Understanding New Zealand's Superannuation Scheme and Implications for the Macroeconomy

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Abstract:
During the last two decades, many countries around the world with unfunded social security system have experienced an ageing problem. Some have opted for a compulsory private saving scheme. New Zealand, on the other hand, maintains a unique two-pillar system: universal pension as a public pillar and voluntary savings as a private pillar. This paper provides a summary of findings from the literature to shed some light on these issues. It examines the current social security arrangements in New Zealand and its implications for the macroeconomy, facing the aging problem.

1. Introduction

Referring to a recently published article from a popular magazine *The Economist*, ageing population is yet to become one of the most striking concerns confronted by many countries around the world in the near future. Since 1950 two major demographical trends among most industrialised nations have been noticed, that people tend to live longer and have less children. Consequently, the number of people who are of working age and supporting the old will tend to be stabilising or even falling, and this fact will present tremendous threat to the pay-as-you-go (PAYG) system which is currently adopted by many countries.

The feasibility of this unfunded superannuation scheme therefore has to be questioned. Should we implement a social security reform so that the burden is shifted from the current taxpayers to a funded system, and that private pension funds add to the pool of investment capital which promotes liquidity, increases investment and in turn GDP as a result? Or should we stay with the unfunded system so that we could transfer the money to the old immediately, without worrying about inflation or potential negative real returns on the invested funds under a funded scheme otherwise. Aside from different ways of transferring funds, do we have any other options? Should we lift up the age of retirement entitlement? Or should we cut benefits and increase higher contributions? Perhaps none of them are entirely satisfactory solutions.

Asano and Bandyopadhyay (2003) note that investing in human capital will substantially improve overall social welfare and inevitably reach the sustainable social security optimum. In other words, under either scheme, enhancement in education and child care are the eventual solutions to high

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1 I thank my dissertation supervisor Dr. Debasis Bandyopadhyay for invaluable help and support.
quality future generations, which in turn, leads to higher level of output and alleviates the problem of shrinking labour force and pool of social security funds.

New growth literature pioneered by Romer (1986) and Lucas (1988) had identified human capital accumulation as the engine of growth and led to debates on how investment in human capital affects different social security systems. Kemiz and Wigger (2000) find unfunded scheme is more efficient and provides more output than the funded. Zhang and Zhang (2003) and Sánchez-Losada (2000) concur with the above conclusion that unfunded social security is more likely to promote growth. Feldstein (1995), on the other hand, states that funded social security retirement program would imply a larger capital stock and a higher level of real income than an unfunded program that provides the same level of benefits. Also argued in Kemnitz and Wigger (2000), that an introduction of a pay-as-you-go pension system cannot lead to a Pareto-improvement, because unfunded scheme discourages individuals to save privately for the old age and economic growth is positively related to total savings. However they show that a properly designed unfunded social security system can lead to higher output growth than a fully funded one. The model I shall propose considers both funded and unfunded social security components. Different aspects of the two, as we shall see in later sections, will be analysed and discussed.

Various other authors share similar views and advocate different ways of enhancing human capital and in turn, economic growth and social welfare. For example, in Kaganovich and Zilcha (1999), public investment in education is one of the potential stimulants that promote growth; the model developed in Eckstein and Zilcha (1994) shows that human capital of the children is determined by that of the parents and the amount of time parents dedicate to their children. The literature however, has yet to provide a model which unifies different social security systems under various public policies and regulations as a whole, and is capable to compare the optimums case by case.

Many work in the literature has adopted an overlapping generation model where homogeneous representative agents who live for two periods, i.e. they are young and go to work in the first period; they retire and receive benefits in the second period. The production function has two factors, namely, physical capital stock and human capital. Social welfare is an increasing function of consumptions of the young and the old, the number of children and their human capital. The amount of social security benefit received by the old has a positive relation to the number of their offspring. On the contrary, Sinn (1998) regards PAYG as the insurance of the old-age because of the moral hazard problem where children are unwilling to pay their parents a pension, and suggests that it is more efficient to have fewer children. In Groezen, Leers and Meijdam (2003), introducing child allowances would correct distortion of this sort and increase domestic population growth.

I plan to develop a model in my dissertation to include a tax rebate on expenses spent on both childcare and children’s education, i.e. part of one’s consumption can be redeemed by claiming taxes paid on those costs. This tax rebate can play an important role of maximising the overall utility and establishing an optimal social security system.

Similar to the case in Kaganovich and Zilcha (1999), I focus on the case of one-side altruism of parents towards children. Parents derive utility from human capital of their children and hence invest during their working period in children’s education. At the same time, positive social externality arises from the investment in public education. The central government distributes (unfunded) social security benefit to the old and subsidies to public educational institutes, by taxing the labour income of the young. What differentiates the model here from Kaganovich and Zilcha (1999) is the tax rebate, on childcare expense in particular, which is not considered in the other.

Following the review of key findings from the literature, I focus on the ageing problem. Next in section 3, I discuss the multi-pillar system suggested by the World Bank in response of global ageing and implications for New Zealand’s pension system according to its demographic trend. In section 4,
I present a brief description of social security systems of a few important trading partners of New Zealand followed by an outline of the New Zealand system in section 5. Next I suggest a few remedies for financing the projected increasing pension costs in New Zealand. In section 7, I report the option of the second pillar as practiced in Australia. Pros and cons of the current system are compared and contrasted in section 8 followed by an outline of a model to study formally one of the remedies in section 9. Finally, I provide some concluding remarks in section 10. The appendix after the conclusion contains a chronological description of changes in New Zealand social security followed by the complete list of references.

2. The Ageing Problem

The population in most developed countries is ageing. In other words, the number of old people has been steadily rising and their life expectancy continues to grow. For example, the Japanese population ages at the highest rate than any other industrialized country.

Figure 1 Ratio of the number of aged people (65 years or more) to total population

Source: Ministry of Finance, the Japanese Budget in Brief, 2001

At the same time, the number of children per adult has been declining in those countries. As a result, number of future taxpayer declines and number of retiree increases, feasibility of many current social security schemes blurs as this trend continues.

The problem may not be that acute in New Zealand which I shall investigate into more details in later sections. Nonetheless it is an important issue in the public media. According the projection by New
Zealand statistics, within the next 40 years, the percentage of the New Zealand population over 65 years old will be well above 40 percent and children dependency ratio will be below 30 percent. Consequently many worry that current system of social security may not be viable. Also introduction of various changes to salvage the system may lead to an inequitable distribution of benefits across different generations. This is reflected as a global concern and many countries around the world also have been actively seeking new schemes in the aim of improving sustainability and intergenerational equity.

3. The World Bank’s recommendation

In 1994 the World Bank advocated an idea of designing a pension system consisting three pillars. The first pillar is mandatory, publicly managed and tax financed; it provides a basic pension (sometimes called a “safety net”) with main object of alleviating old age poverty. This public provision is unfunded and provided through the PAYG system, i.e. current retirement benefits are paid out of current contributions. It is unfunded in a sense that the amount of benefit one receives does not depend on his/her contributions. Size of the first pillar varies from country to country. The second pillar, is fully funded, mandatory and contributory, however is the most controversial among all three pillars. Depending on specific purposes, economic and demographic conditions, it can be either publicly or privately managed, funded or unfunded, defined benefit or defined contribution. The third pillar is uncontroversial, voluntary and funded, consisting of either occupational pension or personal savings. The voluntary pillar is funded since it links intimately benefits to contributions. The system has the following structure:

Figure 1: Multi-pillar pension system suggested by the World Bank

<table>
<thead>
<tr>
<th>Pillar 1</th>
<th>Pillar 2</th>
<th>Pillar 3</th>
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<tbody>
<tr>
<td>Mandatory</td>
<td>Mandatory</td>
<td>Voluntary</td>
</tr>
<tr>
<td>Publicly managed</td>
<td>Public/Private</td>
<td>Privately managed</td>
</tr>
<tr>
<td>PAYG</td>
<td>PAYG/Funded</td>
<td>Funded</td>
</tr>
<tr>
<td>Redistributive</td>
<td>Forced saving</td>
<td>Personal saving</td>
</tr>
<tr>
<td>Means-tested/Flat</td>
<td>Contributory</td>
<td>Contributory</td>
</tr>
</tbody>
</table>

Source: The World Bank (1994)

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4 Singapore has a very different public pension provision from many others, see discussion below.
5 For example, New Zealand has first tier pension of flat-rate above the poverty line, the UK has the flat rate equal to the poverty line. See Barr (2001).
6 A defined benefit plan provides retirement benefits according to a pre-defined formula; whereas a defined contribution plan specifies the amount (usually as a fraction of one’s earnings) to contribute and pays whatever is accumulated plus investment return upon one’s retirement, i.e. it links benefits and contributions.
During the last two decades, many Latin American and European countries experienced social security system reforms as the population ages and number of the working age supporting the retired declines. Reforms involved incorporating pre-fund, privately managed scheme into mandatory social security systems, partial shift from defined benefit plans to defined contribution plans, or partially shifting an unfunded PAYG to a funded scheme. The following table illustrates current pension schemes of a few selected countries. Numbers in brackets correspond to the three-pillar system described in World Bank (1994).

Table 1: Comparison pension schemes of selected countries

<table>
<thead>
<tr>
<th>Selected countries</th>
<th>Publicly managed (all compulsory)</th>
<th>Privately managed (all funded)</th>
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<tr>
<td></td>
<td>Unfunded</td>
<td>Funded</td>
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4. A brief description of social security systems of other selected countries

Chile
Since early 1920s Chile had adopted a fully funded pension scheme which however was abolished due to low returns and unsustainable contribution-to-benefit ratios. From 1980 Chile started experiencing a radical reform of its social security scheme. There had been a gradual transition from “one-pillar” PAYG to a new “three-pillar” pension system. The first pillar CHL[1] is financed out of general government revenue, state-run and means-tested targeting the old-age poor. The first pillar also acts as the transitional arrangements for worker transferring from the old PAYG scheme to the new scheme. The second pillar CHL[2] is a funded mandatory defined contribution scheme, consisting individual pension accounts that managed by private industry of pension fund managers and insurance companies. The voluntary pillar CHL[3] is comprised by tax incentives supplementing the first two pillars beyond mandatory retirement savings.

Australia
Australia has three-pillar pension system that is similar to the one in Chile. The first pillar AUS[1] is strongly redistributive, income- and asset-tested (old-age pension) defined benefit, and financed out of general revenues through PAYG. A mandatory privately funded second pillar based on “defined contribution” AUS[2] was introduced in 1991, supplemented by the “tax-advantaged” voluntary pillar AUS[3]. Returns on the second pillar, however, depend on the performance of pension portfolio.

The United States
The US has two-tier social security scheme. The public provision US[1] is earnings-related and redistributive, largely financed through PAYG; the second pillar US[2] comprises employer-provided pension benefits based on either defined benefit or defined contribution.\(^7\) There have been several proposals for partial pre-funding of Social Security through the introduction of personal Social Security.

\(^7\) More people in the US are shifting from defined benefit plan to defined contribution plan, Mitchell (1998) believes a mandatory defined contribution plan offers much promise and reduces political risk.
Security accounts. There have been two reasons for these proposals. One is that the rate of return on these accounts would be much higher than the implicit rate of return on contributions to a PAYG system, and the other is to stimulate personal savings.  

**Singapore**

Singapore is well-known for its mandatory publicly managed pension scheme. The Central Provident Fund (CPF) was established in 1951 and Central Provident Fund Act came into effect under the Ministry of Manpower in 1955. CPF is a form of compulsory saving scheme; interestingly different from that in Chile, CPF is a publicly managed funded scheme. There are mandatory contribution rates (which vary with age) for the individual accounts. While the country relies almost exclusively on this mandatory public provision, with the introduction of the Supplementary Retirement Scheme (SRS) in 2001, voluntary saving makes up the second pillar for Singapore’s social security system. In matching the table above, the CPF refers to the first pillar SGP[1] and voluntary savings refer to the second pillar SGP[2].

**Japan**

Japan, whose population will age faster than any other industrialized country, currently has a step-up contribution public pension system, while many of the European countries adopt a pay-as-you-go system. A step-up contribution system, alike a partially funded PAYG system, is designed to accumulate social security fund in advance and keep it in reserve (similar to that in the US), preventing the level of social security contributions from soaring as the system matures. The public provision JAP[1] has two tiers, one is the flat-rate basic pension provided to the entire population (one third of which is financed out of the government’s general tax revenues and the rest is financed by contributions) and the other is earning-related pensions. The funded second tier JAP[2] is consisted of occupational pensions and personal savings.

5. The case of New Zealand

New Zealand maintains a simple two-pillar retirement scheme: universal flat rate state pension supplemented by voluntary private savings (NZ[1] and [2] respectively in Table 1).

The first pillar aims to guarantee minimum income to the aged and is mandatory as in every other country. What makes New Zealand’s state pension different from most others is that it is non-contributory and non-earnings-related. Retirement income is of defined benefit type and paid out via pay as you go mechanism. Part of the tax revenues collected from income of the working population and consumption taxes from general public are paid out to current retirees. Hence there is no separate tax account accumulating social security funds. It is compulsory in a sense that anyone who works and/or consumes are obliged to pay certain amount of tax required. In New Zealand, there are no means tests, anyone who meets requirements on age and residency is entitled to the benefit, regardless of wealth level.

To smooth PAYG and meet future projected retirement payment, New Zealand’s public pension scheme has recently incorporated a system of partial prefunding known as the Cullen Fund. Aside from immediate transfers to the current elderly, part of the tax collected are invested and paid back with returns attached upon current taxpayer’s retirement. Returns from the Fund somehow depend on

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8 See detailed discussions in Borsch-Supan and Miegel (2001).
9 The projected ratio of the number of aged people (65 years or more) to the total population will be over 27% by 2025. See “The Japanese budget in brief” by Japanese Ministry of Finance, 2001.
10 According to World Bank (1994), New Zealand and Australia were the only industrial countries that refused to make public pensions dependent on prior earnings and contributions.
11 For example, at present, all prices of goods and service in New Zealand include a consumption tax rate of 12.5 percent.
performance of the portfolio managed by the state, in both domestic and foreign financial markets. It is however unclear whether the establishment of Cullen Fund has promoted economic growth through the changes in individual saving behaviours, eventually national savings.\footnote{The Cullen Fund fits into the narrow sense of prefunding since it accumulate assets against future costs. Since the effect of the introduction of the Fund on national saving is not clear, it does not imply the broad sense. See Orszag and Stiglitz (2001).}

The potential problem with the PAYG public pension scheme in New Zealand is that it only guarantees secured retirement income to the aged as long as the government has collected enough tax revenues.

New Zealand population is growing old. As a consequence, support ratio, number of working age supporting one retiree, falls. Currently New Zealand state pension costs about 4 percent of GDP and this percentage is expected to be more than doubled within the next 50 years (New Zealand Treasury, Governance of Pension Funds, p9). As there is greater proportion of population quitting the labour force and needing retirement benefits than participating in the labour market and paying for the retired, how does the government handle the cost if the trend continues? What would happen to the retired who did not save enough and PAYG collapsed eventually at some stage in time?

The trend that people tend to have fewer children leads to less people joining future labour force to pay for future retirees. Once income taxes generated from the working population in addition to certain amount of consumption taxes are not sufficient to finance the first pillar, it would not be wise for the government to solve the problem in a longer term by squeezing the generosity of the benefit paid out or raising tax burden of the young.

6. Possible Remedies?

Here I list three possible remedies.

Consumption tax:

One possible way of solving the problem, though, can be thought as shifting the burden onto consumptions of the total population, when one relaxes the assumption above. In other words, public pension may be viable in long run if it is financed mainly from consumption taxes since the amount taxes collected from consumptions does not necessarily decrease even the population ages. Everyone pays consumption tax, so unlike the case of income tax, total revenue from consumption tax does not fall when the old to young ratio increases. The general tax pool from which New Zealand finances public pension benefit does include consumption tax. The point is that, however, the government should rely more heavily on consumptions taxes than income taxes to mitigate the ageing problem related to a sustainable public pension system.

Productivity growth:

One may also argue that the growth of aggregate productivity in an economy rather than the number of taxpayers matters more for sustainability. Zhang (1995) argues that a reduction in the number of taxpayers is more than offset by an increase in human capital per taxpayer so as to cause faster growth of output and hence tax revenue. This proposition holds in his model especially when benefits are independent of contributions. This condition seems to be similar to those public pension schemes that constitute the first pillar as the one in New Zealand.

A new deal with future generations
In addition to providing a universal public pension, we could make a new deal with future generations. To do this we define a part of the retirement benefit in terms of how much the old contributed when young to the growth and welfare of the young generation who finance those benefits. In other words, the root cause of the ageing problem is the shrinkage of the tax-base for financing pensions. Two ways a society can expand its tax base: through population growth and by improving the quality of its labour force with investment in human capital. The problem with the modern world is that adults are worried about saving for their own old age. Consequently, they do not invest their time and financial resources in having children and raising the human capital of those children. Those actions not only aggravate the ageing problem but also retard economic growth. To improve social welfare, therefore, a new pension scheme could be designed. The new scheme provides for a retirement benefit that increases with personal contribution towards raising the size and quality of the future labour force.

7. The option of compulsory saving as the second pillar?

In order to protect the “safety net” from bankrupt and solve problem of insufficient private savings (so called “myopia”), many countries have been moving away from a public defined benefit pension system toward a private defined contribution one during the last two decades. New Zealand’s closest neighbour, Australia, has adopted a compulsory private second pillar since 1992.

Australia has a similar functioned state pension system as in New Zealand except it is means tested. The second pillar, also known as Superannuation Guarantee, bases on occupational superannuation schemes by mandating employers to make superannuation contributions on behalf of their employees.13

The Superannuation Guarantee has several features. It is mandatory since employers who fail to do so face legal charges. It is privately rather than publicly managed. Employees have the right in choosing which superannuation funds they would like their employers to contribute to.14 It operates under a defined contribution system since the mandated fraction of earnings is pre-specified; funds accumulated are converted into some combination of annuitization, lump sum and pension upon one’s retirement. It is fully funded since one’s retirement benefit from this pillar completely depends on one’s contribution in his/her individual account.

According to Edey and Simon (1996), the level of Australian national savings did not significantly increase after the implementation of the mandatory private retirement saving scheme. The most plausible reason is that, it has been observed in the Australian post-reform financial market that huge amount of funds were transferred from saving account to superannuation and retirement account, leaving the aggregate amount unchanged.

Evidence from the social security system reform in Chile suggested that including a private compulsory saving scheme has strong positive impact on national saving rate. However it is unclear how much of the increase in national savings were attributed by the reform.15

8. Pros and cons of New Zealand’s current system

13 In Australia, current contribution paid by employer is 9 percent of earnings.
14 Private institutions include life insurance companies and investment managers.
15 See Kay (1997).
The current system in New Zealand, however, does not make use of a second pillar such as the one in Australia. Instead, as I have discussed earlier, it relies on the first public pillar and voluntary private savings. It is simple and efficient, and in a sense that simplification cuts down significant administration costs.

The first pillar well meets the purpose of pension system in terms of guaranteeing minimum income for each retired. It is non-contributory, non-earnings-related, and non-means-tested, thus protects the aged from poverty. Financing of general tax revenues instead of purely payroll tax is feasible since it provides a broader base.

Establishment of the partial prefunding system, to some extent, improves intergenerational equity by reducing burdens of future taxpayers. The private pillar gives individuals options of choosing funds managers of their preference, as well as provides additional support upon their retirement. And the freedom of choosing how much to save may lead to a level of saving that is closer to the optimal.

In addition, it is may not be the case that New Zealand is disadvantaged by the fact of not having a second mandatory pillar. After all, the effect of mandatory saving on national saving and overall economic growth is not clear. Nevertheless, even if the level of national savings was lifted by changes in private saving behaviours, it may not lead to economic growth. Keeping national output and consumption patterns constant, increase in one’s saving may leave less available financial resources to education for future generations. In a longer term, less investment in education is more likely to lead to the consequence of lower human capital in future generations and in turn lower future output.

On the other hand, in the case of fast population ageing and insufficient savings due to individual myopia, current arrangement may not be effective any more. For example, drop in income tax revenue as the result of shrinking working population coupled by insufficient growth in human capital may threaten the sustainability of the public pillar. Without the compulsion from the government, one may rely on the commitment of the state rather than self-providing retirement income, causing large fiscal deficit and loss of welfare. Together with reducing the problem of moral hazard, an introduction of a mandatory saving scheme may also well develop New Zealand’s financial markets into more depth.

St John and Willmore (2001) report that New Zealand’s social security system does not conform to the three-pillar pension system advocated by the World Bank. They argue that, however, New Zealand’s current system does ensure “a stable and adequate retirement income for all citizens, moderating income inequality”.

There are a few issues raised in St John and Willmore (2001) are worth examining regarding New Zealand as a model for other countries. First, moral hazard exists when the first pillar offers generous benefits rather than providing a minimum old age income. This argument weakens the necessity of the second mandatory pillar, an over generous public pension scheme is more likely to have adverse effect on voluntary savings, and in turn, growth of income and standard of living of future generations. Second, introduction of partial prefunding increases inter-generational equity. By forcing the working population to save, the government invests some fraction of tax revenues and repay certain amount to the same generation, which leads to intra-generational instead of immediate inter-generational transfer. This way of financing may alleviate the ageing problem in New Zealand. Third, since the first pillar is universal and non-contributory, the poor benefits from the public scheme more and therefore the prevalence of pillar one provides equity among retirees. Fourth, New Zealand’s superannuation system has lower administration costs comparing with others who have a second pillar since there are no individual accounts.

Issues remain, however, as to what are the optimal saving rate as well as investment when one considers the trade-off between quantity and quality of children, which St John and Willmore (2001) has not included.
9. Some suggestions for improvement of the New Zealand pension system

Considering a number of macroeconomic implications that I discuss below, I propose a few suggestions for improvement in this paper. I now briefly outline rationale behind those suggestions using a simple macroeconomic model.

Here I follow the model first developed by Asano and Bandyopadhyay (2003). In any one phase in time, two generations, namely the young and the old, co-exist. Agents derive their utility from their consumptions in both periods, number of children, and human capital of their children. The current technology of production maps labour and human capital into output. The government provides subsidy for child care and education either directly by adjusting the taxable income of the young. It could also adjust the retirement benefits of the old based on their contribution at the young age to the child care and education of their children.

Under the above environment, the representative young chooses the optimal number of children, the optimal investment in education of her children and the optimal hours of work so as to maximise her lifetime utility given government’s policy on superannuation. All factors are in their marginal product. The government chooses the optimal superannuation regime given the optimal choice of the representative young so as to maximise a social welfare function that assigns equal weights on the utility of each generation.

Numerical simulation of the above model can be used to evaluate the merit of the current superannuation system of New Zealand relative to the proposed new scheme.

10. Concluding Remarks

Labour market in New Zealand like in other developed countries does not provide a decent level of income for retirees. At an individual level, without secured retirement income, an aged cannot live at any standard; at an aggregate level, without stable and secured living environment for the retired, one country cannot have sustainable growth. Therefore to achieve steady growth in the long run, one country needs to have a well-designed social security system.

In this paper I raise a few concerns regarding how to raise the tax base to ensure viability of such a system by evaluating the current social security arrangement in New Zealand. The new scheme that has been proposed in this context needs to be examined further to settle those concerns.
Appendix

Some historical background on NZ superannuation events

With the passage of the Old Age Pensions Act 1898, the age pension, described as tax-financed, flat rate and non-contributory, was first introduced into New Zealand in 1898. The entitlement age was 65 and the age pension was both means tested and asset tested (i.e. only the poorest were entitled to an old-age pension).

In 1939 a dual pension system for public provision was introduced with the Social Security Act 1938. There were two tax-funded flat rate pensions: one is non-taxable however means tested age benefit payable from age 60, the other one is a universal taxable flat pension for those over the age 65 not on the age benefit. In 1964 the Social Security Act was abolished and the social security system was financed by from general taxation revenue which included a special social security tax on incomes.

The 1972 Royal Commission on Social Security reviewed the structure of state superannuation and rejected the proposal of compulsory earnings-related contributory scheme recommended by New Zealand’s third Labour Party government.

In 1974 the New Zealand Superannuation Act was passed with the governance of the Labour Party. The implementation of the Act in 1975 introduced a fully funded, publicly managed, earnings-related contributory component on top of the universal flat-rate basic pension provision (two-tier scheme). Both tiers are taxable and inflation-adjusted. However the scheme was short-lived; The National Party came to power in 1976 and abolished Labour’s contributory scheme, moving to a one-tier universal flat rate pension payable out of general taxation. The name of the universal superannuation benefit was changed from New Zealand Superannuation to National Superannuation. OECD (1987) has described National Superannuation as “remarkably simple and generous”. Under this scheme, those who have not contributed were eligible for a flat-rate benefit financed by general tax revenue in New Zealand; while retirement incomes in most other OECD countries are earning-related pension based on past contributions.

In 1997 compulsory contributory second tier pension plan proposed by Winston Peters’ New Zealand First — opposed by both National and Labour — was “non-negotiable”.

In the same year, the National government adopted a taxable universal, more generous, public pension called National superannuation. There were neither income nor asset tests.

In 1984 National superannuation became an income-tested benefit and included a tax surcharge of 20 cents in the dollar on other income received. It was funded on a PAYG basis from general revenue regardless of past contributions. National superannuation was renamed Guaranteed Retirement Income (GRI) in 1990 however reverted to National superannuation in 1991.

A multi-party accord on retirement income policies signed by the three major political parties and formalised by the Retirement Income Act 1993. National superannuation was renamed New Zealand Superannuation (NZS). In 2001 the New Zealand Superannuation Act 2001 passed and the New Zealand Superannuation Fund was established.

As the cost of pension and the concern of feasibility of long-term funding scheme increased in the late 1990s, a partial pre-funding mechanism of instituting a special superannuation fund (Cullen Fund)

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16 See the “The Supreme political football,” Centre for Retirement Research, Working paper, Boston College. Website: http://www.bc.edu/crr
drawn as a fixed share of income tax revenues was introduced in 2001. The primary purpose of establishing an independently managed Fund is to meet the cost of NZS and smooth PAYG system, both in the present and out into the future.\textsuperscript{18}

Reference:


\textsuperscript{18} Under current arrangements, annual payments of NZ Superannuation are expect to rise from 4% of GDP to about 9% of GDP over the next fifty years. See “Pre-funding New Zealand Superannuation: Funding arrangements” by Michael Cullen, September 2000.


