THE PLACE OF KIWISAVER IN NEW ZEALAND'S RETIREMENT INCOME FRAMEWORK

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SUMMARY OF KEY POINTS

Purpose of the Report

This report provides background for the 2013 Review of Retirement Income policy by the Commission for Financial Literacy and Retirement Income (CFLRI) on the role of private savings for retirement, with particular reference to trends in KiwiSaver, and the role of the financial services sector in helping to ensure the adequacy of retirement income for New Zealanders. The report will contribute to the overall review as it considers the ideal future balance between pay as you go (PAYGO) (i.e. tax-based) and save as you go (SAYGO) funding in New Zealand's retirement income framework. Increases in the cost of NZS arising from demographic change, along with increased expectations of standards of living in retirement, point to likelihood of a greater role for private savings.

Overview of KiwiSaver

- KiwiSaver was set up to encourage a long-term savings habit with a view to supporting a similar standard of living post-retirement as in pre-retirement.
- It locks in savings until age 65 via a voluntary approach to retirement savings with incentives for everyone, and automatic enrolment (with opt-out provisions) for new employees, as well as compulsory employer contributions.
- Employees elect to contribute from their after-tax pay at the rate of 2% (the minimum), 4% or 8% of their gross salary.
- Employees who do not select a scheme are randomly allocated to a default scheme.
- Employers must contribute an amount equal to 2% of gross salary to their employees' KiwiSaver schemes.
- The minimum rates of employer and employee contributions to KiwiSaver will increase to 3% of gross pay in April 2013.
- Employer's superannuation contribution tax (ESCT), which is typically the same as the employee's marginal tax rate, is deducted from employer contributions before they are paid to KiwiSaver accounts.
- Employers with their own qualifying work-based savings schemes can offset contributions to these schemes against KiwiSaver obligations, but typically only for employees who joined before 1 April 2008.
- Employers send both employer and employee contributions to Inland Revenue with PAYE payments.
- Government provides a one-off, $1000 *kick-start* contribution to a new KiwiSaver account, and a Member Tax Credit (MTC) contribution of 50c for each dollar a member contributes (up to a maximum MTC of $521 per year, which equals $10 per week). Complying superannuation funds also access the MTC where member contributions are paid on a KiwiSaver equivalent 'locked in' basis.

- After three years in KiwiSaver, individuals and couples can withdraw their own, and their employers', contributions to buy a first (and in limited circumstances a subsequent) home and receive a first home purchase subsidy of $1,000 per year of KiwiSaver contributions (up to $5,000 each and $10,000 for a couple).
- From July 2013 (and initially as at 30 June 2013) fund managers must begin reporting their performance and returns, fees and costs, assets and portfolio holdings, liquidity and liabilities, and key personnel, along with any conflicts of interest, in a standardised format.

Membership, contributions and withdrawals

- KiwiSaver is now part of the retirement income framework for half of eligible New Zealanders. Membership has hit 2 million and continues to rise.
- Around 38% of KiwiSaver members were automatically enrolled and fewer people now opt out. KiwiSavers have slightly higher incomes than non-members.
- Non-members who are self-employed, casual employees, or not in work, are not subject to any "soft compulsion" triggers.
- Almost as many KiwiSaver members have opted in directly with providers as have either opted in via their employer or been automatically enrolled by their employer.
- In the year to June 2012, around 75% of members who are eligible for the member tax credit made some contributions to their account.
- The proportion of wage and salary earners who contribute at the lowest level of 2% has grown from 41% in 2010 to 59% in 2012.
- In 2010/2011, the median annual contribution by wage and salary earners (excluding the employer contribution) was $829. Members over 18 years who earned only non-salary or wage income mostly contributed either $1,043 or $1,200 per annum to their KiwiSaver – that is at a level to maximize their MTC.
- The Crown contributed 32% of all contributions to KiwiSaver between in 2011/12, down from 55% in 2007/08.
- IRD reports that at 31 December 2012, 15,575 KiwiSaver members, or a third (32.5%) of the estimated members who were eligible to withdraw savings because they had reached the age of 65 and had been members for at least five years, had closed their KiwiSaver accounts. Further analysis on withdrawals is forthcoming.

The funding of employer contributions

- Most employer contributions are in addition to an employee's gross salary or wages but some employers have negotiated a total remuneration package – that is an employee receives a fixed amount of remuneration and, if that employee is a member of KiwiSaver, the cost of the employer contribution comes out of the employee's pay.
- The Employment Court has ruled that, under a total remuneration approach, gross wages cannot fall below the minimum wage of $13.50 an hour.

- Pressures on remuneration budgets across the public and private sectors may lead to more employers using a total remuneration approach if they can reduce current and future costs this way.
- Since July 2012, state sector agencies have had to fund KiwiSaver contributions from their own budgets – previously a central fund of around $181 million reimbursed them for employer contributions to KiwiSaver and other retirement schemes.
- KiwiSaver members and employers generally benefit from KiwiSaver contributions being an additional payment. Where employers have a strong position in negotiations, taking a total remuneration approach with new employees can reduce their future liabilities. A total remuneration approach is also likely to reduce the costs to employers from future increases to the level of their compulsory contributions.
- A total remuneration approach makes pay systems transparent and would benefit non-KiwiSaver members. However, total remuneration also reduces the attractiveness of KiwiSaver to all members.

Investments in KiwiSaver schemes

- $14,096 million of the $35,163 million assets under fund management held in superannuation schemes are KiwiSaver funds. This is 18% of the $78,692 million total funds under management (September 2012).
- Based on self-reporting in a 2010 survey, approximately 36% of individual contributions to KiwiSaver represented additional saving
- At 31 March 2012, the average balance across all KiwiSaver accounts was $6,668 and the average balance in a default fund was marginally lower at $6,530.
- An analysis of three KiwiSaver providers found higher balances by age. Adult male balances were higher than female balances, and the gap widens between age 20-50.
- Morningstar finds average returns to KiwiSaver were low in the initial years particularly for more growth oriented funds; the most recent annual data shows growth oriented funds lead default and conservative funds.
- KiwiSaver is based on a competitive market for providers, including default providers, as well as the option to switch providers at any time. There is no government guarantee that KiwiSaver accounts will retain their value, let alone grow.
- Discipline on KiwiSaver providers comes from: the Financial Markets Authority (FMA) which is responsible for the administration, compliance monitoring and enforcement of the KiwiSaver Act; self-management and disclosure by KiwiSaver providers, and market pressure from KiwiSaver clients. The Reserve Bank's capital market regulations also have an impact.
- From July 2013 (and as at 30 June 2013), the KiwiSaver Periodic Reporting Regulations will require fund managers to report their performance and returns, fees and costs, assets and portfolio holdings, liquidity and liabilities, and key personnel, along with any conflicts of interest, in a standardised format on their websites.

- At 31 March 2012 24% of KiwiSaver members were in a default fund. Most (93%) members in an employer-chosen scheme are in the default option of that scheme.
- A discussion document on default provider arrangements was released in late 2012. There is no date set for decisions on a post-2014 regime.
- The absence of annuities that convert lump sums into regular payments until death will matter more as KiwiSaver balances grow and more members are eligible to withdraw. Without any compulsion to purchase annuities, there is little prospect for using KiwiSaver savings to offset New Zealand Superannuation or other health and welfare expenditures that benefit the retired population.

The place of KiwiSaver in the Retirement Income Framework

- KiwiSaver has grown quickly to become a large programme with over 2 million members with funds that hold $14 billion in assets.
- Policy is underdeveloped in relation to: the broader market of work-based superannuation schemes that comply with or complement KiwiSaver; KiwiSaver's fit in the Retirement Income Framework, and its relationship with other programmes.
- Other issues needing more attention include: the impacts of KiwiSaver on: wages and remuneration patterns; growth and productivity; fairness, and fiscal implications over the longer term.
- Currently, there is no direct relationship between KiwiSaver and other retirement income policies.
- Clarity about how KiwiSaver fits alongside other retirement polices, and how this may change in the future, is essential if stakeholders are to work together to support KiwiSaver going forward, and for any trade-offs to be identified and planned for.
- Gaps in information and data are difficult to prioritise without clear policy.
- It would be valuable to track the value of individual accounts by gender, age and other factors, such as employment status. This type of data could be obtained through sampling the tax records of individuals as all KiwiSaver schemes must file a return for individual members. However, IRD have noted that access to this data is governed by the Tax Administration Act.
- Tracking the extent to which employment agreements (both collective and individual) in both the private and the public sector involve total remuneration approaches, and who is impacted and how, is suggested.
- There is considerable reliance on KiwiSaver providers supplying their own information about their schemes. Transparency would be better supported by an independent and timely distillation of the disclosed information by the FMA, including the analysis of membership data within schemes.

SECTION ONE: INTRODUCTION

Background

KiwiSaver, a voluntary, subsidised, private retirement savings regime, has been in place less than six years and has over 2 million members. The Terms of Reference for the 2013 Review of Retirement Income policy by the Commission for Financial Literacy and Retirement Income (CFLRI) include a requirement to assess the role of private savings for retirement, including:

- trends in KiwiSaver, particularly withdrawal patterns of those retiring and the issues that these may raise; and
- the role of the financial services sector in helping to ensure the adequacy of retirement income for New Zealanders.

The 2013 Review will address the ideal future balance between pay as you go (PAYGO) (i.e. tax-based) and save as you go (SAYGO) funding in New Zealand's retirement income framework as increases in the cost of NZS arising from demographic change, along with increased expectations of standards of living in retirement, point to a greater role for private savings.

Approach

The paper has largely been developed through analysis based on secondary sources (literature and data) along with an analysis of KiwiSaver in Collective Employment Agreements (CEAs) undertaken by the Industrial Relations Centre, Victoria University. This paper has also been informed by discussions with Malcolm Menzies, CFLRI; Michelle Lloyd and Barb Lash, Statistics New Zealand; Teneti Ririnui, Meade Perrin, and Donna Finlayson, Inland Revenue Department (IRD); Adam Hunt, Financial Markets Authority (FMA); Cath Jackson, State Services Commission and Glenn Barclay, Public Service Association.

Structure of this report

- ***Section Two*** provides an overview of KiwiSaver design and rules
- ***Section Three*** looks at trends in membership, contributions and withdrawals
- ***Section Four*** discusses employers' approaches to funding compulsory contributions to KiwiSaver
- ***Section Five*** considers investments in KiwiSaver schemes
- ***Section Six*** comments on key policy issues and data gaps

SECTION TWO: KIWISAVER STRUCTURE

History and purpose

The KiwiSaver scheme was announced in Budget 2005, enacted by the KiwiSaver Act 2006 (the Act) and commenced on 1 July 2007.

The stated **purpose** of the Act is to: *"encourage a long-term savings habit and asset accumulation by individuals who are not in a position to enjoy standards of living in retirement similar to those in pre-retirement. The Act aims to increase individuals' well-being and financial independence, particularly in retirement, and to provide retirement benefits. To that end, this Act enables the establishment of schemes (*KiwiSaver schemes*) to facilitate individuals' savings, principally through the workplace* (Section 3)*"*. The objectives of KiwiSaver, as set out in its legislation, make no reference to national saving, productivity growth or debt reduction goals (Hurnard, 2011) although these could be regarded as implicit objectives.

KiwiSaver features

KiwiSaver is designed to lock in savings until age 65 via a voluntary approach to retirement savings with incentives for everyone and automatic enrolment (with opt-out provisions) for new employees, as well as compulsory employer contributions. Box One below sets out the main features in relation to overall scheme design, coverage and obligations of employees, obligations of employers, tax and subsidies, housing and forthcoming changes. KiwiSaver is most prescriptive for employees and their employers, and offers others the opportunity to save as much and as often as they choose within the KiwiSaver scheme. See also www.KiwiSaver.govt.nz and www.ird.govt.nz

Box One: KiwiSaver features

Scheme design

- KiwiSaver is open to all New Zealand citizens, and people living in, and entitled to live in New Zealand, permanently, who are under the age of 65.
- Saving occurs via individual accounts in a scheme provided by a registered KiwiSaver provider that provides a scheme to the public or a section of the public.
- Individuals can choose their KiwiSaver scheme and switch schemes at any time.
- Savings are locked in until the age of 65, and at least 5 years' membership (or death).
- Significant financial hardship or serious illness are grounds for early withdrawal.
- Individuals who leave New Zealand permanently can close their KiwiSaver account on signing a Statutory Declaration one year after departure (but must return their member tax credit amount to Inland Revenue) – from 1 July 2013 this will no longer be permitted following emigration to Australia, but transfers to Australian complying superannuation schemes (including member tax credits) will be permitted.

- After at least three years of membership and savings, first home buyers may access their savings (excluding the Government contributions amount) and apply them towards the purchase of a house in which they will live (see below).
- Individuals who are not employees (e.g. who work on contract and pay their own tax) enrol with a KiwiSaver scheme and choose how much and how often they contribute.
- Savers can remain KiwiSaver members after age 65 (or after completing 5 years' membership, if later) but will no longer attract any government contribution for new savings.

Employees

- Employees who meet residence/citizenship, age (18-64), and employment (not own account, casual or temporary) criteria are automatically enrolled in KiwiSaver when they start a new job (unless their employer has an approved alternative work-based saving scheme) and have an eight week period to opt out.
- Employees under 18 can join KiwiSaver but only by choosing and contracting direct with a KiwiSaver provider.
- Temporary employees employed for up to 28 continuous days are not enrolled automatically, but can opt in to KiwiSaver.
- Casual employees engaged on an irregular and intermittent basis and who receive holiday pay with their wages are not subject to automatic enrolment. Employees who are visiting New Zealand and live elsewhere or hold temporary, visitor or student work permits, cannot join KiwiSaver.
- Employees elect to contribute at 2% (the minimum, rising to 3% on 1 April 2013), 4% or 8% of their gross salary.
- Auto-enrolled employees who do not select a scheme, and those who 'opt in' to KiwiSaver without choosing a scheme, are randomly allocated to a default scheme provided by AMP, ASB, Mercer, OnePath or Tower (or, if their employer has chosen a scheme for KiwiSaver auto-enrolment purposes, their employer's chosen KiwiSaver scheme).
- After 12 months' membership, employees can take a contributions holiday for up to five years and can take as many contribution holidays as they like.

Employers

- Employers must automatically enrol all new employees in KiwiSaver and provide them with KiwiSaver information.
- Some employers with their own work-based saving scheme are exempt from automatically enrolling new employees in KiwiSaver, due to having a scheme that was approved by the FMA (before November 2009) as meeting criteria including being open to all new permanent employees and requiring a minimum overall contribution rate of 4%.

- Employers with their own qualifying work-based savings schemes can offset contributions to these schemes against KiwiSaver obligations, but typically only for employees who joined before 1 April 2008.
- Employers must contribute a minimum of 2% of gross salary to their employees' KiwiSaver schemes, rising to 3% on April 1 2013. Employers generally pay KiwiSaver contributions in addition to salary, but a total remuneration approach is possible.
- Employers send both employer and employee contributions to Inland Revenue with PAYE payments. IRD then passes contributions on to the relevant scheme providers.
- Employers are obliged to make contributions only when an employee's account is active, but can also voluntarily do so during contribution holidays.
- Employers do not have to contribute to KiwiSaver schemes for employees under 18.

Tax and subsidies

- Government provides a one-off, $1,000 *kick-start* contribution to a new saver's KiwiSaver account. This $1,000 contribution cannot be withdrawn under the hardship provisions, nor when purchasing a first home, but is part of withdrawals when closing a KiwiSaver account on leaving New Zealand permanently.
- At KiwiSaver's inception on 1 July 2007, Government paid an annual Member Tax Credit (MTC) of up to $1,043 per year (which equalled $20 per week) by matching individual contributions dollar for dollar for members aged over 18. Since July 2011, this has been reduced to a 50c contribution for every dollar contributed by a member, up to a maximum Government contribution of $521 per year (which equals $10 per week). This subsidy is returned to government in cases where individuals leave New Zealand permanently and close their accounts (from 1 July 2013, it can be transferred to an Australian complying superannuation scheme following permanent emigration to Australia).
- Government's payment of an annual KiwiSaver account fee subsidy of $40 has been rescinded.
- Since April 2012, employer's superannuation contribution tax (ESCT), which is typically the same as the employee's marginal tax rate, has been deducted from all employer contributions; this reduces the net amount paid into an employee's KiwiSaver.
- The investment income earned within KiwiSaver schemes is subject to relatively favourable tax treatment as a Portfolio Investment Entity.
- Existing superannuation schemes that become KiwiSaver-compliant can access (in relation to member contributions made on a KiwiSaver-consistent 'locked in' basis) the annual member contribution subsidy but not the *kick-start* payment.
- Lump sum payments on retirement, or earlier withdrawals, are not taxable in the hands of recipients.

Housing

- After three years' membership of KiwiSaver, individuals and couples who are buying a first home (in which they will live) can withdraw their own, and their employer's, contributions (including any returns earned) to apply towards buying that home.
- First home buyers can also receive a first home purchase subsidy of $1,000 per year of KiwiSaver contributions (up to $5,000 each and $10,000 for a couple).
- Home purchase withdrawals and the home purchase subsidy are also available to KiwiSaver members who establish that their financial position is the same as would be expected of a first home buyer (and who meet certain other qualifying criteria, including income and purchase price caps, in case of the home purchase subsidy).

Forthcoming changes

- The minimum rates of employer and employee contributions to KiwiSaver will increase to 3% of gross pay in April 2013.
- A planned, one-off, automatic enrolment of all qualifying employees has been deferred without an implementation date.
- The KiwiSaver Periodic Reporting Regulations, which come into force on 1 April 2013 and will first require a quarterly disclosure statement (prepared as at 30 June 2013) in July 2013, will require fund managers to report their performance and returns, fees and costs, assets and portfolio holdings, liquidity and liabilities, and key personnel, along with any conflicts of interest, in a standardised format on their websites. The aim is to enable KiwiSaver members to make direct comparisons across funds.

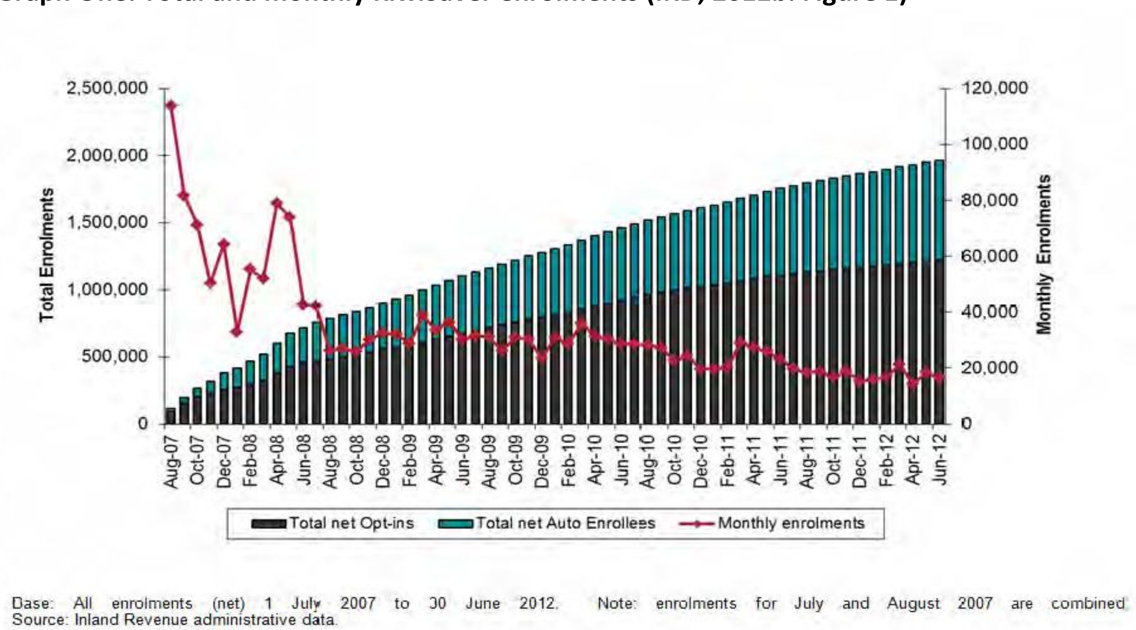
SECTION THREE: TRENDS IN MEMBERSHIP, CONTRIBUTIONS AND WITHDRAWALS

Membership

Over two million people are now members of KiwiSaver (2,048,656 at December 2012 www.KiwiSaver.govt.nz). Membership growth has started to slow and total membership growth will slow even more as the older cohort of members withdraw from the scheme (Graph One).

An estimated 38% of current KiwiSaver members were automatically enrolled as new employees. The proportion of people who opt out after being auto-enrolled has declined from 35% in 2009 to 6.2% in 2012 (IRD, 2012a; MBIE, 2012). This suggests that should the extension of automatic enrolment to all employees, on a one off basis, go ahead, this is likely to significantly increase KiwiSaver membership.

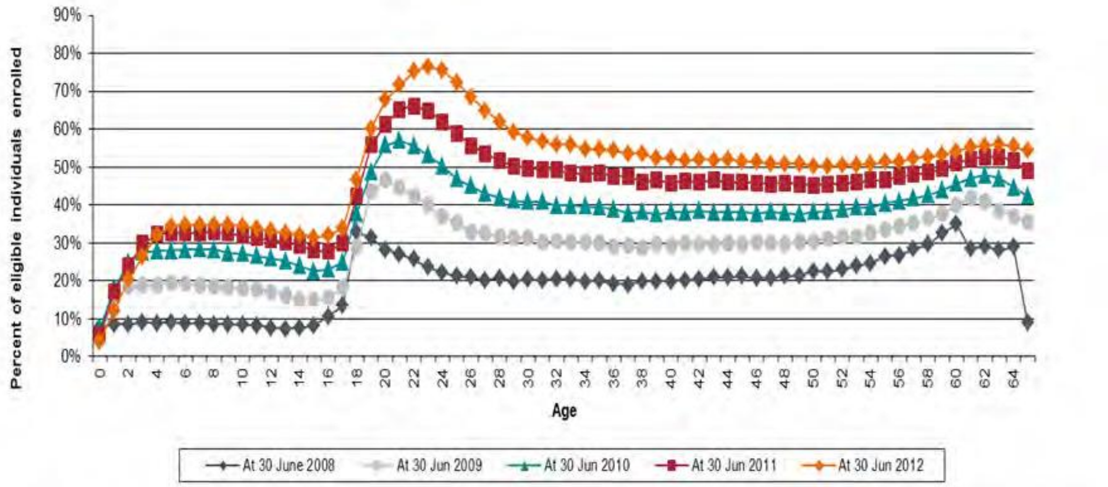
Graph One: Total and monthly KiwiSaver enrolments (IRD, 2012b: Figure 1)



Member characteristics

Around half of the eligible population has now joined KiwiSaver (Graph Two). The KiwiSaver Annual evaluation report (IRD, 2012) attributes the highest membership rates amongst 18-24 year olds as likely to be due to automatic enrolment on starting employment. There are slightly more women (1,051.416) than men (987, 432) who are KiwiSaver members (December 2012 www.KiwiSaver.govt.nz).

Graph Two: Proportion of KiwiSaver members by age group over time IRD, 2012b: Figure 4)

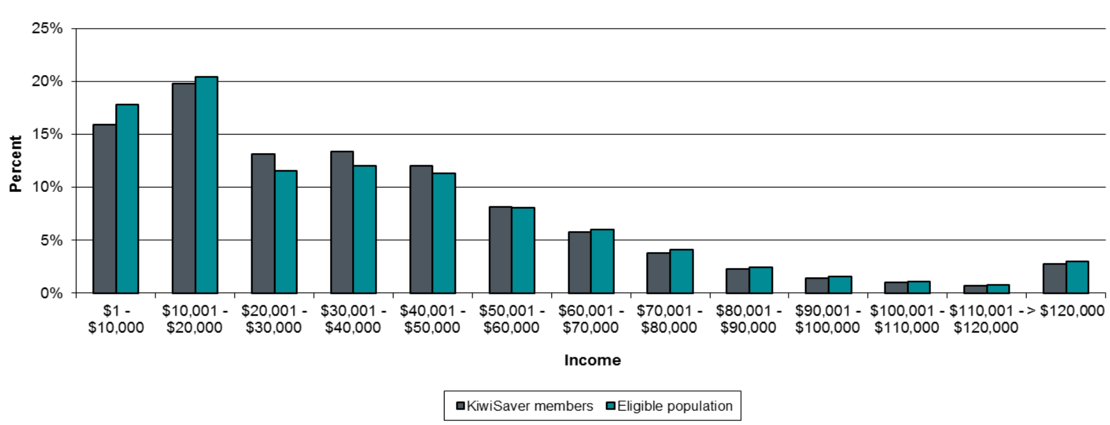


Base: All members at 30 June 2012. Eligible population are those eligible to join KiwiSaver (i.e. those who are New Zealand citizens or residents and under the age of 65 years), whether or not they have joined.
Source: Inland Revenue administrative data and Treasury long-term fiscal model for eligible population 2011/12.

Socio-economic status of members

There are disproportionately fewer KiwiSavers at lower income levels (below $20,000 pa), but disproportionately more KiwiSavers at incomes between $20,000 and $50,000 (Graph Three). An early survey in 2007-2008 found KiwiSaver members at that time were less likely to be Māori or Pacific people, but more likely to hold a degree or higher qualification (Gibson et al, 2009). A survey in 2009 found demographic profiles of members and non-members to be similar (Colmar Brunton, 2010a). Definitive data on the characteristics of KiwiSavers compared with the rest of the population (such as ethnicity), as well as the factors that influenced those decisions, will come from forthcoming analysis of data from the Survey of Family Income and Expenditure (SoFIE).

Graph Three: Income distribution of KiwiSaver members (IRD 2012b Figure 5)



Base: All members at 30 June 2012 with income for the 2011 tax year. Eligible population are those eligible to join KiwiSaver (i.e. those who are New Zealand citizens or residents and under the age of 65 years), whether or not they have joined, with income for the 2011 tax year. Income relates to the 2011 tax year and includes income from salary and wages (including benefit payments) and IR3 returns (including income from self-employment, overseas income, rental income, estate, partnership or trust income and royalties and other income without PAYE deducted). Those members with no income for 2011 are excluded. Source: Inland Revenue administrative data.

Gibson et al (2009) point to significant differences in the characteristics of direct enrolees (people who are not earning wages and salaries including children and people who opt in via their employers) and people who are automatically enrolled, and note the importance of exploring issues for different sub-groups of the KiwiSaver population.

Population who opt out of KiwiSaver

Non-members who start employment or change jobs are automatically enrolled in KiwiSaver and must then actively choose to opt out within eight weeks. Each year, fewer people opt out of KiwiSaver. The IRD evaluation suggests the drop in the proportion of auto-enrolled members who opt out indicates a broadening acceptance of KiwiSaver. Compared with the distribution of the population enrolled automatically on taking a new job, a slightly higher percentage of 25-44 years olds opted out. Of those who have opted-out of KiwiSaver, around 32% have since joined KiwiSaver (IRD, 2012b). Non-members who are self-employed, casual employees, or not in work, are not subject to any "soft compulsion" triggers to join KiwiSaver.

Income sources of KiwiSaver members

Almost as many KiwiSaver members have opted in directly with providers (1,014,104) as have either opted in via their employer (249,954) or been automatically enrolled by their employer (784,598) (December 2012 data, www.KiwiSaver.govt.nz). Table One below shows that 73% of KiwiSavers are earning some salary or wages, but some of these may be part of the group of employees where employer contributions are not mandatory (refer Table One). St John et al (2011) calculate that of the 3.7 million New Zealand residents under the age of 65, about 1.7 million (46%), which is 74% of the total labour force of 2.29 million, are potentially entitled to the employer contributions. Thus, employees are better represented than the rest of the population.

Table One: KiwiSaver members by income source (IRD, 2012b from administrative data)

Income source	Members	Percentage
Salary and/or wage income only	1,080,977	55%
Salary and/or wage plus other income	353,940	18%
Other income only	83,893	4%
No income source	447,634	23%
Total	**1,966,444**	**100%**

Non-contributing KiwiSaver members

In the year to June 2012, around 75% of members who are eligible for the member tax credit made some contributions to their account (MBIE, 2012). The 414,000 non-contributing members are mostly those with no income and around 83,000 are on an active contributions holiday (that is they are members via employment). The proportion of members who had not contributed to their KiwiSaver account in the previous two months is increasing; 23% in 2009, 40% in 2010 and 45% in 2011 (FMA, 2012). However,

it appears most of these non-contributing members are not eligible for the member tax credit (e.g. aged under 18) or contribute at some point during the financial year.
An IRD analysis found that there has been an increase in the number of contributions holidays taken since the scheme began (note only employees who qualify for employer contributions have to formally take a break in contributions – other KiwiSavers can contribute as little or as often as they like). Most members on a contributions holiday make some contribution to their account during this period (IRD, 2012a).

Contribution levels

The KiwiSaver evaluation provides some information on annual contributions to KiwiSaver, which includes data for members who belonged for only part of the year.

The proportion of wage and salary earners who contribute at 2% (the lowest possible level for employees since the minimum employee contribution rate was reduced from 4% to 2% from 1 April 2009) has grown from 41% in 2010 to 59% in 2012 (Table Two).

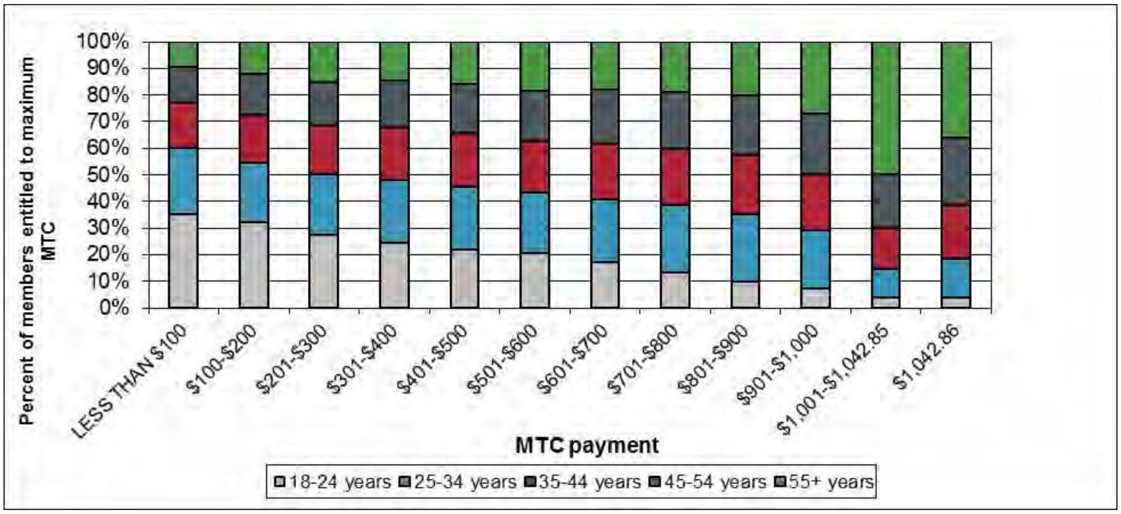
Table Two: Current member contribution rates – wage and salary earners (IRD, 2012b)

Contribution rate	Proportion of members 2010	Proportion of members 2011	Proportion of members 2012
2%	41%	53%	59%
4%	55%	43%	36%
8%	4%	4%	4%
Other %	<1%	<1%	<1%
Total	**100%**	**100%**	**100%**

In 2010/2011, the median annual contribution by wage and salary earners (excluding the employer contribution) was $829. In the same year, 18% of members (of all ages) earned only non-salary or wage income and, for these members over 18 years old, most contributed either $1,043 or $1,200 per annum to their KiwiSaver – that is at a level to maximize their access to the Member Tax Credit (MTC), or slightly higher (IRD, 2012b).

In 2011/12, MTCs were paid to 1.23 million KiwiSavers. Less than half (43%) received the maximum MTC payment. This is perhaps not surprising as, at a member contribution rate of 2% of gross wages or salary, the maximum MTC is only received at annual wages of $52,150 and above. The NZ Income Survey recorded a median wage for the June 2012 quarter of $806 per week or $42,025 pa. When the minimum contribution increases to 3% in April 2013, the maximum MTC will be achieved at annual wages of $34,767 and above. Graph Four below shows the amount of MTC received by age for the year to June 2011 – effectively a picture of contributions by age up to $1043 per annum. The graph shows the impact of lower wages and part-year or part-time earnings, particularly for those under 24. In line with gendered patterns of wages and average hours worked, women's contributions to KiwiSaver accounts are also lower on average than those of men (Dwyer, 2012).

Graph Four: Amount of MTC received by age for the year to June 2011 (IRD, 2012b: Figure10)

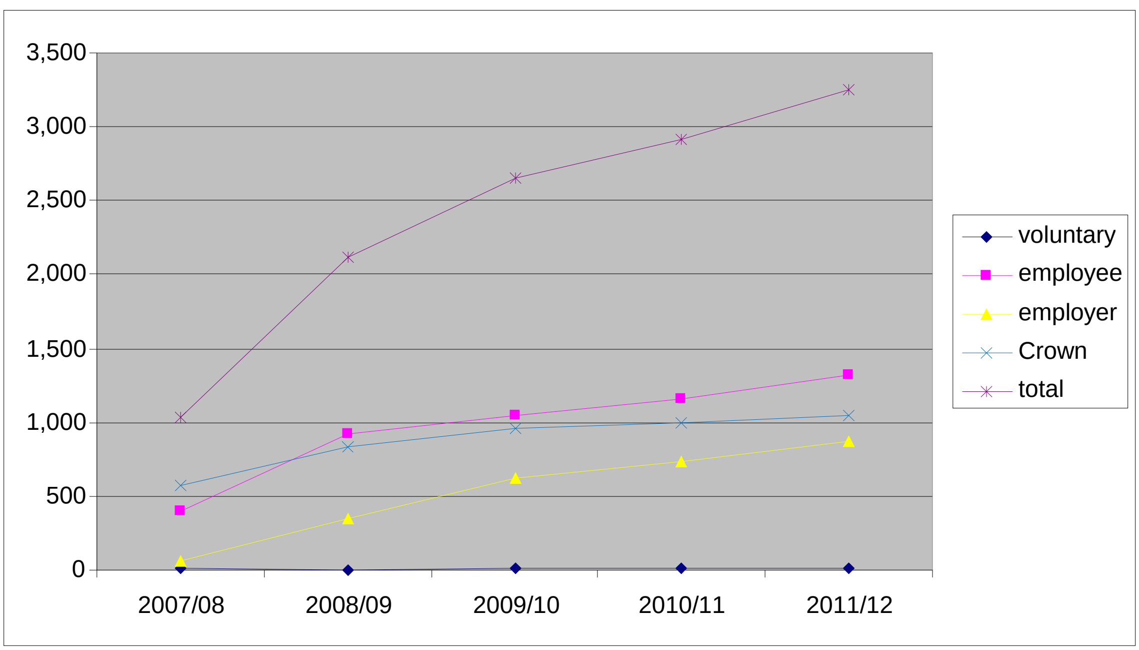


Base: All members at 30 June 2011 who have submitted a MTC claim and are eligible for the maximum MTC. The maximum annual MTC members were entitled to during that year was $1,042.86 per annum up to and including 30 June 2011.
Source: Inland Revenue administrative data.

Overall contributions by government, employers and members to KiwiSaver

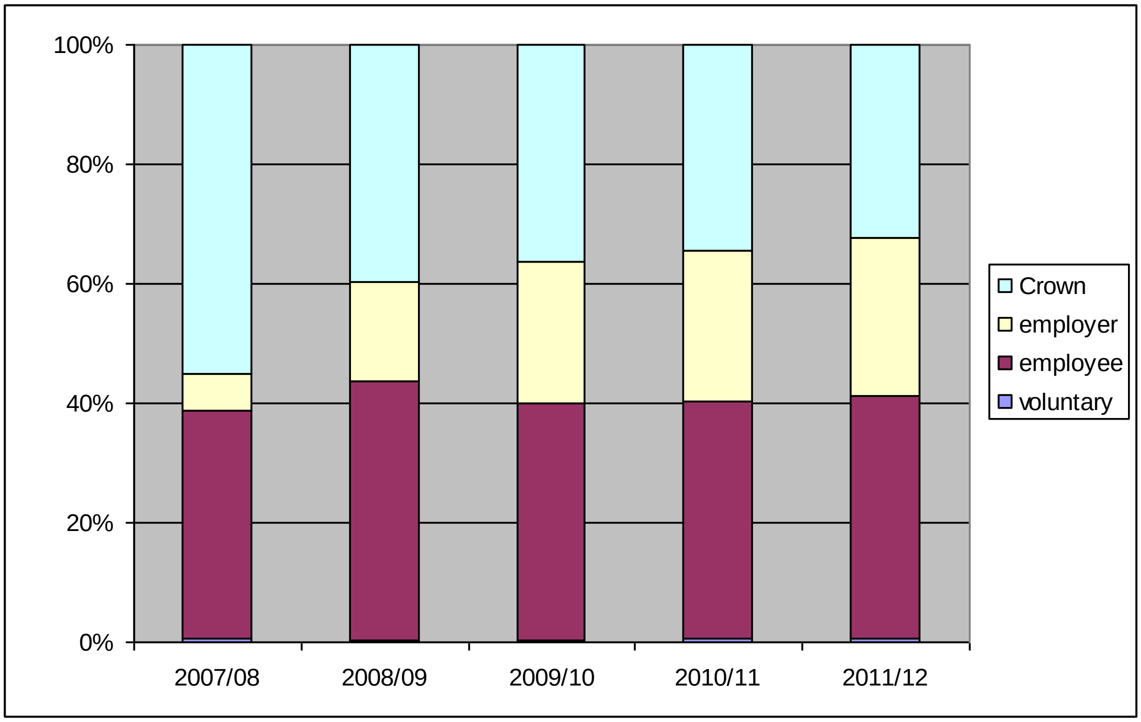
Graph Five shows the different levels of annual contributions to KiwiSaver and Graph Six shows the proportional share of contributions. The Crown's share of contributions has reduced from 55% in 2007/08 to 32% in 2011/2012.

Graph Five: Annual contributions to KiwiSaver $ million



Source: IRD annual KiwiSaver Reports

Graph Six: Share of KiwiSaver contributions



Source: IRD annual KiwiSaver reports

Fiscal costs

In the year to 30 June 2012, the Crown contributed $1,045 million in contribution payments to members of KiwiSaver schemes and complying funds (*kick-starts* to new KiwiSaver members and member tax credits to KiwiSaver and complying funds). The annual direct costs to the Crown are about 12% of the current costs of New Zealand Superannuation (around $9 billion pa).

Table Three: Crown costs (years ended 30 June) ($m)

Cost	2008	2009	2010	2011	2012	Total
Payments to members	572	842	970	998	1,045	4,427
Employer tax credit	38	206	n/a	n/a	n/a	244
Total	**610**	**1,048**	**970**	**998**	**1,045**	**4,671**

Source: IRD, 2012b

Users of the first home option

Between July 2010 and September 2012 there were 9,321 first home buyers withdrawals from KiwiSaver (IRD, 2012b). In the year to June 2012, just over $57 million was withdrawn from KiwiSaver funds for first home purchases (FMA, 2012: Appendix One).

Infometrics calculated that the likely total capital value of properties purchased through leveraging KiwiSaver was some $3 billion and notes that, given tight lending conditions, at least some of these new home purchases would have been facilitated by the KiwiSaver first home policies (Infometrics, 2012).

Patterns of withdrawals from KiwiSaver by members eligible to do so

Since 1 July 2012, KiwiSaver members who are 65 and who have been a scheme member for at least five years have been able to withdraw their KiwiSaver balances. There is no data on the value of the balances but from contributions data, IRD estimated that over three quarters of the accounts that could be withdrawn in July and August 2012 had received between $5,000 and $20,000 in contributions with half of those having between $10,000 to $15,000. It is also estimated that there is a small proportion of members who have only ever had the kick start of around $1,000 and a few have received over $35,000 in contributions (IRD, 2012b).

IRD reports that at 31 December 2012, 15,575 KiwiSaver members or a third (32.5%) of the estimated members who are eligible to withdraw savings for retirement, had fully withdrawn their savings and closed their KiwiSaver accounts. These figures do not include members who have withdrawn some of the account balance and whose KiwiSaver account remains open. Further analysis on withdrawals is forthcoming. IRD is about to begin a survey of 1,000 KiwiSaver members who are eligible to withdraw their funds to understand their intentions, and what underpins these. Findings are likely to be available by May 2013. Concurrently, IRD will undertake a survey of providers to understand more about their communication and engagement with KiwiSaver members who are eligible to withdraw their funds.

SECTION FOUR: THE FUNDING OF EMPLOYER CONTRIBUTIONS TO KIWISAVER

"Your employer compulsory contributions must be on top of your employee's regular pay. This means that if you have agreed to a total remuneration package with your employee, the compulsory employer contributions must be paid on top of that package. Your employee's take-home pay should not be reduced because you are making a compulsory contribution.

Through good faith bargaining, a salary package under an employment agreement can be negotiated whereby compulsory employer contributions can be offset against the employee's gross pay."
http://www.ird.govt.nz/KiwiSaver/employers/administering/employer-contributions

The standard approach taken by employers has been to pay employer contributions in addition to an employee's gross salary or wages. As is made clear in the quote above from the IRD website, an employment agreement can be negotiated whereby a total remuneration or "salary sacrifice" approach is taken, that is an employee receives a fixed amount of remuneration and, if that employee is a member of KiwiSaver, the cost of the employer contribution comes out of the employee's pay.

To what extent are total remuneration approaches taken to KiwiSaver?
There is no standard information collected on the extent to which a total remuneration approach is being taken to KiwiSaver. No data is collected on the use of total remuneration approaches to superannuation within either the public service or the wider public sector.

A survey of employers in Small and Medium Enterprises (SMEs) in 2009 found that, from a small sample of 170 SMEs, 18 employers (11%) took a total remuneration approach to KiwiSaver. Most employers had not changed their approach to remuneration, nor did they intend to, as a consequence of KiwiSaver. The report notes that use of a total remuneration approach is associated with a lower take up of KiwiSaver and the report suggests the use of 'salary sacrifice' negatively impacts on the uptake of KiwiSaver (Colmar Brunton, 2010b).

In a survey of collective employment agreements (CEAs) representing just under 20% of all wage and salary earners, 2/3 of whom were in the public sector, 60% of workers covered by CEAs had a provision dealing with superannuation. Only 1 in 5 CEAs included detailed superannuation and/or KiwiSaver provision. Eighteen agreements, or only 1 percent of all the agreements surveyed, specified a total remuneration or salary sacrifice approach. Of the 18 agreements that were specific about a total remuneration approach, half were in the private sector and 7 in the local government sector. A much higher proportion of this group of agreements (32%) than for the whole sample (8%) had no wage/salary rates included in the agreement. Of those that did include wage rates, seven out of the eighteen agreements (39%) included a minimum printed rate of pay below $600 per week, a lower proportion than that for the whole sample (50%) In other words, the workers covered by these agreements were less likely to be on a gross rate of pay under $600 per week (Industrial Relations Centre, 2013).

Total remuneration cannot lower wages below the minimum wage

In a recent employment court case, Faitala and Goff vs Terranova Homes and Care Ltd, the plaintiffs, Faitala and Goff, were paid the statutory minimum wage of $13.50 per hour and worked under an individual employment agreement which specified a total remuneration approach to KiwiSaver. The gross hourly pay of both plaintiffs was reduced to $13.24 an hour, as a consequence of their KiwiSaver membership, which the plaintiffs considered was a breach of the Minimum Wage Act. The judgment deemed the payment of a wage below the minimum as unlawful. It drew on the purpose of the minimum wage being to protect vulnerable workers and enable people to meet the basic necessities of day-to-day living (Employment Court of Wellington, 2012). The judgment also drew attention to the confusion within the KiwiSaver legislation which talks about employer contributions being "on top of" wages when in fact this is clearly not the case under total remuneration.

Implications of the increase of minimum employer and employee contributions to 3%

In April 2013, the rates of compulsory employee and employer contributions to KiwiSaver will increase from 2% to 3% of gross wages. In cases where 2% is being paid now, an employee under a total remuneration agreement will have the additional 2% contribution deducted from their gross pay. Where an employer pays the KiwiSaver contribution on top of gross salary or wages, the employer will pay an extra 1% and the employee, the other 1%.

Equity implications

Whilst the proportion of the workforce on total remuneration arrangements appears to be low at present, there are pressures on remuneration budgets across the public and private sectors that may lead to employers wanting to use a total remuneration approach more often in future if they expect employer contributions to rise in the future, and if doing so enables them to keep costs down. Both public and private sector businesses need to find the resources to increase KiwiSaver contributions by 50% in April 2013.

Given that most of the New Zealand workforce are on individual employment agreements, Faitala and Goff vs Terranova Homes and Care points to the need for a reality check around the extent to which employers may shift employees on individual employment agreements into total remuneration arrangements where those employees have little say over their conditions of contract.

Until recently, most agencies in the state sector received central funding to reimburse them for the cost of employer contributions to KiwiSaver, the State Sector Retirement Savings Scheme and the Teachers Retirement Savings Scheme. The cost of this funding was estimated in a report to Cabinet to be $181 million for 2010/11 with increases expected beyond this date (Treasury and SSC, 2011). Government removed this central funding from mid-2012 and public sector employers are now responsible for paying the employer contributions for KiwiSaver and other superannuation funds. Whilst associated cost pressures within the public sector were acknowledged, particularly in health and education, these were expected to be managed on a case by case basis (CAB Min (11) 15/16). The employment court case also raises questions for the 2013 Review of Retirement Income Policy. In particular, it begs the question of whether budgets within the wider public sector are sufficient to cover the employer costs of KiwiSaver for the many low paid workers, employed by not-for-profits and private firms in the health and education sectors, which are dependent on government-funded contracts.

KiwiSaver aimed to create a fair and attractive voluntary savings scheme for low earners by ensuring workers are entitled to join whether they work full or part-time, that employee contributions are set at an affordable level, that employer contributions are compulsory and vest immediately, that the scheme is portable, and that employees are incentivized through the opt out arrangement and tax concessions that reach their maximum at a relatively low contribution level. The most regressive element of the scheme, the waiving of ESCT, has been rescinded.

Tax concessions for voluntary retirement savings schemes tend to be regressive because those who join are disproportionately higher earners and higher earners also access a more valuable tax concession than do lower earners. Though the MTC is capped at a relatively low level, many employees (on lower wages) do not achieve the maximum MTC. Even without tax concessions, older style employer sponsored superannuation schemes, such as the Government Superannuation Fund, favoured long-term career employees via long vesting periods and a lack of portability (Dwyer, 2012).

When set up, KiwiSaver envisaged that employer contributions would be additional to gross wages. In 2008, parliament removed prohibitions on total remuneration arrangements negotiated in good faith after 13 December 2007. KiwiSaver members benefit more from employers' KiwiSaver contributions being an additional payment. For employers, making KiwiSaver contributions "additional" can be cheaper as they only have to provide payments to KiwiSaver members. Where employers have a strong position in negotiations, however, taking a total remuneration approach with new employees can reduce their future liabilities. A total remuneration approach across the board is also likely to reduce the costs to employers from any further increases to the level of their compulsory contributions.

However, total remuneration approaches are transparent and have been regarded as an important tool to achieve fair remuneration. Under a voluntary retirement saving scheme, total remuneration approaches are likely to be fairer, particularly since the members of KiwiSaver are on slightly higher incomes on average than non-members (Graph Three) and employer contributions to KiwiSaver are not mandatory for some of the lowest paid employees (e.g. workers under 18 and some casual workers). A simple increase in minimum employer contributions to KiwiSaver members from 2% to 3% of gross pay will widen the remuneration gap between KiwiSaver members and non-members.

The current KiwiSaver design, where it is both voluntary to join (but where there are specific employer contributions) and where there is the option for those contributions to be part of total remuneration, appears to be an unsatisfactory hybrid that is at best opaque, and at worst potentially more inequitable than a total remuneration approach.

A total remuneration approach, however, is likely to reduce the attractiveness of KiwiSaver to all members due to the direct trade-off between wages and the employer contribution. It is also likely to increase the attractiveness of contribution holidays. Making KiwiSaver compulsory would effectively mean a total remuneration approach across the board.

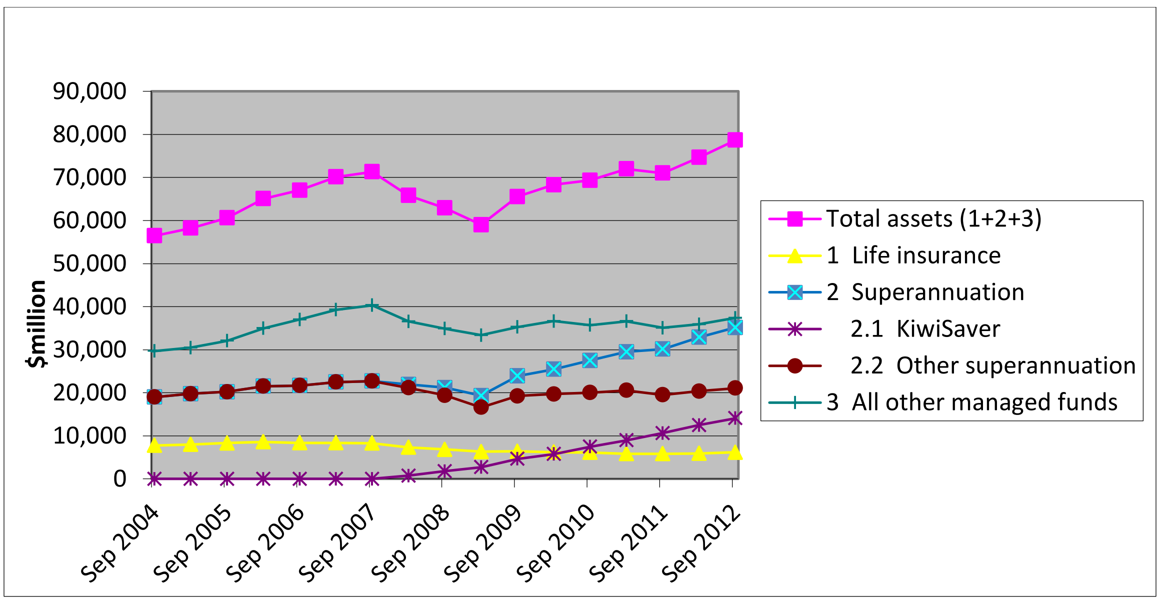
SECTION FIVE: INVESTMENTS IN KIWISAVER SCHEMES

The relative significance of KiwiSaver in the managed funds sector

In September 2012, KiwiSaver made up $14,096 million of the $35,163 million assets under fund management held in superannuation schemes and 18% of the $78,692 million total funds under management (Reserve Bank, 2013).

Graph Seven provides an overview of trends of the value of funds under management based on data for the March and September quarters between 2004 and 2012. Whilst funds under management declined in value between 2007 and 2009, presumably as a consequence of the economic slowdown, they have subsequently recovered and increased in value. Life insurance continues to decline in value. Other managed funds (including unit trusts and group investment funds) fell in value between 2007-2009 and have held, rather than increased value since that time. KiwiSaver funds have steadily increased in value since its introduction in 2007 which is consistent with the growth in members. The value of other superannuation funds has begun to grow, following a downward trend in 2007-2009. This uplift is only slight and may be largely investment returns-driven but might also reflect a slight increase in the attractiveness of non-KiwiSaver work-based schemes (which offer the benefits of earlier access to funds) as a complement to KiwiSaver, given the reduced KiwiSaver savings incentives.

Graph Seven: changes in funds under management by category RBNZ



Source: RBNZ, 2013

To what extent has KiwiSaver led to more personal savings and asset accumulation?

The purpose of KiwiSaver is "to encourage a long-term savings habit and asset accumulation by individuals who are not in a position to enjoy standards of living in retirement similar to those in pre-retirement" An initial exploration of the impact of KiwiSaver on retirement saving, based on a nationally representative survey in early 2010 (Colmar Brunton, 2010a), found KiwiSaver members reported that, on average, they would have saved 64% of the money they were contributing to KiwiSaver. It also found that KiwiSaver had reached about a third of its target population and that 80% of KiwiSaver members did not expect to have an income shortfall in retirement. The report noted that these findings were after only three years of KiwiSaver. Further analysis of the effects of KiwiSaver on wealth accumulation, the composition of assets and liabilities, wealth in retirement, retirement income adequacy and target effectiveness will be a focus of the SoFIE analysis in the KiwiSaver evaluation (Law et al, 2011).

Balances in KiwiSaver funds

At 31 March 2012, the average balance across all KiwiSaver accounts was $6,668.00 and the average balance in a default fund was marginally lower at $6,530 (derived from FMA data). No data source shows the distribution of balances across members by age, gender and other factors (e.g. whether contributing or not, whether accessing employer contributions or not). An analysis of data from three KiwiSaver providers (which is not necessarily representative of the overall picture) shows a pattern of higher balances by age, and higher male than female balances for those over 19 with the gap between males and females widening with age between age 20-50 (Infometrics, 2012).

The earnings of KiwiSaver schemes

Table Four replicates Morningstar's (an international investment data company) summary of annual average returns to different types of KiwiSaver investment funds, over one year to 31 March 2012, and over the previous three and five years, which reflect the impact of the economic slowdown. A few schemes do not provide data to Morningstar. The averages disguise variation in returns across schemes.

Table Four: KiwiSaver Peer Group Averages: Total returns % per annum Years to 31 March 2012

Fund type	Assets $M	1 year	3 years	5 years
Default options	4,211.6	7.5%	5.7%	4.9%
Conservative	4,975.9	7.8%	5.8%	5.0%
Moderate	1,830.0	9.6%	6.7%	4.4%
Balanced	2,223.8	11.6%	6.2%	2.6%
Growth	2,028.5	13.1%	6.4%	1.2%
Aggressive	851.9	12.6%	4.7%	0.0%

Source: Morningstar, 2012

For individuals, net earnings will be affected not just by the fund selected but by contribution levels, breaks in contributions, fees and access to employer contributions and the MTC. As is the case with balances, there is no information currently about the distribution of earnings for individual groups of KiwiSaver members.

There may be elements of the current KiwiSaver design and management that are barriers to the best returns to KiwiSaver accounts. Issues include the Reserve Bank's different treatment of cash in bank accounts and KiwiSaver accounts, and whether there is too much flexibility for members to move from scheme to scheme.

Regulation and oversight of KiwiSaver schemes

The New Zealand KiwiSaver scheme is based on a competitive market of KiwiSaver providers, including default providers for those who are automatically enrolled and have not actively selected a provider, as well as the option to switch providers at any time. There is no government guarantee that KiwiSaver accounts will retain their value, let alone grow. The discipline on KiwiSaver providers comes from: the government's Financial Markets Authority (FMA) which is responsible for the administration, compliance monitoring and enforcement of the KiwiSaver Act; self-management and disclosure by KiwiSaver providers, and market pressure from KiwiSaver clients. The Reserve Bank's capital market regulations also impact.

FMA role

Via the Financial Markets Authority Act 2011, the FMA has a broader mandate to promote and facilitate the development of fair, efficient, and transparent financial markets, strengthen the public's confidence in New Zealand financial markets, promote innovation and grow New Zealand's capital base. The FMA requires annual statistical information from all KiwiSaver schemes. It engages with individual KiwiSaver scheme managers and advisers around trust deed issues. This includes, for example, ensuring that schemes comply with obligations such as fees to be "not unreasonable" through providing guidance notes and requiring schemes to advise FMA of increases in fees. The FMA determines which employers have exempt status, and determines the funds that have Complying Superannuation Fund status. The FMA manages the Default Monitoring Panel, which supervises the six default KiwiSaver schemes which have a specified fee regime and investment strategy.

KiwiSaver Periodic Reporting Regulations

The KiwiSaver Periodic Reporting Regulations, which are due to come into force on 1 April 2013 and will first apply with respect to the 12 months ended 30 June 2013, will require fund managers to report their performance and returns, fees and costs, assets and portfolio holdings, liquidity and liabilities, and key personnel, along with any conflicts of interest, in a standardised format on their websites. The aim is to enable KiwiSaver members to make direct comparisons across funds. Currently, the main provider of regular statistics on most KiwiSaver providers – including the value of their funds under management, returns for each of their schemes, expense ratio, fees and market share is Morningstar. CFLRI has data on fees within one of its calculators on the *Sorted* website https://www.sorted.org.nz/calculators/KiwiSaver-fees

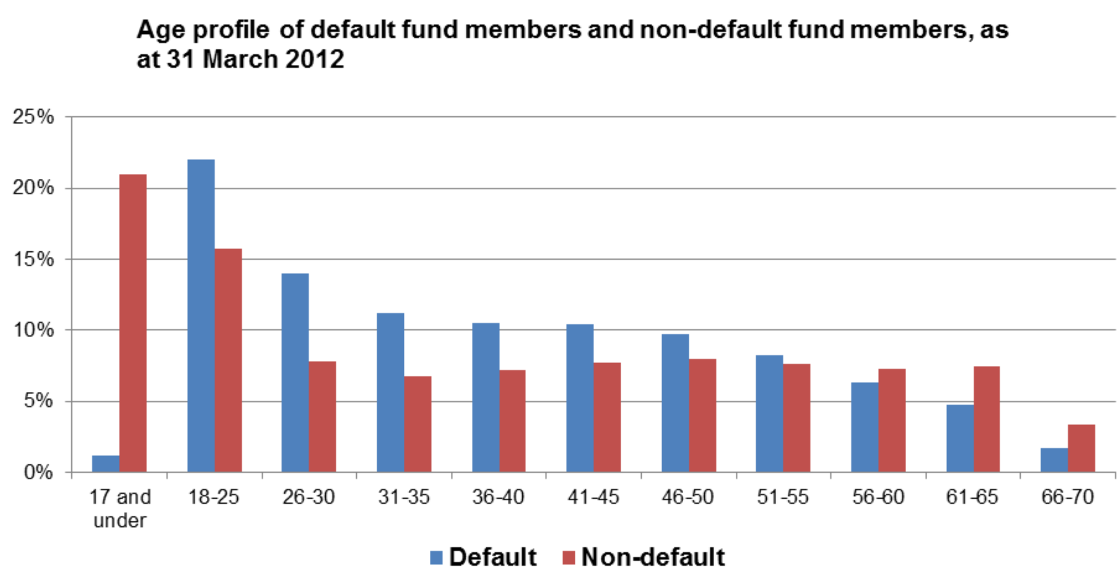
Default providers and the rules governing default funds

Default fund members

At 31 March 2012 there were 1.9 million KiwiSaver members of whom 447,274 members (24%) were in one of the default funds. In addition, 93% of the 178,000 members in their employer-chosen scheme are in the default option of that scheme.

Excluding those aged 17 and under, 42% of default members are non-contributing compared with 31% of active-choice members (MBIE, 2012). The default options are more conservative than other KiwiSaver conservative portfolios and hold around 80% of their assets in fixed interest or cash. Assets of the default funds were worth 23% of the value of all KiwiSaver assets under management at 31 March 2012 (FMA, 2012: Appendix one) thus are, on average, of a similar value to other KiwiSaver funds. As shown in Graph Eight, 18-35 year olds are more likely to be in the default funds than other age groups.

Graph Eight: distribution of default fund members by age (MBIE, 2012 from FMA, 2012)



Default provisions after 2014

The default provider arrangements for KiwiSaver are under review. Key issues under consideration are the objectives of the default schemes and whether these should change, the best design to achieve the desired objectives and the most appropriate institutional arrangements and transition.

New Zealand is not alone in considering what might be the most appropriate default fund arrangements for automatic enrolment or compulsory savings schemes. In particular, several countries have in place, or are considering, default arrangements that mandate a life-cycle or “age appropriate” investment for the savings of default fund members with a view to gaining better investment returns for individuals and to better suit long-run investment needs. This approach has been recommended by government-initiated reviews in New Zealand, including the Capital Markets Development Taskforce, and the Savings Working Group. Where governments decide for people, however, the risk that government has to step in, in the case of poor performance increases. Another option is to increase financial education and to encourage the use of professional advice. A discussion document on default provider arrangements was released in late 2012 (MBIE, 2012). No date has been set for advice and decisions on a post-2014 default regime.

Annuities

Annuities are regular payments of a fixed amount or adjusted on an agreed basis (e.g. inflation). For older people, they commonly include insurance against the risk of longevity and are paid until death, but they can be paid for a fixed term only and have a lump sum component if death occurs prior to the end of the term.

There are almost no annuity products in New Zealand, and there have been many calls for government to facilitate the development of the annuities market (e.g. St John, 2009; Capital Market Development Taskforce, 2009; Savings Working Group 2011). The absence of annuities in the market will become more pressing as KiwiSaver balances grow. Some consideration of this situation is underway (MBIE, 2010). Without any compulsion to purchase annuities, there is little prospect for saving on New Zealand Superannuation or other health and welfare expenditures that benefit the retired population.

SECTION SIX: THE PLACE OF KIWISAVER IN THE RETIREMENT INCOME FRAMEWORK

"It is timely to ask: a success for whom? Is KiwiSaver a numbers game? Has it had the effect on the economy that was originally desired? What are the macro implications as opposed to the micro effects of subsidising some citizens to have more resources in retirement? Will they in fact have more, or will members simply reduce other savings to compensate? In the long term, what are the implications for New Zealand's overall pensions framework, and in particular the very successful universal state pension?"

St John et al, 2011

KiwiSaver has grown quickly to become a large programme with over 2 million members who hold $14 billion in assets. It has been lauded for its popularity and growth. However, its cost to taxpayers, and lack of planned integration with retirement income policy, have been questioned. It has also been subject to considerable policy change, particularly in relation to the contributions of employees, employers, and Government, as well as the rules around disclosure.

The KiwiSaver evaluation has rightly focused on KiwiSaver's performance in relation to its own purpose. The report of the Savings Working Group (2011), current analysis of default schemes (MBIE, 2012) and some Treasury analysis have considered the broader policy issues (e.g. Law et al, 2011). Beyond government, there has also been some attention to broader macroeconomic and equity issues (e.g. Gibson et al (2009), Crossan (2010), Hurnard (2011), St John et al (2011) and Infometrics (2012)).

Overall, however, policy is underdeveloped in relation to: the broader market of work-based superannuation schemes that comply with or complement KiwiSaver; KiwiSaver's fit in the Retirement Income Framework, and its relationship with other programmes.

Many issues beyond the retirement income framework need more attention. These include: the impacts of KiwiSaver on wages and remuneration patterns; growth and productivity; fairness, and fiscal implications over the longer term.

Retirement savings is a long term game for governments and individuals. Over three quarters of all 24 year olds are now KiwiSaver members – and it is for this, and younger, cohorts that locked in savings can occur over a long enough period to generate a substantial sum on retirement. Under current policy settings, this would be available to individuals at age 65 as a lump sum, with no diminishment of other entitlements, nor any compulsion to turn all or part of the lump sum into an annuity, should there be acceptable annuity products.

Clarity about how KiwiSaver fits alongside other retirement income polices, and how this may change in the future, is essential if the many skilled and knowledgeable stakeholders with disparate views on KiwiSaver – employers, trade unions, associations of KiwiSaver providers and financial advisers, consumer groups and academics – are to work together to support the appropriate development of KiwiSaver going forward, and for any trade-offs to be identified and planned for.

There are many gaps in the data available from official statistics including those developed specifically for the KiwiSaver evaluation. Given the implications for government, and individuals making decisions about a growing resource that is locked in until retirement, it would be timely to take stock of the key policy questions, and information gaps and plan a comprehensive approach to statistics. Gaps in information and data are, of course, difficult to prioritise in the absence of a clear end game. The following areas are suggested for attention.

Dissagregated data on savings and earnings
Data on who is saving what within KiwiSaver is very limited. IRD indicate there is likely to be some use made of the New Zealand Government's Integrated Data Infrastructure, which builds from the Linked Employer Employee Dataset, to provide a clearer picture of the patterns of contributions by employees in relation to other factors such as earnings and industry, as recorded on the Employer Monthly Schedule (EMA). However, this will only provide data on KiwiSaver contributions for members who are employees.

In countries which have individual retirement accounts, such as the USA and Australia, the value of individual accounts tend to be tracked by gender, age and other factors, such as employment status (e.g. AMP NATSEM, 2009). This type of data could be obtained through sampling the tax records of individuals as all KiwiSaver schemes must file a return for individual members. IRD note that access to this data is governed by the Tax Administration Act. However, in its absence, the only option is to build a picture of the value of accounts by gathering data from each provider. In addition, there appears to be very little information on the Complying Superannuation Funds which are treated like KiwiSaver schemes.

KiwiSaver, wages and remuneration
Tracking the extent to which employment agreements (both collective and individual) in both the private and the public sector involve total remuneration approaches, and who is impacted (KiwiSaver members, non-members, employers) and how, is suggested.

Data on KiwiSaver
Responsibility for maintaining and developing data on KiwiSaver is spread across government agencies and industry bodies. In addition to official government data on KiwiSaver (produced mainly by IRD, FMA and the Reserve Bank), the CFLRI has responsibilities including a periodic review of Government's retirement income policies. A number of industry bodies report, advocate and develop data on KiwiSaver and associated retirement income provision. Whilst private data such as the Morningstar surveys is regular, there is no guarantee that this will continue into the future, and there is no way to relate this information about the industry to data on individual members or groups of members.

Transparency would be better supported by an independent and timely distillation of the disclosed information by the FMA, including the analysis of membership data within schemes.

An issue for consideration is whether the new disclosure laws are sufficient to enable the public to make an educated choice about their KiwiSaver scheme, or whether there is a need for a more direct education and information programme.

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