Retirement Policy and Research Centre

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Universal pensions

- the case for New Zealand (and one person's journey)

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Outline

- New Zealand’s pension landscape
- ... and the results
- The UK’s pension landscape
- ... and the results
- What I used to think
- My damascene experience
- The ‘proper’ roles for governments
- Other provision at Tiers 2 & 3
- Pension sustainability

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Background material

- On universal pensions
- On China's pension issues
- References in slides
- The New Zealand 'snapshot'
- New Zealand vs. UK - pensions

pensionreforms
Promoting high quality international debate on pension issues
veritas propter investigationem truth through research

Abstracts that cover Universal Pensions

At 15 November 2011

pensionreforms
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Abstracts that cover China

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References in Michael Littlewood's presentation

www.pensionreforms.com

NZ’s pension landscape – Tier 1

- ‘New Zealand Superannuation’ (started 1940)
  - Universal (modest residence requirements): no income or asset tests
  - Taxed as ordinary income
  - State Pension Age is 65
  - Non-contributory and was purely PAYG
  - Relatively generous – net 65% NAW for couple
  - Linked to average wages
- Current net cost: 3.7% of GDP
- 2050 net cost: 6.7% of GDP (source: Treasury 2011)

NZ’s pension landscape : private

- KiwiSaver (since 2007):
  - national, auto-enrolment, opt-out
  - privately administered
  - defined contribution scheme
  - employer-subsidised (to 2% of pay)
  - modest tax-subsidy (0.5% of GDP)
  - popular (39% of total population have joined)
- All other savings – ‘tax neutral’ (TTE)

… and the results (NZ)

- New Zealand has the simplest public pension in the developed world
- ... and amongst the lowest poverty rates amongst the age 65+ (2% - source: OECD 2008)
- ... at amongst the lowest total cost (4.2% of GDP - public pension + tax breaks for private)
- The regime for private provision is amongst the simplest
- New Zealanders are slightly over-saving for retirement (source: Treasury 2009)

UK's pension landscape: Tier 1 and Tier 1 ½

- Basic State Pension:
  - Modest
  - Full entitlement requires full contribution record (from 2010, 30 years)
  - Complex rules to cover non-earning periods, e.g. spouses, unemployed
- Pension Credit: a complex, income-tested, overall guarantee of minimum total pension incomes (public & private)

UK’s pension landscape: Tier 2

- State Second Pension (S2P, formerly SERPS)
  - Defined benefit pension based on earnings band
  - Originally maximum of 25% of covered earnings
  - From 2002, accrual favours lower-paid
  - From 2030, will be flat-rate
- Private Tier 3 schemes can ‘contract out’ of S2P (minimum benefit for lower NI contributions)

UK's pension landscape: Tier 3

- Relatively low level of private scheme membership (40% - source: PPI 2009)
- Relatively low levels of *private* pension income (average 28% vs. 42% from state: source DWP 2009)
- NEST starts 2012: auto-enrolment, opt-out requiring 8% contributions – 4% employees, 3% employers, 1% government
- NEST run by government

…and the result (UK)?

- Complex, expensive, constantly changing, public and private pension environment
- From 2012, even more complex
- Cost of tax breaks 1.5% of GDP (source: Hughes 2002)
- Poverty level for age 65+: 16% (source: PPI 2011); 10% on OECD basis (source: OECD 2008)
- Poverty levels (post NEST) should reduce to 7% in 15 years (source: PPI 2011)

What I used to think

- New Zealand Superannuation (Tier 1) should <u>not</u> be paid to people who didn’t need it
- Demographic costs unaffordable
- New Zealanders should be forced to save for retirement as they were not behaving ‘sensibly’
- Tax breaks for retirement saving encouraged self-provision

My damascene experience

(Task Force on Private Provision for Retirement: 1991-92)

- A simple, sustainable, universal, PAYG, Tier 1 is essential
- ‘Universal’ means ‘for everyone, regardless of income and/or assets’
- Of three alternatives for private provision, tax breaks are by far the worst; compulsion only slightly better
- By far the best is ‘voluntary’
- + great data, communicated well
- + political and community consensus on all of the above

The ‘proper’ roles for governments

- Only governments can:
  - Deliver Tier 1 pension to prevent/limit poverty in old age
  - Deliver credible assurances about health provision
  - Collect and deliver great data
  - Create/maintain a level regulatory playing field
  - Even-handedly supervise disclosure of relevant educational information.
- Everything else should be for employers, employees, providers, business owners, investors, educators and other individuals.

Other provision at Tiers 2 & 3

- A ‘successful’ **Tier 1** means the government has satisfied its income-support obligation
- **Tier 2** (compulsory supplementary provision, public or private) is unnecessary
- **Tier 3** (all other provision) is for employees, employers and individuals to decide
- Government’s role limited to regulation, information and education
- ….and then getting out of the way

Pension sustainability – what really matters

- All retirement provision arrangements (public or private pensions; occupational or personal savings) are claims on future economic output
- The cost of pensions is the benefits paid (regardless of financing arrangements)
- What really matters is the future economy
- With growth, everything is possible
- Anything else is about wealth distribution

The ten most dangerous words in the English language are: ‘Hi, I’m from the government and I’m here to help.’

Ronald Reagan, U.S. President, 1988