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**A commentary from the Retirement Policy and Research Centre**

# Saving KiwiSaver: why contributions matter more than fees.

*PensionCommentary 2021-1*[1] *by guest contributor David Boyle.*

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The RPRC is pleased to publish this PensionCommentary on KiwiSaver from David Boyle.[2] There has been a heightened public awareness of the effects of fees on final outcomes for KiwiSavers but as David Boyle points out, an even more pressing issue is the high number of KiwiSaver members who are not contributing at all or too little to gain the maximum government subsidy. The situation is likely to be worse in the COVID pandemic with negative gender, ethnic and age implications. The RPRC calls for better and more in depth statistics to elucidate trends in KiwiSaver contributions, and a review of current policy settings around total remuneration practices and employer contribution,[3] the self-employed and those engaged in socially vital unpaid care work.[4]

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KiwiSaver fees have hogged the headlines more than ever over the last year, sparked first by the Financial Markets Authority (FMA) 'value for money' crusade in 2020 before culminating in the Ministry of Business, Innovation and Employment (MBIE) default scheme announcement last month.

The regulator, of course, has a duty to monitor fees under its mandate to oversee KiwiSaver (and the broader licensed funds market), while the government itself has had a specific interest to see management fees come down, especially given the allocation of free new customers to the default providers. The writing was on the wall when MBIE's tender document for default providers came out last year with a 60% weighting to fees - a point not lost on a number of newly appointed providers. The key, though, in a lower-fee world, is whether the default providers can still adequately service their new members, but more on this later.

[1] PensionCommentaries are opinion pieces published as contributions to public debate, and do not necessarily reflect the view of the RPRC.
[2] First published in Investmentnews NZ 11.6.2021. David Boyle is Head of Sales and Marketing at Mint Asset Management Limited. The commentary provides information and does not purport to give investment advice.
[3] See RPRC PensionBriefing 2020-1: Would Total Remuneration improve KiwiSaver fairness? Total Remuneration (TR) is the total value of an employee's annual compensation package and includes both basic pay or salary and the financial and non-financial benefits, including KiwiSaver contributions. Some regard this approach as equitable, while others argue that the employer's KiwiSaver contribution should be an addition to gross wages. This PensionBriefing investigates the equity of three possible options.
[4] See RPRC PensionBriefing 2021-1: Women and the pensions gap based on the RPRC 2020 Working Paper, *Women and Retirement in a post COVID-19 world*, by M.Claire Dale and Susan St John, comparing gender pay gaps, gender pension gaps and COVID-19 penalties in New Zealand, Australia and Ireland.

The just-completed Default Review addressed both the unsuitability of the default mix and squeezed the sticker price for managing a balanced KiwiSaver portfolio to between 0.2% and 0.4% – all without fixed annual member fees. If we compare this with our Australian neighbours who have over A$3 trillion under management and charging on average 0.7% in management fees, you could say it was an incredible feat.

Announcing the new default scheme terms, Commerce Minister David Clark said: "We're sending a clear message to KiwiSaver members that the government believes they deserve much better bang for their buck."

Now with a better default mix and the fee argument settled, at least for the moment, the time has come to focus on far more systematic problems with KiwiSaver – most notably, the high proportion of non-contributing (and under-contributing) members. We also need to ask whether KiwiSaver schemes have the resources to properly assist members during market volatility, in particular, preventing unwise switching to conservative options amid market downturns as occurred post the COVID-19 crash in 2020.

While the government has achieved a reduction of default fund fees down to bargain basement levels, KiwiSaver members deserve more attention on other ways to maximise their savings over the long term. Costs are just one side of the equation, with asset allocation, investment returns, advice and contribution behaviours all likely to be weightier factors in this calculation.

The FMA 2020 KiwiSaver report categorises about 1.2 million members as non-contributors, about 40% of the total 3 million+ New Zealanders signed up to a scheme.

During my stint at the Commission for Financial Capability, Te Ara Ahunga Ora (CFFC), research from the Inland Revenue Department (IRD) found about half of all KiwiSaver members had not heard of the member tax credit (MTC). If 1.5 million KiwiSaver members are not aware of the prospect of $521 in 'free money' each year for making the minimal $1,040 contribution, then something is wrong with the marketing machine.

About 1.1 million members missed out on the full MTC including about 580,000 who received no government top-up at all. I suspect the MTC dial has not moved very far since. There has been no detailed analysis of KiwiSaver data since the 2015 IRD KiwiSaver evaluation,[5] but five years on with 1.2 million classified as non-contributing and a further unknown number contributing less than required for the full government contribution, it is safe to assume that roughly a third of all KiwiSaver members are contributing less than $20 a week to save for their retirement.

Government, regulators and industry have long been aware of the contribution catastrophe in KiwiSaver and all have attempted in one way or another to bridge the gap. Clearly, all have failed so far. With fees now dealt to, perhaps we need to flesh out a better understanding of why New Zealanders are not contributing to what is actually a pretty cheap, effective retirement saving scheme for most New Zealanders.

With little in-depth research to call on, we can only make assumptions about what is keeping Kiwis from making full use of KiwiSaver, however, there are some obvious contenders including:

- unemployment;
- self-employment;
- child-rearing;

[5] Inland Revenue (2015). KiwiSaver evaluation: Final summary report. A joint agency evaluation 2007–2014.

- caregivers in unpaid work
- those on contribution suspensions or using hardship withdrawals due to genuine affordability issues.

By my reckoning, though, the above factors don't account for the full 1 million plus KiwiSaver members on low, or nil, contribution rates.

I suspect that a kink in New Zealand's employment law could be another, over-looked reason behind the missing KiwiSaver contributions.

Under the legislation, the intent was for employer contributions to be in addition to employees' salary or wages. However, due to significant lobbying at the time, the law was amended to allow employers to negotiate deals in 'good faith' with employees to include employer KiwiSaver contribution calculations as part of a total remuneration (TR) package.

Employees opting for a TR approach can choose to contribute the allocated extra amount to KiwiSaver or use it for other purposes. On paper, the TR method offers great flexibility while maintaining pay equity between all employees whether they contribute to KiwiSaver or not.

More importantly, many New Zealanders now work on a contract basis, which exempts employers from including KiwiSaver as part of the bargain, although a savvy contractor might negotiate employer contributions as part of an overall pay rate. Anecdotally, via my Radio Live show 'Your Money', in a number of extreme cases a few years back, some employers just didn't mention KiwiSaver at all.

Most New Zealand firms are no doubt responsible employers who see KiwiSaver as part of an overall employee well-being program and comply with their obligations.

Until there is detailed information available on why so many enrolled members are not contributing to KiwiSaver, we can only guess at their reasons.

After the government announcement in May 2021, Minister David Clark said that, on average, an 18 year-old entering a default fund today under the lower fees regime would save about $3,900 by age 65, which equates to about $80 a year. Although, in inflation-adjusted terms the real fee saving amounted to around $2,400 over a 47-year KiwiSaver-contributing lifetime – or $50 a year.

The government and regulator have put a lot of effort into reducing KiwiSaver fees, which obviously will help to some extent. However, in the broader scheme of things the fee reduction is just a drop in the bucket compared to the long-term compounding effect of full employee and employer contributions. At the very least, all Kiwis need to be contributing at a level to receive the MTC, which collectively adds $1,500 plus each year to member accounts (excluding the impact of investment returns).

After completing its fee investigation, perhaps government – with a little help from the industry – can now do more to find out why such a large percentage of KiwiSaver members are not making the most of contributions.

With better understanding of this problem, providers could find more effective ways to communicate with the non-contributing population and, ultimately, improve the retirement prospects for many more New Zealanders.

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