OFFICE OF THE MINISTER OF FINANCE

29 August 2005

Chair
CABINET BUSINESS COMMITTEE

KIWISAVER – MODIFICATIONS TO SCHEME DESIGN

Executive Summary

1. In Budget 2005, I announced the creation of KiwiSaver, a new work based savings scheme, to encourage voluntary saving for retirement and home ownership.

2. I am seeking Cabinet's agreement to modify the KiwiSaver scheme design slightly:

   - to align the lock-in of individual's own contributions and the upfront government contribution in retirement to reduce the risk of gaming by those close to the age of eligibility for New Zealand Superannuation (NZS); and

   - to address industry feedback that some features of the scheme for existing registered superannuation schemes (RSS) would not work as well as intended, which may result in the windup of good RSS.

3. These decisions are necessary now to ensure that legislation can be introduced by early 2006 and the scheme commence on 1 April 2007.

Proposal

4. This paper seeks Cabinet's agreement to:

   - requiring individuals' own contributions be locked in until the age of eligibility for NZS or five years since their first contribution to the scheme, which ever is later;

   - permitting members of existing retail and employer RSS to convert into a KiwiSaver scheme at the individual member level;

   - modifying the exemption from the automatic enrolment provisions for new employees that employers with existing RSS can apply for given concerns that few, if any, employers would be eligible for the exemption; and

- aligning the point that the upfront government contribution is received and the point where a contribution holiday can be taken.

Background Information

5. KiwiSaver is designed to complement NZS for those that wish to achieve a higher living standard in retirement. Savings will help individuals to build up assets, reduce debt dependency and increase financial independence and flexibility, particularly in retirement.

6. KiwiSaver will enable employees to make regular contributions from their wages and salary deducted through the tax system and passed on to be invested in privately provided investment vehicles. New employees will be automatically enrolled, with the ability to opt out, and existing employees will be able to opt in.

7. KiwiSaver has been designed to minimise compliance costs on employees and employers by utilising the existing tax system infrastructure. In addition, the design of the scheme has been driven by equity, simplicity, and practicality considerations.

8. In order for KiwiSaver to be up and running on 1 April 2007, legislation has to be passed, providers selected, systems put in place, and information packs prepared and distributed. The overall timetable is tight and requires legislation to be passed by mid 2006.

9. The initial set of drafting instructions will be provided to the Parliamentary Counsel Office in mid August. These instructions will cover Cabinet decisions to date and further decisions made by me, in consultation with the Minister of Housing, Minister of Education and Minister of Commerce.

Comment

Access to contributions for those close to the age of eligibility for NZS

10. Cabinet agreed that, with the exception of the specified withdrawals, KiwiSaver funds would be locked in until the age of eligibility for NZS (CAB Min (05) 13/9 paragraph 3.9 refers). However, the upfront government contribution would be locked in until the age of eligibility for NZS or five years in the scheme, whichever is greater, to reduce the risk of gaming (CAB Min (05) 13/9 paragraph 3.16 refers).

11. This means that KiwiSaver imposes different lock in periods for employees close to the age of eligibility for NZS on their own contributions and the government upfront contribution. As a result, people close to the age of eligibility for NZS may be able to receive the government upfront contribution without needing to lock in their own contributions for any significant period. In addition, it adds unnecessary complexity.

12. Hence, I propose that individuals' own contributions also be locked in until the age of eligibility for NZS or five years in the scheme, whichever is later. This approach will further reduce the risk of gaming for those close to the age of eligibility for NZS while not precluding the ability of this group to join KiwiSaver.

Existing superannuation scheme conversion

13. Cabinet agreed that an existing RSS could choose to fully convert to a KiwiSaver scheme and in doing so meet all the KiwiSaver characteristics (CAB Min (05) 15/2 paragraph 2 refers). The rationale for conversion mechanism was to reduce the risk that existing RSS would be wound up, leading to the withdrawal of funds and a lower level of employer contributions to saving.

14. I undertook to consider whether the existing legislative requirement that all members need to agree to any change to an RSS that may reduce members' rights and benefits should apply for RSS that convert to a KiwiSaver scheme (CAB memo (05) 15/2 paragraph 6 refers).

15. I had been considering whether a lower level of member consents would facilitate more RSS converting into KiwiSaver schemes while still maintaining adequate member protection. However, less than 100% member consent would undermine this important investor protection without increasing the likelihood of conversions given RSS may have significantly different terms and conditions from those of KiwiSaver.

16. Therefore, I consider that conversion is only likely to be practical at the individual member level and with the prior consent of the individual member.

17. I propose allowing RSS to convert by:

    - establishing a discrete section within their existing scheme voluntarily that meets the minimum contribution amount and other KiwiSaver criteria;

    - permitting members individually to voluntarily transfer to that section; and

    - requiring employers to automatically enrol new permanent employees into the KiwiSaver section but these employees could opt out.

18. Members of the KiwiSaver section would then be eligible to receive the upfront government contribution, fee subsidy and be eligible for the housing deposit subsidy.

19. The above option would reduce the incentive for employers or trustees to wind-up RSS, increase conversions, and require employers and trustees to deal with two different types of members. To the extent that this option encourages more RSS members to become KiwiSaver members than would have otherwise been the case, it will increase the fiscal cost of the savings package.

20. Both employer-sponsored and retail schemes would be able to establish a discrete section.

Employer exemption from the automatic enrolment provision

21. Cabinet agreed that employers with existing RSS be eligible to apply for an exemption from the automatic enrolment provision for new employees if their schemes:

- are portable;
- are open to all permanent employees; and
- with total actual contributions (employee plus employer) of at least 4% vested in the employee immediately (CAB Min (05) 15/2 paragraph 5 refers).

22. The employer exemption from the automatic enrolment provision was to recognise that many employers with existing RSS often provide significant employer subsidies and reduce the risk that good employer schemes windup.

23. Members of RSS with employers that qualify for this exemption will be eligible for the housing deposit subsidy on the same terms and conditions. However, they will not be eligible for the upfront government contribution or the fee subsidy. As a result, the criteria for the employer exemption from the automatic enrolment provisions need not be the same as for KiwiSaver generally.

24. [text deleted]
expressed a concern that few, if any, employers would be eligible for the exemption from the requirement to automatically enrol new employees in KiwiSaver despite employers actively encouraging workplace saving.

25. Most employers with existing RSS will not meet the existing criteria given the low level of minimum prescribed employee contributions, longer vesting period and schemes not being accessible to all employees.

26. Therefore, I propose that the employers with RSS that do not convert be eligible for the exemption from the automatic enrolment provision if their RSS meets the following criteria:

    - portability (ie balances can be transferred to other similar products upon leaving the employer). This criteria is the same as agreed previously;
    - open to all *new* permanent employees (coverage through multiple schemes is permissible). This limits the earlier criteria to new employees as some employees may be members of old schemes and not able to join more recent employer sponsored schemes; and
    - the minimum prescribed amount the employee must contribute plus the maximum employer contribution for all employees must be at least 4% of gross salary which vests in the employee within 5 years. For example, a scheme, where members are required to contribute a minimum of 1% of salary and the employer is willing to match member contributions up to a maximum of 3% would result in a total notional contribution of 4% of salary.

27. This proposal should discourage good employer RSS from winding up while still giving employees with these employers the choice of joining their employer RSS or opting in to KiwiSaver, if they wish.

28. However, many employers with RSS will still not be eligible for the employer exemption from the automatic enrolment provision. This reflects the fact that

many schemes are not open to all new permanent employees, require the completion of a minimum period of service with the sponsoring employer before a new employee is eligible to join the scheme and have longer vesting periods. I considered that it was not possible to accommodate these features without compromising the objectives of KiwiSaver.

Upfront government contribution timing

29. Cabinet agreed on the automatic enrolment process that:

- Inland Revenue will hold contributions in trust for a further eight weeks after the first contribution is received (CAB Min (05) 15/2 paragraph 13 refers);
- the upfront government contribution will be provided to an individual's account eight weeks after the first contribution is received (CAB Min (05) 15/2 paragraph 14 refers); and
- a contribution holiday option not be available unless the person has been contributing to KiwiSaver for at least three months (CAB Min (05) 15/2 paragraph 18 refers).

30. I consider that it would be preferable to align the timing that an individual receives the government's upfront contribution, the point funds are passed to providers and the time that a contribution holiday can be taken. Hence, I propose that the upfront government contribution be provided to the individual three months after Inland Revenue receives the first contribution. This proposal would delay the fiscal profile by around one month.

Financial Implications

31. The financial implications for the savings package were incorporated as part of the contingency for the Savings Allocation agreed in Budget 2005 (POL Min (05) 9/1(4)). The proposals contained in this paper may increase the overall fiscal cost and hence have some implications for the size of the Savings Allocation although these costs are unlikely to be large relative to the size of the overall package. At this stage, it is not possible to quantify the impact of the various policy changes.

32. Officials will undertake a broader review of the estimates underlying the Savings Allocation later this year incorporating the impact of these proposals. If this review suggests that the current Savings Allocation is not adequate then I will report back to Cabinet later this year to seek agreement to any change in the Savings Allocation.

Legislative Implications

33. Legislative implications for KiwiSaver as a whole were outlined in the initial and subsequent Cabinet paper (CAB Min (05) 13/9 and CAB Min (05) 15/2 refer).

Regulatory Impact and Business Compliance Cost Statement

34. Based on the information provided in the attached RIS/BCCS, the Regulatory Impact Analysis Unit considers that the disclosure of information is adequate, and the level of analysis is appropriate given the likely impacts of the proposal.

35. The proposals in this paper will generally decrease compliance costs on employers and providers. However, steps will be taken to minimise compliance costs on employers and providers, such as through consultation and providing guidance.

36. A RIS is not required for the change in the time of the upfront government contribution as it is of minor and machinery nature and does not substantially alter existing arrangements (see Cabinet Office Circular (04) 4).

Treaty Implications

37. KiwiSaver has no treaty obligations as presently designed.

Human Rights Act

38. The proposals in this Cabinet paper appear to be consistent with the rights and freedoms affirmed in the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993. A final view will be possible once the Bill has been drafted.

Publicity

39. No publicity is planned. However, I propose that the RIS/BCCS material will be published at the time the legislation is introduced into Parliament.

Consultation

40. The following agencies have been consulted in the preparation of this Cabinet paper: Inland Revenue Department, Ministry of Economic Development, Ministry of Justice, Ministry of Social Development (MSD), Housing New Zealand Corporation, Department of Labour, Te Puni Kokiri, State Services Commission, Ministry of Youth Development, Ministry of Pacific Island Affairs and Ministry of Women's Affairs. The Department of Prime Minister and Cabinet has been informed.

41. The MSD noted that the changes for those close to retirement may not deter people from joining and may be fiscally expensive and only encourage minimal contributions to saving. The MSD suggested an alternative be considered where the full entitlement for the upfront government contribution is only available where there is at least a total of five years of contributions made. For less contribution periods, a proportional payment would be made. The MSD proposal would add unnecessary complexity to KiwiSaver and reduce the incentive for people to participate significantly. In addition, the MSD questioned the benefits of changing the criteria for the exemption from the automatic enrolment provisions on the grounds that it does little to raise the bar in terms of superannuation schemes provided by employers and may reduce the incentive to save.

42. [text deleted]

were consulted at a high level on the proposed design changes for registered superannuation schemes and the employer exemption from the automatic enrolment provisions. This consultation has also informed development of the detailed policy design issues included in this Cabinet paper.

Recommendations

I recommend that Cabinet:

1 **note** that on 11 April 2005 Cabinet agreed that, with the exception of the withdrawals in the case of purchasing a first home, financial hardship or permanent emigration, funds will be locked in until the age of eligibility for New Zealand Superannuation [CAB Min (05) 13/9 paragraph 3.9];

2 **rescind** the decision referred to in paragraph 1; and instead

3 **agree** that, with the exception of the withdrawals in the case of purchasing a first home, financial hardship or permanent emigration, funds will be locked in until the age of eligibility for New Zealand Superannuation or for five years from the first contribution, whichever is later;

4 **agree** that any existing registered superannuation schemes (RSS) be able to convert to being KiwiSaver compliant by:

4.1 establishing a discrete section within their scheme that complies with the KiwiSaver criteria;

4.2 permitting members individually to voluntarily transfer to that section; and

4.3 requiring employers to automatically enrol new permanent employees into the KiwiSaver section but these employees have the opportunity to opt out;

5 **agree** that members of a KiwiSaver section of an RSS will receive the upfront government contribution, fee subsidy and be eligible for the housing deposit subsidy;

6 **note** that on 2 May 2005 Cabinet agreed that employers with existing RSS be eligible to apply for an exemption from the automatic enrolment provision for new employees if their schemes are:

6.1 portable;

6.2 open to all permanent employees;

6.3 total contribution (employer plus employee) of at least 4% of gross salary that vests in the employee immediately [CAB Min (05) 15/2 paragraph 5];

7 **rescind** the decision referred to in paragraph 6; and instead

8 **agree** that employers with existing RSS be eligible for an exemption from the automatic enrolment provisions for new employees if their schemes:

8.1 are portable;

8.2 are open to all new permanent employees;

8.3 require the minimum prescribed employee contribution plus the maximum employer contribution for all employees to be at least 4% of gross salary that vests in the employee within five years;

9 **note** that on 2 May 2005 Cabinet agreed that:

9.1 Inland Revenue will hold contributions in trust for a further eight weeks after the first contribution is received;

9.2 the upfront government contribution will be provided to an individual's account eight weeks after the first contribution is received [CAB Min (05) 15/2 paragraphs 13 and 14];

10 **rescind** the decision referred to in paragraph 9; and instead

11 **agree** that Inland Revenue will hold contributions in trust for a further three months after the first contribution is received;

12 **agree** that the upfront government contribution will be provided to an individual's account three months after the first contribution is received (at the same time Inland Revenue passes funds to a provider);

13 **note** that the proposals in this paper may increase the overall fiscal cost though it is not yet possible to quantify the impact of these changes;

14 **request** the Minister of Finance to report back to Cabinet if a forthcoming review of the estimates underlying the Savings Allocation suggests that the current Savings Allocation is not adequate;

15 **invite** the Minister of Finance to issue drafting instructions to the Chief Parliamentary Counsel, in conjunction with Inland Revenue's Internal Drafting Unit, to draft legislation to give effect to Cabinet's decisions [CAB Min (05) 13/9 and CAB Min (05) 15/2] and decisions made by the Ministers of Finance, in consultation with the Minister of Housing and Minister of Education; and

16 **agree** to instruct Parliamentary Counsel Office to draft in accordance with paragraph 15.

Hon Dr Michael Cullen
Minister of Finance

REGULATORY IMPACT STATEMENT

STATEMENT OF THE NATURE AND MAGNITUDE OF THE PROBLEM AND THE NEED FOR GOVERNMENT ACTION

In Budget 2005, the Government announced that it would introduce a work based saving scheme, KiwiSaver, to commence from 1 April 2007. KiwiSaver is designed to obtain a change in behaviour for people who are not currently saving or are under saving, and to get them into the habit of saving. More detail on the overall regulatory impacts of KiwiSaver can be found in the other KiwiSaver regulatory impact statements available on the Ministry of Economic Development's website at www.med.govt.nz/buslt/compliance/risbccs/hints-tips/hints-tips.html.

The following problems with KiwiSaver have been identified:

- <u>Access to contributions for those close to the age of eligibility of New Zealand Superannuation</u>: that the lock-in for a member's own funds may be significantly less than the $1000 upfront government contribution for people close to the age of eligibility for New Zealand Superannuation. This may create an incentive for this group to join KiwiSaver, make only three months contributions (or less if they cease being wage and salary earners) and then take a contribution holiday until the age of eligibility for New Zealand Superannuation. In addition, these people could withdraw their own contributions as soon as they reach the age of eligibility for New Zealand Superannuation, which result in their own funds only being locked in for months. Hence, the $1000 may not be compensation for forgoing the use of their funds for a significant period and may not encourage higher savings;

- <u>Existing superannuation scheme conversion</u>: existing trust deeds may only be altered if 100% of members consent, which means that if one member opposes or withholds their consent then the trust deed cannot be amended. This requirement is likely to preclude any registered superannuation scheme (RSS) from being able to fully convert into a KiwiSaver scheme, given the longer lock-in and 4% minimum contribution rate. In the absence of RSS being able to convert, RSS may be more likely to wind up rather than needing to deal with two workplace saving schemes;

- <u>Employer exemption from the automatic enrolment provision</u>: few, if any, employers with existing RSS would be eligible for the exemption from the automatic enrolment provisions given most RSS are not open to all permanent employees, do not require significant member contributions and have longer vesting periods. All of these criteria must be met for an existing RSS to be exempt from the automatic enrolment provisions. These employers would then need to offer two workplace saving schemes (their own RSS and KiwiSaver) and there is also a risk that some employers may wind up their RSS as a result.

STATEMENT OF THE PUBLIC POLICY OBJECTIVES

The primary objectives of KiwiSaver are:

- to support a cultural change in New Zealanders' attitudes toward savings to increase self reliance and forward planning; and

- to help create a financial buffer for New Zealand households through the building up of assets, reducing debt dependency and giving people increased financial independence and flexibility, particularly in retirement.

STATEMENT OF FEASIBLE OPTIONS (REGULATORY AND/OR NON-REGULATORY) THAT MAY CONSTITUTE VIABLE MEANS FOR ACHIEVING THE DESIRED OBJECTIVE(S) AND NET BENEFITS (INCLUDING NON-QUANTIFIABLE BENEFITS) OF THE PROPOSAL, AND OTHER FEASIBLE OPTIONS

The key features of the status quo and the proposed option(s), including the benefits and costs, are outlined below. The key features of the status quo reflect the decisions already taken in regard to KiwiSaver unless specified. The status quo is not preferred as it does not meet the policy objectives to the same extent as the preferred option.

Access to contributions for those close to the age of eligibility for New Zealand Superannuation

Status quo:

- The individual's own KiwiSaver funds would be locked in until the age of eligibility for New Zealand Superannuation.

Alternative option:

- Individuals within five years of the age of eligibility for New Zealand Superannuation (i.e. individuals aged 60-64) would not be automatically enrolled or able to opt in, but they may continue to contribute to a KiwiSaver account if they have opened it prior to reaching this age.

While this option would lower the fiscal cost, it is not preferred because it would prevent those close to the age of eligibility for New Zealand Superannuation from being able to join and save through KiwiSaver.

Preferred option:

- All individual's own funds would be locked in until the age of eligibility for New Zealand Superannuation or for five years from their first contribution, which ever is later. This would apply to all age groups not just those aged 60-64. For example, if a person aged 62 joins KiwiSaver and starts contributing then their funds would be locked in until they turn 67.

Government

The government may have a slightly lower fiscal cost because employees within five years of being eligible for New Zealand Superannuation may be less likely to join the scheme and obtain the upfront contribution and fee subsidy given their funds will be locked in for longer. The amount of fee subsidy paid for those employees that join in this age group may be greater given their balance is higher for longer (fees are often levied as a percentage of funds under management) which may partly offset some of the decline in fiscal costs. However, participation may not be significantly lower as the upfront contribution was subject to a minimum of five years lock in anyway.

Providers

Providers may face less demand for KiwiSaver but benefit from funds being locked in for longer, holding less small balances and having fewer withdrawals to administer given those that join near the retirement age would be unable to access their funds for a minimum of five years. Fewer withdrawals to administer may reduce compliance costs on providers. These costs are detailed in the Business Compliance Cost Statement.

Employees

According to the Statistics New Zealand, there were 104 700 people aged 60 to 64 years old inclusive in the labour force in the March quarter 2005 out of a population of 177 800 in this age group.

Employees who join KiwiSaver close to retirement will not be able to access their funds for a minimum of five years after their first contribution. As a result, this will defer any withdrawals, except in the case of financial hardship, on retirement for this group. It may also discourage some employees in this age group from joining KiwiSaver and obtaining the $1000 upfront government contribution.

Existing Superannuation Scheme Conversion

Status quo:

- A converted scheme would need to meet all the characteristics of the KiwiSaver, including 4% employee contribution and lock-in until age 65. Members of RSS that fully convert would be entitled to all KiwiSaver benefits (fee subsidy, up-front government contribution, and would be eligible for the home ownership deposit subsidy) (CAB Min (05) 15/2 paragraphs 2 and 3 refer).

- Members of RSS would only be eligible for the upfront government contribution, fee subsidy and housing deposit subsidy through their scheme if it converted.

- A RSS would be only able to convert if 100% of members agreed to the conversion.

Alternative option:

- Reduce the existing legislative requirement that 100% of members need to consent before a RSS could convert into a KiwiSaver scheme.

This option is not preferred because it would undermine important investor protections, and would be unlikely to encourage RSS to fully convert into a KiwiSaver.

Preferred option:

- Existing retail or employer sponsored RSS would have the option of establishing a discrete section within their scheme that meets the minimum contribution amount and other KiwiSaver criteria, such as 4% employee contribution and lock-in until age 65. This would effectively permit two classes of members: one class with existing terms and conditions; and the second class with 4% employee contributions, lock-in until age 65, any employer contributions (subject to the any terms set by the employer), and entitled to the upfront government contribution and fee subsidy.

- Establishing a discrete KiwiSaver section would be optional and at the discretion of both the provider and employer in the case of an employer operated scheme. It would also be optional and discretionary for providers running purely their own retail schemes.

- Members of the RSS would be permitted individually to voluntarily transfer to that discrete section. A person saving in that discrete section would both be an RSS and KiwiSaver member.

- Employers would be required to automatically enrol new permanent employees into the KiwiSaver section but these employees have the opportunity to opt out.

Government

To the extent that this encourages more RSS members to become KiwiSaver members through transferring to the KiwiSaver section than would have otherwise been the case, it will increase the fiscal cost of the savings package.

The government as an employer is directly affected by the treatment of the various existing state sector schemes, including the new State Sector Retirement Savings Scheme (SSRSS). These state sector schemes would need to decide whether to offer a discrete KiwiSaver section which members could voluntarily select.

RSS members and employees

In 2005, RSS had around 643,000 members and $16.7 billion in assets (not including the Government Superannuation Fund).

As conversion will be possible at the individual member level, it is likely that some RSS members will select this account to obtain the government contributions, where the option is available. This will result in effectively two classes of RSS members: existing RSS members and RSS KiwiSaver members. RSS KiwiSaver members will be able to obtain any employer contributions, upfront government contribution and fee subsidy, through a single contribution (of either 4 per cent or 8 per cent).

It is difficult to judge how many RSS will establish a discrete section or how many employees would transfer or select this section. Nevertheless, employees and members of RSS may be more likely to participate in KiwiSaver and save more if conversion is possible at the individual member level.

If a discrete KiwiSaver section is not available, RSS members will still have the option of joining KiwiSaver direct (that is, outside of their RSS). In this case, the RSS member would need to make two contributions (one to their RSS and another to KiwiSaver) assuming they wish to continue saving through their existing RSS.

Employers

Employers can choose whether to establish a KiwiSaver section within their scheme or not. It will not be necessary to seek member consent before doing this, given that opting in will be voluntary for existing RSS members.

Employers may consider establishing the section to retain staff or in response to employee demand for this option. An employer will incur compliance costs in establishing a discrete section, such legal costs in amending the trust deed. These costs are further detailed in the Business Compliance Cost Statement.

Employers or trustees may have less incentive to wind-up their RSS as an additional discrete section can be established within their existing scheme. This option is likely to be more feasible for employer schemes operated by retail master trusts rather than operated directly by the employer. Employers with existing RSS may be able to avoid the need to deal with two different saving schemes (although it may add an additional member type).

The requirement to enrol new permanent employees into a KiwiSaver section where available may increase costs on employers as more employees might take up membership of the RSS and be entitled to any employer contribution.

Providers

Providers may establish a KiwiSaver section to attract new members and retain existing members who may otherwise have left the scheme to join KiwiSaver in order to qualify for the government contributions. Provider will incur costs in establishing a discrete section. For large providers, the cost may not be substantial as many schemes already operate with several sub accounts or classes of members.

Employer exemption from the automatic enrolment provision

Status quo:

- For RSS that do not convert, employers with existing RSS would be able to apply for an exemption from the automatic enrolment provisions if their schemes are: portable, open to all permanent employees, and with total actual contributions (employee plus employer) of at least 4 per cent vested in the employee immediately (CAB Min (05) 15/2 paragraph 5 refers).

Preferred option:

- Employers with existing RSS will be eligible for an exemption from the automatic enrolment provisions for new employees if their schemes are portable, open to all new permanent employees, and require the minimum prescribed employee contribution plus the maximum employer contribution for all employees to be at least 4 per cent of gross salary that vests in the employee within five years.

Government

To the extent that more employers are eligible for the exemption for the automatic enrolment provision for new employees and hence more employees are excluded from the automatic enrolment mechanism, the fiscal cost may decrease as the automatic enrolment mechanism tends to increase the likelihood of new employees joining KiwiSaver over those that opt in given inertia.

Employers

Employers who contribute to their employees' superannuation will need to decide whether to continue to contribute to their existing RSS, close the scheme to new members and/or make their contributions to KiwiSaver accounts. More employer schemes may be eligible for the revised employer exemption criteria given schemes often permit low minimum contributions, treat existing and new employees differently, and have long vesting periods for employer contributions.

Employers that qualify for the exemption from automatic enrolment provisions will not need to automatically enrol their new employees which will reduce compliance costs. The detail is discussed in the Business Compliance Cost Statement.

Employees

As more employees may be exempt from the automatic enrolment provision, there may be less of an incentive to save.

Employees who work for exempt employers and save in their RSS will be eligible for the housing deposit subsidy (subject to qualifying) to assist in purchasing their first home. Hence, to the extent that more employers qualify for the exemption from the automatic enrolment provisions then more employees may be in this category.

Members of RSS that do not work for an exempt employer will not be eligible for the housing deposit subsidy but still will be able to join KiwiSaver to obtain the housing deposit subsidy and other government contributions.

STATEMENT OF CONSULTATION UNDERTAKEN

Stakeholder consultation

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were consulted at a high level on the proposed design changes for registered superannuation schemes and the employer exemption from the automatic enrolment provisions. This consultation has also informed development of the detailed policy design issues included in this Cabinet paper. These stakeholders supported the direction of the changes to the employer exemption to the automatic enrolment provision and conversion mechanism but were still concerned that too few employers would be eligible for the revised employer exemption. It was not possible to accommodate these concerns while ensuring that all employees were provided with an adequate opportunity and incentive to save through the workplace or provide adequate consumer protection for members of RSS.

Government Departments/Agencies Consultation

The following agencies have been consulted: Inland Revenue Department, Ministry of Economic Development, State Services Commission, Housing New Zealand Corporation, Ministry of Social Development, Department of Labour, Ministry of Justice, Te Puni Kokiri, Ministry of Pacific Island Affairs, Ministry of Youth Development, and Ministry of Women's Affairs. Department of Prime Minister and Cabinet has been informed of these proposals. Several agencies raised concerns about the alternative option for access to funds in retirement given that many people continue in the labour force beyond 65, there is a real appetite of older age groups for savings and the gaming risk is not limited to this group. These concerns have been reflected in the preferred option by continuing to allow people aged 60-64 to join KiwiSaver.

The MSD noted that the changes for those close to retirement may not deter people from joining and may be fiscally expensive and only encourage minimal contributions to saving. The MSD suggested an alternative be considered where the full entitlement for the upfront government contribution is only available where there is at least a total of five years of contributions made. For less contribution periods, a proportional payment would be made. The MSD proposal would add unnecessary complexity to KiwiSaver and reduce the incentive for people to participate significantly. In addition, the MSD questioned the benefits of changing the criteria for the exemption from the automatic enrolment provisions on the grounds that it does little to raise the bar in terms of superannuation schemes provided by employers and may reduce the incentive to save.

BUSINESS COMPLIANCE COST STATEMENT

The proposals in this paper will generally decrease compliance costs on employers.

The greater lock-in of funds for those that join KiwiSaver close to the age of eligibility for New Zealand Superannuation will improve the economics for providers in holding these accounts. Providers and trustees will have less separate withdrawals to administer for people at or past the age of eligible for New Zealand Superannuation, as all funds will be locked in for the same period. As a result, providers and trustees will incur less compliance costs processing requests for withdrawals for financial hardship and for employees seeking to access their own contributions. These costs include dealing with queries and costs incurred in selling parts of their portfolio to generate the required funds.

Existing registered superannuation schemes will incur compliance costs if they choose to establish a KiwiSaver section in their schemes. These costs are likely to include the costs of changing the trust deed, prospectus and investment statements, including legal costs, and any costs incurred in registering the section as a KiwiSaver scheme.

The exemption from the automatic enrolment provision would reduce ongoing compliance costs for exempt employers, especially those with high staff turnover, as they would not be required to provide information packs (basic information about KiwiSaver) to new employees and make payroll changes unless they had a KiwiSaver section and new employees opt in.

It is not possible at this stage to estimate the compliance costs of the proposed changes to the KiwiSaver. In addition, consultation with affected groups has been at a high level and has not been directed at ascertaining the potential quantum of compliance costs.

However, steps will be taken to minimise compliance costs, including through putting information on the web, preparing guidance notes, consulting with providers in developing the information pack and outlining the options available for existing RSS.