

Workplace Savings NZ

Te māngai penapena ā-mahi

30 April 2010

Diana Crossan
Retirement Commissioner
Level 3, 69 – 71 The Terrace
PO Box 12-148
WELLINGTON

Dear Diana,

Retirement Commission 2010 Retirement Income Policy Review

Workplace Savings NZ wish to submit the following thoughts and comments relating to the 2010 review of Retirement Income Policy. We have noted the particular aspects and topics provided in the Terms of Reference by the Government, although our submission is not restricted to the aspects and topics mentioned.

It is clear that a number of noteworthy events have occurred during the three years since the last review in 2007 and that these will have a major influence on Retirement Income Policy going forward. We therefore think that the review should be broad based, focusing on how policy can reflect what we have learnt in recent years and how it can encourage further activity aimed at improving the environment for those in or facing their retirement years.

What has happened in the last three years that may influence future Retirement Income Policy?

In summary, we believe that the following will, or should, influence future Retirement Income Policy. Not all of these are 'events' as such; some being issues that have become clearer as time has passed. Most will also be influential on government policies other than those related solely to retirement income:

1. The KiwiSaver Scheme commenced in July 2007. This has proved to be much more successful than initially thought it would be. Uptake was influenced by the addition of further tax concessions.

2. Introduction of the PIE tax regime in October 2007. PIE removed disincentives to saving through managed funds versus direct investment.
3. Economic recession and the 'global financial crises' that emerged during 2008. An outcome has been the end of a period of government surpluses and the halting (temporary?) of contributions to the NZ Superannuation Fund.
4. Collapse of a number of Finance Companies.
5. Quality of financial advice. A start has been made to address the perceived lack of objectivity and professionalism within the financial advice industry. An issue that has been around for some years but highlighted by shortcomings in suitability of recommendations that became evident following the global financial crises and finance company collapses.
6. The generally poor level of financial literacy throughout NZ.
7. Quality of product disclosure material aimed at the average investor. Problems have been identified that relate to disclosure material that seems to be aimed at protecting the product provider in a regulatory regime that is, at best, uncertain, rather than informing investors. Particular issues surround the lack of transparency and consistency in the calculation and/or presentation of fees, product expenses and investment returns.

What aspects should be considered, in particular, in the 2010 review?

Workplace Savings NZ believes that the following aspects should be considered as part of this year's review. This list is not exhaustive but includes those areas that we think are important to consider at this time.

It is recognised that answers to many of the questions mentioned will not be readily available at present. We believe though that retirement income policy needs to be dynamic and suggest that a programme of ongoing research and debate is vital.

1. KiwiSaver
 - 1.1. Is it leading to higher savings levels overall
 - 1.1.1. Savings diverted to take advantage of tax concessions?
 - 1.1.2. Savings targeting the annual level of tax credit?
 - 1.2. Default investment portfolios. Consideration of suitability of conservative portfolio for all.

- 1.3. Policy needs to recognise that a large proportion of the public believe that KiwiSaver is 'Government guaranteed' and may prefer to minimise the level of likely investment losses.
 - 1.4. Reduction in standard contribution rate to 2%. Has this left an impression that saving at the rate of 2% + 2% (Employee and Employer Contribution) is sufficient to meet retirement needs?
 - 1.5. Impact of contribution holidays and hardship claims. The number of people joining KiwiSaver schemes has been high. How many will continue to contribute over the longer term.
 - 1.6. Arguments for and against making membership compulsory for those in the workplace need to be debated.
 - 1.7. Is there value/justification to extending tax incentives to all those in the workplace who contribute? At the younger end, those under 18 who are working might be encouraged to get into a savings habit if they received the same incentives as their over 18 work colleagues. At the older end, those over 65 may be encouraged to stay in the workforce.
 - 1.8. Should government regulate the forms KiwiSaver withdrawal should take at retirement age? For example Australia has introduced tax favoured "Allocated Pensions" in an attempt to change investors' behaviour.
 - 1.9. Should discretionary hardship and serious illness withdrawals be deferred to the Financial Markets Authority so that a consistent approach is applied across all providers, reducing the inefficiencies of claimants 'shopping around'?
2. Adequacy of retirement savings. Need for further research on:
- 2.1. Requirements for capital on, or in, retirement. That is, individuals do not consume all of their capital on day one of retirement. Many will continue to invest, living on earnings while running capital down over time.
 - 2.2. Requirements for income. Ongoing research is required to stimulate public debate on what level of personal retirement savings, if any, is appropriate to assist individual enjoy certain types of life style in retirement. E.g. basic, modest, or comfortable. Of course we recognise that such an approach can only be used as a guideline and will vary according to factors such as age, gender, retirement location, housing (owners versus renters), household composition, etc.
 - 2.3. Annuities.
 - 2.3.1. Lack of demand suggests it is probably too soon to expect providers to be thinking about reintroducing a range of annuity type products but perhaps the time is now right to remove any tax disincentives on annuities over the next two to three years,

2.3.2. Many potential annuity providers would be able to source an ever increasing range of options for differing annuities from overseas markets when they judge market timing to be appropriate.

2.4. Other Options

2.4.1. Many countries promote a diverse range of retirement income options for retirees. Government should be encouraging research in this area to facilitate choice for retirees in New Zealand.

3. Regulation and supervision of financial product providers

3.1. Changes proposed in Securities Trustee and Statutory Supervisors Bill. A number of recent events have shown up shortcomings in existing governance processes and this Bill is designed to address some of the issues raised.

3.2. Registered superannuation schemes and KiwiSaver Schemes.

3.2.1. Not initially covered by the Bill referred to above, but certain events surrounding the behaviour of the managers/trustees of one KiwiSaver scheme has led to the suggestion that the scope of the Bill should be extended, now reflected in Ministerial announcements on 28 April.

3.2.2. Under the present rules, superannuation schemes (including KiwiSaver schemes) are not subject to rules that seek to separate the functions and responsibilities of trustees from managers. Such schemes are fundamental elements in the provision of funds to be used in retirement.

3.2.3. We are not aware of any evidence that the position of superannuation schemes, where full responsibility for the activities of participants lies with the trustee, has proved to be detrimental to investors when compared to the split responsibilities model. However, there may be some logic in having a single governance regime applying to all similar types of managed funds offered to the public at large (i.e. unit trusts and superannuation schemes other than those operating solely in the workplace environment, where a different dynamic applies).

3.2.4. If a change for superannuation schemes were to be proposed, should the provisions of existing schemes and their trustees be protected?

4. Financial literacy. Is the level of knowledge of the population as a whole improving? What more should be done and what improvement can we realistically expect of those nearing or in retirement

5. Provision of financial advice. Should policy be aimed at encouraging people to seek financial advice?

- 5.1. Regulation of advisers. Legislation is due to take effect from late 2010. The legislation is aimed at enhancing/restoring public confidence in the financial advice profession. Its impact will need to be monitored.
 - 5.2. Enhancing adviser competence. This is clearly a cornerstone of the adviser legislation and should, over time, help in raising the level of financial literacy generally.
 - 5.3. Paying for Advice. The NZ public have generally shown that they are not enthusiastic about directly paying for financial advice and surveys have reinforced that the amount that the perceived 'worth' of advice is low. While this is clearly linked to a perception that the quality of advice is generally poor, has the high level of emphasis that has been placed on attempts to 'force down' product fees and constrain commission payments been interpreted as suggesting that advice has a low value?
6. Disclosure regime for financial products used for retirement savings purposes
 - 6.1. Review of Securities Act/Regulations. A full review is due to be completed by the end of 2010, although some aspects have been subject to revision on a piecemeal basis.
 - 6.2. What is appropriate? To what degree should the current level of financial literacy, and the public's willingness and ability to absorb information, shape the disclosure regime. What research has been done, or should be done, to establish what might work for the public as a whole - before introducing a new regime. What, and how, does policy help ensure that investors are told what they really need to know to enable them to make their decisions?
 - 6.3. Transparency/Consistency for calculating and expressing fees, expenses and investment returns. The lack of transparency and consistency in these areas, both in calculations and in how they are expressed, has been a major criticism of the current regime and needs to be addressed. Does the industry need to data warehouse such information under the control of an entity that is trusted by the investing public, such as the regulator?
7. NZ Superannuation
 - 7.1. Debate on sustainability. The continued availability of universal NZ Superannuation on the current basis has been a subject for ongoing discussion for many years. Major political parties appear to not want to raise any questions of sustainability as they seem to fear that this will be portrayed by their rivals as an intention to reduce current or future benefits.
 - 7.2. Workplace Savings NZ believes that renewed debate on sustainability is vital, such that options for the future can be properly considered and any desirable changes

implemented without undue haste. We believe that debate under the following headings is appropriate:

- 7.2.1. Age of entitlement. Currently set at 65. In common with many other countries, NZ has an ageing population (even if the perceived problem is not so acute in NZ as in some other places). Most other places also have, or had, an entitlement age of 65 and have reacted by announcing a planned increase in entitlement age over the coming decades.
NZ experienced a rather concentrated increase in entitlement age during the early 90s when the age moved from 60 to 65. There are other factors that may suggest that a higher entitlement age is now realistic. These are, firstly, that average life expectancy has increased significantly over the years. It is therefore reasonable to defer retirement beyond the previously accepted usual age.
- 7.2.2. Secondly, a shortage of labour is expected as the current working population retires from the workforce. A higher 'normal' retirement age (that related to being entitled to receive retirement benefits) may encourage workers to stay in the workforce longer.
- 7.2.3. An associated suggestion to assist here is that level of the benefit could be raised if receipt of the benefit is deferred.
- 7.2.4. Level related to NAWW. Currently set at 66% for a couple, indexed each year. Various suggestions for alternatives have been put forward in the past and are worthy of debate.
- 7.2.5. Universal Benefit. Largely, the NZ Super provides the same benefit (taxable), irrespective of income received or capital held. For universality to truly exist, in our view, NZ Super needs the relationship status and accommodation anomalies removed.
- 7.2.6. Asset and/or income testing could be considered / debated.
- 7.2.7. Contributions to NZ Superannuation Fund. These were discontinued, for fiscal reasons, in the 2009 Budget. What are the real and/or perceived impacts of this decision?

A Retirement Income Policy for New Zealand

Lastly, we would like to suggest that New Zealand needs to strongly consider an integrated approach for the outcomes of any Retirement Income Policy debate. For example, in our view, the much needed debate about the sustainability of NZ Super can not take place without the inclusion of research based discussion/debate on what constitutes retirement income adequacy, and role of 'self responsibility' for personal provision of retirement savings.

I would be pleased to discuss our comments or answer any queries in relation to the submission.

Thank you for the opportunity to make this submission. We hope that our comments will be of assistance in the review process and look forward to ongoing participation.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Bruce Kerr', with a large loop on the left side and a vertical line on the right.

Bruce Kerr
Executive Director

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