Adequacy of the Social Welfare System in providing Pre-Retirement Financial Security

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Agenda

- Background
    - Genesis
    - Industry Funds Forum
    - IFS Broking
- Purpose
    - Separately for Death and for Disability
    - Define Financial Adequacy – Pre-Retirement
    - Test the Social Welfare System
- Comparison – Method and Results

Introduction

- Pre Retirement Income – how important?
  - more important than post retirement income. eg.
    - a key determinant of post retirement income
    - financial Dependents

- Financial security pillars for disability and death
  - Social Welfare System
  - Insurance through Super, Employer, Union, Personal
  - Compensation schemes
  - Sick leave
  - Personal savings

Introduction

"The view of all the Social Security experts at the Centre is that no one could safely rely on the Social Security safety net as it currently exists. The levels of income support are at virtually subsistence levels and the legislation is subject to constant review and change by governments regardless of their political persuasion."

Welfare Rights Centre 2009

Adequacy Definition

The amount that ensures the long term living standards of the person and their dependents are similar before and after the death or disability of the person

- The sum of:
  - Income required to maintain living expenses
  - Saving for retirement
  - Transition costs
  - Ongoing Care (disability)

Adequacy Definition

- Different to formula used by
  - superannuation fund Calculators
  - financial advice industry

- Emphasis on future expenditure needs, not specific expenditure items or current liabilities

- eg families with children
  - 4% of expenditure on school fees
  - 7% on of expenditure on interest payments for family home

Adequacy Definition

Principle	Death	Disability
1. Ongoing Living Expenses	No Dependents – Nil Dependents – $r_1\%$ x Household Income	$r_2\%$ x Household Income
2. Saving for Retirement	No Dependents – Nil With Dependents – 9% of 1.	12% of 1.
3. Transition Costs	$10,000	$50,000 over 5 years
4. Ongoing Care	N/A	Couple - $0 as healthy partner is carer and home duties Single - $50,000 p.a.

Adequacy Definition

- r% equates current household income with the income required to maintain household expenditure

- r% varies by
  - Household type
  - Income
  - Death/Disability

Social Welfare Benefits Death and Disability

- Extremely complex
  - more than 20 benefits, allowances and supplements
  - subject to varying eligibility, income and asset tests.

- Examples
  - Disability Support Pension and Supplement - long term disability
  - Sickness Allowance and NewStart Allowance - short term disability
  - Carers Payment, Parenting Payment, Family Tax Benefit A and B *,Large Family Supplement *; Youth Allowance *
  - Widow Allowance
  - Rent Assistance
  - Pharmaceutical Allowance; Remote Area Allowance; Mobility Allowance; Telephone Allowance; Utilities Allowance
  - Concession Card – inc. Pensioner Concession Card (PCC)
  - Health Care Card
  - Education Entry Payment *

* don't have to be 'disabled' to be eligible

Inadequacies of Welfare System

- If benefits financially adequate still major issues

  - Unknown and unknowable benefit;
    - Multitude of fringe benefits;
    - Benefit interactions;
    - Numerous means tests and their interactions;
    - Varying rules on what is income and what is an asset;
    - Restrictions and eligibility rules;

  - Indexation = CPI, not AWOTE;

  - Government changes benefits frequently;

  - Assessment and Payment Delays;

  - Disability – poor design for return to work

Comparison – Modelling Disability

- Comparison of current cashflows
  - Ignores variation over time CPI v AWOTE
  - Variables
    - level of disability;
    - age and number of children;
    - home ownership;
    - household type and income quintile;
    - post disability income;
    - net assets;
    - level and source of care

Comparison – Modelling Death

- Comparison of PV of future cashflows
  - PV allows for remarriage rates of widowed people, mortality, AWOTE and CPI
  - Variation over time is very significant
    - Annuity factor varies by age and gender
    - maximum of around 16 for females at 40
  - Variables
    - age and gender of survivor;
    - age and number of children;
    - home ownership;
    - household type and income quintile;
    - post death income; net assets

Modelling

SINGLE DISABILITY
WITH/WITHOUT CHILDREN
HOUSEHOLD INCOME

Pre – disability

SS	+
PY	+
IY	=
$PRE	

Post – disability

SS	↑	+
PY	↓	+
IY		=
$POST		

RATIO

$$\frac{\$POST}{\$ADEQUATE}$$

- Calculated for a point in time
- Does not include effect of AWOTE and CPI

Adequate

$PRE x RR	+	
EXTRAS	=	
$ADEQUATE		

Key
SS – Social Security
PY – Personal Income
IY – Investment Income

Extras include:
- Saving for retirement
- Transition costs
- Ongoing care (inc. Household duties)

Comparisons

- Results are preliminary and still being refined

- Quintile 1 can be ignored
  - Heterogeneous group of people on social welfare and small business taking/making low income

- Net asset distribution - only Quintile 5 has assets approaching the first Social Welfare cut-off shown
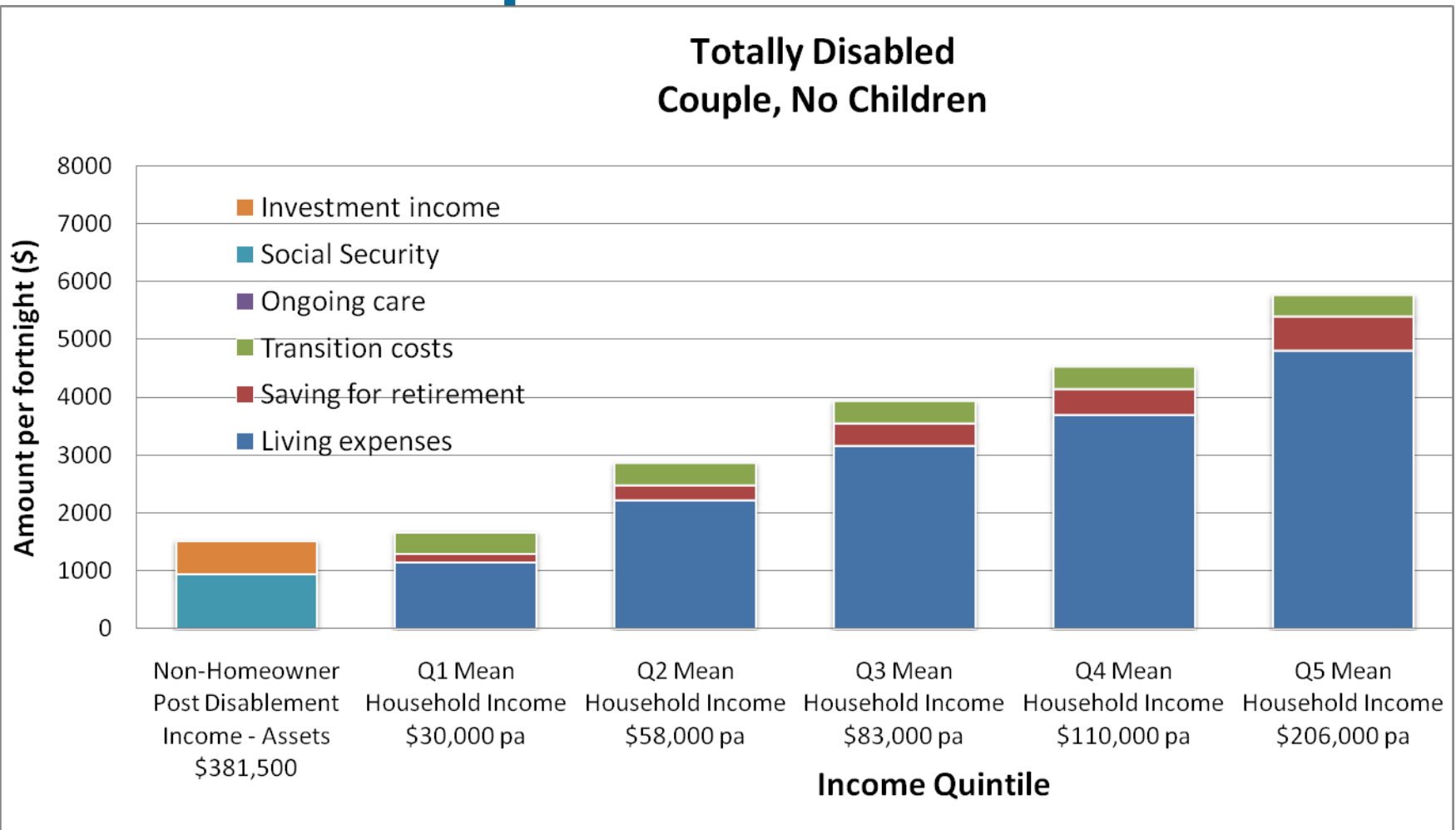
- Employees mainly in income quintiles 2,3,4
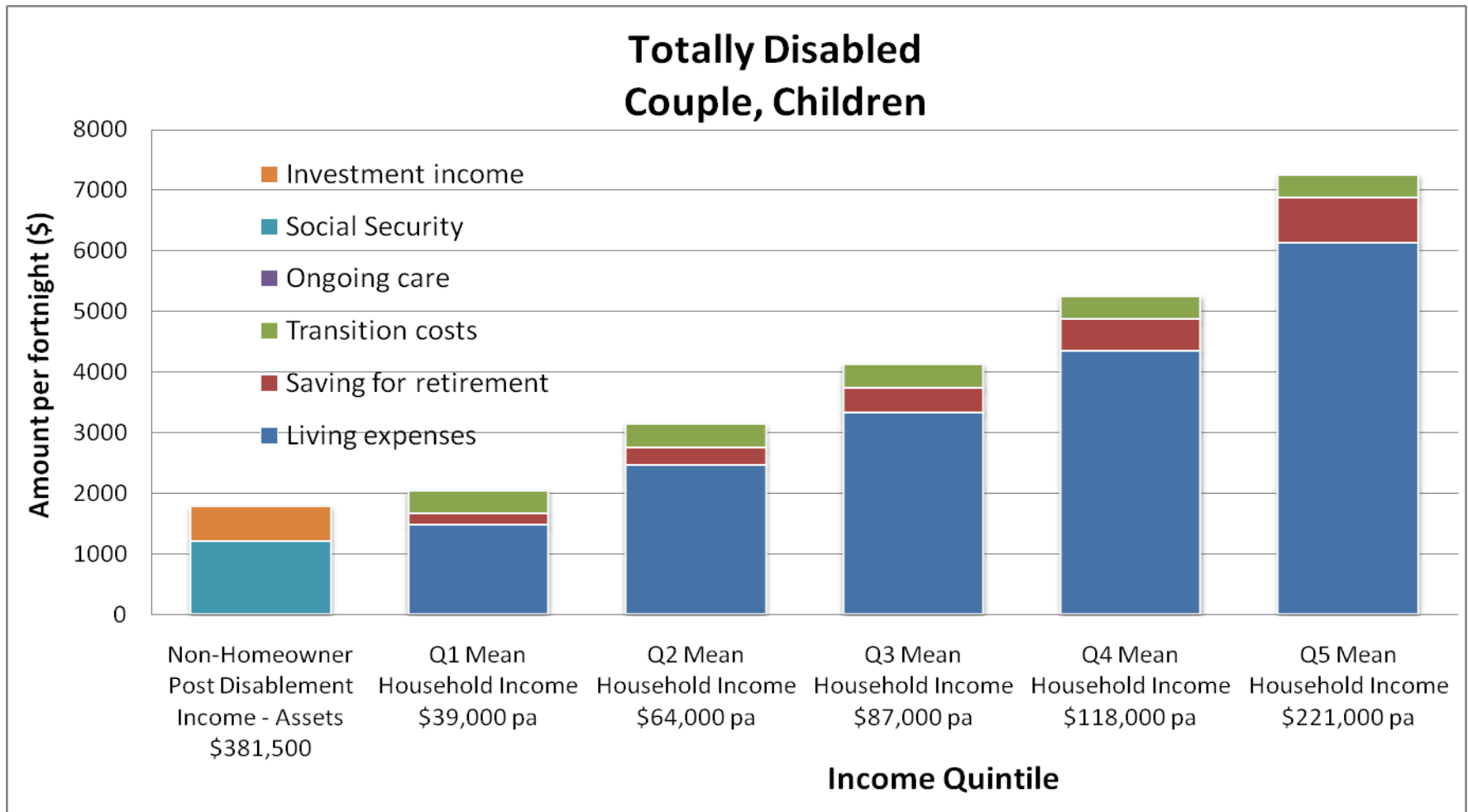
Comparison – Totally Disabled Single No Children
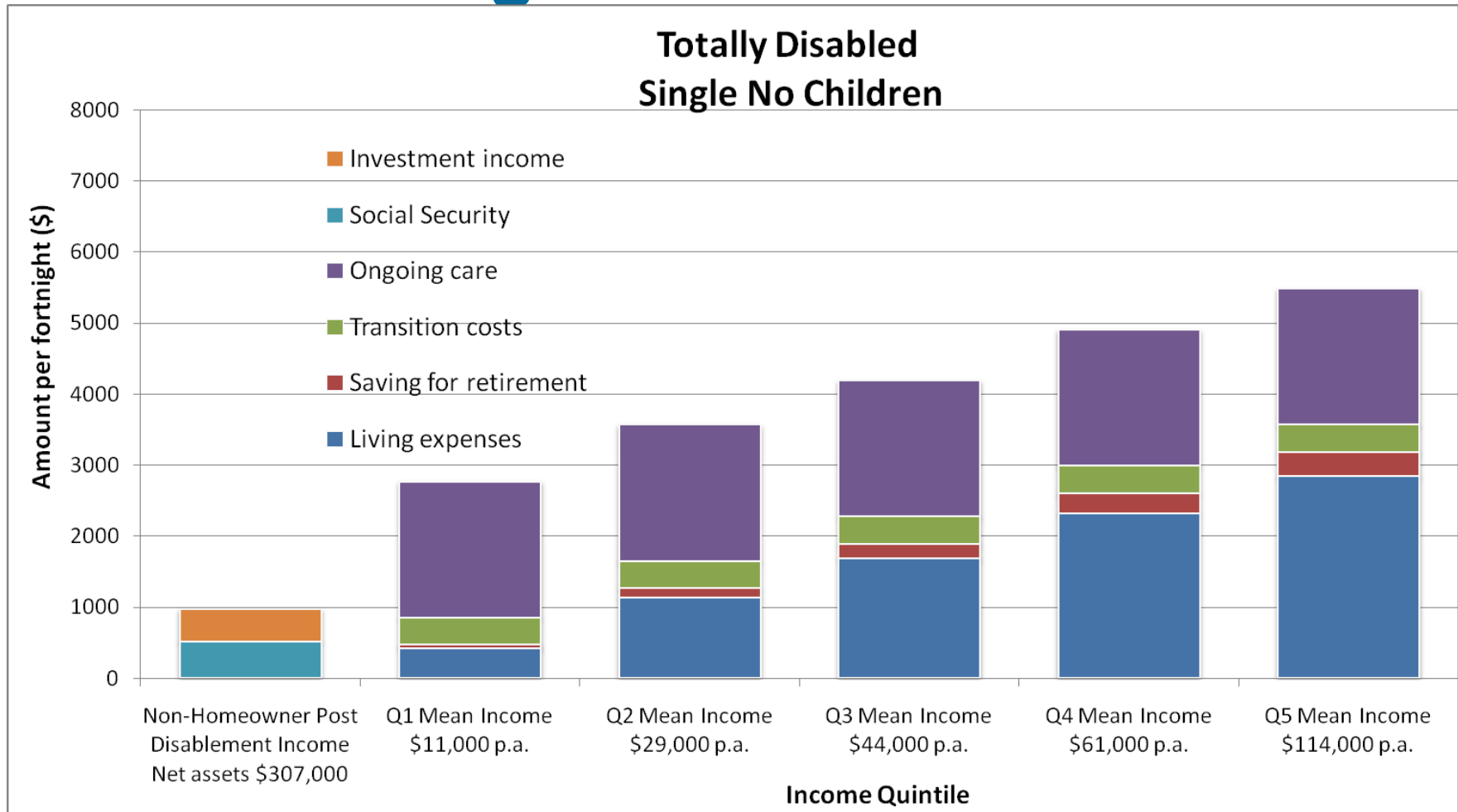
Comparison – Totally Disabled Couple No Children

Totally Disabled Couple, No Children

Comparison – Couple With Children Totally Disabled

Totally Disabled
Couple, Children