Australian Council of Social Service

16 June 2015

Committee Secretary
Senate Standing Committee on Community Affairs
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Committee Secretariat,

Re: Inquiry into the Social Services Legislation Amendment (Fair and Sustainable Pensions) Bill 2015 ('the Bill')

Thank you for the opportunity to participate in this inquiry.

ACOSS is a national voice for people affected by poverty, disadvantage and inequality. Our vision is for a fair, inclusive and sustainable Australia where all individuals and communities have the opportunities and resources they need to participate fully in social and economic life.

The Bill being considered by the Committee would effect changes to the Pension Assets Test and make a range of other changes to pensions.

Policy context

As the population ages, Governments will face challenges financing quality aged and health care and decent retirement incomes. The fairest and most effective way to respond to these challenges is to better target age-based payments and tax concessions rather than reduce investment in or impose higher user charges for essential services. While the current bill would improve the targeting of the pension, the bigger problem lies on the tax side, with one third of superannuation tax concessions going to taxpayers in the top 10% who are likely to save for retirement without such support and who are unlikely to rely on the Age Pension in any event.

For the most part, our social security system is well targeted. Australia's social security system concentrates support to the bottom 20% of the households more than any other OECD nation and our social security expenditure is low by OECD standards (at 8% of GDP compared to 12% on average in the OECD). Social security payments, including the Age and Disability pensions, Parenting Payment Single, Carer Payment, and Allowances provide a vital shield against poverty. These payments are frugal by international standards. In some cases, especially Allowances, they are clearly well below what is needed to meet essential living costs.

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However, during the mining boom of the 2000's, some social security payments including the Age Pension, were extended to people who did not need them. In 2006, the assets test for the Age Pension was eased to such an extent that, today, a couple with up to $1.1 million in assets besides the family home can access the part pension, and receive with it a range of concession cards and supplements funded by Government.

In addition, many retirees who are too wealthy to receive a pension under these generous rules receive a cash payment from Government: the Seniors Supplement. The Supplement also extends to many people with high superannuation incomes since the income test for existing Supplement recipients is based on taxable income, and as such does not include tax-free superannuation benefits.[1]

ACOSS has proposed a significant tightening of the Pension Assets Test to target income support more effectively to those who need it. The Government has now proposed its own changes to the Assets Test. Broadly speaking, tightening the Assets Test is a much fairer way to improve the sustainability of the Age Pension than the policy announced in the last Budget to index Pension Payments to CPI, which would have reduced the full rate of the pension for people facing a much greater risk of financial hardship.

ACOSS therefore supports the Pension Assets Test changes in this Bill, which we believe would better target the pension to those who need assistance from government. However, we believe that any changes to the Assets Test need to be done in parallel with a broader review of the retirement incomes system, which specifically addresses the fairness and sustainability of the superannuation system; and be complemented by the establishment of a regular independent review of payment adequacy, as outlined below. More broadly, governments should guarantee access to affordable and decent health and aged care services to ensure that people have security in retirement. This is related to retirement incomes policy in two ways: firstly, future governments will not have the resources to ensure access to services if superannuation tax concessions and the future costs of age pensions are not contained. Secondly, many retirees are understandably anxious about drawing down on their superannuation to meet current living costs because they fear that they may not be able to afford those services as they grow older.

ACOSS' policy goals

1. People without adequate private income should receive social security payments that meet essential living costs, according to community standards. This would mean:

    a) Social security and family payments for people without private income (including pensions, Newstart Allowance and Family Tax Benefit Part A) would

[1] A related 2014 Budget proposal, which has passed, tightens the income test for the Seniors Health Card and Supplement by including superannuation income in the test. However, since existing recipients are 'grandfathered' it will be many years before this generates substantial budget savings.

be indexed to wages as well as inflation, to stop living standards falling behind the rest of the community; and

   b) Payments for those in the deepest poverty would be raised, including those for unemployed people, sole parents, and social security recipients renting privately.

2. To the extent that pensions or other payments are extended to people who do not need public income support, income or assets tests should be tightened. In this way, Governments can save revenue to improve social security payments for people who need them, and fund essential health and community services.
3. Revenue should be adequate to meet the reasonable expectations of the community in the context of an ageing population. A tax reform dialogue is needed that does not rule in or out any reforms prior to the dialogue being held.
4. The Age Pension access age should not be raised until:
   a) Newstart and other alternative payments are made adequate (since more people will have to rely on those payments for longer);
   b) the superannuation preservation age is raised to parity with the Age Pension access age, with provisions for early access for those who need it; and
   c) employment opportunities for older people improve.

Background

Current Arrangements for Pension Payments

The individual pension rate is currently effectively indexed to wages (27.7% of Male Total Average Weekly Earnings (MTAWE)), or by movements in the CPI or Pensioner and Beneficiary Living Cost Index (PBLCI) whichever gives the highest result. This applies to the age, disability, wife, carer, bereavement and Widow B pensions.

Parenting Payment Single is set at the lower rate of 25% of MTAWE, though the indexation arrangements are otherwise the same as for other pensions.

The Age Pension is subject to an income and assets test (including income deemed to be earned from assets), with payments determined by the test that produces the lowest payment. The assets test only applies to assets apart from the owner occupied home.

The assets test taper rate reduces the value of the Age Pension according to the value of assets owned above a certain asset threshold (referred to as the ‘assets test free area’). Currently the Age Pension is reduced at a rate (the taper rate) of $1.50 for every $1000 owned above the threshold (see table 1).

By contrast, the Parenting Payment Single, along with Newstart and other Allowance payments, has a ‘sudden death’ assets test in which any assets above the assets test free area immediately disqualify people from payment. This difference in treatment of the different payment types is unjustified and inequitable.

The definition of assets under the assets test is broad and includes real estate, financial and business, and other non-financial assets (e.g. automobiles). Superannuation investments are generally regarded as a financial asset once a person reaches age pension age, and as such are included in the assets test for the age pension (they are generally disregarded for those under Age Pension age, and so would not be included in the assets test for other pensions including, for example, the Disability Support Pension). In any future assets test reform, it would be worth considering drawing a distinction between assets which can be drawn down, such as superannuation, and personal use assets such as cars and household furniture.

The 2014-15 Budget measures

The 2014 Budget proposed to reduce future pension rates for all pensioners (including the Age Pension, Disability Support Pension, Parenting Payment Single and Carer Payment) by indexing pensions to the Consumer Price Index (CPI) only instead of wages. This would have reduced the single pension rate by $80pw in 10 years' time, compared with payments people will receive under existing rules.[2]

The Government also proposed to increase the Age Pension access age to 70, which would have shifted many older people unable to find paid work onto the much lower Newstart Allowance for a further 3 years until they are eligible for the higher pension.

The changes in this Bill have been introduced following opposition from ACOSS and others to the measures in last year's budget, as they would have affected people on the very lowest incomes. ACOSS therefore welcomes the Government's decision to withdraw its policy to index Pension Payments to CPI (though notes the proposal to lift the Age Pension access age to 70 remains in place).

ACOSS Position on the Assets Test changes in the current bill

The proposed reform of the Pension Assets Test would significantly improve the means testing of Pensions by targeting the payment towards those who do not have significant assets.

An important policy goal of the superannuation system is to encourage people to contribute to their superannuation during working years, and then draw down their superannuation during retirement (rather than passing it on to the next generation). If the assets test is too liberal, this will not occur, as people will instead rely on the tax-payer funded Age Pension. Encouraging people to draw down on their assets to fund their retirement reduces the cost of the Age Pension and helps ensure that it is always there as a safety net for those who need it. The proposed reform of the Age Pension assets test would improve the draw-down incentives for those with higher assets.

[2] This estimate is based on analysis by the National Commission of Audit.

We consider that those who would be adversely affected by the pension Assets Test changes proposed are unlikely to face financial hardship because the assets available to them are sufficient to provide a buffer against poverty, in addition to any part age pension to which they may be eligible. Those with significant assets can generally avoid financial hardship through a combination of investment income, part-pension income and, where necessary, partial draw down of their financial assets, bearing in mind that once assets fall below a certain level the pension will increase.

ACOSS strongly believes that any reform to pension payments should be part of a wider consideration of reform of the retirement income system, particularly reform of superannuation tax concessions. The present tax concessions for superannuation are unfair. Currently, a third of the value of tax concessions accrues to the top 10% of income earners while the bottom 50% receive less than 20% of their total value. This is inefficient as well as unfair, as those in the top 10% are more likely to save for retirement without tax concessions and are less likely to rely on pensions in any event, yet receive more benefit from tax concessions per dollar contributed to super than low or middle income-earners.

Further, too little attention has been paid to the design of the retirement phase of superannuation. The system does not make it easy for people to steer a path between drawing down their assets to fund their retirement (which is the purpose of superannuation, not to leave tax-assisted savings to their children) and leaving themselves open to longevity risk by running down their assets too quickly. Few people can afford guaranteed or lifetime income stream products, which ensure the holder against both longevity and investment risks, while alternative account based products which are much more common and affordable allocate the entire longevity risk to retirees.

It should be recognised that retirement incomes are only one aspect of a secure retirement, and interact with other elements including affordable housing, health and aged care.

Weaknesses in the post-retirement super system, uncertainty about the future availability of what are now (largely) universal health and aged care services, and a lack of affordable housing for those who have to rent privately, are among the key reasons that many people are retaining a large portion of their capital throughout retirement. This is a bad outcome for retirees and for future Budgets.

The changing dynamics of home ownership also point to the need for a review. In the past, owning a home outright has been regarded as a pre-requisite for a secure retirement in Australia, and has been factored into the level of the Age Pension and other public supports. Yet a growing proportion of Age Pensioners do not own their own home, and are renting privately. This will become an increasing problem, given that that the pension payment is not sufficient for many households to cover the cost of rent while meeting other cost of living expenses.

While the Age Pension is a key pillar of the retirement income system, it also sits within a broader network of social security payments. Tightening the Pension Assets Test leaves unresolved the anomalies in maximum rates and indexation of income support and family payments more widely. Until 2009, the maximum rate of Family Tax Benefit A for low income families was tied to the married couple pension rate, to ensure that family payments perform their role in reducing child poverty. That link has been broken. Further, Allowance payments such as Newstart Allowance are indexed to the CPI only. Different indexation arrangements, together with the large one-off rise in the rate of the Age Pension in 2009, have resulted in a growing and unsustainable gap between pension and allowance payments (now $160pw for singles) for people with the same income support needs.

ACOSS therefore supports the Government's proposal to reform the Pension Assets Test providing:

- The indexation of pensions to CPI (only) is withdrawn;
- Any risk of adverse effects on retirees who need public income support is minimised;
- There is a commitment to a thorough public review of retirement incomes, including superannuation tax arrangements, that takes account of the affordability of health and aged care and housing, and that this is undertaken without ruling out possible policy outcomes in advance; and
- An independent expert body is established to regularly review the adequacy and indexation of social security payments for people on low incomes (including the age pension, working age payments, family payments and supplements) and that the independent expert body report to the Government and Parliament its findings and recommendations at least every four years.

Other measures proposed in the Bill

1. Defined Benefit Income Streams

The proposal to include a larger proportion of income from 'defined benefit' income streams in the Social Security Income Test (by capping the amount that can be deducted from income for the purposes of the test at 10%) will improve means testing of social security payments. It is supported.

2. Proportional payment of pensions outside Australia

The proposal is to reduce from 6 months to 6 weeks the length of time that people on the pension who have lived in Australia for less than 35 years can be paid their full means tested pension while overseas. This will mean those who rely on the full pension will not be able to travel overseas (for example to keep in touch with family, including children living abroad and to fulfil family obligations) with access to their income for any more than six weeks. As income support will be available to people who receive the payment but have lived in Australia for over 35 years, it disadvantages more recent cohorts of migrants.

3. Energy supplement replacing seniors supplement

As noted above, ACOSS strongly supports the proposed abolition of the Seniors Supplement. The Supplement is a cash payment available to many retirees who are too wealthy to receive a pension. It also extends to many people with high superannuation incomes since the income test for existing Supplement recipients is based on taxable income, and as such does not include tax-free superannuation benefits.

4. Pensioner Education Supplement and Education Entry Payment

ACOSS opposes these measures. Many people, especially sole parents, reply on the Pensioner Education Supplement and Education Entry Payment to help meet the costs of study. Further education and skills development improves work prospects, enabling people to rely less on income support in the future.

Yours sincerely,

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