Submission to Senate Education, Employment and Workplace Relations References Committee Inquiry into 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

Peter Whiteford, Crawford School of Public Policy, Australian National University

1. Introduction

The Terms of Reference of the Senate Education, Employment and Workplace Relations References Committee Inquiry into the adequacy of the allowance payment system for jobseekers and others, the appropriateness of the allowance payment system as an incentive and support into work, and the impact of the changing nature of the labour market are wide ranging.

In this submission I focus on the first of the issues identified, namely "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".

In considering how to address these issues, it is worthwhile noting that the Government has fairly recently undertaken an official review of the adequacy of pension payments as part of the Harmer Review (2009). I consider that it would be most desirable for a similar review of the allowance system and related payments to be undertaken. While there are differences in the balance of objectives for allowances and pensions, there is also a great deal of similarity between some of the objectives of the different payments, and the evidence collected and analysed for the Harmer Review is highly relevant to an assessment of the adequacy of the allowance payment system.

2. The Harmer Review's Approach to Assessing Adequacy

One of the central questions for the Harmer Review was the level at which the full rate of pension should be set. The Review's approach to this question was to test whether current rates of pension were providing a <u>basic acceptable standard of living, accounting for prevailing community standards</u>.

The Review considered that the full rate of pension should provide a basic acceptable standard of living for those who are wholly reliant on it, often for extended periods, without any assumptions about access to private income or assets. In adopting this approach, the Review notes that while the question of adequacy can be conceived of in both absolute and relative terms, ultimately it needs to be answered in the context of contemporary society, and the living standards of others.

The Review examined a range of different measures of adequacy and outcomes to consider both the adequacy of pension payments and the relativities between pensioners. In doing so, the Review observed that no single measure or benchmark could be used to determine whether or not the pension was adequate, but rather a judgement needed to be made across a range of measures.

The Harmer Review argued that "The social security system primarily supports the broader social protection system by providing a safety net for Australians without the means to achieve a basic acceptable standard of living." The Harmer Review went on to note that "... providing a basic standard of living for those not able to support themselves is a key principle of the income support system. Every citizen should be able to meet their basic needs and participate in Australian society." (Emphasis added.)

I would strongly endorse this basic principle and argue that it should also apply to allowance recipients. As noted above, there are additional considerations to be taken into account in considering the appropriate rate of allowances, particularly the desirability of assisting the unemployed in finding and returning to work. Nevertheless, adequacy is a core value in the Australian social security system. In my view there are strong arguments that in seeking a balance between adequacy of allowance payments and incentives to work, successive governments over the past two decades have moved too far from the adequacy objective, and as the system is currently configured this problem will continue to grow.

3. Background – recent labour market and income trends in Australia

The world economic situation is uncertain. Unemployment in the Euro area increased from 10.0% to 11.2% between February 2011 and June 2012, the highest level in 15 years. Even though the unemployment rate in the USA has fallen from 10% towards the end of 2009 to 8.2% currently, the proportion of adult Americans in employment (58.4%) has not increased at all over this period.

These trends stand in marked contrast to Australia, where unemployment peaked at around 6% before falling back to around 5.2% currently and the adult employment to population ratio remains close to historic highs (61.8%). While Australia has not been unscathed by global economic turmoil, we remain far better-placed than most other rich countries.

These recent trends followed a period of sustained increases in Australian living standards. Between 2002 and 2011 real per capita household disposable income in Australia grew by 2.8% per year (compared to an average of 1% per year over the previous 21 years) (Gregory and Sheehan, 2011).

These trends are also reflected in the household income surveys conducted by the Australian Bureau of Statistics (ABS). Median household income fell marginally in the period between the onset of the global financial crisis and the most recent survey in 2009-10, but in the decade before the GFC median household income grew by 53% after adjusting for inflation. Income growth was highest for the richest 20% of the population at close to 60% in real terms, but even for the poorest 20%, real incomes grew by more than 40% between 1996 and 2007.

Despite ongoing uncertainty about global economic conditions, prosperity in Australia remains both very high and relatively widespread. But clearly there are groups not sharing in this abundance. Incomes and wealth are dynamic – even if most people on average are better-off than similar groups in the past, individuals rise up and fall down the income ladder. But there is one group in Australia who has not shared at all in our rising national prosperity - people receiving unemployment allowances.

4. Assessing the adequacy of Newstart Allowances

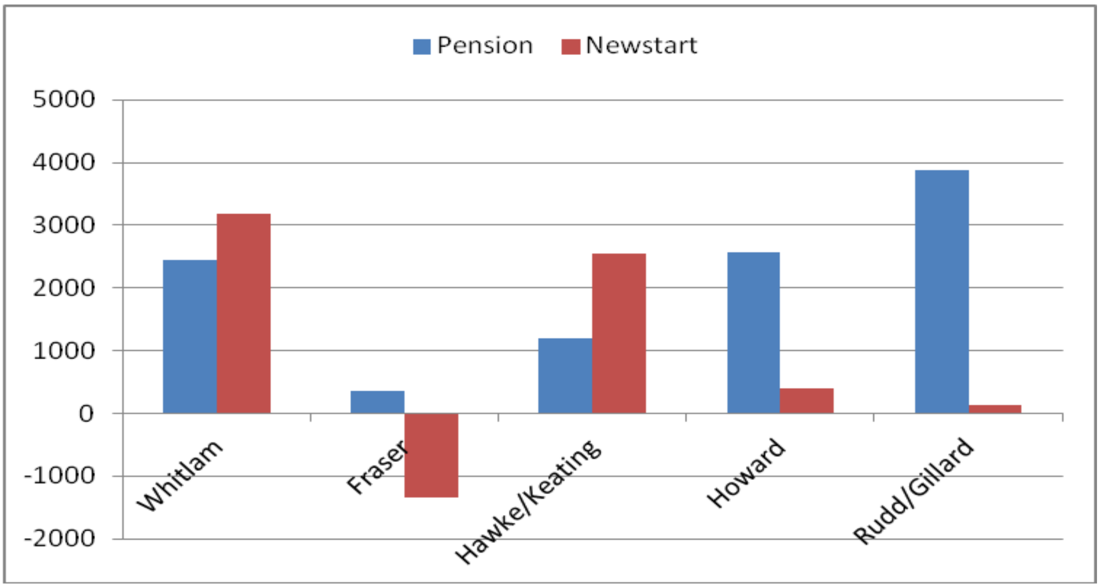
People reliant on pensions and benefits are generally recognised as being amongst the poorest in our community. Age and disability pensioners have always received higher payment rates than the unemployed, but since 1997 the gap has widened significantly, when the Howard government started to index pensions to average weekly earnings, but continued to index payments for the unemployed to the CPI.

Following the recommendations of the Harmer Review, in September 2009, the federal government increased the single rate of age pension by more than $35 per week: this was the largest pension increase in Australian history. The scale of this increase is not widely appreciated. The increase in real pension rates in 2009 was roughly equal to the cumulative real increase in pensions over the 11 years of the Howard Government, and was also greater than the cumulative increase in pensions in the period of the Whitlam government, usually regarded as the highpoint in welfare state expansion in Australia.

Figure 1 shows the cumulative increases in the single rate of pension and Newstart Allowance since 1972, adding together all the real increases that occurred by period of government. [1]

Figure 1: Change in real values of single Age Pension and single Newstart Allowance, 1972 to 2012, by period of government

Change in 2012 dollars



Source: Personal calculations.

[1] Note that this calculation shows small real increases in Newstart payments under the Howard government and the Rudd/Gillard government. This reflects the "indexation lag effect". If inflation falls over a specific period, then the indexation increase in a specific period can be slightly greater than the actual inflation rate over the same period

The 2009 pension increase was a very welcome change that significantly reduced income poverty among the aged. However, the 2009 increase widened the gap between benefits for the unemployed (including payments for lone parents with children eight years and over) and pensions for older people, people with disabilities and carers, to the point where the shortfall is now nearly $266 per fortnight. In 1996, a single unemployed person received 92% of what was paid to a pensioner; that ratio is now 65%.

It is not just that the unemployed are falling behind other social security recipients – they are falling behind every other group in the community on virtually any measure that one can come up with:

- Since 1996 payments for the single unemployed have fallen from 23.5% of the average wage for males to 19.5% currently;
- Since 1996 the level of Newstart for a single person has fallen from around 54% to 45% of the after-tax minimum wage;
- Newstart has fallen from 46% of median family income in 1996 to 36% in 2009-10 – or from a little way below the common relative income poverty standard to a long way below;
- In 1996, a single unemployed person would have received an income that was about $14 a week (in 2010 values) less than a person at the 10th percentile of the overall income distribution. In 2009-10 they would have been $116 a week below a person at the 10th percentile.

In brief, Newstart recipients are falling into continuously deepening poverty.

The impoverishment of Newstart recipients is written into legislation and cannot be alleviated without deliberate government policy change. As the system is currently configured these gaps will continue to grow over time.

The *2010 Intergenerational Report* shows the scale of the challenge. Under current policies, age, carers and disability pensions are indexed to wages, while most other payments for people of working age and families are indexed to prices. The Intergenerational Report projects that wages and therefore pensions will rise by 4 per cent a year on average, while benefits and allowances would rise in line with prices by 2.6 per cent a year. The result – if the indexation provisions actually continued for forty years – would be that in 2050 a single unemployed person would be receiving a payment little more than 11 per cent of the average male wage, compared to 19.5% now.

5. Incentives to work

But does this matter – surely the best solution for unemployment is for people to find a job? As noted earlier, Australia has been very fortunate in having one of the lowest increases in unemployment of any OECD country since 2008, but we shouldn’t overlook the fact that unemployment has still risen significantly. In June 2008 the number of people receiving Newstart Allowance was just under 430,000, its lowest level since the 1980s; this rose to 602,000 in February 2010 and has come down to 581,000 in June this year (the most recent available figure). The number of people on Newstart for twelve months or more rose from 250,000 in late 2008 to around 351,000 in recent months.

Policy changes designed to encourage employment of welfare recipients, particularly people with disability and lone parents, will mean that we can expect that more working age income support recipients will be paid under Newstart conditions in future.

Would raising benefits to a more adequate level keep the unemployed out of jobs or even cause low paid workers to give up jobs? As noted earlier, since 1996 the level of Newstart for a single person has fallen from around 54 per cent to 45 per cent of the after-tax minimum wage. If it were still 54 per cent of the net minimum wage, then benefits would be around 19 per cent higher. It is difficult to see that going back to the 1996 relativities between Newstart and the minimum wage would pose serious disincentives to work. In addition, do we really think that people need to be impoverished in order to maintain incentives to work?

Currently, single unemployed adults receive about $490 per fortnight in Newstart payments, or $35 per day. If they're renting privately, they're entitled to up to $120 per fortnight in rent assistance, but to get that amount their rent has to be more than $267 per fortnight, leaving them with just $24.50 per day for everything else; and that assumes you can find somewhere to rent for $267 a fortnight. The NSW government's *Rent and Sales Report* found that in late 2011 the cheapest one-bedroom homes in Sydney's outer ring were in Wyong – around 90 kilometres from the CBD. If you were on Newstart and paying rent for a one bedroom property in Wyong you would have just $17.15 a day left over for your food, clothing, transport and other bills. If you were paying a typical rent for a one bedroom flat in Liverpool, only 40 kilometres from the CBD, you would have less than $10 a day for everything else. While nearly 30% of Newstart recipients are under 25 and may be able to live with their parents, 36% are over 40 years of age, and are likely not to have this option.

This year's budget made some changes that changes are particularly welcome, even if their impact is more symbolic than substantial. The Income Support Supplement will be equivalent to an increase of around $4 a week in the single rate of Newstart, which is not likely to make much of an impact on the deepening poverty of this group, but it is at least some recognition of the fact that there has been no real increase in the level of payment for close to 20 years. Just as welcome is the decision to double the liquid assets test thresholds which will help reduce the likelihood that people will have to impoverish themselves just to get on to Newstart in the first place. But these are still very small changes.

Other Budget changes are more problematic. From January 2013 lone parents with a youngest child aged 8 years and over (and partnered parents with a youngest child aged 6 years and over) and who had previously been protected from policy changes in 2006 that reduced the age of eligibility for Parenting Payment will no longer be eligible for Parenting Payment. Over time up to 150,000 lone parents could be moved on to Newstart to join the 45,000 or so who are already receiving this payment.

For lone parents Newstart is about $40 a fortnight more than for other single people, but the transfer of parents from Parenting Payment to Newstart will still reduce their basic income support payment from $648 per fortnight to $530 a fortnight, or by nearly $120 a fortnight. This will be partly offset by the new Income Support Supplement and by the targeted family payment bonuses and education benefits announced in the Budget. But even adding these in a lone parent family with one child moved from Parenting Payment to Newstart will still have their benefits cut by $60 to $80 a fortnight (depending on the age of their child).

6. Conclusion

A surprising feature of the Australian social security system is that while we now have one of the least generous benefits for the unemployed among OECD countries, we actually have one of the most generous systems of payments for children in low income families in terms of the higher rate of Family Tax Benefit. But in 2009 in the same Budget that increased pensions, the government changed the indexation of family payments. Where previously, family payments had been effectively linked to the married rate of pension and therefore indexed to wages, they are now indexed to the CPI. Since it is a short period since 2009 this change in indexation arrangements has not yet had much of an impact, but in the longer run we can expect to see exactly the same problems that we now observe with Newstart. The system will become increasingly less effective in reducing poverty.

The problems faced by the unemployed have been recognised by the Henry Review of the tax system, which pointed out the need for a principles-based approach to setting payment levels. “Establishing adequacy benchmarks for transfer payments not considered in the Pension Review would make the system more robust, particularly if the benchmarks were preserved through a common but sustainable indexation arrangement.” This “would mean an increase to base rates for single income support recipients” on Newstart. The Henry Review also recommended that the maximum rate of rent assistance should be increased and the rent maximum should be indexed by movements in national rents.

So, the official inquiry into Australia’s tax and benefit system recognised that unemployment benefits are too low. This problem is not going to go away. Current policies are simply going to make the problem more difficult to deal with if decisions are postponed. It is worthwhile remembering that one of the first initiatives of the Hawke government was to increase the rate of unemployment benefits, recognising that lack of consistent indexation had made these payments inadequate. It’s time the current government recognised that unemployment payments need to be increased.

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