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RPRC Update

Retirement Policy and Research Centre

September 2012 | Volume 5, Issue 3 of the quarterly RPRC Update

RPRC Working Paper 2012-1 *September 2012*
New Zealand Superannuation and Overseas Pensions: Reform Option 2

During this quarter, the Retirement Policy and Research Centre (RPRC) has maintained a focus on the many inequities of New Zealand's overseas pensions policies. Examples of the bad policy design, and the harsh human consequences, appear regularly in the media, for example SUNDAY STAR★TIMES www.sundaystartimes.co.nz 22 July: Time to address NZ Super-immigrant policy, and 6 August: Pension puzzles for travellers; and on 9 September: Injured vet's move home blocks his war pension in The New Zealand Herald

Pension portability becomes more important as populations become more mobile. New Zealand Superannuation (NZS), the universal age pension, requires 10 years residence between ages 20 and 65 for full eligibility. Most countries accrue entitlements to state-provided pensions through a means-test, or contributions, periods of employment, or similar measures. A full pension requires a 'complete' record, with reciprocal bilateral agreements accommodating time in different countries. On grounds of fairness, the rules reduce NZS where a claimant has accrued entitlements to another country's state pension.

Currently, those rules are opaque and inconsistent. Section 70 of the Social Security Act 1964 requires abatement of NZS by overseas pensions that are deemed analogous. The present Direct Deduction Policy (DDP) has been reviewed on a number of occasions but remains unchanged despite acknowledged difficulties in its application. Changes to the New Zealand Superannuation and Retirement Income Act 2001 addressed the situation for pensioners who emigrate after qualifying for NZS (after age 65), but not the issues faced by New Zealand residents with entitlements from overseas state systems.

The three most common perceived injustices in the application of the DDP are, firstly, application of the DDP to pensions that are *not* analogous to NZS. Secondly, inequity occurs when for example, a husband has accumulated a large overseas pension, and the DDP is applied to his NZS entitlement, with any remainder applied to his wife's NZS entitlement. Her right to NZS is ignored, clearly a breach of the spouse's right to be treated without discrimination. Thirdly, there is a widespread misperception, encouraged by the language in official documentation, that people with overseas state age-pension entitlements would receive that income *in addition* to NZS.

A number of solutions are possible. Reform Option 1 (Dale and St John 2012) suggests a 25 year qualifying period for NZS. This paper fleshes out Option 2: for immigrants with an entitlement to another country's state pension, change the design of NZS to a 45 year accrual. Under both Options, the $ amount and terms of any other state pension then cease to be a concern when calculating the immigrant's NZS. Some suggest more radical reform of NZS entitlements that would affect all applicants, not just those with an overseas pension entitlement. That is described, for consistency, as Reform Option 3. Overall assessment of Options 1, 2, and 3 will be undertaken by the RPRC in 2013.

The latest Working Paper is available here.

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The Retirement Policy and Research Centre thanks its sponsors, close collaborators, and partner organisations.
In particular, grateful thanks to the MSA Trust; and to our host, the Department of Economics at The University of Auckland.

Achieving sustainable retirement policy in New Zealand

Paper delivered by Susan St John, co-director RPRC, at 20th Annual Colloquium of Superannuation Researchers, hosted by the Centre for Pensions & Superannuation Research, and the School of Risk & Actuarial Studies, UNSW, Sydney, 12-13 July 2012

Abstract: Improving the affordability and equity of New Zealand Superannuation (NZS) in the context of a growing role for KiwiSaver is a pressing task for New Zealand as society undergoes rapid ageing. Raising the age of eligibility for NZS is widely seen as necessary for fiscal sustainability, yet this is not the only policy lever available to improve affordability, nor the most equitable.

A subtle mix of the three possible parametric changes: the age of eligibility, the pension level, and the degree of targeting, may be preferable. Increasing the degree of targeting may also address some of the current inter-generational inequities. In addition it could contribute to more convergence in state pension design between Australia and New Zealand with benefits for Trans-Tasman policy integration. Also critiqued is the recent suggestion by the Financial Services Council that, 'to catch up with Australia', New Zealand should shift toward partial Save As You Go (SAYGO). KiwiSaver has a role to play, but 'more SAYGO less PAYGO' will not solve the problems and may create others.

Maturity of KiwiSaver is a long way behind maturation of the Superannuation Guarantee scheme in Australia, but it is not too soon to start planning for the role it could play in the future in improving fiscal sustainability and intergenerational fairness.

The Superannuation Researchers' Colloquium website is here.

RPRC's Advisory Board Inaugural Meeting 8 August 2012

The RPRC is honoured to welcome the members of the Advisory Board: Toni Ashton, Natalie Jackson, Matthew Abel, Craig Elliffe, Jonathan Eriksen, and Malcolm Menzies. Short biographies are available here.

After summarising their current projects, Co-Directors Susan St John and Michael Littlewood, and Research Fellow M.Claire Dale proposed a draft Strategic Plan. The Board members expressed their willingness for co-developing projects and peer review of publications. The Board will reconvene in February 2013.

The 5 elements of the Strategic Plan are:

- Closer international collaboration;
- Closer domestic collaboration;
- Offering a PhD or Masters scholarship in 2013;
- Closer liaison with industry groups; and
- Peer review by Board in areas of expertise.

RPRC's first step to activate the Plan will be visiting Australia's Centre of Excellence in Population Ageing Research (CEPAR), a collaboration between the Australian Government and Australian Research Council, the Australian National University, and the Universities of New South Wales and Sydney.

RPRC in the media and public presentations and contributions

9 July *PensionReforms* reviews The Financial Services Council's *Pensions for the Twenty First Century: Retirement Income Security for Younger New Zealanders* (2012) here.
12 July *Scoop Business* The Financial Services Council welcomes the contribution of Michael Littlewood, in his PensionReforms blog, to the conversation on how to provide future retirement incomes for New Zealanders here**.**
22 July *Sunday Star Times* Opinion*: Fair policies needed for overseas pensions,* by M.Claire Dale.
25 July *Journal of Ageing and Society*, Susan St John contributes as a Reviewer.
20 August *interest.co.nz* Amanda Morrall comments on RPRC's PensionCommentary 2012-4 on older workers here.
20 August *Aging Workforce News* (US-based) reports on RPRC's PensionCommentary 2012-4 on older workers here.
30 August, Wellington, Susan St John contributes to the external panel on the Long-term Fiscal Statement.
31 August *NZ Herald* in *Crossan speaking up for super*, Michael Littlewood on Retirement Commissioner Diana Crossan's retirement here.
5 September *J. Pension Economics & Finance* Susan St John reviews 'Reforming Pensions for Civil and Military Servants'.
6 September *Financial Literacy Symposium* Wellington Michael Littlewood 'What do we know about financial literacy?'
7 September *In$pring Financial Literacy Symposium*, Auckland, M.Claire Dale 'Nga Tangata Microfinance'.
9 September *RadioNZ* Chris Laidlaw interviews Susan St John on universal benefits and the welfare state here.
18 September *FST Media/Bravura* roundtable discussion: Michael Littlewood on the future of KiwiSaver.
26 September, Wellington, Susan St John contributes to the external panel on the Long-term Fiscal Statement.
September *Pension Watch* (Germany) online: oral submissions by Michael Littlewood and Larry Wilmore to a committee of Hong Kong's Legislative Council in November 2011 are now available here.

Susan St John: *Intergenerational Equity Issues for Investors*

Keynote Speaker at Investment Special Interest Group Meeting, 21 June 2012, at New Zealand Institute of Chartered Accountants' Conference Centre, Auckland.

Abstract: The world as it is suggests a future of discordant and surprising changes, and increasing tussle over who gets what of diminished resources. This is not only between nations but within, particularly between the generations as the baby-boom population ages. We shy away from a debate over distribution at our peril.

Investment is a dangerous word with different meaning in different contexts. The world is being turned on its head, and in 'investment' nothing is as the textbooks suggest. And nothing in economics is as the textbooks suggest. Yet we persist with the pretence that it is business as usual and all that matters, for example, is that KiwiSaver Provider A performs marginally better on post-tax/fees returns than KiwiSaver Provider B.

Intergenerational discontent is simmering amidst rising inequality compounded by ill-conceived public policy, with a changing demographic structure in a fragile economy. Hardship in New Zealand is not concentrated among those aged 65+, only around 4% of whom are in poverty. The baby-boomers have gained from free university education, capitalization of Family Benefit to purchase their first home, then benefitted from secure employment and a series of property booms. The global financial crisis may have harmed them, but it hasn't dealt a body blow. In stark contrast , youth unemployment hit 27% in 2009, the highest rate on record (see NBR here).

To improve intergenerational equity: adjust NZ Super, either by increasing the age of entitlement or means-testing it; revisit the tax system; reform PIEs and other means of tax avoidance; deal with the housing issues; and in particular, invest in the young.

New Zealand Herald July 18, Fran O'Sullivan: *Dear John: Generational Equity a must* here.

Susan St John: *How prepared is NZ for the ageing population: Can KiwiSaver save us?*

Keynote Speaker, Christmas Gouwland Limited and ANZ Business & Investment Seminar, 15 August 2012, at Ellerslie Event Centre, Auckland.

Abstract: New Zealand Superannuation is coming under the spotlight as the baby-boomers enter their twilight years. How well designed are New Zealand's policies? The McLeod Review 2001 stated: "We generally conclude that the [3-decade] reform programme has been a success and should not be reversed… There is little evidence that changes to the tax system will induce higher saving other than by redistributing from those who are less likely to save (typically poorer households) to those who are more likely to save (typically wealthier households)."

Our policies are fair. NZS is a flat-rate, universal pension, providing the same for everyone. It is good for women, who tend to have less time in paid employment. It does not require work-based contributions. It is taxable, with no hidden tax incentives that tend to be pro-male, pro-rich and costly. It is enhanced by KiwiSaver, a portable savings scheme with modest incentives introduced in 2007.

Have our policies prevented poverty? More successfully than just about anywhere else in the world, with around 4% of those aged 65+ in poverty (Ministry of Social Development 2012). This has nothing to do with how rich a country is. For example although Ireland has the highest wealth per capita in the EU, it has the worst record of pensioner 'relative poverty'.

Australia is often held up as the country doing the right thing by taking a save-as-you-go approach. Yet around 80% aged 65+ still rely on the means-tested Age Pension for more than 50% of their income. The private saving scheme, the Superannuation Guarantee (SG), is compulsory, very complex, and the tax incentives are very costly.

The harsh reality is that in 2009 the average SG balance was $198,325 for males aged 60 to 64 and $112,630 for females; and the median super balance for this group was only $58,630 for males and $9,770 for females (Clare, ASFA, 2012).

A popular fallacy in New Zealand is that saving will save us. But real investment is independent of saving in managed funds. There is no evidence that KiwiSaver has added to national saving or resulted in better investment, nor is it ever likely to. KiwiSaver will not save us.

PensionCommentary 2012-4, 13 August 2012

A commentary on older workers and some HR issues facing employers

New Zealand's baby boomers, born between 1946 and 1966, have started reaching age 65 and becoming eligible for New Zealand Superannuation.

Increasingly, as the workforce ages, reaching the state pension age does not mean stopping work. There is a growing difference between the present pension age and average retirement ages. In part, that has been caused by economic conditions but changes to state pension systems and longer healthy lives are also factors.

In New Zealand in 2006 (the most recent available data), about 85,000 of the approximately 500,000 people aged 65+ were in this group of 'labour market participants'.

Nevertheless, New Zealand faces a skill shortage as a consequence of falling birth rates and emigration. Employers will need to engage with older workers to maintain access to this important resource.

Baby boomers present a human resources' challenge to employers on at least two grounds: their retirement will leave labour and skill gaps that will need filling, and they will change the whole process of retirement.

Employers able to harness those two challenges will probably fare better as the 'silver tsunami' moves through New Zealand's age groups.

Link to the PensionCommentary here.

New Zealand's first *Financial Literacy Week*

A project inspired by Dianna Crossan, Retirement Commissioner (inset photo). The Commission for Financial Literacy and Retirement Income runs the New Zealand Network for Financial Literacy, a focal point for initiatives to improve New Zealanders' financial literacy, and home of the National Strategy for Financial Literacy.

On 6 September at the ***Financial Literacy Symposium – Connecting research with practice***, hosted in Wellington by the Auckland Centre for Financial Research and the New Zealand Centre for Personal Financial Education, Michael Littlewood's presentation used reports listed on www.PensionReforms.com to answer the question 'What do we know about financial literacy?'

On 7 September at the ***In$pring Financial Literacy Symposium***, hosted by Comet, in Auckland, M.Claire Dale spoke about Nga Tangata Microfinance, launched in 2011 in South Auckland. She argued that in New Zealand's low-wage economy, safe, fair, affordable credit becomes an essential service, like electricity. Currently, predatory lenders are keeping poor families in poverty. She advocated: teaching financial literacy in schools, workplaces, public places; supporting safe, fair, affordable lenders; and capping interest rates, so it would no longer be legal to charge a desperate person 500% interest on a small loan to buy food.

pension*reforms*

PensionReforms.com, giving direct, on-line access to 'pension' papers and providing summaries and commentaries, has just loaded its 600th abstract. The papers discussed are mainly academic, on public policy issues relating to ageing populations, for example, pensions, retirement, and retirement saving.

The reports now cover aspects of pension arrangements in 58 countries and four international groups of countries, such as the EU. There are more than 152 'International' reports that cover multiple countries. 789 authors from 200 institutions have written the 600 reports.

The three most recently loaded abstracts are:

Pension reform and long-term old age income security- the case of Taiwan: In Taiwan's complex pension arrangements, there are four main programmes: one is non-contributory; the others are contributory and two are heavily tax-subsidised. There is little information on how it all works but gaps are likely. more

Accounting Devices and Fiscal Illusions: Most governments run their financial reporting systems on a cash rather than an accruals basis. Most of the reasons that private enterprises are required to use accrual accounting also apply to governments but with some particular wrinkles. more

The End of Informality in Mexico? Fiscal Reform for Universal Social Insurance: The Mexican 1943 social security arrangements aren't working. Modelled on the Bismarckian system, they cannot cope with widespread 'informality'. The answer, apparently, is to 'strengthen' revenues with a consumption tax. more

Mark your diary: RPRC Symposium 30 November, The University of Auckland

Spending the Savings: *Decumulation & Middle-income Retirement*

Supported by the Commission for Financial Literacy & Retirement Income [More here]