Excerpts from "KiwiSaver: How to make it work for you"

Part One: What is KiwiSaver?

Let's go!

KiwiSaver is a voluntary scheme under which New Zealanders can save money for their retirement. While people who start new jobs are automatically enrolled in KiwiSaver, nobody has to stay in if they don't want to. But most people *should* stay. KiwiSaver is so attractive that, arguably, all of us should sign up ourselves and perhaps also our kids – even if we have to add to the mortgage money to do it.

The scheme includes a number of attractive incentives, such as a $1,000 kick-start and a tax credit of up to $1,040 a year. Many members will also receive employer contributions, and some will get a $5,000 subsidy towards buying a first home. Many people refer to KiwiSaver as 'workplace savings', but every New Zealander aged 0 to 64, employed or not, can join. Employees have the advantage of receiving contributions from the boss. On the other hand, non-employees have more flexibility.

While KiwiSaver is a great way for individuals to save, it's not so clear that it is good for the country as a whole. Any savings scheme with incentives distorts decisions. Without the incentives, many people who join KiwiSaver might have invested in another way – such as in their own business or in tertiary education – which might well have been better for them and for the country's growth.

Also, the scheme will be costly for many businesses a few years down the track, and immediately burden them with extra administration. Many employees will suffer from the effects of this, with pay rises likely to be lower. (The best way to make up for that will be to join KiwiSaver.) But I'm not so convinced about some other criticisms of KiwiSaver, such as:

- "Lower income people can't afford to join."

Not so. People who aren't employees can sign up and contribute as little as, say, a one-off payment of $10. While employees basically have to contribute 4% of their income for at least a year, there are ways some people can reduce the impact of that.

- "There are no government guarantees on investment returns."

No investments come with government guarantees because that wouldn't work well. KiwiSaver providers and investors wouldn't bother to take much care if a bailout was guaranteed, leading to more reckless investing. And why should taxpayer money support such recklessness? If you can't cope with volatile investment returns, there are plenty of conservative KiwiSaver options.

- "KiwiSaver is just a gift to providers who will charge too-high fees and make lots of money."

Many providers will probably do really well out of KiwiSaver. But some providers are planning to charge low fees. If we seek out the schemes that charge low fees – which is a good idea, everything else being equal – competition should help keep the providers in line. There is one concern here, though, and that is that not all fees are disclosed in an obvious way. Let's all pressure the government to change the rules about fee transparency.

I've even heard people say they won't join KiwiSaver because they don't support the Labour Government. That's cutting off your nose to spite your face. Whether you like it or not, the government has directed a large chunk of taxpayer money towards KiwiSaver. You might as well claim your share of it.

There is, of course, one big downside to KiwiSaver – or at least it's a downside for most people – and that is that your money is usually tied up until you reach NZ Superannuation age, currently 65. Because of this, the best strategy for many – maximising the incentives but tying up as little money as possible – will be as follows:

- Employees should contribute 4%, rather than 8%, of their pay – unless they need to pay 8% to get the maximum $1,040 tax credit.
- The self-employed and adults not in employment should contribute $1,040 a year.
- Children should sign up and contribute minimally.

For many people, of course, it's a great idea to save more than those amounts. And KiwiSaver will get people into a savings habit. But you might want to save the extra in another savings vehicle with more flexible withdrawal rules – unless you're one of those who *prefers* to tie up your money so you're not tempted to spend it.

Note: Some of the details about KiwiSaver – particularly the tax credits and compulsory employer contributions – have not been made law yet, and will pass through the select committee process. So expect some changes.

Revved up without the risk

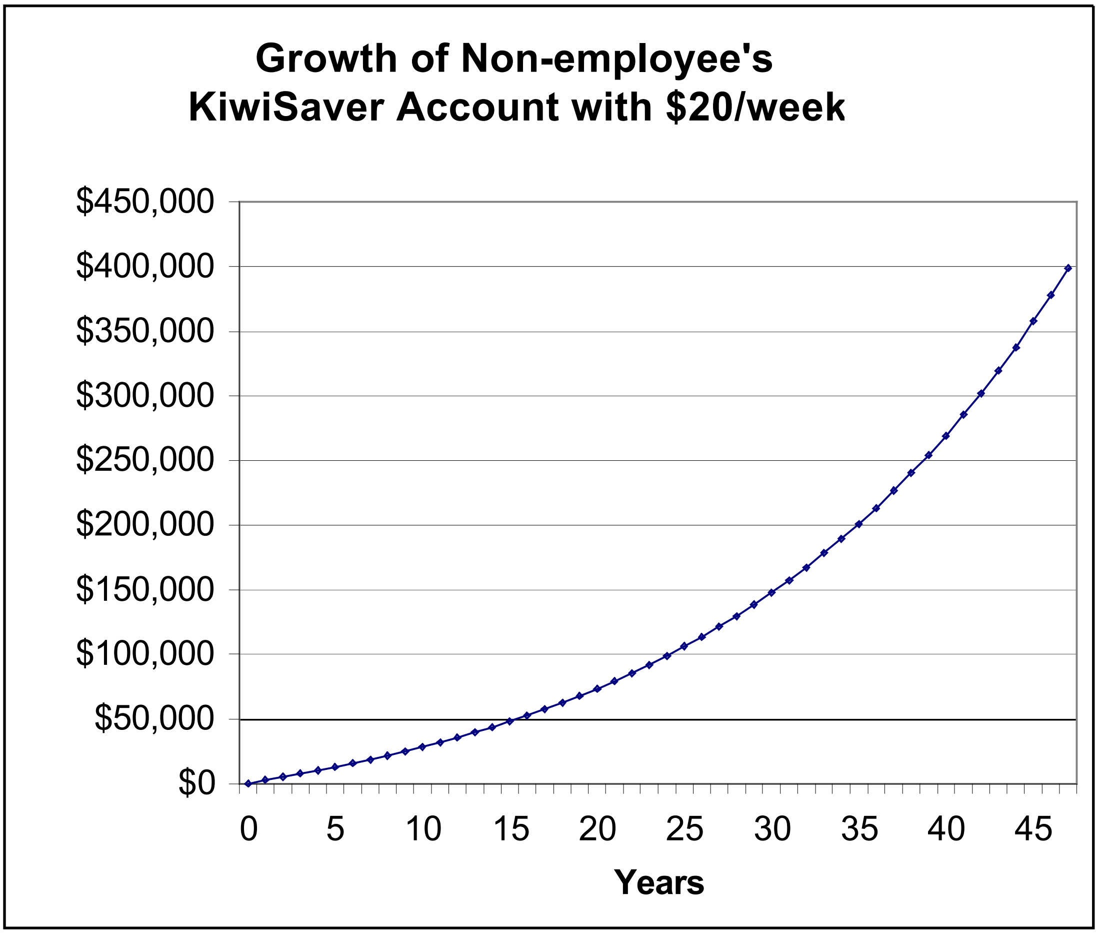
Usually, in investment, the higher your return, the more risk you have to take. But with KiwiSaver, members' returns are revved up by the $1,000 kick-start, tax credits and often also employer contributions.

Many people will end up with more than twice as much money going into their accounts as in a normal savings plan. Some, on lower incomes, will end up with three times as much. That means their total savings at retirement will be twice or three times as big. And yet there is no extra risk. It's powerful stuff.

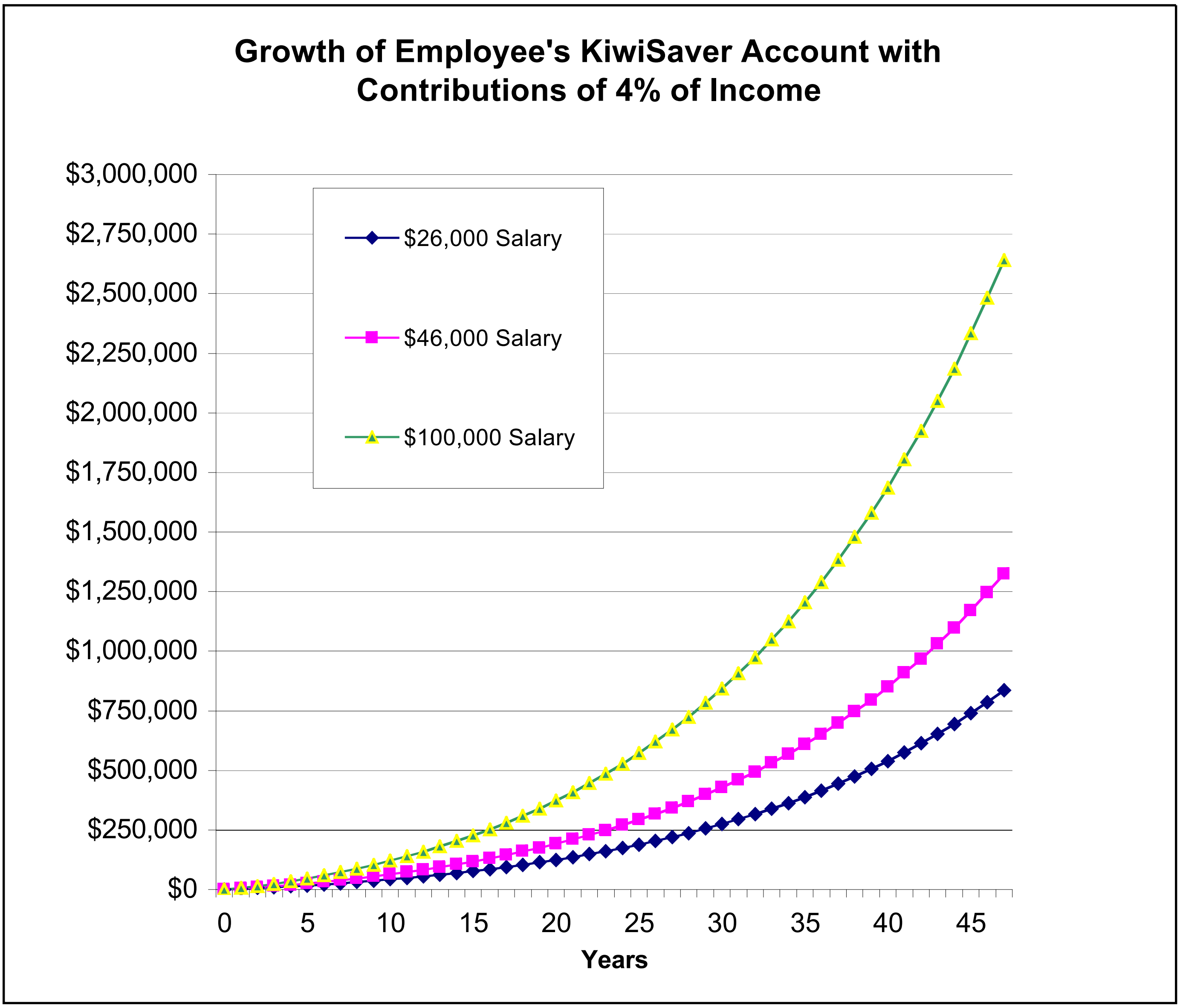
Move fast – especially if you are 64

Practically every New Zealand resident is eligible to join KiwiSaver up until their 65th birthday. (See 'Who can join KiwiSaver'.) If you are approaching 65, I suggest you sign up while the going is good. You can then belong for five years, enjoying the kick-start, tax credits and, in some cases, employer contributions. Even over a relatively short period, those incentives will boost your savings considerably.

Others, of whatever age, should also sign up for KiwiSaver sooner rather than later. That way, you'll receive more tax credits – and employer contributions if they apply – over your lifetime. Also, nobody knows what the politicians will get up to. Get in while the going is good.



The $1,000 kick-start and tax credit of $1,040 a year considerably boost $20 per week savings growing at 5% a year. If you join KiwiSaver at 18 and save until you are 65 (for 47 years) you will have about $400,000 in your account.



We assume you join KiwiSaver in September 2007, so employer contributions start at zero and grow to 4% of income from April 2011. Those contributions, plus the $1,000 kick-start and $1,040 per year tax credit add greatly to employee 4% contributions. The return is 5% a year. $26,000 a year is the income level at which the tax credit stops growing. $46,000 is the average pay for a full-time worker. Income grows by 3% a year.

Note: The 5% return in both graphs is what might be conservatively expected on a long-term investment in a KiwiSaver fund, after fees and taxes.

To give an idea of the effect of 2% inflation on the numbers:
If you have saved $200,000 over 20 years, that will buy roughly what $135,000 buys today.
If you have saved $500,000 over 30 years, that will buy roughly what $275,000 buys today.
If you have saved $1 million over 47 years, that will buy roughly what $400,000 buys today.
For other numbers, adjust proportionately, e.g. if you will have saved half of $200,000 over 20 years, that will buy items worth half of $135,000 today.

We have assumed the kick-start and tax credit are not adjusted for inflation, as the government has not indicated that they will be. However, they should be – and if they are, your total will be considerably higher.

Q: As a single woman of 60 living in rented accommodation, is there any point in joining KiwiSaver? I find it a struggle now without having less income to live on. If I join this year, how much will I have in 5 years? My income is in the late forties.

A: Let's say your income is $48,000, and it grows by 3% a year. We'll assume you join KiwiSaver around September 1, 2007, and that you get a return of 5% a year after fees and taxes. If you are an employee and contribute 4% of your pay, you'll have more than $25,500. If you are not an employee, and you contribute $20 a week, you'll have about $13,000.

How it all works

Joining up

When you start a new job – unless you are exempt (see 'Who's excluded?' below) – your employer will give you an information pack from Inland Revenue, sign you up, and start deducting 4% from your first pay. Neither you nor your employer has any choice about your being enrolled, unless the employer has another approved work super scheme. In that case, you can join either scheme or none, whichever you like.

If you're an employee not starting a new job and you want to join KiwiSaver, ask your employer or Inland Revenue for the info pack and the forms to sign. Or you can sign up directly with a KiwiSaver scheme provider. In that case, the provider will tell Inland Revenue whether you want 4% or 8% deducted, and Inland Revenue will pass that info on to your employer.

Children, the self-employed, beneficiaries, and other adults not working will have to go directly to a provider to join up.

Q: How long can current employees take before deciding whether or not to opt in to KiwiSaver?

A: As long as you like – provided the scheme is still running. But you might want to get in fast so you can start receiving the benefits the scheme offers as soon as possible.

Generally, once you are in KiwiSaver, you are in until you reach the age that NZ Super starts, or you have been a member for five years, whichever comes later. You might join as a self-employed person, child, beneficiary or other adult out of the work force, making small contributions. If you then move into employment you will be expected to contribute at least 4% of your pay – unless you take a contributions holiday.

Q: My son's a uni student and works each Christmas holidays for about three months. Will he be automatically enrolled into the scheme and then have to opt out each year? Will he get back his contribution in time to start the new uni year? After all, it's a big struggle now without him getting 4% less.

A: Yes, he will be enrolled unless he happens to be excluded. But he should be able to easily opt out after two weeks. And while it might take a while for him to get back the 4% he has put in, it won't be a lot of money. In any case, I would think that most tertiary students would be expecting to spend a fair bit of their summer earnings later in the year. So having the money tied up for several weeks shouldn't affect them much.

Your employer isn't legally allowed to prevent you from joining KiwiSaver, or to treat you differently from other employees on the basis of who is in KiwiSaver.

Who is excluded from automatic sign-up?

The following people won't be automatically enrolled when they start a job – although they can join if they wish, or continue contributions if they are already members:

- Those employed on a contract for 28 days or less, and the contract is not later extended.
- Casual agricultural workers employed on a day-to-day basis for no more than three months.
- Election day workers.
- Private domestic workers, such as cleaners and nannies.
- People on government paid parental leave that is paid via Inland Revenue.
- People who work for a company that has an alternative 'exempt' super scheme. New employees may join the company's exempt scheme or KiwiSaver or neither, but they won't be automatically enrolled in either.
- People who receive payments subject to withholding tax, such as directors.
- Workers for employers who are taken over, provided the workers stay on the same payroll.

- People receiving weekly compensation from ACC.

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Opting out

If you have been automatically enrolled in KiwiSaver and you don't want to belong, you can opt out any time between the end of week two and the end of week eight. Get an opt-out form from Inland Revenue's KiwiSaver employee pack or www.kiwisaver.govt.nz (your employer may also have some copies), fill it out and give it to your employer or Inland Revenue.

> Q: If you are automatically enrolled and then opt out, how long will it take to get your money back? Will you get interest on that money?
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> A. Inland Revenue is hedging its bets on the timing. 'It will differ for each case, so it's difficult to quantify a prescribed timeframe,' the department says. If it is taking a ridiculous amount of time, write and tell me and I'll address it in my column.
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> On the question of interest, employers will refund any deductions they haven't yet sent to Inland Revenue, but they are not required to pay interest on that money. However, Inland Revenue says you will get interest earned on the money they hold. To simplify things, that interest will be calculated as if your total contributions each month were received by Inland Revenue on the 15th of the month. Some people will be penalised a little by this, while others will gain a little from it. It's not worth fretting about.
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> Q. If you are automatically enrolled and don't opt out within eight weeks, but then you want to stop contributions as soon as possible, when can you do that? Is it a year from when you were first enrolled?
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> A. Generally, yes, you would have to wait a year from when Inland Revenue receives your first contribution. But if you are suffering financial hardship or serious illness, or you emigrate, you could apply to stop your contributions sooner.

Contributing - employees

Employees are required to put in 4% or 8% of their total pre-tax income, including bonuses, overtime, holiday pay, redundancy pay and so on. You can change your mind, from 4% to 8% or the reverse, as often as every three months – or more often if your employer allows it.

Until 1 April 2008, those amounts can be made up of employee and employer contributions. For example, you and your boss might each put in 2%, or one of you might put in 1% and the other 3%. After 1 April 2008 you have to put in the full 4%.

> Q: They talk about me making my contributions as either 4% or 8% of gross salary. If that is taken from my gross salary then surely I am not paying tax on it? Or does it mean they work out 4% of my gross salary to contribute and whip the regular 39% out before they put it into the scheme? Or something else entirely?
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> A: Something else. All your pay will be taxed the same as it is now. Out of your after-tax income, an amount equal to 4% or 8% or your *pre-tax* income will go into your KiwiSaver account,
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> Q: I read somebody's comment on the misleading use of '4% or 8% of gross income', when in fact it could mean more like '5% or 10% of net income.' I wonder why they didn't do it this way because it is a more accurate way of describing the deduction?
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> A: It could be that people are more likely to know their gross income. It could be that the government put KiwiSaver together quickly and didn't stop to think about it. It doesn't bother me much though. I think people can get too caught up in this sort of issue. It's not as if the government is taking the money away from us, nor that the scheme is compulsory.
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> Q: What is the situation regarding a person holding down several jobs?

A: You can join KiwiSaver through any or all of the jobs you hold on July 1, 2007. After that, if you join KiwiSaver the 4% or 8% applies to all income from all new jobs – unless you are on a contributions holiday at the time. You can take contributions holidays from just some jobs if you wish, after you have been a KiwiSaver member for a year.

Q: If you had a $100,000/year job and also a part-time job paying $1,000 a year, could you just put in 4% of the lower-paying job?

A: Yes, but only if you hold the higher paying job on July 1, 2007. This is a significant point for those wanting to contribute minimally.

How much is 4%?

Weekly before-tax income	Annual before-tax income	Weekly KiwiSaver contribution	Annual KiwiSaver contribution
$50	$2,600	$2	$104
$200	$10,400	$8	$416
$500	$26,000	$20	$1,040
$1,000	$52,000	$40	$2,080
$2,000	$104,000	$80	$4,160

To calculate contributions from your pay, go to the Retirement Commission's website, www.sorted.org.nz and use the Quick KiwiSaver calculator.

Contributing - non-employees

For the self-employed, beneficiaries, and other adults out of the work force, the 4% or 8% rule doesn't apply. You go directly to a provider and negotiate how much you will contribute and how often. (Note, though, that if you get a job during the first 12 months – or after that and you are not on a current contributions holiday – you will have to contribute 4% of that income.)

If you want to put in heaps, you can do that. If you want to put in as little as possible, you could make just a single contribution of, say, $10, receive the government's $1,000 kick-start and then, after a year, go on contributions holidays until you are 65. While some providers may be unwilling to sign you up on that basis, at least some will. Shop around.

The best strategy for many will be to contribute a total of $1,040 a year, whether it's $20 weekly, $87 monthly, $1,040 annually or whatever. That way, you get the maximum tax credit, and yet don't tie up any more money than necessary until NZ Super age. If, however, you like having the money tied up, or the fee subsidy makes KiwiSaver your most attractive savings option, you will probably want to contribute more.

Contributing extra money

Q: Is 8% the absolute total amount that can be contributed i.e. 4% from employer and 4% employee or 8% from employee?

A. No. All KiwiSaver members can also make extra payments – either lump sum or regularly – into their accounts. You have to make these payments directly to your KiwiSaver provider or Inland Revenue, not via an employer. Going directly to your provider will probably be the easier way.

This money is locked in under the same rules as regular contributions.
If you do contribute extra to KiwiSaver, you won't get employer contributions, but you will get tax credits if you haven't already contributed $1,040 or more and you are over 18. If your wage or salary is less than $26,000 (which means your total contributions will be less than $1,040) and you can manage to pay more, it would be good to do one of the following:

- If you are contributing 4%, raise your contributions to 8%. Note that you won't get employer contributions on the second 4%.
- Contribute enough extra to reach $1,040 and maximise your tax credit.

Some financial experts argue that, for those already getting the maximum annual $1,040 tax credit, there is no point in putting more into KiwiSaver, as opposed to saving elsewhere (perhaps in a scheme with fees that are equal to or lower than KiwiSaver, or that offers more flexibility in withdrawing money). However, you might wish to make extra contributions to KiwiSaver because:

- The fees are lower than on alternative savings plans.
- You like the idea of tying up your money until retirement,
- You prefer to keep your savings simple, all in one account.
- You don’t want to go to the hassle of selecting and setting up an alternative savings plan.