Briefing No: 1.03

CPI-only pension indexation

Outcome: 1

POSSIBLE QUESTION / ISSUE(S): Why is the Government changing pension indexation arrangements?

TALKING POINTS

1. Subject to legislation, from September 2017, pensions will be indexed to changes in the Consumer Price Index (CPI) only. This will affect around 3.6 million social security and Veterans' Affairs pensioners.
    - Indexation of Parenting Payment Single by CPI only was intended to start from 20 September 2014 - affecting around 250,000 recipients.
2. However, legislation to give effect to these measures has been delayed.
3. Pensioners and Parenting Payment Single (PPS) recipients will continue to receive pension increases twice a year, in March and September.
4. Purchasing power will be maintained through indexation to movements in prices.
5. Indexation to the CPI will help to slow the growth in pension outlays, and ensures that indexation arrangements across all social security payments are consistent.
6. The measure will save $449 million over the forward estimates across the Department of Veterans' Affairs and DSS.
    - DSS only savings are estimated to be $393 million over the forward estimates.
7. Legislation to change pension indexation to CPI only has been reintroduced to Parliament in two separate new Bills on 2 October 2014.

BACKGROUND

Under the new indexation arrangements announced in the 2014-15 Budget, benchmarking to Male Total Average Weekly Earnings (MTAWE), and indexation to Pensioner and Beneficiary Living Cost Index (PBLCI), will be removed.

Subject to the passage of legislation, this change will take effect in September 2017 for indexation of Age Pension, Carer Payment, Disability Support Pension and other pension payments, as well as equivalent Veterans' Affairs payments.

Subject to the passage of legislation, the Parenting Payment Single measure will also affect recipients of allowances whose rates are set at the Parenting Payment Single rate – i.e. single, principal carers of dependent children, exempt from the activity test for foster caring, home schooling, distance education or large family. (The new start date for Parenting Payment Single is the date of the Royal Assent, which effectively means 20 March 2015, the next relevant indexation point – provided the legislation is passed before that date)

Customers affected

Around 3.8 million payment recipients across the Department of Social Services and the Department of Veterans' Affairs will be affected by the measure when fully implemented (around 3.6 million pensioners and around 250,000 Parenting Payment Single recipients).

Current indexation provisions:

- Parenting Payment Single (PPS) is indexed twice a year, in March and September, to changes in the CPI. If the maximum basic rate of PPS after CPI indexation is less than 25 per cent of MTAWE, then the rate is increased to equal 25 per cent of MTAWE.
- Pensions (excluding PPS) are indexed twice a year, in March and September, to the higher of changes in the CPI or changes in PBLCI. The combined couple rate of maximum basic pension is then compared to 41.76 per cent of MTAWE and increased if necessary. The maximum single basic pension is set at 66.33 per cent of the combined couple rate (around 27.7 per cent of MTAWE).

20 September 2014 indexation details

- On 20 September 2014, the maximum rate of pension increased by:
  - $11.50 a fortnight for a single pensioner and $17.40 for a couple (combined).
  - $7.20 a fortnight for PPS recipients.
- The pension increase of 20 September 2014 was driven by the PBLCI increase of 1.4 per cent over the six months to 30 June 2014.
- In the same period the CPI increased 1.0 per cent.
- Once the base pension for a couple combined was indexed by PBLCI, it exceeded the benchmark of 41.76 per cent of MTAWE, so the benchmark did not have an impact at this indexation point.
- The rate of Parenting Payment (Single) was increased by the CPI, and the increase in the CPI exceeded the 25 per cent MTAWE wages benchmark used for PP(S).

Background - MTAWE and PBLCI

- The MTAWE benchmark was legislated in 1997 and implemented to ensure pensions kept up with improvements in community living standards as measured by wages.

- Before 1997, the decision on whether to benchmark to wages was considered at each indexation point and made on an ad-hoc basis according to budget priorities.
- The MTAWE benchmark for single pensioners (apart from Parenting Payment Single recipients) was increased in 2009, from 25 per cent to around 27.7 per cent.
- PBLCI was introduced in 2009 and was designed to better reflect the actual spending patterns of pensioner and beneficiary households.

Indexation under the new arrangements:

Once the measure is implemented, payments will be indexed to changes in the CPI, using ABS data on the movement in prices:

- over the 6-month period from the previous December to the previous June for 20 September indexation; and
- over the 6-month period from the previous June to the previous December for 20 March Indexation.

The measure will not affect Defence Forces Retirement Benefits Scheme (DFRB) and Defence Force Retirement and Death Benefits Scheme (DFRDB) pensions. They are superannuation-type payments, indexed in January and July each year.

Index all payments to the CPI (from September 2014 for Parenting Payment Single and September 2017 for pensions)

Note: 2014-15 Budget estimates – to date, the delay in passage of legislation has not affected these estimates. The Budget savings estimates assumed indexation by CPI for the 20 September 2014 indexation point. Irrespective of the passage of legislation, it was the CPI that drove the indexation of PPS on 20 September 2014.

	2014-15	2015-16	2016-17	2017-18	Total
Administered Savings	-$1.502 m	-$16.636 m	-$44.203 m	-$331.485 m	-$393.826 m
DSS departmental costs	$0.382 m	$0.263 m	$0.328 m	$0.180 m	$1.153 m
Total DSS savings	**-$1.120 m**	**-$16.373 m**	**-$43.875 m**	**-$331.305 m**	**-$392.673 m**
DHS costs	$1.6 m	$0.1 m	$2.0 m	$3.1 m	$6.8 m
DVA	-	-	-	-$65.1 m	-$65.1 m
Total (Whole-of-Government) impact	**$0.5 m**	**-$16.2 m**	**-$41.8 m**	**-$393.2 m**	**-$449.0 m***

*This figure includes DHS costs for 2013-14 of 1.8 m.
Customer numbers in first year: Around 250,000 Parenting Payment Single recipients will be affected
Customer number over the 4 years: All pensioners and Parenting Payment Single recipients will be affected from 2017-18 – currently around 3.8 million.