that the following changes be introduced in the 2013 Budget:

- An increase of \$50 per week in the *maximum single rate* of allowance payments for adults on allowance payments and people on YA living independently of their parents and 'away from home' from March 2014 (benefiting around half a million people);
- the indexation of these allowance payments (including for couples) to wage movements from then on;
- a simpler income test for NSA including a simpler earnings credit;
- improvements in employment assistance, especially Job Services Australia assistance for people unemployed long-term.

These benefit reforms are consistent with Henry Report recommendations.

Over the next few years we recommend that the system of social security payments and employment supports for people of working age be independently and publicly reviewed:

- Over the medium term, structural reform of the system of income support payments for people of working age should be undertaken to replace the present three tier system of payments for people of working age (pensions, employment related allowances and student payments) with a common 'core' rate of payment together with supplements for additional living costs.

'Living on the dole is not living, it's surviving.' (Graham, Newstart Allowance)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, University of Melbourne, Allen & Unwin. (name changed to protect privacy)

Recommendations for the 2013 Budget:

1. (a) Allowance payments for single people (other than those on student payments) should be increased by \$50 per week from March 2014, and benchmarked to 66.3% of the combined married couple rate of Allowances as is the case for pension payments (a higher rate in the case of sole parents). This applies to people on Newstart Allowance, Widow Allowance, Sickness Allowance, Special Benefit, Crisis Payment, and those on Youth Allowance (Other) living independently of their parents and away from the parental home.

(b) Allowance payments for single people on student payments (Austudy Payment, Abstudy Payment and Youth Allowance Student) who are living independently of their parents and away from the parental home should also be increased by \$50 per week from March 2014 and benchmarking of those payments to 66.3% of the married rate should be phased in.
(Cost: approx. \$500 million in 2013-14 or \$1,500 million in a full year)
2. From March 2014, all of the above Allowance payments (for singles and for couples) should be indexed at least annually to movements in a standard Australian Bureau of Statistics measure of typical fulltime wage levels (before tax), as well as six monthly to movements in the Consumer Price Index.
3. From March 2014, the following changes should be made to the income test for the Newstart Allowance and Youth Allowance (Other) payments in order to encourage participation in casual employment, simplify the system for unemployed people, and reduce over and under-payments:
 - (a) The working credit should be replaced by a simpler system where people on allowances can 'bank' their fortnightly income test 'free area' for up to 26 weeks;
 - (n) The free area should be increased by \$9 per week to \$40 and the 50% and 60% taper rates replaced by a consistent 60% taper rate;
 - (c) the 'free area' should subsequently be indexed to the CPI.
4. From 2014, Job Services Australia services should be improved by:
 - (a) increasing service fees and Employment Pathway Fund allocations for each year of the 'Work Experience Phase' for people who are unemployed long term, to at least the levels provided for Stream 3 clients in their first year of unemployment.
(Cost: approx. \$200 million in a full year)
 - (b) expanding the current wage subsidy scheme for 'very long term unemployed people' to 20,000 places a year and introducing a scheme that fully subsidises 6 months of paid employment (e.g. in the community sector or social enterprises)
(Cost: approx. \$300 million in a full year)

Recommendations for future reform:

5. An independent public inquiry should be established to critically assess current employment participation policies for people receiving income support payments and recommend future directions for reform.
 - (a) Its Terms of Reference should include assessment of:
 - recent labour market trends and future employment prospects for people on working-age income support payments
 - trends in reliance on income support including the current and likely future profiles of people on social security
 - the adequacy, targeting and employment effects of income support payments for people of working age, and options for reform to facilitate transitions to employment, improve fairness and simplify the system
 - the effectiveness of employment services for disadvantaged jobseekers (Job Services Australia and disability employment services), including how these might be better integrated with vocational training, work experience, and social support services.
 - (b) The inquiry should be led by a small panel of independent experts and supported by a Secretariat drawn from the relevant Government Departments.
 - (c) It should prepare issues papers on the above topics including options for reform, consult widely with stakeholders and policy experts, and prepare a report with recommendations for Government within 18 months of its establishment.
6. If the inquiry described in the above recommendation is not established by December 2012, a separate independent review should be conducted into the effectiveness of the Job Services Australia program to inform a re-design of the system in advance of the 2015 contracts:
 - (a) This review should be led by a small panel of independent experts and supported by a Secretariat drawn from the Employment Department.
 - (b) It should prepare an issues paper outlining the strengths and weaknesses of the present system and future challenges and options for reform, consult widely with stakeholders and policy experts, and prepare a report with recommendations for Government within 12 months of its establishment.
7. Over time, the present three tier system of income support payments for people of working age (pensions, employment-related allowances, and student payments) should be replaced by a system with:

- (a) a common base rates of payment for singles and partnered people respectively, based on a minimum acceptable standard of living
- (b) common basic eligibility requirements such as residency
- (c) activity requirements that adjust in flexible fashion (from none to regular job search) to any constraints imposed by disabilities or caring responsibilities and each individual's pathway to employment (including fulltime study where appropriate)
- (d) income tests that target individuals and families in greatest need of income support while encouraging part or fulltime employment as appropriate – including major reform of the income-test treatment of irregular employment
- (e) supplements for additional non-discretionary costs experienced by a substantial minority of people receiving people on income support including the costs of disability, caring, sole parenthood, and rent – while retaining a separate system of Family Tax Benefits to assist with the costs of dependent children.

I Reliance on working age income support payments and rates and payment

I.0 Income support payments

The system of income support payments² for people of working age is divided into three tiers: pensions such as Disability Support Pension (DSP), Allowance payments for people participating in the labour market including Newstart Allowance (NSA) and Youth Allowance (Other - YAO), and student allowances including Youth Allowance (student- YAS) and Austudy Payment. Compared to pension payments, Allowances are lower, have tighter income tests, and include activity requirements such as job search or study (table I).

Altogether, 1,200,000 people receive allowance payments comprising 800,000 with employment related payments and 400,000 with student payments.

By 'income support' payments we mean social security payments to meet the basic general living costs for adults and young people without adequate means of support, as distinct from Family Tax Benefits for children and supplementary payments for special costs such as Rent Assistance. In Australia, income support payments are paid at flat maximum rates regardless of previous earnings, and are income-tested to target them towards in greatest need of financial support. They are the basic safety net payments in our social security system. By 'working age' we mean 18 to 64 years.

Table 1: Major working-age income support payments

Payment	Target group	Number of recipients (2011)
Pensions (paid at higher rate, less or no activity requirements, more liberal income tests)		
Disability Support Pension (DSP)	People with disabilities assessed as 'unable to work full or part time'	819,000
Parenting Payment Single (PPS)	Sole parents of children under 8 years old	326,000
Carer Payment (CP)	People providing constant care for a person with a disability	186,000
Sub-total	Pension payments	1,330,000
Employment related allowances (paid at lower rate, more activity requirements, tighter income tests)		
Newstart Allowance (NSA)	Unemployed adults	527,000
Youth Allowance Other (YAO)	Unemployed young people up to 21 years	86,000
Parenting Payment Partnered (PPP)	Primary carer of children under 6 years in a couple	118,000
Widow Allowance	Widow over 50 years	29,000*
Widow Pension	Widow over 50 years	1,000*
Partner Allowance	Partner of allowance recipient	17,000*
Wife Pension (of DSP recipient)	Partner of disability pensioner	12,000*
Sickness Allowance	Temporarily ill while employed	7,000
Special Benefit	General safety net payment	6,000
Sub-total	Allowance payments	800,000
Student allowances (paid at lower rate, fulltime study requirement, more liberal income tests)		
Austudy/Abstudy Payment	Full time students over 24 years /Indigenous students	76,000
Youth Allowance Student (YAS)	Fulltime students up to 24 years	325,000
Sub-total	Student payments	400,000
All		2,540,000

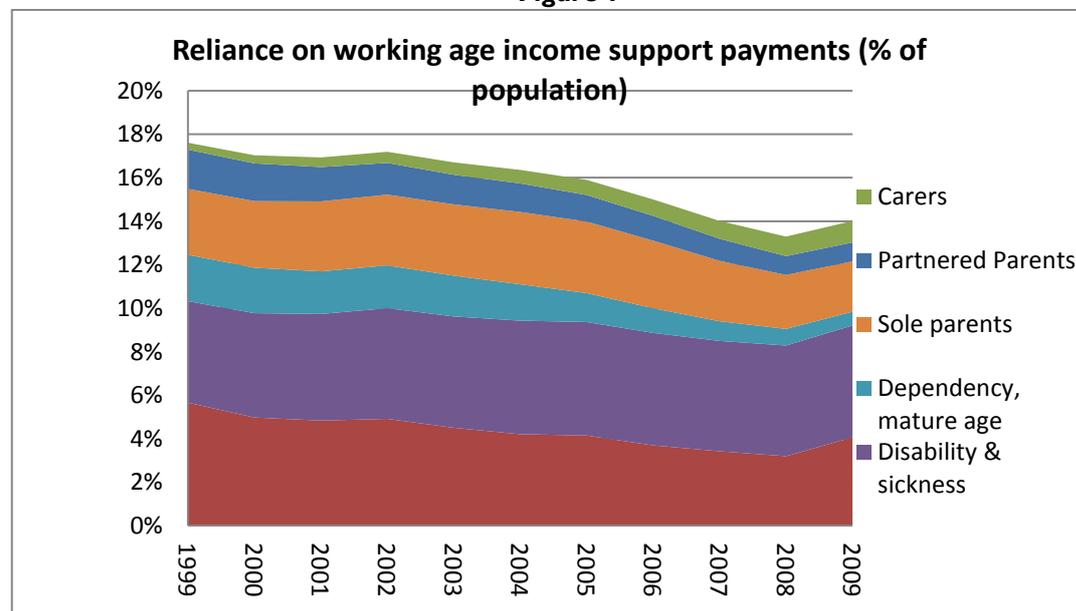
Source: FAHCSIA 2012, Income support payments a statistical overview, Statistical Paper No 10.

* payment is being phased out

1.1 The changing profile of people of working-age on social security payments

Over the decade prior to the GFC in 2009, reliance on these payments fell sharply in proportion to the population of working age (figure 1). This was due to a combination of solid employment growth, the extension of activity requirements and employment supports to groups previously exempted (including many mature-age people), and a tightening of income test for some groups (including sole parents affected by the 2006 'welfare to work' policy). Reliance on working age payments in Australia is below the OECD average level.

Figure 1



Source: FAHCSIA (various years), Income support customers: a statistical overview; OECD population data
 Note: Excludes student payments and aged and veterans payments.

'Dependency and mature age' refers to payments that are being gradually phased out for people over 50 years of age, for example Widow Allowance and Mature Age Allowance. New applicants for income support are not generally able to claim these payments.

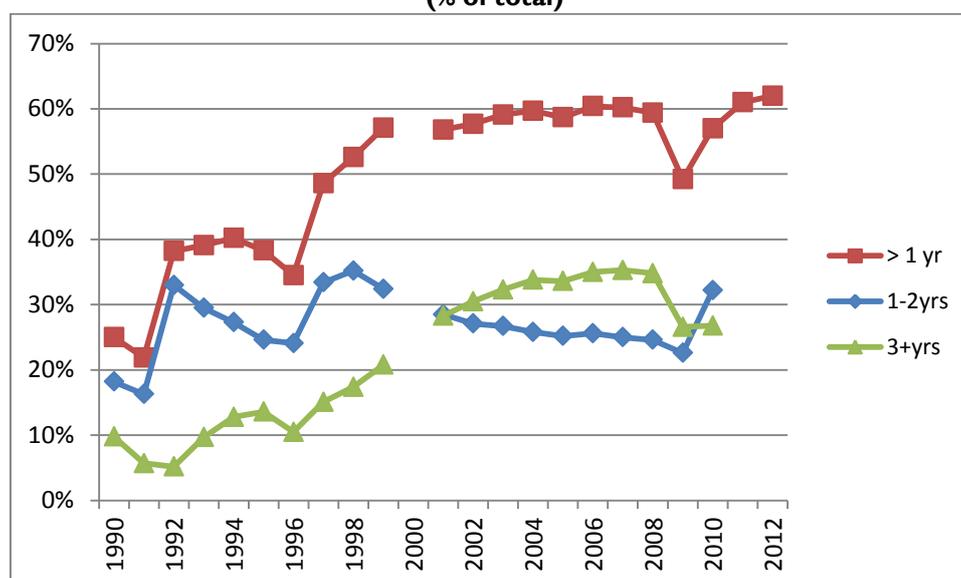
On the other hand as unemployment has fallen, the profile of those still reliant on income support has become more disadvantaged. This is reflected in the higher overall proportion of people on non-activity tested payments such as the DSP, and the more disadvantaged profile of those on activity tested payments such as NSA and YAO payments.

In March 2012, 62% of people on NSA/YAO had received income support continuously for over one year and at least one quarter for over 3 years (figure 2). The proportion of long-term recipients (top line) rose from the mid 1990s, fell after the GFC (as more new claimants entered the system), and subsequently resumed its upward trajectory (as the economy recovered and more people on payments 'short term' left the system). In addition, an unknown but probably growing proportion of 'shorter term' NSA/YAO recipients had a previous spell on social security payments

within the last few years and are ‘churning’ on a long-term basis between income support and casual employment.

Another way to profile people on NSA is to compare the circumstances of all individuals who receive the payment throughout a given year. We do not have access to the data required to do this, but it is likely that when counted in this way a higher proportion would be short-term recipients (those with less than a year’s duration). Nevertheless, long term recipients still account for the majority of the annual fiscal cost of the payment because each receives the payment for a longer period of time.

Figure 2: People receiving Newstart and Youth Allowance (Other) by duration (% of total)



Source: FAHCSIA (various years), Income support customers: a statistical overview; DEEWR (2011 & 2012), Labour market payments.

The profile of people receiving NSA/YAO is also disadvantaged in the labour market in other ways (table 2):

- one in six has been assessed as able to work part time only due to a disability,
- one in sixteen is a sole parent,
- one in ten is Indigenous,
- one in three is over 44 years of age,
- half of people participating in Job Services Australia services have less than Year 12 qualifications³.

‘You know, like I’ve had one (employment service) consultant admit to me that when you hit fifty, you’re not going to find a job ever again... I think if you fall in the too-hard basket for them, they’ll go through the motions and I’m sure they’ll say, get up and swear on a stack of bibles that they’re looking for work and all that for you, but in reality, no.’ (Jimmy, Newstart Allowance)

Murphy et al 2011, ‘Half a citizen’: The stories of 150 welfare recipients in Australia, Allen & Unwin.

³ The last statistic comes from DEEWR 2011, Labour market assistance outcomes.

**Table 2: Characteristics of people receiving Newstart and Youth Allowance (other)
(August 2010)**

	Number	%
Sex and age		
Male	369,134	60%
Female	248,051	40%
Under 25 years	163,760	27%
25-44 years	255,098	41%
Over 44 years	198,327	32%
Other key characteristics		
Over 1 year on income support ²	379,000	57%
Over 3 years on income support	172,000	27%
Indigenous	60,431	10%
Disability ¹	96,404	16%
Sole parent	37,811	6%
With earnings from employment ⁴	103,000	19%
Total		
All	617,185	100%

Source: DEEWR 2010, Response to Senate Education Employment and Workplace Relations Committee Question on Notice EW0534_11.

Notes:

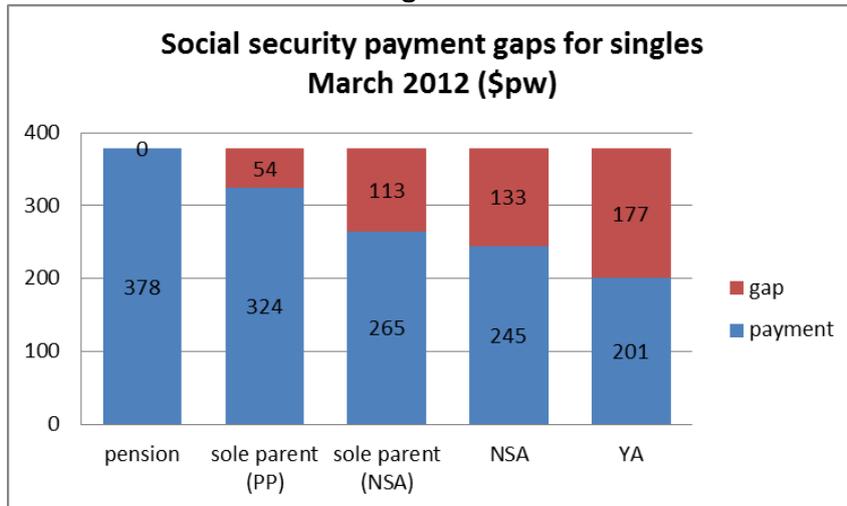
1. People with a partial work capacity (formally assessed as 'able to work' less than 30 hours a week)
2. Currently, 62% of recipients have durations over 1 year

1.2 Current rates of payment

In March 2012, the maximum single rate for NSA was \$245 per week or \$35 a day. This is \$133 per week less than pension payments such as age and disability pensions. Further, student payments such as YAS for single people living independently of their parents are currently \$210, which is \$44 per week less than NSA (this includes Austudy and Abstudy Payments, which are paid to fulltime students aged up to 64 years). The rate of NSA for sole parents is slightly higher than the standard single rate at \$265, but this is still \$59 less than the PPS which in turn is \$54 less than other pension payments (figure 3).

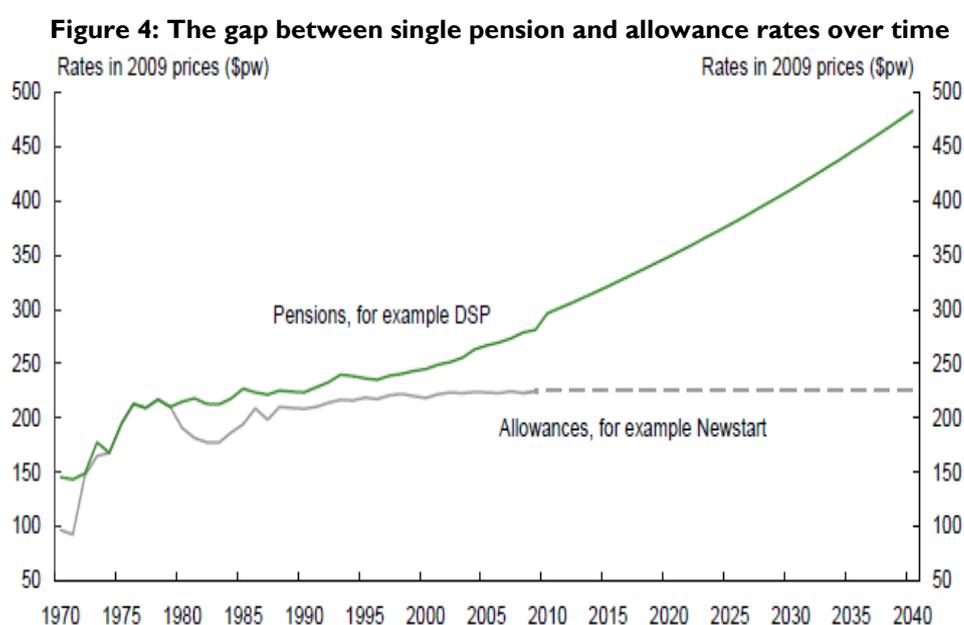
⁴ In December 2010, from DEEWR 2011, Response to Senate Estimates Question on Notice EW0930_11

Figure 3:



2 Policy history

Aside from a commitment by the Hawke Government in 1983 to raise the then Unemployment Benefits to the pension level (which was not fully implemented by the end of that Government's term), the level of Allowance payments has been arbitrarily determined. The growing gap between pension and allowance payments is an artefact of their different indexation arrangements: allowances to the Consumer Price Index (CPI) only and pensions to both average wage movements and measures of inflation. Even before pension payments were raised by \$32 per week above normal indexation in 2009, the Henry Report estimated that by 2040 the single Newstart rate would be just half that of the pension (figure 4).



Source: Australia's Future Tax System (2010), *Report to the Treasurer*.

The single pension rate has been informally benchmarked at 25% of Male Total Average Weekly Earnings since 1983 and this link was legislated in 1998. The link to average wages is responsible for most of the increase in pensions since then as wages have risen more quickly than prices. The 25% benchmark was arbitrary. It was not based on a detailed assessment of the needs or living standards of pensioners. Nevertheless, it was historically close to poverty lines typically used in Australia including the Henderson Poverty Line and the 50% of median income poverty line (discussed later).

The adequacy of Allowance payments has not been reviewed since the mid 1990s, and even then only as part of wider studies examining the adequacy of social security payments. In 1994 the then Department of Social Security, assisted by an expert advisory group on which ACOSS was represented, assessed different approaches to benchmark the adequacy of social security payments. The then Government subsequently commissioned two research projects: a 'Budget Standards' study undertaken by the Social Policy Research Centre which was published in 1998, and a study of 'relative deprivation' among people on different payments prepared by the

National Institute of Labour Studies⁵. The results of the former study are discussed later in this submission.

That year (1994) was also the last in which Allowance payments for single people were increased in real terms (by \$3 a week), aside from GST compensation in 2000 and the forthcoming Allowance Supplement. This means that the living standards of single people on Allowance payments (including single parents) have been effectively frozen for almost 20 years, to a time when the internet was in its infancy.

From 1994 to 2011, the incomes of people reliant on single-rate Allowance payments rose at only half the rate of the population generally: household disposable income per capita rose by 130% while the single rate of allowances rose by 65%⁶. As discussed below, the purchasing power of allowances actually declined over that period as the cost of living of recipients rose more quickly than the Consumer Price Index.

Partnered allowees have fared somewhat better as their payment levels were linked to the partnered pension rate until 1998. This is one of the reasons we advocate giving priority to a one-off increase in allowances for single people.

Rates of 'youth' payments for independent young people have not increased in real terms since 1987, and this is part of the reason that those payments are much lower than Newstart Allowance today. Student payments for adults over 24 years (Austudy and Abstudy Payments) have been tied to youth payments, notwithstanding the fact that they extend to fulltime students up to 64 years of age. For the most part, subsequent policy changes in this area have focussed more on easing income tests (both parental and personal) than on the adequacy of maximum rates of payment. This is in response to two factors: pressure from middle and high income parents to extend entitlements for post-secondary students more widely, and a growing trend among post-secondary students to combine full time study and part time employment, often at the expense of their studies. The adequacy of youth and student payments for those who are unable to secure employment has not been properly assessed. The recent Bradley Review of the tertiary education system did not make precise recommendations to increase student payments although it found they were inadequate. That Review mistakenly assumed that the Harmer Review was dealing with the adequacy of student allowances.

The 2008 pension review (Harmer Review) provided an opportunity to rectify these inequities and properly benchmark all income support payments to a minimum standard of living. Unfortunately the opportunity was missed as allowance payments and the Parenting Payment for sole parents were excluded from its terms of reference. The Review examined the adequacy of pension payments only, though it had access to substantial research on the relative living standards on allowance

⁵ DSS 1995, Developing a framework for benchmarks of adequacy for social security payments, Policy Discussion Paper 6; DSS 1998, Indicative Budget Standards for Australia, Research Discussion Paper; Travers & Roberston (1996), Relative deprivation among DSS clients, National Institute of Labour Studies Monograph Series No 2.

⁶ Melbourne Institute 2012, Poverty Lines.

payments as well⁷. It assessed the relative living standards of different groups of pensioners and concluded that the pensioners in greatest hardship were private tenants. It also found that single pensioners were significantly worse off, on average, than couples. It recommended a substantial increase in single pension rates to enable them to attain a similar living standard to partnered pensioners. The Review also recommended the modernisation of indexation arrangements, suggesting that median fulltime wages would be a more appropriate benchmark against which to index pensions than male total average weekly earnings. It argued that pension increases should be paid for partly by tightening the pension income test to better target people on lower incomes.

In 2009, the Government legislated a \$32 per week real increase (now significantly greater due to indexation) for single pensioners to 66.3% of the combined married pension rate, or 25.7% of male total average weekly earnings. The Government went beyond the Review's recommendations and also increased the partnered pension rate. ACOSS welcomed the increase for single pensioners, which was the largest pension rise since at least the Whitlam Government in the 1970s. However we criticised the lack of any increase for people on allowance payments and sole parents on the PPS payment (which up until then had been aligned with other pension rates).

The pension rise was paid for in part by tightening the pension income test – the 'taper rate' was increased from 40% to 50% as recommended by the Harmer Report. Also in the 2009 Budget, the long standing link between the maximum rate of Family Tax Benefit Part A and pension rates (and hence wages) - the centrepiece of the Hawke Government's efforts to reduce child poverty - was removed. Thus, sole parent families missed out on both a pension increase and automatic real increases in their future family payments.

Allowance recipients and sole parents on PPS were also excluded from the vast majority of the one-off stimulus payments awarded by the Government to stave off a recession in late 2008 and early 2009 (apart from Family Tax Benefit payments and a small training allowance). They also miss out on the \$10 a week Utility Allowance payment to help with the cost of power bills.

As a result of the above policy changes, and the different indexation arrangements for pensions and allowances, the gap between the single pension and Newstart Allowance payments rose from \$55 per week in September 2008 to \$133 per week in March 2012.

In 2008, the Henry Review of the tax-transfer system was given the task of recommending reforms to income support payments generally. By early 2009, there was already presumption that the Government was likely to award a substantial increase to pensioners.

⁷ This included a report commissioned from the Social Policy Research Centre that was subsequently released through the Senate Estimates process. See Saunders & Wong 2008, Deprivation and Other Indicators of the Living Standards of Older Australians.

While there are policy benefits in considering tax and transfers system reforms together, given its very broad scope the Henry Review lacked the time and resources to properly examine the adequacy of social security payments. For example, it argued that pensions should provide a 'basic acceptable standard of living' without examining in detail how this might be defined or benchmarked. It focussed instead on the same issue that led the Harmer Report to advocate an increase in pensions for singles: the relative living standards of singles and couples. It found that: 'Available evidence supports the same relativity [between singles and couples] for working age income support payment rates as applied to pension rates'⁸.

It also concluded that:

'Different indexation for pensions and allowances is creating an ever widening gap between pensions and allowances that can create inequities between assistance for individuals in similar circumstances as well as disincentives to work'⁹.

The Henry Report therefore recommended that the formula applied by the Harmer Report to pensions – a single rate equal to 66.3% of the combined partnered rate – should apply to Allowance payments¹⁰. Currently, that would require an increase of approximately \$50 per week in the single rate of the relevant Allowance payments. It also recommended that allowance payments be indexed in similar fashion to pensions to prevent the payment gap from growing further¹¹. That implies indexation of allowances to a measure of wages as well as the CPI, though the Report did not specify exactly how this should be done.

⁸ AFTS 2009, Report to the Treasurer, p512.

⁹ Ibid, p520.

¹⁰ Recommendation 83 at page 521.

¹¹ Recommendation 84 at page 522.

3 The adequacy of allowance payments

This part of the submission addresses the first term of reference of the Inquiry: *'(a) the adequacy of the allowance payment system for jobseekers and others, with particular reference to the adequacy of the Newstart Allowance payment as an income support payment for jobseekers and the adequacy of all other allowance payments that support a range of recipients who study or provide care'*

The main purpose of Australian income support payments is to prevent poverty. They are the main safety net for people unable to obtain a decent income through work or investment. Maximum rates of payment must be adequate for that purpose, so the first step in fixing rates of payment should be to determine the minimum adequate amount that is needed by people with no other means of support to achieve what the Henry Report refers to as a *'basic acceptable standard of living'*.

There are further steps beyond this. Policy should also take account of the impact of a given level of payment on incentives to seek fulltime employment and leave income support, where appropriate. Factors other than the maximum rate of payment impact on employment incentives, including activity requirements, the quality of employment assistance, direct costs of employment, such as travel to work, and income tests.

It is only by first assessing the minimum adequate level of payments that we can make well informed judgements about the balance between adequacy of income support for those with no other means of support and the need to maintain work incentives. Too often, the two issues are conflated, or the adequacy of payments is not properly assessed at all.

In order to assess the adequacy of income support, it is not sufficient to compare current and past rates of payment. Payments should be benchmarked against an adequate minimum standard of living. This is not straightforward as it requires the exercise of judgement as to how we define and measure a *'minimum living standard'*. Currently there is no widely accepted definition of a *'minimum adequate standard of living'* for Australia. It also requires robust empirical evidence of the living standards of people on social security payments, in comparison with other households.

One approach which sidesteps the definitional problem to some degree is to compare the living standards of people on different forms of income (income support payments or wages) to assess their *relative* adequacy. That was the approach taken when the Harmer Review compared the living standards of single and partnered pensioners. This approach still requires us to find a way to accurately measure and compare the living standards of different groups in the community.

In this part of the submission we compare the level of the single adult rate of allowance payments with two benchmarks of income adequacy used in poverty research (poverty lines and budget standards) and then compare the incomes and living standards of people on allowance payments with those of other groups

including other people with social security payments and wage earners. A particular focus is a comparison between the adequacy of the single rates of allowance payments and pensions, the adequacy of which was evaluated in the Harmer Review. To compare the living standards of people receiving allowance payments with other households we use a number of research tools including budget standards and deprivation studies.

We do not rely on any single measure, as each contributes to a valid assessment of the adequacy of allowances. In any event, the results from these measures tell a consistent story.

3.0 Poverty lines

Poverty lines are a simple and readily understood way to benchmark the living standards of groups in the community. The idea is that households living below a certain disposable income face a particularly high risk of economic hardship. Poverty measured in this way is not identical to economic hardship as a number of factors other than income mitigate against hardship, - including home ownership and other assets and family support. Poverty lines are set at levels which would be generally be regarded as just enough for people to meet the basic costs of living.

Since expectations about living standards vary between countries and within countries at different times, poverty lines are usually set by reference to incomes in the community generally. For example, the poverty line used by the OECD is set at 50% of the median (or middle) disposable income for the country concerned, while the European Union uses a higher 60% benchmark. While these are measures of 'extreme inequality' rather than absolute living standards, it is fallacious to argue that this method of measuring poverty guarantees that it can never be reduced. Poverty as measured in this way does vary substantially in response to such factors as changes in national employment levels and social security policies.

Once a poverty line is set for a single adult, higher poverty lines are set for larger families, based on 'equivalence scales'.

Table 3 shows the proportion of individuals living in various households below the 50% and 60% of median income poverty lines in Australia in 2006. The relevant poverty lines (in 2006 dollars) for single adults living alone were \$281 per week (for 50% of median income) and \$337 per week (for 60% of median income).

Table 3: Poverty rates for individuals in Australian households (2006)

	50% poverty line	60% poverty line
Unemployed	45%	65%
Sole parents	16%	33%
Single >64 years	47%	66%
Couple >64 years	18%	44%
Main income social security	41%	70%
All	11%	19%

Source: Saunders, et al 2008, Poverty in Australia: Sensitivity Analysis and Recent Trends, Report for ACOSS.

The maximum rates of allowance and pension payments for single people were well below these poverty lines at that time, which explains the high incidence of poverty among people whose main income was social security. The other categories, including 'unemployed' and 'sole parent', include people who did not receive income support. Nevertheless, poverty as measured in this way was very high among unemployed people generally and single people over 65 years.

Given income growth in the community since 2006 and the lack of any increase in allowance payments since then, poverty among their recipients is likely to be much higher today. On the other hand, the large real increase in single pension rates in 2009 is very likely to have substantially reduced poverty among people over 65 years of age.

A more direct way to use poverty lines to assess the adequacy of payments is to compare different rates of payment with the relevant poverty line. The following table compares maximum pension and allowance payments for single adults with the two poverty lines used above between 1996 and 2009.

Table 4: Single rate of Newstart Allowance as a % of two poverty lines

Poverty line:	1996	2003	2009
NSA			
50% of median income	92%	78%	72%
60% of median income	77%	65%	60%
Pension			
50% of median income	99%	91%	105%
60% of median income	82%	76%	90%

Sources: Whiteford 2012, Falling behind, the unemployed in Australia, at www.theconversation.edu.au; Saunders et al, 2007, Poverty in Australia: Sensitivity Analysis and Recent Trends, Report for ACOSS

This clearly shows the effect of the effect of the \$32 per week real increase in single pension payments in 2009. From 2003 to 2009 the single pension rate moved from 91% to 105% of the lower of the two poverty lines, which would have substantially reduced poverty (measured in this way) among retired households.

In contrast, from 1996 to 2009 the single rate of NSA fell from 92% of the lowest poverty line to just 72%. In 2009 the gap between the NSA rate and the 50% of median income poverty line was \$106 per week, and this is likely to be somewhat higher today.

'I've done the whole 'I'm not eating very much or eating a pack of noodles a day, because I don't have any food' kind of thing. It's not very nice, but I'm still pretty good with that, because I know a lot about nutrition and stuff and I go to the markets and get food out of bins if I need to...and go to places and agencies where people provide food for free on certain days. I reckon it's pretty disgusting. Basic things like food and shelter and stuff that people should be provided with.' (Taylah, Newstart Allowance)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, Allen & Unwin.

3.1 Budget standards

A set of 'Budget Standards' were developed for Australia by the Social Policy Research Centre in 1996, in work commissioned by the then Department of Social Security. The method used was to estimate budgets to meet the basic costs of living for different kinds of households, with input from experts such as dieticians.

The 'low cost' budgets were limited to basic essentials, and were intended to be used to benchmark the adequacy of social security payments. Although the output of budget standard research was a measure of expenditure rather than income, the budgets can reliably be compared with the maximum rates of income support payments provided the latter do not attract income tax, a condition that is met in Australia. Since they were compiled 17 years ago, the basket of goods and services used for the budgets and also their prices have fallen out of date. As recommended by the original researchers, we have updated the budgets by indexing them to the CPI. However this approach does not capture changes in the 'basket' of essential goods and services as community living standards rise. This suggests that the budgets presented below are a conservative measure of today's minimum living costs.

The table below shows the lowest of the budget standards (those for mature age home owners) which take no account of additional costs such as rent, the costs of disability or the costs of seeking employment. Although these additional expenses are often faced by people on working-age social security payments, this is an appropriate starting point for benchmarking the base rates of *core income support payments*, since these additional expenses can be compensated by supplementary payments such as rent assistance. However, it is worth noting that there are major gaps in the current system of income supplements, such as the costs of disability and costs of job search.

**Table 5: Income support payments and 'Low Cost' Budget Standards for mature age home-owners
(December 2011 in \$pw)**

	Low Cost Budget (mature age home owner)	Pension rates	Gap (Low Cost Budget minus payments)	Newstart Allowance rates	Gap (Low Cost Budget minus payments)
Single, no children	\$322	\$374	-\$52*	\$243	\$79
Couple, no children	\$440	\$610	-\$170*	\$439	\$1

Sources: Saunders 2004, Updating and extending indicative budget standards for older Australians, SPRC. Note: Budget standards indexed to December 2011 using the CPI.

* In these cases, the sign is negative because the payments are higher than the relevant Budget Standard.¹²

The table shows that by 2011, pension rates were significantly above the budget standard for mature age home owners, though to reiterate these budget standards should be regarded as conservative. Prior to the increase in single pension payments in 2009, the single pension rate was significantly below the relevant budget standard.

On the other hand, in 2011 NSA for single adults was \$79 per week below the relevant budget standard. NSA for couples was very close to the relevant budget standard.

Because different budget standards were developed by the researchers for households of different ages and family complements, they can also be used to estimate the *relative* minimum living costs facing different groups on social security payments. Table 6 shows estimates of the relative minimum costs of living for households of different ages and family types, derived from the budget standards. The minimum living cost of a single mature age home-owner is used here as the benchmark.

Table 6: Relative minimum costs for different households

	Single	Couple (combined)
Mature age home-owners	100%	137%
Working age private tenants	137%	177%

ACOSS estimates derived from Saunders et al 1996, Indicative budget standards for Australia, DSS Policy research paper No74, p442.

¹² These Budget Standards are for mature age home-owners, so do not include rent or the costs of working or job search. They have been updated to Dec 2009 using the CPI. Payment rates include the pension supplement (which is paid to all recipients of qualifying pensions) but not those supplements that are restricted to people with particular costs (such as Rent Assistance).

Compared to the low cost budget estimated for a mature age single adult homeowner, the budget for a single adult of working age was 37% higher, due in part to higher housing costs (the research assumed that typical low income earners of working age rented while typical age pensioners owned their homes outright), as well as the costs of employment or job search and minor factors including a slightly higher food budget. The effect of these factors was offset to some degree by the higher estimated health costs of older households. Interestingly, the research suggests that single person households need much more than 66% of the income of an equivalent couple (the benchmark now used in the pension system) to attain the same living standard.

Unfortunately, it is difficult to disentangle the effect of extra housing costs (the cost of renting rather than owning accommodation) from the other factors affecting the relative living costs of mature age and working age households.

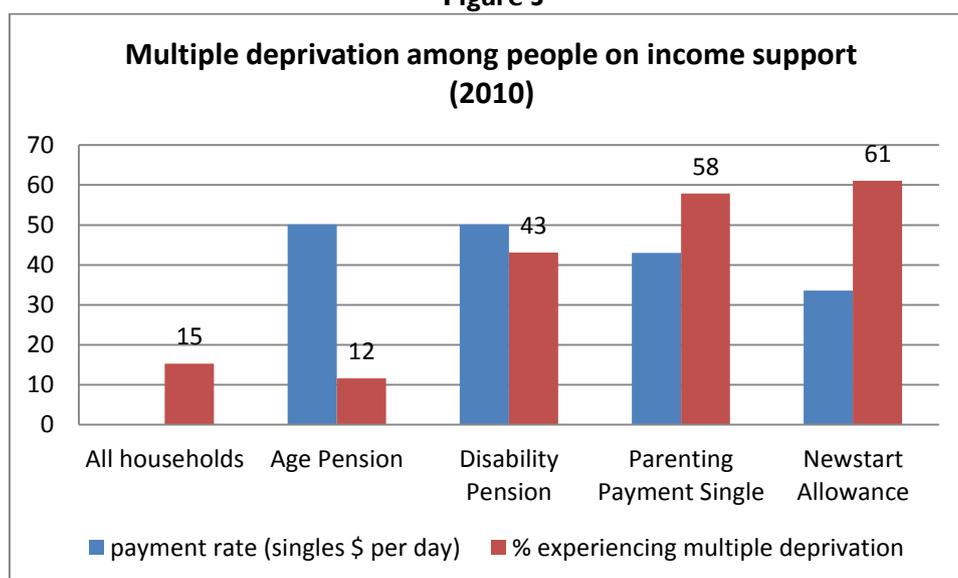
3.2 Deprivation

'Material deprivation' is a direct measure of hardship. That is, instead of measuring hardship using income as a proxy for living standards it attempts to measure them directly. By 'material deprivation', we mean that households lack what are generally accepted as the 'essentials of life' - such as a 'decent and secure home' - and that this is due to a lack of resources such as income and savings.

The following data comes from the PEMA survey conducted by the Social Policy Research centre in 2010. The survey asked a random sample of Australian adults whether they regarded a list of items as 'essential', whether they had those items, and if not, whether this was because they could not afford them. Only those items which at least 50% of respondents regarded as essential were included. From this, the researchers derived a list of 24 essentials (see Attachment). A household was described as experiencing 'multiple deprivation' if they lacked 3 or more of these 24 items because they could not afford them. Respondents were also asked whether they identified their own household as 'poor'.

Figure 3 shows the rates of 'multiple deprivation' so defined (right hand columns) across the community as a whole, and for households whose main source of income was certain social security payments. This is compared with the rates of the various payments (left hand columns).

Figure 3



Source: ACOSS 2012, Who is missing out? ACOSS Paper 187, derived from Saunders & Wong (forthcoming), Promoting inclusion and combating deprivation, Social Policy Research Centre.

In contrast to the poverty data presented earlier, the incidence of multiple deprivation was much higher among people of working age receiving income support than age pensioners. Rates of multiple deprivation among households whose main source of income was NSA (61%), PPS (58%), and DSP (43%) were two to four times higher the average for all Australian households (15%) and those reliant on the Age Pension (12%). There was an inverse relationship between the level of maximum payments and the incidence of deprivation (deprivation was more likely among those on lower payments).

As noted in the above discussion on budget standards, one likely explanation for the higher deprivation rates among people on working age payments is their higher housing costs (which are not captured in the abovementioned poverty data). By way of illustration, rates of multiple deprivation among private tenants generally (36%) were more than double those for all households (15%). Similarly, private tenants on the AP had almost twice the levels of multiple deprivation (20%) of AP households generally (12%).

Other factors likely to contribute to high deprivation rates among people of working age on social security payments include the costs of disability, job search and employment, and the fact that they are less likely than age pensioners to have financial assets which they can draw down for essential expenses.

As shown in figure 3, the lower rates of income support payments for people of working age (aside from people receiving the DSP and CP payments) are another likely contributing factor.

It is interesting to compare the incidence of deprivation of particular essentials from the PEMA survey (see Attachment for more detail):

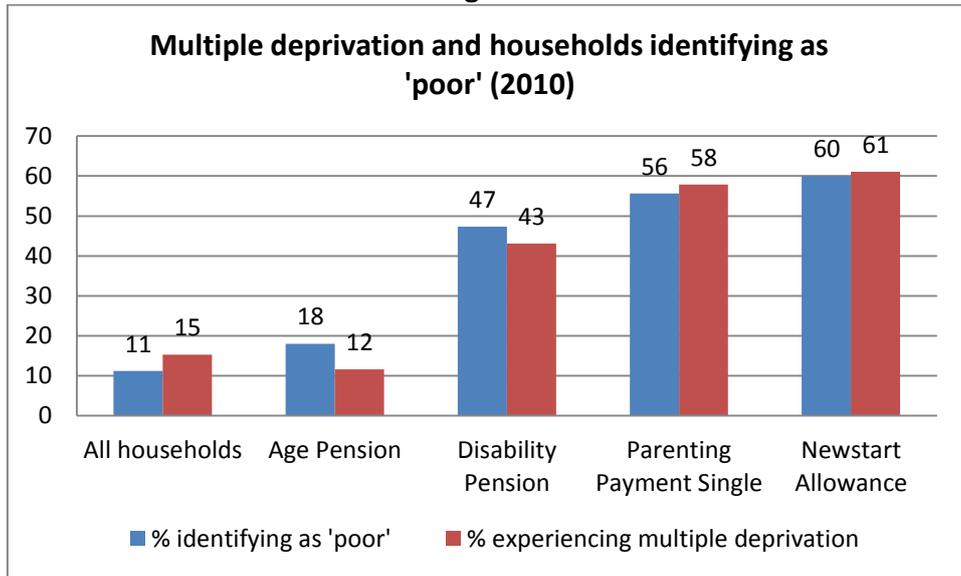
- Among people whose main source of income was NSA, PP or DSP, at least one third lacked \$500 in emergency savings (compared with 21% of all households) and over 40% could not obtain dental treatment when needed (compared with 17% of all households).
- Around one fifth or more of children living in households relying mainly on PP or NSA lacked up to date schoolbooks and uniforms, and over one quarter lacked a hobby or leisure activity, compared with 3% and 5% of families with children generally.
- 40% of people on the NSA payment were unable to afford to pay a utility bill on time during the last year;
- Over a quarter of people living on the DSP and PP were unable to afford gifts for family and friends at least once a year, compared with 5% of all households.

'I feel terrible saying I can't buy you a new pair of shoes this week, you're going to have to wait two weeks. How can you say that to someone when their toes are getting curled over at the end? There's been times where I haven't been able to afford to buy him things and my youngest as well and it's awful. I feel like a terrible person. How can I have brought kids into this world when I can't even afford to look after them the way they should? Just the basic minimum things that they should have.' (Caroline Parenting Payment Single)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, Allen & Unwin.

People's own perceptions of whether their household was 'poor' were also recorded in the PEMA research. As the graph below shows, those perceptions were remarkably accurate when 'poverty' is measured using multiple deprivation. There was less than 10% variation between the proportions of people receiving NSA (60%), PP (56%) and DSP (47%) describing themselves as 'poor' and the proportions of those groups experiencing multiple deprivation (figure 4).

Figure 4



Source: ACOSS 2012, ibid.

3.3 Financial stress

The Australian Bureau of Statistics (ABS) has developed a set of financial stress indicators which it used in its 2009 Household Expenditure Survey. Financial stress is not the same as deprivation, as people can experience stress because of their spending preferences (such as buying a home in a desirable suburb) as well as inadequate resources. Nevertheless, the results - especially the relative incidence of financial stress among people receiving different payments - are very consistent with the deprivation research discussed above (figures 3 and 4).

Table 7: Financial Stress Indicators, main source of income social security, 2009-10

	Payment type					
	Age pension	DSP & Carer	NSA, Youth & study	Parenting Payment	Other	Total
Number of indicators of financial stress experienced by households in the last 12 months						
None	53.6	23.7	9.2*	8.8	39.3	31.5
One	16.2	11.7	6.5*	6.7	18.4	12.2
Two	8.8	7.6	5.5*	7.4	9.6*	8.0
Three or more	21.4	57.0	78.7	77.0	32.7	48.3
Proportion of persons in household that experienced indicator in the last 12 months						
Unable to raise \$2000 in a week for something important	13.7	45.0	56.8	57.0	19.8	34.5
Spent more money than received	10.3	20.3	36.7	31.2	19.5	21.6
Could not pay electricity, gas or telephone bills on time	5.5	24.9	40.0	43.4	12.9	23.6
Could not pay car registration or insurance on time	2.1*	7.8	15.0	15.8	6.8*	8.6
Pawned or sold something	0.6*	7.4	12.3*	13.9	1.5*	6.8
Went without meals	0.9*	7.4	13.0*	12.4	2.1*	7.4
Unable to heat home	1.8*	8.4	10.0*	8.8	6.3**	5.6
Sought assistance from welfare/community organisations	0.4*	9.0	14.1	16.9	4.0*	8.8
Sought financial help from friends or family	2.9*	16.9	27.0	30.0	7.9*	15.6
Could not afford holiday for at least one week a year	28.0	56.2	75.3	74.2	39.4	49.8
Could not afford a night out once a fortnight	25.3	48.0	63.2	58.3	32.5	40.8
Could not afford friends/family over for a meal once a month	9.7	19.8	34.7	28.2	9.5	19.3
Could not afford a special meal once a week	17.1	33.0	41.6	43.7	21.4	29.6
Could only afford second hand clothes most of the time	11.2	33.0	46.1	45.7	15.2	27.8
Could not afford leisure or hobby activities	12.9	37.0	51.7	48.1	18.3	29.3
* estimate has a relative standard error of 25% to 50% and should be used with caution						
** estimate has a relative standard error greater than 50% and is considered too unreliable for general use						

SOURCE: ABS 2011: Household Expenditure Survey, Australia: Feature Article: Government Pension and Allowance Recipients. Cat no: 6530.0. Available:

<http://www.abs.gov.au/AUSSTATS/abs@.nsf/Latestproducts/6530.0Feature%20Article%202009-10?opendocument&tabname=Summary&prodno=6530.0&issue=2009-10&num=&view=>

The ABS found that 48% of households dependent upon government pensions and allowances as their main source of income had experienced three or more indicators of financial stress within the past 12 months, compared with 24% of all households.

Among people receiving income support payments, 79% of people on NSA and 77% of those on PP experienced three or more indicators of financial stress, compared with 57% of people receiving DSP or CP and 21% of those on age pensions.

'Well from a carer's position, the money that you earn covers roughly your food and enough (for) paying the bills to a degree. What you miss out on is sometimes socially going out, not being able to go out, not being able to take your person out. I try and take her out once a week...sometimes I can't do that for up to a couple of weeks if I don't have enough money. I can't go out so I can't network and have a life instead of just being isolated all the time. Sometimes we go without certain things. I haven't bought clothes in nearly 3-4 years. Just things like that, you make do with what you've got.' (Gregory, Carer Payment)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, Allen & Unwin. (name changed to protect privacy)

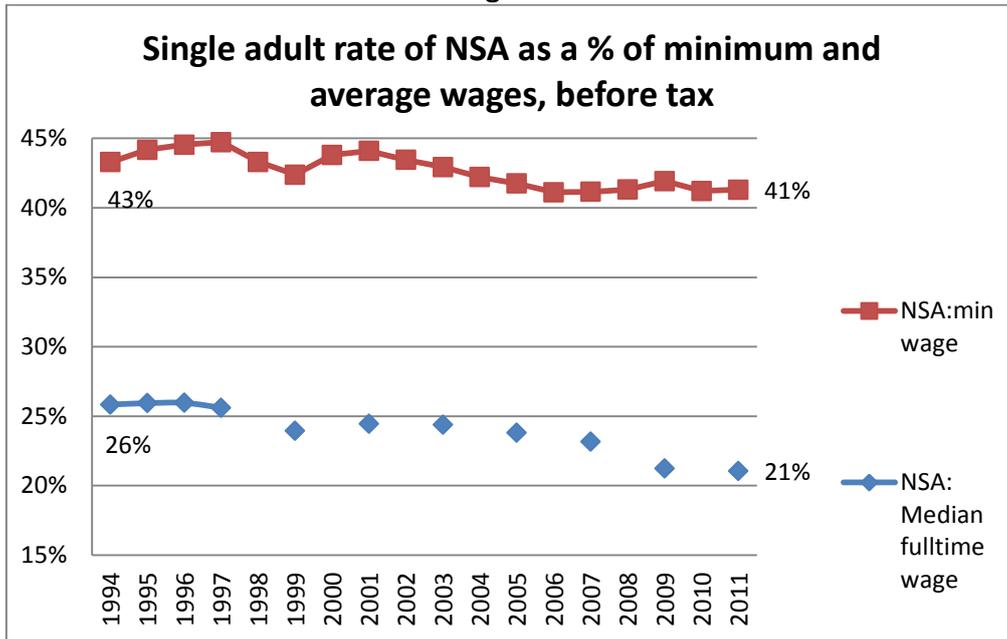
3.4 Allowance payments compared to wages

Most households of working age rely on wages as their main income, so movements in average or typical wages are often used as a measure of improvements in community living standards and as a benchmark of income adequacy. For example, the single rate of pension is indexed to 27.6% of male total average weekly earnings (MTAWE).

Figure 5 below compares the single rate of NSA with minimum and median fulltime wage rates, before tax. The comparison with minimum wages is also relevant to work incentives (discussed later). We also compare NSA with median fulltime wages because this is a better indicator of 'typical' wages than average earnings, a measure that is especially sensitive to movements in wages at the top end of the distribution¹³. The Harmer Review suggested indexing pensions to median fulltime earnings partly for this reason.

¹³ The median individual is simply the person in the middle of the distribution, while the average is the sum of all wages divided by the number of wage earners. A measure of fulltime earnings is not biased by changes in the proportion of wage-earners employed part time.

Figure 5



Sources: Fair Work Australia, ABS Employee Earnings and Hours series.

Since allowance payments are indexed only to the CPI, and wages have risen more than inflation over at least the last 20 years, their value has fallen behind that of most other household incomes in the community. From the time of the last increase in NSA in 1994 up to 2011, the single rate of NSA has fallen from 43% to 41% of the fulltime minimum wage, before tax. Over the same period, it fell from 26% to 21% of the fulltime median wage.

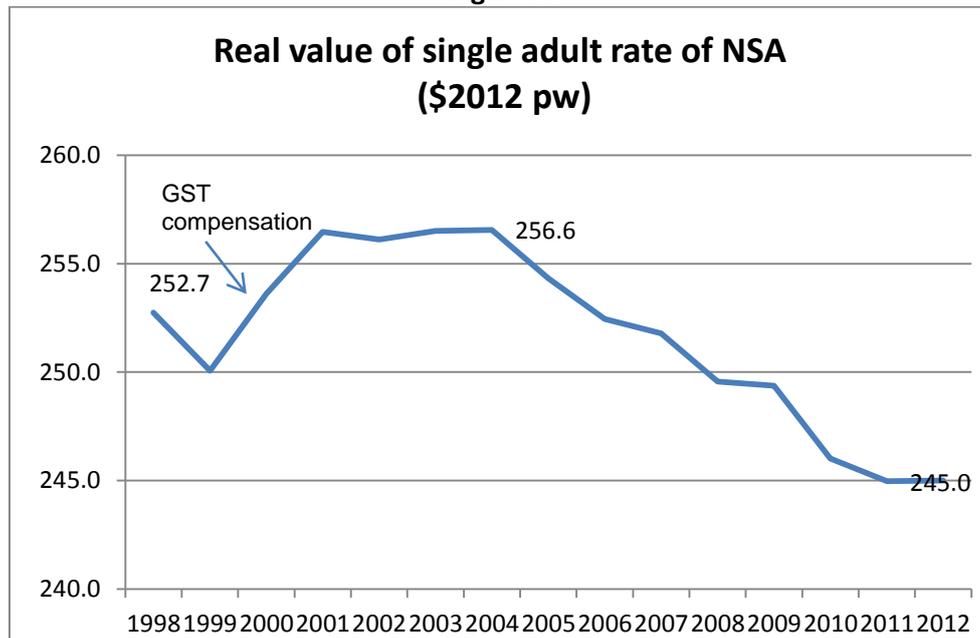
If the single NSA rate had been consistently indexed over that period to movements in median fulltime earnings, it would now be approximately \$45 per week higher.

3.5 Single Allowance rates and inflation

Although allowance payments are indexed to the Consumer Price Index (CPI) this is not an accurate measure of changes in the cost of living, nor is it intended to be. The ABS has developed separate measures for this purpose, the Analytical Living Cost Indexes or ALCI. There is a separate ALCI for people receiving social security payments other than pensions.

Figure 6 adjusts trends in the single rate of NSA to movements in the ALCI (rather than the CPI) since 1998, the year in which that index was developed.

Figure 6:



Source: ABS Analytical Living Cost Index for 'other Government benefit recipients'

This shows that the purchasing power of the single rate of NSA has fallen by \$8 per week since 1998. Although this is not as important a cause of the declining relative value of allowance payments as their lack of indexation to wages, it means that the living standards of people receiving NSA payments are likely to be lower now than those of their counterparts 15 years ago.

Pension payments are indexed to the relevant ALCI as well as the CPI and wage movements, but allowance payments are only indexed to the CPI.

3.6 The assets of pensioners and allowees

Income is not the only factor that determines a household's spending power. Investment in financial assets enables people to smooth their consumption over time by saving or drawing on their savings.

The table below compares the assets available to different social security payments, derived from social security data and other sources.

Table 8: Home ownership and other assets of people receiving social security payments (2011)

	Home owners	Private tenants/ boarders	Other housing status (incl. social housing)	With assets above \$182,000 (single) or \$258,000 (couple)	With liquid assets above \$2,500 for singles; \$5,000 for couples ²
NSA	18%	52%	31%	0%	\$2,500 for singles; \$5,000 for couples
YA	3%	32%	65%	0%	\$2,500 for singles; \$5,000 for couples
PPS	26%	51%	23%		N.A.
DSP	37%	33%	30%	1%	N.A.
AP	61%	11%	28%	12%	N.A.

Sources: FAHCSIA (2011), Income support customers.

Seelig et al 2008, Housing consumption patterns & earnings behaviour of people receiving income support recipients over time, AHURI Final Report No 119.

Australian Bureau of Statistics (2012), Australian Demographic Statistics, Dec 2011. Cat no: 3101.0

¹ Pension assets test reduces the pension for home-owners above these levels, which do not include the home. People on Allowances owning their home cannot have any assets (apart from the home) above these levels.

² Applicants for allowance payments must serve waiting periods if they have liquid assets (eg bank savings) above these levels.

Table is incomplete due to lack of publicly available data.

Pensioners must have assets (other than the primary home) valued at less than the levels shown in the table to secure the maximum pension entitlements. Those receiving Allowance payments cannot hold any assets above those levels. In addition, they must 'pass' a liquid assets test which measures assets held in financial institution accounts. The table shows that both the financial and liquid assets of people receiving NSA and YA are very limited.

In Australia the most important household asset is the family home. Home ownership, especially if unencumbered, shields households from financial hardship by substantially reducing housing costs which account for around one fifth of a typical low income household's budget. People can also use their homes as collateral to borrow at relatively low rates of interest. Although the impact of housing tenure is already captured in measures of living costs such as budget standards, a comparison of the incidence of home ownership is a good indicator of the ability of households with similar incomes to achieve a minimum adequate standard of living. In the deprivation survey cited previously, the multiple deprivation rate for private tenants generally was 36% compared to just 15% for the population as a whole.

Rates of home ownership are low among people receiving working age income support payments. Compared with 61% of those on AP, only 18% of those receiving NSA, 26% of those on PPS, 37% of those on DSP, and 3% of people receiving YA own or are paying off their home. Half of all those on NSA and PPS are renting privately (52% and 51% respectively). They have faced rapidly increasing housing costs over the last 5 years.

People receiving income support payments who rent privately are entitled to Rent Assistance if their rents exceed certain levels. Currently, the maximum rate of Rent Assistance for a single adult on income support is \$60 per week rising to \$71 for a family with two children. This is a small proportion of typical private rents around Australia. In March 2012, the median rent for a two bedroom flat in Sydney was \$450 per week¹⁴. The equivalent rent in Melbourne was \$295¹⁵. Rent Assistance is indexed to the CPI not to housing rents which have risen much more rapidly in recent years.

'Pay rent, eat some food, not a whole lot more. It doesn't allow you to do a whole lot of things. I would have – after I pay rent, I think I have left maybe \$15 a day, something like that.' (Stuart Newstart Allowance)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, Allen & Unwin.

It is not surprising that most older people have greater access to home ownership and financial assets. They are at a stage of life where they have had more time than people of working-age receiving social security to accumulate these assets. At the same time, around a quarter of age pensioners lack the financial protection afforded by home ownership. As noted by the Harmer Report, this is a key marker of financial disadvantage among age pensioners. The living standards of pensioners who rent are comparable to those of the majority of people on working-age payments.

The Australian social security system is almost unique in targeting income support on the basis of a family's current income rather than previous wages, as in overseas social insurance schemes. The allowance income tests are designed to limit those payments to individuals and families with very limited means. The personal income test restricts access to NSA to single people earning less than \$455 per week and couples earning less than \$830. In any event, only one in five of people receiving NSA has any significant earnings from employment.

It is clear that people on allowance payments are drawn from the most financially disadvantaged groups in the community: those with limited access to jobs, secure housing, financial assets, and financial support from their partners. This reinforces evidence presented later in this submission (table 10) that the transition from a fulltime wage to income support is more financially stressful for unemployed people in Australia than in other OECD countries.

¹⁴ Department of Family and Community Services, Housing NSW, Rent and Sales Report Issue 99.

¹⁵ Department of Human Services Victoria, 2012: Rental Report March quarter 2012

3.7 Post-secondary student payments

This part of the submission discusses the adequacy of post-secondary student payments: Youth Allowance or Abstudy Payment for students 18 years and over, and Austudy and Abstudy Payment for students over 25 years.

There is a long-standing tension between two competing policy objectives of post-secondary student payments - to alleviate poverty among students and their families with limited means (the main goal of income support payments generally) and to supplement the incomes of a broader cohort of young students as a public investment in their education. We argue that priority should be given to the first of these goals.

The first objective is the traditional goal of income support payments. It requires the maximum level of student payments for young people to be adequate to meet basic minimum living costs. Consistent with the targeting of income support payments to prevent poverty, that objective is more likely to be met if personal and family income tests restrict the payment to low income households.

The second objective treats student payments more as investments in human capital, either by government alone or by government and students jointly (in the case of student loans schemes). The adequacy of the maximum rate of payment is less important from this perspective as it is assumed that students can access labour or capital markets to support themselves while they study. However, such as payment would not be tightly income tested, either on the student's personal income (since the payment supplements their earnings) or parental income (since the payment's main purpose is not to prevent poverty).

The result is a 'hybrid' payment with a lower maximum rate and more liberal income tests (see table below).

Table 9: a comparison of Newstart Allowance and Youth Allowance/Austudy Payment

	NSA	YA student /Austudy
Maximum rate (single no children, independent)	\$245	\$201
Income test (personal)	Free area: \$31pw Taper rate: 50%/60% Cut out point: \$494pw*	Free area: \$118pw Taper rate: 50%/60% Cut out point: \$460pw*
Income test (parental)	N/A	If under 22 years: Free area: \$46,400pa Taper rate: 20% Cut out point: \$98,600 [does not apply if student has worked 30 hours a week for 18 months; or

		more than 15 hours each week for at least two years if required to study away from home and parents earn less than \$150,000]
--	--	---

* Those on YA student payments can 'bank' up to \$6,000 of their free area annually to undertake casual employment; people receiving NSA can draw down a much less generous 'working credit' for the same purpose.

This helps explain why post-secondary student payments have been treated as a 'special case'. Those who adopt a 'human capital approach' to student payments accept that it may be paid at a level below minimum expenditure needs. They argue that while the current incomes of postsecondary students may be low they will be relatively well off over their lifetimes due to their higher qualifications. However, there is still a risk from a human capital point of view that students from low income backgrounds will be discouraged from completing their education (undermining the national skills agenda and increasing future income inequality) if student payments are inadequate and their parents are unable to financially support them.

The human capital approach is problematic for poverty alleviation as it assumes that students only need payments to supplement income from earnings, parental support or loans, rather than 'full' income support. Yet it is precisely the students from the most disadvantaged backgrounds who are least likely to have access to these alternative income sources.

The average incomes of young students are relatively low. In 2008, while the average total income from all sources for full-time workers under 25 years was \$822 a week, the average total income of full-time students was less than a third of this at \$269 weekly¹⁶.

The Bradley Report on higher education found that:

*'The survey of student finances shows clearly that students believe that the current level of support provided to eligible students is insufficient to live on. This is also supported in a number of submissions to this review.'*¹⁷

However, that review did not recommend specific increases in payment rates as it mistakenly believed that the Harmer review was examining 'income support benefits of all types'.

A further problem with high levels of reliance on casual earnings is that this interferes with study. According to a survey of Melbourne University students submitted to the Bradley Review, 38% of students believed that work adversely affected their study; 50% were worried about their finances, and 11% of students answered that food or necessities are unaffordable. Additionally, 37% answered that they were placing financial pressure on their families or their source of financial support by studying¹⁸.

¹⁶ NATSEM 2008

¹⁷ Australian Government 2008, Review of Australian Higher Education, Final Report

¹⁸ Bexley 2008, Student Finances at the University of Melbourne

There is a tension between the poverty alleviation objective and the present targeting regime for student payments. It is more costly to raise the maximum rates of payment to an adequate level if the payment applies to people with a wide range of personal incomes and family backgrounds. It is also likely that many post-secondary students *do* have access to the other sources of income identified above. The Bradley Report was concerned that in 2008, many students from high income families qualified for Youth Allowance due to liberal tests of 'independence' that applied at the time (meaning the parental income test did not apply). It reported that 35% of people receiving Youth Allowance living at home were in families with incomes above \$100,000. While the tests for independence have since been tightened, the parental income test has been eased so that the Youth Allowance for a student over 18 living away from home cuts out at a parental income of around \$100,000. Further, the age at which an automatic assumption of independence applies has been lowered from 25 to 22 years.

A further problem with the current payment gap between student allowances and other income support payments such as NSA is that it hinders transitions between unemployment and fulltime study, even if the study were approved by an employment service provider as a stepping stone towards secure employment. An unemployed person over 21 years of age who studies fulltime for more than 12 months or so to improve future job prospects faces a \$44 per week drop in income support. This runs counter to the public policy goal of giving everyone the opportunity for a second chance to achieve a minimum level of qualifications (Certificate III) so that they can compete in the labour market of the future.

Clearly limits should be placed on the extent that people can study fulltime while receiving income support but this is best achieved by circumscribing the types and durations of courses that people can undertake (as is the case already). The payment of a lower benefit to full time students is a very blunt policy instrument.

The Austudy and Abstudy Payments for adult fulltime students up to 64 years of age are still tied to Youth Allowance rates of payment. This is an anachronism. As a result, the number of people receiving Austudy Payment has declined substantially over the long term and take up is particularly low among students aged 30 years and over (Bradley 2009).

To circumvent this problem, long term unemployed people who study fulltime may be paid at the higher Newstart Allowance rate. This begs the question of why these two payments are not aligned for all fulltime adult students, as is the case for Youth Allowance students and unemployed young people under 22 years of age.

There is also a strong case on grounds of both poverty alleviation and equity of access to post-secondary education to raise the maximum rate of YA for all young people 18 years and over living away from home and independently of their parents to the same level as NSA. In 2008, around 50,000 people on YA fell into this category (Bradley 2009). This would probably require some tightening of income tests to ensure that the higher payment is well targeted.

If this were implemented now, another option for reform that could be considered at a later time is to introduce a smaller educational supplement that is less tightly targeted to students with low personal income and/or low-income family backgrounds. The supplement could fulfil the broader 'human capital investment' purpose of student payments, so that this could be clearly separated from the core poverty alleviation objective. For example student payments could be structured along similar lines to Family Tax Benefit Part A which combines a higher 'maximum' payment targeted to low income families and a lower 'minimum' payment that is designed to assist middle income families with the cost of raising children.

3.8 Conclusions on the adequacy of allowance payments

The above evidence indicates that:

- maximum single rates of allowance payments are inadequate to meet basic living costs and prevent poverty and material deprivation.
- The typical living standards of people receiving NSA or PP are well below those on AP while those of people receiving DSP and CP lie in between.

We have compared the living standards of single people on NSA and AP in order to complete the analysis commenced in the Harmer Review, which benchmarked single pension rates to those for married pensioners but was prevented from considering the relative adequacy of allowance payments. **This should not be interpreted to suggest that we believe that pension payments are anything but frugal.** ACOSS called for and welcomed the rise in single pensions in 2009.

Youth and student payments for single people living independently of their parents are \$44 per week lower than even the NSA payment. This applies equally to 18 year old and 64 year old fulltime students, and runs contrary to recent Government initiatives to guarantee low skilled workers access to training up to a minimum qualification level so that they can compete in the labour market of the future. The evidence suggests that many people on these payments live in poverty and that inadequate income and the need to supplement it with part time earnings undermine their studies. If these payments were raised to the same level as NSA, it would be desirable to target them more effectively to families on the lowest incomes.

In response to the Harmer Review, the single rate of pension was raised by \$32 per week in real terms in 2009. That decision was informed by expert advice and evidence. The increase was designed to enable typical single pensioners to achieve a similar living standard to typical pensioner couples. However, allowance payments were not increased and, unlike pensions they are not indexed to wages. As a result, the single allowance rate is \$133 per week less than the single pension and the ratio between the single and partnered allowance rates is 55.4% compared with the benchmark of 66.3% set by the Government for pensions. The Henry Report recommended that single allowance rates be raised to the same 66.3% benchmark as single pensions, which would require a one off increase of approximately \$50 per

week in the single allowance rate for unemployed people, adult students, and young people living independently of their parents.

The Henry Report also recommended a change to the indexation of allowance payments so that the gap between pension and allowance payments for people of working age does not widen further. It estimated that otherwise, by 2030 the single allowance rate would be worth just half the pension, an outcome that is neither fair nor sustainable. It recommended that allowance payments be indexed to a measure of wage movements. One option is to tie both allowance payments and pensions for people of working age to movements in fulltime median earnings, which as the Harmer Report noted is a more appropriate wages benchmark for this purpose than average male earnings.

However, we do not support the Harmer report's suggestion that payments be tied to movements in net earnings (after tax). That would reduce predictability and certainty for people receiving social security. It could also lead to perverse outcomes. For example, if income taxes on wages were sharply reduced, net earnings would increase, and so would social security payments. The Government would be faced with a higher social security bill at precisely the time when its revenues from income tax are reduced. Conversely, if income taxes were raised, social security payments would arbitrarily fall.

Indexing allowances to median fulltime earnings is unlikely to seriously erode work incentives for the foreseeable future. As discussed later, the single rate of NSA is currently less than half the fulltime minimum wage (after tax) and has declined relative to minimum wages over the last two decades or so. Although median earnings have risen more rapidly than minimum wages since the last NSA increase in 1994, if allowances had been indexed to median wages over the whole of that period, the single rate of NSA would be just under \$50 per week higher today – the increase recommended by the Henry Report.

Another indexing option that would maintain work incentives is to index allowances to the minimum wage. However, Fair Work Australia would then determine payment levels for a much larger number of people on social security than workers benefiting from minimum wage increases. This arrangement would also reduce financial certainty for people receiving social security, many of whom are either living in poverty or close to it.

3.9 Recommendations to improve the adequacy of allowance payments in the short term

- I. (a) Allowance payments for single people (other than those on student payments) should be increased by \$50 per week from March 2014, and benchmarked to 66.3% of the combined married couple rate of Allowances as is the case for pension payments (and a higher rate in the case of sole parents).

This applies to people receiving Newstart Allowance, Widow Allowance,

Sickness Allowance, Special Benefit, Crisis Payment, and those on Youth Allowance (Other) living independently of their parents and away from the parental home.

(b) Allowance payments for single people on student payments (Austudy Payment, Abstudy Payment and Youth Allowance Student) who are living independently of their parents and away from the parental home should also be increased by \$50 per week from March 2014 and the benchmarking of those payments to 66.3% of the married rate (higher for sole parents) should be phased in.

(Cost: approx. \$500 million in 2013-14 or \$1,500 million in a full year)

2. From 2014, all of the above Allowance payments (for singles and for couples) should be indexed at least annually to movements in a standard Australian Bureau of Statistics measure of typical fulltime wage levels (before tax), as well as six monthly to movements in the Consumer Price Index.

4 Work incentives

This part addresses the second term of reference, relating to work incentives, and partly addresses the third, relating to the responsiveness of the system to changes in labour market conditions:

'(b) the appropriateness of the allowance payment system as a support into work, with particular reference to:

(i) the effectiveness of the payment as an incentive into work
(c) the impact of the changing nature of the labour market, particularly the rise of insecure work and decline of unskilled jobs, on the:

(i) nature and frequency of individual interaction with the allowance payment system, and

(ii) over and underpayment of allowances to recipients.'

We focus here on the NSA payment.

Australian income support payments are financed from general government revenues and targeted to reduce poverty through family based income tests. Any such system of income support requires trade-offs within the so-called 'iron triangle' of adequacy, incentives and fiscal cost.

We first discuss the trade-off between income adequacy for people out of paid employment and incentives to move from income support into fulltime employment, and then turn to the trade off between targeting for poverty alleviation and incentives to seek full and part time employment.

4.0 Incentives to move into fulltime employment

Incentives to move from unemployment to a fulltime job are typically measured using 'benefit replacement rates', or the ratio between after-tax income on income support and after-tax income on wages in jobs for which unemployed people are competing.

Since NSA is low by international standards and Australian minimum wages are relatively high, financial incentives to seek fulltime employment are relatively strong, especially for single people. ***If a single adult on NSA obtains a fulltime job at the minimum wage, they would more than double their disposable income.*** Put another way, the benefit replacement rate to the fulltime minimum wage is just 45%. In 1994, it was 52%. If the single rate of NSA was the same proportion of after-tax minimum wages that applied 18 years ago, it would be about \$40 per week higher. If work incentives for a single person on NSA were considered adequate 18 years ago, then our proposed \$50 per week increase is unlikely to undermine them today.

Few fulltime employees are paid as little as the minimum wage. If we set aside jobs at below-award rates (for example, 'cash in hand' jobs) this means that the single rate

of NSA is likely to be less than 40% of the after-tax earnings an unemployed person would typically obtain in fulltime employment.

Figure 5 above showed that NSA has fallen relative to *before-tax* minimum wages over the last two decades. Over this period increases in the Low Income Tax Offset and the recent increase in the tax free threshold have also significantly reduced the overall rate of income tax paid by a minimum wage earner.

Financial incentives to seek fulltime low paid employment are not quite as strong for people on unemployment allowances with a partner out of paid work because the combined married rate of payment is greater than the single rate. However they were considerably strengthened for 'second earners' in low income families by a 1994 reform which separated the income tests applying to each partner in a couple, and remain strong by international standards. Apart from comparing international benefit replacement rates for couples as well as single unemployed people (table 10 below) we have not examined work incentives for couples in detail as we do not advocate an immediate increase in the partnered rate of allowance payments.

Low-income families with children are entitled to Family Tax Benefits (FTB) in addition to income support payments. Since the maximum rate of the Part A payment is paid to families with incomes of less than \$46,400 per year regardless of the employment status of the parents, family payments do not undermine incentives for at least one parent to undertake employment at the minimum wage (though the FTBA income test and the Part B payment reduce work incentives for second earners). An unemployed couple in which one partner obtains employment at the fulltime minimum wage retains the maximum rate of the FTBA payment. This means that comparisons of the disposable income of unemployed families and low paid working families should include family payments in both cases, a detail that is often neglected in debates on work incentives for unemployed families.

There is no evidence to suggest that a substantial number of unemployed people on NSA are discouraged from seeking a fulltime job by the level of the payment. On the contrary, qualitative research, including focus groups on work incentives commissioned by the former Fair Pay Commission, confirms that people receiving NSA believe they would be substantially better off financially in a fulltime paid job¹⁹.

Table 10 compares benefit replacement rates based on fulltime average production worker wages in the OECD countries in 2010. Unlike our previous comparisons between unemployment payments and wages, these data include housing benefits such as Australia's Rent Assistance. The equivalent benefit replacement rates for Australia *without* housing benefits, which are significantly lower, are listed at the foot of the table.

¹⁹ Colmar Brunton Research 2006, Work decisions and the tax-transfer system, Australian Fair Pay Commission.

Table 10: Social security and housing payments for people in their first year of unemployment as a % of a low fulltime wage (67% of average wage) in 2010

OECD Countries	Single person no children	Double income no children	Sole parent 2 children	Double income 2 children
Australia	40	53	60	69
New Zealand	50	55	69	64
Turkey**	53	80	52	80
United Kingdom	54	60	72	70
Austria	55	80	72	85
Estonia	55	77	63	79
Korea	55	78	57	78
Greece	58	80	71	87
United States	60	82	60	84
Germany	61	87	76	90
Slovak Republic	61	83	71	84
Canada	62	81	78	84
Finland	64	78	85	83
Norway	67	84	90	86
Japan	68	85	89	86
Sweden	68	84	81	85
France	69	84	78	84
Italy	71	85	76	88
Hungary	75	88	84	89
Poland	75	76	97	81
Portugal	75	91	79	91
Ireland	76	75	82	82
Netherlands	76	83	76	81
Slovenia	76	88	83	92
Czech Republic	77	87	82	92
Iceland	79	89	85	91
Spain	80	90	77	89
Luxembourg	82	89	89	93
Switzerland	83	89	85	90
Denmark	84	91	90	93
Israel*	84	92	76	95
Belgium	89	85	88	86

Source: OECD Benefits and wages data base

Any income taxes payable on unemployment benefits are determined in relation to annualised benefit values (i.e. monthly values multiplied by 12) even if the maximum benefit duration is shorter than 12 months. For married couples the percentage of AW relates to the previous earnings of the "unemployed" spouse only; the second spouse is assumed to have no earnings and no recent employment history. Where receipt of social assistance or other minimum-income benefits is subject to activity tests (such as active job-search or being "available" for

work), these requirements are assumed to be met. Children are aged four and six and neither childcare benefits nor childcare costs are considered.

Note: If housing benefits are excluded the benefit replacement rates for Australia were 32% for singles, 60% for couples, 45% for sole parents with 2 children, and 66% for couples with two children.

In 2010, Australia had the lowest benefit replacement rate in the OECD for single people recently unemployed, compared with a low fulltime wage (two thirds of the average wage).

Table 10 shows that relevant social security payments (including FTB) for unemployed households were worth between 40% and 70% of the after-tax value of a low fulltime wage, depending on family type. Note that at this earnings level, a family with children is likely to receive the maximum rate of FTB. This indicates that financial work incentives are very strong for unemployed people in Australia, relative to other countries.

There is no consistent relationship internationally between low benefit rates and low unemployment. For example, prior to the GFC in 2007 the unemployment rate in Denmark was around 2%. Yet its unemployment insurance benefits are set at 90% of the previous wage (up to a ceiling) and the social assistance benefits paid once unemployment insurance expires are set at 60-80% of the unemployment insurance benefit rate. This and other international evidence suggests that other factors mitigate against any unemployment-increasing effect of high benefit payments. In the case of the Danish 'employment miracle', those included robust activity requirements for people on benefit payments and substantial investment in work experience and training programs for long term unemployed people²⁰. The role of reasonable activity requirements and supportive employment services in improving employment outcomes has long been recognised internationally²¹.

Australia has a stringent system of activity requirements for unemployed workers including a default requirement to seek 10 jobs a fortnight and demonstrate this to Centrelink, a requirement to register with an employment service and attend regular interviews, to sign and adhere to an employment pathway plan, and to participate in training and other employment related activities.

If there is a weak link in the system it is public investment in employment services, which is among the lowest in the OECD. As discussed later, the resources and incentives for Job Services Australia (JSA) providers to invest in work experience training and other help for long term unemployed jobseekers are particularly weak.

Under these circumstances, the immediate increase we propose to maximum single rates of allowance payments should not significantly reduce incentives to seek fulltime employment. The proposed \$50 per week increase would increase the replacement rate to after-tax minimum wages from 43% to 52%. As discussed

²⁰ Andersen & Svarer, Flexicurity, labour market performance in Denmark, CESifo economic studies Vol53 3/2007, p389.

²¹ Atkinson A 1991, Unemployment compensation and labour market transitions, a critical review. Journal of Economic Literature Vol 9.

previously, it would approximately restore the relativity to the median fulltime wage to that which applied in the early 1990s. Single people on allowance payments currently have a very strong financial incentive to move into fulltime employment.

In any event, given the disadvantaged profile of most people receiving NSA, financial work incentives are not the main hurdle to reducing reliance on that payment. As discussed above and in other ACOSS publications, the main hurdles are limited employment capacity (due for example to disability, health problems and low skills) and limited employer demand for workers with characteristics shared by many people on NSA (such as mature age and long term unemployment)²². In this context, a \$50 increase in the payment is unlikely to significantly reduce employment outcomes.

On the other hand, given the very low level of allowance payments, an increase would improve employment outcomes for many people. The current payment level is inadequate to cover the direct costs of job search and training (including applying for up to 10 jobs a fortnight and travelling up to 90 minutes each way to do so). Further, people on NSA cannot afford the rents charged in areas with good employment opportunities such as capital cities. If they are forced to move to areas with lower housing costs, this is likely to reduce their employment prospects.

The Henry Report recommended the equivalent of a \$50 per week increase in the maximum single rate of allowance payments. The Panel included a business leader, a former senior Treasury official, an academic expert, and the then Secretaries to the Treasury and Families Housing Community Services and Indigenous Affairs Departments. It was advised by a Secretariat drawn from the Treasury, and Employment and Family and Community Services Departments. It is very unlikely that such a Report would advocate proposals that seriously erode work incentives among unemployed people. If any criticism can reasonably be levelled at the Henry Report's social security proposals, it is that they were too conservative in their approach to reforming the payment structure.

4.1 Incentives to undertake part time and casual employment

At around 30% of all jobs, Australia has the second highest rate of part time employment in the OECD (after Holland) and at around 25% of all jobs the second highest rate of casual employment (after Spain). Most part time jobs are also casual. Significantly for income support policy, most low skilled jobs are part time.

Therefore a major policy challenge for Australia is to facilitate transitions to part time and casual employment without trapping people in part time jobs, or on a carousel between income support and casual employment. On the other hand, for some groups (including parents with young children and some people with disability)

²² ACOSS 2011, Beyond stereotypes: Myths and facts about people of working age who receive social security

part time employment is more appropriate at this stage in their lives and policy must be responsive to their circumstances and needs.

Over the last 20 years, social security policy has responded to the changing labour market, particularly growth in *part time employment*, by easing income tests. In order to reduce high 'effective marginal tax rates' (which are mainly a by-product of social security income tests rather than the income tax system), the main 'taper rate' for NSA was progressively reduced from 100% in 1994 to 60% today, and it is now proposed to reduce it further to 40% for sole parents. Compared with the equivalent 'social assistance' payments in most overseas social security systems (where benefits are often withdrawn dollar for dollar when people have private income), these income tests are relatively liberal. This is appropriate in a country with such a high incidence of part time employment.

There is a trade-off between easing income tests to encourage part time employment (enabling people to combine part time earnings with 'part' income support payments), and encouraging transitions from part time to full time jobs.

Another constraint on the further easing of allowance income tests is budgetary cost. The cost effectiveness of income support in reducing poverty is improved if payments are targeted those most at risk of poverty. For this reason, up until now income support payments for adults of working age have generally been targeted towards families who are not engaged in fulltime employment. In Australia, fulltime minimum wages have been set on the assumption that it is the employer's responsibility to meet the basic living costs of (at least) the wage earner, and as a result they are high by international standards. If income support had always been paid to fulltime minimum wage earners generally, it is likely that minimum wages would now be lower. This would further increase the budgetary cost of reducing poverty among low income families. Conversely, countries that provide 'earned income tax credits' for low paid fulltime workers, such as the United States, do so partly to compensate for inadequate minimum wages.

On the other hand, a range of supplementary payments such as FTB do extend to minimum wage-earning families. This is justified on the grounds that wages cannot accurately take additional living costs such as the number of children in a family into account. These payments have a different role to adult income support payments such as NSA and they are not exclusively targeted to reduce poverty. For example, FTBA also acts as a defacto tax allowance to take account of the costs of children (which reduce an individual's capacity to pay income tax). As discussed in the next part of this submission, similar 'horizontal equity' arguments may apply to other supplementary payments.

To avoid extending income support payments to minimum wage earners generally, the income test for income support payments for people of working age would have to be designed so that the 'cut out point' (the private income level above which no

benefit is paid) is below \$606 per week, or at least not far above it²³. If the maximum rate of payment is increased, then the income test must be correspondingly ‘tighter’ to achieve this target. Table 11 illustrates this by comparing the current NSA payment and income test with a payment that is \$50 per week higher (as we propose), and the single pension payment.

Table 11: Single allowance and pension rates compared with the minimum wage (after tax – July 2012)

Reform options	Maximum rate (\$pw)	Maximum rate as a % of after-tax minimum wage	Income test	Income test ‘cut out point’ as a % of after-tax minimum wage
NSA status quo	\$245	43%	Free area: \$31pw 1st taper rate: 50% 2 nd threshold: \$125pw 2 nd taper rate: 60%	\$455 (80%)
NSA max rate increased by \$50pw	\$295	52%	As above	\$538 (95%)
NSA max rate increased, \$40pw free area, uniform 60% taper	\$295	52%	Free area: \$40pw Taper rate: 60%	\$538 (95%)
Pension rate & income test	\$379	67%	Free area: \$75pw Taper rate: 50%	\$831 (147%)

Source: ACOSS calculations

Note: Net minimum wage refers to minimum wage after tax (\$566 per week in July 2012)

The table shows that part of the single pension payment extends to fulltime minimum wage earners. This can be justified where the main goal is to encourage part time employment and the person is not expected to seek a fulltime job, as is the case for age and disability pensioners, and people with part time work requirements in the Allowance system (parents caring for school age children and people with so-called ‘partial work capacity’). It is unlikely have implications for minimum wage-setting since the majority of minimum wage earners do not fall within these categories.

The table shows that there is room within the above constraint to increase single allowance payments by \$50 per week as we propose. However this does not leave much room for substantial easing of allowance income tests across the board.

People on allowance payments often have problems managing their reporting obligations to Centrelink when they undertake employment. Together with the insecure nature of much of the work available to them, these factors are likely to be at least as important as high ‘effective marginal tax rates’ in discouraging part time

²³ If only a small ‘residual’ benefit was available to full time minimum wage earners, take up of the benefit is likely to be low in any event.

and casual employment²⁴. Only a minority of people understand how income tests work and many reportedly assume they are tougher than they actually are (a perception that discourages part time employment). The allowance income test is complex, with two separate thresholds (\$31 per week and \$125 per week) and taper rates (50% and 60%).

Many people on social security payments earn very small amounts of income from part-time jobs. To reduce the administrative burden of reporting these earnings and to boost compliance with income reporting requirements, income tests have a small 'free area' – income that is disregarded by Centrelink. Although the pension income test free area of \$75 per week (for singles) is indexed for inflation, the allowance 'free area' of \$31 per week is not indexed and has not increased for over 20 years.

One option to simplify the system and reduce the administrative burden of reporting small amounts of income, without increasing the overall 'cut out point' of the Allowance income test, is to raise the free area and at the same time remove the 50% taper rate that applies to earnings between \$31 and \$125 per week so that the taper rate is a uniform 60% (except for groups required to seek part time employment such as parents with school age children and people with partial work capacity).

Our social security policies have attempted to encourage *casual fulltime employment* by allowing people to remain on income support at a 'zero rate' for up to three months to avoid the need to reapply when the job ends, and by introducing various forms of 'income averaging' including the 'Working Credit' for recipients of NSA and the 'Income Bank' for student payments.

'So what I would like is for (Centrelink) (to) average out the hours over the year and do it like that, rather than over one fortnight. I think because people that are on DSP, often their ability to work fluctuates up and down and Centrelink can't take that into account. ...You might work a period of 40 hours in one week, and then actually nothing for four months, so instead of averaging that out, they'll look at the 40 hours and they'll say, oh you worked 40 hours here. Well not only are we taking your income, but we're going to suggest that you move off DSP, because obviously you can work those hours, and that's the problem with it' (Rhianna Disability Support Pension)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, Allen & Unwin. (name changed to protect privacy)

The main weakness of the Working Credit is that, unlike the Income Bank for students which allows people to 'bank' their income test free area over a period of time, it is very complex. For example, it is too complex to explain its workings in the 'Guide to Australian Government Payments' issued by Centrelink, which summarises the main social security entitlements. If people are unable to understand it, it is unlikely to improve incentives to undertake casual jobs. One option to improve its visibility and effectiveness is simply to allow people to 'bank' their income test free

²⁴ See Bodsworth 2010, Making work pay and making income support work, Brotherhood of St Laurence.

area for up to six months. This would allow them to earn roughly a fortnight's wages at the fulltime minimum wage every six months without any loss of benefits. This would still be much less generous than the Income Bank for student payments and it should not have substantial cost implications (especially if account taken of under-reporting of small amounts of earnings).

Much more could be done to make it easier for people on allowance payments to undertake casual employment without running into problems with Centrelink, and to reduce the high level of under and overpayments that are almost embedded in the design and administration of income tests. The British Government is introducing a scheme whereby earnings data for social security purposes are collected from employers through the tax system. They also have a 'better off in work calculator' that is used by personal advisers in the social security system to demonstrate to people in simple terms what will happen to their social security payments if they earn a certain level of wages. Of course, if income tests were simpler in the first place then these and other administrative reforms to make it easier for people to declare their earnings are more likely to bear fruit.

'I'd rather not have all this bureaucracy in my life. I don't think anyone who is not divorced and doesn't go on welfare, could understand the amount of paperwork. I mean I've got a filing system in there and you'd just love to burn it. It's just files full of stuff'. (Gayle, Parenting Payment Single)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, Allen & Unwin. (name changed to protect privacy)

Although beyond the scope of this submission, other work related costs outside the social security and tax system have a large impact on work incentives for unemployed people, including the withdrawal of social housing rental rebates at 25 cents in the dollar, the risk of losing a place on social housing waiting lists, child care costs, and the paucity of public transport in many regional and outer urban areas.

4.2 Recommendations to improve incentives to undertake part time and casual employment

3. From March 2014, the following changes should be made to the income test for the Newstart Allowance and Youth Allowance (Other) payments in order to encourage participation in casual employment, simplify the system for unemployed people, and reduce over and under-payments:

(1) The working credit should be replaced by a simpler system where people can 'bank' their fortnightly income test 'free area' for up to 26 weeks;

(2) The free area should be increased by \$9 per week to \$40 and the 50% and 60% taper rates replaced by a consistent 60% taper rate;

(3) the 'free area' should subsequently be indexed to the CPI.

5 Necessary improvements to employment services

Reform of the benefit system for unemployed people should be considered in the wider context of changes in the labour market and the employment services that are funded to assist them into employment. ACOSS has consistently argued for coordinated reform of payment and employment services since our goal is to assist as many people as possible into secure employment with adequate wages rather than leave them to rely on income support. Further, as indicated previously a well-designed system of activity requirements and employment supports can ease any impact that unemployment payments might otherwise have on employment incentives.

This does not mean that the form of employment assistance offered to each individual should be tied mechanically to their income support payment status. Employment assistance should meet people's individual needs.

More substantial reforms to employment service purchasing arrangements are detailed in another ACOSS paper, our 'Submission to APESAA' (ACOSS Paper 184). We focus here on immediate changes to improve the effectiveness of Job Services Australia (JSA) services for people disadvantaged in the labour market.

As argued previously, employment services today are working with a growing proportion of people receiving income support who are unemployed long-term, or are at risk of prolonged unemployment. This group, extending well beyond the target group for 'Stream 4' JSA services, are likely to need one or more of the following:

- intensive case management,
- vocational or basic skills training,
- work experience in regular employment,
- integrated service provision from a range of employment, health and social support services.

The challenge for JSA providers is to invest in the most effective assistance for each client without over-investing, and the challenge for Governments is to design an employment services system that gives providers the resources and incentives to do so.

When the JSA system was introduced it was intended to improve employment assistance in the following ways:

- more intensive assistance for people at risk of long term unemployment (especially Stream 4 jobseekers);

- more flexibility for providers to determine the timing and nature of periods of more intensive training, work experience or other activity. This was intended to support innovation and to keep jobseekers 'active' in the labour market a more productive way;
- attempts to simplify administration, for example of the Employment Pathway Fund;
- a more open and collaborative relationship between the Department and providers.

However, the JSA system has the following weaknesses in regard to services for people disadvantaged in the labour market:

- Since the overall level of resources in the employment services system was reduced (JSA cost less than the programs it replaced), higher levels of support for jobseekers in their first year of unemployment came at the expense of lower levels of support for people unemployed long term and those assigned to 'Stream 1';
- Employment Pathway Fund credits for long-term unemployed people in the Work Experience phase are generally much less than those available to assist people in Streams 3 and 4 who are unemployed short-term. Work experience and training are thus poorly resourced in the 'Work Experience' phase. Providers are funded to interview people every two months together with \$500 in the EPF. While an additional \$1,000 EPF credit will become available this year for providers to assist each people unemployed for 24 to 36 months, this EPF credit must fund up to 11 months of 'activity' in that year – an average of less than \$100 for each month of intensive activity;
- The introduction of four streams of assistance and the distinction between provider assisted and brokered outcomes increased the complexity of the system and its focus on identifying each jobseeker's 'barriers' as distinct from their employment potential²⁵.

The services provided on the ground for disadvantaged jobseekers are often inadequate to meet their needs. Under-investment in employment services for people unemployed long term is short sighted since well-designed and well-resourced programs can improve their employment prospects in the medium-term (for example, one year after assistance) by around 10 percentage points. If such outcomes are sustained, such investment would make a substantial difference to unemployment, poverty, and reliance on unemployment payments, and would probably pay for itself.

It is no simple matter to design an employment services purchasing system that targets assistance to where it is most needed and will do the most good, and gives providers the right mix of incentives and resources to invest efficiently in services for disadvantaged jobseekers without interfering too strongly in the way that services are provided on the ground.

²⁵ We welcome the recent decision to remove the distinction between assisted and brokered outcomes.

We identify three short-term changes to the present JSA system which together should significantly improve employment outcomes for disadvantaged jobseekers: giving unemployed people more effective choice in their provider, strengthening the levels of investment in long term unemployed people, and expanding wage subsidy programs.

5.0 Choice of provider

Unemployed people on income support generally exercise limited choices over which provider will help them and the kind of help they receive. As a result they are less engaged with the employment services system than they could be and unable to bring 'consumer pressure' to bear to improve the quality of services where this is needed.

In our APESAA submission we raised options to strengthen the influence of consumers (jobseekers and employers) within the system, including by easing restrictions on the allocation of 'business shares' by the Employment Department.

One simple change that would increase the ability of unemployed people to make an informed choice of provider is to give people a fortnight from the date of application for income support - rather than 48 hours - to make the decision. If the system of centralised business-share allocations was eased at the same time, providers would be more likely to actively compete for clients (beyond locating services close to Centrelink offices). They could also be required to participate in meetings at the local Centrelink office at which 'new' jobseekers are informed about the help available to them in the employment services system and introduced to their local providers.

5.1 Investment in people unemployed long term

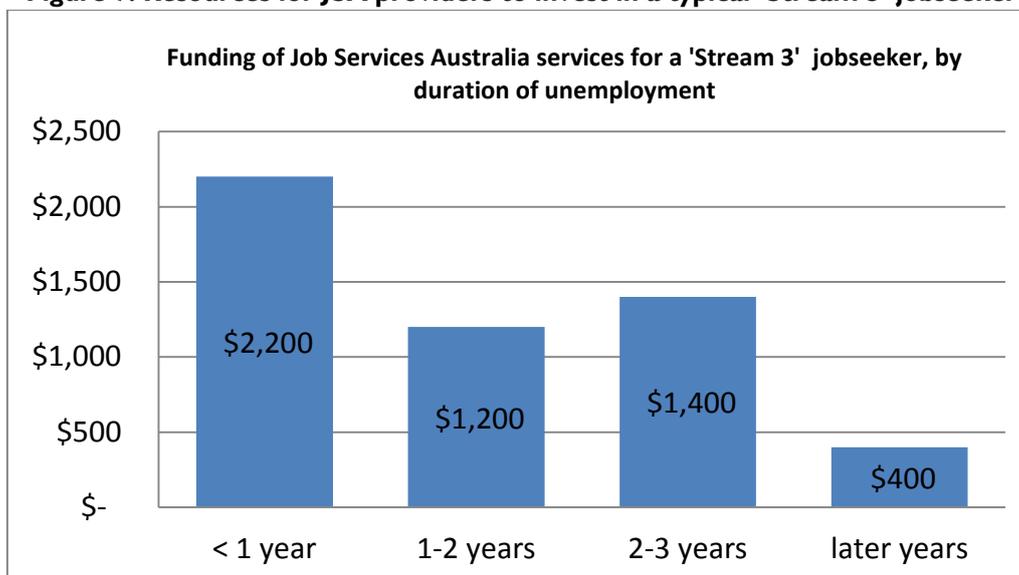
It is widely accepted internationally that employment assistance should target people who are unemployed long-term (this generally refers to people unemployed for more than 12 months). The reasons for this include the adverse social effects of prolonged unemployment and the findings of program evaluations that employment assistance has a greater impact on the job prospects of this group than on individuals who have been employed for a short time only. This is because the 'deadweight cost' of employment assistance is lower for long term unemployed people as their prospects of finding a job without assistance are much less. This was demonstrated in the Australian context in the last 'net impact study' of the former Job Network system, which found that the average impact of 'Customised Assistance' services was greater for people unemployed for 24 months than for 12 months or shorter unemployment durations²⁶.

Put simply, the system should not 'give up' on people once they have been out of paid work a long time.

²⁶ DEEWR (2010), Labour market assistance, a net impact study.

It also makes sense to target people at high risk of long term unemployment for more assistance, as the JSA system does for people in Streams 3 and 4. However, as shown in the graph below, typical service fees and Employment Pathway Fund (EPF) credits for Stream 3 jobseekers fall sharply once the jobseeker completes a year on income support and enters the so called 'work experience phase'

Figure 7: Resources for JSA providers to invest in a typical 'Stream 3' jobseeker



Note: Service fees and Employment Pathway Fund credits for a typical 'Stream 3' jobseeker in 2012-13. Does not include outcome payments as data on average 'paid outcomes' are not available.

In the second year of unemployment, the provider is paid to interview the jobseeker every two months and invest \$500 in assistance to overcome barriers to employment. In last year's Budget the Government increased the EPF credit for the third year of an individual's unemployment to \$1,000 but providers are now required to invest in 11 months of work experience activity for these jobseekers (an average of around \$100 per month in EPF credits). That will not fund effective work experience or training.

Although employment outcome payments increase with longer durations of unemployment these are modest and form the minority of overall payments received by providers.

The recently released Employment Pathway Fund evaluation gives an indication of the levels of investment by providers in different jobseekers using EPF credits. On average, the EPF funds invested in each training course were around \$300 which suggests that training courses were very limited in duration and intensity.

The average EPF investment in a wage subsidy was higher at around \$2,000. The evaluation found that wage subsidies were effective in improving people's employment prospects, increasing the average probability of exit from income support 12 months later by around 14% among those who were placed in a job. However, only one fifth of wage subsidies were offered to very long term

unemployed people (unemployed over 24 months). Most wage subsidies were offered to Stream 2 jobseekers, a group that was probably much more likely to find a job without the subsidy²⁷.

5.2 Wage subsidies

In last year's Budget \$27 million per year was allocated to fund around 10,000 wage subsidies for people unemployed 'very long term' each year. We understand take-up of the subsidies has been good among providers.

Since well-targeted wage subsidies are a relatively effective way to improve the job prospects of disadvantaged jobseekers, and there are almost 400,000 people unemployed long term on NSA or YAO, there is scope to expand the program without compromising its quality and effectiveness.

5.3 Recommendation for the 2014 Budget:

4. From 2014, Job Services Australia services for disadvantaged jobseekers should be improved by:
 - (a) increasing service fees and Employment Pathway Fund allocations for each year of the 'Work Experience Phase' for people unemployed long term, to at least the levels provided for Stream 3 clients in their first year of unemployment.
(Cost: approx. \$200 million in a full year)
 - (b) expanding the current wage subsidy scheme for people unemployed 'very long term' to 20,000 places a year and introducing a scheme that fully subsidises 6 months of paid employment (e.g. in the community sector or social enterprises) for deeply disadvantaged jobseekers.
(Cost: approx. \$300 million in a full year)

²⁷ DEEWR 2012, Employment Pathway Fund evaluation.

6 Future reforms of the support system for people of working age

This part of the submission deals with the following term of reference:

'(b) the appropriateness of the allowance payment system as a support into work, with particular reference to:

- (i) the effectiveness of the payment as an incentive into work,*
- (ii) the effectiveness of the allowance payment system in facilitating transitions between working and other activities, such as studying, caring and retirement, or in the event of illness or disability, and in helping or hindering recipients to overcome barriers to employment, and*
- (iii) the impact of the differences between pensions and allowances on the transition between working and other activities.'*

6.0 Policy development

Social security payments and employment and other supports for people of working age are best evaluated as an integrated system of support, taking account of the changing profile of people on income support and labour market conditions. Given its terms of reference and the time available to it, such an evaluation could not be undertaken by the Henry Review of the tax-transfer system. The last thorough independent review of this kind was the McClure review over a decade ago²⁸.

That review recommended more individualised assistance for disadvantaged jobseekers (including social supports as well as employment services), major reform of the 60 year-old income support payment structure for people of working age, improved financial work incentives, activity requirements and supports for unemployed people, and local service delivery partnerships to assist those people who are most disadvantaged in the labour market.

In 2002, the then Ministers for Family and Community Services and Employment and Workplace Relations released a discussion paper entitled 'Building a simpler system to help jobless families and individuals'²⁹. This raised the option of replacing separate pension and allowance payments for people of working age with a common base rate of payment and supplements for additional living costs. The goals of such reform included simplifying a complex social security system, shifting its focus from categorising people according to their barriers to employment towards help to secure it, and removing anomalies and inequities embedded in the pension/allowance system³⁰.

²⁸ Reference group on welfare reform 2000, Participation support for a more equitable society, Department of Family and Community Services.

²⁹ Vanstone & Abbott 2002, Building a simpler system to help jobless families and individuals, Departments of FACS and EWR.

³⁰ The idea of replacing our categorical income support payment system with a simpler one was not new. It had already been advanced by Minister Baldwin in the previous Government. See Perry 1994, A common payment? Department of Social Security.

The proposed reform was not implemented and pension and allowance payments continued to diverge. One reason for this was the separation of policy responsibility for income support payments between two Departments, FACS and DEWR. In 2006, the Welfare to Work policy shifted the boundaries between the pension and allowance systems for many sole parents and people with disabilities by closing off access to pension payments. Activity requirements and employment supports were extended to these groups and at the same time their rates of income support payments were reduced.

It is time to reassess whether the system of supports for people out of paid work is working as well as it can to prevent poverty and assist people to take whatever steps they can towards financial independence. A decade after the release of the 'Simpler System' report, the social security system is even more complex and riddled with payment anomalies and the gap between pension and allowance payments has grown from around \$30 per week to over \$130 per week. Since responsibility for student payments was recently shifted to the Industry, Innovation and Tertiary Education Department, policy development for income support payments is now shared by three separate Departments: DEEWR, FAHCSIA and IISRTE.

The profile of people on income support is now more disadvantaged. The ageing of the population and the prospect of future labour shortages provide opportunities to bring into paid work many people who have been excluded from it, but this will not happen without major changes in employment services, better investment in the most disadvantaged jobseekers, and better engagement with employers. The Government is experimenting with local service delivery partnerships in regions with high unemployment and social disadvantage and it is a good time to carefully assess whether the current approach is effective, including the balance between nationally determined target groups and programs and local initiative, and the incentives and resources for service providers to partner to improve people's employment prospects.

The need for external review of the employment services system is relatively urgent. The next contract round is due to commence in July 2015, so decisions on the shape of that system will have to be made in the 2014 Budget context. That means that unless an external review commences by the end of 2012 it will not be able to consult effectively with those who have a stake in the system, including jobseekers and employers. Ideally, this would be part of a wider review of the system of supports for people on income support payments, but if this is not in place by that time, a separate review of employment services should be undertaken.

The last external review of employment services was the Productivity Commission's review of the Job Network in 2001 which independently assessed the effectiveness of the existing system, sought the views of stakeholders and experts, and recommended significant changes³¹. The Job Network was substantially changed after 2003.

³¹ Productivity Commission 2001, Independent evaluation of the Job Network.

Unfortunately there was insufficient time to conduct a thorough review of the previous employment services system to inform the development of the JSA system, as the last round of Job Network contracts was due to expire in 2009. A quick public consultation process was undertaken³². The release of the evaluation of the previous employment services system, the 'Active Participation Model' of the Job Network was delayed and that information was not available to people making submissions to the Government on the future shape of employment services at that time³³.

An independent review of employment services should be undertaken now. This should be informed by DEEWRS ongoing evaluation of JSA, including a 'net employment impact' study to assess the 'value added' by employment services.

6.1 Recommendations for policy development

5. An independent public inquiry should be established to critically assess current employment participation policies for people receiving income support payments and recommend future directions for reform.
 - (a) Its Terms of Reference should include assessment of:
 - recent labour market trends and future employment prospects for people on working-age income support payments
 - trends in reliance on income support including the current and likely future profiles of people receiving social security
 - the adequacy, targeting and employment effects of income support payments for people of working age, and options for reform to facilitate transitions to employment, improve fairness and simplify the system
 - the effectiveness of employment services for disadvantaged jobseekers (Job Services Australia and disability employment services), including how these might be better integrated with vocational training, work experience, and social support services.
 - (b) The inquiry should be led by a small panel of independent experts and supported by a Secretariat drawn from the relevant Government Departments.
 - (c) It should prepare issues papers on the above topics including options for reform, consult widely with stakeholders and policy experts, and prepare a report with recommendations for Government within 18 months of its establishment.
6. If the inquiry described in the above recommendation is not established by December 2012, a separate independent review should be conducted into the effectiveness of the Job Services Australia program to inform a re-design of the system in advance of the 2015 contracts:

³² O'Connor 2007, The future of Employment Services in Australia.

³³ DEEWR 2007, Active Participation Model evaluation.

(a) This review should be led by a small panel of independent experts and supported by a Secretariat drawn from the Employment Department.

(b) It should prepare an issues paper outlining the strengths and weaknesses of the present system and future challenges and options for reform, consult widely with stakeholders and policy experts, and prepare a report with recommendations for Government within 12 months of its establishment.

6.2 The pension-allowance system

Historically, the Australian social security system for people of working age has been divided into pension payments for people who were 'unable to work' and benefit (later allowance) payments for people who were available for employment. Pension payments had no activity requirements whereas allowance payments had requirements to register with employment services, seek employment and participate in programs that improve their job prospects. Rates of allowance payments were lower than pensions on the grounds that people would only need to rely on allowances for short periods between jobs and that allowance payment rates had to preserve work incentives. Underpinning the different rates of payment was the notion that those on pensions were more 'deserving' of income support than those on allowances because they were 'unable to work'.

The implicit contract between Government and people on pension payments was they would be 'left alone' on a higher payment in return for limited expectations of help to secure employment. Pension payments were harder to obtain, but people were expected to rely on them for a long time.

The key features of pension and allowance payments are compared in table 12³⁴.

Table 12: The main differences between pensions and allowances

	Allowances	Pensions
Major payments	Newstart Allowance Youth Allowance Abstudy and Austudy Payments	Disability Support Pension Carer Payment Parenting Payment Single ¹ .
Levels of payment	Lower	Higher
Eligibility requirements to get the payment	Less strict	Stricter
Activity requirements to keep	Stricter, including work	None or less strict

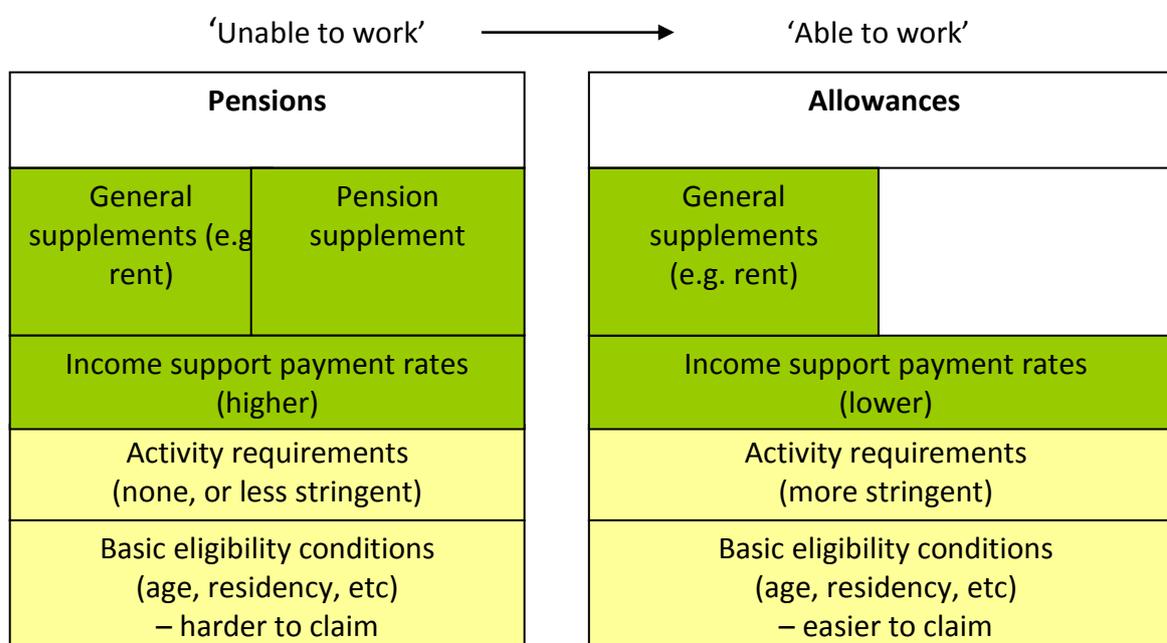
³⁴ For more detailed analysis of the pension/allowance divide and options to reform the system, see our submission to the Henry Review on the subject: ACOSS 2009, Out of the maze, ACOSS paper No .

the payment	requirements	
Income and assets tests	Tighter	Looser

1. Since 2009 the PPS payment has been treated as a hybrid payment, with lower rates than other pensions and higher rates than Allowance payments.

Australia has a categorical system of income support, with separate payments for each 'target group' such as unemployed people and people with disabilities. As indicated in the table, some are pensions and others are allowances. The pension and allowance payment systems, and to some extent each individual payment, have evolved independently, so over time not only the payment rates but also eligibility conditions and income tests diverged between different payments. In effect, we have two social security payment systems for people of working age (figure 8)³⁵.

Figure 8: Structure of the present income support system for people of working age



Note: dark shaded areas represent payment rates, lighter shaded areas represent conditions of payment

6.3 Pressures for change

The labour market and social environment has changed in three ways over the last 20 years, undermining the assumptions on which the pension-allowance system is based.

³⁵ We arguably have three systems, with allowances divided between employment participation and student payments.

First, as unemployment has fallen a growing proportion of people receive allowance payments long-term. In March 2012, 62% of people on NSA and YAO received income support for over 12 months continuously, compared with 40% in 1994. In addition an unknown proportion of people on payments 'short term' are cycling between income support and insecure employment. This challenges the notion that allowances are 'short term payments'.

Second, as unemployment has declined the profile of unemployed people has become more disadvantaged in other ways as well. In 1990, a survey of people on the former Unemployment Benefit long-term found that 3% identified as Aboriginal people, 4% had a substantial disability, and 20% were over 44 years of age³⁶. In 2010-11, 9% of *all* people on NSA identified as Indigenous, 17% were assessed with partial work capacity, and 39% were over 44 years of age³⁷. It is likely that these groups, which are generally acknowledged as disadvantaged in the labour market, form a much higher proportion of those on NSA *long term*. In addition, as discussed previously 62% of people on NSA and YA(O) are long term recipients, a proportion that has risen as unemployment has fallen.

Third, employment participation or 'activation' policies have challenged the old assumptions that people were 'unable to work'. We no longer take it for granted that people with disabilities and the main carers of children are 'unable to work' (of course carers always 'work', only without pay). The social security system increasingly expects people who were formerly categorised as 'pensioners' to seek paid employment. The old social contract referred to above is breaking down.

'I've come to sort of realise that, okay, in many ways disability is a social construction. I can't work because the workplace actually doesn't provide me with carers. It doesn't provide me with suitable equipment so that I can work. I can (no) longer drive. Now I cannot use the buses. Transport is not wheelchair accessible. How do I get to work? Wheelchair accessible taxis, the service is, one, very expensive; and, two, quite poor and unreliable in peak times. So again I realised that society was also putting restrictions on me so that even if I wanted to work it was actually going to be extremely difficult.' (Leah, Disability Support Pension)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, Allen & Unwin. (name changed to protect privacy)

Activity requirements have extended to more groups. Over the past 20 years, a number of non-activity tested payments for mature age people have been closed, and principal carer parents with school age children and people with 'partial work capacity' have faced activity requirements. Since this happened within the pension-allowance framework, many people who previously would have received pension payments have been shifted to the lower allowance payments. Thus, 8% of Newstart Allowees in 2010 were principal carers of school age children (mainly sole parents)

³⁶ Kalisch 1991, Long term UB recipients, the impact of Newsart and economic conditions, National Social Policy Conference, Sydney, July 1991.

³⁷ DEEWR, Response to Senate Estimates question EW708-12.

and 17% had a partial work capacity. *The profile of people receiving NSA today increasingly resembles that of yesterday's pensioners.*

These changes have placed increased pressure on the pension-allowance system, which lacks the flexibility to respond to them. To continue with the present distinction between pensions and allowances in these circumstances is unfair and counterproductive.

The system is *unfair* because, as the Henry Report indicated, people in similar circumstances are receiving different treatment. For example, some people with disabilities and sole parents receive \$133 and \$59 per week less than others, respectively. Most people on NSA rely on income support long-term yet receive much lower payments. Put another way, payment rates are based on people's distance from employment (and assumptions about 'deservingness') rather than their living costs.

It is *counterproductive* for the employment participation agenda for four reasons.

First, at a time when public policy is encouraging more people to engage with the labour market, the income support system pays people less the closer they come to paid employment. It requires them to prove they 'cannot work' in order to receive a higher, more secure payment. On the other hand, once they are in the pension system, especially the DSP, people are fearful of seeking employment in case they subsequently lose the job and have to fall back on NSA instead of a pension payment. Despite recent policy attempts to ease this fear, for example by giving people with disabilities 'two years grace' in paid employment before their eligibility for the pension is reassessed, it remains widespread. This is neither irrational nor surprising, since people with disabilities are vulnerable to both unemployment and financial hardship.

Second, a large part of the complexity and cost of our income support system is due to the distinction between pensions and allowances, the need for Centrelink to make increasingly fine distinctions between degrees of 'inability to work'. For example, Job Capacity Assessors must classify people according to four different levels of work capacity.

Much administrative effort is devoted to categorising people according to their degree of labour market disadvantage and presumed 'deservingness'. On the other side of Centrelink counters, applicants for payment are forced to devote considerable effort to 'proving' their inability to undertake paid work. This diverts energies on both sides of the counter away from the principal goals of the income support system: to prevent poverty and improve people's employment prospects. Inevitably, many of those judgements are arbitrary yet they now make a big difference to people's financial wellbeing.

The system is needlessly complex in other ways. Since the pension and allowance systems have developed their own independent eligibility requirements many of the differences are arbitrary. A good example is the requirement for people to be

Australian residents for at least 10 years to obtain a pension, including the DSP. No such requirement applies to allowance payments.

'I always get a chuckle from the first question I do: 'Do you require an interpreter?' I tick yes. Then [they ask] for what? SS to English.' (Stephen, Disability Support Pension)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, Allen & Unwin. (name changed to protect privacy)

Third, the pension-allowance system makes life difficult for people as their circumstances change and they have to move from one payment to another. On the 8th birthday of their youngest child, sole parents on income support arbitrarily lose \$59 per week in income support. This bears no relationship to the family's living costs, which are unchanged.

Fourth, the pension-allowance system throws up hurdles to employment participation reform. As employment participation policies are extended to more groups, the boundaries between pension and allowance payments are shifting, undermining the income security that was once promised to people on pensions. Recently, there has been public discussion of the option of activity-testing the majority of people already on the DSP payment. Although it is possible to extend activity requirements and employment supports without cutting payments, in the present pension-allowance system 'activation' is usually associated with payment reductions. Since Governments are reluctant to cut the payments of people *already* on income support (recent budget decisions with regard to sole parents are a notable exception), grandfathering arrangements are often introduced to protect their entitlements. These arrangements create their own set of anomalies and workforce disincentives.

6.4 A framework for reform

The solution to these problems with the pension-allowance system is simple: income support payments should be set on the basis of financial need rather than employability. Employability is still important in determining which activity requirements and employment supports (if any) should apply, but it should not determine levels of payment.

We outline below a framework for simplification and reform of the present system of income support payments for people of working age. These changes would not affect age pensions or Family Tax Benefits, which would remain separate. We have not developed detailed proposals because the options for reform should be carefully considered by the independent review recommended above. **However, a key condition for our support for social security reform of this kind is that no group in need of income support is left financially worse off.**

Common base rates of payment would be set for single people and couples, respectively, based on the *minimum costs of attaining a 'basic acceptable standard of*

living, the benchmark set by the Henry Report. This would remove the key distinction between pensions and allowances for people of working age. This means that people would no longer be penalised with lower payments as they move closer to employment.

The base rate of payment would be *income tested* to target income support to those in most need of financial support. Broadly speaking, the income test for those required to seek fulltime employment would be designed to cut out around or below the fulltime minimum wage. For those required to seek part time employment this constraint would be eased to make part time employment financially worthwhile.

The system would be further simplified by introducing a *common set of basic eligibility requirements*, such as residency requirements, for income support payments for people of working age.

Categories of payment (such as parenting, caring and disability) would still be needed to circumscribe the *activity requirements* that apply to individuals. In the absence of payment categories there is a risk that activity requirements would be determined arbitrarily and there would be little certainty for people about the range of requirements that might apply to them. However, the removal of the link between activity requirements and payment levels would open up opportunities to apply activity requirements in a more flexible way. They could be based on a realistic assessment of the activities and supports most likely to assist each individual to secure employment. In cases where employment prospects are very limited, no activity requirements would apply.

Supplements would be paid to assist people facing substantial non-discretionary living costs above the *minimum costs* referred to above. Examples include rent, and the extra costs associated with disability, caring, and raising a child alone. Since these costs often vary significantly among low-income households, and (apart from rents) and these variations are difficult to measure accurately, the supplements would generally be flat rate payments based on the *average* additional costs faced by the relevant target group. For example, although the Pharmaceutical Benefit Scheme covers most of the costs of prescribed drugs, many people with disabilities still face above-average pharmaceutical costs. A modest disability supplement would assist with these 'residual' costs, and as such it would be separate and distinct from a National Disability Insurance Scheme.

'I think with the amount that we are given in our pensions is not enough to cover basic, basic, basic living expenses, that for example when I hurt my back, for me to be able to get well enough to actually gain employment, I didn't have the support for it. To be able to afford physiotherapists, hydrotherapy. Even through the public assistance places where you had to pay a smaller fee for those things. Maintaining things like medications were just ridiculous. There were pills and vitamins to take to get my health to optimum levels.'

(Serena, Disability Support Pension)

Murphy et al 2011, 'Half a citizen': The stories of 150 welfare recipients in Australia, Allen & Unwin. (name changed to protect privacy)

The supplements have a different purpose to the ‘core’ income support payment. They improve horizontal equity (ensure that people can achieve similar living standards despite facing different non-discretionary costs) as well vertical equity (reducing poverty). This implies that they need not be targeted as strictly as the common base rates of payment. For example, disability, carer, sole parent and rent supplements could extend to those low fulltime wage-earning individuals or families who face additional costs, or (as is the case now with Carer Allowance) they could be paid without income testing subject to Budget priorities. In this way the supplements would strengthen incentives for people to transition from income support to at least low paid employment. As is the case with Family Tax Benefits, former recipients of income support would retain the supplementary payment once they become employed.

Another option raised in the McClure Report was to provide a modest ‘participation supplement’ to assist with the cost of job search and training, and improve incentives to undertake those activities.

The structure of the proposed system is illustrated in figure 9.

Figure 9: Proposed structure of payments for people of working age

Supplements, e.g:	Rent	Disability	Carer	Sole Parent	Job search	Training
Income support payments Based on minimum costs of living for a single adult/couple						
Activity requirements none -----work preparation/part time employment-----fulltime employment (based on disability-caring-parenting status)						
Common basic eligibility conditions residence, age etc						

Note: dark shaded areas represent payment rates, lighter shaded areas represent conditions of payment

The proposed framework retains many features of the present system. Many of the existing payments and supplements would remain in place, though rates and conditions of eligibility would change. This is desirable since evolutionary reform is more likely to be publicly supported and transitional costs and risks would be minimised.

To compare the present system with the proposed framework, we describe below how the proposed system would assist a person with disability or a sole parent with young child.

A *person with disability* would receive the same common base payment regardless of their prospects of employment. They would no longer be financially penalised because they are assessed as able to work full or part time.

If they are assessed with disability, this has two implications for their social security payments. First, their common base payment would be classified as a disability payment so that their activity requirements (if any) are adjusted according to their work capacity and best feasible path to employment. Depending on the severity of the disability this could mean that no requirements apply, but this would not affect their maximum level of payment. The income test would be less stringent to encourage part time employment (as is the case now for people on the DSP). Second, they may qualify for a disability supplement to assist with the extra costs of disability.

If they obtain employment and lose their base payment (due to the income test), they would still retain all or part of the supplement. If they lose the job and re-apply for income support, they could return to the common base payment and would receive the same level of payment as previously. Their activity requirements, if any, would depend on their work capacity.

The proposed system would allow more seamless transitions between income support and employment for people with disabilities, as well as recognising the extra costs they face whether unemployed or in paid work. Employment incentives would be significantly improved.

A *sole parent* would receive the same common base rate of payment regardless of the age of their youngest child. There would be no reduction in income support payments as the child grows older. If the child is less than 16 years of age the payment would be classified as a parenting payment. This would not affect the maximum rate of payment though the income test would be less stringent to encourage part time employment. Activity requirements would also be adjusted to take account of caring responsibilities.

The parent would also be eligible for a sole parent supplement to assist with the extra costs of supporting a child alone. Since there is already a sole parent supplement in the Family Tax Benefit System (the Part B payment extends automatically to most sole parents), this could either be paid through the income support system or the FTB system. Unlike the present FTB arrangements, the supplement would not reduce as a dependent child grows older since the costs of raising a child alone do not fall in this way. The supplement would be available to sole parents in low and middle-income employment and would act as a work incentive as well as compensating for their extra costs³⁸.

³⁸ It is widely acknowledged that sole parent families have a greater risk of poverty than couples with children, and that part of the reason for this is the additional costs of raising a child alone. These are due in part to reduced economies of scale in the family budget, in part to the time constraints facing sole parents, and also to the fact that parents on low incomes often sacrifice their own living standards to ensure that their children are not socially excluded and this is more difficult to manage when there is only one parental income.

The financial implications of the proposed system would depend mainly on the rates of the common base payment and supplements, and the income tests that apply to each. For example, the system could be designed so that most people would receive the same levels of payment they receive in the present system after the short term improvements advocated above (including the \$50 increase for those on single allowance payments) are put into place. The main exceptions to this are likely to be the new supplementary payments, though elements of these already exist in the present system. By removing the distinction between pension and allowance payments, the proposed system would lead to significant administrative savings and it would strengthen workforce participation as well as the fairness of the system.

6.5 The UK experience with income support reform

The British Government is reforming its social security system for people of working age broadly along the lines described above. It is replacing the main income support payments for people of working age and a tax credit for low paid workers called the Working Tax Credit with a single income support payment called the '*Universal Credit*'. This has been legislated and will be implemented from 2013 to 2017³⁹.

Presently there are three main payments for people of working age: Job Seekers Allowance (equivalent to Newstart Allowance), Income Support (mainly paid to sole parents) and the Employment and Support Allowance which is progressively replacing the Incapacity Benefit (equivalent to our Disability Support Pension), following changes legislated by the previous Government. The Employment and Support Allowance applies to new applicants for social security who have disabilities and is being phased in for those already on Incapacity Benefit. It is expected that the majority of new applicants will receive the 'employment component' element of this payment, which has work related requirements (mainly attendance at job centre interviews and relevant work preparation activities rather than active job search). A minority of applicants with more severe barriers to work will instead receive the 'support component' which has no activity requirements. These reforms have proved controversial because the majority of people with disabilities who would previously have qualified for Incapacity Benefit are being transitioned onto the 'employment component'.

A 'Working Tax Credit' is currently paid through the tax system in place of income support payments for individuals employed for more than 16 hours a week. This dual system of payments through the social security and tax systems is administratively complex and has created problems for people who move in and out of casual employment (who must cycle between the two systems). Further, there are limited financial incentives for people to undertake less than 16 hours a week of employment because the income support payments (unlike their Australian counterparts) are reduced Pound for Pound by earnings above a low threshold.

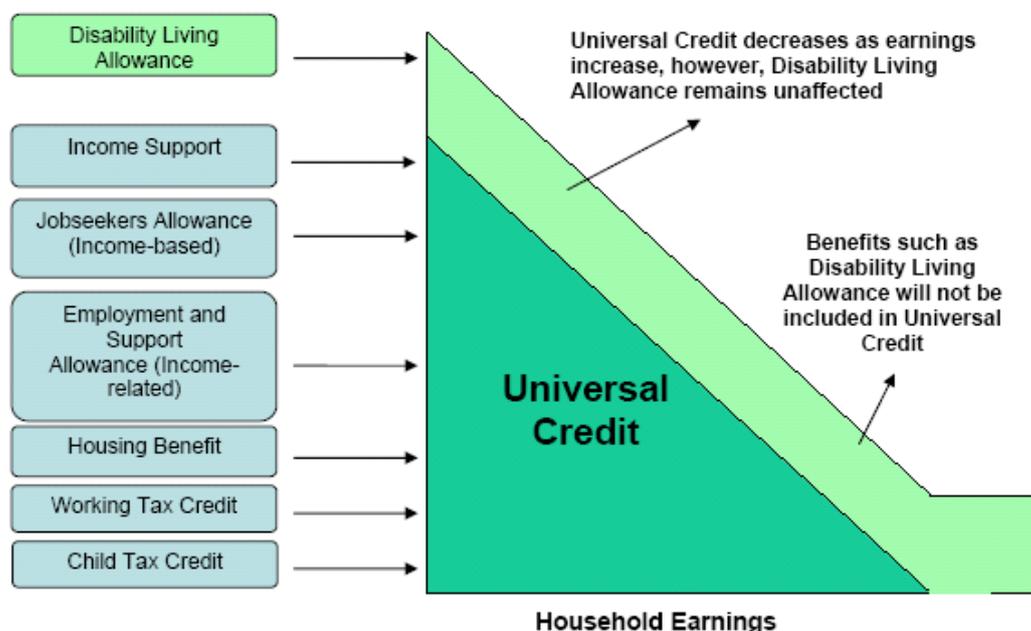
³⁹ More information is available at www.cpag.org.uk/universalcredit/.

In 2007, a landmark report on welfare reform commissioned by the previous Government, the Freud Report, advocated replacing these payments with a single base rate of income support payment. The Report suggested that activity requirements would range from active search for fulltime work to search for part time employment (for parents whose youngest child is over 12 years) and work preparation activity (for many people with disabilities). Supplements would continue to be paid to assist with the direct costs of a disability, housing costs, and the costs of caring for people with disabilities.⁴⁰

Reform of income support payments along these general lines is a bipartisan commitment. The new Government's *Universal Credit* is replacing all of the above payments with a single payment with a common base rate and a more liberal income test than the current income support payments. Activity requirements vary according to whether the recipient has a disability or is caring for a dependent child or person with disability. The proposed system more closely resembles our income support system than the status quo in the United Kingdom, except that there is no distinction between 'pension' and 'allowance' payments.

A range of supplementary payments including Housing Benefit and a 'Disability Living Allowance (a 'costs of disability' supplement), will remain in place on top of the Universal Credit (figure 13).

Figure 13: The British Universal Credit payment



Although we do not agree with all aspects of the Universal Credit policy, it is a major simplification of the structure of the British income support system broadly consistent with the framework for reform outlined above.

⁴⁰ Freud 2007, Reducing dependency, increasing opportunity, Report for Department for Work and Pensions. See also Sainsbury & Stanley 2007, One for all: active welfare and the single working age benefit, Institute for Public Policy Research, London.

6.6 Recommendations for future income support reform

7. Over time, the present three tier system of income support payments for people of working age (pensions, employment-related allowances, and student payments) should be replaced by a system with:
 - (a) common base rates of payment for singles and partnered people respectively, based on a minimum acceptable standard of living;
 - (b) common basic eligibility requirements such as residency;
 - (c) activity requirements that adjust in flexible fashion (from none to regular job search) to any constraints imposed by disabilities or caring responsibilities and each individual's pathway to employment (including fulltime study where appropriate);
 - (d) income tests that target individuals and families in greatest need of income support while encouraging part or fulltime employment as appropriate – including major reform of the income-test treatment of irregular employment;
 - (e) supplements for additional non-discretionary costs experienced by a substantial minority of people receiving people on income support including the costs of disability, caring, sole parenthood, and rent – while retaining a separate system of Family Tax Benefits to assist with the costs of dependent children.

Poverty and Exclusion in Modern Australia (PEMA) survey 2010										
	Primary income source and housing tenure									
Deprivation indicators:	All	All renting privately	Wages	Wages renting privately	'AP'	AP' renting privately	'DSP'	'PP'	'NSA'	'Other CL'
No of households in sample	2,645	364	1,632	250	264	26	55	19	20	37
% of households*	100	14	62	9	10	1	2	1	1	1
Overall outcomes (%)										
Would you describe your family as poor? (% that say yes)	11.2	23.1	6.2	13.7	18	32	47.3	55.6	60	25
Multiple deprivation (lack 3 or more out of 24 items %)	15.3	35.9	14.2	33.5	11.6	20	43.1	57.9	61.1	36.1
Housing (%)										
A decent and secure home (% who can't afford)	6.1	25.6	5.6	23.3	4.5	20.8	17	23.5	23.5	17.7
Home contents insurance (% who can't afford)	7.8	28.3	6.6	26.9	8.7	26.1	20.8	44.4	41.2	9.4
Financial resources (%)										
\$500 in emergency savings (% who can't afford)	20.7	33.1	15.3	31.4	10.9	16	37.5	36.8	50	32.4
Could not pay utility bill (at least once in the last 12 months - %)	11.6	22.8	11.7	21.3	6.9	8	26.4	31.6	40	30.3

Deprivation indicators (cont.):	All	All renting privately	'Wages'	'Wages' renting privately	'AP'	AP' renting privately	'DSP'	'PP'	'NSA'	'Other CL'
Health (%)										
Unable to buy prescribed medicines (% who can't afford - %)	2.9	6.4	2.6	5.4	0	5.5	10	11.1	25	5.7
Access to dental treatment when needed (% don't have)	16.5	31.3	15	28.3	19.2	25	42.9	47.4	44.4	28.6
Social and community participation (%)										
Regular social contact (% who can't afford)	4.7	9.9	3.8	8.4	5.4	4.2	14.3	26.3	12.5	5.7
Presents for family and friends on special occasions at least once a year (% who can't afford)	5.1	11.1	3.8	9.3	5	8.3	27.1	26.3	11.8	12.1
A week's holiday away from home (% who can't afford)	18.5	33.5	16.4	30.4	19.3	24	51.1	63.2	64.7	30.3
Child well-being (%)										
Children can participate in school activities and outings (% who can't afford)	2.6	6.5	2.1	4.6				15.8	6.3	
Up to date schoolbooks and clothes (% who can't afford)	3.4	6.4	2.3	4.1				27.8	18.8	
A hobby or leisure activity for children (% who can't afford)	4.7	9.3	3.3	6.4				26.3	31.3	

Source: Data supplied by Social Policy Research Centre from the Poverty and Exclusion in Modern Australia (PEMA) survey.

Note: Shaded cells have values of 25% or over. *13% of households in the sample are not included here (e.g. self employed and independent retirees)

AP refers to Age Pension; DSP refers to Disability Support Pension; PP refers to Parenting Payment (mainly for sole parents on low incomes);

NSA refers to Newstart Allowance (for unemployed people); Other CL refers to other Centrelink payments including Youth Allowance and Carer payment

'Could not pay utility bill' is a financial stress indicator in the PEMA survey.

24 essential items from the PEMA survey

Item	Per cent of respondents considering it 'essential'
Warm clothes and bedding, if it's cold	99.9
Medical treatment if needed	99.9
Able to buy medicines prescribed by a doctor	99.5
A substantial meal at least once a day	99.4
Dental treatment if needed	98.4
A decent and secure home	97.1
Children can participate in school activities & outings	95.8
A yearly dental check-up for children	94.9
A hobby or leisure activity for children	92.7
Up to date schoolbooks and new school clothes	92.8
A roof and gutters that do not leak	91.3
Secure locks on doors and windows	92.4
Regular social contact with other people	91.6
Furniture in reasonable condition	89.0
Heating in at least one room of the house	87.0
Up to \$500 in savings for an emergency	81.4
A separate bed for each child	81.3
A washing machine	77.7
Home contents insurance	72.4
Presents for family or friends at least once a year	71.4
Computer skills	72.6
Comprehensive motor vehicle insurance	59.9
A telephone	59.7
A week's holiday away from home each year	53.9

Source: Data supplied by Social Policy Research Centre from the Poverty and Exclusion in Modern Australia (PEMA) survey.