

RETIREMENT INCOME REPORT 2003



PERIODIC REPORT GROUP

December 2003

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FOREWORD

Preparing for old age and retirement is an important challenge for New Zealanders. Retirement preparation requires long-term planning, and is best done in an environment of reasonable economic stability supported by quality information and advice.

Increased life expectancy may mean changes in the way New Zealanders transition from working life to retirement. It may mean we need increased savings to support our lifestyle for a longer period in retirement, or longer working lives.

Younger New Zealanders are experiencing different circumstances through their life than those currently retired or approaching retirement. These changes require careful monitoring to ensure that appropriate policy settings are in place for the future.

The message is clear: planning for retirement is important.

The 2003 Periodic Report Group reports with terms of reference that are focused on private provision. As required, we have given attention to work-based savings and population groups including women, Māori and Pacific peoples.

Our report contains a significant number of recommendations. These are designed to enhance and invigorate the voluntary approach that continues to underpin retirement savings in New Zealand. We believe that New Zealanders need to be encouraged to take greater personal responsibility for their future, and the recommendations are designed to support this and enhance the partnership between public and private provision.

Those who may have expected the 2003 Periodic Report Group to promote major changes of direction will be dissatisfied. Preparing for old age is a long-term project. Changes will be necessary but these must be signalled and implemented well in advance and the position of those in retirement and close to retirement must be protected. Sudden changes of direction are not helpful.

New Zealand is fortunate in that it has a window of opportunity before the population begins to age rapidly, but that window is closing and we must use the available time wisely. Our report is presented with this in mind.



Vance Arkinstall

Chair

December 2003



EXECUTIVE SUMMARY

EXECUTIVE SUMMARY

The role of the Periodic Report Group 2003 (PRG2003) is to review the system of private provision for retirement in New Zealand. Our report seeks to advance and inform the policy debate about how New Zealand ensures that the older members of our society have adequate living standards.

We find the current system of voluntary private provision and a universal pension is working reasonably well for the currently retired and those approaching retirement. Future retirees will have very different life and work experiences from the current generation of retirees. There is no room for complacency about the current system's ability to provide for future cohorts. There are places where it needs refinement and invigoration and we recommend more regular and ongoing assessment of its effectiveness.

The issue of whether a voluntary approach to private provision in combination with New Zealand Superannuation (NZS) is the best means of ensuring adequate income and living standards for retired New Zealanders, while at the same time facilitating economic growth, was extensively analysed by both the 1992 Task Force on Private Provision for Retirement and the 1997 Periodic Report Group. We also propose no change from the current voluntary approach to private provision, nor have submissions reflected a strong interest in departing from the current voluntary model.

Economic growth

New Zealand, and indeed the populations of the industrial world in general, is transitioning to an older population age structure. This is at the heart of concern over the affordability and sustainability of retirement income provision. One impact of this transition is that it could mean fewer workers will be available to support a burgeoning population of retirees. In this scenario, continuing to improve the living standards of the working population and the retired at the same time will require strong economic growth.

The simple fact is that the stronger the economic growth the greater will be the quantity of goods and services available for all, whether retired or working. Overall living standards will largely be determined by economic growth rather than by the details of financial arrangements.

Risks and opportunities

Current research demonstrates that most older people are doing quite well and have relatively few material restrictions and difficulties in terms of basic needs. This reflects a combination of income from NZS, high levels of mortgage free home ownership on retirement, and some private savings. For those close to retirement the available evidence suggests that they are also likely to have an adequate standard of living in retirement.

For younger cohorts of middle-income New Zealanders, the picture is less clear, because the impact of their saving habits on asset accumulation is not yet observable. We think there are a number of risks and opportunities that may impact on future cohorts' savings behaviour, and living standards in retirement, that will require close monitoring in the future.

The risks include: higher debt levels, student loans, changes in relationship status, later child bearing and potentially lower levels of mortgage free home ownership, which may lead to less private provision and lower standards of living in retirement. Opportunities include the increasing participation of older New Zealanders in the labour market and changing attitudes to old age with a blurring of life-stage and life-cycle.

The ageing population creates pressure on the long-term sustainability of NZS. The two main fiscal pressures arising from this older population will be increased spending on NZS and rising health costs. The New Zealand Superannuation Fund is the Government's main tool for meeting the increased fiscal pressures created by an ageing population. However, the Fund is designed to cover only part of the increase in future NZS costs.

Future Governments will need tools in addition to the Fund to address the increasing fiscal pressures. Unlike many countries facing similar issues, these fiscal pressures are not immediate in New Zealand. We have a window of opportunity before the baby boomers start claiming NZS in increasing numbers in the middle of the next decade. PRG2003 would like to see an open and informed discussion about future public provision.

Policy approaches to bolstering private provision

We identify a number of refinements to the current policy approach that aim to bolster private provision. Our focus is on middle-income earners. NZS is not designed to provide complete income replacement for this group and many could save more and their private savings would contribute to the maintenance of living standards in retirement.

Work-based savings

Our terms of reference require us to consider mechanisms for Government, employers and the savings industry to work collaboratively together to promote employer-based superannuation.

Although work-based savings schemes are not strongly entrenched in New Zealand, PRG2003 thinks there is value in promoting greater use of work-based savings schemes as a way for New Zealanders to save for retirement.

Such schemes may help to overcome those aspects of human behaviour such as procrastination that may otherwise represent hurdles to starting and continuing to save. Work-based savings schemes provide deduction at source, economies of scale and an avenue to reach a high proportion of the population. They also provide a context for employees to consider their retirement planning decisions and a venue for education.

However, this is an area where progress will require groups such as employers, unions, Government, product providers and others to work together to increase access to and participation in work-based schemes. For this reason PRG2003 recommends the Government establish a work-based savings group comprised of representatives from the public and private sectors. We would ask such a group to report by the end of 2004 on an agreed approach to promoting and developing work-based savings that aims to reduce the barriers to the participation of employers and employees. This suggests a move away from the more traditional employer sponsored superannuation schemes towards an environment of individualised, portable schemes, where employers at least facilitate access to savings.

Education and information

New Zealand's move from a regulated to a deregulated financial market over the last 20 years has resulted in a rapid increase in the number and complexity of products and services. This in turn has increased New Zealanders' need for clear and impartial education and information. PRG2003 believes that accurate education and information on which to base effective decision-making on retirement is vital in an environment that places the responsibility for financial planning decisions on the individual. A dedicated effort in this area can make important gains.

We recommend that the education and information service provided by the Retirement Commission be extended to include, facilitating workplace seminars, increasing the promotion and substance of Sorted and other education programmes and developing a face-to-face or telephone information service to supplement these programmes. The programmes should meet the education and information needs of low and middle-income New Zealanders and be mindful of the specific issues related to women, Māori, and Pacific peoples.

We also see value in the Retirement Commission extending its provision of information on the extent and level of public provision, and developing methodologies to enable people to compare and assess savings products and advice.

Removing tax distortions and reducing compliance costs

We favour a broadly neutral tax system, with disparities and resulting distortions removed as far as possible. Distortions that need to be addressed include the distortions to savings via the capital/revenue boundary, inconsistent treatment of domestic and foreign investments, and the over-taxation of low to middle-income earners in some retirement savings vehicles. We recommend that Government give priority to addressing these distortions in its tax work programme.

We conclude that there is not a strong case for using tax incentives to increase private provision. If Governments choose to introduce some form of tax incentives for savings, we believe the design of such incentives should focus on the needs of low and middle-income earners.

The key compliance cost we identified was the requirement that employer superannuation schemes maintain a prospectus. We support proposals before Parliament to remove this requirement.

While we don't recommend fundamental change to the regulation of financial services, we suggest there is merit in considering a self-regulatory regime for financial advisers, and recommend that the finance sector present Government with an agreed approach to self-regulation by the end of 2004.

Ongoing analysis and research activities

As the baby boomers get closer to retirement, New Zealand cannot continue to rely on an ad-hoc approach to collating, monitoring and analysing information related to savings. It is important we improve our understanding of the complex dynamics that will shape future living standards in retirement and this requires an ongoing research agenda.

We consider that a key element in this research agenda is an investigation into household savings behaviour. To this end we recommend that the Retirement Commission be responsible for managing a research fund set up for this research. The research agenda should also include repeating the 2001 Household Savings Survey so that over time we gain a better understanding of the savings behaviour of different age groups to determine if there is a savings problem among younger cohorts of New Zealanders and to assess the size of any such problem.

In addition to this work led by the Retirement Commission, research from other government agencies and academics will contribute to the growing knowledge base on retirement income issues. We see value in the Retirement Commission having an information sharing and co-ordination role for this ongoing research.

Towards the future

We think policy reviews occurring only once every six years are too far apart to adequately inform retirement income policy. By the time the next scheduled review takes place in the year 2009 the advance guard of the ageing baby boomers will be entering their 65th year. Thereafter, the growth in the numbers of those aged 65 plus will be rapid.

We recommend the establishment of an ongoing work programme to replace the six-yearly reviews. We anticipate the work programme would be based on the Government's response to PRG2003's policy proposals and would include the establishment of a work-based savings group and a process for the ongoing monitoring of savings, tax and regulatory issues.

The role of the Retirement Commission would be to monitor the progress of the work programme. In the context of this monitoring role we recommend that the Retirement Commission establish an advisory group to create a mechanism for stakeholders to provide comment and input into the work programme. The advisory group should include employers, unions, finance industry representative bodies and experts.

In addition we recommend that by the end of 2007 the Retirement Commission, in consultation with its advisory group, review retirement income policy. The review should:

- report on progress and change in retirement income policy
- report on the risks and opportunities identified in the PRG2003 report
- highlight the issues needing policy attention
- assess the proposed work programme approach and whether it should be continued.



INTRODUCTION

INTRODUCTION

This is the report of the Periodic Report Group 2003 (PRG2003) on retirement income policy. It is required by section 22 of the Retirement Income Act 1993, which states that a report will be produced every six years. The concept of a six-yearly review of retirement income policy was developed by the 1992 Task Force on Private Provision for Retirement (1992 PPR Task Force) as part of their recommendation for an enhanced voluntary approach to private provision.

The basic approach to private provision entrenched in response to the recommendations of the 1992 PPR Task Force remains in place. Private provision for retirement is voluntary and is underpinned by a broadly tax-neutral savings framework, supported by education and information from the Retirement Commission and a six-yearly review.

However, the political, policy and economic environment has changed substantially since 1992 and the subsequent 1997 Periodic Report Group (PRG1997) reports. The political accord that underpinned retirement income policy has fallen into disuse. Public provision is now established under the New Zealand Superannuation Act 2001, which establishes the entitlements to New Zealand Superannuation (NZS) and creates the New Zealand Superannuation Fund (NZ Superannuation Fund). This Act also establishes a process for signalling political agreement on the parameters for NZS. The wider economic environment for the private provision of retirement income has been in flux, with many savings schemes, until recently, experiencing a period of negative returns.

In this context, our focus is on assessing the impact and role of private provision on retirement income, rather than attempting to re-examine all retirement income policies.

TERMS OF REFERENCE

Our terms of reference require us to include:

- In relation to the Government's retirement income policies, an update of the trends, and the likely future developments, since the production of the 1997 periodic report that will affect, or will be likely to affect, private provision of retirement income.
- A commentary on any changes to the Government's retirement income policies since the 1997 periodic report and their effect on the private provision of retirement income.
- An identification of areas of risk or unsatisfactory performance in relation to the private provision of retirement income.
- A commentary on the interface between private savings for retirement and other savings undertaken during the life cycle for pre-retirement purposes.

- A commentary on the ability of specific population groups, including women, Māori and Pacific peoples, to make private provision for retirement income.
- Suggestions for the adjustment of any of the Government's retirement income and savings policies in order to enhance the provision of private retirement income, including those relating to:
 - mechanisms for Government, employers and the savings industry to work collaboratively together to promote employer-based superannuation, and
 - the impact of the tax system on the private provision of retirement income.

MEMBERSHIP OF THE PERIODIC REPORT GROUP 2003

Vance Arkinstall, (Chair), Chief Executive of the Investment Savings and Insurance Association of New Zealand Inc.

Lynn Middleton, (Deputy), National Secretary of the Public Service Association

Diana Crossan, Retirement Commissioner

Owen Nash, MCA Limited (resigned September 2003)

Public sector officials

Bryan Perry, Ministry of Social Development

Vicky Robertson, Treasury

Mike Nutsford, Inland Revenue Department

SUBMISSIONS AND CONSULTATION

To ensure there was the opportunity for interested parties to have an input into our deliberations, we undertook a consultation process. We wrote directly to a number of key individuals and organisations to give them the opportunity to share their views. At the same time, we placed notices in the major newspapers seeking submissions from the public. As a result, we received 52 written submissions.

These are listed in Appendix G, along with the submitters we met with.

To aid our deliberations, we met throughout the year with a number of people who are also listed in Appendix G.

BACKGROUND PAPERS

PRG2003 had a number of background papers prepared to aid our understanding and analysis of retirement income issues. The views expressed in the background papers are those of the author(s) and do not necessarily reflect the views of PRG2003.

The papers are listed in Appendix H.

STRUCTURE OF THE REPORT

Chapter One, 'Context', establishes the wider context for analysing private provision, focusing on the changing demographics, the importance of economic growth and the impact of recent policy changes on private provision.

Chapter Two, 'Private provision: the risks and opportunities', reviews the risks and opportunities related to private provision for retirement income, focusing on savings and the living standard of New Zealanders.

Chapter Three, 'An ageing population: the fiscal pressures', addresses the fiscal risks related to an ageing population and the need to discuss these issues.

Chapter Four, 'Work-based savings', reviews the current role of work-based savings and how that role could be developed in the future.

Chapter Five, 'Personal financial education and information', reviews the education and information on private provision for retirement income provided to New Zealanders and how it could be developed in the future.

Chapter Six, 'Issues for women, Māori and Pacific peoples', considers the issues from the perspectives of women, Māori and Pacific peoples.

Chapter Seven, 'Taxation of savings', reviews the taxation of savings and how the tax regime might best ensure the consistent treatment of savings.

Chapter Eight, 'Financial services market and regulation', addresses the regulation of the financial services sector and the means to minimise the related costs.

Chapter Nine, 'Implementing PRG 2003's proposed work programme', focuses on the post-PRG process and the implementation of a work programme to address the risks and opportunities related to private provision.

ACKNOWLEDGEMENTS

A number of people deserve mention and acknowledgment for their assistance.

We thank all submitters for their efforts and the high standards of their submissions.

We thank all those who took the time to meet us and who contributed their expertise.

We thank the secretariat, Colin Lynch and Bede Hogan.

Finally, we thank David Feslier (Retirement Commission), Brock Jera (Treasury) and other officials from the Ministry of Social Development, Treasury and the Inland Revenue Department for their technical and administrative support.

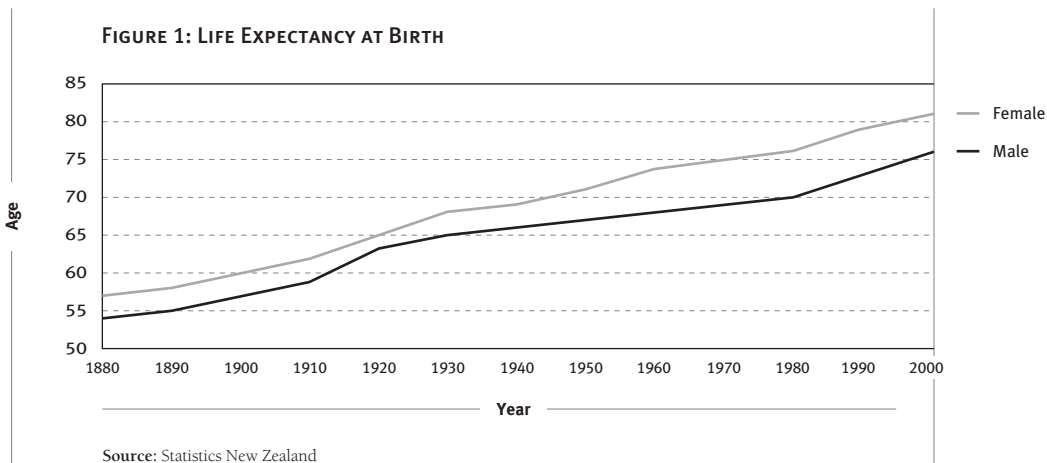


CHAPTER ONE CONTEXT

The demographic context

New Zealand is currently experiencing a major demographic transition into an older population age structure. This is caused by reduced fertility leading to lower birth rates, and by rising life expectancy in older age.

Over the last century, life expectancy has been increasing as shown by Figure 1. In 2001 the life expectancy at age 65 for a New Zealand male was 18.2 years, while for a female it was 21.9 years.¹ Life expectancy is expected to increase further over the next 40 years, but not at the same rate as in the previous 40 years. A recent review concluded that, within each age group, health status probably has also been improving over the long run.² Seventy-year-olds now, for instance, tend to be healthier than seventy-year-olds 20 years ago.



Longer lives and an increasingly older population are at the heart of the debate on retirement income policy. An ageing population will increase pressure on the public provision of income and services for older New Zealanders and this will have to be funded by a smaller working age population.

1 The Treasury (2003a)
2 Ibid

The New Zealand pattern is not unique. Other developed countries are passing through a similar demographic transition towards a much older age structure, with fewer children and young adults and many more older people. Indeed, New Zealand is less advanced on this ageing path than is now the case in most European countries and Japan, where the number of children per woman has fallen much further than in New Zealand and the proportion of those aged 65 plus is well above New Zealand levels. In this context, New Zealand has more time to adjust to the demographic transition than many other developed countries.

The demographic transition

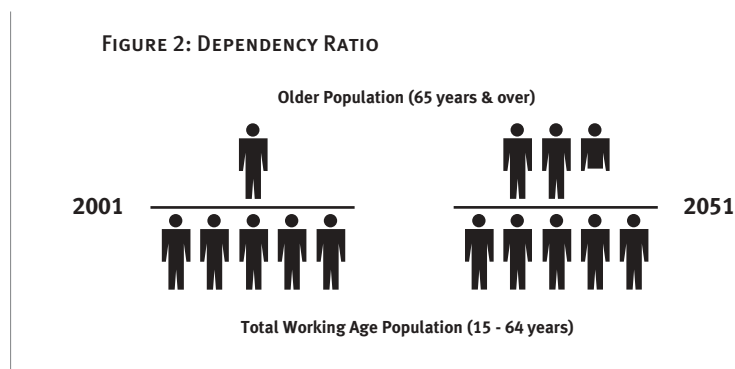
The demographic transition through which New Zealand and most other developed countries are passing involves significant shifts in the 'dependency ratio' of the population. This is the proportion of older people to those in the traditional working age groups.

The demographic transition through which New Zealand is passing can be viewed as having three main stages:

- An early stage when birth rates fall, the share of the population in the labour force age groups rises and a relatively young work force is still expanding from the impact of higher birth rates in the earlier period. The share of older people in the population begins to rise, but by much less than the fall in the share of children.
- A middle stage where the labour force middle-ages, but still increases, and the rising proportion of older people is less than the ongoing fall in the proportion of children.
- An advanced stage where the number and proportion of older people rises rapidly, the labour force age groups shrink and the total population may begin to decline.

New Zealand passed through the first stage of structural ageing in the later 20th century. It is now moving through the second stage of middle-ageing.

After about 2011, and especially after about 2021, the retirement of the 'baby boom' generation will rapidly escalate the dependency ratios. The ratio of the older population (65 years and over) to those of working age (15 to 64 years) is predicted to increase from the present 18 per 100 persons of working age to 43 per 100 by 2051.³ The changing dependency ratios are illustrated in Figure 2.



³ Khawaja M (2000)

However, these demographically based calculations do not take into account the changes in patterns of labour force participation. For example, 15 is now an unrealistically young age to enter the labour force and it is possible that, in the future, people will remain in paid work, under more flexible conditions, beyond the age of 64, either voluntarily or to support their desired living standards.

The economic context

While our report focuses on the private provision of retirement income, this, on its own, does not solve the emerging demographic pressure. The living standards of future generations of working and retired New Zealanders will depend on the size of the economy over their lives. This is because the goods and services consumed by the retired population are generated by the current production of the economy.

The simple fact is that, the stronger the economic growth, the greater will be the quantity of goods and services available for all, whether retired or working. Overall living standards will largely be determined by economic growth rather than by the details of financial arrangements.

The importance of economic growth was neatly summarised by Michael Savage in a 1938 parliamentary debate on the Social Security Bill.

For those who are due to get the universal superannuation or pensions, I do not care how it is described, so long as the money is there; it can only come from the productive forces of New Zealand. We cannot give them any more. It does not matter how much we manipulate the money system; we cannot give the people any more than we are able to produce.

Of course, simply asserting that economic growth is what matters does not provide answers about how best to ensure New Zealanders have an adequate standard of living in old age. What we do know is that private savings are an important determinant of the standard of living of individuals in retirement because they give savers ownership of a share of future production.

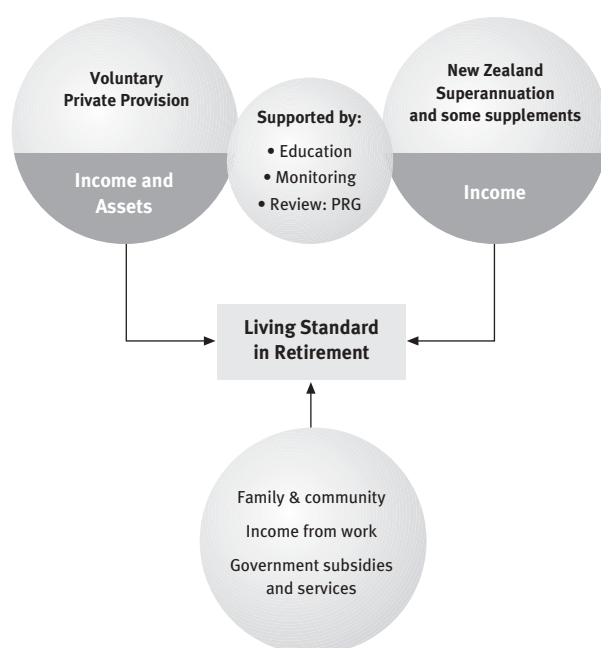
The importance of economic growth for future living standards leads us to conclude that an important question for any policy proposal aimed at increasing private provision is: how will it impact on long-term economic growth?

New Zealand's retirement income policy

New Zealand has a two-tier system of retirement income provision. The first tier is NZS, a universal public pension funded from general taxation. The second tier consists of voluntary private provision by individuals to enhance their standard of living in retirement.

Supporting these tiers are the families and communities who support and assist their older members, the earnings of New Zealanders who choose to work past 65, and other government services available to older New Zealanders. The broad framework is summarised in Figure 3.

FIGURE 3: SUMMARY OF NEW ZEALAND'S RETIREMENT INCOME FRAMEWORK



What public provision provides

It needs to be clearly understood that NZS is not a complete form of retirement income provision. NZS and its associated social welfare supplementary assistance provides:

- an adequate replacement income in retirement for low-income earners
- an independent source of income in retirement for non-earners
- a base income for all retirees, to which they can add their own self-provision.

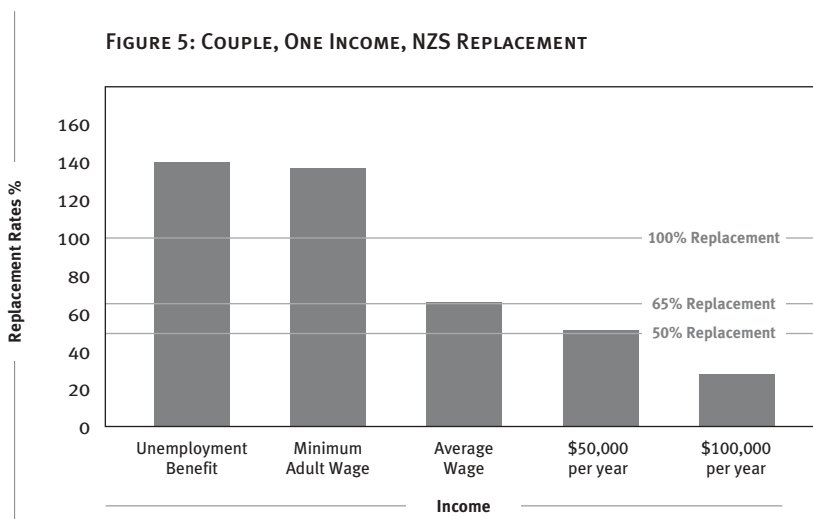
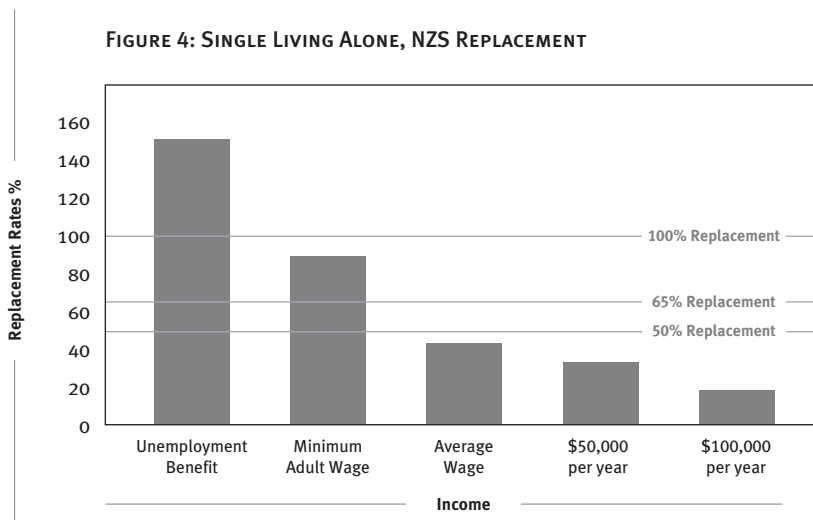
NZS is paid to those fully qualified at a standard dollar amount unrelated to previous earnings. The amount is dependent only on marital status and living arrangements. There are three basic rates at which NZS is paid - the married person rate, the single sharing rate, and the single living alone rate. NZS rates as at 1 April 2003 are shown in Table 1.

TABLE 1: NZS RATES AS AT 1 APRIL 2003

Rate	Net (weekly)	Gross (weekly)	Gross (annual)
Married Person	\$188.69	\$224.76	\$11,687.52
Single Sharing	\$226.43	\$272.58	\$14,174.16
Single Living Alone	\$245.30	\$296.49	\$15,417.48

Source: Ministry of Social Development

Figures 4 and 5 show the extent to which NZS replaces the income people earned or received before retirement. The replacement rates are expressed as percentages of their previous income after tax. Figure 5 assumes that only one person was previously earning. Hence, for couples in which both people were earning, the real drop in income is likely to be larger. It can be seen that NZS provides a high replacement income for low-income earners and beneficiaries and a moderate replacement income for an average-wage earner. But it provides a lower replacement income for single people on average wages and people on above-average incomes.



What private provision provides

While public provision does some things well, for most of the population, it leaves gaps that need to be filled by private provision.

In the context of our report, we define private provision broadly to include private savings, assets such as the family home and businesses, income from work in retirement, and the support provided by family and the community.

As highlighted in Figures 4 and 5, private provision is needed to provide:

- higher levels of income replacement in retirement for middle and upper-income earners
- a buffer to deal with large cash outlay needs such as those involved in replacing motor vehicles or paying for large unexpected medical costs.

Maintaining pre-retirement living standards is an important component of ensuring social cohesion between the working age population and the retired population, and this will become increasingly important as the population ages. The current retired population has largely succeeded in maintaining adequate living standards, with most older people doing quite well, with relatively few material restrictions and difficulties in terms of basic needs.⁴ The challenge will be to ensure that the mix of public and private provision is sufficient to achieve this outcome for future generations.

Reviewing policy developments since 1997

Our terms of reference require that, in relation to the Government's retirement income policies, we provide an update of the trends and the likely future developments since the production of the 1997 periodic report that will affect, or will be likely to affect, private provision of retirement income.

The period since the 1997 periodic report has been one of significant change in the funding of public provision, but little change in private provision and related policies.

Public provision

The most significant change in public provision has been through the introduction of the New Zealand Superannuation Act 2001. The Act has two parts. Part One provides for the current entitlements to NZS, which have remained largely unchanged since the 1997 periodic report. Part Two creates the NZ Superannuation Fund, and provides a new opportunity for political parties to indicate their support for either or both Part One and Part Two. The Accord on Retirement Income Policies, while still existing, has fallen into disuse since 1998.⁵

⁴ Fergusson D et al (2001)

⁵ The Accord on Retirement Income Policies is a document signed by the Alliance, Labour and National parties in August 1993, and by the United Party in 1995, the purpose of which was to achieve consensus on retirement income policies to be implemented in New Zealand.

Private provision

In the context of private provision, the most significant policy development since the last PRG report has been the increase in the top marginal tax rate. In 2000, the top marginal tax rate was increased from 33 to 39 percent. This resulted in a tax benefit for high-income earners who invested in registered superannuation schemes because the schemes are taxed at 33 percent, in contrast to their marginal tax rate of 39 percent. Also, employer contributions to schemes are taxed at 33 percent rather than at the top marginal rate.

Economic developments

After recovering from the Asia crisis in 1998, the New Zealand economy has experienced a period of good growth. In the last four years, GDP has increased, on average, around 3.5 percent a year.

At the same time, the global equity markets moved from a strong 'bull' market before 2000 to a strong 'bear' market, resulting in negative returns to most equity investment schemes. As a result, there has been a decline in the absolute level of household financial savings. However, it appears this may be coming to an end, with recent data showing a significant and positive turnaround in equity prices.⁶

Household financial liabilities have risen steadily over the last six years, from 106 percent of disposable income in 1997 to 130 percent in 2002.⁷ However, on the asset side of the household balance sheet, the value of houses has risen sufficiently to outweigh increasing debt levels and declines in the value of financial savings. Consequently, household net worth has risen.⁸

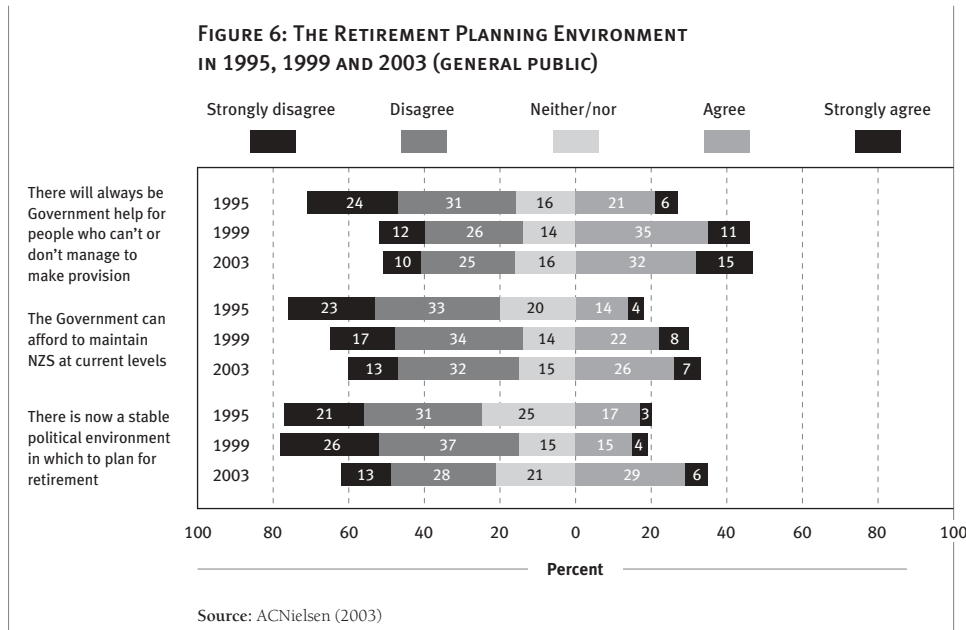
6 Westpac (2003)

7 Thorp C (2003)

8 Net worth equals the total value of assets less the total value of debts.

The impacts of policy developments on private savings for retirement

While most New Zealanders remain sceptical about the stability of retirement income policy, they are less so than they were four years ago. A recent Retirement Commission survey found that New Zealanders are now more inclined to agree with the statement: “there is now a stable political environment in which to plan for retirement”.⁹ In 2003, 35 percent agreed with this statement, compared to 19 percent in 1999. Disagreement decreased from 63 percent to 41 percent. See Figure 6.



Furthermore, there is increasing agreement with the statement: “there will always be Government help for people who can’t or don’t manage to make provision”. Levels of agreement have increased from 27 percent in 1995 to 47 percent in 2003. Perceptions of the Government’s ability to afford to maintain NZS at current levels are also increasing, although disagreement still outweighs agreement (45 percent disagreement versus 33 percent agreement).

The change that was expected to have the greatest effect was the establishment of the NZ Superannuation Fund. An initial Treasury analysis of the possible impacts of the fund highlighted that if pre-funding led to greater certainty about public provision, private provision could decline.¹⁰ Recent surveys suggest the Fund is having little impact on savings decisions. The AMP SuperWatch Survey in June 2003 found little evidence that the NZ Superannuation Fund was putting people off making private provision.¹¹

9 ACNielsen (2003)

10 The Treasury (2000)

11 AMP SuperWatch, http://www.amp.co.nz/default_thenewsp.htm

The Retirement Commission survey also found that, despite a more stable environment and increasing certainty around NZS, the majority of respondents didn't think the NZ Superannuation Fund had affected their financial preparation for retirement. However, the real impacts of the NZ Superannuation Fund are difficult to assess. As the Retirement Commission survey noted, many people do not really understand the NZ Superannuation Fund. As the Fund grows over time, awareness and understanding will increase, and how that impacts on private provision will need to be closely monitored.

The effect of increasing the top marginal tax rate in 2000, which created a tax subsidy for high-income earners, appears to have had a minimal impact on savings by high-income earners through tax-advantaged superannuation schemes. The survey prepared for the PRG2003 by the ESR Consortium shows that, of the firms interviewed, only a very small proportion of employees (0.4 percent) actually take advantage of the tax subsidy.¹²

The impact of the increase in the tax rate on taxpayers' disposable income and, hence, their ability to save will have far outweighed any small increase in savings in response to the subsidy it created. The level of taxes matters more for saving than the existence of a tax subsidy.

Overall policy changes appear to have had limited impact on private provision. Rather, it is wider economic factors that have dominated changes to private provision since 1997.

12 ESR Consortium (2003)



CHAPTER TWO
PRIVATE PROVISION:
THE RISKS AND OPPORTUNITIES

CHAPTER TWO PRIVATE PROVISION: THE RISKS AND OPPORTUNITIES

Overview

Our terms of reference require us to assess and identify areas of risk and unsatisfactory performance in relation to the private provision of retirement income.

Any assessment of risk and opportunity in relation to private provision needs to assess the issues related to today's working age population. The relative strength of the factors that will determine the living standards in retirement of those yet to retire will be different than those for the already retired. Also, between working age cohorts, there are likely to be very significant differences. The lifetime experience of today's 55 to 65-year-olds and the impact it had on their ability to make private provision for retirement will be very different to that of current 25 to 35-year-olds.

We take an approach that recognises that living standards in retirement reflect not only asset accumulation and public provision, but also the fact that asset accumulation will vary over a lifetime and reflect factors such as family commitments, access to paid employment and health. All of these factors impact on the ability to make private provision for retirement.

The 2001 Living Standards Survey shows that most older New Zealanders were doing quite well and had relatively few material restrictions and difficulties in terms of basic needs. The private provision older New Zealanders have made, combined with NZS, is sufficient to enable most older people to avoid hardship.

The outlook for subsequent cohorts is more complex and dynamic.

New Zealanders save in many ways. Their main asset is their home, accounting for 36 percent of total asset value recorded in the 2001 Household Savings Survey. Financial assets, including bank deposits and superannuation, account for 16 percent of total asset value. The remainder is made up of businesses, trusts, farms and property.

However, the distribution of assets and income is uneven. The 30 to 40 percent of New Zealanders with low incomes are unlikely to have sufficient disposable incomes over their working life to save much for retirement. They will be largely dependent on NZS in old age. The top 10 to 20 percent of income earners appear to be accumulating adequate savings for retirement.

Consequently, middle-income New Zealanders are our key concern in terms of risks and opportunities in relation to the private provision of retirement income. They have some capacity to make private provision for retirement and, if they do not, many are likely to

experience a significant fall in living standards on retirement. NZS will provide them with a basic income, though.

Initial analysis of the 2001 Household Savings Survey suggests that the current 45 to 55 age cohort is not under-saving as a group. For younger cohorts of middle-income New Zealanders, the picture is less clear, because the impact of their savings habits on asset accumulation is not yet observable.

We think there are a number of risks and opportunities that may impact on future cohorts' savings behaviour and these will require close monitoring in the future.

Increasing financial liabilities

There has been a rapid increase in household liabilities. While overall net worth of households has increased in recent years on the back of increasing house prices, household financial liabilities have increased from 74 percent of disposable income in 1992 to 130 percent in 2002. This largely reflects the impact of financial liberalisation increasing access to credit and it is not clear yet how it will impact on private provision.

Increasing financial liabilities are not a problem if households can service them. However, it raises concerns that access to credit may translate into future cohorts of middle-income New Zealanders not making adequate provision for retirement because easy access to credit may reinforce a tendency to consume today rather than save. For example, people may reach retirement with significant debt that will impact on their living standards.

Student loans

Student loans are now the most common form of debt for young New Zealanders. Initial evidence suggests student loan debt has modest effects on net worth. However, the student loan scheme is still relatively new and most of those with student loan debt are under 35 years of age. How the existence of student loans impacts on the ability to save for retirement is not yet understood.

Home ownership

The risks and opportunities also relate to wider changes in the economic and social environment. A key emerging risk is the decline in home ownership. High levels of mortgage free home ownership on retiring, something that may not be the case in the future, contributes to the adequate living standards of those currently retired. The interaction of home ownership and financial provision for retirement will need to be closely monitored and researched.

Changes in family structure

The trend for later child bearing combined with the increased longevity of older people may result in increasing numbers of people who have both dependent elderly parents and children to care for at the same time.

Longer working lives

The most notable emerging opportunity is the increasing participation of older New Zealanders in the labour force. This will contribute to improved living standards for those entering retirement. Understanding the extent of, and factors that lead to, increased labour market participation in older age requires further monitoring and analysis.

Attitudes

Another important opportunity is the changing attitude to old age. There is an increased blurring of life-stage and life-style, and baby boomers show every intention of ageing disgracefully. An active older population will contribute positively to living standards in the future and this should be facilitated and encouraged.

Recommendations

The analysis that follows results in PRG2003 recommending that:

- The Retirement Commission take responsibility for co-ordinating the ongoing monitoring of risks and opportunities to private provision, initially focussing on:
 - the impact of increasing financial liabilities on private provision for retirement
 - the impact of student loans and home ownership on private provision for retirement
 - the impact of labour force participation by those aged 65 plus on net worth, retirement income and decisions to retire.
- We need ongoing data and research to give estimates of net worth at different points in time. The Household Savings Survey has been an important step forward, but only a first step, and should be repeated. This would enable the analysis of cohort effects (such as the impact of household debt) and ongoing patterns of saving, and the testing of policy changes on savings behaviour.
- A research fund, managed by the Retirement Commission with guidance from an independent panel of experts to be appointed by the Retirement Commissioner, is established to extend and develop research on household saving behaviour.

Factors that determine the living standards of older New Zealanders

The research on the living standards of older New Zealanders investigated the factors that may lead to a variation in older people's living standards.¹³ More detail on the living standards survey is set out in Appendix C.

The research findings suggested that an accumulation of factors reflecting a person's current circumstances and previous life history, rather than one single factor such as annual net income, determined a person's living standards in older age.

The following factors were identified as contributing to diminished living standards:

- lower levels of net annual income
- lower levels of savings and investment
- high accommodation costs (mortgage and rental payments)
- increased exposure to economic stresses in the last year (such as the replacement of household appliances, major house maintenance, large car repair bills, and funeral costs)
- Māori ethnicity¹⁴
- Pacific ethnicity
- lack of formal educational achievement
- low socio-economic status occupation when aged 50 to 59 years.

The research highlighted the importance of pre-retirement policies, including encouraging savings and investment during a person's working life to meet their economic needs in older age and developing social policies to ensure high levels of employment and adequate income levels over the life course before retiring age. These findings also emphasised the need to consider any major cohort differences in terms of people's capacity to accumulate assets over their working lives.

Of particular relevance to the cohort of New Zealanders aged 65 years and over in 2000 are the government housing policies of the 1930s to 1970s, which supported home ownership through subsidised loans.¹⁵ The research on the living standards of older New Zealanders found that, of the five percent who had quite marked material hardship, at least half reported having no savings or assets, paid rent or mortgage, were exposed to economic stresses when aged 50 to 59 years and had no formal qualifications.

13 Fergusson D et al (2001)

14 Ethnicity data was coded to one prioritised ethnicity code, such that if a person identified with more than one ethnic category, the following priority order was used: Maori, Pacific people, other, European.

15 Ferguson G (1994)

The contribution of private provision to living standards in retirement

For the current population of older people, it is possible to demonstrate the importance of private provision in preventing hardship by considering the level of hardship among those who lack such provision.¹⁶

For the present purposes, lacking private provision is defined as:

- having no income in addition to NZS
- living in accommodation that is rented in the private market and
- not having financial assets that exceed \$1000 in total value.

For the group of current older people who do not have any of these types of private provision, 31 percent are in hardship, compared with less than seven percent of older people generally; that is, not having private provision of any of the types specified is associated with a four-fold increase in the likelihood of hardship.¹⁷

The more types of private provision an older person has, the lower is the likelihood of hardship. Those who lack any type of private provision have 13 times the likelihood of hardship compared to those who have all three types of provision.

Risks and opportunities for future cohorts of older New Zealanders

In this section, we identify risks and opportunities that may impact on future cohorts' savings behaviour. While we conclude that there is no savings crisis, there is no room for complacency and the identified risks will require close monitoring in the future.

Measuring and understanding household savings is a complex issue. With the completion of what we hope is just the first Household Savings Survey, we had a lot more information about savings than at the time of the PRG1997.¹⁸ In addition, the Reserve Bank series of household assets and liabilities data also provides a useful time series perspective.¹⁹ Additional analysis of the Household Savings Survey data is presented in Appendix B.

We also commissioned the New Zealand Institute for Research on Ageing (NZiRA) at Victoria University to provide a report on the emerging social and economic trends that may have an impact on future cohorts.²⁰ The NZiRA analysis, combined with a paper prepared for us by the Ministry of Social Development on living standards, identifies a range of emerging trends.²¹ These trends show a very different context and working life pattern for future cohorts of older New Zealanders than those experienced by the current generation of older people.

16 Ministry of Social Development (2003a)

17 Hardship is defined as ELSI scale, level one to level three. Around 9 percent of the 65 and older population fit the definition of no private provision, as used in the paper. The 31 percent with 'no private provision' who are in hardship make up about three percent of the 65 and older population.

18 Statistics New Zealand (2003b)

19 See Thorp C and Ung B (2002)

20 New Zealand Institute for Research on Ageing (2003)

21 Ministry of Social Development (2003a)

Risks

Adequacy of retirement savings

It is widely believed that people typically do not save adequately for retirement. However, there is no unique measure of adequacy, and even if there were evidence people were making inadequate savings, it might simply be that these individuals had decided not to save 'adequately'.

Using the 2001 Household Savings Survey data, Scobie and Gibson made an initial attempt to answer the difficult question: are retirement savings adequate?²²

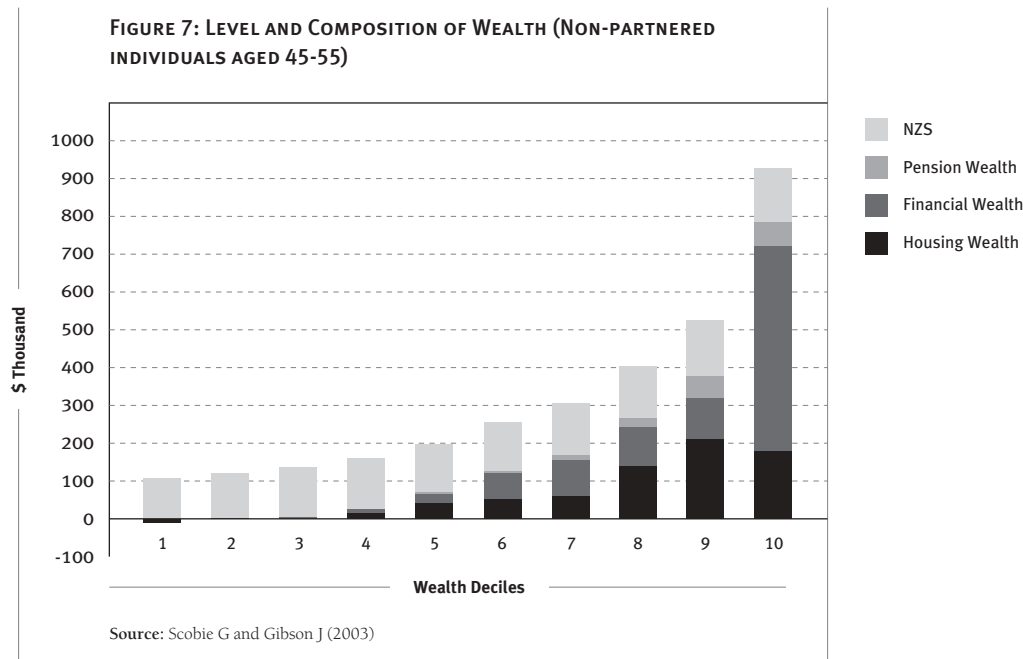
Their approach was to estimate the potential retirement income based on the observed levels of asset accumulation of 45 to 55-year-olds at the time of the survey. From that, they have derived the implied saving rate for maintaining post-retirement consumption at pre-retirement levels.

After allowing for the income from NZS, they estimated what stock of wealth at retirement would be needed to achieve a given level of consumption smoothing, and then they estimated the saving rate needed until retirement to achieve that goal. They found a wide variability in this prescribed saving rate across both income and wealth levels. However, some initial evidence suggests the prescribed saving rates are consistent with the actual pattern of saving we observe among households aged 45 to 55.

Accepting their definition of adequacy, they found no significant evidence of gross under-saving for retirement by New Zealand households in this age cohort. This, of course, does not mean some individuals might be saving at a rate that they may later come to view as too low. There is undoubtedly a distribution of individuals at every wealth level with some saving below the prescribed level and others above the level. But for the cohort as a whole, the evidence does not appear to support a claim that New Zealanders aged 45 to 55, as a group, are under-saving.

Their analysis also illustrates the importance of NZS when any decisions are made about the adequacy of retirement savings. Using the 2001 Household Savings Survey data, Scobie and Gibson calculated future retirement wealth of the cohort aged 45 to 55 and broke this down by housing wealth, financial wealth, private pensions plus the expected value of future NZS payments. See Figure 7.

²² Scobie G and Gibson J (2003)



Their analysis indicates that for the lowest 40 percent of the income distribution in the 45 to 55 cohort, 90 percent of their total wealth in retirement will come from NZS. They conclude this evidence suggests that, among the lowest 40 percent of the income distribution, lifetime welfare would be reduced if these groups were to increase their current savings and reduce their pre-retirement consumption. Those in the top deciles appear to be making adequate provision for their retirement.²³

Consequently, it is middle-income New Zealanders who are our key concern in terms of risks and opportunities in relation to the private provision of retirement income. They have some capacity to make private provision for retirement and, if they don't, many are likely to experience a significant fall in living standards on retirement.

We need ongoing data and research to give estimates of net worth at different points in time. The 2001 Household Savings Survey has been an important step forward, but only a first step, and should be repeated over time. This would enable:

- cohort effects to be monitored, such as the impact of household debt
- estimates to be made of household savings rates
- policy changes on savings behaviour to be tested.

Increasing household liabilities

A feature of the household net wealth data is the major and continuing increase in household liabilities. The Reserve Bank household asset and liability data shows the changes in net wealth of New Zealand households over the last two decades.²⁴ Table 2 presents the data in real terms, so that the relative values of household asset, liability and wealth categories can be more easily followed over time.

²³ A decile refers to the population being ranked from lowest to highest net worth and then divided into 10 even-sized groups where decile 10 is the highest. Net worth equals the total value of assets less the total value of debts.

²⁴ Thorp C and Ung B (2002)

TABLE 2: REAL NET FINANCIAL WEALTH AND NET WEALTH*\$ Billion, 1980 values*

As at December	1980	1985	1990	10 year growth	1995	2000	10 year growth
Total household financial assets	21	27	27	32%	34	38	39%
Household financial liabilities	7	8	11	48%	16	24	129%
Household net financial wealth	13	19	17	23%	18	13	-19%
Housing value	29	40	43	47%	53	58	37%
Household net wealth	42	59	59	40%	71	72	21%

Source: Thorp C and Ung B (2002)

The main cause of increasing household liabilities has been attributed to the financial liberalisation of the mid-to-late 1980s. These reforms enhanced households' abilities to access credit.²⁵ Changes included:

- reforms that directly affected financial institutions, such as the removal of interest-rate controls, compulsory reserve ratios and credit guidelines
- macroeconomic reforms giving better access to overseas credit and opening New Zealand's financial markets to foreigners.

Changes and innovations in the mortgage sector have also improved households' abilities to purchase houses and access home equity, such as lowering the down payment required by homebuyers and 'revolving credit' type mortgages that also serve as cheque accounts that can be used to pay day-to-day expenses and access credit at mortgage rates.

We do not know whether the factors driving the increase in household liabilities will translate into future cohorts not making adequate provision for retirement. The continuing increase in debt raises concerns that access to credit may translate into future cohorts of middle-income New Zealanders not making adequate provision for retirement, because easy access to credit may reinforce a tendency to consume today rather than save.

Households are still adjusting to the impact of financial liberalisation and it is not clear yet how it will impact on private provision for retirement. This is a key area that will need close monitoring.

Student loan debt

Student loans are a contentious issue. It is not surprising that there is considerable focus on the possible negative effects that student loans have on students well after they have completed their study.

It should be noted when considering net worth data that student loans, unlike other debt types (such as mortgage debt), have no corresponding easily measured asset. It is an investment in the borrower's human capital. This means that no real asset is measured to balance the resulting debt. In contrast, those with a mortgage will have a housing asset.

²⁵ Hull L (2003)

According to the 2001 Household Savings Survey, student loan debt is only about five percent of total household debt.²⁶ It shows that 21 percent of all non-partnered individuals reported having a current student loan, while the figure for couples was 10 percent. While student loan debt makes up a relatively small percentage of total debt across the whole population (five percent), it is a particularly significant debt for certain sub-groups of the population; particularly those aged 18 to 24. Approximately 40 percent of people within this age band had a student loan debt.

In addition, the 2003 Student Loan Scheme Annual Report shows that:²⁷

- the total outstanding debt was \$5.267 billion for 390,027 people
- the average student loan outstanding is about \$13,500
- fifty-two percent of borrowers had a loan balance under \$10,000
- the amount borrowed is forecast to increase by 5.6 percent a year over the next four years.

Gibson and Scobie, in an initial analysis of the 2001 Household Savings Survey data, explored whether student loans made a difference to net wealth across households.²⁸ The study found that:

- a student loan had no clear effect on the net worth of couples but, for non-partnered individuals, net worth was approximately \$15,000 lower
- the presence or value of a student loan had no effect on the probability that a couple had a mortgage but, for a non-partnered individual, there was a negative effect
- a student loan had no effect on the value of mortgages held by couples but, for non-partnered individuals, there was a negative effect
- the presence or value of a student loan had no effect on the number of children a couple had.

While this study shows a student loan appears to have some modest effects, certain groups will face difficulties that could impact on their ability to save for retirement. The 2003 Student Loan Scheme Annual Report estimates the average repayment period at 9.5 years, but females and non-Europeans have longer-than-average repayment periods.

Although the analysis of Gibson and Scobie shows student loan debt has a modest impact, it is early days yet. The student loan scheme is still relatively young. Many of those with student loan debt have not yet reached the age where we expect them to be at their peak savings period, at about 40 to 50 years of age, when income levels are at their highest. Even though the student loan debt reality is that most students leave tertiary education with moderate debt, the psychology of student loan debt means that individuals may defer savings longer than they might otherwise do. As a consequence, we will need to continue to monitor the impacts of student loan debt for future cohorts.

²⁶ Statistics New Zealand (2002b)

²⁷ Ministry of Education et al (2003)

²⁸ Gibson J and Scobie G (2003)

Home ownership

Accommodation costs are one of the key factors that determine the living standards of older New Zealanders. The Living Standards Survey shows that those paying higher accommodation costs, renters, were relatively disadvantaged compared to those with low accommodation costs, homeowners.²⁹

The emerging trend for future cohorts of older people is of reduced home ownership, particularly for those with low incomes. This trend is shown in Table 3. The decline in ownership appears to reflect a complex mix of social and economic factors, including a shift in consumption away from housing, later marriage and an increase in the number of single people, increased mobility and the reduced affordability of houses for low-income families.

TABLE 3: HOME OWNERSHIP OF HOUSEHOLDS

	1991	1996	2001
All households	74%	71%	68%
Couples without children	82%	79%	78%
Couples with dependent children	81%	76%	74%
Couples with children (all ages)	83%	79%	76%
Sole parents with dependent children	54%	46%	42%
Sole parents with children (all ages)	60%	53%	49%

Source: Statistics New Zealand, 2001 Census 'Families and Households' tables

The decline in house ownership occurred across all household types. The sharpest decline was among single parent households with dependent children.

This decline in home ownership suggests that current working age cohorts may need to have increased alternative asset accumulation or income available to offset higher accommodation costs in retirement. A continued decline in home ownership without an increased alternative asset accumulation would be a cause for concern in the future and warrants close monitoring.

Increased changes in partnership status

Future cohorts of older New Zealanders are more likely than the current cohort of older people to have experienced separation and divorce and to have cohabitated. This suggests a more disrupted pattern of asset accumulation than for the current cohort of older people and the need for a higher level of overall asset accumulation to offset the additional transaction costs of relationship breakdown.

Later child bearing

The trend for later child bearing combined with the increased longevity of older people may result in increasing numbers of people who have dependent elderly parents and children to care for at the same time. This will place expenditure demands on people later in their working lives during a period when consolidation and key asset accumulation may have occurred for the current older population.

²⁹ Fergusson D et al (2001)

Offsetting this risk is the fact that future cohorts are likely to have fewer children. This suggests a reduction in expenditure demands and an increased capacity for asset accumulation during working life.

Opportunities

Workforce changes and educational experience

The labour force in New Zealand has undergone significant changes over the last decade. There has been a strong increase in workforce participation by men and women aged 60 to 64, which largely reflects changes in the age of eligibility for NZS. While beyond age 65 few people remain in paid work, the number in paid work has doubled over the last decade. These trends for older people are important, as workforce participation past the age of 60 makes a significant contribution to living standards in retirement.

Future cohorts of men and women will have higher educational achievements than the current older population. At present, around a third of people over the age of 60 have no educational qualifications, but this applies to only 15 percent of people in their twenties. Higher levels of education will not only afford people wider paid work opportunities, higher incomes and greater financial knowledge; they may mean that people will be more inclined to continue studying as they move into later life.

The future environment raises increasing possibilities for older people who wish to continue working, perhaps moving gradually from full-time to part-time work. The workforce is ageing rapidly as smaller cohorts follow the baby boom bulge through the population. By mid-century, based on present assumptions about participation, growth in the labour force is expected to be negative. Labour shortages can be expected and skills shortages are already emerging in many areas. This suggests greater attention should be paid to maximising the potential of older workers.


Attitudes

The NZiRA paper prepared for PRG2003 notes that much has been said and written about the different attitudes baby boomers will bring to their later life. Although this is only speculative, we can see some of the indications already. There is a blurring of the life-stages in lifestyle and consumer behaviour. Different generations are buying the same brands and products and enjoying similar types of entertainment and popular culture.

Advertisers who look at the older generation as made up of a mid-life crisis followed by 20 years of compliant serenity are in for a rude shock.

Peter Biggs, NZiRA Seminar 2002

Retirement itself may become an out-dated term. Older people may be actively working or actively 'recreating' to a much older age. This will depend on staying healthy well into old age and on the financial means available. Many older people already remain keenly involved in community life after retirement and make significant contributions to the wellbeing of others, which is sometimes overlooked in the discussion of ageing as a 'burden'. They contribute as unpaid workers, as mentors, as creative artists and, perhaps most pervasively, as grandparents and 'kin-keepers'.



**CHAPTER THREE
AN AGEING POPULATION:
THE FISCAL PRESSURES**

CHAPTER THREE

AN AGEING POPULATION: THE FISCAL PRESSURES

Private provision for retirement cannot be viewed separately from public provision, since much of the composition and magnitude of private provision in New Zealand is shaped by the existence of publicly funded and provided income and services. How much New Zealanders with discretionary income actually save for their retirement is affected by their expectations about the future level of NZS and the age at which they'll receive it.

The ageing population creates pressure on the long-term sustainability of NZS. The two main fiscal pressures arising from this older population will be increased spending on NZS as a proportion of GDP, and rising health costs. Total expenditure on net NZS and health is expected to rise by 9 percentage points of GDP by 2051.

The NZ Superannuation Fund is the Government's main tool for meeting the increased fiscal pressures created by an ageing population. However, without increased contributions to the Fund it cannot cover all future increases in NZS funding requirements. Also it is not designed to accommodate the increasing need for health spending. Future Governments will need tools in addition to the NZ Superannuation Fund to address the increasing fiscal pressures.

Unlike many countries facing similar issues, these fiscal pressures are not immediate in New Zealand. We have a window of opportunity before the baby boomers start claiming NZS in increasing numbers in the middle of the next decade. PRG2003 would like to see an open and informed discussion about future retirement provision. The discussion needs to focus on options that are appropriate and sustainable. The options include: maintaining NZS for future retirees at current levels but increasing taxes or reducing other expenditure; considering the age of NZS entitlement; changing the way NZS rates are set; and targeting NZS.

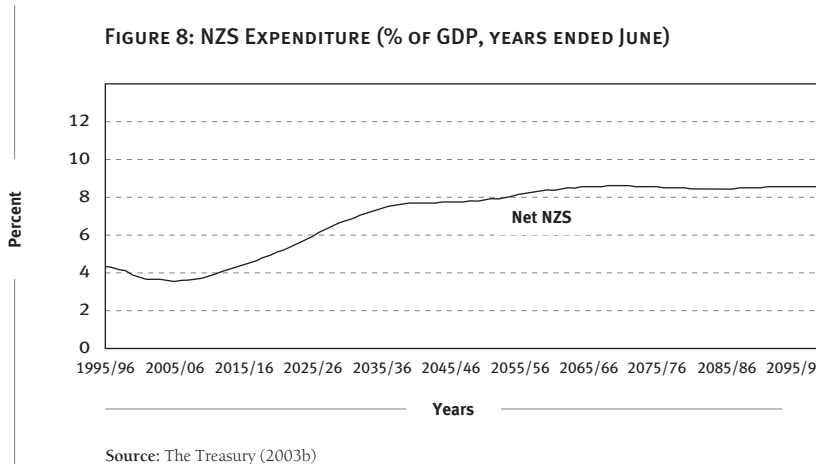
It is not within our remit to advocate any particular option or combination of options, but we do emphasise that in the future any changes made to address the fiscal pressures, should be made prospectively. Those already receiving NZS, and those approaching retirement, should not have their entitlements changed.

Long-term fiscal projections

Treasury's long-term fiscal projections prepared for the PRG2003 show that New Zealand is passing through a 'trough' in its ratio of NZS to GDP spending because of previous changes to NZS, as shown in Figure 8. This ratio will begin to rise after the middle of this decade. The ageing population will also lead to major increases in health expenditure, meaning that total age-related spending is expected to rise substantially.

The ageing population will create some fiscal gains, such as reduced spending on primary and secondary education, family support for children, benefits for working age people, and law and order. However, the combined rise in NZS and health spending will more than offset these gains.

The Treasury projections show that NZS costs net of tax are projected to rise from 3.6 to 7.8 percent of GDP between 2002/03 and 2050/51.



Over the same period health spending is expected to rise from 6.3 to 11.1 percent of GDP. After allowing for some demographically linked cost savings elsewhere, total core government spending excluding debt service is expected to rise from 30.4 to 37 percent of GDP. This is an increase of over 20 percent in funding requirements to be met from revenues. The extent to which this requires a corresponding rise in average tax rates will also depend on other factors such as the level of public debt and the balances in the NZ Superannuation Fund.

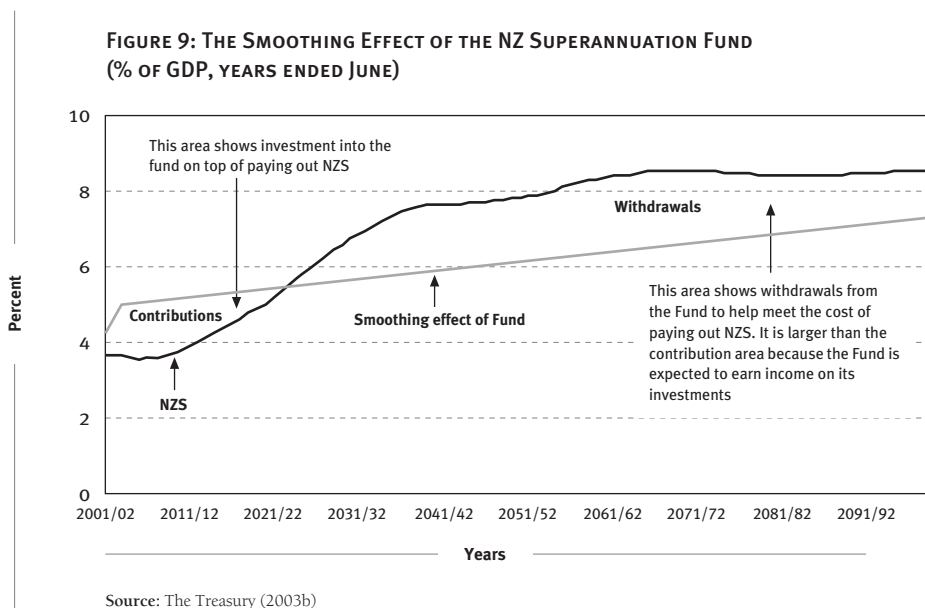
NZ Superannuation Fund

The NZ Superannuation Fund makes a contribution towards easing long-term fiscal pressures. It can be described as providing partial tax smoothing to accumulate surpluses to fund part of the future cost of NZS.

Partial tax smoothing involves keeping tax rates above the level needed to fund current spending in order to reduce the need for higher taxes or reduced expenditure in the future. A currently favourable fiscal situation has allowed significant amounts to be channelled into the Fund without requiring tax increases. See Figure 9.

However, the Fund has a 40-year time horizon. On current projections, it will begin paying out money during the 2020s. The Fund won't completely avoid the need for increased taxes or reduced expenditure. By 2040 the Fund is projected to fund 29.5 percent of the cost of NZS.³⁰ After this the proportion financed by the Fund earnings will begin to decline as NZS costs continue to rise.

³⁰ This includes tax receipts from the Fund



As we identified in Chapter One there is confusion about the role of the NZ Superannuation Fund. We think the Retirement Commission and the guardians of the Fund will have an important part to play in ensuring that the role of the Fund is understood by all New Zealanders.

Options in addition to the NZ Superannuation Fund

The partial tax smoothing approach taken by the NZ Superannuation Fund reduces the scale of the need for future tax increases or expenditure reductions. However, without increased contributions to the Fund it cannot cover the increasing fiscal pressure from future increases in NZS funding requirements. It is also not designed to accommodate the increasing need for health spending. Future Governments will need options in addition to the NZ Superannuation Fund to address the increasing fiscal pressures.

PRG2003 expects the best solution will be a combination of the options outlined below - a combination that is likely to change over time. The options chosen by future Governments should not affect people already retired or close to retirement age.

Submissions to PRG2003 reflected that each of these options is contentious, and that there are strong and divergent views on each option's relative benefits. It isn't within our remit to analyse the options but we do emphasise the need to have an informed discussion on the issue.

If NZS is to be maintained in its current form, it will require increased taxes and/or reduced expenditure to provide the necessary revenue. However, neither is popular. Tax increases may impede economic growth and reduce the disposable income from which people save, and thus impede private provision. Reducing expenditure is likely to be difficult. It is not easy to cut back on health and other services voters have come to expect, particularly given that increased fiscal pressures will also occur in relation to other social services.

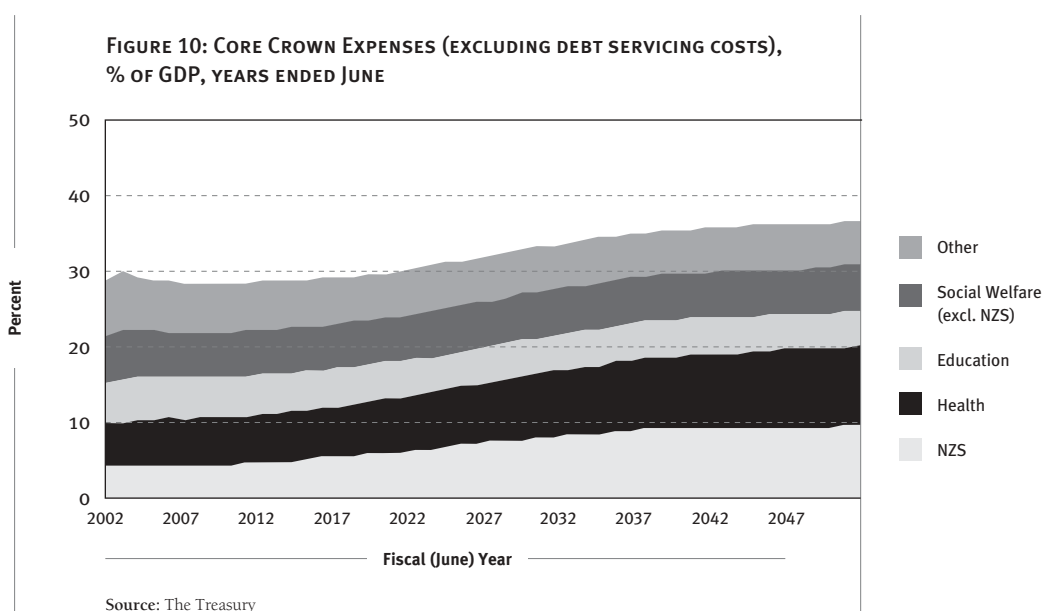
Other options for addressing the medium term fiscal pressures include:

- Altering the age of entitlement to NZS, by either increasing the age or possibly making the age of full entitlement to NZS more flexible. We recognise that working after the age of 65 is easier for people in non-manual work and in good health. If future Governments change the age of entitlement, they will need to make provision for low-skilled and manual workers who are unable to continue work and have no other income.
- Altering the way NZS rates are set. Options that could be considered include the link to wages and the pension to wage ratio.
- Targeting NZS entitlements against other income or assets. This has equity arguments in its favour, but this approach has proved extremely unpopular in New Zealand.

All these options will require an informed public debate and support before the Government considers changing NZS entitlements in future.

Reporting on long-term fiscal pressures

As the previous sections highlighted, the fiscal pressure arising from the ageing population is not limited to retirement but also includes health related expenditure. The cumulative effect of the increasing fiscal pressure is highlighted in Figure 10. The Figure shows the gross cost of NZS. The net cost of NZS will be funded by withdrawals from the NZS Fund and tax revenues.



PRG1997 recommended the Government “include in the fiscal strategy reports, statements of fiscal policy intents for addressing prospective demographic and other pressures beyond the ten year minimum period currently specified in the Act.”³¹

We welcome the recently announced proposed amendment to the Public Finance Act that will require Treasury to report every four years on long-term fiscal pressures.³²

Direct deduction policy for overseas pensions

When a NZS recipient also receives a public pension from overseas, New Zealand’s policy is to deduct the amount of the pension from their NZS.

Not surprisingly, submitters to PRG2003 who are affected by this direct deduction policy consider that no such deductions should be made. They stated that these pensions should be regarded as similar to employer superannuation schemes or other forms of private saving.

This is a very difficult issue that has not been resolved. PRG2003 understands the issue is under ongoing review by the Ministry of Social Development. However, PRG1997 also noted the issue was under review, and little visible progress has been made in the last six years. We would like to see substantive progress made on this issue.

31 Periodic Report Group (1997)

32 <http://www.beehive.govt.nz/mallard/public-finance/index.cfm>



CHAPTER FOUR WORK-BASED SAVINGS

Overview

Our terms of reference require us to consider mechanisms for Government, employers and the savings industry to work collaboratively to promote employer-based superannuation.

Work-based savings are a key element of retirement income policy in many OECD countries. For these countries, work-based savings provide the second tier of retirement income provision, with public provision being the first tier and all other forms of private provision being the third tier. In New Zealand, the emphasis has been on public provision as the primary source of retirement income.

New Zealand does not have a strong tradition of work-based saving and no longer uses compulsion or tax incentives to support work-based savings. Schemes are voluntary for employers to establish and employees to use.

New Zealand membership of work-based savings schemes is considerably less than in some OECD countries. Less than 15 percent of the labour force are members of registered work-based superannuation schemes. Many New Zealanders do not have access to these schemes and those who do often do not take advantage of them even when they receive employer subsidies. Membership tends to be concentrated among executive and salaried staff.

There are a number of reasons work-based savings are traditionally not a strong plank in the private provision of retirement income. New Zealand has a large number of small firms, has changing employment patterns, has seen a shift from pay plus benefits to a total remuneration environment in the private sector and has increasingly competitive retail products. Also, for most employers, the costs of providing and promoting work-based savings outweigh the direct benefits.

We think there is value in promoting greater use of work-based savings schemes as a way for New Zealanders to save for retirement. Such schemes may help to overcome those aspects of human behaviour such as procrastination that may otherwise represent hurdles to starting and continuing to save. Work-based savings schemes provide deduction at source, economies of scale and an avenue to reach a high proportion of the population. They also provide a means for employees to consider their retirement planning decisions and a venue for education. An improved environment for work-based savings will strengthen the current voluntary regime by providing better access to one of the more effective ways to save for retirement.

As employer support for work-based savings increases, so does employee participation. Offering education and information is a first step. Employee participation increases when employers pay fees for administration costs and increases again when there are employer contributions to savings.

The two associated challenges will be to improve participation rates in existing savings schemes and to encourage the spread of new schemes. These objectives will require minimising costs of participation for employers and employees, suggesting a move away from traditional employer sponsored superannuation schemes towards an environment where employers, at a minimum, facilitate access to savings.

Recommendations

The analysis that follows results in PRG2003 recommending that:

- The Government establish a Work-based Savings Group (WSG) to develop an agreed approach to promote work-based savings by the end of 2004.
- The WSG membership should include employers, unions, academic experts, officials, the financial services industry, and be chaired by the Retirement Commissioner.
- The WSG should focus its work programme on:
 - education through the workplace for employees
 - minimising regulatory and compliance costs
 - scheme design and best practice
 - training and resource support for employers and unions
 - sector or industry-wide approaches to facilitating work-based savings
 - reducing the costs for employers to provide access to work-based savings
 - assistance for small employers to encourage work-based savings
 - assistance for those on low incomes to access work-based savings
 - getting employees started saving for retirement.
- The WSG should set milestones to assess changes in the membership of work-based savings schemes.
- The Government consider the possibility of extending the new public service savings scheme beyond the core public service; in particular, providing for organisations in the wider state sector to opt into the new scheme.

DEFINING WORK-BASED SAVINGS

The term ‘work-based savings’ can encompass a wide spectrum of schemes and designs with different levels of commitment by employers and employees.

There are two broad types of schemes. First, a defined-benefit scheme, where benefits are calculated in relation to, usually, the final average salary and years of membership at the date on which a person stops being a member. The employer bears the investment performance risk. New Zealand has few remaining defined-benefit schemes. Second, a defined-contribution scheme, where benefits relate to the contributions paid by, or in respect of, a member (including interest on those contributions). Most New Zealand schemes are defined-contribution.

There are a number of options for those providing a scheme. The employer can establish and manage their own scheme for their employees. Alternatively, there is a range of products available an employer can use; for example, master trusts, which are usually managed by a third party.

Within these different types of schemes employer participation can include:

- providing education and/or information
- providing a payroll deduction facility
- subsidising the scheme’s administration costs
- making co-contributions to the contributions made by an employee.

Of course, there is usually a mix of these features in any work-based savings scheme.

Benefits of work-based savings schemes

Work-based savings schemes are a good form of saving for employees because they:

- deduct savings at source, so savings do not get mixed up with discretionary income
- provide economies of scale: direct deductions are cheap, savings products can be bulk purchased, and the workplace is an efficient and effective way to communicate with scheme members
- may prompt an employee to consider their retirement savings decisions
- present an additional context for savings-oriented education.

The Retirement Commission commissioned an analysis of the 2001 Household Savings Survey to assess the impact of membership in superannuation schemes on net worth.^{33,34} The analysis shows that, for some people, saving in a work-based superannuation scheme appears to increase net worth relative to those who do not save in such a scheme. There appears to be something about saving in work-based schemes involving an employer-based contribution that makes a positive difference to the overall level of net worth. A summary of the results is set out in Appendix E.

Work-based saving provides benefits for employers too: it may help employers keep workers in an increasingly global labour market, it attracts employees, it reduces problems of retiring workers and it makes a 'good employer' in the wider social context of rights and responsibilities in the workplace.

Despite these benefits, the reality is that the costs of voluntarily providing and promoting work-based savings can outweigh the direct benefits for New Zealand employers.

Barriers to work-based savings schemes

There is little doubt that the workplace is an efficient and effective environment for facilitating saving for retirement. The challenge is to minimise costs of participating in work-based saving for both employers and employees.

Barriers for employers

The main barriers for employers are the time and money it costs to make a scheme available and to administer it, to explain the scheme and to promote it to employees, and, in some schemes, to make contributions to administration costs or subsidise savings.

Barriers for employees

Even where employees have access to workplace savings schemes, many do not take advantage of them, for a complex range of reasons. A survey prepared for the Retirement Commission found the barriers to participating in work-based savings schemes are related to people's perceptions of returns from superannuation plans, other financial priorities and their life-cycle stage.³⁵ Characteristics associated with plans were found to be less of a barrier. This indicates that non-participation in schemes partly reflects active decisions by employees to use alternative savings methods, or simply not to save at that particular time.

33 Scobie G and Le T (2003)

34 The Household Savings Survey was a cross-sectional nationwide survey that collected information in 2001 on New Zealanders' assets and debts. The survey looked at the stock of savings, the total value of assets less the total value of debts, described as 'net worth' in the survey.

35 ACNielsen (2003)

Other barriers to work-based savings for employees include a natural tendency for people to procrastinate about joining a work-based savings scheme, a lack of knowledge and information about work-based savings, and employers not telling employees about a scheme to minimise costs.

Scheme design can put employees off, especially if the scheme has a long vesting period, restricted access, limited ability to maintain membership during broken employment, eligibility criteria to do with minimum periods of employment, and the inability to accept small contributions.

Although the unions support efforts to encourage work-based savings, there is some reluctance from employees and unions to trade off future increases in wages and salaries for employer contributions to a savings scheme.³⁶ In the current environment, work-based saving is likely to be down the queue of bargaining priorities.

The extent of work-based savings in New Zealand

There is limited data available on work-based savings in New Zealand. The primary data is from the Government Actuary. We supplemented this with a survey we commissioned from the ESR Consortium and additional analysis of the 2001 Household Savings Survey data. A summary of the analysis is presented in Appendix D.

From the available information, we concluded that:

- Many New Zealanders do not have access to work-based savings, and those that do often do not take advantage of them even when they receive subsidies from their employers.
- Among small firms, access is likely to be low. A large number of New Zealanders are employed in these firms.
- Membership is concentrated among the salaried and professional staff. If work-based savings are to play a greater role in retirement saving, membership of both new and existing schemes will need to be widened beyond this group.
- While work-based savings have been in decline for the last decade, more recently, membership in workplace schemes has stabilised.
- Among the largest employers, there is a more access to schemes than we had anticipated.

³⁶ Harris P (2003)

Increasing participation in work-based savings

We think there is value in promoting greater use of work-based savings schemes as a way for New Zealanders to save for retirement. Work-based schemes are a good form of saving for employees because they deduct savings at source and provide economies of scale.

We recognise that revitalising work-based savings is a difficult task, but an improved environment for work-based savings will strengthen the current voluntary regime by providing better access to one of the more effective ways to save for retirement.

For real progress to be made on work-based savings, there must be ownership of an agreed approach by all interested parties. The challenge is to move to a virtuous circle where all interested parties have an incentive to advance the participation in work-based savings.

We suggest that the Government establish a Work-based Savings Group (WSG) chaired by the Retirement Commissioner to bring together employers, unions, academic experts, officials and the financial services industry to develop an agreed approach to promote and develop work-based savings by the end of 2004. The approach developed by the WSG should be consistent with the current voluntary approach to the private provision of retirement income.

The WSG should set milestones to assess the changes in membership of workplace savings schemes.

This approach could potentially provide the circuit breaker that is needed to translate the good intentions of interested parties into more employees participating in work-based savings.

We hope the following outcomes will emerge from the proposed approach:

- from employees, an increased awareness of the value of work-based savings and a consequent increased participation
- from employers, a baseline provision of direct deductions for contributions to work-based savings, the promotion of work-based savings within firms, and the opportunity for time to access education related to retirement savings
- from unions, that they be an initiator, promoter and educator and, where practical, a direct negotiator for employer contributions
- from the financial services sector, the creation of more innovative and flexible savings schemes that facilitate access to saving through the workplace
- from the Government, leadership by example, a supportive regulatory and neutral tax environment, and investment in education and information for employees and employers.

We acknowledge there have been attempts in the past to encourage work-based savings. In particular, the Retirement Commission, with help from Business New Zealand, developed a programme to publicise and facilitate savings in the workplace and included a video-based seminar for employees.

Employers met the programme with good intentions but a lack of action, partly reflecting the limited resources available for the programme. This highlights the importance of taking a wider approach to the issues, such as through the WSG, and of having the resources available to put in place any proposals developed by the WSG.

The basis for a working group is already in place

Employers, unions, Government and the finance industry have all recently shown a strong interest in addressing the issue of work-based savings:

- The ESR Consortium study asked employer participants if they have a role to help employees to save for retirement.³⁷ The responses were generally positive. Employers were favourably disposed towards providing information and education, and access to employer-endorsed, but not subsidised savings.
- A report we commissioned on the role of unions in work-based retirement savings noted that unions are aware and supportive of efforts to bolster retirement savings.³⁸ Also, unions have the will and capacity through their networks to be advocates for retirement saving. However, they lack confidence and technical knowledge about superannuation.
- Industry representative bodies such as the Investment, Saving and Insurance Association (ISI) and Association of Superannuation Funds of New Zealand (ASFONZ) have a strong interest in growing work-based savings, and have also been actively promoting debate about savings policy, most recently through the Saving New Zealand Forum held early this year.³⁹

There is also an informal group that meets to consider savings policy issues. The Retirement Commissioner chairs the group and the members are Business New Zealand, the Council of Trade Unions, ISI and ASFONZ. This might form the core of the proposed WSG.

Work programme

We recommend the Work-based Savings Group's work programme focus on the following issues.

Education through the workplace

The group needs to develop an education and information campaign to underpin its approach. A range of education and information initiatives is detailed in Chapter Five 'Personal financial education and information on private provision'.

Regulatory and compliance costs

The options developed by the WSG should aim to minimise the compliance and regulatory costs imposed on employers.

The key concern for employers with existing work-based savings schemes is the cost of complying with the regulatory regime. Employers are particularly concerned about the requirement to maintain a prospectus for the schemes. These issues are dealt with more fully in Chapter Eight 'Financial services and market regulation'.

³⁷ ESR Consortium (2003)

³⁸ Harris P (2003)

³⁹ www.isi.org.nz

Scheme design and best practice

Work-based schemes will need to become more flexible to meet the needs of an increasingly diverse workforce. The traditional non-portable employer-sponsored schemes, designed for long-serving executives and salaried staff, are less likely to meet the needs of future savers.

The labour market has moved away from the model of full-time 'jobs for life' to a more diverse working model. Increasing numbers of men and women follow a diverse pattern of employment that accommodates child rearing, mid-life career changes and longer periods of study.

The Women in Super submission raised a number of scheme-design issues that the proposed WSG needs to consider in the wider context of scheme design. These include:

- Portability. Without portability it will be hard to encourage more employees to participate in work-based savings. Future schemes may require products close in design to existing retail schemes, but accessible through the workplace.
- Employer subsidy. The extent and nature of employer subsidy can make a significant difference to the participation in a scheme.
- Choice and flexibility. Work-based schemes will need to provide members with sufficient choice and flexibility to accommodate their changing circumstances.
- Shorter vesting periods. Long vesting periods are likely to discourage membership among an increasingly mobile and diverse workforce. Nearly half of all current work-based schemes have vesting periods of over five years.
- Eligibility criteria. Criteria such as two-year minimum periods of employment and the exclusion of part-time and non-executive staff limit participation.
- Rollover provisions. When employees leave a workplace, they often have to cash up a scheme rather than simply roll it over into another scheme. Rollover provisions would help maintain continuity of savings in an environment of increased mobility.
- Shorter qualifying periods. Providing a short qualifying period for an employee joining a firm encourages take-up. When the qualifying period is extended beyond recruitment, take-up tends to be much lower. Recent analysis in the US suggests that automatic joining, which requires the employee to decide to opt out of a scheme, also encourages take-up. Participation rates are markedly lower when employees choose whether to join the scheme, rather than whether to opt out.⁴⁰

We recommend the proposed WSG develop best-practice guidelines for work-based schemes, as a guide to both existing schemes and new schemes. The proposed guidelines should draw on the experience of existing successful work-based schemes and should also cover trustee and governance arrangements.

There may also be value in concentrating some effort on the larger employers as a 'testing ground' approach. One objective would be to maximise the benefits to employers and employees of existing savings schemes. Another objective would be to determine if such schemes could be successful in a favourable environment before moving to the more difficult setting of smaller employers.

⁴⁰ See: Madrian B et al (2000), Choi J et al (2001a), Choi J et al (2001b)

Training and resource support

We suggest the proposed WSG develop options to provide training and resource support to employers and unions, perhaps through the Retirement Commission.

Employers and unions rarely have the time or the resources to commit to understanding the complexities of work-based savings. Providing training and resources would facilitate increased participation in work-based savings.

Training and resource support may also help the development of advocates for work-based savings. Anecdotal evidence shows that many of the more successful work-based schemes have a strong commitment from employers and individual employees or union officials, who champion saving within their organisations. Advocates actively promote the schemes to new staff members and often advocate retaining superannuation benefits in wage negotiations.

Sector or industry-wide approaches

PRG2003 considers there is potential for industry or sector-wide approaches to encourage employee participation in work-based schemes.

A recent example of an industry-level initiative is the discussion on establishing a new retirement savings scheme in the public service and related departments, in the compulsory education sector, and for kindergarten teachers.

In particular, an industry-wide approach could:

- encourage industry and sector-level collaboration around constructing savings schemes
- reduce employer resistance to being placed at a competitive disadvantage by bearing the extra cost of providing work-based savings
- remove retirement savings from bargaining over wages and other conditions of employment, and create some distance in the trade-off between wages and superannuation entitlements
- allow employers and unions to pool expertise and share the costs of accessing expertise.

Assistance for small employers

Recent analysis of the dynamics of small firms highlights their importance in New Zealand and their impact on the labour market.⁴¹ New Zealand has a very high ‘turnover’ of small firms, resulting in high employment turnover within these firms.

Despite these challenges, PRG2003 considers there may be ways to encourage work-based savings through small employers. Particularly relevant is scheme design that allows portability for individual employees.

The Government’s recent discussion document “Making tax easier for small business” recognises that compliance costs impact on small firms’ ability to survive and thrive.⁴² The document suggested a subsidy to encourage small employers to use payroll agents to help with the compliance costs associated with tax obligations, such as having to deduct PAYE, child support and student loan repayments from staff wages.

41 Carroll N et al (2002)

42 www.taxpolicy.ird.govt.nz/publications/files/html/makingtaxeasier/index.html

The subsidy would pay the payroll agency fees for up to, say, five employees of a small business. The subsidy would stop being available when employees' PAYE and Specified Superannuation Contribution Withholding Tax (SSCWT) deductions exceeded \$100,000 per annum.

Under the proposal, the employer would pay the gross wages to the payroll agent. The payroll agent would deduct the PAYE and other deductions from the gross wages and pay the net wages to each employee each pay period. The proposal would be optional for employers. We think this proposal could be extended to cover employee contributions to a savings scheme.

Assistance for those on low incomes

We recommend the WSG work programme include a review of approaches to providing low-income savers with access to low-cost savings vehicles that can accommodate small levels of contributions.

People on low incomes provide a particularly difficult challenge. They have limited disposable income from which to save and often work in relatively insecure jobs. Expecting them to save is often unrealistic. While NZS will provide a reasonable replacement income in retirement for this group, even a small amount of savings can improve living standards in retirement.

A good starting point for the review might be to consider the Industry Retirement and Insurance Scheme (IRIS) established by the distribution and service sector unions. Even very small employer contributions - for example, covering the \$1.50 weekly administration fee, and/or covering the small weekly death benefits cover - was seen as sufficiently attractive to commit to the minimum \$5 a week contribution. Over time, the balances have built up to levels that workers on these low and often part-time incomes would never have imagined achievable.

Getting employees started saving

We recommend the proposed WSG review whether a kick start is likely to encourage additional savings for retirement and, if so, whether it could be integrated with work-based savings and potentially applied more widely to retail schemes.

A 'kick-start' would aim to encourage participation in savings schemes by providing a bonus at the end of each of the first few years to those who stayed in their scheme. The objective would be to encourage a savings habit.

A barrier to employees participating in workplace schemes or retail savings schemes is procrastination. The incentive to act today is weak for many of us. We concluded that there might be merit in investigating a modest kick start for savings to overcome initial procrastination.

We could use the kick start as a signal to remind people of the importance of savings.

The advantages of this approach include:

- it is a one-off reward, unlike the recurring nature of an annual tax break
- it is likely to be less fiscally costly than a tax incentive
- it is focused on one of the key barriers to saving, getting started
- it is a lump sum and so avoids the inequities of many tax incentives that tend to favour those on high incomes.

There are, of course, potential disadvantages, including the fact that it may result in a substitution of existing saving rather than the generation of new saving.

Work-based savings in the public sector

A significant new initiative in work-based savings was the November 2003 announcement of the Government's intention to set up a new voluntary contributory retirement saving scheme for government employees. The proposed scheme, which incorporates an employer subsidy, is the most important retirement income development for government sector employees since the Government Superannuation Fund was closed to new members.

A distinctive feature of the proposal is the intention to allow members to choose between several alternative superannuation providers, with contributions into individual members' accounts being both vested and portable. This means that scheme members will be able to retain their membership when they change employers, and will also be able to shift their membership between the competing providers, subject to specified constraints.

We welcome this initiative. It signals the importance of private provision for retirement and of the role of work-based savings. The design features of the scheme - in particular, portability on changing employers, base salary plus retirement saving contribution, not as part of total remuneration, choice of schemes, no vesting period, and membership for all employees - overcome many of the traditional weaknesses of work-based savings schemes that discourage participation.

We suggest the Government consider the possibility of extending the new public service savings scheme beyond the core public service; in particular, letting organisations in the wider state sector opt into the new scheme.



**CHAPTER FIVE
PERSONAL FINANCIAL EDUCATION
AND INFORMATION**

Overview

Personal financial education (PFE) provides people with information and skills to help them make sound decisions about financial planning and management throughout their lives. It does not market or promote any particular product or service - individuals remain responsible for their own decisions and actions.

New Zealand's move from a regulated to a deregulated financial market, and the resulting rapid increase in products and services, and their complexity, has increased New Zealanders' need for clear and impartial PFE. This is particularly relevant in New Zealand's voluntary savings environment, which places the responsibility for financial planning and management decisions on the individual.

In New Zealand, the Retirement Commission provides most of the country's PFE programmes on retirement savings, with the remainder available through product-provider initiatives. PRG2003 thinks there is a need to expand and develop PFE to support the private provision of retirement income, particularly given the importance of retirement savings for the wellbeing of future generations and the limited options available for influencing savings behaviour.

The provision of information is an integral part of PFE. Information is different from education. It comprises the facts and figures New Zealanders need to know, or need access to, in order to make informed personal financial decisions. Education, on the other hand, provides people with the ability to apply that information to their own situations.

People need information on both public and private provision. There is scope to extend the current information provided to New Zealanders through the Retirement Commission, and its accessibility.

Recommendations

The analysis that follows results in PRG2003 recommending that the Retirement Commission:

- Promote workplace seminars and either provide them itself or contract providers to do so.
- Extend the Sorted programme to include more information, targeted information and supplementary written materials.
- Increase its promotional campaigns to encourage New Zealanders to use Sorted and other PFE programmes.
- Provide a face-to-face or telephone information service to supplement Sorted.

- Enhance and extend its provision of information about public provision.
- Establish a methodology to make fees for savings products more transparent.
- Develop criteria for assessing the appropriateness of savings products and advice for retirement saving.

The value of PFE

Research indicates that PFE can be very effective in changing people's financial behaviour. A recent study of the long-term effects of education on saving pointed out "the growing body of evidence that education may be a powerful tool for stimulating personal saving".⁴³

PFE can offer benefits through:

- helping people to assess their own financial position and to plan and make informed decisions based on this assessment
- helping individuals to make complex financial decisions that best suit their attitudes, values and desires (rather than being directive)
- encouraging and motivating people to seek further information and education
- being relatively inexpensive to implement compared with the costs of tax incentives or the compliance costs associated with compulsory savings.

PFE is not a panacea for the complex issues of retirement income policy. It is important that people have realistic expectations of what it can achieve. It also does not always lead to an immediate increase in saving, but can make people's financial decisions more effective.

PFE on saving for retirement

Providing New Zealanders with effective PFE is likely to result in their making better financial decisions throughout life. As a result, their financial position when they reach retirement, and during retirement, is likely to be much improved.

In New Zealand, the Retirement Commission provides most of the country's PFE programmes on retirement savings. Its main initiative is the successful Sorted website (www.sorted.org.nz), whose topics include:

- debt management, including student loans
- investing, mainly financial products
- budgeting
- saving
- goal setting and building net worth
- risk management
- retirement preparation - how much you may need, how much to save and state provision.

⁴³ Bernheim B et al (2001)

The Retirement Commission has also run a series of promotional campaigns to build and maintain awareness of the importance of retirement savings, to build awareness of the Sorted website and to change public attitudes and behaviours. As well as promoting the Sorted website these campaigns have covered issues such as:

- what sort of lifestyle will you have in retirement?
- if you want more than \$235 per week provided by NZS, take action
- how much do you want to live on in retirement?
- starting saving
- issues for women
- managing debt.

There is currently little financial literacy education provided through the compulsory curriculum in New Zealand. The Retirement Commission is working with the Ministry of Education to embed personal financial literacy in the curriculum. It is also developing programmes, to be part of the Sorted website, that will make personal financial education material available to parents, teachers, children and young adults. PRG2003 supports these initiatives.

The Retirement Commission also sponsors the “Pathways to Financial Literacy” programme, which was developed by the Enterprise New Zealand Trust and is delivered by trained teachers.

Recent evaluations of the Retirement Commission’s website show:

- a high demand for PFE, with more than 600,000 unique user sessions on the *Sorted* website since October 2001
- user action levels higher than 50 percent in response to recent promotional campaigns.⁴⁴

Overseas, momentum is gathering for enhanced PFE. For example, the United Kingdom has taken major steps towards including PFE in the school curriculum, and the Personal Financial Education Group has been established to provide resources for educational institutions. The country’s financial services authority also provides some PFE for all citizens. Meanwhile, workplace seminars are popular methods of PFE, and are often linked to employer savings schemes.

Extending PFE

We think there are four key areas where PFE could be extended.

Workplace seminars

PRG2003 is aware that attempts to interest New Zealand employers in workplace seminars have had limited success. Reasons include the money and time required, the lack of independent providers and a lack of perceived benefits to employers. However, similar work-based programmes in the US have proved effective in influencing financial behaviour, and we consider workplace seminars are worth pursuing.

⁴⁴ ACNielsen (2003)

The Retirement Commission could provide the seminars or contract providers to do so. A promotional campaign may be necessary to persuade employers of the benefits of an informed and financially responsible workforce.

Extending Sorted

Evidence indicates that extending Sorted would be an effective way of increasing PFE for New Zealanders. This work could include:

- promoting the website more
- providing more information for targeted audiences such as Pacific peoples
- providing information on specific financial products
- developing more written materials that supplement the website information.

Promotional campaigns

Promotional campaigns play an important role in:

- raising awareness of the importance of an issue
- providing accurate information
- directing people to other sources of information and advice
- encouraging people to use and act on PFE programmes.

Campaigns are particularly relevant for topics in which it is challenging to engage the public. However, they need to be carefully developed to ensure they reach their target audience.

To date, the Retirement Commission's promotional campaigns have been limited to television commercials, online advertising and occasionally other media. There is scope to broaden its campaigns using existing methods and adding others.

Face-to-face programmes

Until now, the Retirement Commission's programmes have been delivered via the Internet and related printed material. An independent, impartial, face-to-face or telephone education programme could provide information, rather than advice, on basic financial matters, debt management, and saving and retirement income options.

The concept would include people located throughout the country who could provide information to individuals or groups, and run seminars. A telephone helpdesk would be set up to both support the work of the information service and answer queries direct from the public.

Information

Information on public provision

When undertaking retirement planning, New Zealanders need to understand the level of public provision available. Without accurate information on public provision, it is very hard to estimate private provision needs.

Many New Zealanders are confused about the extent of public provision. A survey commissioned by the Retirement Commission brought a wide range of responses to questions about the levels of NZS.⁴⁵ Most underestimated, while one in three overestimated, the dollar values of NZS. Views were typically more accurate the closer people were to retirement age.

In addition, work undertaken by the ESR Consortium found that 64 percent of employees in their survey mistakenly thought NZS was income tested and 47 percent thought it was asset tested.⁴⁶

Confusion about public provision is likely to be caused by a number of factors, including the often confused debate about the issues and the ongoing changes to policy over the last two decades. One contributing factor may be the way New Zealand's current NZS entitlements are described as "65 at 65".

The term means that, at age 65, a couple will receive a pension equal to 65 percent of the average wage after tax. However, it is misleading for many people, as the actual figure for a single person living alone is 42.25 percent, and for a single person in shared accommodation it is 39 percent. In addition, couples that are both income earners, with a combined income above the average wage, may experience a significant drop in retirement income.

In future, we would like to see reference to the level of NZS being in absolute terms to avoid the confusion created by the "65 at 65" catch phrase.

45 ACNielsen (2003)

46 ESR Consortium (2003)

CASE STUDY: “65 AT 65”

Jim and Mary are thinking about retirement. They own their own house and their children have grown up and left home. Jim works for a plumbing firm and has a gross annual income of \$40,000. Mary is a part-time nursing aide and earns \$15,000 per year. After tax and ACC levies, their combined net weekly income is \$840.18.

Jim thinks they will do very well on NZS when they retire. After all, it's set at 65 percent of the average wage. “We're pretty close to average earners,” he says, “and our house is paid off. Sixty-five percent of our current income will suit us very well.”

Mary isn't so sure. She asks her friend Delia from accounts to do some calculations. When Delia produces the figures, Jim and Mary find that at current NZS rates, they'll each get \$188.69 after tax. Combined, this is \$377.38 a week, or 44.9 percent of their current weekly income.

Jim forgot that while NZS will be paid to them as a couple, it's set by the earnings of one average wage earner. Jim and Mary's combined income is well above the average single wage.

Another factor likely to cause confusion in the future is the NZ Superannuation Fund. As the quantum of the Fund increases, there is a risk it will provide a sense of security about the extent of public provision and, consequently, reduce private provision.

Given the widespread confusion about public provision, including the role of the NZ Superannuation Fund, we think the initiatives currently under way through the Retirement Commission to provide information on state provision should be continued and expanded. The guardians of the Fund will also have an important part to play in ensuring that the purpose of the Fund is understood.

Information on private provision

The complex range of products and investment choices in the financial services market creates confusion and uncertainty for consumers.

We consider there is value in savers having access to clear product information about what existing products are available. People need to trust the information required for making choices about how much to save and where to save.

Savers who have decided to take action need to know:

- what is available and who to trust
- how much it will cost
- how to use the product.

The Retirement Commission could act as the facilitator for the production of some of this information. We think there are two particular areas where the Retirement Commission could provide assistance:

- criteria for assessing products and advice
- information on the cost of products.

Criteria for assessing products and advice

We think there is value in investigating the feasibility of developing criteria for products suitable for retirement savings. The extent and scope of this material could range from questions for consumers to ask product providers to an independent 'qualmark' for products that meet agreed criteria.

Potential criteria for a savings product suitable for retirement might include:

- transparent fees, using an industry-standard approach, to enable consumers to compare fees across similar products
- a written product illustration of projected net real returns and the expected volatility
- information for consumers, expressed in easily understood language that explains the following product attributes: total costs, risk, projected returns, stop-start issues, complaints procedures and the like
- access through the workplace; in particular, to enable employers to contribute
- regular, simple communications about product performance relative to the market.

Information on costs of products

Although some information is provided through investment statements, PRG2003 considers information on costs needs to be standardised and made more transparent.

Comparing products and their costs can be difficult and makes selecting a savings product even harder. The Retirement Commission has already initiated work on a methodology that enables comparisons of costs across products. We would like to see this methodology further developed to enable accurate comparison of products.



**CHAPTER SIX
ISSUES FOR WOMEN, MĀORI
AND PACIFIC PEOPLES**

CHAPTER SIX ISSUES FOR WOMEN, MĀORI AND PACIFIC PEOPLES

Our terms of reference require us to provide a commentary on the ability of specific population groups, including women, Māori and Pacific peoples, to make private provision for retirement.

Combined, the groups represent about 60 percent of New Zealand's population. The diversity within and between each group makes any deliberations on the private provision of retirement income complex and challenging.

The most common features of the three groups are largely to do with limited disposable income and lower labour force participation than the general population. As a consequence, it is unrealistic to expect many in these groups to make substantial private provision for retirement.

NZS plays a vital role for all these groups in maintaining living standards in retirement, as it is not linked to past economic status. Nevertheless, we consider more can be done to help women, Māori and Pacific peoples to make private provision for retirement. Even a small amount of savings can contribute to improving living standards in retirement for these groups.

Women

Overview and recommendations

Women are entering retirement in a very different situation than women a generation ago. Changes in the range of employment options and family situations that women are now experiencing in their lifetimes mean the issues around how they make private provision for retirement income are becoming more diverse and complicated.

Women still bear the prime responsibility for caring for dependants, particularly children, and may have varying periods out of the workforce when they earn no personal income. Hourly earnings for all women are still, on average, lower than those of men, and the gaps are larger for Māori and Pacific women.

This combination of fewer hours and years in paid employment and lower hourly earnings adds up to lower earned incomes and lifetime savings potential for women in their own right.

Although the main reason women do not save for retirement is their lack of access to disposable income, a growing proportion of women are having smaller families and working in paid employment longer. This creates the potential for these women to have enough disposable income for some retirement savings.

There is still, however, a sizeable minority of women who will enter retirement with few or no assets. NZS and supplementary welfare assistance will continue to provide a basic income for these women.

Recommendations

The analysis that follows results in the PRG2003 recommending that:

- The Retirement Commission make it a key education priority to increase the knowledge of women about the need to save for retirement on their own behalf. We recommend a particular focus on the periods in women's lives when they have disposable income.
- The Retirement Commission develop criteria for a 'best-practice' vehicle for retirement savings that accommodates the needs of those people with periods of broken employment or reduced earnings during their working life.
- Efforts continue to be made to close the gender pay gap in the state sector and recommend these efforts extend across the labour market.

Issues

There are a number of retirement saving issues that are specific to women and common to most women. The major ones centre around responsibilities for the care of dependants, particularly children, which still fall mainly on women. There are also differences in hourly earnings.

Responsibility for the care of dependants has a number of impacts:

- Women may leave the paid labour force for a period to look after dependent children, during which time they have no personal earned income. This also results in a loss of seniority and job experience. At any time, this group includes about one third of partnered women with dependent children and about half of sole parents.
- When they return to work, women with children generally work fewer paid hours than their male counterparts.
- Many women who have young dependent children and work in paid employment have to fund significant childcare costs.

Hourly earnings for women are still, on average, lower than those of men. For all occupations, the total average hourly earnings of women were 85.4 percent of those of men in September 2003.⁴⁷ While this gap can be expected to narrow over time, with more highly skilled younger women entering the labour market and increasingly filling traditionally male skilled and professional occupations, the earnings gap will still persist for most of the current cohorts of middle-aged women. Hourly earnings gaps are larger for Māori and Pacific women than for their Pakeha counterparts because of the lower percentages of the two groups in well-paid skilled occupations.

The combination of fewer hours and years in paid employment and lower hourly earnings when employed adds up to lower lifetime earned incomes and, hence, lowers lifetime savings potential for women in their own right.

⁴⁷ Statistics New Zealand (2003)

Impact of family structure on savings

The actual effect of lower earnings on the assets of women as they enter retirement also depends on their family structure, its stability, and the degree to which couples' resources are actually shared.

The 2001 Household Savings Survey indicated that couples approached retirement with more assets per head than unpartnered individuals, even though the woman in the couple, on average, had presumably spent less time in paid employment than single women without children, though more than sole parents.⁴⁸ In the age band 55 to 64, the median net assets of unpartnered people, at \$137,500, were only 43.5 percent of those of couples.

The impact of marriage and partnership break-ups and of sole parenthood may explain much of the apparent asset accumulation differential between partnered and unpartnered people. Sole parents approaching retirement were in the worst asset ownership situation.

What emerges is a complex situation where the retirement assets women can expect to accumulate are a mix of effects from their own earnings, a partner's earnings (if part of a couple), family responsibilities and the longer-term stability of couple-based households. For women with children whose partnership breaks up, financial outcomes will, in part, depend on laws relating to the division of relationship property and child support payments.

Implications for retirement saving by women

The principal reason for women's lack of direct participation in private provision for retirement is lower personal lifetime income. This is, to a large extent, a result of gender-related disadvantages in their experiences of employment and pay structures and of the return they receive from education, and because their labour force participation has to fit around their unequally large share of unpaid work responsibilities.

Current cohorts of women will approach retirement a much more varied group in terms of economic circumstances than their counterparts of a generation ago. A larger minority will potentially have substantially more assets, another large minority will have few or no assets, and the middle group is likely to be smaller than among the currently retired.

With smaller families and women in paid employment until later in life, there will be longer periods when women have disposable income, allowing them to save. Barriers to this happening include attitudes to women saving on their own behalf that may not yet reflect the new economic and social realities, and problems in existing retirement savings schemes that do not accommodate the needs of women with varying periods in and out of the paid workforce. These are both areas where policy attention could focus.

Other barriers to women saving for retirement relate to the inadequacy and use of disposable income during the working age years. Solutions lie mainly in policies geared towards working age people, and to women in particular. These include:

- access to education and training, which equips people for better-paid jobs
- the ongoing development of a five-year plan of action by the Taskforce on Pay and Employment Equity in the Public Service, Public Health and Education Sectors

⁴⁸ Statistics New Zealand (2002b)

- employment policies
- childcare costs
- levels of family support and other assistance to families with dependent children
- student loan and tertiary study assistance policies
- laws affecting child support and marital or relationship property
- house purchase assistance, using taxes
- a range of other policies that affect the ability of households to save and accumulate assets.

NZS and supplementary welfare assistance will continue to provide a basic income for women who enter retirement with minimal income or assets. This group includes parents, single women in low-paid occupations, long-term beneficiaries, and women in single-earner households who are partnered with low-earner or unemployed males.

Māori

Overview and recommendations

The Māori population is diverse and a mix of factors shapes the issues facing Māori when making private provision for retirement income. Some will have similar personal and financial circumstances to their non-Māori counterparts. For others, the differences are marked.

Māori average earned income is slightly lower than the national average, but a higher-than-average proportion of working age Māori are on benefits and not in employment. High levels of sole parenthood and larger numbers of children for families to support compound the effect. These factors reduce the potential for asset accumulation for retirement.

Asset ownership is below the national average, house ownership is falling, and Māori are less likely to have private superannuation or investment income or asset holdings. Māori families and communities often have large collective assets. How these assets are managed in the future may make a significant difference in outcomes for Māori approaching retirement.

The Māori population has a very young age structure. With more of the younger generations of Māori having a tertiary education and advanced job skills, there is higher savings potential.

Recommendations

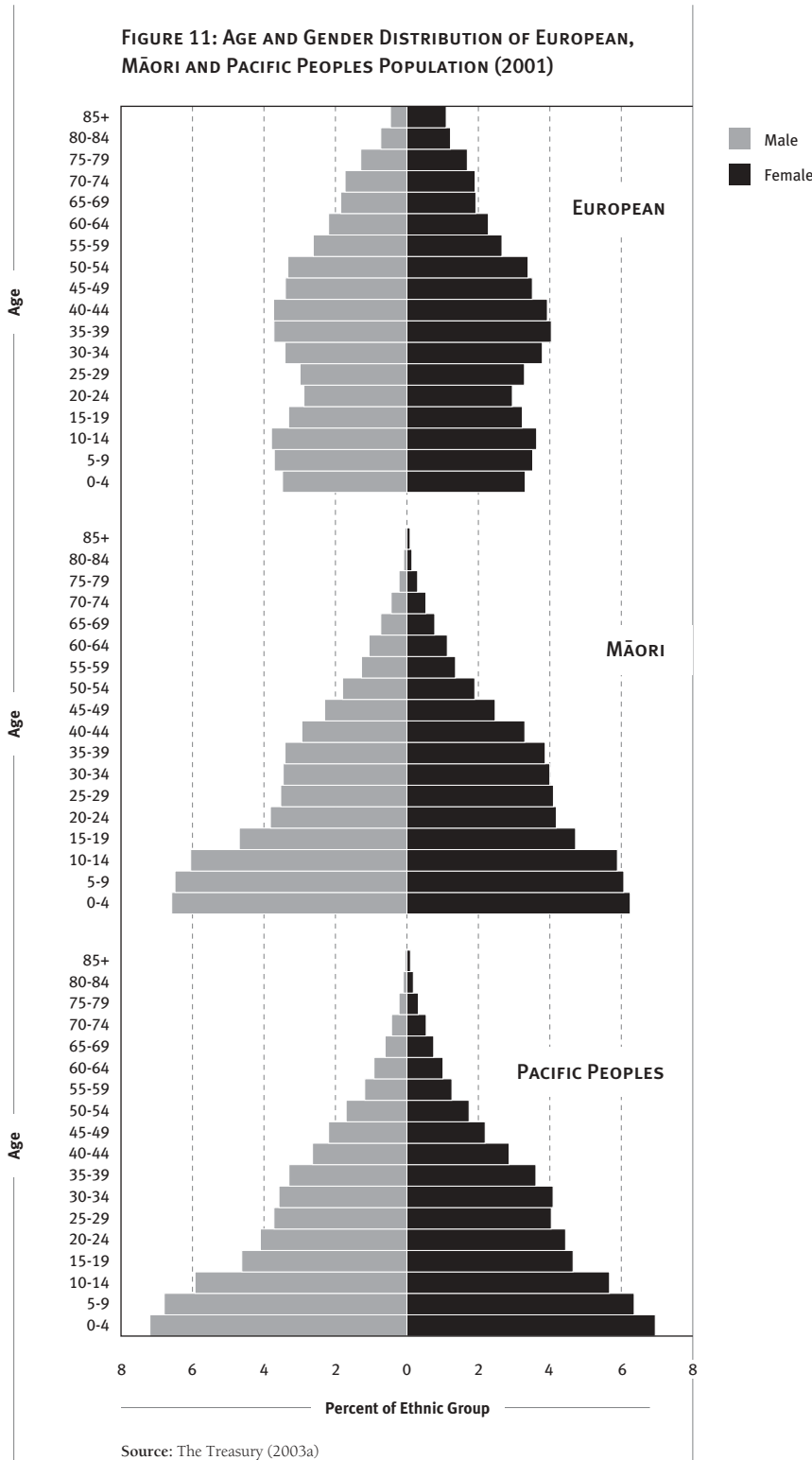
The analysis that follows results in the PRG2003 recommending that:

- The Retirement Commission, in consultation with Te Puni Kōkiri, develop a research programme to address the information gaps regarding Māori experience and attitude to savings and to facilitate a better understanding of Māori attitudes to retirement saving.
- If it is successful, the financial education pilot programme for young Māori, developed in partnership between the Retirement Commission and Ngāi Tahu, is extended.
- The Retirement Commission and Te Puni Kōkiri work with interested Māori organisations to assess the feasibility of those organisations taking an active role in the provision of savings and insurance services for the organisations' beneficiaries.

Issues

Demographic situation

The Māori population has a very young age structure. At the time of the 2001 Census, only 3.4 percent were aged 65 plus and 37.3 percent were less than 15 years of age. As shown by Figure 11, this population distribution is very different in structure from the population as a whole.



The low number of older Māori has often meant retirement savings issues have been seen as less important than the issues affecting the larger number of younger people, such as unemployment, education, low family incomes and sole parenthood.

However, the proportion of older Māori is rising, and the issue of their retirement income levels has to move up the policy agenda. By 2021, the number of Māori aged 65 plus is expected by Statistics New Zealand to grow by around 185 percent to about 57,000 people, although the proportion of Māori aged 65 plus is still projected to be around only 7.6 percent of the Māori population.

Income and assets

Māori median earned incomes are lower than the national average. The 1999 figure showed weekly earned incomes for employed Māori were 90.5 percent of the national average. While this earnings gap may not seem particularly large, the earned income effect is compounded by larger-than-average proportions of working age Māori being on benefits rather than in employment, by high levels of sole parenthood (over 40 percent of Māori families with dependent children) and by Māori families having larger numbers of children to support. All these factors tend to reduce the potential for asset accumulation before retirement. Further, proportionally fewer Māori have been employed in occupations that provide work-based savings.

The Living Standards Survey of Older Māori indicated that older Māori were less likely than the older population in general to have private superannuation or investment income.⁴⁹ Overall assets of all Māori, from the 2001 Household Savings Survey, were below the national average. However, research suggests that as much as 70 percent of the difference in net asset ownership was due to the much younger age structure of the Māori population.⁵⁰ Even correcting for age structure differences, the general Māori pattern is one of lesser asset accumulation than the national average, with home ownership being the main asset accumulated.

Māori families and communities often have large collective assets. Over the next few years, collective assets are likely to become more important. The 2001 Household Savings Survey indicated that these collective assets of trust boards and incorporations were worth \$8.8 billion.⁵¹ How these collective assets are managed over the period ahead and how they impact on Māori employment, training, house purchase and specific income distribution may make a significant difference to outcomes for Māori as they approach retirement.

Te Puni Kōkiri recently commissioned a report that looks at Māori economic development.⁵² The report shows that the New Zealand economy benefits from the positive and profitable contribution of the Māori economy. Māori production amounts to \$1.9 billion a year and the Māori economy earns about \$826 million in operating surplus.

As we have already emphasised, economic growth is critical. It provides a bigger base from which to provide both public and private retirement income. Consequently, the success of the Māori economy will be crucial to the ability of Māori to make private provision in the future.

49 Cunningham C et al (2002)

50 Gibson J and Scobie G (2003)

51 Statistics New Zealand (2002b)

52 NZIER (2003)

Implications for retirement saving by Māori

In the current situation, the margin for savings among Māori people is less than average, particularly among those now middle-aged. The pattern is changing as younger people obtain higher education and more advanced job skills, and family size declines. However, among the current cohorts of middle-aged Māori, a disproportionate number will be dependent on NZS and supplementary social welfare benefits in retirement.

The younger generation of Māori includes far more people with tertiary education and advanced job skills and higher savings potential. This group would seem to be the better target for increasing private savings.

More generally, to an even greater degree than among the population as a whole, the longer-term adequacy of retirement savings among Māori will depend on the success of policies focused on the young and working age groups. These include education, health, training, employment and housing policies.

Our review of the ability of Māori to make private provision for retirement highlighted that we know very little about Māori attitudes to savings, including:

- what are Māori perceptions about the value of saving?
- how well does the concept of savings fit with values that operate within different Māori whānau and communities?
- are there equivalent concepts in Māori society that interventions focused on private savings could utilise?

We see value in assessing the financial risks, costs and benefits for Māori asset holders being actively involved in savings and insurance schemes. For example, encouraging greater provision for health insurance or health plans, life insurance and income protection are all ways of reducing the financial impact of illness, death or loss of income.

Pacific peoples

Overview and recommendations

The population of Pacific peoples in New Zealand is a combination of those born within and outside New Zealand. As a result, Pacific peoples range from those holding traditional views and beliefs to those who have adopted more western values. This creates a number of challenges, apart from the more apparent socio-economic issues.

The expectation that the extended family is responsible for looking after parents and older members in their old age is strong and pervasive. Not only do Pacific peoples place a high priority on extended families, but they also feel a strong obligation to financially support the church and community groups. This results in a different use of disposable income than in the wider community.

Pacific peoples are the poorest major ethnic community in New Zealand and have the lowest net worth. This reflects the lower average earned incomes of Pacific peoples, a falling home ownership rate, the financial strains of family and community obligations and difficult conditions for low-skilled workers.

Pacific peoples in New Zealand have a very young age structure compared to the total population. Many of these New Zealand-born Pacific peoples are adopting different values to the more traditional ones. This will increasingly affect how Pacific peoples look at issues of independence, financial commitments to families and communities, and private provision for their own retirement.

Recommendations

The analysis that follows results in the PRG2003 recommending that:

- The Retirement Commission work with Pacific communities to facilitate education programmes, tailored to the Pacific peoples, which highlight the benefits of preparing for retirement. These programmes should take into account the important characteristics of Pacific peoples we have identified, such as the existing commitments to the church, the extended family and the community.
- The Retirement Commission, in consultation with the Ministry of Pacific Island Affairs, facilitate research to see whether the current arrangements in which extended family groups establish trusts for various events, such as weddings and funerals, could be involved in superannuation funds and insurance schemes.

Issues

Demographic situation

The demographic and economic situations of Pacific peoples in New Zealand show many similarities to those of the Māori population. Pacific peoples have a youthful population age structures, with a predominance of young adults and children and proportionally few people aged 65 plus, as shown in Figure 11. While the proportion of older Pacific peoples will rise rapidly in the next 20 years, it will still be well below the current average for New Zealand as a whole.

Income and assets

Pacific peoples in New Zealand are the poorest of the major ethnic communities and have the lowest level of net worth. Pacific peoples have lower average earned incomes than the population as a whole. A Statistics New Zealand report shows that 61 percent of Pacific peoples aged 15 years and over had an annual income of \$20,000 or less in the year to 31 March 2001.⁵³ In comparison, just over half of the national population fell into this income band. Meanwhile, seven percent of Pacific peoples received an annual income of over \$40,000 per annum during this time period, compared with 18 percent of people in the general population.

53 Statistics New Zealand (2002a)

The 2001 Household Savings Survey indicated that median net worth for Pacific couples was only 6.4 percent of the overall median.⁵⁴ Single people had zero net worth, in comparison to the overall median of \$10,300. The disparity in the figures, in part, reflects the age structure of the Pacific population compared to the national age structure, as is also the case for Māori.

Home ownership has also dropped among Pacific peoples. In the last 10 years, ownership has fallen from 61 percent to 48 percent for 40 to 59-year-olds, and from 44 percent to 35 percent for 20 to 39-year-olds.

While some issues around providing for retirement apply equally to Māori and Pacific peoples, there are important differences. In addition to economic factors (for example, Pacific peoples lack the large collective asset base many Māori have), there are important differences in values and beliefs.

Pacific peoples' pattern of extended families and their obligation to their parents and other relatives is strong and pervasive, particularly among the Pacific born. Pacific peoples also place a high priority on outlays supporting community groups and churches. This suggests a different pattern of cash use than in the wider New Zealand community. Finally, the concept of specifically saving for retirement is not part of traditional Pacific peoples' culture as the expectation is that extended family members will care for their older members.

Implications for retirement saving by Pacific peoples

Migration to New Zealand has meant huge changes for the various Pacific peoples' communities now resident here. The very favourable employment and housing conditions encountered by the earlier migrants in the 1960s and 1970s were succeeded by more difficult conditions for the low skilled during and since the economic restructuring of the 1980s.

For middle-aged and older Pacific peoples, the risk is they will have only NZS in retirement and be increasingly dependent on supplementary social welfare assistance. Low asset ownership and the financial strains of multiple family and community obligations will impact on living standards.

As well as the difficulties imposed by generally low disposable incomes, many Pacific peoples do not see private provision for retirement as an essential expense or commitment. Commitments to family, church and community events take priority. Furthermore, responsibility for looking after parents in their old age and providing for their living needs continues to feature in the values and beliefs of many Pacific peoples.

Change is occurring, with an increasing number of Pacific peoples now New Zealand born and adopting more western values. Although this can result in conflicts with parents and other members of the family, the subsequent mix of values and beliefs will influence views on independence, financial commitments to the extended family and private provision for retirement.

⁵⁴ Statistics New Zealand (2002b)



CHAPTER SEVEN TAXATION OF SAVINGS

Overview

Our terms of reference require us to provide suggestions for the adjustment of any of the Government's retirement income and savings policies in order to enhance the provision of private retirement income, including those relating to the impact of the tax system on the private provision of retirement income.

Tax reforms from 1988 onwards have broadly focused on ensuring all savings and investments are taxed on the same basis, and in the same way, as income from wages and business. This neutral tax regime aims to reduce complexity, remove distortions in savings and investment, and remove the favourable treatment some taxpayers received under the previous system.

New Zealand's current tax system does not intentionally offer incentives to any particular form of savings.⁵⁵ However, it does contain clear disincentives for some savers and some methods of saving.

The key disparities of the current system are:

- an unclear boundary between capital gains and ordinary income
- different tax rules for similar domestic and international investments
- inequities for some savers in superannuation funds and life insurance companies
- inequities for some savers with regard to employer contributions to superannuation schemes.

Another disparity arises from the fact home owner-occupiers are not taxed on the imputed rent from their properties. We discuss this anomaly briefly in the analysis that follows, but we don't recommend a change to the status quo.

It is worth noting that reducing tax on savings is not a cure-all. Tax on savings has significantly less impact on a person's ability or motivation to save than tax on income. A tax reduction on savings means tax needs to be recouped elsewhere, possibly from tax on wages or business income. This can simply result in a decreased ability to save.

In addition, the resulting effect of higher after-tax returns is not clear. While the incentive to save is increased, the amount needed to save for the same returns is reduced. In other words, savers find it easier to reach a savings target, but do not necessarily save any more. The relative impact of the two effects is an empirical question and the analysis to date shows mixed results.

⁵⁵ The increase in the top marginal tax rate to 39 percent created a tax incentive for high earners directly contributing to work-based superannuation, or investing in some superannuation and life insurance products.

We favour a broadly neutral tax system, with disparities and resulting disincentives removed as far as possible.

A neutral tax system is the most efficient and avoids the distorted savings that tax incentives can create. We are aware, however, that removing disincentives may require complex structural change, with a final impact on savings that is hard to determine. Careful analysis and trade-offs are required.

PRG2003 considers the case for tax incentives is not strong. Submissions to PRG2003 were divided between favouring tax incentives and opposing them. Submitters were, however, in agreement about the need to remove disparities and disincentives in the current tax system.

Recommendations

The analysis that follows results in PRG2003 recommending that the Government:

- Make it a priority in its tax work programme to resolve the tax non-neutralities arising from the indistinct capital/revenue boundary.
- Continue its work to resolve disparities in the treatment of international investments.
- Revisit options, such as those developed by the Working Party on Taxation and Life Insurance and Superannuation Fund Savings (TOLIS), to address inequities in the taxation of superannuation funds and life insurance companies.
- For equity reasons, either remove the tax advantage for employees earning over \$60,000 on employer contributions to superannuation funds or make it available to all taxpayers irrespective of their marginal tax rate.
- Review the fund withdrawal tax and remove it if there is no compelling evidence it is successfully acting as an anti-avoidance mechanism.

THE CURRENT TAXATION TREATMENT OF SAVINGS

There are three potential taxable flows of funds associated with savings. These are:

- contributions to savings accounts - the income initially received by the saver in the form of, for instance, salary or wages from employment that becomes a contribution when it is deposited in a savings account
- income accruing on savings - such as interest
- withdrawals from the account.

Under the current income tax system, all income is subject to tax as it is derived. Contributions are made from income, which is subject to tax (T). In that sense, contributions can be said to be taxable under an income tax regime. Income accruing is also taxable (T). Withdrawals, on the other hand, merely represent the conversion of an asset in the form of a positive savings account balance to an asset in the form of cash. Withdrawals do not constitute income of the taxpayer and are not taxed (E).

This income tax treatment of savings is described as the taxed/taxed/exempt regime - TTE.

The capital/revenue boundary

New Zealand has no capital gains tax. As a general rule, profits on the sale of personal property such as equities are taxed only if the property was acquired with the intention of sale or as part of a profit-making scheme. In these cases, profit on the sale is taxed as part of ordinary income.

Disparities arise because of the indistinct boundary between capital gain and ordinary income. As a result, investments through intermediaries, such as fund managers or superannuation funds that actively trade investment portfolios, are taxed as ordinary income while direct investment in property and equities are less likely to be taxed.

This indistinct boundary contributes to taxpayers who manage their own portfolios, often investing directly in property and equities, rather than investing through an intermediary such as an insurance company or a superannuation fund. This direct investment is less likely to lead to a profit being classed as ordinary income.⁵⁶ This potentially distorts economic investment decisions, such as over-investment in some sectors and under-investment in others. This also may reduce the long-term returns on savings.

Resolving issues around this boundary is very difficult. PRG2003 considers that addressing the issue of the capital/revenue boundary should be a priority.

Taxation of international investments

The disparities between the taxation of domestic and international investments are particularly complex. As a rule, domestic investments have more favourable tax rules than similar investments made offshore, with exceptions including some investment products in the United Kingdom and Australia. For example, an investment in a New Zealand resident unit is taxed only on the dividend distribution, while a similar offshore investment is taxed on an accrual basis.

We understand that an officials' issues paper on the taxation of offshore portfolio investment in equity will be released at the end of 2003 and will provide options to address these disparities.⁵⁷ PRG2003 does not favour any particular approach, but does recommend the Government continue its efforts to resolve the disparities around international investments.

⁵⁶ Whether an investment is on capital or revenue account depends on the specific facts, such as the size of the portfolio, its sophistication and its management.

⁵⁷ See www.treasury.govt.nz or www.taxpolicy.ird.govt.nz

Over-taxation for savers in superannuation and life insurance schemes

Superannuation funds and life insurance companies have an entity tax rate of 33 percent that may not be the same as a saver's marginal tax rate, which may be 21, 33 or 39 percent. There is no mechanism that allows the two tax rates to be aligned, leading to over or under-taxation of savers.

In 1996 the TOLIS working party developed a range of options to address these inequities. However, the administrative tax credit solution chosen by the Government had significant compliance and administrative costs. It found little favour and the initiative failed in Parliament.

PRG2003 considers the Government should revisit the over-taxation issues, including the options developed by the TOLIS working party, with a view to developing new proposals to address over-taxation of savers on a low marginal tax rate. These new proposals could include a revised proxy rate, a tax credit or a qualifying fund.

PRG2003 understands the Minister of Finance has instructed officials to look at the design of a TET model to address this issue. This approach would avoid the compliance costs of a tax credit, but would probably apply to only a narrow range of products. The issue of over-taxation of low-income earners would remain in those vehicles not covered by the suggested TET treatment. The costs and benefits of tax incentives such as TET are discussed in more detail later in the chapter.

Inequities in employer contributions to super funds

Taxation on employer contributions to superannuation funds may also result in inequities for savers. Contributions to funds are subject to a Specified Superannuation Contribution Withholding Tax (SSCWT) that attracts withholding tax of 33 percent. Depending on a saver's marginal tax rate, this may also result in over or under-taxation.

PRG2003 welcomes the recent Government decision to allow employers to pay SSCWT on employer contributions at the employee's marginal tax rate.⁵⁸ But it is disappointing that this is voluntary. However, consistent with our call for tax neutrality, we believe all taxpayers should be treated equitably. Either the current concession of six cents in the dollar to those employees earning over \$60,000 should be available to all or no concession should exist.

We recommend the Government should either remove this tax advantage or make it available to all taxpayers, irrespective of marginal tax rates.

58 Taxation (Annual Rates, GST, Trans-Tasman Imputation and Miscellaneous Provisions) Act 2003

Fund withdrawal tax

The fund withdrawal tax was introduced in 2000 to counter avoidance concerns that persons earning over \$60,000 might substitute employer superannuation contributions for salary or wages to avoid the top personal tax rate. This occurs because employee contributions are taxed at 33 percent compared to a 39 percent marginal tax rate. In general, it works by applying a five percent tax on certain withdrawals from superannuation funds that comprise employer contributions for members whose earnings exceed \$60,000.

The fund withdrawal tax has increased compliance and administrative costs for trustees, employers and funds in determining whether withdrawals are subject to the tax. As part of the ESR Consortium survey commissioned by PRG2003, employers were asked if they offered a “salary sacrifice” facility for taxpayers on the 39 percent marginal tax rate. The indicative findings from this question were that 30 percent of the employers surveyed offer such a facility and that less than half a percent of all employees subject to the survey use it. This indicates employees are not using salary sacrifice to avoid the top personal tax rates, where such a facility is offered by an employer.

This evidence suggests that either the fund withdrawal tax is successful as an anti-avoidance mechanism, or there is limited interest in salary sacrifice and the tax is simply imposing additional compliance costs. In the context of minimising compliance costs for work-based savings, we suggest the tax be reviewed in the light of this evidence and removed if there is no compelling evidence it is successfully acting as an anti-avoidance mechanism.

No tax on home owner-occupiers

PRG2003 sees no value in addressing the anomaly created by no tax being imposed on the imputed rentals from owner-occupied housing. We recognise this is a distortion of the current tax system. However, many New Zealanders rely on housing to ensure they have a reasonable standard of living in old age.

The debate about tax incentives

The debate about the merits or demerits of tax incentives, such as TET, EET or TTE, is well worn. The lack of clarity about the purpose and benefit of tax incentives, however, has led to considerable confusion in the debate. PRG2003's analysis reaches the same conclusion as previous reviews of retirement income. The costs of tax incentives outweigh the benefits.

Benefits of tax incentives

The key benefit of tax incentives is that they might encourage increased private provision. However, evidence shows that tax incentives generally do not increase the amount of savings, but do result in a change in the mix of savings. Their impact will depend on the specific design features of the incentive.⁵⁹

Tax incentives will generate benefit only if the increased savings increases net worth, enabling New Zealanders to better provide for themselves in retirement. Net worth depends on both the level of savings and the rate of return. Benefits may not arise if incentives result in a reduction in before-tax returns to savings.

Costs of tax incentives

The tax incentives used to encourage savings both in New Zealand and internationally have a number of costs. The extent of these costs will usually depend on the specific design of the incentive.

Tax incentives are generally not equitable. They favour the better off, who do most of the saving and already make adequate provision for their retirement. They can result in a transfer of wealth from savers to non-savers, from poor to rich, and from younger to older. Research in the United Kingdom estimated that 50 percent of the value of the country's retirement saving tax incentives is captured by the top 10 percent of taxpayers. The researchers estimated that 25 percent of the value is captured by the top 2.5 percent of taxpayers.⁶⁰

Tax incentives increase the inefficiency of the tax system. They have the potential to distort saving patterns by encouraging savers to divert their savings into tax-preferred products. Tax incentives also require funding. If the funding comes from increased tax elsewhere, it will result in additional dead-weight losses. The opportunities provided for tax planners to produce unanticipated tax products could distort saving patterns further.

Complex tax and regulatory fences are often needed to address unintended consequences such as savers moving into tax-preferred products. International experience suggests the complexity and high compliance costs of tax incentives make them hard to sustain over time. Once a tax incentive is in place, political pressure to extend it is hard to resist. This leads to tinkering with incentives, resulting in confusion for savers and increasing regulatory costs.

⁵⁹ Engene E et al (1996)

⁶⁰ Agulnik P and Le Grand J (1998)

In the absence of a means-tested state pension, tax incentives will increase the total fiscal costs of retirement income and this detracts from the long-term sustainability of public provision. The costs of tax incentives can be very high. In Ireland, tax incentives constitute 100 percent of spending on public provision; in Australia, 60 percent; in the United Kingdom, 33 percent.⁶¹

Important features of a tax incentive scheme

While PRG2003 is not convinced there is a case for tax incentives, we recognise they could be used to signal the Government's commitment to private provision. Any such tax incentive scheme would require certain features to ensure it increases private provision while minimising economic distortions:

- It should be confined to new savings and be product neutral. This would reduce savers' movement into tax-preferred products and avoid the cost of specific product regulation for the tax-preferred product.
- It should be designed to ensure people on high incomes, who mostly make adequate provision for retirement already, are not the main beneficiaries.
- It should be simple and easily accessible to low and middle-income savers.
- It should minimise costs to providers.
- Its impact should be closely monitored, and reviewed after five years; and the incentive scheme removed, rather than increased, if it is not effective in increasing private provision for retirement income.

61 Pensions Policy Institute (2003)



CHAPTER EIGHT FINANCIAL SERVICES MARKET AND REGULATION

Overview

The financial services sector plays an important part in the private provision of retirement income. When making private provision for retirement, people want to achieve the best possible risk-adjusted return from their savings. This requires a competitive, efficient and trusted financial services sector, which can identify and direct savings to the best investment opportunities, while managing risks.

A key element required to ensure the financial services sector delivers products that enable saving, is an effective regulatory regime. Well designed regulation will enhance the savings environment, providing confidence to savers that the products can be trusted, while minimising the costs to providers and consumers. However, poorly designed regulation can distort savings decisions and impose costs on consumers and providers.

New Zealand's financial services sector has a disclosure-based regulatory regime that applies to all financial services entities except registered banks, and to all types of financial services. The regime is based on the principle of informing consumers through disclosure, and leaving them free to make decisions. The regime places a greater emphasis on disclosure and caveat emptor than most other developed economies.

PRG1997 concluded the regulatory regime was comparatively non-intrusive, and not likely to reduce competition between providers. Six years later, PRG2003 considers this conclusion still stands.

The regime is well established and well understood, and no submitter suggested it acted as a barrier to private provision. However, submitters raised some issues concerning the way the regime operates in practice. Most of these concern regulations that affect employer superannuation schemes. PRG2003 agrees these issues need attention.

Issues about the regulatory regime are:

- the requirement that employer superannuation schemes maintain a prospectus
- member consent-based transfer provisions leading to leakage of members from employer superannuation schemes
- the lack of a dispute resolution scheme or body for members of group or employer superannuation schemes.

Issues about the financial services market in general are:

- the regulation of financial advisers
- an undeveloped annuities market.

Recommendations

The analysis that follows results in PRG2003 recommending that:

- The Government remove the prospectus requirement from employer superannuation schemes, as proposed in the Business Law Reform Bill currently before Parliament.
- The Ministry of Economic Development and the Government Actuary review how much leakage is taking place from employer superannuation schemes because of written consent requirements for member transfers, and assess whether it is practical to better facilitate transfers in cases where transfer provides equivalent benefits.
- The Retirement Commission promote best practice guidelines for dispute resolution for group and employer superannuation scheme members.
- The financial services sector develop an agreed approach to self-regulation of financial advisers and report to Government with a comprehensive proposal by the end of 2004.
- The Government's proposed review of the tax rules applying to life insurance consider the tax barriers to the development of annuities; in particular, home equity reverse annuity mortgages.

Prospectus requirement in employer superannuation schemes

The Securities Act 1978 and the Superannuation Schemes Act 1989 require an employer superannuation scheme to maintain a prospectus, an investment statement, and prepare annual financial statements and annual reports.

PRG1997 raised concerns about the requirement to maintain a prospectus. It stated that this requirement created significant additional compliance costs and could result in the closure of employer superannuation schemes.

PRG1997 recommended that the then Ministry of Commerce, the Securities Commission and employers work together to seek solutions to the problem. However, the proposal was not acted on. A number of employer superannuation schemes have since closed their schemes to new members, to remove the need for a prospectus. For example, Toyota New Zealand in its submission cited the compliance costs related to maintaining a prospectus and having to replace it annually as the main reason it closed its existing superannuation scheme to new members.

The Business Law Reform Bill before Parliament includes a clause that removes the prospectus requirement from employer superannuation schemes. PRG2003 supports this clause and we have made this view known to the select committee that considered the Bill.

We consider the change will not impact significantly on the form or volume of information available to scheme members. Almost all the material information is readily available in other disclosure and reporting documents, and schemes will still be required to provide investment statements, annual reports and financial statements. Scheme members will still be able to request information under section 17 of the Superannuation Schemes Act and regulation 23A of the Securities Regulations 1983.

Transfer provisions in employer superannuation schemes

Submitters noted that the need for employers to get the written consent of employees to transfer them to a new superannuation scheme on the same terms and conditions seems to be creating leakage of members. For instance, on acquisition of a firm it may be considered appropriate to transfer the members of the firm's superannuation scheme, for administrative reasons, from their existing scheme to a new scheme, with equivalent benefits.

Trustees are legally required to get the written consent of members to transfer to the new scheme. This makes it too easy for people to withdraw from the scheme. While there is no written data on the extent of the leakage, PRG2003 has anecdotal evidence that the main beneficiaries of the provisions are often car and boat dealers.

PRG2003 considers this leakage is often unnecessary and unhelpful, especially given that employer superannuation schemes are, for many members, the most significant financial asset after their home. It would be useful to have better information about the extent of the leakage and, if necessary, assess whether it is practical to better facilitate transfer in cases where transfer provides equivalent benefits.

Dispute resolution for members of group and employer superannuation schemes

The banking and investment and insurance and savings ombudsmen schemes were established in response to the 1992 PPR Task Force concerns that there was no mechanism to provide redress in disputes between consumers and product providers. One of the statutory functions of the Retirement Commissioner is to monitor the effectiveness of these schemes. At the start of 2003, the Retirement Commissioner reviewed the banking and investment and insurance and savings ombudsmen schemes and concluded they both worked well for disputes within their terms of reference.

However, the Retirement Commissioner also noted that these ombudsmen schemes do not extend to disputes relating to insurance cover provided to members of group or employer superannuation schemes and, more generally, members of these schemes do not have access to an independent dispute resolution body. In the case of insurance, this is because the contract is between trustees or employers and the insurer and not between the individual scheme members and the insurer. The trustees of group and employer schemes are required to act in the interests of all members, but disputes do arise. It is important members feel they receive a fair hearing.

One potential remedy is that trustees or sponsoring employers of superannuation schemes should be legally obliged to become participants of an ombudsman or other disputes handling scheme. That approach would introduce further compliance costs for employer schemes and would, in our view, be difficult to justify in terms of the number and nature of disputes arising between trustees/employers and members.

We consider the promotion of best-practice guidelines for dispute resolution would be a good solution for members of these schemes. These guidelines could be based on the dispute resolution procedures that the Retirement Commission and a number of schemes have already developed.

Regulation of financial advisers

New Zealand's more than 3000 financial advisers are largely unregulated, with the exception of disclosure requirements under the Investment Advisers (Disclosure) Act 1996. PRG2003 recognises that a number of industry bodies have established codes of practice, disputes resolution and disciplinary procedures, and training for their members. However, a significant number of advisers are outside existing self-regulatory regimes.

The Investment Advisers (Disclosure) Act 1996 does require a disclosure statement from advisers. However, the statement puts the onus on consumers to decide about the advice and adviser. Most consumers are not likely to have the necessary experience or knowledge to make an informed decision and the costs of getting the necessary knowledge may be prohibitive.

In addition, most advisers are paid on commission and are not required to disclose their commissions unless requested. PRG2003 considers this limited disclosure and onus on consumers may be affecting consumers' willingness to use financial advisers and impacting on private provision for retirement.

We welcome the Government's decision to strengthen the disclosure regime and expect improvements for consumers. Financial advisers will be required to disclose:⁶²

- whether they belong to a professional body
- what dispute resolution facilities are available to clients
- what fees are charged for the service
- the date the disclosure statement was prepared.

Advisers will also be required to provide their clients with updated information if, after the adviser has supplied the disclosure statement, there is any change in circumstances that might affect the client's investment decisions.

These changes will do much to increase transparency. However, PRG2003 is still concerned that:

- no disputes procedure is available to consumers if the adviser does not belong to a professional body
- there are no industry-wide codes of conduct or ethics
- advisers cannot easily be excluded from the industry.

We are aware of initial discussions between the financial services industry, the Ministry of Economic Development and the Securities Commission about an appropriate regulatory regime for financial advisers and, particularly, the possibility of further regulation. We welcome these discussions and urge progress towards a self-regulatory model for financial advisers, in a manner that minimises the costs imposed on advisers and consumers.

We think the best way to achieve this would be for the financial services industry to develop an agreed approach to self-regulation and report back to the Government with a comprehensive proposal by the end of 2004. An independent chair from within the industry could facilitate this.

62 Review of Securities Trading Law: Investment Advisers, see www.med.govt.nz

This approach should ensure timely progress is made towards an agreed regulatory regime between the industry and Government, as part of the wider review of the Securities Act and related legislation.

We anticipate the proposed self-regulatory approach would cover all those who provide savings and investment advice and would include a code of ethics, dispute resolution and disciplinary procedures and, possibly, training for advisers.

Post-retirement and the role of annuities

PRG2003 considers the post-retirement phase in general, and annuities in particular, are an important piece of the private provision jigsaw but have received limited policy attention.

Annuities are products that enable people to convert an asset into a future income stream. They are usually purchased from a life insurer for a lump sum and provide a regular income for a fixed period or until the purchaser dies. The use of annuities is the main way retirement income assets are converted to income in some OECD countries.

Debate about private provision in New Zealand is focused on asset accumulation; there has been little focus to date on converting assets to income. Converting assets to income will become increasingly important in New Zealand as the population ages.

Susan St John prepared an analysis of the annuity market for PRG2003. Her findings confirmed the earlier findings of the 1992 PPR Task Force and PRG1997: that there is little purchase of annuities in New Zealand and the annuities market here remains undeveloped.⁶³

The lack of demand for annuities is caused by various factors, including New Zealanders' desire to self-manage their assets and the fact that NZS is a form of annuity payment. PRG2003 considers the tax treatment of annuities is a significant barrier to their development. Susan St John describes the tax treatment of annuities as their "death knell".

The problem is the same as that affecting superannuation schemes and life insurance funds, as discussed in Chapter Seven 'Taxation of Savings'. Most potential annuitants are on a marginal tax rate of 21 percent, while annuity funds are taxed at 33 percent. They would be over-taxed by 12 percent if they purchased annuities.

As housing is the primary asset for most New Zealanders, house equity reverse annuity mortgages could play an important role in future private provision. PRG2003 is aware of a number of companies who are interested in developing house equity reverse annuity products in New Zealand. Removing the tax barriers would be a step towards encouraging the use of annuities as a form of private provision.

63 St John S (2003)

An additional tax barrier exists for home equity reverse annuities. Under a home equity reverse annuity, the homeowner is able to purchase an annuity by using the equity in the house to pay the premium. The premium is payable on the death of the house-owner (a deferred premium). Under the current life insurance tax rules, the income earned by the annuity provider on behalf of the annuity purchaser in respect of the annuity investment should be taxed. However, due to a technicality with the existing rules, such investments are over-taxed.

PRG2003 understands that the latter problem could be addressed in the context of the proposed review of the tax rules applying to life insurance, which will be considered as resources permit.



**CHAPTER NINE
IMPLEMENTING PRG2003's
PROPOSED WORK PROGRAMME**

CHAPTER NINE IMPLEMENTING PRG2003's PROPOSED WORK PROGRAMME

We think policy reviews occurring only once every six years are too far apart to adequately inform retirement income policy. By the time the next scheduled review takes place in the year 2009, the advance guard of the ageing baby boomers will be entering their 65th year. Thereafter, the growth in the numbers of those aged 65 plus will be rapid and will put increasing pressure on the government budget, particularly for NZS and health costs.

A six-year gap is also too long to review trends in private saving. A lot could change for future cohorts, such as declining home ownership, and increasing household debt. Trends in public provision, too, need to be kept under more regular review.

We understand that the Government intends to transfer the responsibility for preparing periodic reports to the Retirement Commissioner.⁶⁴ This change provides an opportunity to restructure the policy review process and better define the Retirement Commission's role in the process.

We recommend the establishment of an ongoing work programme to replace the six-yearly reviews. We anticipate the work programme would be based on the Government's response to PRG2003's policy proposals.

The role of the Retirement Commission would be to monitor the progress of the work programme. In the context of this monitoring role we recommend that the Retirement Commission establish an advisory group to create a mechanism for stakeholders to provide comment and input into the work programme. The advisory group should include academic experts, representatives from employers, unions, finance industry, and officials. In addition we recommend that by the end of 2007 the Retirement Commission, in consultation with its advisory group, review retirement income policy. The review should:

- report on progress and change in retirement income policy
- report on the risks and opportunities identified in the PRG2003 report
- highlight the issues needing policy attention
- assess the proposed work programme approach and whether it should be continued.

64 Ministry of Social Development (2002)

Work programme

Throughout our report we have made a number of recommendations. All of these recommendations are set out in Appendix A. Our key recommendations are brought together here to form a possible work programme.

Establishing a Work-based Savings Group

A key proposal that we have identified to ensure progress is made with work-based savings is the establishment of a Work-based Savings Group, chaired by the Retirement Commissioner, whose membership would comprise employers, unions, academic experts, officials and the financial services industry.

Enhanced education and information

The Retirement Commission needs to have an enhanced role in ensuring that people have the required information on both public and private provision to help them make sound decisions about financial planning and management throughout their lives.

The Retirement Commission's role should be extended to: promoting workplace seminars; expanding the Sorted programme and supplementing it with a face-to-face or telephone information service; establishing a methodology to make fees for savings products more transparent and promulgating the methodology as an industry standard; and developing criteria for assessing the appropriateness of savings products for retirement saving.

The ability of women, Māori and Pacific peoples to make private provision for retirement face the obvious barrier of limited disposable income and lower labour force participation. While it is unrealistic to expect many in these groups to make substantial private provision for retirement we consider more can be done to help these particular groups. This primarily must involve the Retirement Commission developing education and information programmes tailored to meet the characteristics of each group.

Further research and monitoring of trends

The Retirement Commission needs to take responsibility for co-ordinating the ongoing monitoring of risks and opportunities to private provision. The initial focus should be on the impact on private provision for retirement of variables such as financial liabilities, student loans and home ownership.

A research fund, managed by the Retirement Commission with guidance from an independent panel of experts to be appointed by the Retirement Commissioner, needs to be established to extend and develop research on household saving behaviour.

Removing tax disincentives

Priority must be given to removing the taxation disincentives that exist for some savers and some methods of saving. For Inland Revenue and Treasury this includes: resolving the tax non-neutralities arising from the indistinct capital/revenue boundary; resolving disparities in the treatment of international investments; addressing the inequities in the taxation of superannuation funds and life insurance companies; addressing the inequitable situation for the tax on employer contributions to superannuation funds; and reviewing the fund withdrawal tax.

Improvements to the regulatory environment

Further work can be carried out to improve the regulatory environment. An important first step is ensuring that the Government removes the prospectus requirement from employer superannuation schemes, as proposed in the Business Law Reform Bill currently before Parliament. In addition, there are other areas where improvement can be made.

First, the Ministry of Economic Development and the Government Actuary can review how much 'leakage' is taking place from employer superannuation schemes because of the written consent requirement for member transfers, and assess whether it is practical to better facilitate transfer in cases where transfer provides equivalent benefits. Second, the financial services sector needs to agree on an approach to self-regulation of financial advisers. Finally, the tax barriers that exist to the development of annuities, in particular home equity reverse annuity mortgages, should be examined by Inland Revenue and Treasury.



APPENDICES

APPENDIX A: RECOMMENDATIONS

PRIVATE PROVISION: THE RISKS AND OPPORTUNITIES

The Periodic Report Group 2003 (PRG2003) recommends that:

- The Retirement Commission take responsibility for co-ordinating the ongoing monitoring of risks and opportunities to private provision, initially focussing on:
 - the impact of increasing financial liabilities on private provision for retirement
 - the impact of student loans and home ownership on private provision for retirement
 - the impact of labour force participation by those aged 65 plus on net worth, retirement income and decisions to retire.
- We need ongoing data and research to give estimates of net worth at different points in time. The Household Savings Survey has been an important step forward, but only a first step, and should be repeated. This would enable the analysis of cohort effects (such as the impact of household debt) and ongoing patterns of saving, and the testing of policy changes on savings behaviour.
- A research fund, managed by the Retirement Commission with guidance from an independent panel of experts to be appointed by the Retirement Commissioner, is established to extend and develop research on household saving behaviour.

WORK-BASED SAVINGS

PRG2003 recommends that:

- The Government establish a Work-based Savings Group (WSG) to develop an agreed approach to promote work-based savings by the end of 2004.
- The WSG membership should include employers, unions, academic experts, officials, the financial services industry, and be chaired by the Retirement Commissioner.
- The WSG should focus its work programme on:
 - education through the workplace for employees
 - minimising regulatory and compliance costs
 - scheme design and best practice
 - training and resource support for employers and unions
 - sector or industry-wide approaches to facilitating work-based savings
 - reducing the costs for employers to provide access to work-based savings

- assistance for small employers to encourage work-based savings
- assistance for those on low incomes to access work-based savings
- getting employees started saving for retirement.
- The WSG should set milestones to assess changes in the membership of work-based savings schemes.
- The Government consider the possibility of extending the new public service savings scheme beyond the core public service; in particular, providing for organisations in the wider state sector to opt into the new scheme.

PERSONAL FINANCIAL EDUCATION AND INFORMATION

PRG2003 recommends that the Retirement Commission:

- Promote workplace seminars and either provide them itself or contract providers to do so.
- Extend the Sorted programme to include more information, targeted information and supplementary written materials.
- Increase its promotional campaigns to encourage New Zealanders to use Sorted and other PFE programmes.
- Provide a face-to-face or telephone information service to supplement Sorted.
- Enhance and extend its provision of information about public provision.
- Establish a methodology to make fees for savings products more transparent.
- Develop criteria for assessing the appropriateness of savings products and advice for retirement saving.

ISSUES FOR WOMEN, MĀORI AND PACIFIC PEOPLES

Women

PRG2003 recommends that:

- The Retirement Commission make it a key education priority to increase the knowledge of women about the need to save for retirement on their own behalf. We recommend a particular focus on the periods in women's lives when they have disposable income.
- The Retirement Commission develop criteria for a 'best-practice' vehicle for retirement savings that accommodates the needs of those people with periods of broken employment or reduced earnings during their working life.
- Efforts continue to be made to close the gender pay gap in the state sector and recommend these efforts extend across the labour market.

Māori

PRG2003 recommends that:

- The Retirement Commission, in consultation with Te Puni Kōkiri, develop a research programme to address the information gaps regarding Māori experience and attitude to savings and to facilitate a better understanding of Māori attitudes to retirement saving.
- If it is successful, the financial education pilot programme for young Māori, developed in partnership between the Retirement Commission and Ngāi Tahu, is extended.
- The Retirement Commission and Te Puni Kōkiri work with interested Māori organisations to assess the feasibility of those organisations taking an active role in the provision of savings and insurance services for the organisations' beneficiaries.

Pacific peoples

PRG2003 recommends that:

- The Retirement Commission work with Pacific communities to facilitate education programmes, tailored to the Pacific peoples, which highlight the benefits of preparing for retirement. These programmes should take into account the important characteristics of Pacific peoples we have identified, such as the existing commitments to the church, the extended family and the community.
- The Retirement Commission, in consultation with the Ministry of Pacific Island Affairs, facilitate research to see whether the current arrangements in which extended family groups establish trusts for various events, such as weddings and funerals, could be involved in superannuation funds and insurance schemes.

TAXATION OF SAVINGS

PRG2003 recommends that the Government:

- Make it a priority in its tax work programme to resolve the tax non-neutralities arising from the indistinct capital/revenue boundary.
- Continue its work to resolve disparities in the treatment of international investments.
- Revisit options, such as those developed by the Working Party on Taxation and Life Insurance and Superannuation Fund Savings (TOLIS), to address inequities in the taxation of superannuation funds and life insurance companies.
- For equity reasons, either remove the tax advantage for employees earning over \$60,000 on employer contributions to superannuation funds or make it available to all taxpayers irrespective of their marginal tax rate.
- Review the fund withdrawal tax and remove it if there is no compelling evidence it is successfully acting as an anti-avoidance mechanism.

FINANCIAL SERVICES MARKET AND REGULATION

PRG2003 recommends that:

- The Government remove the prospectus requirement from employer superannuation schemes, as proposed in the Business Law Reform Bill currently before Parliament.
- The Ministry of Economic Development and the Government Actuary review how much leakage is taking place from employer superannuation schemes because of written consent requirements for member transfers, and assess whether it is practical to better facilitate transfers in cases where transfer provides equivalent benefits.
- The Retirement Commission promote best practice guidelines for dispute resolution for group and employer superannuation scheme members.
- The financial services sector develop an agreed approach to self-regulation of financial advisers and report to Government with a comprehensive proposal by the end of 2004.
- The Government's proposed review of the tax rules applying to life insurance consider the tax barriers to the development of annuities; in particular, home equity reverse annuity mortgages.

IMPLEMENTING PRG 2003'S PROPOSED WORK PROGRAMME

PRG2003 recommends that:

- An ongoing work programme, based on the Government's response to PRG 2003's recommendations, is established to replace six-yearly reviews.
- The Retirement Commissioner monitors the progress of the work programme.
- The Retirement Commission establishes an advisory group to provide a mechanism for stakeholders to provide input into the work programme.
- By the end of 2007 the Retirement Commission, in consultation with the advisory group, review retirement income policy. The review should:
 - report on progress and change in retirement income policy
 - report on the risks and opportunities identified in the PRG2003 report
 - highlight the issues needing policy attention
 - assess the proposed work programme approach and whether it should be continued.

APPENDIX B: SAVINGS IN NEW ZEALAND

Measuring savings is a complex issue. The ongoing debate about New Zealand's national and household savings is complex and often confused, mixing concerns about low national saving, current account deficits, household liabilities and retirement income. A paper prepared for PRG2003 by Treasury provides a synthesis of the wider debate about saving in New Zealand.⁶⁵

We do not attempt to address the wider savings debate. Our focus is on retirement savings. We focus our analysis on the 2001 Household Savings Survey disaggregated household data. It tells us much more about savings dynamics than aggregate savings data which hides the differences between households that may be saving for retirement and younger households that may not have started saving, or households of retired people who are running down their savings.

DEFINING SAVINGS

Saving is the use of income for any purpose other than consumption. There are two ways to measure saving. First, the 'flows' approach, which looks at the difference between current income and expenditure over a certain period. Second, the 'stocks' approach, which looks at the change in net wealth (assets less liabilities) from one period to the next.

Our broad focus is on retirement savings, but we also consider whether retirement savings are different to savings in general. Theoretically, there is no difference - all saving is simply the excess of income over expenditure. However, some differences can be identified.

Generally, retirement savings are more difficult to measure because there is a far greater length of time between the decision to postpone consumption and when consumption may occur in the future. Retirement savings also tend to occur later in life because of the life-cycle dynamic where, in early years, income is lower and there are other competing priorities (for example, caring for children and mortgage commitments).

HOW DO NEW ZEALANDERS SAVE?

The Household Savings Survey was a cross-sectional nationwide survey that collected information in 2001 on New Zealanders' assets and debts. The survey looked at the stock of savings, the total value of assets less the total value of debts, described as net worth in the survey. While the survey is a rich data source, it provides only a snapshot.

⁶⁵ The Treasury (2003c)

The Household Savings Survey findings were summarised in a Statistics New Zealand report called 'The Net Worth of New Zealanders: A Report on Their Assets and Debts'.

The Household Savings Survey estimated the total net worth of New Zealanders aged 18 years and over at \$366.98 billion and median net worth at \$68,600.⁶⁶

Assets

Table 4 shows that New Zealanders hold most of their assets in the form of real assets and hold proportionally low amounts in financial assets. The value of total assets held by New Zealanders, as measured by the Household Savings Survey, was estimated at \$444 billion.

TABLE 4: ASSET COMPOSITION

Asset type	Population with asset %	Total value (million) \$	Proportion of total asset value %	Median \$
Māori assets	3	8,790	2	15,000
Trusts	4	28,709	6	216,000
Farms	4	38,257	9	350,000
Businesses	12	38,574	9	43,000
House, living in	48	159,205	36	160,000
Time share	1	137	0	8,000
Holiday home	2	4,361	1	80,000
Rental property	6	18,887	4	135,000
Overseas property	1	4,194	1	40,000
Commercial property	2	7,343	2	150,000
Other property	4	9,863	2	95,000
Superannuation	21	24,737	6	25,000
Life insurance	14	8,797	2	15,000
Credit cards (positive balances)	3	95	0	500
Bank deposits (incl. bonus bonds)	91	26,000	6	2,300
Shares	21	13,986	3	5,000
Managed funds	9	11,864	3	23,900
Other financial assets	5	5,792	1	30,000
Money owed to respondent	8	3,835	1	5,000
Motor vehicles	77	16,871	4	8,000
Cash	3	191	0	1,600
Collectibles	25	6,857	2	5,000
Other assets	44	6,685	2	3,000
Total value		444,030		125,300

Source: Statistics New Zealand (2002b)

In terms of the value of assets, homes made up the largest proportion of total asset value (36 percent). The next largest asset types in terms of value were farms and businesses, which each made up nine percent of the total asset value.

⁶⁶ The median is for economic units, which are made up of the survey's two population groups - individuals (non-partnered) and couples. Unless otherwise stated, all data refers to economic units.

Liabilities

Table 5 shows that the value of total liabilities held by New Zealanders was \$68.3 billion. Mortgage debt made up the largest proportion, at \$54.6 billion, or 80 percent of total debt. The next largest debt type in terms of value was bank debt, at approximately \$6.7 billion, or 10 percent of total debt.

TABLE 5: LIABILITY COMPOSITION

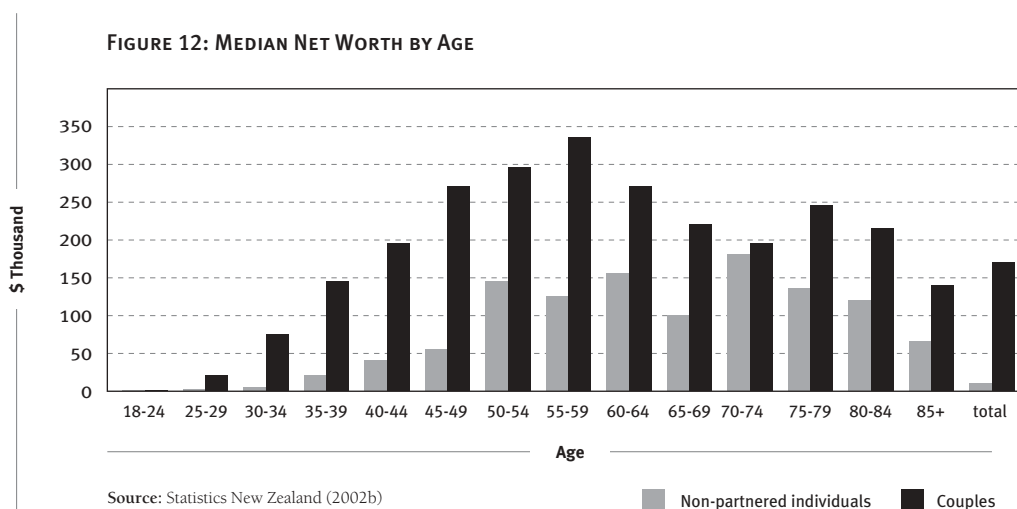
Debt type	Proportion of population with debt %	Total value (million) \$	Proportion of total debt value %	Median debt value \$
Mortgage	29	54,526	80	86,000
Bank debts (including accounts in overdraft)	24	6,707	10	3,000
Credit card (money owing)	46	1,926	3	1,000
Student loan	16	3,511	5	8,500
Hire purchase	18	741	1	1,100
Other debt	6	852	1	4,000
Total value		68,263		15,000

Source: Statistics New Zealand (2002b)

Student loan debt is the most significant debt type for those in the younger age groups. For those in the middle age groups, mortgage debt is the most significant, and for those 65 years and over, credit card debt is the most common debt type. Credit card debt (and bank debt to a lesser extent) is relatively common across all age groups but the value tends to be lower than student loan or mortgage debt.

Life cycle of saving

The Household Savings Survey data also confirms the life-cycle pattern of savings. Net worth tends to accumulate over the life cycle but decreases in later years. Figure 12 provides an overview of the pattern of the distribution of median net worth by age groups for non-partnered individuals and couples.

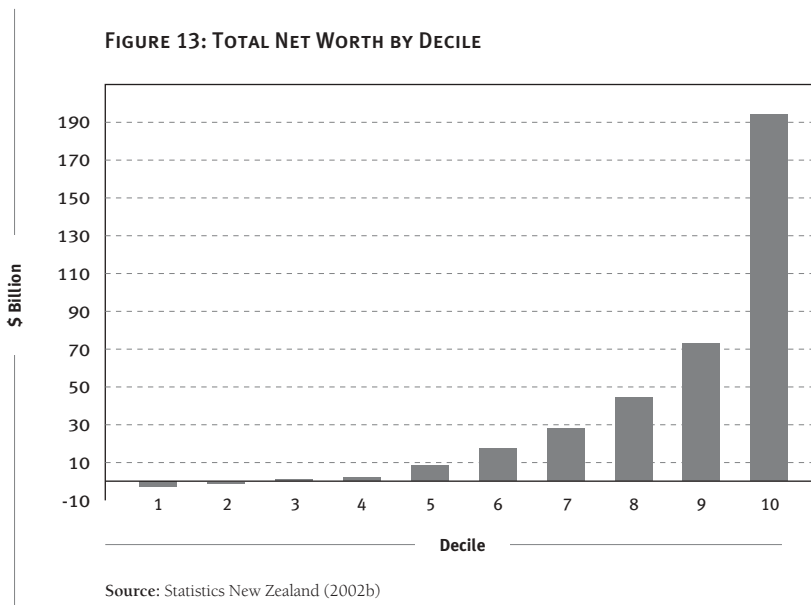


These life-cycle characteristics are important when considering the overall distribution of net worth, or when making comparisons between groups. For example, nearly half of 18 to 24-year-olds are in the lower quartile for net worth and just two percent are in the upper quartile. Figure 12 highlights that most New Zealanders do not begin to accumulate significant net worth until their mid-thirties, with net worth reaching its peak in the late fifties. Median net worth more than doubles between the mid-thirties and late fifties.

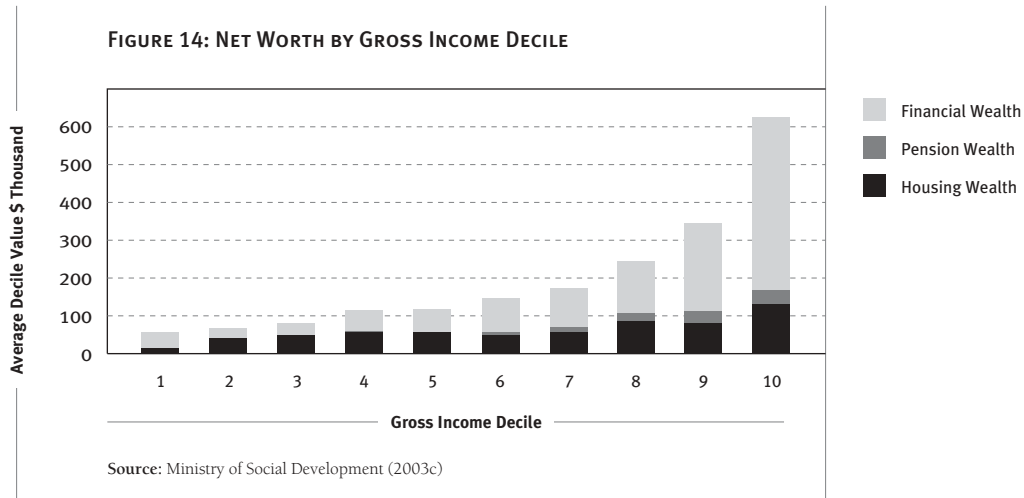
Distribution of net worth

Net worth is unevenly distributed. This is shown by the large difference between the median and mean net worth. For non-partnered individuals, the median was \$10,300 and the mean was \$97,900. For couples, the median was \$172,900 and the mean \$322,300. These differences arise because relatively small numbers have a very high net worth.

The uneven distribution of wealth becomes very apparent when the population is divided into deciles: the population is ranked from lowest to highest net worth and then divided into 10 even-sized groups, with decile 10 being the highest. Figure 13 shows the ninth and tenth deciles hold about 70 percent of total net worth, while the bottom three deciles have negative or minimal net worth.



Additional analysis of the net worth by gross income decile, by asset category, further highlights the uneven distribution of net worth. This is shown in Figure 14.



APPENDIX C: THE LIVING STANDARDS OF OLDER NEW ZEALANDERS

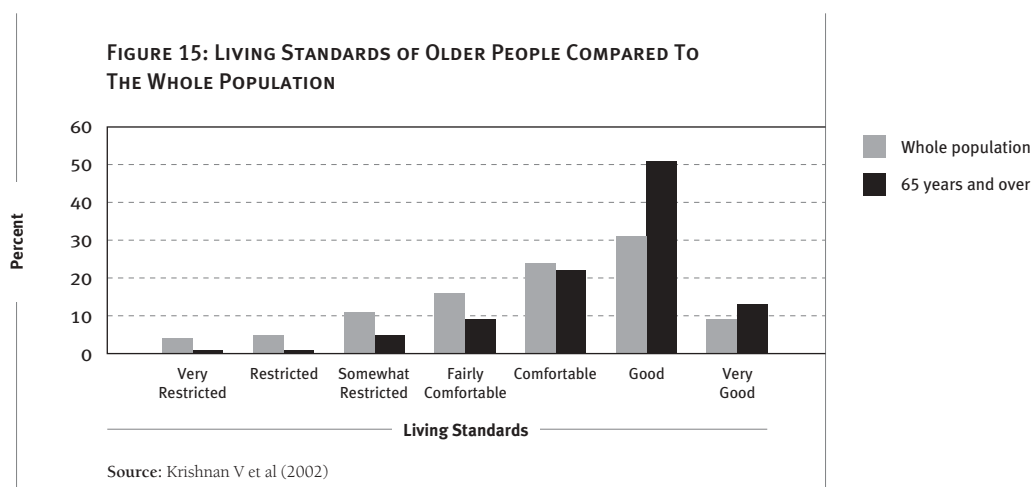
Since PRG1997, the development of the research on the living standards of older New Zealanders has been a key addition to our understanding of the impact of private provision on older New Zealanders. This research was initiated by the Super 2000 Taskforce and continued by the Ministry of Social Development.⁶⁷ The main survey involved 3,060 nationwide face-to-face interviews with older New Zealanders living in private dwellings and was supplemented by surveys of 500 Māori aged 65 to 69 years, and of 3682 people of working age.

The living standards that people experience in their retirement are based on both the public provision of income and assistance through NZS, subsidies and services (for example, health subsidies and public health services) and the private assets people have accumulated and the related income from these.

Some assets provide an income during retirement and other assets contribute to retirement living standards by reducing the income required; for example, a mortgage-free home. Retirement living standards will, therefore, be affected by private provision in the form of assets that offset living expenses (and the requirement for private income) as well as income.

The report on “The Living Standards of Older New Zealanders” showed that most older New Zealanders were doing quite well and had relatively few material restrictions and difficulties in terms of basic needs. A minority, around five percent, of older people have quite marked material hardship and a further five to 10 percent have some restrictions and hardship.

The better living standards of older New Zealanders compared to the total population are summarised in Figure 15.



67 See Fergusson D et al (2001) and Krishnan V et al (2002)

The research showed that nearly all older people received NZS. Eighty-eight percent of single persons and 93 percent of couples reported at least one other income source. Nevertheless, the research reinforced the importance of NZS, with over 60 percent of the total income received by single persons and couples being from NZS.

The overall levels of savings reported were also modest. For example, three-quarters of single respondents had savings and investments worth less than \$37,500 and three-quarters of the couples had savings and investments worth less than \$100,000. The findings indicate a population with relatively low levels of financial resources.

This is supported by additional analysis of the Household Economic Survey.⁶⁸ Across all 65 plus households, 55 percent of all income is from NZS and other transfers, like the disability allowance. For the lower 70 percent of couple households, 84 percent of all income is from NZS; for the lower 70 percent of single households, 96 percent of all income is from NZS.

Seventy-five percent of singles have less than \$5,000 per annum of income from sources other than NZS. Sixty percent of couples have less than \$7,700 per annum of income from sources other than NZS. For all individuals aged 65 plus, 65 percent have less than \$5,000 above NZS.

Significantly, the report on the Living Standards of Older New Zealanders found that the majority of the older population owned their own home (68 percent of single respondents and 86 percent of couples).⁶⁹ Further, most respondents who owned their own home did so mortgage-free. As a consequence of high home ownership, the accommodation costs across the older population were generally low.

The “Living Standards of Older New Zealanders” concluded that NZS and other associated payments, such as accommodation allowances, were able to protect the great majority of older people from hardship and material deprivation.

Although this was the case, the report noted that the avoidance of hardship in retirement is based on a combination of public and private provision. More specifically, therefore, these findings show that, *given the private provisions for retirement the current cohort of older people had made*, NZS and associated payments were sufficient to enable the majority of older people to avoid hardship.

68 Ministry of Social Development (2003c)

69 Fergusson D et al (2001)

APPENDIX D: WORK-BASED SAVINGS IN NEW ZEALAND

GOVERNMENT ACTUARY DATA

The Government Actuary annual report has consistently highlighted the decline of work-based savings over the last decade. Table 6 shows that membership of schemes declined from 310,741 in 1990 to 246,946 by this year.

While membership declined rapidly in the early 1990s, the membership appears to have been stable at around 245,000 over the last four years and increased by almost 2,000 in 2003, the first increase since 1990. We suspect the increase partly reflects the establishment of the new Teachers' Scheme in 2002. The decline in the number of schemes reflects the closure of a large number of smaller schemes and the amalgamation of schemes into master trusts.

While membership of registered employer schemes has declined, this has been offset by a rapid increase in membership of retail super schemes, with total membership of retail schemes almost doubling since 1990.

TABLE 6: NATURE OF SUPERANNUATION SCHEMES

Nature of scheme	Number of schemes		Total Assets (\$m)		Total Membership	
	1990	2003	1990	2003	1990	2003
Private	508	49	58	29	550	70
Employer (1)	2,242	514	9,508	9,572	310,741	246,946
Employer (2)	0	7	0	364	0	16,710
Retail	113	125	1,466	7,350	236,062	420,205
Total	2,863	695	11,302	17,314	547,353	683,931

Source: Government Actuary Newsletter, No. 56, July 2003

Note:

'Private' - set up by individuals for themselves and family.

'Employer (1)' - sponsored by private sector employers and all NPF employer sponsored schemes.

'Employer (2)' - provide superannuation arrangements as alternative to the Government Superannuation Fund, sponsored by public sector employers and approved under section 84C of the State Sector Act 1988.

'Retail' - membership is made available to the general public.

HOUSEHOLD SAVINGS SURVEY

The Retirement Commission commissioned further analysis of the 2001 Household Savings Survey data to provide a snapshot of the coverage of both personal and work-based superannuation schemes.⁷⁰

The analysis shows that across all couples, in 20 percent of the cases, at least one partner has a work-based superannuation scheme. However, across all non-partnered individuals, four percent are members of work-based schemes.

Non-partnered individuals

Of the total population of unpartnered individuals, 88 percent have neither personal nor work-based schemes, while one percent have both; four percent have a work-based scheme and eight percent of all individuals have a personal scheme.

Overall, the mean value of the holdings in work-based schemes is \$51,226 and in personal schemes is \$48,723. These distributions are highly skewed, with a few individuals having very large holdings. The median holdings are, respectively, \$11,665 and \$12,000.

The median holding by females is much higher than that for males for both types of schemes. The mean level of personal superannuation is higher for females, while their mean holdings of work-based super are lower than for males, suggesting that women make greater use of personal rather than work-based schemes.

For unpartnered individuals not holding a work-based scheme, the median net worth is \$6,000 for males and \$12,500 for females. In comparison, those holding such schemes (many of whom will be older workers) have median net worth of \$66,120 and \$61,583 of net worth respectively.

Couples

Across all couples, in 35 percent of the cases, at least one partner has a superannuation scheme; 15 percent have a work-based scheme, 13 percent have a personal scheme and seven percent have both. The remaining 65 percent of couples have no superannuation scheme.

Of couples in which at least one partner holds a work-based scheme, over 40 percent have in excess of \$50,000 value in the scheme. Over 50 percent of couples holding a personal scheme have more than \$20,000 value in the scheme.

The median net worth of couples with a work-based scheme is over \$80,000 more than a comparable couple without a scheme. The median value of the holdings by couples with at least one partner enrolled represents 30 percent of their total net worth.

There is some tendency for the proportion of couples enrolled in a work-based scheme to increase with age, but the overall trend is not striking. The value of the holdings increases markedly with age and, for older couples, work-based superannuation reflects an important share of their total net worth.

70 Scobie G and Le T (2003)

ESR CONSORTIUM SURVEY

To better understand the current state of employer-based savings in both private and public organisations, we commissioned the ESR Consortium to conduct a survey of employers and their employees based on the Top 100 employers by number of employees.⁷¹ The survey also looked at a range of medium and small enterprises and covered a total of 306,000 employees and 162 organisations. The survey's coverage is set out in Table 7.

TABLE 7: ESR CONSORTIUM SURVEY COVERAGE

	Number of employers	Total employees
Top 100	78	288,542
Middle group	53	17,096
Smallest firms	31	553
Totals	162	306,191

Seventy-one percent of the firms interviewed had a plan open to at least some of their employees. The larger the firm, the greater the probability of having an open plan. Seventy-eight percent of the Top 100 firms had a plan. For the middle group, the figure is 65 percent, and for the smallest firms, 60 percent.⁷² Overseas-owned employers were most likely to have an open plan, with 82 percent having an open plan. See Table 8.

TABLE 8: SUPERANNUATION PLAN OPEN TO NEW ENTRANTS

	All employers	By all employees	By employers only:		
			Top 100	Middle group	Smallest
Those with an open plan	71%	81%	78%	65%	60%
No plan open	29%	19%	22%	35%	40%
Number of employer responses	160	160	78	52	30
Proportion employees eligible to join	79%	79%	79%	74%	100%
Number of employer responses	72	72	46	21	5

Note: Only 72 (75%) of 113 open plans in respect of all employers supplied information on eligibility. There would probably be a tendency for the proportion of eligible employees to be overstated, as those with 100% eligibility would say so. Those with restricted eligibility probably find it more difficult to extract the information requested.

Even allowing for the fact that the survey is skewed towards the largest employers, the number of employers with open schemes points to a more positive environment for employer super than we had anticipated finding. Of those with open plans, respondents estimated about 79 percent of employees were eligible to join and 89 percent were subsidised. The subsidies were mainly in the form of a retirement saving subsidy (75 percent), with 50 percent providing fees and 40 percent life disability insurance. See Table 9.

⁷¹ ESR Consortium (2003)

⁷² The number of small and medium firms with open plans is likely to be exaggerated, as the sample was very small and not intended to be representative of small firms nationally.

However, while there were more open plans than we had anticipated, only 27 percent of employees in the organisations with open schemes were members of the scheme. Membership of the schemes identified in the survey appears to be focused on executives and salaried staff, with waged and part-time staff having less access. Also, participation rates in the schemes - that is, the percentage of eligible members who join the schemes - vary significantly from 68 percent for executives to 42 percent for part-time workers. See Table 9.

TABLE 9: SUMMARY OF PLAN MEMBERSHIP AND PARTICIPATION

	By all employers	Top 100	Middle group	Smallest
Total plans	123	70	35	18
Total membership	83,465	75,764	7,502	199
% all employees in group	27%	26%	44%	36%
Average members per plan	679	1,082	214	11
Whether plan subsidised:				
- yes	89%	90%	91%	78%
- no	11%	10%	9%	22%
Level of subsidy (see note):				
- fees	50%	43%	63%	56%
- life/disability insurance	40%	30%	71%	17%
- retirement saving	75%	77%	77%	61%
Who can join (% eligible employees who have joined)?				
- executives	84% (68%)	79% (55%)	86% (86%)	100% (88%)
- salaried	88% (63%)	80% (61%)	100% (68%)	94% (56%)
- waged	67% (55%)	66% (51%)	71% (64%)	61% (50%)
- part time	43% (42%)	43% (41%)	37% (37%)	56% (55%)

Note: Plans can have more than one type of subsidy.

These findings are broadly consistent with the recent analysis of collective contracts from the Victoria University employment contract database.⁷³

Thirty-nine percent of the 288,000 workers covered by collective agreements have a superannuation provision in the agreement, with two thirds of those having an employer contribution available. The coverage in the private sector was lower, 31 percent, than in the public sector, 44 percent.

73 Thickett et al (2003)

APPENDIX E: MEMBERSHIP OF SUPERANNUATION SCHEMES - A POSSIBLE IMPACT ON NET WORTH

The Retirement Commission commissioned an analysis of the 2001 Household Savings Survey to assess the impact of membership of superannuation schemes on net worth.⁷⁴ The analysis shows that, for some people, saving in a work-based superannuation scheme with an employer contribution appears to increase net worth relative to those who do not save in such a scheme. The type of saving vehicle used matters. There appears to be something about saving in work-based schemes that makes a difference to the overall level of net worth. Why this might be is a matter for further research, but one possible explanation is that because the savings are deducted directly from pay, individuals make subsequent saving decisions based on their net pay and take limited account of their work-based savings.

The analysis attempted to isolate the impact of both private and work-based superannuation schemes on net worth from the impact of other variables such as age, gender and income.

For most unpartnered individuals, membership in a private or work-based superannuation scheme appears not to have a statistically significant impact on net worth. However, a strongly significant effect is found for unpartnered females holding personal retail schemes. They have a total net worth of over \$60,000 more than females not enrolled in a personal scheme.

The analysis shows that, for couples in which either partner had a work-based superannuation scheme, their net worth was \$80,000 greater than couples in which neither partner had a work-based scheme. It appears that couples where a partner has a scheme have chosen to accumulate funds in a work-based scheme without making a comparable reduction in other forms of saving.

Some caution is needed in drawing conclusions from these results.

Even in the case where those having a scheme have a higher total net worth, this could reflect the fact that those with a greater inclination to save are the ones most likely to be enrolled in a work-based scheme. In other words, a small proportion of people have voluntarily signed up for work-based schemes and, even in the absence of such schemes, it may be that they would have higher accumulations anyway. The extent of self-selection is hard to assess, but our judgement is that it is unlikely to be sufficient to nullify the results.

It is also important to emphasise that it does not follow from these results that those who invest in these schemes in the future will accumulate more retirement wealth. Some caution is needed before inferring that these patterns would be repeated in the wider population, especially if an extended work-based scheme did not involve the employer contributions that applied in the case of those surveyed.

⁷⁴ Scobie G and Le T (2003)

APPENDIX F: WHAT ABOUT THE AUSTRALIAN APPROACH?

We are often asked why New Zealand didn't simply adopt the Australian approach to retirement income. The simple answer is different sets of circumstances and different trade-offs.

Australia's compulsory system was introduced in 1986 and extended in 1992. It was introduced when a set of very specific circumstances existed. At the time, Australia had a highly centralised wage fixing system, and an electoral accord between the Australian Labour Party and the Australian Council of Trade Unions. Australia also faced a balance of payments crisis. There was wide support for the idea of converting a wage increase due into individual savings account balances. The combination of these factors made it possible to introduce a compulsory system. The regime is widely accepted in Australia.

New Zealand has chosen a different option. Both regimes are creatures of the environments in which they developed. Each is designed to meet the retirement income objectives of their respective countries.

APPENDIX G: SUBMISSIONS AND MEETINGS

Written submissions are available on www.treasury.govt.nz/prg

We had written submissions from:

Age Concern	Mary Holm
Alice Cheng	MCA Ltd
AMP Financial Services	Mercer Human Resource Consulting
Apex Advice Group	Michael Littlewood
Association of Superannuation Funds of New Zealand (ASFONZ)	National Council of Women
AXA New Zealand	NZ Business Roundtable
BT Funds Management	NZ Council of Trade Unions
Business NZ	NZ Society of Actuaries
Christopher Arnesen	NZ University Students Association
Consumers' Institute	Office of the Banking Ombudsmen
Dr Nancy Pollock	Patricia Underwood
Eriksen & Associates Ltd	Patrick Adamson
Financial Services Federation	Peter Lynch
G Ross Gibson	Pip van Duyn
Grey Power Horowhenua	Planit Plans Ltd
Grey Power New Zealand	PMW van Bussel
Hamilton Budgeting Advisory Trust	Rob Dowler
ING (NZ) Ltd	Robert J Gregory
Insurance and Savings Ombudsmen	Ruth Humphrey
Investment Savings and Insurance Association (ISI)	Sean McRae
John Stockman	Sovereign Group Ltd
Lyndon Weggery	Susan St John
Margaret M Diprose	TDW
Marie and John Brophy	Tony Williams
Mark Weaver	Toyota Group Pensions Plan
	United Future
	Women in Super

We had meetings with:

Hon Steve Maharey (Minister for Social Development and Employment)
Hon Dr Michael Cullen (Minister of Finance)
John Melville (Government Actuary)
Women in Super
Angela Foulkes
Professor Gary Hawke
Anne Knowles
Colin Blair
Peter Harris
Judith Davey (NZ Institute for Research on Ageing)
Ross Kent (AMP)
Rodney Hide (ACT Party)
Gordon Copeland (United Future Party)
Rod Donald (Green Party)
Don Brash (National Party)
Simon Carlaw (Business NZ)
Simon Swanson (Investment Savings and Insurance Association)
Roger Kerr (NZ Business Roundtable)

Bruce Kerr and Mike Woodbury (ASFONZ)
David Russell and Peter Rankin (Consumers' Institute)
Ross Wilson and Peter Conway (NZ Council of Trade Unions)
Lili Tuioti and representatives of the Pacific peoples community
Jill Spooner
Michael Chamberlain
Mary Holm
Ian MacDonald (Carter Holt Harvey)
Bernard Reid and Mark Weaver (NZ Society of Actuaries)
Craig Stobo (BT Funds Management)
New Zealand University Students Association
Jonathan Eriksen (Eriksen & Associates Ltd)
Philip Matthews (Financial Planners and Investment Association)
Ralph Stewart and David Hair (AXA New Zealand)

APPENDIX H: BACKGROUND PAPERS AND OTHER REFERENCES

BACKGROUND PAPERS

The papers are available on www.treasury.govt.nz/prg and www.retirement.org.nz

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