Who pays for what?

Attached is the written submission from consumer group Kaspanz, on the review topic above. The primary focus of this submission relates to New Zealand Superannuation costs. Kaspanz is an incorporated society which began in February 2013, as a voice on retirement income issues for consumers. Our website is www.kaspanz.com . If there are to be consultations arising from the review submissions, Kaspanz would certainly wish to participate in them.

NEW ZEALAND SUPERANNUATION

The cost of NZ universal public pension is currently 4.1% GDP*, and* over the next 20 years will gradually increase to about 5.5% [1] . We note that most reviews conducted to date start from an assumption that taxpayers 2060 will be paying an expected 6.7% of GDP for NZS, and this figure is probably unacceptable. We challenge the presumption that the cost is unaffordable, and maintain it's reasonable and cost effective.

We note that New Zealand Superannuation is taxed at individual source, different to most other countries, and this difference is frequently misunderstood in comparative tables with other countries. Great care needs to be taken on this point, particularly with statistical tables. NZS is taxable income to recipients; the after-tax cost is the only one that matters. Estimated costs ten years out, then twenty years out, should be utilised much more, and where a projection past those time periods is used, qualifying comment on the accuracy should be mandatory

We support and understand the rationale for long term projections, but urge caution in the use of these figures in the context that the variables are significant, and forecasting into the future has so often proved to be wrong[2]. Even local commentators*,* question strongly the ability of experts to get things right[3].

Even for the gloomiest of predictions for costs associated with New Zealand Superannuation e.g. 7% of GDP by 2060, we suggest that this cost will still be one of the lowest in the OECD group, and due to the quality of our two major retirement instrument models (NZS& Kiwi Saver), costs at that level remain reasonable.

Despite the dire prediction around affordability, Treasury's modelling shows NZ Super as a proportion of GDP has actually dropped during the past decade, *"Even if the net cost of NZS increases by more than 60% to 6.7% by 2060, it will be a lot less than today's OECD average"* [4]. This is because GDP is growing rather than the actual costs diminishing[5]. Enhanced economic performance reduces NZ Superannuation cost, something the doom and gloom brigade rarely comment upon.

New Zealand is the smart country in relation to retirement income issues. When considering who pays for what from a public policy approach, the simplest and most reasonable policy formula should be accepted.

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[1] Tetlock P, Superforecasting: *The Art and Science of Prediction,* September 29, 2015
[2] Op. cit.
[3] Fisher C, Managing Director Fisher Funds, "*Experts put in their place*" March 24, 2016,The Herald
[4] Littlewood M , page 3
[5] Gascoigne JH, National Superannuation...affordable and sustainable National Grey Power Mag, June 2016

Some form of means testing. This may be logical in theory but impractical in practice; administration costs, and the significant use of trusts and similar schemes to camouflage income is a significant issue. Universality is also great for women. *The case for having a universal, flat-rate NZS pension remains very strong. It provides efficient longevity risk protection by guaranteeing a minimum real level of income for as long as a person lives. It avoids the disincentives to save and to continue earning and employment beyond eligibility age (unlike most overseas pension designs). It is simple to administer because it does not require lifetime earnings or contributions records to be kept. Its clear set of individual, unconditional entitlements by virtue of citizenship fosters social cohesion and is part of our sense of national identity... Finally NZS, together with a range of other supporting programmes, provides a really effective safety net and is the means by which New Zealand has achieved the lowest rates of poverty among older people in the OECD5 (even while poverty remains noticeably higher among younger age groups")* [6].

Two of New Zealand's eminent commentators Michael Littlewood and Martin Hawes both recently strongly supported the New Zealand Superannuation Model. *New Zealand Superannuation (NZS) is one of the simplest, most effective, and most cost effective Tier 1 schemes in the developed world. We mess with it at our peril" with* Hawes agreeing[7] *"NZ Super is a system so simple and cheap that we need to give people certainty and stop playing football with it". NZ Super is too good a scheme for the country to abandon. It should be protected and treasured".* Susan St John, from the Retirement Policy and Research Centre, Auckland University Business School emphasizes the gender fairness of New Zealand Superannuation," *it's an equalizing force for women upon retirement"* [8].

What are the comparative costs?

The following extract from Littlewoods paper (2015) on Superannuation costs, refers

Table: Projections of public expenditure on pensions 2010 & 2060 (as % GDP)

	2010	**2060**		**2010**	**2060**
Austria	14.1%	16.1%	Korea	0.9%	6.5%
Belgium	11.0%	16.6%	Netherlands	6.8%	10.4%
Canada	5.0%	6.2%	Norway	9.3%	14.2%
Denmark	10.1%	9.5%	Portugal	12.5%	12.7%
France	14.6%	15.1%	Spain	10.1%	13.7%
Germany	10.8%	13.4%	Sweden	9.6%	10.2%
Greece	13.6%	14.6%	United Kingdom	7.7%	9.2%
Ireland	7.5%	11.7%	United States	4.6%	4.7%

[6] Focusing on the Future, Report to Government, 2013 Review of Retirement Income, Commission for Financial Literacy and Retirement Income, Executive Summary page 6
[7] Hawes M, *The Great Gift of Super*, Sunday Star Times, October 19,2016@ *NZ Super: The $500,000 Gift*, October 20,2013
[8] Susan St John, e-mail communication to writer , 21 July 2016

Source: OECD *Pensions Outlook 2012*, p.210. The table shows gross costs which in many cases are the same as net costs. It ignores countries for which 2060 information was not supplied. Of the 31 countries reporting for 2010, only Australia (3.6%), Iceland (4.0%) Korea (0.9%) and Mexico (2.4%) reported a cost less than New Zealand's net 4.1%.
By 2060, of the 25 OECD countries reporting, only Canada, Korea and the United States expect public pension expenditure to be less than New Zealand's 6.6%. In fact, of the 31 countries reporting for 2010, 23 of them already pay more in 2010 than the net cost New Zealand expects to pay in 2060. The OECD 28 country average for 2010 was 9.3%.This is not to diminish the challenge of a 61% increase in the net cost of NZS over the next 50 years but rather to place that in an international context.

New Zealand may conclude today that a net 6.6% of GDP will be acceptable to 2060 voters, in which case the NZS pension itself doesn't need to change. However, if those 2060 voters decide that, say, 5.5% was preferable; the benefits can be cut relatively quickly to bring that cost down. A one-sixth reduction in the annual pension would do the trick and that could happen overnight... If today we expect that a net 6.6% might be too much then pensioners who will be alive in 2060 need as much notice as practicable. While they are working, they can save to replace the shortfall in their total retirement incomes[9].

Our comment on the above table would be the Australian cost appears to be understated, it is higher in a number of other projected and current tables, but it's the overall comparative analysis which we find interesting.

Why then is there such exaggerated rhetoric re pension unaffordability? The answer is the tabloid media approach of headlines rather than article substance, also a lack of research discipline by a number of commentators. More than a few of today's media commentators base their views on perception, adopting a world view based on a pack mentality among journalists commenting on NZ Super who have read what their peers say, but who appear to have done little in-depth research. It appears fashionable to start from a position critical of the status quo, by asserting NZ Super is unsustainable, without any demonstration of what economic pressures might make it so!

Add in the poor knowledge by many writers of trends over time, limited historical analysis, and denial of the various policy lever options available on retirement income issues, when considering options or redress. Perceptions and opinion is everywhere, much without rigour! We have yet to see a sustainable and coherent alternative to New Zealand Superannuation

We endorse the approach adopted by Hurnard[10]; commenting on New Zealand Superannuation

- It is extremely low cost in an administrative sense because it is funded out of general revenue, requires no individual contribution records to be kept and places no compliance cost on employers.
- There is no cost in administering an income test or monitoring changes in financial or employment circumstances.

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[9] Littlewood M
[10] Hurnard Roger, *Mixed messages: the future direction of NZ retirement income policies*,(2011) page13

- The absence of any employment or income test means that there are no built-in penalties from earning additional income beyond eligibility age. The present value of future pension wealth embodied in the scheme is unaffected by when a worker chooses to retire. This feature helps to explain why New Zealand has one of the highest rates of labour force participation of older people in the OECD.
- Knowing well in advance how much NZS will be worth proves a secure basis for people to judge how much additional income they need to plan for in order to achieve their own desired standard of living in retirement.
- Standard amounts for each person signals fairness and promotes social cohesion. Women in particular are protected by NZ Super.
- The scheme covers longevity risk efficiently by providing a known, fully indexed, gender neutral annuity. This is a critical contributor from New Zealand Super as a form of annuity that covers longevity risk, particularly for women

Another positive difference for NZ pension affordability is that the future NZ pension fund bill will be partly offset by the NZ Superannuation Fund. When projecting NZ Super costs long-term, we note few commentators off-set their cost projections with an assumption of the likely NZ Super Fund contribution. Current assumptions are somewhere between 8%-10% of future costs will be covered, not an insignificant amount.

The trend of encouraging people to work is also one of the most effective ways of reducing costs. The significant increase in NZ over recent years for seniors to remain in the work force in some form makes an enormous contribution to reduction in costs, and that trend is unlikely to reverse. . A workforce that stays employed for longer, whether or not the state pension age increases, is likely to produce more, save more and pay more taxes. It may also reduce the costs of ageing as older people who work may stay healthier for longer. A quarter (25.1%) of men and 14.8% of women aged 65 and over are now in paid work, up from just 8.7% of men and 3.4% of women only 15 years ago.

Let's get it out there. The New Zealand Super model is a world leader, no alternative system comes within a bull's roar of its overarching benefits across a range of indicators. Any cost saving requirements can be appropriately managed by any number of policy levers, with only minor adjustments, if any adjustment is considered necessary

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