Sustainable Pension Reform

Submission by
National Seniors Australia
to the
Australian Government's Pension Review

October 2008

Introduction

National Seniors Australia (NSA) believes that Australia's pension system should deliver a decent standard of living to its beneficiaries and should ensure that those under considerable financial pressure are provided with direct assistance so that they do not fall further behind as a result of cost of living increases.

With the ageing of the population there is widespread concern that the current pension system will become a more significant drain on government finances and may prove to be unsustainable in the longer term. Consistent with trends overseas, successive Australian Governments have introduced a range of initiatives aimed at taking the pressure off the public pension system, most notably through reforms to the tax and superannuation systems, to ensure the financial sustainability of the pension system for both current and future retirees.

The current retirement income system is working reasonably well for the majority of retirees. However, a significant minority, particularly those without, or with very little, private income, are in need of some form of additional assistance.

Without diminishing the importance of the fiscal impact of pension reform, NSA calls for a coherent and balanced approach to pension reform, recognising that sustainability and adequacy must be pursued jointly.

This submission reflects the views of NSA members as expressed through extensive consultations, including a recent Cost of Living survey, and focuses on:

1. Ensuring the safety net works;
2. Financial incentives for working later in life;
3. Addressing existing inequalities in retirement incomes; and
4. Improving voluntary pension provision.

Key Points

- For too long, the Australian pension system has refused to countenance the possibility that the pension base rate may be too low for those who depend on it as their main or sole source of income. It is for that reason NSA calls for the introduction of a Pensioner and Carer Cost of Living Guarantee. Just as there is a minimum wage in this country, Australia needs to ensure its pensioners and carers have enough to live on.

- The Pensioner and Carer Cost of Living Guarantee is a fortnightly income supplement (which varies from pensioner to pensioner much as a part pension does) to pensioners whose combined income from the pension and any other sources is insufficient for a modest standard of living.

- To promote continued workforce participation by older Australians, full time or part time, NSA calls for the expansion of the Pension Bonus Scheme. A more effective and generous Pension Bonus Scheme will promote workforce participation through the creation of a more even playing field, either as part of retirement or through deferred retirement. This will also reduce Government expenditure on age pension payments by several billions of dollars.

- National Seniors Australia continues its call for an increase in the rate of the single pension from 60 per cent to 67 per cent of the combined couple's pension. This would benefit all single pensioners and carers. A number of anomalies or inconsistencies across retirement income payments for a range of other groups and individuals should also be addressed as a matter of urgency.

Summary of Recommendations

1 Ensuring the safety net works

National Seniors recommends that the Australian Government:

1.1 Provide a 'Pensioner and Carer Cost of Living Guarantee' in the form of a fortnightly supplement to those pensioners and carers who are unable to support themselves on the current level of pension, and supplementary payments and concessions.

1.2 Maintain the current method of bi-lateral indexation (using both a wage and price index), while actively working towards the development of an accurate Analytical Living Cost Index (ALCI) for low-income pensioner households for use in pension indexation as well as the setting of a Cost-of-Living Guarantee.

1.3 Consider more appropriate indexation of the Utilities Allowance (UA) and Seniors Concession Allowance (SCA) to ensure they maintain their relative levels. This should have regard to the likely impact of the Carbon Pollution Reduction Scheme.

1.4 Take leadership through Council of Australian Government (COAG) in calling for all levels of government to adopt a framework for the proper indexation of state, territory and local government concessions provided to pensioners and low income self-funded retirees. This should also have regard to the likely impact of the Carbon Pollution Reduction Scheme.

2 Financial incentives for working later in life

National Seniors recommends that the Australian Government:

2.1 Expand the scope of the Pension Bonus Scheme by providing all those of age pension age, including those receiving a pension, with a rebate on all pension entitlements foregone due to earning 'wage based' income. This should be 50 per cent of all foregone pension entitlements and should be provided in the form of a lump sum rebate paid at the end of the financial year.

2.2 Undertake a public awareness campaign in order to increase uptake of the Pension Bonus Scheme, and to increase understanding of the eligibility requirements amongst those currently participating on the scheme.

3 Addressing existing inequalities in retirement incomes

National Seniors recommends that the Australian Government:

3.1 Immediately increase the rate of the single age pension from 60 per cent to 67 per cent (two-thirds) of the couple (combined) amount. This increase should be paid to age pensioners, carers, disability support pensioners and other pension categories.

3.2 Immediately index the rate of Widow's Allowance to the base rate of the single age pension, and extend the Pensioner Concession Card (PCC) to all Widow's Allowance recipients.

3.3 Immediately index Commonwealth funded superannuation and military pensions against the higher of MTAWE or CPI, in line with that applied to the age pension.

3.4 Increase the bereavement payment to 6 months for those receiving an eligible pension, benefit or allowance; extend the couple (combined) income and assets test for a period of 6 months for surviving partners; and consider additional support for those in receipt of an age pension or carer payment, who experience a divorce or whose partner/spouse becomes illness separated.

3.5 Immediately index the Pharmaceutical Allowance (PhA) to the cost of two concessional co-payments, and expand the payment to Widow's Allowance recipients and Commonwealth Seniors Health Card (CSHC) holders; and introduce a separate PBS safety net for single concession card holders set at 29 co-payments (half the standard safety net).

3.6 Immediately index the income limits for the Commonwealth Seniors Health Card (CSHC) against the higher of MTAWE or CPI, in line with that applied to the age pension.

4. Initiatives to improve voluntary pension provision

National Seniors recommends that the Australian Government:

4.1 Encourage financial institutions to do more in relation to raising people's awareness of the need to save for retirement.

1 Ensuring the safety net works

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1.1 Keeping up with the cost of living

For a significant number of pensioners, particularly those with no, or with very little, private income, increases in the age pension have lost pace with the cost of living, placing them in a very precarious position. To ensure that those under considerable financial pressure are provided direct assistance and do not fall further behind cost of living increases, NSA calls on the Government to put in place a safety net under the current pension system to provide pensioners with a Pensioner and Carer Cost of Living Guarantee.

The creation of this safety net would require regular review of cost-of-living pressures (including private residential rents), which may be different for different categories of pensioners and may lead to different safety net outcomes similar to the way in which the minimum wage is determined. The Pensioner and Carer Cost of Living Guarantee could be provided as a top-up payment in the form of a fortnightly supplement. It could be designed as the difference between a pensioner or carer’s actual or deemed income and the income needed for a modest standard of living, and it could vary depending on individual circumstance.

To better enable the government to determine eligibility for the Pensioner and Carer Cost of Living Guarantee payment, as well as an appropriate level of support, it is proposed that a series of benchmarks be developed, along the lines of the Analytical Living Cost Index (ALCI). These benchmarks will need to be sufficiently disaggregated to distinguish cost pressures for distinct groups of age pensioners (such as singles, and private renters).

1.2 Indexation

From an aggregated viewpoint, benchmarking against the higher of CPI or 25 per cent of Male Total Average Weekly Earnings (MTAWE) over the last ten years has resulted in a real increase in the pension. From June 1998 to June 2008, the pension increased by 54 per cent, compared with a 36 per cent increase in the CPI, and a 38 per cent increase in the Analytical Living Cost Index (ALCI) for Age Pensioner Households. For this reason, NSA supports the current method of bi-lateral indexation of pensions (using both a wage and price index).

However, this method of pension indexation is, in part, based on the assumption that, if pensions are increased in line with national economic development, the standard of living of all pensioners will be maintained or improved. While this assumption needs to be revisited (particularly so with the imminent introduction of a Carbon Pollution Reduction Scheme likely to accelerate price increases for essential goods and services), it also needs to be challenged on the basis that it does not countenance the possibility that the base rate of the pension has always provided a subsistence income only, particularly for single pensioners. In other words, current pension indexation does not acknowledge that the pension may be set too low.

For this reason, NSA urges the Australian Government to further develop and improve the ALCI approach. The current ALCI approach has a number of shortcomings on which there appears to be general agreement. Firstly, there is currently no ALCI which encompasses all pension recipients; instead there are separate ALCIs for age pension households, and other welfare recipient households. Secondly, the assumption in the ALCI approach is that even the lowest income level is adequate. However, the weighting of commodity groups within the ALCI is based on the 2003 Household Expenditure Survey, which only tracks actual expenditure and not whether survey participants were able to purchase all essential goods and services and, if so, in sufficient measure.

The Australian Bureau of Statistics (ABS) has done much valuable work in this area, however NSA believes that more needs to be done to track the adequacy of the base rate of the pension and favors the use of an improved ALCI for pensioner households in determining the level of the pension base rate and the Pensioner Cost of Living Guarantee.

1.3 Supplementary payments

On 20 September 2008 a number of supplementary payments were also increased in line with CPI, including Utilities Allowance (UA) and the Seniors Concession Allowance (SCA). The use of the CPI for these payments has overestimated their real value and has widened the gap between the level of assistance they provide and the cost of the goods and services which they target. There is an obvious case for changing the basis of indexation for these allowances to a more appropriate commodity group, such as the utilities component of the CPI.

The 2008-2009 Federal Budget increased the UA and SCA to an amount that has more than compensated for any loss in value over recent years. However, the continued indexation against the CPI has already led to a reduction in their real value since the 2008-2009 Budget. Both allowances, which started off at $500 per annum in March 2008, now stand at $514 per annum due to indexation. Had the utilities component of the CPI been applied in September this year, the allowances would now stand at $517.50 per annum. In other words, after just six months the value of both allowances has fallen $3.50 behind actual utilities costs over the same period.

1.4 State, territory and local government concessions

In addition to federal government support, pensioners receive a range of concessions at the state, territory and local government levels. These concessions form an integral part of pensioners' income and assist with several major household expenditure items, such as energy, water and sewerage and local rates. The differentiation of concessions across jurisdictions enables the value of concessions to be set according to regional variances in the cost of particular goods and services, such as energy or water prices. However, in reality this opportunity has not been realised, with concessions in many cases losing their real value due to infrequent or inappropriate indexation.

In many jurisdictions, concessions currently fail to recognise the particular circumstances of those pensioners living in rural and regional areas. The Senate Community Affairs Committee Report *A decent quality of life* (2008) found that transport-related costs are a particularly prominent cost pressure for older people living in rural and regional Australia, and have strong implications for community involvement and social interaction. The current irregularity of concessions provided to low income self fund retirees across jurisdictions also needs to be addressed.

The Australian Government's commitment to assist households to adjust to the impact of the Carbon Pollution Reduction Scheme by increasing payments above automatic indexation is welcome. To assist in ensuring that supplementary payments and concessions do not also lose their relative values in the face of increased energy and utilities costs, it is essential that all levels of government develop an appropriate framework for the setting and maintenance of concessions provided to low-income households.

2 Financial incentives for working later in life

2.1 Expand the scope of the Pension Bonus Scheme by providing all those of age pension age, including those receiving a pension, with a rebate on all pension entitlements foregone due to earning 'wage based' income. This should be 50 per cent of all foregone pension entitlements and should be provided in the form of a lump sum rebate paid at the end of the financial year.

2.2 Undertake a public awareness campaign in order to increase uptake of the Pension Bonus Scheme, and to increase understanding of the eligibility requirements amongst those currently participating on the scheme.

2.1 Expanded Pension Bonus Scheme

Due to its inflexibility and relatively low level of financial incentive, the Pension Bonus Scheme is currently failing to encourage continued participation on an adequate scale. The effect is that savings for government and the opportunity for additional accumulation for the individual are being under utilised. Currently, only 3.2 per cent of age pensioners have private earnings (FAHCSIA Budget Statement 2008-2009).

There is also considerable scope for the Pension Bonus Scheme to be expanded in order to provide an incentive for those who are currently receiving an age pension to earn additional income. The current income test applied to pensions and allowances is serving to discourage income support recipients from remaining in, or re-entering the workforce. This has directly contributed to the inadequacy of retirement incomes for some pensioners, as they have been discouraged from topping-up their incomes through part-time employment. For a single rate pensioner earning $200 per week in wages, every $1 in income earned reduces the pension by 25 cents a week. In effect, this represents a virtual tax rate of over 25 per cent (see Figure 1).

Figure 1: Impact of additional income on single rate pension entitlements & total income (under current income test)

Private wage based income (per week)	**$100**	**$150**	**$200**	**$250**	**$300**	**$350**	**$400**
Pension reduction (per fortnight)	$25	$65	$105	$145	$185	$225	$265
Net impact on additional (wage) income	-12%	-22%	-26%	-29%	-31%	-32%	-33%

(Source: National Seniors Australia, National Policy Office)

Expanding the Pension Bonus Scheme to provide those already receiving an age pension with a 50 per cent rebate on lost entitlements resulting from 'wage-based' income would enable those who are eager to top up their incomes to do so without being unfairly penalised. Under this proposal a single rate pensioner earning an additional $250 per week would be over $35 a week better off than under current arrangements, and a pensioner couple earning $600 per week (combined) would be $76 a week better off (see Figure 2).

Figure 2: Impact of additional income on single rate pension entitlements & total income (under expanded Pension Bonus Scheme)

Private wage based income (per week)	**$100**	**$150**	**$200**	**$250**	**$300**	**$350**	**$400**
Pension reduction (p/fortnight)	$25	$65	$105	$145	$185	$225	$265
Pension rebate (p/fortnight)	$12	$32	$52	$72	$92	$112	$132
Net impact on additional (wage) income	-6%	-11%	-13%	-15%	-15%	-16%	-17%

(Source: National Seniors Australia, National Policy Office)

In order to provide a worthwhile incentive to postpone retirement, the Pension Bonus Scheme should provide participants in the scheme with at least 50 per cent of their foregone pension entitlements. Further, to ensure that participants are rewarded equally irrespective of the length of participation on the scheme, bonus payments should be based on the number of days that entitlements have been foregone with no minimum or maximum claim periods. The current requirement that participants in the scheme make a claim within 13 weeks of ceasing work should also be removed.

3 Addressing existing inequalities in retirement incomes

3.1 Immediately increase the rate of the single age pension from 60 per cent to 67 per cent (two-thirds) of the couple (combined) amount. This increase should be paid to age pensioners, carers, disability support pensioners and other pension categories.

3.2 Immediately index the Widow's Allowance to the base rate of the single age pension, and extend the Pensioner Concession Card (PCC) to all Widow's Allowance recipients.

3.3 Immediately index Commonwealth funded superannuation and military pensions against the higher of MTAWE or CPI, in line with that applied to the age pension.

3.4 Increase the bereavement payment to 6 months for those receiving an eligible pension, benefit or allowance; extend the couple (combined) income and assets test for a period of 6 months for surviving partners; and consider additional support for those in receipt of an age pension or carer payment, who experience a divorce or whose partner/spouse becomes illness separated.

3.5 Immediately index the Pharmaceutical Allowance (PhA) to the cost of two concessional co-payments, and expand the payment to Widow's Allowance recipients and Commonwealth Seniors Health Card (CSHC) holders and introduce a separate PBS safety net for single concession card holders set at 29 co-payments (half the standard safety net).

3.6 Immediately index the income limits for the Commonwealth Seniors Health Card (CSHC) against the higher of MTAWE or CPI, in line with that applied to the age pension.

Under the current pension system, NSA has identified a number of anomalies or inconsistencies across retirement income payments for a range of groups and individuals that should be addressed as a matter of urgency.

3.1 Single Age Pensioners

There is substantial evidence to suggest that single age pensioners are more likely than partnered pensioners to be to be at risk of having insufficient income to cover living expenses. The Senate Community Affairs Committee's 2008 report, *A decent quality of life: Inquiry into the cost of living pressures on older Australians,* highlighted that the age pension alone is insufficient to meet the expenses needed for a modest living in retirement, and those most at risk of financial stress are single pensioners receiving the maximum rate of pension and living in private rental accommodation.

The current single rate of pension in Australia, at just below 60 per cent of the combined couple amount, does not adequately recognise that singles lack the benefits of shared living and economies of scale. We argue that an increase in the proportion of the single rate to two-thirds of the combined couple amount would restore the balance between actual costs for a single and the level of support provided by the single pension. This will also bring the Australian single rate closer to the rate in countries such as the US, UK and New Zealand. We acknowledge that this would require a change to the current basis of calculating the rate of pension from the single rate to the partnered rate.

3.2 Widow's Allowance

Recipients of the Widow's Allowance currently receive a lower base rate payment compared with pensioners and carer payment recipients. Some Widow's Allowance recipients also do not receive many of the state, territory and local government concessions that are provided to Pensioner Concession Card holders.

The 2008-09 Federal Budget extended a number of supplementary payments to allowance recipients. However, while welcome, these payments will not fully offset inadequacies resulting from the low base rate. The gradual extension of some but not all payments to Widow's Allowance recipients has also created confusion as to whether these recipients should be treated the same as pensioners or those on Newstart Allowance.

3.3 Commonwealth superannuation & military pensions

Between June 1998 and June 2008, MTAWE increased by 50 per cent while the CPI increased by only 36 per cent. In contrast to the bi-lateral indexation of age and disability pensions and the carer payment, military pensions and commonwealth superannuation are indexed solely against the CPI. A non-uniform approach to the indexation of retirement incomes is both inequitable and divisive, and serves to undermine public trust in retirement standard benchmarks. NSA believes that the Government should immediately implement the recommendations of the Senate Report on Superannuation and Standards of Living (2002), that commonwealth superannuation be indexed against the higher of MTAWE or CPI.

3.4 Transition to a single rate

Aside from the emotional impact, the transition from being in a couple to being single can result in considerable financial pressure. This impact is likely to be more pronounced for those who experience bereavement while in receipt of a pension or allowance. Under current arrangements, bereaved partners receive inadequate support, while those who experience divorce or illness separation receive no additional support.

NSA estimates that surviving partners, who had a combined private income of between $5,000 and $40,000 as a couple, would see a reduction in their total income of between 21 and 35 per cent as a result of the application of the single income test. The impact of the single means test could also result in a surviving partner losing all eligibility for the age pension, and its associated concessions provided at the state, territory and local government levels.

The bereavement payment currently provided by the Department of Families, Housing, Community Services and Indigenous Affairs for those in receipt of an eligible pension, benefit or allowance gives only 14 weeks to adjust to a new situation. In many cases, widowed pensioners face additional expenses with a much reduced income, such as the financing of house and car maintenance and repairs that previously were undertaken by their late partners. An increase in the amount of payment, and an extension in the period before the application of the single means-test would greatly assist surviving partners to adapt to their new financial circumstances.

3.5 Pharmaceuticals

Over the last 10 years, the Pharmaceutical Allowance (PhA) has increased by only 7 per cent, compared with a 36 per cent increase in the CPI. This has resulted in a decrease in the real value of the allowance, and as a consequence the PhA is now equal to only 1.2 co-payments per fortnight. Indexing the PhA to the cost of two co-payments would ensure it maintains its value over time, and would restore the original intent to pay for two fortnightly co-payments for PBS listed prescription medicines.

Typically, self-funded retiree households spend proportionally more of their income on health-related costs, compared with all other household types, including age pensioners. The impact of increasing health costs, and particularly pharmaceuticals, would therefore have been greater for self-funded retirees. From December 2007 to June 2008, the cost of pharmaceuticals increased by over 12 per cent, more than all other goods and services, with the exception of automotive fuel costs. Extending the PhA to Commonwealth Seniors Health Card (CSHC) holders would greatly assist in relieving these health-related cost pressures.

The PBS Safety Net assists individuals and families with high prescription medicine costs. Each year the Government sets a safety net threshold for general and concessional patients, after which PBS medicine is either cheaper, or without cost, for the remainder of the calendar year. Eligible concession card holders currently pay $5 per PBS-listed prescription for the first 58 scripts ($290), after which they are free. This system disadvantages individuals who have to reach the same threshold as couples and families. The introduction of a safety net for individuals, set at 29 co-payments ($145) for concession card holders, would restore an equitable balance between singles and couples in respect to pharmaceutical costs.

3.6 Commonwealth Seniors Health Card (CSHC)

The scope of the Commonwealth Seniors Health Card (CSHC) has widened significantly since its introduction in 1994, from solely providing pharmaceutical concessions to providing a range of payments to assist with utilities and communication costs. However, unlike the level of assistance provided by the CSHC, the income limits have remained the same, having not been increased since July 2001. The immediate indexation of these income limits in-line with a wage based index would ensure a uniform approach, and would restore parity with the method for increasing the age pension.

4. Initiatives to improve voluntary pension provision

4.1 Encourage financial institutions to do more in relation to raising people's awareness of the need to save for retirement.

It has been asserted that people who are not totally prepared for retirement are vulnerable to falling into poverty into later life (*The Future of Retirement: Investing in later life*, *HSBC insurance, 2008*). Research shows that almost half of all working Australians are not prepared for retirement. A global reference study of 26 countries showed that Australians are slow to start their own retirement planning. More alarmingly, 39% of those already retired have never reviewed their retirement plans, the majority of whom are low and middle income earners (*AXA Retirement Scope 2008*).

We believe that much more needs to be done in relation to raising people's awareness of the need to save for retirement. We believe that this needs to be an ongoing priority, and will require the allocation of significant resources to be effective.

We know that many people – not just retirees – do not have sufficient information or expertise to plan adequately for the use of their retirement funds over their remaining lifetime. In particular, there is a risk that those who live substantially longer than the average may run out of funds. This is an issue that needs to be addressed by building on the work that is currently being done by Centrelink, through the Financial Information Service (FIS). There is also considerable scope for banks, financial institutions and superannuation funds to develop financial planning education programs for their clients.

National Seniors Australia – Members Survey

Between 15th September and 1st October 2008, National Seniors' members were invited to complete a Cost of Living Survey. Over one thousand members, aged over 50 years, completed the survey. Of these, 56% receive a government pension or allowance and 35% have a Commonwealth Seniors Health Card (CSHC). Fifty-one percent of the respondents were female and 63% were married. Results from this survey support the recommendations made in this submission and are summarised below.

1. Ensuring the safety net works

- 45% of those whose principal source of income is a government pension or allowance say their income is not enough to meet everyday needs. This compared with 11% whose principal source of income is superannuation and 10% whose principal source of income is salary/wages.
- 28% of older people who receive a pension/allowance are living on $15,000 or less per year, compared to 4% of non-pensioners.

2. Financial incentives for working later in life

- 17% of those receiving a government pension or allowance have taken up part-time work in retirement to top up their income. This compared with 36% of those not receiving a government pension or allowance.
- 24% of pensioners have actively looked for work, compared to 37% of non-pensioners.
- 20% of those receiving a government pension or allowance have turned down part-time work because it would reduce their entitlements.

3. Addressing existing inequalities in retirement incomes

- 45% of women receiving a government pension or allowance have put off visiting a doctor/dentist in the last 12 months to keep costs down – compared with 27% of men.
- 26% of those living in rural areas have had to seek financial help in the last 12 months – compared to 12% of those living in capital cities.
- 50% of those receiving a government pension or allowance that are divorced/separated/widowed have used the annual bonus to pay off debt – compared to 35% of those receiving a government pension or allowance and who are married/de facto.
- 67% of those in rental accommodation who are receiving a government pension or allowance always have difficulty putting money aside for savings, compared with 37% of people who own their home outright.
- 22% of those living alone would be unable to raise $2,000 in an emergency compared with 10% of those living with partner/spouse/others.

4. Initiatives to improve voluntary pension provision

- 80% of those receiving a government pension or allowance have difficulty putting money aside for savings.
- 40% of those receiving a government pension or allowance have used the annual seniors and carers bonus to pay off debt.