An annuity, based on the private incomes of old, would help the young stretch their KiwiSaver into old age.


What really matters for most people contemplating a healthy and happy retirement is good health and financial security.

A few fortunate New Zealanders retire without a care in the world, and these Kiwis tend to be drawing pensions for life or with substantial investments. With regular income arriving each month to add to the basic NZ Superannuation, are able to engage in ways they see fit, continuing to work in a paid job, supporting the tourist industry, looking after grandchildren and older relatives, indulging in other productive unpaid activities, and contributing to the creative and cultural environment.

Today, one-in-ten retired people have an additional income stream from an occupational pension. There are around 22,000 company scheme pensions and 46,000 pensions paid to retired civil servants. While many of these private pensions are small, they can make a real difference.

However, by the time today’s 48 year-old arrives at retirement, the number getting any private pension at all will be very few, let alone pensions that are inflation-protected. Mainly, the few large pensions left will be paid to civil servants in the old Government Superannuation Fund that was closed to new entrants in 1991.

Many of our politicians will have such pensions, or be otherwise protected and may not appreciate how life is for others.

The beauty of such an income stream, otherwise known as an annuity, is that it goes on for as long as the person lives. It is helpful for those who need expensive long-term care at the end of life and, while there is a transfer from those who die young to those who live the longest, this kind of sharing is needed to reduce the pressure of paying for the old away from the young.

In the past, employer pensions were either paid by the firm, or employees were required to use their accumulated saving from their superannuation scheme to buy an annuity from an insurance company. These annuities were fixed in dollar terms and lost value over time.

Those in the Government Superannuation Fund could take up to a quarter of their superannuation as a lump sum, with the rest as an inflation-adjusted annuity.

While capital had to be given up to buy an income stream, it was better than worrying about the future, scrimping and saving, and then maybe dying early, leaving unintended bequests.

Those days have long gone for the X-generation. What will today’s 48 year-old do with her KiwiSaver savings when she reaches retirement in 2031? She has a good chance of living another 35 years. How will she make her nest egg last?
There are real problems with expecting the private sector to come up with credible annuity products. Not least is the almost total unfamiliarity of New Zealanders with the concept of annuities, and a deep suspicion of the financial sector.

Other countries have a greater tradition of turning retirement savings into income for life. Nevertheless, all is not well in these countries. A recent UK report was very critical of the kind of annuities that people have been forced to buy with their tax-subsidised retirement savings. This year, in a surprise announcement, the UK budget did away with the legal requirement for people to turn their retirement savings into an annuity.

The problem in the UK is that many people have been stuck with a really bad deal in a poorly performing annuities market. But commentators are saying that the baby is being thrown out with the bathwater.

It is time we listened, learned and debated these issues.

With KiwiSaver, New Zealand has done two things right that put us potentially well ahead. First, the individual is in control of his or her KiwiSaver saving, not the employer. When jobs change, KiwiSaver goes with the employee, who can then keep the same provider. In other countries people can have several pots of retirement savings with different employers.

We have also cleared the way to have a much fairer system. In the UK, very badly designed expensive tax incentives of the kind New Zealand got rid of in the late 1980s, ensure that the better off you are, the bigger the tax subsidy in your pension.

Instead of subsidising the build-up of funds, we could have a well-designed subsidy for those who turn their savings pots into a modest additional income stream. Let’s call this annuity ‘KiwiSpend’. It might be offered by KiwiSaver providers, but would have certain characteristics. It could be inflation-proofed, with low fees, the same capital cost for women and men, inclusive of long-term care insurance and regulated by the Financial Markets Authority (FMA).

KiwiSpend would need to be carefully underwritten by the State with subsidies to make it attractive enough to achieve the social objectives intended. It won’t make the costs of the coming tsunami of the old any less, but it could provide more security for the X generation, and begin to share the costs more fairly.

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