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"Learn lessons for a BritSaver from KiwiSaver" says Pensions Policy Institute

The PPI today launches a new report *NPSS policy and design choices*.

The Pensions Commission proposed boosting private retirement income by auto-enrolling employees into a new National Pensions Savings Scheme (NPSS).

The PPI has researched in detail the only other plan for a national auto-enrolment scheme: the KiwiSaver in New Zealand. This paper explores the relevant lessons from KiwiSaver for the NPSS and concludes that:

- Inadequate state pension reform would threaten the success of the NPSS.
- A 'BritSaver' learning the lessons from KiwiSaver could be a more appealing and less risky proposal than the NPSS.

"Auto-enrolment into a low-cost savings scheme is widely supported", said Alison O'Connell, Director of the PPI. "But it is untested on a national scale, so we should tread carefully".

"The only other country to be planning such a scheme is New Zealand which has a high universal state pension and only around 5% of pensioners means-tested for their basic income. That raises alarm bells for the NPSS in the UK as, even after the Pensions Commission's proposals have worked through, eligibility for Pension Credit would remain at around 45% of pensioners".

"This adds to the need for Government to consider bolder state pension reform that would reduce the scope of means-testing from its current level – not just contain its future growth. Other feasible models of state pension reform in the UK could reduce eligibility for Pension Credit to around 10%, which would help take the pressure off the NPSS."

"KiwiSaver has some product design and implementation features that may be welcomed here for a more flexible 'BritSaver' than the NPSS. For example, annuitisation is not compulsory in KiwiSaver. It comes with support for buying a first home and a package of help for making financial decisions. It is promoted in language about <u>helping</u> people to build up discretionary savings, not about 'we all <u>have</u> to save for a pension'.

"KiwiSaver is being introduced using existing processes rather than a big new system build. It is lower risk than the all-new NPSS".

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A summary of conclusions from the project follows on the next page, together with a comparison of the NPSS and KiwiSaver.
The report can be downloaded from: www.pensionspolicyinstitute.org.uk

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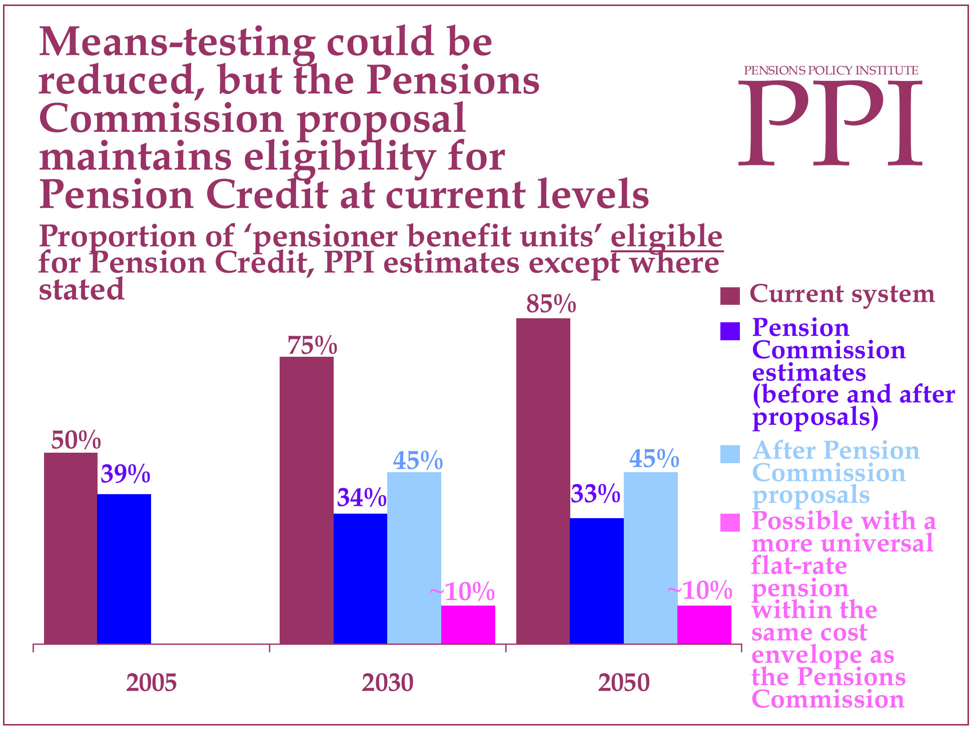
Notes for editors

Means-testing can never be abolished, but the extent of means-testing for basic income through Pension Credit is a concern for pension policy makers. Means-testing increases uncertainty about both the level of pension income individuals can expect to receive from the state and what value they will get from any saving. The PPI believes that the Pensions Commission underestimated the extent of Pension Credit that would remain after the Commission's proposals for reform (see chart). The PPI has worked on alternative state pension reform proposals and considers it possible to design affordable models which reduce the level of means-testing further. This would make introducing an NPSS or similar more likely to succeed. With a better state pension, saving in the NPSS would not have to overcome the means-testing trap before adding to retirement income.



The PPI is an independent research organisation, focused on pension provision. Its aim is to improve information and understanding about pensions (state and private) through research and analysis, discussion and publication. It does not lobby for any particular issue or reform solution but works to make the pension policy debate better informed.

NPSS policy and design choices: Summary of conclusions

Although some countries have introduced compulsory private pension savings, so far only one country – New Zealand – plans a national auto-enrolment scheme: KiwiSaver. Compared to KiwiSaver, the Pensions Commission's proposed NPSS auto-enrolment scheme for the UK has a more prescriptive design and requires greater operational change.

Despite being planned for the only two countries considering national auto-enrolment, the NPSS and KiwiSaver have very different policy aims:

- The Pensions Commission's objective is for the NPSS to make up for remaining inadequacies in the state pension (and continuing high levels of means-testing) and take retirement income above adequacy. The NPSS is a new design for a low cost pension product.
- The New Zealand Government has developed KiwiSaver to help people get into the habit of saving because saving is seen as good for improving security and choice. KiwiSaver is designed around existing products and infrastructure where possible.

The Pensions Commission believes *it is a reasonable aim of public policy to seek to ensure that the median earner achieves an income replacement rate of at least 45%*. This defines a target and asserts that the target should be reached by a specific combination of state pension and state-sponsored saving. It puts Government 'on the hook' for getting people to a standard of living in retirement that is higher than adequate.

This sets a very high standard for the success of the NPSS. If instead state pension reform guaranteed adequacy with less means-testing than now, the aim of the NPSS could be more like that of KiwiSaver: to encourage discretionary savings. This could stand more chance of success:

- A general savings product could be more appealing than a prescriptive pension and more effective at promoting personal responsibility.
- Implementation and liability risks for the Government and employers would be lower, while the investment risk to individuals would be less critical to their overall retirement income.

If this purpose for the NPSS is preferred (and it is in line with many pension experts' views) then the policy priority would be to push for as high a level of guaranteed adequacy in the UK's state pension as possible.

However state pensions are reformed, there are some product design and implementation lessons from KiwiSaver for a 'BritSaver':

- Ways to increase appeal as a discretionary savings product should be investigated, including flexible withdrawal options, the appropriate form of savings incentives and help in making financial decisions.
- Ways to minimise the risks of implementation should be considered, such as working with existing providers and processes, phasing in and aiming to lower cost without making very low cost the focus.

Basic description of the NPSS and KiwiSaver

	NPSS	KiwiSaver
Timing	Proposed introduction 2010	Due to launch April 2007
Target population	All employees from age 21 earning over a threshold	All employees and self-employed
Nature of compulsion	Employees auto-enrolled. Right to opt out. Others can opt in. Employer contributions compulsory.	Employees auto-enrolled. Right to opt out. Others can opt in. Employer contributions not required.
Number of members	Expected 7m members (in NPSS or alternative)	Expected roughly 680,000 after 7 years
Minimum contribution level	As % of gross earnings between £4,888 and £32,760: 5% by employees (including 1% from tax relief), 3% by employers	4% of gross salary or wages paid by employee
Incentives	Tax relief as above. Tax-free lump sum (as existing pension provision).	NZ$1,000 (£365) on joining. Up to NZ$5,000 towards first home purchase. Government make a contribution towards members' account fees.
Benefit restrictions	Annuity or drawdown equivalent between ages 55 and 75 (as existing pension provision)	Partial withdrawal available after 3 years membership for deposit on first home. Full amount available after age 65 as a lump sum.
Contribution collection system	Need new system as current PAYE system is annual	Can use existing monthly PAYE system
Approach to industry	Change cost base and nature of operation	Work with existing products and providers
Investment choice	Core of 6-10 funds; one default fund controlled by NPSS	Providers apply to be approved for KiwiSaver. A limited number of default providers selected by competitive tender.
Guidance on opt-out and investment choices	Not covered in Pensions Commission report	Existing *Sorted* website gives generic financial information. Government to run education campaign explaining KiwiSaver. Providers able to give 'advice'.