pensionbriefing

THE UNIVERSITY OF AUCKLAND BUSINESS SCHOOL

A briefing paper from the retirement policy and research centre

A condensed history of public and private provision for retirement income in New Zealand - 1975-2008

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This *PensionBriefing* gives a short history of the changes to the regulatory environments for both public and private retirement income provision in New Zealand in the last 33 years.

In summary

Since 1975, the regulatory environment for both public provision (now New Zealand Superannuation) and private provision (now including KiwiSaver) has been changed regularly, and sometimes significantly, as governments have come and gone.

Change can be expensive and disruptive to the plans that New Zealanders make for their retirement income. It is important to be aware of New Zealand's history when trying to understand the current tax and regulatory environment as well as how New Zealanders have reacted to that change.

Attached is a short summary of the main events in the superannuation timeline since 1975.

Four main periods

New Zealand's history with respect to public and private provision for retirement can be divided into four main periods:

1. **Before 1975**

   From 1940 to 1974 the structure of state pensions - the Tier 1 age pension (means-tested from age 60) and universal superannuation (taxable from age 65) remained largely intact while the level of benefits gradually increased. 1974 marked the passing of the legislation that introduced the compulsory Tier 2 New Zealand Superannuation Scheme in 1975.

2. **1975 to 1987-90**

   In 1976, following the 1975 election, the Tier 2 New Zealand Superannuation Scheme was disbanded and in 1977 the universal Tier 1 "National Superannuation" for all from age 60 was introduced. The environment for both public and private provision for retirement was highly politicised. Among changes, a surcharge on National Superannuation was introduced in 1984 and tax incentives for private provision were removed between 1987and 1990.

3. **1990 to 2007**

   An acrimonious political attempt to change National Superannuation into a welfare benefit in 1991 (and to move the state pension age out to 65) created instability. The 1992 Task Force on Private Provision for Retirement led to the

1993 Accord that helped to restore stability at least until 1996. The gradual loss of the Accord resulted in further politicisation of retirement income provision, but throughout this period the provision of a basic Tier 1 state pension for all was retained with voluntary, unsubsidised saving.

4. After 2007

The introduction of KiwiSaver in 2007 marked a large shift in public policy on private provision. As well as the contribution requirements from both the members who choose to join and their employers, there are significant tax-funded subsidies. KiwiSaver has introduced a new period of uncertainty in the public/private retirement income environment. The new government elected in November 2008 has promised further changes to KiwiSaver.

Drawing conclusions from the history

New Zealand has had a generally unsatisfactory history of changes in the retirement income environment. In fact, over the roughly 30 year period covered by this *PensionBriefing*, New Zealand has probably experienced more changes or proposed changes to both public and private provision than any other developed country. In this area of public policy, New Zealand does not have a proud record.

The following lessons may be drawn from the history of the last 30 or so years:

(a) Changes to both public and private provision without appropriate analysis and supporting evidence are unlikely to be durable. Consideration also needs to be given to the relationship between public and private provision when changes are made to either.

(b) It is unsatisfactory when policy is driven by political considerations rather than the needs of savers and pensioners (or taxpayers).

(c) When changes are made with comparatively short implementation periods, uncertainty is created for individuals who are making very long-term decisions about their retirement income needs. Changes with relatively short implementation periods also impose unnecessary costs on the administrators of both public and private retirement income schemes.

With the election of a new government in November 2008, there will be yet more changes – this time to KiwiSaver, even though that has been in place for only 16 months and has already been changed significantly from the original legislation in 2006. It also appears there will be changes to the investment objectives of the New Zealand Superannuation Fund (that serves to partially pre-fund New Zealand Superannuation).

The lessons from New Zealand's past indicate that further changes should be approached with caution and full analysis to avoid repeating problems or creating new ones.

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Public and private provision for retirement -a condensed history 1975-2008[1]

There is a glossary of defined terms and acronyms at the end of this summary.

Year	Public provision	Private provision
To 1975	Two-step Tier 1 pension: - "Old Age" – ages 60-65 - "Universal age 65+. Implemented by Social Security Act 1938 – "Old Age" pension income-tested to age 65.	1. Pension schemes: EET. 2. Lump sum schemes: EEE Driven out of tax requirements in the Income Tax Act.
1975	Compulsory third layer added – the "New Zealand Superannuation Scheme". A Tier 2 benefit – related to employment.	Existing plans could be retained or converted to "alternative plans" – EET. Approved alternative plans could contract out of Tier 2 compulsory NZSS.
1976	NZSS abolished by National following the 1975 election.	Approved alternative plans abolished.
1977	National Superannuation introduced: 70% (gross to gross) of the National Average Earnings (NAE)to married couple from age 60; 42% for a single person – first of two steps.	
1978	National Superannuation (gross) now at full level 80% of gross NAE for a married couple (and 48% single).	
1979	National Superannuation reduced - pension formula changed to net 80% of the net NAE.	Human Rights Commission Act effective – outlawed age discrimination in employment benefits.
1980		1 April compliance date for Superannuation Schemes Act 1976 regulations and tax approval.
1982	McCaw report recommended that non-cash benefits provided by employers be taxed ("Fringe Benefit Tax").	Investment income: - lump sum schemes taxable from 5 August (ETE); saving provisions for existing "lump sum schemes" – "Class A" and "Class B" funds. - deductibility increased (pensions).
1983		1983 Superannuation Schemes Regulations announced – all schemes to be classified.
1984	Surcharge announced following election of Labour in 1984 - income test on National Superannuation.	1984 Budget announces tax review 1 April – all schemes classified as "lump sum" or "pension".
1985	Surcharge effective. Fringe Benefit Tax (FBT) introduced.	Reserve Bank ratios that controlled scheme's investments dropped – normal trustee/beneficiary rules now apply.
1986		1 April compliance date for 1983 Regulations
1987		Government Economic Statement issued and, effective from 17 December: - employee contributions not deductible; - employer contributions subject to Fringe Benefit Tax (FBT). Tax regime now TET[2] until 1 April 1988.
1988	Royal Commission on Social Policy; Government review announced.	Investment income taxable 1 April – now TTT. Consultative Document issued March. Brash Committee reports July.
1989	"Guaranteed Retirement Income" (GRI) and "Retirement Tax" announced – net GRI to be net 65-72.5% of NAE. Essentially, National Superannuation re-named with a "tagged" income tax.	FBT on employer's contributions replaced by withholding tax (SSCWT). Renegotiation for tax-induced benefit changes – effective by 1 April 1990.

1 This is an extended and updated version of a table that appeared in *The Options*, a report of the Task Force on Private Provision for Retirement (the first "Todd Task Force"), August 1992.

2 Tax treatment references in 1987, 1988 and 1990 apply to pension schemes only and ignore the commutation option that allowed up to 25% as a tax-free lump sum.

Year	Public provision	Private provision
1990	GRI implemented.	All pensions tax-free from 1 April – now TTE; for both pensions and lump sum benefits. New Life Office tax regime introduced. New regulatory regime ("registered superannuation schemes") starts 1 April.
1991	"Mother of all Budgets" following National's election in 1990: - "Claw back" by joint income test to replace "surcharge" from 1992; - State Pension Age to increase from 60 to 65.	First Todd Task Force on Private Provision for Retirement appointed in October: Interim Task Force report December 1991.
1992	State pension age starts increasing from 60 to 65. Legislation for "clawback" reversed and the surcharge tightened. GRI becomes "National Superannuation".	Permitted compulsory retirement ages increase. "Todd Task Force" includes public provision and reports: - "The Options" (August); - "The Way Forward" (December).
1993	The Accord (August) signed by National, Labour and Alliance. Retirement Income Act 1993: - State Tier 1 pension now called "New Zealand Superannuation". - "Accord" included in the Act. Superannuation not an election issue for first time in 18 years.	
1995	Office of the Retirement Commission established.	
1996	Accord starts unraveling - superannuation again an election issue.	
1997	Referendum (after first MMP coalition government between National and NZ First) on "Compulsory Retirement Saving Scheme" (92% to 8% defeat). Second "Todd Task Force" – the 1997 Periodic Report Group – reports on both public and private provision: - July (to inform Referendum debate); - December (final report). Surcharge rate reduced; income threshold raised	
1998	Surcharge abolished after 13 years. Super 2000 Taskforce appointed (December). "Floor" for NZS to reduce from 65% of NAE for a married couple to 60% through CPI only increases.	
2000	"Floor" for NZS restored to 65% following Labour's re-election. Super 2000 Taskforce disbanded (March). New Zealand Superannuation Bill introduced.	"Salary sacrifice" can save tax because of break between new top marginal tax rate (39%) and SSCWT rate (33%) - first tax break for private saving since 1990.
2001	New Zealand Superannuation and Retirement Income Act 2001 passed (October): - replaced the Retirement Income Act 1993 and moved provisions governing New Zealand Superannuation from Social Security Act; - established New Zealand Superannuation Fund.	
2002	State pension age now 65	
2003	2003 Periodic Report Group meets and reports (December) - report is largely ignored. New Zealand Superannuation Fund starts investing (September).	

Year	Public provision	Private provision
2004		Variable SSCWT rates start 1 April – opens up further tax-planning possibilities for salary sacrifice. Savings Product Working Group appointed (May) and recommends (September) a national, auto-enrolment, workplace scheme with modest "sweeteners".
2005	Floor for New Zealand Superannuation raised to 66% (married) – resulted from a side agreement under MMP between Labour and NZ First	
2006		KiwiSaver I announced in Budget (a Tier 3 scheme): - auto-enrolment + opt-out; - $1,000 "kick start" + $40 p.a. fee subsidy; - member can contribute 4% or 8%; - A world-first, national experiment to encourage New Zealanders to think about saving specifically for retirement. Adopts principles of "behavioural economics". - (December) employer contributions announced as tax-free to 4% of member's pay.
2007	Retirement Commissioner's 2007 Review of Retirement Income Policy (December)	Variable SSCWT rules tightened from 1 April to limit tax planning. KiwiSaver II announced in May Budget: - Member Tax Credit $1,043 a year; - Employer Tax Credit $1,043 a year; - Compulsory employer contributions at 1% from 2008 increasing to 4% by 2011. KiwiSaver II starts 1 July. Aside from employer contributions, tax treatment now E^{+}TE. For average earner, Member Tax Credit is worth more than a straight tax deduction at member's marginal tax rate. Employer contributions are a straight "E". PIE tax regime starts 1 October (effectively).
2008	In response to Retirement Commissioner's 2007 Review: - Government establishes "cross-agency working group" to report by May 2009; - Some other recommendations to be reviewed by officials.	SSCWT now "Employer Superannuation Contribution Tax" (ESCT). Compulsory KiwiSaver employer contributions start 1 April. New National-led government announced policy to reduce tax subsidies and scale of KiwiSaver II: - Minimum member contributions now 2%; - Employer's compulsory contribution limited to 2%; - ESCT-free employer contribution also limited to 2%; - $40 a year fee subsidy dropped.

Note: a glossary of defined terms and acronyms appears on pages 6-7.

Glossary

The following expressions have been used in the *History*:

CPI — Consumer's Price Index, the most commonly used inflation measure in New Zealand.

EET, TET, TTE etc. — The taxonomy of retirement saving treatment is summarised by three letters with some combination of "E" (exempt from tax or, in the case of contributions, fully deductible from other income and, therefore, from pre-tax earnings), "T" (fully taxable or, in the case of contributions, paid from after-tax earnings) or "t" (partially favoured under the tax regime).

The first letter describes the way contributions are treated; the second letter the investment income in the savings plan and the third letter, the way benefits are taxed. The common international treatment of retirement saving is EET (**E**xempt contributions; **E**xempt investment income and **T**axable benefits). Benefits can be described as "tax neutral" under the normal income tax treatment if they are TTE. By contrast, EET can be seen as "neutral" by reference to an expenditure tax regime.

ESCT — Employer Superannuation Contribution Tax – a new name for SSCWT from 1 April 2008.

FBT — Fringe Benefit Tax – payable by an employer on non-cash benefits delivered to employees like insurance, low-interest loans etc.

GRI — Guaranteed Retirement Income – the state's Tier 1 pension – named so between 1990 and 1993. Now New Zealand Superannuation.

KiwiSaver — An auto-enrolment, opt-out, workplace Tier 3 savings scheme that started on 1 July 2007.

NAE — National Average Earnings – the annual New Zealand Superannuation pensions are calculated in relation to the after-tax national average, ordinary time weekly earnings and are adjusted in relation to the NAE each year. There is a floor of the annual movement in the CPI.

NZSS — The New Zealand Superannuation Scheme, a Tier 2 scheme that survived briefly (less than a year) in the mid 1970s.

New Zealand Superannuation — Or NZS – confusingly, this has nothing to do with the New Zealand Superannuation Scheme of the 1970s. It is the name of New Zealand's Tier 1 pension payable to all from age 65.

New Zealand Superannuation Fund — Or NZSF - a government-run 'sovereign wealth fund' set up in 2001 to partially pre-fund future payments of New Zealand Superannuation. Also sometimes called the 'Cullen Fund'.

SSCWT — Specified Superannuation Contribution Withholding Tax, payable by way of deduction from the employer's contributions to a Tier 3, workplace superannuation scheme. A proxy for the tax due from employees on the value of the benefit delivered through superannuation. Became ESCT in 2008.

Surcharge
The income test that applied to National Superannuation (now New Zealand Superannuation) between 1984 and 1998.

Tiers of pension
Tiers explain the way that retirement benefit entitlements arise. Hence:

- **Tier 1:** the basic pension, payable by the state (New Zealand Superannuation).
- **Tier 2:** an earnings-related (either as to contributions, benefits or both)scheme with mandatory contributions by employees, employers or both – New Zealand briefly experimented with this in the mid-1970s.
- **Tier 3:** all other voluntary savings whether through the workplace or directly; whether through formal saving plans or by direct investment. KiwiSaver is in this group.