

Reforming workforce age payments – towards a fairer and more flexible system

A guide to the issues

May, 2003

Prepared by the Australian Council of Social Service (ACOSS) in response to the Government's "Building a simpler system to help jobless families and individuals"

Background

On 12 December 2002 Senator the Hon Amanda Vanstone, Minister for Family and Community Services and the Hon Tony Abbott MP, Minister for Employment and Workplace Relations released the Commonwealth Government's consultation paper, *Building a simpler system to help jobless families and individuals*¹.

This guide aims to:

- provide information about the Government's consultation and policy development process;
- summarise the key issues and possible future directions;
- outline ACOSS's preliminary thoughts and concerns;
- identify the essential objectives and principles for Australia's income support system; and
- seek feedback to assist in the preparation of ACOSS's written submission.

In developing ACOSS's written response we will explore the key areas of:

- economic and social drivers of change;
- anomalies, disincentives, and traps in the current system; and
- possible system design opportunities.

We do not directly answer the questions posed in the Government's consultation paper, nor include, at this stage, detailed proposals for change (although general policy recommendations are included). To exchange further information and views on proposals and directions for reform ACOSS is hosting forums in Canberra (June 4), Sydney (June 10) and Melbourne (30 May). Further details will be provided shortly.

If you wish to provide comments to ACOSS on any of the issues raised in this paper please Email them to vicki@acoss.org.au or send by fax to (02) 9310 4822 by 12 June 2003.

¹For a copy of the consultation paper visit the FaCS website - http://www.facs.gov.au/welfare_reform, or call 1800 778 827.

The consultation process

The Government has set up a multi level public consultation process that involves:

1. Written responses to *Building a simpler system to help jobless families and individuals* (**due 20 June 2003**).
2. Sixteen specific and general roundtable sessions for welfare organisations, business representatives and academics in capital cities and major regional centres between March and May 2003.
3. Twelve focus groups with income support recipients, people in paid work and retirees to put forward their views on what the objectives, design principles and key features of a new income support system for people of working age should be.

Building a simpler system to help jobless families and individuals has been based on the McClure recommendations around a simpler income support system that is “more responsive to individual needs, circumstances and aspirations and that improves incentives to work”. It sets out some basic assumptions, objectives and design principles and asks 13 questions about the possible design of a new income support system for people of workforce age.

Proposed options for reform are identified, ranging from:

- ‘Mini’: focusing primarily on the incentives and disincentives in the current system; to
- ‘Mid way’: involving a common payment for all working age income support recipients with ‘add ons’ for individual circumstances; or
- ‘Maxi’: involving radical redesign of the income support, tax and wage systems so they work more effectively together.

ORIMA consultancy are facilitating the roundtable and focus group sessions, and will consolidate the information into a report by late July 2003. A paper for Ministerial consideration is expected by the end of 2003. We understand that the Government has committed to further consultations following this, and before any reform begins.

The need for a fairer and more flexible system

Changes over time have added new layers of complexity to a basic social security structure which was designed 50 years ago. At that time there was a much clear distinction between people who needed long term payments (pensioners) and those requiring short term support (allowances). The various adjustments made to the system over the years has resulted in the complex patchwork of assistance we have today. However, reforms to date have still not fully confronted the extent of change within the labour market, family arrangements and social needs that have occurred in Australian society.

For example:

- Many recipients of social security allowances are unemployed or jobless for long periods, but are paid at a rate that assumes that their joblessness is a short-term problem.
- Many unemployed people have to overcome deeply entrenched barriers. However, few receive substantial help to overcome them (for example wage subsidies, training, and other employment assistance services).

- People with disabilities rightly have expectations of participating more fully in economic and community life, but many are held back by the high costs associated with their disability, and the lack of employment and other support services.
- Those who do get a job are more likely to find part-time or casual employment, yet the income test for allowances heavily penalises such employment.
- The different rates of payment for pensioners, Newstart Allowees, Austudy recipients and independent young people, cannot be justified on the basis of the financial needs of these groups.
- There are 15 different income support payments for people of workforce age, with widely different activity requirements which cannot be rationalised on the basis of the employment capacities, caring roles and other circumstances of the groups concerned.
- Many people face dramatic - often adverse - changes in their payments and activity requirements when they transfer from one payment to another (eg. when a sole parent's youngest child reaches 16 years or after a person on a Disability Support Pension undergoes rehabilitation and transfers to Newstart Allowance).
- Rent Assistance is ineffective in resolving the worsening housing affordability problems of people living in major capital cities.
- Australian mothers increasingly aim to combine parenting and part-time employment, yet the income tests for Family Tax Benefit, Youth Allowance, and Child Care Benefit, together with taxation, impose very high effective tax rates on mothers from low income families.

Of greatest concern is the failure of the system to meet its most important objective: to protect people from poverty. In fact, the system often discriminates against the very groups who face the highest risk of poverty (such as unemployed people and independent young people) by offering them the lowest payments. Others (notably sole parents, carers and people with disabilities) receive insufficient support to meet the special costs they face.

As the table below illustrates, despite some progress over the last 30 years, many households' social security payments are significantly lower than Australian income poverty benchmarks.

Table 1: Comparison of Social Security Payments to the Henderson Poverty Line (including housing costs) — \$ per week, September quarter 2002

Family/Income Unit	Base Rate	FTB A and/or B	Rent Assistance	Total Payment \$ per week	Poverty line \$ per week	Rate as % of poverty line
Head in Workforce						
Single adult unemployed	\$185	N/A	\$45	\$230	\$294	78%
Single, independent 18-20 unemployed.	\$150	N/A	\$45	\$196	\$294	67%
Couple unemployed – 0 children	\$333	N/A	\$43	\$376	\$393	96%
Sole Parent unemployed – 1 child	\$211	\$101	\$53	\$365	\$378	97%
Sole Parent unemployed – 3 children	\$211	\$228	\$60	\$499	\$536	93%
Couple unemployed – 1 child	\$333	\$63	\$53	\$449	\$473	95%
Couple unemployed – 3 children	\$333	\$190	\$60	\$583	\$632	92%
Head not in Workforce						
Single adult student	\$151	N/A	0	\$151	\$238	63%
Single student, independent 18-25	\$151	N/A	\$45	\$196	\$238	82%
Single Age/Disability Pensioner	\$211	N/A	\$45	\$256	\$238	108%
Age/Disability Pensioner couple – 0 children	\$352	N/A	\$43	\$395	\$338	117%
Sole Parent not in labour force – 1 child	\$211	\$101	\$53	\$365	\$322	113%
Sole Parent not in labour force – 3 children	\$211	\$228	\$60	\$499	\$481	104%

Source: Melbourne Institute, Poverty Lines and Centrelink information. The Poverty Lines used are the simplified Henderson Poverty Lines, based on the benchmarks set by the National Poverty Inquiry, updated since 1973. Note that these Poverty Lines do not take account of variations in the cost of housing, or the costs of disabilities.

Assumptions: All households have zero private income and assets. All single people live alone. All rent privately and receive the maximum rate of Rent Assistance, except adult students who are ineligible. All children are aged 5-12 years, except in the case of independent young people. Pharmaceutical and telephone allowances are not included.

GST compensation payments are included, which means that the real value of payments is overstated here since this component was designed to compensate people for the inflationary effects of the GST.

As well as being set too low, the safety net has major gaps. New migrants to Australia, are generally denied social security payments for two years. Unemployed people who fall foul of the harsh "breach" regime are frequently subject to substantial reductions in payments, or loss of payments, for extended periods of time.

Despite these problems, Australia's income support system for people of working age has many positive features. It:

- has much wider coverage than most overseas schemes;
- has payments that are based on current need rather than past wages;
- is targeted towards people on lower incomes (albeit too tightly in many cases);
- guarantees fundamental entitlements through legislation which also ensures fairer application of rules nationally;
- is linked with and articulated into the age pension system;
- is administered by a single Government agency, Centrelink, that acts as gateway to other services.

These positive aspects should be maintained in any redevelopment of the system.

Initial response from ACOSS

Overview

The present reform process provides an opportunity to reframe the structure of the social security system in a contemporary context. At the same time it allows us to identify medium term reforms that can progressively deliver a fairer and more flexible system which is responsive to modern life courses, labour markets, and social needs.

In particular, the social security system needs major structural change to improve income adequacy, remove anomalies, ease transitions, reduce work disincentives, connect it with improved employment and other support services, and make it more responsive to individual needs without treating people inconsistently.

The main objectives for any reform of the income support system should be to:

- ensure that it adequately meets people's basic income needs and reduces poverty;
- make the system fairer by removing anomalies in payment rates and conditions;
- broaden people's employment and other life opportunities in ways that respond to the diverse needs of individuals and families;
- make it simpler, more transparent, and easier to use.

This consultation process provides a welcome opportunity to advance those aims.

ACOSS has long argued the need for streamlining the present payment structure and removing the anomalies that are embedded in it. However, simplification should be regarded as only *one* of the objectives for reform, not the main goal. It should also be kept in mind that reducing the number of payments does not necessarily lead to a simpler system.

It is also unrealistic to expect the social security system to reduce poverty on its own, nor to expect it to substantially reduce unemployment. For these reasons, it is important to strengthen its role as a 'gateway' to other support systems, such as education, community services and employment, and for Governments to invest substantially in those systems. Stronger employment growth, especially in disadvantaged regions, is crucial.

We are generally sceptical of proposals to integrate the social security and income tax system, or to provide income support (beyond Family Tax Benefits) through tax credits as well as direct payments. The social security and tax systems have different objectives and political constituencies, so such proposals are likely to add to complexity instead of reducing it. Moreover, payments or tax credits that are tied to earnings from employment (such as earned income tax credits) can have a divisive effect, by separating payments for wage earners from those for jobless people. The experience in the United States is that the tax credits have grown dramatically. The separation of income support into payments for jobless people and tax credits for wage earners also poses problems for people who move frequently in and out of employment. A more effective way to improve work incentives would be to ease and streamline the most severe income tests in the social security system - which are the main source of work disincentive problems.

Another risk is an over-emphasis on the role of work incentives, both in reducing unemployment and in welfare reform. Financial disincentives are only one of many reasons that large numbers of social security recipients remain jobless. Sluggish jobs growth (especially in full-time jobs over the 1990s) is a much more important factor, as are the low education and skill levels of many jobless people. Therefore, the focus should be on the worst "benefit traps", and the most difficult workforce barriers faced by disadvantaged job-seekers.

The Australians Working Together package of \$1.7 billion over four years, announced in 2001-02 Budget, was a first down payment on welfare reform. There were a number of important measures contained in this package, including the working credit, Personal Advisers and expansion of the Personal Support Programme. However, it fell well short of the \$4 billion over two years estimated as needed by ACOSS, and unnecessarily extended the risk of harsh breach penalties to parents and mature age jobseekers.

We welcome the Prime Minister's commitment that no social security recipients will be worse off as a result of the Government's reforms. While acknowledging that there are likely to be choices and trade offs made in this process, at the least the basic entitlements should be safeguarded both for current and future recipients. Overall payment rates should not decline. Indeed, they should *increase* for the groups who are most disadvantaged by the present system. Fair and effective welfare reform will require significant investment, although it is likely to ease the rate of growth of social security expenditure in future years if the present high levels of involuntary joblessness are reduced.

Staged introduction of major structural reforms of social security is supported, commencing with the removal of the worst anomalies in rates of payment, the easing of the worst income tests, and the strengthening of public investment in crucial support services such as the Job Network and disability services, and their connections with the social security system. Options will be explored in more detail in our written submission.

Design principles and directions for reform

This section discusses some of the principles on which reform of the system should be based and outlines some possible directions for reform. This is not a comprehensive list of the problems with the present system, or our proposals for change.

The final McClure report on welfare reform² recommended, in the medium to long term, the implementation of an integrated payment system which provides adequate income support and incentives for participation. It suggested that existing categories of payment (such as Newstart Allowance) might be replaced by the single workforce age payment with the following components:

- a common individual base payment rate (probably equivalent to the lower "married rate" of payment);
- 'add on' payments recognising family status (such as living alone or supporting children) and other costs such as the costs of disability and private rents;
- supplements to help meet the costs of participation in job search, education and training.

We address each of these three components of the proposed system separately below. We also deal separately with the idea of a "single payment" for people of workforce age, and appropriate rates of payment for different family types and circumstances.

1. Categories of payment

To remove unfair anomalies, ease transitions within the system, and reduce complexity, the income support system for people of workforce age should be streamlined and better integrated. Integration should be achieved without reducing any basic entitlements.

One option raised in the final McClure Report was the replacement of existing payment categories (such as Disability Support pension and Newstart Allowance) with a single payment for people of workforce age (not including age pensions or child payments). This option is being considered as part of the present review, including the possibility of a separate disability payment (presumably not activity tested) for those people with "profound disabilities" unlikely to secure employment.

There is a risk that a *single* payment for people of workforce age would lead to a *more* complex, or *less transparent*, system. The reason for this is that any system for administering social security payments must rely on "categories" whether they are legislated as separate payments or outlined in administrative guidelines. For example, when Youth Allowance replaced two separate payments for unemployed young people and students, these payments were, to a large extent, "reproduced" within the Youth Allowance system in the form of separate categories of Youth Allowance for unemployed people and students.

Nevertheless, there are serious problems with the present categorical system. There are probably more payments than necessary. Further, the "sudden death" nature of transitions from one payment to another (such as the move from a Disability Support Pension that is not activity tested at all to a Newstart Allowance that has very rigorous activity requirements) is problematic.

Easing these *transitions* is a higher order goal than reducing the *number* of payments. Removing anomalies between the rates of different payments is critical to this.

²Final Report of the Reference Group on Welfare Reform (July 2000), "*Participation support for a more equitable society*", p34.

Aside from these broader concerns, we are wary of proposals to limit any future disability payment to the minority of people who have "profound" disabilities. This could send a signal that the Government considers they have no future employment prospects and will not support them to secure a job. It could also mean that the social security system fails to properly acknowledge the needs of the majority of social security recipients with disabilities likely to receive the "single workforce age payment" instead of Disability Support Pension. The failure of the present system to take proper account of the disabilities of many recipients of Newstart Allowance underscores this concern.

Although the idea of a single payment should not be ruled out, payment "categories" should be made transparent through legislation. Payments should be progressively integrated to remove unfair anomalies and allow smooth transitions when a persons circumstances change.

2. Adequate base rates of payment

The adequacy of income support payments directly affects people's ability to participate in the economic and social life of the community. Some payments are too low to cover basic costs of living, and slight changes in circumstances can produce serious difficulties for some people.

Table 1 (above) shows, for example:

- a single unemployed adult receives just 78% of the Henderson Poverty Line;
- a single adult full-time student receives even less, at 63% of the poverty line.

The basic principle that should apply to the setting of base rates of payment for each type of family (or single people without children) is that all essential living costs should be met based on the current needs of each group of recipients.

It is not sufficient to design a system which, *on average*, ensures that people have an adequate income across the life course, based on "insurance" principles. Countries with social insurance systems³, have to supplement payments (such as unemployment insurance) with social assistance payments. Indeed, changes in the labour market and family relationships have exposed major weaknesses in social insurance systems, in particular their inability to offer basic income protection for sole parents and for unemployed people with a limited history of full-time employment. Social insurance systems are inflexible, and changing the benefit system to reflect social and economic change is difficult because payments are based on past contributions.

Removing the worst anomalies in the present payment structure would go a long way towards reducing income poverty. The groups most disadvantaged by these anomalies - unemployed people, adult students, and young people - face a relatively high risk of poverty but are paid at lower rates than pensioners.

These payment anomalies also discourage people from moving towards employment. It is easy to see the unfairness and inbuilt disincentives, for instance, in moving off a pension to Newstart and then on to education⁴ when:

- A single disability pensioner over 21 with no children receives \$220 per week, plus Rent Assistance of \$47, additional health and other concessions, no activity/compliance tests, more liberal income and assets tests, and a payment indexed to Male Total Average Weekly Earnings.

³ These usually involve employer, employee and Government contributions to a Government-run social security fund that pays benefits based to a large extent of people's previous wages.

⁴Rates used are those effective for 20 March - 30 June 2003.

- A single adult unemployed person over 21 with no children receives \$188 per week, plus \$47 Rent Assistance, with compulsory activity tests, harsher income and assets tests, less concessions, and a payment that is only indexed to the Consumer Price Index.
- A 16-24 year old independent Youth Allowance recipient living away from home receives \$155 per week plus \$47 Rent Assistance, with compulsory activity tests, harsher income and assets tests, less concessions, and a payment that is only indexed to the Consumer Price Index.
- An adult student (over 25) on Austudy is even worse off, receiving \$155 per week but no Rent Assistance, few concessions, and a payment that is only indexed to the Consumer Price Index.

Base rates of payment for people on unemployment and student allowances, and independent rates of Youth Allowance, should be progressively raised to pension levels.

3. Taking account of family circumstances

Another key feature of any social security rate structure is the way in which the needs of different kinds of families (and single people) are taken into account.

The Government's discussion paper suggests that these be addressed by fixing a base rate of payment (presumably equivalent to the existing "married rate") and then "adding on" components to take account of the extra costs of living alone (adding up to the equivalent to the present single rate), and the costs of children.

Levels of payment for different family types and sizes must take adequate account of differences in the costs of living of these types of families (and single people living alone). These relativities should be based on research into the essential costs faced by different families.

This includes taking account of the additional costs associated with raising a child alone. Failure to take this adequately into account is to a large extent responsible for the relatively high poverty levels experienced by these families.

The discussion paper raises the possibility of a fundamental change in the way the system takes account of family circumstances: to determine rates of payment on the basis of the kind of *household* people live in rather than the kind of *family* they live in. Instead of single and married rates of payment, there would be a lower rate for people living with other adults in the same household and a higher rate for people living in a household without any other adults.

This has profound implications for the levels of payment people might receive:

- Three 30 year old adults sharing a house for six months would each receive the lower "shared household" rate instead of the single rate they presently receive, whether or not they actually share household expenses other than rent.
- If the income test were also applied on a household basis (as is the case for social housing tenants), they would have to ensure that they coordinate their income declarations to Centrelink.
- A sole parent family with two children, one unemployed and aged 21 years (treated as independent for social security purposes) and another child under 16 years, would receive Parenting Payment and Newstart Allowance payments at the lower "shared household" rate instead of the current single rates of payment.

Although it is reasonable to expect adults in the same household to share rent to a certain extent, it is probably unreasonable to expect them to share all costs. However, this proposal implies a general sharing of costs among members of a household (as distinct from members of an immediate family).

Adjustments to the base rate of payment to take account of family circumstances should be based on solid evidence of the relative costs facing different kinds of families.

The maximum rates of payment for different types of family (including single people) should accurately reflect differences in essential costs for each type of family, including the additional costs associated with raising children alone, and sharing the care of children between two families.

Differences in rates of payment should be based on people's immediate family status (for example, single or married) rather than their household status, although some account might be taken of the latter in determining maximum rates of Rent Assistance.

4. 'Add ons' to assist with special non-discretionary costs

A well targeted social security system should recognise *major non discretionary costs*, without attempting to precisely match the living costs of every family.⁵

In particular, there is a case for better assistance to meet:

- the increasingly unaffordable costs of private rents, currently supported through Rent Assistance;
- major costs directly associated with living or working with a disability.

It is an open question as to what extent the costs of community services such as child care and disability services are best met by a general income support payment, service subsidies, or a combination of the two.

Assistance for people to meet major non discretionary costs should be improved by:

- *Increasing overall levels of Rent Assistance and giving consideration to higher rates of payment for people facing the highest rental costs.*
- *Considering the introduction of a Disability Allowance to assist with the direct non discretionary costs of disabilities, in conjunction with improvements in community services to meet the needs of people with disabilities.*

5. Participation costs

Social security pensions and allowances are designed to reflect the real costs of living, or cover extra costs associated with, say, raising a child. However, the lack of recognition of the costs of seeking and preparing for work restricts many people's ability to do so.

Although many recipients are required to actively seek employment, their payments do not recognise the extra costs involved in this activity. For example, Newstart is set at a lower rate than the Age Pension despite the job search requirements attached to the former payment. If people are unable to

⁵A social security system that attempts to do this would be very complex. It would have to give its administrators a very high level of discretion to fix rates of payment for each family. Ultimately, it would look more like an emergency relief system than a social security system.

meet job search requirements due to a lack of resources, they may be breached and their payments may be reduced. This in turn makes it even harder for them to meet the requirement.

The costs of participation are not confined to job search. Many people on income support lack the financial resources to match the extra costs involved when for example, paying compulsory student fees or buying books for study. This can create disincentives for further study or training.

These issues are of particular concern given the recent moves expanding activity requirements to new groups (ie parents and mature age unemployed people) – as requirements to participate directly increase the cost to the individual or family.

In recognition of participation costs, standardised participation payments and service subsidies should be introduced to help meet the extra costs of mandatory job search, education and training activities.

6. Gaps in the safety net

Gaps in entitlement have been constructed to exclude some groups from gaining support. A number of vulnerable groups continue to be adversely affected by these policies – either before payment commences or while on income support.

The complexity of the current system of non payment periods means that potential income support recipients face a confusing system, which for example, demands a waiting period of up to 13 weeks if a single person has liquid assets exceeding \$2 500.⁶

The duration of breach penalties for failing to comply remains unacceptable, in particular the third activity test breach penalty which results in 100% withdrawal of payment for eight weeks. ACOSS and others argue that the high rates of fines imposed and the length of time for which they are imposed cannot be justified, and prove to be counterproductive. This is especially the case for vulnerable groups, such as homeless people, people who have a mental illness, and others who may not have the capacity to comply and subsequently incur a penalty that further marginalises them from social and economic participation.

The lack of an effective safety net for migrants, refugees and asylum seekers while they seek work is a further major concern which is likely to significantly reduce the likelihood of successful settlement into Australian society, let alone the immediate deprivation faced.

The safety net should be extended to vulnerable groups, in particular by reducing the waiting time for newly arrived migrants and extending support to refugees on Temporary Protection Visas on the same basis as other Protection Visa holders. Breach penalties should be eased as proposed by the Pearce Committee.

7. Targeting the system: income tests and poverty traps

Australian social security payments for people of workforce age are generally targeted towards people on low incomes. They are also targeted to exclude most people on full-time award wages, although their partners may receive payments (such as Newstart Allowance) in their own right. Income and asset tests are used for these two purposes. It is difficult to strike the right balance between this requirement and the need to ensure that paid work is not discouraged.

A key issue to be resolved is to what extent the social security system should support low paid full time employment. Governments have done so for many years through family payments for low paid

⁶Liquid assets are any readily available funds, including those of a partner, which can be accessed within 28 days of date last worked (Centrelink website 2003).

workers with children. Since the mid 1990s, social security payments (Newstart and Parenting Payment) have also extended to married couples in which one partner has a low paid full time job. However, social security allowances for adults (for example Newstart Allowance) do not extend generally to single adults employed full time on at least minimum award wages.⁷

Advocates of using the social security system (or tax credits) to subsidise low full time wages generally argue that this is necessary to:

- improve the living standards of these workers; and/or
- allow minimum wages to fall in order to boost employment.

However, the effects of lower minimum wages on employment are likely to be small, unless these wage rates are cut drastically. Moreover, there is a risk that much of the benefit of such a subsidy would flow to employers of low paid workers (rather than the workers themselves) since minimum wages would be more likely to fall if they were publicly subsidised. The future cost of maintaining such a subsidy would be considerable.

There is no pressing need for the social security system to subsidise minimum wages for single people because minimum wages are relatively high in Australia - a positive outcome of our system of minimum wages. Because of this, income tests for unemployment payments should continue to be designed to exclude full time workers on minimum wages. The same arguments apply to proposals to subsidise low paid employment through *tax credits*. A further problem with earned income tax credits like those in the United States is that they unfairly discriminate against jobless families and unnecessarily divide the income support system into one set of payments for jobless people and another for wage-earners. If it proves necessary in future to subsidise low pay, extending unemployment allowances to full-time wage earners by easing the income test would be fairer and simpler.

There is still significant scope for an easing of allowance income tests without extending these payments to full-time award wage-earners. This is desirable to address the main problem with current income tests - their effect on incentives to undertake part time employment.

However, if allowance income tests were eased to align them with those for pensions, then payments for unemployed people could extend to many full-time wage earners. From this standpoint, replacing the allowance and pension income tests with a "single income test" (applying the same income test for unemployed people, parents, people with disabilities, and carers) is problematic. However, a single income test (as distinct from uniform *maximum rates of payment*) may not be necessary or realistic, as the underlying purpose of income tests may vary between different groups.

There is a strong case for easing the most severe income tests to reduce high *Effective Marginal Tax Rates*, thereby improve incentives for part-time employment for:

- People on allowances;
- Low income families with children in both the Family Tax Benefit and Youth Allowance systems;
- Social tenants (who face the loss of public rental subsidies as well as social security payments if they obtain employment); and

⁷ Parenting Payment (Single) and Disability Support Pension do extend to some low paid full-time workers, although they comprise only a small minority of all low paid full-time workers.

- recipients of Special Benefit (who face severe "dollar for dollar" claw back of *any* additional income earned).

Some of these effective marginal tax rates are illustrated in the table below. The percentages represent the extent to which extra earnings are *clawed back* through income tests and taxation. They are all much higher than the top marginal rate of income tax.

Table 2: Benefit traps

Characteristics of tax-payer	Effective marginal tax rate on the next dollar of earnings (%)	Main reasons for this high marginal tax rate
Unemployed adult on Newstart Allowance	75%	Income test for Newstart Allowance, income tax at 17%
Low income family with one child in day care	70%	Income tests for Family Tax Benefit (Part A) and Child Care Benefit, income tax at 30%
Low income family with children aged 15 and 17 years	78%	Income tests for Family Tax Benefit (Part A) and Youth Allowance, income tax at 30%

Notes: "Low-income family" in these examples refers to families with incomes of around \$30,000 to \$40,000 per year.

The introduction of the working credit from September this year will provide some relief for people taking up irregular casual employment, but leaves some of the most severe benefit traps in place.

Another important work disincentive is the high level of "gap fees" for child care services. These average more than \$50 per week for full-time day care for a preschool age child.

Benefit traps should be reduced by easing income tests that result in high effective tax rates for unemployed people with casual or part time work, low income families with children attracting more than one income support payment, social tenants, and recipients of Special Benefit. In addition, child care gap fees should be eased for low income parents.

8. Obligations, compliance and penalties

The policy of imposing heavy obligations upon recipients, rather than balanced "mutual obligation" is of concern. "Mutual obligation" requirements must be genuinely two way and based in a legislative framework to prevent unfairness and reduce uncertainty, along with a degree of discretion to negotiate with each recipient.

Activity requirements should also be evidence based, relevant to future employment outcomes, achievable, and supported by substantial investment in employment and other assistance.

The impact of breaching on people's lives is now of significant public concern. Despite this, the number of people affected and the extent of the rate and duration of penalties remains far beyond what is in the interests of either the public or jobseekers.

Recent Government decisions have significantly eased penalties for "first breaches" and reduced the number of people adversely affected. Further action is needed to ameliorate the hardship that results for the people who are breached, and the families and communities they turn to for support.

We support the Pearce Report recommendations that⁸:

- penalties should be fully recoverable if the jobseeker takes 'reasonable steps' to comply with reasonable requirements not later than four weeks after the imposition of the breach;
- the duration of penalties should not exceed eight weeks; and
- the rate of reduction in allowance not exceed 25% of income.

The current harsh breach penalty regime for unemployed people should be further overhauled, the rate and duration of penalties further reduced, and systems developed to ensure they are used only as a last resort.

Any compulsory requirements should be restricted to employment, education and training activities, and participation in other social services and programs should remain voluntary.

9. Pathways to participation

The main purpose of the social security system should be to provide adequate income support. Social security reform cannot realistically be expected to resolve broader social and economic problems such as unemployment and marital breakdown. However, welfare reform can be designed to address a wider set of core issues than income support, including: the availability of jobs; and the education and skill levels of long-term jobless people. In turn, the social security system should be linked with services and supports needed for an individual to participate in employment and in the community, to have a secure living environment and to sustain important relationships.

Wherever the system imposes obligations on recipients to participate economically, these obligations should be underpinned by a commitment by the Government to ensure access to the services people need to meet these requirements in full. This is especially so for the most vulnerable who often have complex needs, tenuous or missing support networks, and unstable living environments.

These services include education, employment and training assistance, housing, counselling and living skills development, and health and community care.

Of particular importance is the need to improve access to secure employment for people who have been excluded from it for a long time, such as:

- long term unemployed people
- parents and carers seeking to return to employment after a number of years of full time care
- people with disabilities who aim to secure employment, and
- those social security recipients who are caught in a revolving door between public income support and insecure jobs due to a lack of skills or substantial work experience.

The ageing of the population both increases the need to integrate these groups into the paid workforce, and the potential opportunities to achieve this goal. The reason for this is that growth in the supply of workers will diminish sharply over the next few decades.

Historically, Australian Governments have guaranteed jobless people access to income support while keeping long term joblessness to a minimum through economic policies designed to maintain "full

⁸Pearce et al (2002), *Report of the Independent Review of Breaches and Penalties in the Social Security System*.

employment". Over the last 30 years, "full employment" policies have either failed or they have not been consistently applied. The result is high rates of "official" unemployment, hidden unemployment, and long term joblessness, and a greater reliance on social security among people of workforce age.

Economic policies that give the highest priority to job generation should be pursued. At the same time, the exclusion from economic life and decent living standards of those who want a job but are jobless for long periods of time should be addressed directly.

The present "guarantee" of income support for jobless people should be buttressed by a new *employment assistance guarantee* of substantial help to overcome barriers to employment for the most disadvantaged jobseekers. This is not available to the vast majority of long term jobless people under the present employment assistance system, despite the recent move to extend Jobseeker and Training Accounts to some jobseekers.

Long term unemployed people, and other long term recipients of social security payments who are seeking employment (for example, people on Disability Support Pension and Parenting Payment), should be offered an employment assistance guarantee of substantial help through an employment assistance provider, to overcome their particular barriers to employment.

The social security system should more effectively link its recipients with a range of social supports at the local level, including child care and home and community care, family support services, and social housing. Personal advisers and social workers have important roles to play in this.

10. Administration

To ensure public accountability, fairness in decision making and national consistency, a single national Government agency should be responsible for assessing and paying social security entitlements. Centrelink should continue to undertake that role, as well as acting as a key "gateway" to employment and social services.⁹

Centrelink's resources should be boosted to effectively resource its role as an initial assessment, payment, and referral agency.

⁹This does not mean, however, that Centrelink is the appropriate agency to deliver these other services. That is a matter for judgement.

In summary

Australia's income support system must continue to evolve. Modernisation of the system is needed primarily to reduce poverty and widen opportunities, not just to reduce numbers of people on payments.

We need to work towards a fairer and more flexible income support system. This requires:

- establishment of realistic poverty and adequacy benchmarks;
- removal of anomalies and rigidities from the payment structure;
- recognition of participation costs;
- liberalisation of some income tests;
- greater responsiveness to individual circumstances without undermining the system's fairness and consistency;
- a greater emphasis on encouragement to participate rather than penalising non compliance;
- commitments to improved employment, housing and other supports;
- better links between the social security and these other systems.

Although it is important to consult widely to develop a comprehensive plan for reform, that does not mean that changes which are obviously necessary should be postponed until the "blueprint" is finalised. We suggest the first elements of reform should be included in the 2004-05 Federal Budget, and that priority be given to addressing the worst anomalies in base rates of payment.

Key priorities and directions for reform proposed by ACOSS

Our key priorities for change are to improve income adequacy, remove anomalies, ease transitions, reduce work disincentives, connect it with improved employment and other support services, and make it more responsive to individual needs without treating people inconsistently. Another outcome of reform, should be a simpler, more understandable system.

The most important priority is improving the adequacy of, and removing anomalies between, base rates of payment.

Pursuing proposals to fully integrate the social security and tax systems are unlikely to bear fruit and are likely to distract from this important reform agenda. Moreover, payments or tax credits that are conditional on employment discriminate against people who are jobless and add complexity to the system. Such payments are not needed to address problems (such work disincentives) because the same goals can be achieved more simply by directly resolving problems in the existing social security system (such as harsh income tests).

We are sceptical of arguments that Governments should subsidise minimum full-time award wages for single people, since minimum wages are relatively high in Australia and reducing them is not a fair or effective way to reduce unemployment. However, the system should continue to support minimum wage-earning families.

ACOSS is developing detailed proposals for reform along the following lines:

- 1. Base rates of payment for people on unemployment and student allowances, and independent rates of Youth Allowance, should be progressively raised to pension levels.*
- 2. Although the idea of a single payment should not be ruled out, payment "categories" should be made transparent through legislation, rather than determined by administrative guidelines. Payments should be progressively integrated to remove unfair anomalies and allow smooth transitions when a persons circumstances change.*
- 3. The maximum rates of payment for different types of families (including single people) should accurately reflect differences in essential costs for each type of family, including the additional costs associated with raising children alone, and sharing the care of children between two families.*
- 4. These differences in rates of payment should be based on people's immediate family status (for example, single or married) rather than their household status, although some account might be taken of the latter in determining maximum rates of Rent Assistance.*
- 5. Assistance for people to meet major non-discretionary costs should be improved by:*
 - Increasing overall levels of Rent Assistance and giving consideration to higher rates of payment for people facing the highest rental costs.*
 - Considering the introduction of a Disability Allowance to assist with the direct non discretionary costs of disabilities, in conjunction with improvements in community services to meet the needs of people with disabilities.*
 - In recognition of participation costs, introduce standardised participation payments and service subsidies to help meet the extra costs of mandatory job search, education and training activities.*

- 6. The safety net should be extended to vulnerable groups, in particular by reducing the waiting time for newly arrived migrants and extending support to refugees on Temporary Protection Visas on the same basis as other Protection Visa holders. Breach penalties should be eased as proposed by the Pearce Committee.*
- 7. Benefit traps should be reduced by easing income tests that result in high effective tax rates for unemployed people with casual or part time work, low income families with children attracting more than one income support payment, social tenants, and recipients of Special Benefit. In addition, child care gap fees should be eased for low income parents.*
- 8. The current harsh breach penalty regime for unemployed people should be further overhauled, the rate and duration of penalties further reduced, and systems developed to ensure they are used only as a last resort.*
- 9. Any compulsory requirements should be restricted to employment, education and training activities and outcomes, and participation in other social services and programs should remain voluntary.*
- 10. Long term unemployed people, and other long term recipients of social security payments who are seeking employment (for example, people on Disability Support Pension and Parenting Payment), should be offered an employment assistance guarantee of substantial help through an employment assistance provider, to overcome their particular barriers to employment. This should be properly funded by the Government.*
- 11. The social security system should more effectively link its recipients with a range of social supports at the local level, including child care and home and community care, family support services, and social housing. Personal advisers and social workers have important roles to play in this.*
- 12. Centrelink's resources should be boosted to effectively resource its role as an initial assessment, payment, and referral agency.*

We would appreciate your feedback on these priorities.

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