

## **Mission Australia's response to the Questions on Notice:-**

### **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**

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#### **1. Can you explain why a greater income free area [earning threshold] is an incentive to find work? What threshold would you suggest?**

A more generous income free area would provide job seekers with a greater incentive to work as recipients could earn more before their income support payment is affected, allowing them to bank a higher income.

Under the current system, a recipient's Newstart payment starts to decrease when their earned income exceeds \$31 per week; however this threshold is not indexed and has only increased by \$1 over the last thirty years. The Newstart threshold could be increased to allow recipients to work more casual hours, helping them to re-engage with the labour market and build their work experience. Working Credits is one mechanism by which to enable recipients to keep more of their Centrelink payments while working as they can automatically build up working credits when they have little or no income – i.e. when income is less than \$48 per fortnight. Jobseekers on Newstart are able to build one working credit for every dollar under \$48 of total income per fortnight, up to a maximum of 1,000 working credits.

Unfortunately the Working Credit system is very complex and therefore people find it difficult to understand, thereby impacting on its effectiveness as an incentive to undertake casual work. One option to improve its visibility and effectiveness would be to allow people to 'bank' income for up to six months. This would allow recipients to earn roughly a fortnight's wages at the full-time minimum wage every six months without any loss of benefits. This system should not have substantial cost implications (especially if account is taken of the current under-reporting of small amounts of earnings) and is still less generous than the Income Bank for student payments<sup>1</sup>.

However, there is a trade-off between encouraging income recipients to work and build their experience while also encouraging them to find the employment they need to get off income support. The purpose of keeping the income free area low is to encourage people to get off the payment quickly. Lifting the threshold may lead to a situation where recipients languish on the payment, undertaking the maximum amount of casual work they are able to do while still receiving their allowance.

Mission Australia believes careful economic modelling is needed to determine how much the earning threshold could be lifted to improve the financial incentive to take up part-time, casual or short-term jobs and therefore employment outcomes in the longer term.

The financial incentives must be clear and easy to explain to individual job seekers who in the short-term may feel that they are trading off the certainty of fortnightly income support payments with the less certain financial return of short-term or fluctuating income from employment.

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<sup>1</sup> Australian Council of Social Services (2012). "Committee on the adequacy of 'allowance' payments", ACOSS Paper 192, August

**2. You make a very important point in relation to unemployed young people being at risk of becoming long-term unemployed.**

**a) Can you explain why this is?**

Young people generally have lower skills, qualifications and/or work experience compared to the general population, making them much more vulnerable to unemployment than adult and older workers<sup>2</sup>. In Australia, demand for low skilled labour has declined. Young job seekers with poor education, low competencies and minimal work experience rely on low-skilled entry-level job opportunities, and this is where the biggest declines in employment have occurred. Only 1 in 8 of the new jobs created in the period of 1990-2003 were taken up by job seekers without post-school qualifications. Nearly three-quarters of all new jobs in the same period were won by university graduates<sup>3</sup>.

More than one quarter of Australia's long-term unemployed are aged 15 to 24. Since 2008, the percentage of young Australians without a job for a year or longer has almost doubled<sup>4</sup>. The longer a person is disengaged from employment the more likely their skills are to erode over time. This is particularly significant for young people who may have limited skills and/or experience. Not only are skills eroded over time, but so too are motivation and general work readiness skills, thereby increasing the likelihood that young people will find it difficult to obtain entry into the labour market. Long periods of youth unemployment may have an ongoing negative effect on young people's careers and futures<sup>5</sup> and significant social and economic costs, particularly if they remain out of the labour force for their entire working age.

**b) You say that "insufficient income support can compound the problem." Does the low rate of payments contribute to unemployment of young people? If so, how so?**

For a young person living away from home, the maximum Youth Allowance with Rent Assistance is \$482 per fortnight or just below \$35 per day. With the cost of living continuing to rise, unemployed young people dependent on Youth Allowance find themselves living in poverty and unable to afford the basics such as food, clothing and medical care. Looking for work is difficult when living in poverty. There are direct costs involved in job search and training, including the travel costs associated with applying for up to 10 jobs a fortnight. It is also difficult for YSA recipients to afford the rents charged in capital and regional cities where good employment opportunities exist; however employment prospects are reduced if they move to regional areas where rents are cheaper but fewer jobs are available.

For young people who are studying, the low rate of Youth Allowance makes them more likely to be reliant on paid work, non-cash assistance and loans to meet their daily needs, all of which adversely affects their capacity to study.

The gap between student allowances and other income support payments like Newstart hinders transitions between unemployment and full-time study. Unemployed young people over 21 years of age

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<sup>2</sup> OECD (2010). *Multilingual Summaries: Off to a Good Start? Jobs for Youth*, 1-5, 2.

<sup>3</sup> Horn, M. 2008. "Rethinking employment assistance to strengthen social and economic participation", Presentation to the 2008 Economic and Social Outlook Conference, 27th March 2008

<sup>4</sup> Foundation for Young Australians (2011). "How Young People are Faring", *National Report on the Learning and Work Situation of Young Australians*, Melbourne.

<sup>5</sup> OECD (2010). *Multilingual Summaries: Off to a Good Start? Jobs for Youth*, 1-5, 2.

who would like to transition to full time study face a \$44 per week drop in income support, making the choice of studying to improve future job prospects a difficult one.

**3. You note that “the income support system remains structured around the assumptions of [lifelong] employment/unemployment” rather than a more transitional understanding of employment.**

- **Can you go into more detail about this?**
- **Which of the policy recommendations you make in particular will address this? In other words, how do we change the allowance system to account for the changing nature of work?**

The nature and distribution of work has changed significantly over the past 30 years. As a general trend, full-time employment is declining and casual and fixed term employment is on the rise.

Work has shifted from a profile of lifelong full time employment and/or unemployment to people making multiple transitions in and out of work throughout their lifetime with an increase in the instance of casual and part-time work. Four common transitions include education / training and employment; private family based activity and paid employment; unemployment and employment; and work into retirement or between periodic incapacity for work and employment<sup>6</sup>.

Despite this shift, Australia’s income support system remains structured around the assumption of full-time employment and/or unemployment. Any deviations from this norm – for example, caring for a child, acquiring a disability, returning to further education after a stint in the workforce, reaching retirement age – are dealt with differently by the system. A new payment is required for each life transition<sup>7</sup> with different application processes, rates of payments, eligibility for concessions and participation requirements for each. All of this contributes to a clunky, complex income support and allowance payment system which rarely meet the needs of those it is trying to assist – a system that requires reform.

To make the income support system align with today’s reality of transitional employment, Mission Australia recommends system reform to introduce a single welfare payment. This would include a base amount with add-on supplements to reflect an individual’s personal circumstances and life transitions. Add-on supplements would include parenting and family assistance supplement for parents, and a rent supplement to assist with the direct costs of housing. People with a disability and those with a partial capacity to work would be eligible for a participation supplement that provides an incentive for them to work part-time.

The idea of a single welfare payment is not new and was first proposed by the McClure Report in 2000<sup>8</sup>. It was also recommended by the 2009 Henry Tax Review<sup>9</sup> in the form of a universal participation payment. The UK Government has also recently introduced ‘Universal Credit’, which brings together different forms of income-related support into an integrated benefit for people in or out of work. It

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<sup>6</sup> Gunther Schmid, cited in the Australian Council of Trade Unions (2012). “Lives on Hold: the report of the Independent Inquiry into insecure work in Australia”, Sydney p.42.

<sup>7</sup> For example, Newstart Allowance, Parenting Payment, Disability Support Pension, Austudy, Aged Pension.

<sup>8</sup> McClure, P (2000). “Participation Support for a More Equitable Society”, Final Report for Reference Group on Welfare Reform, July.

<sup>9</sup> Australian Government, (2009). “Australia’s Future Tax System”, Final Report of the Henry Review”, December.

consists of a basic personal amount with additional amounts for disability, caring responsibilities, housing costs, and children<sup>10</sup>.

If a single welfare payment were to be introduced in Australia, the level of the base or 'universal participation' payment would have to be carefully considered. It must be sufficient to support those who are unemployed to avoid poverty and be able to job search, while low enough to provide a good incentive to work. Setting the base rate should be informed by the submissions made to this Inquiry and previous work examining the issue.

At a practical level, increasing the ease and speed at which income support recipients who have exited the payment system can return if their employment circumstances change will reduce the fear and reluctance that some job seekers demonstrate with regard to the take-up of short-term or casual employment due to the lack of certainty that this provides in the short-term. Speedily reconnecting someone who has lost their job to income support and their employment services provider is likely to assist in re-engagement with the workforce and improved employment outcomes.

#### **4. Can you explain more about progressive taxation (Effective Marginal Tax Rates) interacting with social security benefits to create a barrier to unemployment?**

High effective marginal tax rates for income support recipients are a by-product of social security income tests rather than the income tax system. Taper rates for Newstart have been progressively reduced from 100% in 1994 to 60% in 2012. However the earned income of those receiving Newstart is still treated in a punitive way. A recipient's Newstart payment is taxed by 50 cents in the dollar when their earned income exceeds \$31 per week, and 60 cents in the dollar after \$127 a week. These tax rates create a real disincentive for recipients to take up employment, as losing so much of earned income to tax often makes work seem "not worth it".

In addition, the complexity of progressive taxation is a barrier to taking up work. People on allowance payments often have problems managing their reporting obligations to Centrelink when they undertake employment. Only a minority of people understand how income tests work and many reportedly assume they are tougher than they actually are, a perception that can discourage work<sup>11</sup>.

As per ACOSS's recommendations, 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 income free area and, at the same time, remove the 50% taper rate that applies to earnings between \$31 to \$125 per week, making the rate a uniform 60%<sup>12</sup>.

#### **5. a) You note that even after increasing the tax free threshold disincentives to work may still exist. Can you explain this more?**

Mission Australia acknowledges the raised tax free threshold provides income support recipients with the potential to keep more of their earned income and therefore a greater incentive to work. However we note that the combined effect of making a change to the income free area and taper rates in addition

<sup>10</sup> Department of Work and Pensions (2012). "Universal Credit", accessible at: <http://www.dwp.gov.uk/policy/welfare-reform/universal-credit/>

<sup>11</sup> Australian Council of Social Services (2012). "Committee on the adequacy of 'allowance' payments", ACOSS Paper 192, August.

<sup>12</sup> Ibid

to the raised tax free threshold would offer income support recipients a more effective incentive to work than one or the other measure on its own.

Our submission recommended Government assess the impact of the increased tax free threshold on the earned income of income support recipients, including monitoring of whether any other disincentives to work still exist within the system.

**b) Can you give more detail about other ways “recipients are disproportionately penalised for working”?**

Long-term unemployed job seekers who move from welfare to work are no longer eligible for Health Care and Pensioner Concession Cards as soon as they take on a job. These cards entitle recipients to cheaper medicines and a range of concessions relating to utilities, health, transport and education. Individuals moving from income support to employment not only have their benefits withdrawn but also become ineligible for their concessions once they reach a certain income. For those individuals with significant health or high transport costs, losing their eligibility for concession cards can make the difference between taking or not taking a job. For others it is the *perceived* value of the benefits attached to the concession cards that provides a disincentive.

One way to overcome this disincentive to work would be to allow long-term unemployed to remain eligible for these cards for a time period after they take on a job (e.g. up to 12 months).

The link between income and social housing rent can also create a disincentive to work. For income support recipients, changes in earned income can substantially increase rental payments as these are calculated as a percentage of income. Increasing paid work can also jeopardise an individual’s social housing tenancy, as tenancies are regularly reviewed and reallocated based on need. Given the scarcity and expense of the private rental market, especially in Australia’s capital cities, security of housing can often take precedence over paid work.

To address this, we suggest a review of the model of social housing rents is needed. Consideration should be given to whether rents could be structured differently. One example is the UK model, which attaches a subsidy to the property rather than the tenant. However the full implications of such a change would have to be carefully work through, including the implications for equity.

**6. You say “the income support system needs to be less complex and more flexible”, how do we simplify it while also giving more flexibility?**

We believe introducing a single welfare payment – that is a base amount with add-on supplements to reflect an individual’s personal circumstances and life transitions – will make the income support system less complex and more flexible, in addition to better reflecting the changing nature of work (see Question 3).

Mission Australia believes the complexity of the income support system will not be alleviated unless fundamental reforms are made. However if the Government is not prepared to undertake system reform but still believes further flexibility within the system is needed, one way to do this would be to allow all allowance recipients to ‘bank’ hours worked in excess of the maximum allowable hours/income.

This would give recipients the flexibility to increase their hours when required (or available) without risking financial penalties, and to work fewer hours in times when it suits them such as school holidays. It would also ensure the system better reflected the irregular hours associated with casual work.

Another way to increase flexibility and ensure allowance recipients have the security they need to take up casual work would be to allow them to remain on the Centrelink system for 12 months after commencing work, even though they are not receiving payments, provided the system facilitates rapid reconnection to employment services. This would reduce the risk of taking up employment as those who become unemployed again would avoid both the onerous re-application process and the waiting time associated with returning to income support.

**7. CPSA recommend an independent body set be set up to determine payment rates and a mechanism to maintain their adequacy over time. What do you think of this? Would you support such a body?**

Mission Australia subscribes to the recommendations made by the 2009 Harmer Review of Pensions, which rejected the idea of an independent body to determine payment rates and a mechanism to maintain their adequacy over this. The Review considered decisions on the level of support the nation is willing to provide to those with limited or no means, including pensioners, are most appropriately made by the Australian Government and Parliament as the elected representatives of the Australian people, rather than being a function that can or should be delegated. The use of public money and the political accountability involved in setting the rate of the pension is not appropriate to be under the remit of an independent body.