The Treasury

New Zealand Superannuation Information Release

Release Document July 2017

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[1] 9(2)(a) - to protect the privacy of natural persons, including deceased people

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[3] Deleted – not relevant to the announcements

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THE TREASURY
Kaitohutohu Kaupapa Rawa

Treasury Report: NZ Superannuation Policy Options

Date:	10 February 2017	**Report No:**	T2017/222
		File Number:	AD-1-51

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Steven Joyce)	Note the key points and agree policy preferences to feed into the Cabinet paper.	Prior to Cabinet paper presentation

Contact for Telephone Discussion (if required)

Name	Position		Telephone	1st Contact
Melissa Piscetek	Analyst	[2]	N/A (mob)	✓
Peter Gardiner	Manager		[1]	

Actions for the Minister's Office Staff (if required)

Return the signed report to Treasury.

Provide feedback to Treasury on the NZ Super policy preferences that are to be included in the Cabinet paper

Note any feedback on the quality of the report	

Enclosure: No

Treasury Report: NZ Superannuation Policy Options

Executive Summary

You have asked officials to prepare a cabinet paper proposing changes to New Zealand Superannuation (NZS) policy. This paper outlines these proposed changes, along with options, and provides additional detail and fiscal implications relating to the implementation of proposed changes.

You gave the Treasury direction to examine increasing the age of eligibility from 65 to 67 years of age from 2037. Amongst the reasons for this were generating fiscal savings, encouraging older age group labour force participation, and better targeting welfare spending amongst all vulnerable groups in society. In support of these goals, and in line with your direction we recommend the following policy changes:

- **Raising eligibility age**: You could consider introducing this change from 2027, which would provide even greater fiscal savings.

- **Indexation to longevity**: Raising the age of eligibility by one year every decade starting in 2050.

- **Residency requirements**: From 2027 amending residency requirements so that new superannuation recipients must have lived in New Zealand a minimum of twenty years, with five of those after the age of 50.

- **Non-qualifying partners**: Removing the non-qualifying partner option from 2022, while ensuring all existing non-qualifying partners (up to 1 July 2022) are fully grandparented.

We also recommend a phased approach to the proposed policy changes starting with the removal of non-qualified partners in 2022, followed by changes to residency requirements in 2027 and changes to the age of eligibility in 2037.

Skilled older workers will play an increasing role in increasing productivity which in itself will assist in meeting the challenges of the ageing population. Increasing the age of eligibility for NZS is likely to result in an increase in labour force participation amongst the 65+ age group. However, there will be those unable to work beyond the age of 65 and so further consideration needs to be given to how best to manage the potential welfare implications of transitioning to a higher age of eligibility.

Recommended Action

We recommend that you:

a **discuss** the content of this report with officials before Wednesday 15 February.

b **agree** to increase the age of eligibility for NZS to 67 years starting at the rate of six months per year over a four-year transition period:

a. starting in 2037, or

b. starting in 2027

Agree/disagree.

c **agree** to:

a. provide a mechanism in legislation for increasing the age of eligibility by one year every decade starting in 2050 or,

b. review every 10 years to reflect changes in longevity starting in 2040 with consequential increases coming into effect ten years later

Agree/disagree.

d **agree** to:

a. extend the age of residency to 20 years, with at least 5 years after the age of 50 from 2027, or

b. extend the age of residency to 15 years, with at least 5 years after the age of 50 from 2027

Agree/disagree.

e **agree** to remove the non-qualifying partner option from 2022

Agree/disagree.

f **note** the following sequencing:

a. Removal of non-qualified partners in 2022

b. Extending residency requirements in 2027

c. Changes to the age of eligibility criteria, including indexation to longevity in 2037

g **note** that the Treasury and the Ministry of Social Development will undertake further analysis of linkages between these NZS policy changes to ensure that we fully understand any associated welfare implications.

h **note** that the Treasury and the Ministry of Social Development propose to undertake further work on the policy options for the provision of transitional support to those unable to work past age 65.

Peter Gardiner
Manager, Modelling and Research

Steven Joyce
Minister of Finance

Treasury Report: NZ Superannuation Policy Options

Purpose of Report

1. In January 2017, the Treasury provided you with advice on the fiscal implications of two New Zealand Superannuation (NZS) policy proposals, as follows:

    a. an increase in the age of eligibility by two years in 20 years' time (phased in over four years), and

    b. future indexation of the eligibility age to longevity improvements.

2. You have sought further advice on these NZS policy proposals plus two other policy proposals that we briefly touched on in our January 2017 advice:

    a. an increase to the length of the NZS residence criteria, and

    b. removal of the non-qualifying partner (NQP) option.

3. [3]

4. Therefore, this Treasury Report addresses the fiscal impacts of the three NZS policy proposals: increase in the NZS eligibility age (including indexation to longevity improvements), increase in the residence criteria and removal of the NQP option.

5. This modelling work has been performed by the Ministry for Social Development and the Treasury.

Increase NZS eligibility age

6. New Zealanders are living longer. Life expectancy has risen 12 years over the last 60 years and is projected to rise on average 1.3 years per decade until the end of this century.

7. New Zealanders are also working longer. Within the OECD, New Zealand has one of the highest labour force participation rates of 22.5% for people aged 65 and older and it has increased rapidly since the late 1980s.[1] We expect the labour force participation rate for people aged 65 or over to continue increasing and to reach 30% by the mid-2020s.

[1] As a comparison, Australia has a labour force participation rate of around 13% for people aged 65 or over.

8. The gross cost of NZS (in nominal terms and as a percent of GDP) is projected to rise from 5% of GDP (2017) to approximately 9% of GDP in 2070. The ageing population is also placing pressure on the health system.

9. To mitigate rising costs, we propose two policy options related to the NZS eligibility age:

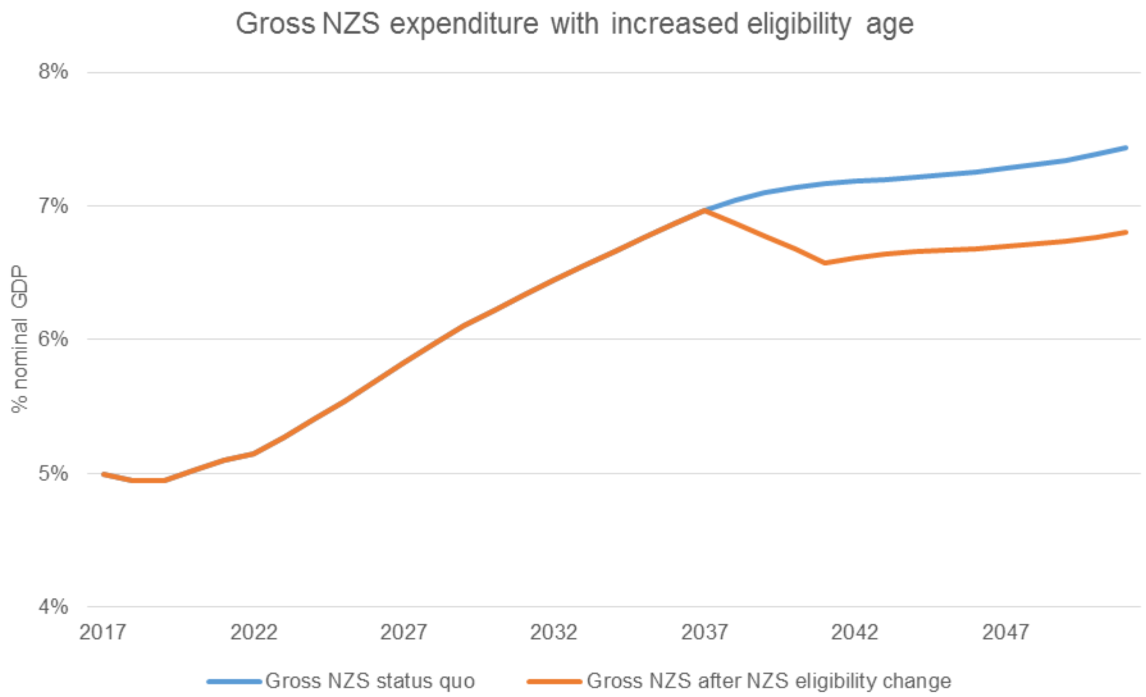
   a. increase the NZS age of eligibility by two years (to 67) in 20 years' time in six-month age increments phased in over four years, and

   b. index future age of eligibility increases to longevity improvements (for modelling purposes we have assumed a one year increase in eligibility age each decade, which closely approximates longevity improvements as projected by Statistics New Zealand).

10. This is in recognition of increased longevity and the on-going pressure this will place on the fiscal sustainability of the pension system.

11. A move to eligibility age of 67 is consistent with international trends. Eligibility age for Australia's state funded pension will gradually increase to 67 by 2023 and in the UK eligibility age will reach 68 by 2046 (or sooner).

12. The gross fiscal cost savings are approximately $4.4 billion by 2042, which is an 8.2% reduction in gross expenditure and 108,000 fewer NZS recipients.



13. If the flow on impact on other benefit categories is accounted for (i.e. movement off NZS to Jobseeker Support (JS)/Supported Living Payment (SLP) for some), then the fiscal savings associated with an increase to the eligibility age are projected to be lower. For example, in 2042 we estimate a combined additional cost of JS and SLP of $511 million, which means that the *net* effect of increasing the age of eligibility would be approximately $3.89 billion of savings (before tax).

14. Treasury recommends that you consider implementing the change in eligibility sooner. For example, implementing this change in 2027 will provide an additional $36 billion in fiscal savings. This is consistent with previous Treasury advice.

15. There are several options to consider for indexing to longevity;

    a. either further increase by one year every ten years, starting in 2050

    b. or review every ten years in light of changing projections of longevity, starting in 2040, with any consequent increase coming into effect ten years later

    c. or include a formula in legislation that automatically triggers an increase in the age of eligibility based on future changes in longevity.

16. With a 2017 announcement and a 20-year lead-in period before the age of eligibility for NZS begins to rise in 2037, there is little justification for a transitional benefit for those approaching the age of 65. Having said this, there are people who are unable to work beyond 65 and who will be required to wait longer to receive NZS and who have poor prospects for their older years. These people will also be disproportionately affected as a result of having to wait longer to receive NZS. There are options for transitional support to be provided to this group. Further analysis of transitional options is required.

Extending residency to 15 or 20 years (with 5 years after age 50)

17. Another possible change to NZS is to increase its residency requirements. Any increase implies a longer contribution to New Zealand to be eligible to receive NZS.

18. You have sought advice on the fiscal impact of increasing the length of residence required for NZS from 10 years (currently) to 15 years and 20 years (with at least five-years after age 50).

19. We have assumed that these increased residency requirements take effect in 10-years' time (i.e. from 1 July 2027).

20. We have assumed that existing recipients of NZS are grandparented. No person who met the residence criteria before the increase in the residency requirement and was granted NZS will subsequently lose their NZS if they do not meet the increased residency requirement.

21. There are no transitional arrangements (i.e. those migrants already in New Zealand who are not of NZS age would not be affected). The increased residential criteria will apply to all new applicants from the date of introduction, which is 1 July 2027.

22. The fiscal modelling assumes that 30% and 35% of the people who do not qualify for NZS, because of the increased residence period, would receive another social security benefit – Jobseeker Support (JS) or Supported Living Payment (SLP) for the 15-year and 20-year residency scenarios, respectively. There may also be increased take-up of supplementary assistance from those who have a lower income.

23. Migrants from countries with which New Zealand has Social Security Agreements would not be affected by an increase in the residence requirement (i.e. migrants from the UK, Australia and seven other countries).

24. The residence requirement operates in tandem with the direct deduction policy. The direct deduction is a way of taking account of periods of time a person has spent overseas and it saves approximately $350 million per annum.

25. Finally, this modelling assesses the impact of the residency policy options in isolation. In other words, we *have not* included the cumulative effects of increased residency requirements plus an increase in NZS eligibility age in this modelling.

26. The fiscal savings associated with increasing the residency requirement to 15 or 20-years (including five-years after age 50) for the first year that the policy is implemented, along with the first year in each decade until 2050, are set out in the table below:

Estimated reduction in gross NZS expenditure due to extending the residency requirement ($ & %)

Annual savings	2028 (yr. 1)	2030	2040	2050
Introduce 15-year residency requirement				
Nominal $ reduction (millions)	(10.84)	(27.65)	(47.88)	(67.13)
% reduction (of gross NZS expenditure)	(0.04)	(0.10)	(0.10)	(0.09)
Introduce 20-year residency requirement				
Nominal $ reduction (millions)	(32.35)	(92.82)	(260.00)	(354.30)
% reduction (of gross NZS expenditure)	(0.13)	(0.32)	(0.53)	(0.47)

Savings are represented as values in brackets.

27. **Increase residency requirement to 15 years:** In 2050 it is estimated that the number of NZS recipients will reduce by around 1,251. The number of recipients of JS/SLP will increase by around 751.

28. **Increase residency requirement to 20 years:** By 2050 it is estimated that the number of NZS recipients will reduce by around 6,604. The number of recipients of JS/SLP will increase by around 3,556.

29. If the flow-on impact on other benefit categories is accounted for (i.e. movement of some NZS recipients to JS/SLP), then the fiscal savings associated with increasing the residency requirements are projected to be lower. This net effect is set out in the table below:

Estimated *overall* gross savings (net of gross JS/SLP increase) of extending the residency requirement ($ & %)

Annual savings	2028 (yr. 1)	2030	2040	2050
Introduce 15-year residency requirement				
Nominal overall $ reduction (millions)	(6.93)	(17.97)	(33.42)	(49.67)
% reduction (as a % of gross NZS expenditure)	(0.03)	(0.06)	(0.07)	(0.07)
Introduce 20-year residency requirement				
Nominal $ reduction (millions)	(21.87)	(63.64)	(189.57)	(271.60)
% reduction (as a % of gross NZS expenditure)	(0.09)	(0.22)	(0.38)	(0.36)

Savings are represented as values in brackets.

30. In relation to facing long-term fiscal challenges, the savings from increasing the residency requirement to 20 years would be more significant than an increase to 15 years, although not substantial in relation to the total NZS spend.

Removal of non-qualifying partner option

31. A third option to mitigate the future costs of NZS is to remove the non-qualifying partner (NQP) option.

32. Currently, individuals that do not qualify for NZS are able to receive a NQP rate in situations where their partner qualifies. A NQP is a partner who is under the age of 65 or aged 65 or over and who does not meet the residency criteria. If a NQP is included, the couple's NZS becomes subject to an income test, taking into account the income of both partners. The operation of the income test means that it is only advantageous for relatively low income households to include a NQP.[2] Where eligible, a couple with a NQP included receive slightly less NZS than a couple who both qualify.[3]

33. We consider that there is a strong case for removing the NQP option, including:

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[2] Joint income of $27,519 gross or more (excluding NZS) means that it is disadvantageous to include a NQP.

[3] The difference is currently $29.34 per week (after tax).

a. The NQP option is at odds with the underlying message of welfare reform and the rest of the NZS settings. Under welfare reform, people, where able, are expected to be in paid work up until the age of eligibility for NZS. NZS settings should do the least possible harm to incentives to work, save and invest.

b. The removal of the NQP option will ensure a fair treatment of people who are not eligible for NZS. Like anyone else, if they are unable to support themselves, they would be able to apply for a social security benefit.

34. We propose a lead-in time to allow for people to plan for private retirement arrangements and for most of the current NQPs to become eligible for NZS in their own right (i.e. 60% are currently aged 60 to 65 years). Specifically, we assume a lead-in time of five years (i.e. the removal of NQP occurs from 1 July 2022).

35. We also propose that all existing NQPs (up to 1 July 2022) are fully grandparented (i.e. no person who met the NQP criteria before the removal of the option loses their NZS after the change is implemented).

36. We assume that, consistent with the residency requirements modelling, 30% of the people who do not qualify for NZS because of the removal of the NQP option would receive another social security benefit (JS or SLP).

37. The timing of this policy change compared to the residency policy change (5 years prior to the residency change) means that there may be a jump in take-up prior to the policy change coming into effect due to people who will not meet the future residency requirements taking this up. We have assumed this additional take-up to be relatively small.

38. Finally, the modelling in this section assesses the fiscal impact of removing the NQP in isolation. In other words, we *have not* included the cumulative effects of a removal of NQP plus an increase in NZS eligibility age or residency requirements in this modelling.

39. The fiscal savings associated with removing the NQP option for the first year that the policy is implemented, along with the first year in each decade until 2050, are set out in the table below:

Estimated reduction in gross NZS expenditure due to removal of NQP option ($ & %)

Annual savings	**2023 (yr. 1)**	**2030**	**2040**	**2050**
Remove NQP option				
Nominal $ reduction (millions)	(23.02)	(329.16)	(666.49)	(1,039)
% reduction (of gross NZS expenditure)	(0.13)	(1.14)	(1.35)	(1.37)

Savings are represented as values in brackets.

40. By 2050 it is estimated that the number of NZS recipients will reduce by around 24,347. The number of recipients of JS/SLP will increase by around 18,268.

41. If the flow-on impact on other benefit categories is accounted for (i.e. movement of former NZS recipients to JS/SLP), then the fiscal savings associated with removing the NQP option are projected to be lower. This is set out in the table below:

Estimated *overall* gross savings (net of gross JS/SLP increase) of removal of NQP option ($ & %)

	2023 (yr. 1)	2030	2040	2050
Remove NQP option				
Nominal overall $ reduction (millions)	(16.75)	(247.37)	(522.78)	(846.00)
Saving as a % of gross NZS expenditure	(0.09)	(0.86)	(1.06)	(1.11)

Savings are represented as values in brackets.

Linkages between the policy options

42. We have considered each of the policy parameters above in isolation. There are, however, linkages between the various policy settings. For example, if the age of eligibility is increased, one of the flow-on effects is likely to be an increase in the number of NQPs and increases to both the age of eligibility and the residence requirement would drive flow-on effects to social security benefits.

Timing of these policy changes

43. In summary, we consider that addressing the fiscal sustainability and fairness of NZS, while maintaining the adequacy of income for older New Zealanders and appropriate incentives to work, save and invest, points towards the following changes to NZS:

- remove the option to include a non-qualified partner in a qualifying partner's NZS from 1 July 2022 and grandparent existing recipients,
- consider an increase to the residency requirement (to 15 or 20 years with five-years over age 50) to commence from 1 July 2027 with full grandparenting of existing recipients,
- increase the age of eligibility to 67 years, to commence in 2037 and to reach 67 by 2040, and
- thereafter, link the age of eligibility to future improvements in longevity (we have assumed one-year increase per decade).

Risks

44. The removal of the NQP option could disadvantage some groups of NQPs for whom employment is not an option. This is because other forms of state assistance to which

they would be entitled are less generous than the NQP rate of NZS.[4] The provision of social security benefits will, however, ensure that no one's income falls below what is considered to be the ordinary social safety net before they qualified for NZS.

45. Skilled older workers will play an increasing role in increasing productivity which in itself will assist in meeting the challenges of the ageing population. In this context, we need to consider the wider economic impact of any changes to NZS. For example, increasing the age of eligibility for NZS is likely to result in an increase in labour force participation amongst the 65 and older age group, but as highlighted below, there will be a group for whom continuation in paid work is not an option.

46. An increase in the eligibility age for NZS to 67 years will have a disproportionate impact on those who work in physically demanding industries and who are unable to work beyond the age of 65. There will be groups within the population approaching the age of eligibility for NZS who have poor prospects for their older years. These people will also be disproportionately affected as a result of having to wait longer to receive NZS.

Next Steps

47. Consideration could be given to transitional support for people unable to work beyond the age of 65. As the current social security system will not cover all of those people who will be required to wait longer to receive NZS, consideration could be given to a means-tested Transitional Benefit – without any work test for vulnerable people aged 65 to 67 years. The parameters for such a benefit would need to be worked through. For example, consideration would need to be given to:

    a. the design of the means test (should this be equivalent to the Supported Living Payment or a more generous income test)?

    b. whether to have a medical test requirement?

    c. what the residency requirement would be (equivalent to NZS or a shorter period)?

    d. what the maximum rate of payment would be (equivalent to the Supported Living Payment or to NZS)?

[4] A difference of approximately $35 per week.