SENATE COMMUNITY AFFAIRS LEGISLATION COMMITTEE

Consideration of Legislation Referred to the Committee

SOCIAL SECURITY AMENDMENT (DISPOSAL OF ASSETS) BILL 1999

NOVEMBER 1999

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SOCIAL SECURITY AMENDMENT (DISPOSAL OF ASSETS)
BILL 1999

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REPORT

SOCIAL SECURITY AMENDMENT (DISPOSAL OF ASSETS) BILL 1999

1. THE INQUIRY

1.1 The Social Security Amendment (Disposal of Assets) Bill 1999 (the Bill) was introduced into the House of Representatives on 30 June 1999 and into the Senate on 24 August 1999. On 13 October 1999, the Senate, on the recommendation of the Selection of Bills Committee (Report No. 17 of 1999), referred the Bill to the Committee for report by 22 November 1999.

1.2 The Committee considered the Bill at a public hearing on 21 October 1999. Details of the public hearing are referred to in Appendix 2. The Committee received six submissions relating to the Bill and these are listed at Appendix 1.

2. THE BILL

2.1 The Bill, foreshadowed in the 1999 Budget, introduces changes to the provisions which prescribe how much a person can dispose of by way of gifts and still remain qualified for income support payments.

2.2 The Bill provides for a reduction in the 'free area' that a person or a couple may gift – from $10 000 per annum to $5 000 per annum – before that gift begins to impact on the level of assistance provided under the *Social Security Act 1991*.[1] Any amount given away in excess of the $5 000 annual free area would, consistent with the current gifting rules, be counted as an asset for social security purposes (a deprived asset) for five years from the date of the gift, and would be subject to the income test deeming rules.[2]

2.3 The Minister in the Second Reading Speech stated that:

> Th[e] annual $10,000 "free area" is anomalous, in that it is greater than the maximum single pension rate – some $9,400 per annum. The result is that under the current rules an income support recipient can give away more than that person is entitled to receive by way of assistance…this loophole has become a favourite tool for many financial planners who exploit it to increase the income support entitlement of their customers.[3]

2.4 The reduction in the annual 'free area' will have effect from 1 July 1999. However, provision is made in the Bill to ensure that any income support paid on the basis of the existing disposal rules before the Royal Assent to the Bill is protected from being recovered from the income support recipient insofar as these amendments are concerned. The Bill will

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1 Explanatory Memorandum, p.i. See also Social Security Amendment (Disposal of Assets) Bill 1999, *Bills Digest No.25*, 1999-2000.

2 Submission No.2, p.3 (FaCS).

3 Minister's Second Reading Speech.

also change the basis for the calculation of the concession relating to gifting from 'pension year' to the more widely understood 'financial year'.[4]

3. ISSUES

Effect on pensioners

3.1 Some organisations claimed that the proposed reduction in the annual gifting 'free area' was harsh and would remove the flexibility in the current rules for many older persons to assist family members in times of financial crises.[5]

3.2 In response, the Department of Family and Community Services (FaCS) stated that the existing gifting free area of $10 000 per annum is very generous and at odds with the underlying rationale of a needs based social security system whereby people are expected to use their own income and assets before relying on the community for income support. The Department noted that an indication of the generosity of the current system is the fact that the amount that a person can currently give away before impacting on their pension entitlements is more than the maximum single rate of pension (that is, $9 500 per annum).[6] This aspect of the current system was also commented upon by the Association of Independent Retirees.[7]

3.3 The Department emphasised that the Government is not seeking to discourage gifting and noted that a $5 000 gifting free area would still provide the opportunity for a pensioner to provide substantial assistance to family members ($100 000 over 20 years).[8]

3.4 FaCS also stated that only a small number of customers will be affected by the proposed measure (with some 3 600 FaCS recipients estimated to be affected in 1999-2000). FaCS indicated that of this number, some 3 100 age pensioners and 300 disability support pensioners would be affected in 1999-2000 – which represents only 0.2 per cent of age pensioners and 0.05 per cent of disability support pensioners.[9] The Department also noted that the income and asset test free area means that people with modest incomes, or with less than sizeable asset holdings, are not likely to be affected by the proposed change.[10]

Maximising pension entitlements

3.5 FaCS indicated that there was evidence of people seeking to maximise their pension through the gifting provisions. The Department cited Department of Veterans' Affairs (DVA) figures on gifts by service pensioners below the current gifting free area. DVA data indicate that for the five year period from 1994 to 1998, 42 per cent of all DVA pensioners who advised they had made gifts of any value had gifted exactly $10 000 in an individual year. This compares with 12 per cent who had made gifts in excess of $10 000 in an individual

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4 The current provisions operate on the basis of a 'pension year', being the anniversary of the day the income support recipient commenced receiving payment. See Explanatory Memorandum, p.i.

5 *Committee Hansard,* 21.10.99, pp.1-2 (NWRN), p.7 (COTA); p.10 (APSF). See also Submission No.1, pp.1-3 (NWRN); Submission No.4, p.1(COTA); Submission No.3, pp.2-3 (APSF).

6 Submission No.4, p.4 (FaCS).

7 Submission No.5, p.2 (AIR).

8 Submission No.2, pp.4,7 (FaCS).

9 Submission No.2, p.7 (FaCS). See also *Committee Hansard,* 21.10.99, pp.12-13 (FaCS).

10 Submission No.2, p.7 (FaCS).

year. The Department stated that this data ‘clearly illustrates that many individuals are setting their gifting level to fully utilise the current $10,000 gifting free area’.[11] FaCS noted that given that the DVA service pensioner population is similar in characteristics to the FaCS age pensioner population it is reasonable to assume that the gifting patterns indicated in the DVA data would be similar for the FaCS pensioner group.[12]

3.6 In addition, FaCS stated that the financial planning industry is promoting ‘gifting strategies’ as part of pension maximisation schemes.[13] Some groups, however, questioned the extent of the practice.[14] The Department responded that the practice is ‘actively encouraged by many financial advisers, including advisers in the mainstream of the profession’.[15] The Department noted that the training and marketing material for financial planners and accountants commonly refers to this method and it is accepted in many quarters as ‘normal’ retirement planning practice.[16] FaCS noted that these practices involve a significant cost to the social security budget and undermine the integrity of the social security means test as a means of targeting assistance to those most in need.[17]

Retrospectivity

3.7 Some groups raised issues relating to the alleged ‘retrospective’ nature of the proposed legislation.[18]

3.8 In response, the Department stated that provision is made in the Bill to ensure that no income support payment would be affected by the new rules until the legislation is passed by the Parliament and has received Royal Assent. FaCS also noted that the Senate Scrutiny of Bills Committee ‘has accepted in its 13th Report of 1999 that the Bill does not have retrospective effect’.[19] The existing gifting rules will continue to operate in relation to any gifts made before 1 July 1999, with the proposed changes to apply to all gifts made after 1 July 1999.

4. RECOMMENDATION

4.1 The Committee reports to the Senate that it has considered the Social Security Amendment (Disposal of Assets) Bill 1999 and **recommends** that the Bill proceed.

Senator Sue Knowles, Chairman

November 1999

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11 Submission No.2, p.4 (FaCS). See also *Committee Hansard,* 21.10.99, p.13 (FaCS).

12 Submission No.2, p.4 (FaCS).

13 Submission No.2, p.5 (FaCS). See also Submission No.5, p.2 (AIR).

14 Submission No.3, p.1 (APSF); Submission No.4, p.1 (COTA); Submission No.6, p.1 (NSA).

15 Submission No.2, p.6 (FaCS).

16 Submission No.2, pp.10-11(FaCS). See also *Committee Hansard,* 21.10.99, p.13 (FaCS).

17 Submission No.2, p.6 (FaCS).

18 Submission No.1, pp.3-4 (NWRN); Submission No.3, p.2 (APSF). See also *Committee Hansard,* 21.10.99, p.2 (NWRN).

19 Submission No.2, p.3 (FaCS). See also *Committee Hansard,* 21.10.99, p.16 (FaCS).

MINORITY REPORT

AUSTRALIAN LABOR PARTY

SOCIAL SECURITY AMENDMENT (DISPOSAL OF ASSETS) BILL 1999

THE INQUIRY

THE BILL

The Bill would reduce from $10,000 to $5,000 the 'free area' for gifting of assets. The free area is the maximum value of the assets that may given away each year without affecting pension entitlements. Any gifts in excess of the free area are subject to the assets test, or the income test, for five years after the gift. Under the Social Security Act, the Department applies whichever test would result in the greater nominal gain, that is, whichever would reduce the pension by the greatest amount.

> The current regulations allow pensioners to dispose of, or give away up to $10,000 per annum without any effect on their pension entitlement. Assets beyond this threshold which are disposed of, have income assessed at the deeming rate, or in cases where the asset was income producing, at the actual rate if it is higher than the deeming rate.[1]

The Bill would apply this change equally to single pensioners and to couples. The Bill is expected to reduce the entitlements of some 3,400 aged pensioners, and 200 disability pensioners, with savings to the Commonwealth rising to an estimated $4.405 million by 2002-03.

Error in 'transitional period' section (127)

The Government intends that the changes to the gifting rules made by the Bill would apply to pensioners who between 1 July 1999 and Royal Assent made gifts in excess of $5,000 and $9,999. Any reduction of pension payments is supposed to apply after Royal Assent. In other words, the Department would not regard as over-payments the pension paid prior to Royal Assent.

The Opposition wishes to draw the Parliament's attention to a drafting error in the Bill, which would appear to render inoperative that section (127) which is supposed to provide for this transitional period. Section 127 refers not to the *Social Security Amendment (Disposal of Assets) Bill 1999*, but to a non-existent Bill, the '*Budget Measures 1999 Legislation Amendment Bill (Social Security - Disposal of Assets) Act 1999*'.[2]

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[1] John Barber, Gillian Moon and Sharon Doolan, *Targeting for Equity: Final Report of the Strategic Review of the Pensions' Income and Assets Tests*, Ageing Agendas, 1994, 8.4.

[2] Bill Digest, p. 5. Verbal advice from Clerk Assistant (Procedure), 19.11.99

BACKGROUND

The free area has changed in the last ten years. Prior to 1991, it was $4,000 for couples and $2,000 for singles. In 1991 the Keating government changed the area to $10,000 for both couples and singles. This was justified by the government as both a reasonable improvement to pensioners' benefits, and a simplification of the rules.

GOVERNMENT'S RATIONALE FOR THE BILL

The Government has justified the Bill on the grounds that:

- it is inequitable for pensioners to be able to gift without penalty more than the annual maximum single pension;
- the current free area rules are at odds with the principles underlying a needs-based social security system;
- only a small number of pensioners will be adversely affected; and that
- abuse of the $10,000 free area is widely promoted by financial advisers as a pension maximisation technique.

The Government insists that its policy is based on the assumption that some 'free area gifting' (that is, gifting without loss of pension entitlements) is reasonable. [3]

LABOR'S POSITION

The amount not the principle is in dispute

There has been a political consensus in Australia that some amount of gifting by pensioners is a legitimate practice.

Essentially the Opposition is not convinced that the Government has made the case for the the Bill's basic premise: that the current free area of $10,000 is too generous to pensioners. The Opposition was more impressed by evidence from senior's groups that a $5,000 free area would impose an excessive penalty on gifts of assets to a family member, and that $10,000 remains the more appropriate level.

The government's main justification for the Bill appears to be that it is inherently inequitable for a pensioner to be able to give away without loss of pension more than the annual rate of the maximum single pension (approximately $9,400).[4] The Opposition has a number of objections to this argument.

Firstly, it appears to be a recently discovered and hastily prepared rationale for what would otherwise be seen as an unadorned savings measure. No evidence has been provided by the Government that the maximum single pension has ever been used as an upper limit for the

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[3] FaCS submission, p. 4.

[4] Minister's Second Reading Speech, House of Representatives Hansard, 30.6.99, p. 7865.

free area. The Government has simply asserted this principle, which is generally rejected by the groups representing retirees.

In fact there have been a number of statements from the Government implying that under the current arrangements individual pensioners are able to give away without penalty more than they receive from the Government in pension payments. For example, the chair of the Committee asked one witness,

> Do you think it is fair, in all honesty, to be able to say to someone, 'You can give away more money than the other taxpayers are going to give you in pension in a year.'[5]

One answer to this rhetorical question is that the perceived inequity could never occur, as according to the Department no one in receipt of the full pension of $9,400 could have sufficient assets to be subject to the assets and income tests:

> A maximum rate pensioner who gifts cash or other financial assets cannot be affected by the proposed change to the gifting free area regardless of the value of the gift. This is because assets owned by maximum rate pensioners and assessed income (including deemed income on financial assets) must be below the existing asset and income test free areas.[6]

Cost of living: $10,000 remains an appropriate free area

The Opposition was impressed by evidence submitted to the Committe that a free area of $10,000 is more appropriate than $5,000, given the cost of living and the demands placed on families. For example, Welfare Rights Network stated:

> Our main concern, however, is that the proposal is merely a mean savings measure. In our experience, the $10,000 for gifting is adequate. To reduce it to $5,000 seems to be harsh and unnecessary.[7]

During the public hearing, the Opposition pointed out that the decision to set the free area at $10,000 was made eight years ago and asked the Department whether cost of living increases since then warranted a reassessment of the level.[8] In fact, based on CPI increases since then, $11,600 is now needed to purchase the goods and services which could then have be bought for $10,000.[9] In terms of the cost of living, the case for the free area being set at $10,000 is, if anything, stronger than in 1991.

Legitimate uses of gifting

The Opposition believes that the Bill does not adequately recognize that gifting of assets by part-pensioners is generally legitimate and socially beneficial. Having heard the evidence put before the Commitee the Opposition considers that objections to the Bill by senior's

[5] Committee Hansard, p. 2.

[6] FaCS submission, p. 7.

[7] Committee Hansard, p. 1.

[8] Committee Hansard, p. 14.

[9] Parliamentary Library. Based on comparison of CPI for 1991 calendar year 1999 September quarter.

organisations are reasonable and based on understanding of how the gifting rules are actually used by most reitrees. Labor believs that the Bill would penalise attempts by older Australians to assist younger or less fortunate members of their own families. This aspiration was noted by the 1994 *Strategic Review of the Pension's Income and Assets Test*.

> Many pensioners with few assets have indicated that at points where they have realised those assets, usually on the sale of the family home, they would like to be able to assist their children.[10]

The point is also made in submissions to the Bill inquiry. COTA deplored the notion that "where somebody is in a family crisis [that] there is a penalty on the older person for assisting the other family member at that time..."[11] In their written submissions, and evidence before the Committee, representative organizations argued that pensioners generally gifted assets to meet family need rather than to maximise pensions. (In fact, the value of the gift is always much greater than the pension gain.)

> Throughout Australia, COTA is aware of the increasing pressures placed on older Australians as a result of family breakdown and other problems such as unemployment. Many older people are called upon to assist family members in times of crisis and financial need. These include assisting with the deposit on a home when there is a marriage separation; family illness; onset of disability; unemployment where the family member has commitments...Limiting the annual gifting to $5,000 has been seen as mean spirited and in contrast to the willingness of parents to assist other family members when misfortune strikes.[12]

Other seniors' organizations agreeds that it was common for gifts to be made to assist younger family members with major purchases, such as a mortgage deposit, or education fees. The AP & SF testified:

> We have found that most of our older people who deem over $10,000 to families to either put a deposit on a home or educate children.[13]

Social benefit of retirees helping younger or less fortunate relatives

In many cases gifting assets helps the younger family members concerned, but is also of wider social benefit. The inquiry was told that assistance from older relatives could prevent younger family members from having to use publicly-funded programs.

> For instance an Aged Pensioner, Ed, may give his frail widowed sister, Margaret, an amount of $20,000 to enable her to pay for a place in a nursing home, in the area that she has lived [in] all her life. Margaret does not want to sell her house, because her house, because her sole parent daughter and grandchildren are currently living in the house with her. If she sells the house to purchase a place in the nursing home, he daughter would probably have to rely on public housing. The only solution for this family is for Ed to give her the money. The current

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[10] *Targeting for Equity*, 8.4.

[11] Committee Hansard, p. 7.

[12] Sub 4, COTA, p. 1.

[13] Committee Hansard, p. 10.

> rules would mean that Ed's Age Pension would be affected for the following five years by the $10,000 he has 'given away'. *No regard is given for the amount of public money that is saved by the sole parent and her daughter not having to rely on public housing* in an area some distance from her mother's nursing home.[14] [emphasis added]

Asset gifts can also be of social value even when the public benefit is less immediate. Pensioners who help younger relatives with mortgage deposits are assisting them to enjoy a better standard of living during their working lives, and in retirement. In fact, home ownership contributes to the self-reliance in retirement which is one of the stated principles informing this Bill. Unfortunately there is evidence that first home buyers are finding it more difficult to purchase a first property.

The Senate Community Affairs Commitee's inquiry into the GST received detailed evidence about the likely effects of the GST on first home buyers.[15] Evidence on this issue was submitted by housing policy research organisations such as the Urban Development Insitute of Australia, and the major industry bodies: the Master Builders' Association, and the Housing Industry Association. The HIA concluded that:

> ...the GST and other tax changes on the residential construction industry will increase the cost of new house prices by 5 per cent in the long term and 8 per cent in the short to medium term...HIA stated that the FHOS [First Home Owner's Subsidy Scheme] will only be available to about 15 per cent of new homebuyers.[16]

The UDIA was particularly concerned that the GST would be levied directly on newly-built homes in the outer suburbs.

> New homes tend to be located on the fringe of our major cities. Young families have tended to move new suburbs because of the lack of affordability in established areas. These new residential suburbs are often the most affordable in our major cities. Unfortunately the GST only applies to new homes. As a result new and emerging suburbs (generally more affordable) will be subject to a tax that established suburbs will not.[17]

The inquiry concluded on the basis of such evidence that "...the new tax arrangements will adversely affect housing affordability."[18]

There is clear evidence that young families on low-middle incomes already experience difficulty in buying a first home, and that this problem is likely to be intensified by the introduciton of the GST. Given these conditions, the Opposition is greatly concerned that the Bill would penalise attempts by older relatives to help first home buyers secure a mortgage deposit.

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[14] NWRN Sub, (1), p. 2.

[15] See Lucky Country, 4.69 -4.85.

[16] Lucky Country, 4.79.

[17] Submission no. 509, p. 3, UDIA, Lucky Country, 4.81.

[18] Lucky Country, 4.81. (p. 96).

Family self-reliance

Labor accepts the evidence given by senior's groups that the Bill would discourage retirees from helping other family members, despite the government's insistence that families should take a greater role in supporting themselves, and particularly their younger members. The Bill would be particularly harsh on modest income families who are supporting young people who are studying or unemployed.

Since the introduction of Youth Allowance in 1998, families are now generally required to support unemployed young people to the age of 21 and students to the age of 25. Youth Allowance has effectively shifted the burden of youth unemployment onto families. At 22.9%, the youth unemployment rate is more than three times the national average for all workers. In such an environment, assistance provided through the generosity of extended family is one way of relieving the financial impact, the introduction of Youth Allowance has had.

The Government has reduced public assistance for families, and with this Bill it is penalising social assistance within families.

Insufficient flexibility

The Opposition shares the concerns expressed by witnesses about the Bill's inflexibility. It fails to recognize that pensioners whose family circumstances compel them to make a substantial gift in a particular year may not necessarily engage in what the Department calls 'serial gifting' over several years.[19] Other options could have been taken to accommodate legatee gifting while addressing any problem of 'serial gifting' for pension maximisation. The *Strategic Review of the Pension's Income and Assets Tests* (1994) canvassed a number of options for reconciling flexibility and revenue protection.

> *Questions of Balance* present an option for cumulative gifting to apply. It was suggested that pensioners be allowed to build up a credit so that at particular times, eg at retirement and/or on the sale of the family home, they could give away greater amounts than is presently allowed.[20]

Witnesses supported the need for a more flexible approach.

> AP&SF does not consider that believe that older people are acting 'irresonsibly by wishing to help their families facing difficult circumstances - quite the contrary. AP&SF notes that the gifting provisions were the subject of some discussion during the 1994 *Strategic Review of the Pension's Income and Assets Tests.* While our own organisation viewed the current rules as satisfactory, we also called for more greater flexibility in the provisions for people facing exceptional circumstances. It is extremely dissapointing to AP&SF that this proposal was not further investigated. We urge the Commitee to consider ways of addressing the issue.[21]

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[19] Committee Hansard, p. 15.

[20] Targeting for Equity, 8.4; and see *Questions of Balance*, Ageing Agendas, July 1994, 10J.

[21] Sub 3, AP & SF, p. 3.

The Opposition is of the view that the government should give serious consideration to innovative proposals for making the gifting rules more flexible while retaing the principles of a needs-based social security system.

Government has not established that the Bill is a reasonable response to 'serial gifting'

Much of the Government's rhetoric has concerned the practice of financial advisers encouraging retirees to maximise their pensions by repeatedly gifting assets with the main purpose of maximising their pension. The AP & SF argued, however, that:

> If, as Government claims, the behaviour of the financial planning industry is causing these problems, the difficulty should be attacked at its root, rather than by penalising pensioners, and taking away legitimate flexibility within the current rules to assist needy family members.[22]

The Opposition accpets that pension maximisation through gifting does occur, but in the course of the inquiry the Government has failed to convince us that:

- the practice is so widespread that the free area should be reduced to $5,000 in order to make such pension maximisation more difficult to achieve;
- the Bill would in fact prevent the kind of schemes that the Government has rightly criticised;
- pensioners who legitimately gift between $5,000 and $9,999 should be penalised.

Again, there is a gap between the government's insistence that the Bill would close down a major area of unethical pension maximisation, and its admittance that:

- many pensioners gift legitimately;
- the Bill would only affect 0.198% of aged pensioners and 0.034% of disability pensioner;
- the Bill would only save the Government about 0.23% of its pensioner budget for 1999.

CONCLUSION

Labor was impressed by the evidence of seniors' groups that the proposed reduction of the free area was mean-spirited. We are not satisfied that the government has made the case for the Bill. If the Goverment objects to the actions of financial planners, it should address those concerns in the appropriate area, rather than penalising the legitimate use of gifting by part-pensioners. The Opposition would support any reasonable measure to address the abuse of gifting, but we are not convinced that this Bill deals with the problem in an appropriate way. On balance the Opposition was more convinced by the evidence of community groups that the Bill was unfair and misconceived than by the Government's contentions that it was equitable.

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[22] Sub 3, AP & SF, p. 1.

RECOMMENDATION

It is recommended that the Bill should not be passed.

Senator Chris Evans
(ALP, Western Australia)

22 November 1999

APPENDIX 1

SUBMISSIONS RECEIVED BY THE COMMITTEE

1 National Welfare Rights Network
– Additional Information, dated 21 October 1999

2 Department of Family and Community Services
– Additional Information, dated 26 October 1999

3 Australian Pensioners' and Superannuants' Federation (AP&SF)

4 Council on the Ageing (Australia) (COTA)

5 Association of Independent Retirees, Inc.

6 National Seniors Association Limited

APPENDIX 2

PUBLIC HEARING

A public hearing was held on the Bill on 21 October 1999 in Senate Committee Room 1S2.

Committee Members in attendance

Senator Sue Knowles (Chairman)
Senator Kay Denman
Senator Chris Evans
Senator Brett Mason
Senator Tsebin Tchen

Witnesses

National Welfare Rights Network

Ms Jackie Finlay, Liaison Officer

Council on the Ageing

Mr Denys Correll, National Executive Director

Australian Pensioners' and Superannuants' Federation ***(via teleconference)***

Ms Yvonne Zardani, Representative

Department of Family and Community Services

Mr Evan Mann, Assistant Secretary, Seniors and Means Testing Branch
Mr Stuart Kennedy, Director, Retirement Policy Section
Mr John Jeffrey, Legal Services Branch