pensioncommentary

THE UNIVERSITY OF AUCKLAND BUSINESS SCHOOL

An article from the Retirement Policy and Research Centre

A commentary on recent proposals from Labour

Susan St John, Michael Littlewood and Claire Dale[1]

PensionCommentary 2014-1[2]

30 June 2014

Public policy changes can have profound and enduring effects on the lives of citizens. Better public policy results from evidence-based consultation and expert analysis, with proper consideration given to possible and probable outcomes, and unintended consequences. This commentary notes with concern that political parties are either ignoring superannuation altogether, or coming up with policies that need consultation and analysis before their announcement. This *PensionCommentary* examines the Labour Party's just-announced KiwiSaver policies.

1. Introduction

In April 2014, the RPRC ran a full-day event bringing together key stakeholders to examine the Retirement Commissioner's 2013 report on the sustainability of New Zealand's retirement income system. Proceedings from the day are here. There was broad agreement that the framework is basically sound and, with some potential future adjustments to address affordability and decumulation, will serve us well.

2. Labour Party's KiwiSaver policy

The Labour Party has recently announced its KiwiSaver policies. In summary:

- Described as 'making KiwiSaver universal', Labour proposes to make membership compulsory. That will be done by compulsory enrolment of all employees who are non-members on 1 October 2015, and removing the current right to opt-out or take a contributions holiday.
- The $1,000 'kickstart' will remain but will be paid over five years in $200 instalments rather than in one sum in the first year of membership.
- The current employee:employer contributions will increase from 3%:3% to 4.5%:4.5% between 2016 and 2021.
- Contributions for new members will increase from 1%:3% in 2015 to 4.5%:4.5% by 2021.
- The following groups will not have to be KiwiSaver members:
  - the self-employed, beneficiaries and students not in the workforce;
  - those earning less than the "minimum annual income threshold";
  - those who are allowed to opt-out on hardship or ill-health grounds.
- As previously announced, Labour will ask the Reserve Bank and the Treasury to develop the 'variable contribution rate' proposal as a tool of monetary policy.
- The following features of KiwiSaver will remain:

---

[1] Susan St John and Michael Littlewood are co-directors of the RPRC; M. Claire Dale is Research Fellow with the RPRC.

[2] An RPRC *PensionCommentary* is an opinion piece designed to provoke discussion on an issue of public significance.

- Access to savings for first-home buyers;
- Benefits available from age 65;
- The annual 'member tax credit' of up to $521 a year.

Labour is the first political party to offer detailed policy on KiwiSaver as we approach the September election. There are several aspects of Labour's announcement that deserve comment.

3. The process

In releasing its KiwiSaver policy, the Labour Party has followed the long tradition in New Zealand politics of making announcements on saving and retirement income issues without prior public discussion and without supporting evidence[3].

The RPRC would welcome a change to that tradition. Labour could have produced its KiwiSaver policy as a discussion paper that would be the subject of a research-led debate after the election. Labour's announcements create a point of difference with the current government's policies but that should not be the objective of saving and retirement income policies – they are too important for that.

New Zealanders deserve a full debate on all issues associated with the financial implications of an ageing population. KiwiSaver must be part of that debate, but cannot be seen as independent of the whole retirement income framework.

4. 'Universal' KiwiSaver?

The RPRC questions the appropriateness of the term 'universal' in Labour's announcement. We have a world-respected *universal* age pension, New Zealand Superannuation (NZS), paid to everyone who satisfies modest residence requirements[4]. Its simplicity and relative generosity contribute to one of the lowest poverty rates amongst the old in the developed world. Another unusual feature that makes NZS very egalitarian and simple is that no contribution record is required. This is particularly good for women as it recognises their unpaid work in all its forms.

Labour's version of KiwiSaver is not 'universal' and to call it that is to devalue the word's meaning in the retirement income context. Rather, the Labour Party's KiwiSaver will be 'compulsory' in the same way and to a similar extent that Australia's Superannuation Guarantee (SG) scheme is compulsory. With universal NZS, all who qualify receive the same taxable amount, but the lump-sum at age 65 from KiwiSaver will reflect the distribution of paid work, with high earners the major beneficiaries.

5. The interface with New Zealand Superannuation (NZS)

Labour's proposals will move New Zealand's retirement income policies in Australia's direction. In fact, with respect to KiwiSaver benefits on permanent emigration, their policy announcement had this to say:

> "We will look towards greater alignment with the Australian scheme."

---

[3] In Retirement Policy and Research Centre (2008), the RPRC summarises the chequered history of superannuation 'reforms' over the 30 years to 2008. New Zealand should not be proud of that history.[4] The RPRC acknowledges there are some who may satisfy the residency requirements but have less NZS because of their overseas state pension entitlements.

[4] The RPRC acknowledges there are some who may satisfy the residency requirements but have less NZS because of their overseas state pension entitlements.

A key feature of Australia's superannuation arrangements is the relationship between a pensioner's income and assets and the annual amount of the means-tested Age Pension (Australia's equivalent to NZS). The policy connection between compelling Australians to save for retirement through the SG scheme and the means-tested Age Pension is the expectation that Australians must contribute to their own retirement incomes.

New Zealanders rejected compulsory retirement savings 92:8 in the 1997 referendum. Part of that rejection was the realisation that there would be an offset to NZS (St John, 1999). Changing the KiwiSaver description from 'compulsory' to 'universal' does not remove the association with the failed 1997 'Retirement Savings Scheme'. If Labour, as it appears, wants to increase national saving then a compulsory KiwiSaver will raise the risk of some offset to NZS being imposed, just as it was in the 1997 scheme.

Michael Cullen (2013) has recently suggested the desirability of an 'integrated' approach, reviving the concept of a direct offset of private superannuation savings against NZS such as was proposed for the 1997 scheme.

There is a further logical gap in Labour's KiwiSaver proposals. Labour says it will "retain the current 65 eligibility age to access KiwiSaver savings" but it has also proposed elsewhere that the state pension age should increase to 67. This would require a law change because currently, the KiwiSaver access age is tied to the state pension age and, if that increases, so will the "eligibility age to access KiwiSaver savings".

Allowing early access (before the state pension age) to KiwiSaver lump sums with no requirement for any kind of annuitisation may encourage early spending of this nest egg much as currently happens in Australia.

6. Data gaps

Labour's KiwiSaver proposal is not accompanied by a detailed analysis. It justifies compulsion on the following grounds:

- "New Zealand has chronically low savings".
- "Many New Zealanders retire with little more than government superannuation to live on."
- "An increasing number don't even own the home they live in."
- Our small savings pool also means our businesses have to turn to overseas lenders and investors when they need capital to grow."
- The result is New Zealand has high international debt and a large part of our economy is owned by overseas investors."
- As a country, we send nearly $10 billion a year offshore in dividends and interest payments."[5]

The implied claim is that compulsory KiwiSaver will address this list of 'problems'.

There is, in fact, little connection between the retirement saving behaviour of New Zealand's households and the macro-economic data to which Labour refers in general terms[6].

[5] Extracts from *Building our KiwiSaver nest egg*, New Zealand Labour Party, June 2014 (accessible here)

[6] The so-called 'household saving rate' looks no better. This is another macro-economic number. In fact, it doesn't measure what households save but rather the difference between two very large numbers – all the income that is measured as attributable to the household sector less all the measured expenditure in the same sector. The difference is called 'household saving' but it should really be called the 'unattributable

A look across the Tasman suggests that compulsion might not be the panacea that Labour suggests:

> "Australia recorded a Current Account deficit of 2.90 percent of the country's Gross Domestic Product in 2013. Current Account to GDP in Australia averaged -3.20 percent from 1960 until 2013 reaching an all time high of 1.40 percent in 1972 and a record low of -6.70 percent in 2007." (*Trading Economics* accessible here; data sourced from Australian Bureau of Statistics)

Australia's 2013 deficit (-2.90%) was only just better than the 53-year average of -3.20% of GDP. Over a shorter period (the 33 years between 1980 and 2013) New Zealand's current account deficit averaged -3.40% (according to Statistics New Zealand), not markedly different from Australia's. Even though the stock of net overseas debt as a percentage of GDP is lower in Australia, it is not clear whether compulsory saving has had the impact sometimes claimed for it. It has however enriched the financial services sector.

In any event, compulsion has other implications for Australia's retirement income framework. The rules cannot prevent members' changing their other behaviour to compensate and Australia provides good examples of this. First, the income/asset-tests that link the SG savings (and all other assets) to the Age Pension are intricate and intrusive[7]. Next Australians now seem to arrive at retirement with greater debt, having effectively 'pre-spent' their retirement savings[8]. Australians also seem to retire early to collect their lump sum saving accounts[9] and spend those before reaching qualifying age for the means-tested state pension[10].

Governments cannot control offsetting financial behaviour. If Labour wants compulsory KiwiSaver to be the pathway to increased self-provision for retirement, we need to be mindful of the offsets that will occur. More KiwiSaver savings may reduce saving in other ways, including slower debt-repayment. Counting the money in the compulsory scheme's accounts (an approach favoured by financial service providers) does not tell us what is happening to total household financial wealth including holdings in other managed funds, let alone total household wealth including property assets[11].

---

difference'. Measures of incomes are more likely to be accurate (though by definition, it doesn't count all income) than measures of expenditure but the difference is not 'saving' in the ordinary meaning. All that notwithstanding, compulsion was first introduced for award-based employees in 1986 and then for all other employees in 1992. Compulsion made no real difference to the slide in the household saving rate that hit bottom in 2002-2003, ten years after full compulsion was implemented. In 2014, it is roughly where it was in 1986 when compulsion first began (per capita, annual rolling – chart accessible here).

[7] Australian authorities require information from each pensioner on a regular basis: see here for the assets test and here for the income test.

[8] People should reduce overall debt as they approach retirement. According to Kelly (2010), that seems not to be the case in Australia. In the eight years to 2012, retirement savings among 50 to 64 year-olds grew 48%, other financial assets by 3% and real estate assets by 58% *but* property debt increased 123% and other debt by 43%. By ages 60-64, debt was 42% of retirement saving balances.

[9] The OECD (2010) estimates that Australia's 'effective retirement age' in 2009 was 64.8 (males) and 62.9 (females). By contrast, New Zealand's was 67.1 (males) and 65.0 (females). The Australian Bureau of Statistics reported in December 2013 that the "…average age at retirement for recent retirees (those who have retired in the last five years) was 61.5 years." Men's average was 63.3 and women's 59.6 (see here).

[10] The post-retirement asset test in Australia also leads to an 'over-consumption' of housing services as the primary residence is exempt under the test - Piggot and Dane (2007).

[11] A 2006 household wealth comparison between Australia and New Zealand (Retirement Policy and Research Centre (2010)) shows that Australians have higher proportions of wealth in retirement saving accounts (19.1% in Australia and about 4% in New Zealand) but much less in 'business investment' (7.6% in Australia and 22.2% in New Zealand).

There is a series of reports that suggests New Zealanders already behaved 'sensibly' with regard to retirement income provision, even before the introduction of KiwiSaver[12].

7. Regressive nature of exemptions

As often happens with public policy, the exemptions Labour proposes for its compulsory KiwiSaver will have some unintended effects. Labour says that those earning less than the "minimum income threshold" will not be required to enrol in KiwiSaver. We do not know what that "threshold" will be as that is one of several things to be resolved by a "tripartite consultation process" (see paragraph 8). Employers will not need to contribute for those employees.

That exemption will doubly disadvantage the low-paid. Not only are they at the bottom of the pay scales but also they will miss part of the remuneration that the other employees who are KiwiSaver members must receive. Labour's policy could instead have exempted them the member's contributions but required the employer to make the same contributions for them as for other employees.

The same approach could also apply to those who are allowed to stop contributing on grounds of hardship or ill health.

It is also very unclear how KiwiSaver will be used for macroeconomic management by changing contribution rates to take the pressure off the need to raise interest rates. This commentary does not analyse this policy further except to note that when KiwiSaver is a small part of financial assets and overall wealth, the burden of this policy will fall on those who can't offset any increased contributions by saving less elsewhere. Dampening demand by taking spending power from the low-paid while leaving those with income from capital unaffected will have negative effects amongst the least-advantaged.

8. 'Tripartite consultation process'

There are three references to issues that Labour intends to resolve through a "tripartite consultation process":

- the setting of the "minimum income threshold",
- the detail of the hardship withdrawal, and
- transfers following migration.

Presumably, there will be three parties involved but we do not know who those will be. Labour shows it is willing to put minor aspects of its proposals to an external group for discussion. The RPRC would welcome the widening of this type of consultation to all of the proposals and the gathering the evidence to support them.

9. Conclusion

Based on announcements made after Labour's policy launch on 17 June, it seems there will be some chance that Labour's KiwiSaver proposals will not be implemented even if they are elected. The current government, predictably, is opposed but the Green Party has also expressed opposition to compulsion. If the Greens stand by that and become part of a future government, compulsory KiwiSaver is perhaps unlikely.

---

12 See for example: Le, Gibson and Stillman (2012); Scobie and Henderson (2009) and Le, Scobie and Gibson (2009).

Regardless of the election outcomes, it is important for New Zealand that all retirement and retirement income issues are discussed in an apolitical arena, that a broad consensus emerges for future stability, and citizens are given appropriate notice of any significant policy change. The long-term retirement income policy framework is far too important to be decided by the whims of politicians who just happen to be the government.

For comments on this *PensionCommentary* and for further information please contact:

Michael Littlewood **P** +64 9 92 33 884 DDI **M** +64 (21) 677 160 **E** Michael.Littlewood@auckland.ac.nz

Retirement Policy and Research Centre
University of Auckland
Private Bag 92 019
Auckland 1142
New Zealand
http://www.rprc.auckland.ac.nz

References

Cullen, M. (2013) *The Political Economy of Long-Term Fiscal Planning from a Social Democratic Perspective* Policy Quarterly **9**(4)

Kelly, S *Household savings and retirement – where has all my super gone? A report on superannuation and retirement for CPA Australia* (2012)

Le, T., Gibson, J. and Stillman, S. (2012) *Household Wealth and Saving in New Zealand: evidence from the longitudinal survey of family, income and employment* New Zealand Economic Papers (accessible here)

Le, T., Scobie, G. and Gibson, J. (2009) *Are Kiwis saving enough for retirement? Evidence from SOFIE*, New Zealand Economic Papers (accessible here)

OECD (2010) *Average effective age of retirement in 1970-2009 in OECD countries*, accessible here.

Piggott, J. and Dane, R. (2007) *Residential Transition Amongst the Australian Elderly*, Australian Institute for Population Ageing Research (accessible here)

Retirement Policy and Research Centre (2008) *A condensed history of public and private provision for retirement income in New Zealand - 1975-2008* (accessible here)

Retirement Policy and Research Centre (2010) *Household wealth in Australia and New Zealand*, RPRC *PensionBriefing 2010-5* (accessible here).

Scobie, G. and Henderson, K., (2009) *Saving Rates of New Zealanders: A Net Wealth Approach* New Zealand Treasury, Wellington (available here)

St John, S. (1999) *Superannuation in the 1990s: where angels fear to tread?* Redesigning the welfare state in New Zealand P. Dalziel, J. Boston and S. St John. Auckland, Oxford University Press.