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Adequacy of the allowance payment system for job seekers,
the appropriateness of the allowance system as a support into
work, and the impact of the changing nature of the labor
market - submission

for the Commonwealth of Australia, Senate Education, Employment and
Workplace Relations Committee

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informing you is a consulting firm.

ABN 25 736 872 835

Post PO Box 176 Surrey Hills 3127

Email info@informingyou.com.au

www.informingyou.com.au

Phone 03 9890 8007

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Background

The Commonwealth of Australia Senate Education, Employment and Workplace Relations Committee seeks submissions for the inquiry into the adequacy of the allowance payment system for job seekers and others, the appropriateness of the allowance payment system as a support into work and the impact of the changing nature of the labor market. This covers:

- (a) the adequacy of the allowance payment system for job seekers and others, with particular reference to the adequacy of the New start Allowance payment as an income support payment for job seekers and the adequacy of all other allowance payments that support a range of recipients who study or provide care;
- (b) the appropriateness of the allowance payment system as a support into work, with particular reference to: (i) the effectiveness of the payment as an incentive into work, (ii) the effectiveness of the allowance payment system in facilitating transitions between working and other activities, such as studying, caring and retirement, or in the event of illness or disability, and in helping or hindering recipients to overcome barriers to employment, and (iii) the impact of the differences between pensions and allowances on the transition between working and other activities; and
- (c) the impact of the changing nature of the labor market, particularly the rise of insecure work and decline of unskilled jobs, on the: (i) nature and frequency of individual interaction with the allowance payment system, and (ii) over and underpayment of allowances to recipients.

The following is a submission into the inquiry into 'the adequacy of the allowance payment system for job seekers 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.' for the Department of Families, Housing, Community Services, and Indigenous Affairs. The submission relates to the adequacy of the payment system for job seekers only and support into work and the impact of the changing nature of the labour market.

Summary

Unemployment occurs systematically after a slowdown in economic activity and in industries that are contracting. This unemployment is not due to employee error which is an economic justification for work search and welfare payments to unemployed persons. Unemployment also occurs due to a mismatch of abilities and employee error. The Commonwealth of Australia pays persons who become involuntarily unemployed to support living conditions and enable work search during unemployment. Not all unemployed are eligible nor apply. This supporting payment is below the Henderson Poverty Line. Insuring for unemployment and redundancy is low cost.

This submission outlines private insurance payments and a combined of the Newstart and insurance payment so that total payments lift to the Henderson Poverty Line. This is at a small cost to the employee and less to no cost to the government. For the first – full insurance – payments for the Newstart allowance end for people unemployed for a duration of up to six months. For each, insurance is tax deductible – a cost to the government. These two payments are 35 per cent of average weekly full-time earnings and less than the high insurance payments, for which evidence is found overseas, that reduce incentive to work. Standard of living and work search are the reason for combined payments. Increasing the use of private insurance is outlined.

Unemployed and changing hours of work

Unemployed typically rise following a slowdown in economic activity and in contracting industries. The seasonal nature of agricultural and work affected by weather and events results in seasonal unemployment. Person also become unemployed in a mismatch of skills and due to error. The current unemployment rate is 5.2 per cent, which is low. As the population rises, the number of

unemployed increase. The percentage of persons seeking more working hours is higher and part-time employment is a rising percentage of positions – the ratio of full-time employed to part-time employed fell from 70 per cent to 68 per cent over ten years to 2012. More females than males are employed part-time. There may or may not be a social reason for this difference. This submission does not explore the reasons for the rise in part-time employed.

Commonwealth unemployment payments

Newstart payments are paid to involuntary unemployed persons between 21 years and 65 years who pass an assets test. The limit for liquid assets is \$3,000 for each person. The payment for a single person is \$489.70 per fortnight that is equivalent to \$12,732 per year. This payment is below the income necessary to meet the Henderson Poverty Line for income after tax, and for income after tax and housing costs (see Table 1). It is 18.2 per cent of average weekly ordinary full-time earnings.

Table 1

Newstart payments below the Henderson Poverty Line			
	Newstart per week	Henderson poverty line - income after tax and housing costs per week	Henderson poverty line - income after tax, before housing per week
Single	\$244.85	\$316.55	\$470.36
Single plus child(ren) - two children for Henderson Poverty Line	\$264.90	\$546.61	\$730.90

Source – Statistical Paper No. 10, *Income support customers: a statistical overview 2011*, Australian Government Department of Families, Housing, Community Services and Indigenous Affairs, and Melbourne Institute of Economic and Social Research – Labour Economic and Social Policy

ordinary full- time earnings. The youth allowance for unemployed young persons is \$201.35 per week for youth living away from home.

Persons receiving Newstart payments at June 2011 were 527,480; 37.3 per cent received payments for the short-term and the remainder for over a year (see Table 2). Persons unemployed at June 2011 were 601,100 – payments from Newstart are received by 87.8 per cent of unemployed. The average duration of Newstart payments for short-term recipients is 21 weeks. The most common duration is 3 to 6 months. Over 21 weeks, or 4.8 months, for short term recipients, a single recipient receives \$5,141.85 in total. For those unemployed and receiving the payment for over a year, the average duration of receipt is 267.6 weeks, or 5.1 years, and the median duration is 156 weeks, or 3 years.

Table 2

Number and duration of receipts for Newstart recipients			
	# Newstart recipients June 2012	Average duration of receipt – weeks	Median duration of receipt – weeks
Total recipients	580,807	175.4	88
Short term recipients	229,330	21	18
Long term recipients	351,477	267.6	156

Source – Statistical Paper No. 10, *Income support customers: a statistical overview 2011*, Australian Government Department of Families, Housing, Community Services and Indigenous Affairs. Labour Market and Related Payments, Department of Human Services, June 2012

Payments are below the Henderson Poverty Line. To lift the single person allowance to the Henderson Poverty Line income after tax and before housing, the allowance rises by 92.1 per cent to \$470.36 per week, equivalent to \$24,458 per year, and more for recipients with children.

Unemployment insurance low cost

Combining Newstart payments with insurance for unemployment and redundancy is a public and private response to protecting standards of living during unemployment. This solution to providing better income support during unemployment has no cost to the Commonwealth, except for the tax deductions for insurance. For employees, private unemployment and redundancy insurance is low cost and tax deductible. Payments are usually restricted to four to six months. This combination suits the most common short term recipient. Examples of current insurance premiums and payments are:

- \$5.84 per week payment by the employee for a \$1,000 per month payment after involuntary unemployment or redundancy or illness – less than 1 per cent of the minimum wage. For a person earning the minimum wage to earning \$37,000, the after tax cost of the premium is \$4.73 per week – 0.8 per cent of the minimum wage. For a person earning average weekly earnings, the after tax cost of the premium is \$3.94 per week.
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- \$5.34 per week payment by the employee for \$2,000 per month payments. Cover includes accidental death and funeral costs. Payments are allowable for 6 months.¹ Another estimate is \$11 per week payment, or 1.8 per cent of the minimum wage, for \$2,000 per month when unemployed.¹¹
- \$15.54 per week (approximate) by the employee – a single parent with one or two children – for \$3,000 per month. Payments are 2.6 per cent of the minimum wage.

Premiums are low cost. Private insurance and Newstart payment protects living standards for people who become unemployed or their job becomes redundant for

up to six months. Adding payments from the insurer to the Newstart payment lifts income to the Henderson Poverty Line. A single person receives \$475.62 per week, that is equivalent to \$24,732 per year. This is equal to the Henderson Poverty Line (see Table 3). It is also 78 per cent of the minimum wage and slightly below the Henry Tax review recommendations for tax-free income. Insurance for \$2,000 per month with the Newstart payment is above the Henderson Poverty Line for single persons and equal to the Henderson Poverty Line for persons with child(ren).

Table 3

Payments from insurer and Newstart lift income over the poverty line					
	Newstart per week	Newstart plus unemployment insurance \$1,000/month	Percent of minimum wage - \$606.20/wk and AWOFE	Newstart plus unemployment insurance \$2,000 per month	Henderson poverty line- income after tax, excluding housing per week
Single	\$244.85	\$475.62	78%/33%	\$706.38	\$470.36
Single + child (ren)	\$264.90	\$495.67	81%/35%	\$726.44	\$7309.90 (2 children)

AWOFE – Average weekly ordinary full-time earnings Source – Statistical Paper No. 10, Income support customers: a statistical overview 2011, Australian Government Department of Families, Housing, Community Services and Indigenous Affairs, and Melbourne Institute of Economic and Social Research – Labour Economic and Social Policy, Australian Bureau of Statistics

Adequate for most short-term unemployed

Combining the lower insurance with the Newstart payment for singles and the higher insurance with the Newstart payment for people with children is a complete solution to standard of living and work search support for 64 per cent of short-term recipients. The most common period of unemployment for short-term

recipients is 3 to 6 months and 64 per cent of short-term recipients and 23.9 per cent of all recipients received payments for up to six months at June 2011.

For the benefits to be received by the unemployed, the payments would be allowable income for the Newstart allowance. For short-term recipients, Newstart allowance does not need to increase for those taking insurance at this low cost to ensure adequate living standards. The Commonwealth shares a small percentage of the payment for insurance through the payment being tax deductible.

Payments for \$2,038 per month for the single unemployed person, lift income to the Henderson Poverty Line. Payments of \$3,167 per month for the single person with one or two children lift income to the Henderson Poverty Line.

Supportive to economy

A wider economic benefit of combining public and private unemployment payments is the increase baseline income across households. This automatically stabilises economic growth to a mild extent by enabling a higher level of expenditure and less use of savings, when unemployment rises after a slowing in growth or recession.ⁱⁱⁱ At an unemployment rate of 5.2 per cent, \$2,000 per month instead of \$1,061 for Newstart for a single person, this is \$3.1 million more over six months and at 7 per cent is \$4.2 million more over six months.

Lifting standard of living when unemployed

Insuring for unemployment and redundancy for adequate standard of living and work search receipts can be increased by:

- the Commonwealth of Australia levying unemployment insurance for employees, similar to the medicare levy. The policy and funds is organised

and managed by a private insurer. The cost of private insurers to provide insurance for up to six months is low and reflected in low weekly payments for insurance. Payments of \$11 per week lift receipts for a single person to the Henderson Poverty Line. Payments of \$15.54 per week lift receipts for a single parent with child(ren) to the Henderson Poverty Line.

- policy changes to allow low unemployment and redundancy insurance payments that pay \$1,000 per month alongside the Newstart allowance,
- the Commonwealth of Australia encouraging employees to take out private unemployment and redundancy insurance,
- trade unions encouraging their members to take voluntary unemployment and redundancy insurance, and
- the Commonwealth of Australia requiring firms to pay unemployment insurance for their employees. The funds are optimally allocated, according to Blanchard, O. and Tirole, J., when firms voluntarily or involuntarily pay severance payments, that may include employer-funded employment insurance.^{iv} This makes employing and unemploying, costs to the firm.

The allocation of employees is also optimal, according to these authors, when layoff taxes, or a combination of payroll taxes and layoff taxes, pay for unemployment benefits in a public unemployment payment system. This submission does not expand on this approach.

Insurance and Newstart payments outside range effecting re-employment

Combined Newstart and insurance payments are outside the range of payments that effect the incentive to return to work. Effects of unemployment insurance on working and the natural rate of unemployment are quantified in research for high unemployment insurance payments that are far above the Newstart payment. increases.^v For one study, the average insurance payout considered is 61.5 per cent of the average pre-unemployment income after tax . For others, the payment is a high percent of around 75 per cent of the pre-unemployment salary.^{vi} The combined Newstart and insurance payment is 35 per cent of average ordinary full-time earnings. The results of these studies are not relevant for the Newstart allowance for all employees nor for the combined Newstart allowance and insurance payments for people earning average ordinary full-time earnings. Moreover, the degree of effect on employment differs across studies. Effects on returning to work are found to be stronger (more negative) for re-employment for older persons but weaker (less negative) for less qualified persons.^{vii} There may be an effect of insurance and Newstart payments for those returning to work on the minimum wage. The combined Newstart and insurance payment is 78 per cent of the minimum wage. In the terms of reference, jobs requiring unskilled persons are noted as declining as a percentage of jobs. This group has declined and is a declining percentage of persons working. A person earning the minimum wage or a low income may take this amount of insurance or more.

The allocation of employees is also optimal according to these authors when
a combination of payroll taxes and payroll taxes pay for
unemployment benefits in a public unemployment payment system. The substitution
does not exceed on this approach.

Conclusion

Newstart payments for all recipients are below the Henderson Poverty Line and less than one-fifth of average weekly ordinary full-time earnings. The rate of unemployment is low but as the population grows the number of unemployed rise. The increase in cost to the Commonwealth of increasing the Newstart payment to be in line with the Henderson Poverty Line is 92 per cent for single people. Private insurance is low-cost and provides effective cover at the Henderson Poverty Line when payments are \$2,000 per month for the single person and \$3,000 for the single person with child(ren) – if payments for the latter are achievable. Lower private insurance also provides effective cover at the Henderson Poverty Line when combined with Newstart allowance for the single person and single parents with two children. Levying unemployment insurance for employees, similar to the medicare levy, and the Commonwealth, or employer, insuring with a private insurer, provides payments for up to six months that are at the Henderson Poverty Line. This covers 64 per cent of short-term recipients. Private insurance can be verbally encouraged. Full insurance or part insurance and public payments reduces the cost to the Commonwealth of increasing the Newstart payment. Insurance ends the cost of Newstart payments to all recipients for the first 6 months, excluding people on low income, and ends the cost of managing Newstart allowance for these people. This lifts the standard of living of those who are involuntarily unemployed.

