

12 July 2007

Clerk of the Committee  
Finance & Expenditure Committee  
Select Committee Office  
Room 10.04, Bowen House  
Parliament Buildings  
WELLINGTON

To the Chair of the Select Committee

**ASFONZ SUBMISSION ON THE TAXATION (ANNUAL RATES, BUSINESS TAXATION, KIWISAVER, AND REMEDIAL MATTERS) BILL ("the Bill")**

We wish to submit the attached in respect of the Taxation (Annual Rates, Business Taxation, KiwiSaver, and Remedial Matters) Bill released on 17 May 2007.

ASFONZ is an independent national, non-profit membership organisation founded in 1969. Its current membership comprises around 100 major workplace superannuation schemes and around 50 organisations and individuals representing the various product and service providers for workplace superannuation.

The mission of ASFONZ is to promote workplace superannuation in New Zealand.

ASFONZ seeks to achieve that mission through:

- 1 **Advocacy** – being the recognised voice for all employers and trustees involved in workplace superannuation, through:
  - (i) advocating legislative and public policy initiatives beneficial to the industry;
  - (ii) making submissions and commentary on existing legislative and public policy initiatives;
  - (iii) issuing regular press releases and other public commentary on matters of wider concern or interest to members; and
  - (iv) staying in regular contact with responsible Ministers, regulatory and industry bodies, the Retirement Commissioner and Government Departments to project, promote and advance members' interests.
- 2 **Education** – promoting trustee, employer and member education through dedicated training programmes, newsletters and special interest seminars.
- 3 **Networking** – providing trustees, employers and service providers involved in workplace superannuation with a regular forum for sharing ideas and information on industry matters.

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I would be pleased to answer any queries in relation to the submission. We would like to appear in person at Select Committee hearings.

Thank you for the opportunity to make this submission.

Yours sincerely

John Melville  
Chairman

# **ASFONZ**

(The Association of Superannuation Funds of New Zealand)

**Submission to the**

**Finance & Expenditure Select Committee**

**on the**

**Taxation (Annual Rates, Business Taxation,  
KiwiSaver, and Remedial Matters) Bill  
("the Bill")**

**July 2007**

## Summary of our submission

The scope of the Bill is wide. The ASFONZ submission does not comment on all of the matters covered by the Bill but focuses on those issues which are of relevance to ASFONZ members. A summary of particular features of our submission that we would like to highlight appears below, followed by a more detailed commentary.

ASFONZ is pleased to note that where additional incentives are proposed to be introduced to encourage savings these have, in general, been extended to Complying Superannuation Funds as well as KiwiSaver Schemes. We believe that this recognises the value of existing superannuation schemes as savings vehicles and will give less cause for such schemes to be discontinued.

Complying Superannuation Funds appear to have been recognised as a legitimate alternative means by which members can be incentivised to lock in savings for retirement. This is very positive and supports the presumed principal policy objective of KiwiSaver. However, the latest proposals undermine the efficacy of Complying Superannuation Funds meaning that they may cease to become a viable option. This means that such schemes are again confronted with considering winding up if they cease to be viable, thus compromising existing savings.

We submit that it is logical and desirable to positively encourage the use of Complying Superannuation Funds as genuine alternatives to KiwiSaver Schemes. This should have the affect of reinforcing the position of employers who have continued to support employees in making provision for retirement and to encourage them to retain the schemes which currently have some \$11.5bn. of accumulated savings in place.

We further submit that proceeding with the proposals as they stand significantly undermines the potential continuation of existing schemes that the Complying Superannuation Funds legislation was intended to promote, with a resulting dissipation of accumulated savings.

ASFONZ continues to question why a participation agreement entered into by an employer after 1 July 2007 (other than as a successor agreement) should not be able to qualify as a Complying Superannuation Fund. As benefits under a Complying Superannuation Fund are to be locked in, in a similar manner to a KiwiSaver Scheme, there seems to be little point to this restriction.

With regard to the acceptability of a successor agreement, we have some difficulty with the term "commercial necessity" – what is this supposed to mean? The most likely need for a successor agreement will be as a result of an employer's dissatisfaction with the original master trust provider and the adoption of another provider. Is this an example of commercial necessity?

The proposed revision to the definition of salary or wages, to be used for calculating minimum contributions to a Complying Superannuation Fund, is likely to be inconsistent with the definition currently in use and familiar to members. We believe that such a change would prejudice the likelihood of employers adopting a Complying Superannuation Fund and submit that schemes should be able to retain the traditional "gross base salary" definition in appropriate circumstances.

Finally, we express our strong support to the proposed extension of legislation introduced in 2006 that allows the Government Actuary to approve the transfer of members to another registered superannuation scheme, without their specific consent, where the receiving scheme offers benefits of no less value to members. The extension to allow approval to be given irrespective of the provisions of the scheme trust deed makes this option available to all schemes and we believe that this was always the intention. We therefore welcome this remedial action.

# Detailed comments for the ASFONZ submission

## Part A – Related to Complying Superannuation Funds

1. The complying superannuation fund criteria under section 35(1) of the Superannuation Schemes Act remain problematic. Those problems are not entirely addressed through clause 240 of the Bill. The complying fund rules evidence the same lock in towards retirement savings as are evidenced by the KiwiSaver Scheme rules. There appears no valid policy reason to restrict complying superannuation fund status to employer-based arrangements entered into prior to 1 July 2007.

The current criteria for participation agreements are uncertain in their application and contrary to competition and to the policy of portability that underpins KiwiSaver. ASFONZ remains strongly of the view that reference to participation agreements having been entered into prior to 1 July 2007 be removed from the criteria. The only grandparenting involved would then relate to the relevant registered superannuation scheme being in existence on 1 July 2007, which ASFONZ submits is the only valid time critical criteria for eligibility.

2. If the 1 July 2007 criteria for complying superannuation fund participation agreements is to be retained:

2.1. ASFONZ supports the extension of the eligibility criteria to include successor participation agreements, and is generally pleased with this positive response to submissions we made on this issue. The only reservation we have is as to how the requirement that the replacement arrangement be driven by “commercial necessity” will be applied in practice.

2.2. By stating that a “participation agreement” includes a trust deed, ambiguity is created. ASFONZ understands the purpose of the new section 35(5) is to recognise the fact that participation agreements might be in the form of a deed. As it stands, it is arguable that an amendment made to the governing deed of the relevant superannuation scheme entered into after 1 July 2007 that impacts on employer participation may place an otherwise complying superannuation fund out of the regime as a relevant “trust deed” is then entered into after 1 July. To avoid such an interpretation, ASFONZ recommends the proposed new section 35(5) be amended to confirm that a “participation agreement” means any form of arrangement pursuant to which an employer facilitates participation in a registered superannuation scheme by its employees, including arrangements documented by way of deed.

2.3. Legislative clarification that contribution holidays for complying superannuation funds are permitted would also be desirable to optimise consistency in contribution philosophy between complying superannuation funds and KiwiSaver schemes. Legislation is currently silent on this point, and it is not a given that all complying superannuation funds will import this flexibility. ASFONZ submits that subpart 4 of part 3 of the KiwiSaver Act, with necessary modifications, be implied into the complying fund rules of every complying superannuation fund.

3. Aligning the minimum amount to be deducted from salary or wages under the proposed new definition of complying fund rules (clause 144(2)(D) of the Bill) with the amount required to be deducted under the KiwiSaver Scheme rules effectively transports the KiwiSaver Act definition of salary or wages into every complying superannuation fund. This is highly unlikely to be consistent with the definition used in affected superannuation schemes that will continue to

apply for contributions that are not subject to complying fund rules. This creates a significant administrative member communication and remuneration design challenge for schemes and employers involved.

For many, the efficacy of adapting complying superannuation fund status is terminally prejudiced by this forced non-alignment with existing scheme definitions. For some, this proposed change has meant that adopting their scheme to provide KiwiSaver equivalence will no longer be an option. Whether that option will be replaced by a true KiwiSaver option for those employers is uncertain – the lack of flexibility inherent in KiwiSaver means it is not as effective in delivering remuneration solutions for employers as had been possible with incorporation of a complying superannuation fund component to run alongside and compliment existing schemes.

ASFONZ would like to see a discretion vested in the Government Actuary to approve salary or wage definitions used for complying fund rules purposes where satisfied that the definition employed is genuinely required to align deductions made, and not a device to circumvent more onerous KiwiSaver obligations. As a minimum, existing salary or wage definitions that are at least equal to “gross base” should be recognised. As it stands, existing complying superannuation funds will need to amend deeds to give effect to this change, if they wish to take on the anticipated added administrative burden.

4. Portability continues to be a problem where complying superannuation funds are concerned. Two aspects need to be urgently addressed:

- 4.1. Portability needs to go both ways, so that if an employee joins a complying superannuation fund his or her KiwiSaver balance can be transferred across to that fund. This should help ease the complications inherent with setting up a regime that will otherwise require dual membership of a KiwiSaver Scheme and of a complying superannuation fund or complying superannuation funds, which will impact on the administrative burden of employer compulsory contributions.

- 4.2. Allowing portability from a complying superannuation fund, at a member’s discretion and at any time, may impact on benefit structures in those funds where benefits such as death or disability benefits are calculated as a salary multiple, with an insured component that offsets accumulated savings. If full [insurance] portability remains, ASFONZ would like to see an ability for complying superannuation funds to adjust benefits of those members exercising transfer rights so as to avoid any consequential increase in costs for the fund, notwithstanding any adverse affect consequences for the member concerned.

5. The proposed section 101H to the KiwiSaver Act, relating to complying superannuation fund provider obligations when an employer fails to pay compulsory employer contributions are unduly onerous. Requiring immediate steps to be taken where a provider has reason to believe there has been a failure to pay is impracticable, and inconsistent with general superannuation scheme reporting obligations. ASFONZ submits that the obligation should be limited to annual certification as to contribution payments, in similar fashion to what is required under superannuation scheme annual reports at present.
6. Members of registered superannuation schemes have not previously had a need to provide IRD numbers for scheme administration purposes and many schemes have not collected this information. In respect of a Complying Superannuation Fund that does not elect to become a Portfolio Investment Entity this will continue to be the case. It would be helpful if the legislation included a power for trustees of a Complying Superannuation Fund to obtain

IRD numbers from the Commissioner or from the employer of a member for the purpose of administering tax credits.

## Part B – Related to KiwiSaver

7. The Taxation (KiwiSaver and Company Tax Rate Amendments) Act 2007, Section 64, requires all employer contributions to a KiwiSaver Scheme to be paid via the Commissioner, by amending section 93 of the KiwiSaver Act. This creates an inconsistency with section 68(2)(b), which prevents any payment for “other things” such as life insurance being made via the Commissioner. Together, these provisions mean that employers are prohibited from funding KiwiSaver Scheme benefits other than retirement benefits in respect of their employees.

Remedial legislation is required to grant relief from the limitation imposed by section 93 in respect of employer contributions paid for other things in terms of section 68(1)(b). Relief is also required to allow employers to make payments direct to providers to subsidise scheme administration costs, being an arrangement that would otherwise fall within section 68(2)(a) but will now need to be paid via the Commissioner, resulting in an unnecessary inefficiency as such payments are not necessarily based on a multiple of salary or wages.

Failing to make the suggested change will result in the legislation creating an undesirable barrier to employers wishing to use the mechanism of KiwiSaver scheme membership to fund wider benefits for employees than retirement benefits, and a barrier to the efficient provision of retirement benefits for employees where that provision is in a form other than traditional employer contributions. ASFONZ notes that this restriction is not placed on complying superannuation fund contributions, and submits that similar flexibility should be afforded to KiwiSaver schemes.

8. Timing issues with respect to accrual of entitlement to tax credits appear to have been addressed by way of a proposed supplementary order paper. ASFONZ supports the remedial proposals already announced in the Ministers’ media statement of 2 July 2007. However, what remains unclear is precisely how the proposed “pro rata” allocation of tax credits – and of the fee subsidy, for that matter – will work in practice in the context of schemes with a range of investment options available, and in the context of a member participating in a KiwiSaver scheme and one or more complying superannuation funds. Are credits intended to mirror current contribution percentage allocations across various funds, or mirror the respective proportion of total savings each fund comprises at the time the credit is received? Legislative clarification would be desirable.
9. The ‘other contributions’ offset allowed against the compulsory employer contribution at the proposed section 101D(2) of the KiwiSaver Act is problematic and unduly limited in its scope. As drafted, it provides an incentive for some employees to exit existing superannuation arrangements where possible in order to obtain a “windfall” employer top up to their savings. In some cases, this may just result in a diversion of current savings. In others, however, the employee member may be able to withdraw all of their existing savings and may exercise this right in the knowledge that doing so will not cut them off from ongoing employer subsidisation of their savings. By grandparenting the offset, the proposed definition also sets up the risk of disparity and inequity in work place remuneration arrangements and may undermine the intent of long term collective employment agreements entered into before 17 May 2007 that cover future employees beyond 1 April 2008, but failed to adequately factor in the rules for compulsory contributions.

ASFONZ submits that:

9.1. paragraph (i) of the 'other contributions' definition be expanded to accommodate employees employed after 1 April 2008, but on terms determined prior to 1 April 2008 or at the very least on terms determined prior to the Bill coming into effect;

9.2. paragraph (ii) be amended to confirm that an employer is able to benefit from the ability to off-set if it was providing its employees in general with access to superannuation arrangements as at 17 May 2007. As drafted, the provision implies that only contributions to a scheme in respect of an employee to whom the employer was providing access to that scheme as at 17 May 2007, will qualify;

9.3. in addition to the presumably unintended early grandparenting of qualifying employees, by limiting the criterion to contributions made to a particular scheme as at 17 May 2007, the offset rules lock in employers to existing arrangements. This penalises employers where existing arrangements are terminated for reasons beyond their control, suppresses competitive activity in relation to master trusts, with employers strongly incentivised not to change providers, and is contrary to the policy of portability that underpins the KiwiSaver Act. ASFONZ notes this concern is similar to that previously expressed in relation to complying superannuation fund participation agreement criteria that has now been addressed (to an extent) through reference to successor agreements, and as a minimum recognition of successor schemes is required;

9.4. paragraph (iii) is again unduly restrictive in its grandparenting approach. Greater flexibility should be introduced to recognise superannuation contributions made by the employer pursuant to any arrangement agreed by the employer prior to 1 April 2008. In that way, consistent with the submission at 5.1 above, long term collective agreements can be given proper effect in the manner contemplated under the Employment Relationships Act;

9.5. many existing schemes that employers may look to utilise for the purposes of the offset will currently maintain a Reserve Account. One of the allowable uses of the Reserve Account may be the payment of employer contributions. It would be helpful if the legislation is clarified to positively confirm that there is no restriction on the payment of any compulsory employer contributions from the Reserve Account where the trust deed of the relevant scheme allows. Paragraph (iii) should accordingly be expanded to allow offsetting for employer contributions paid through allocations from scheme reserves to minimise the extent of double-dipping that might otherwise result in windfall gains for members of over-funded employer superannuation schemes;

9.6. paragraph (iv) needs amendment to overcome the extent to which existing generous employer subsidisation arrangements involving vesting scales might fail to be recognised for offsetting purposes. The amendment proposed is that employers be given the power to fully vest in an employee all or part of any contributions to a registered superannuation scheme or fall in from reserves that would otherwise qualify under paragraphs (i) to (iii), notwithstanding the provisions of any relevant trust deed or participation agreement or restrictions that might otherwise apply at law. In this way, employers have the option of accelerating what for many will be a discretion only available to them when a resignation benefit is paid IF the employer wants relevant contributions to offset its compulsory contribution obligation;

9.7. the "db increase" criteria at proposed section 101D(2)(d) are inappropriate and possibly unworkable in practice. In particular, reference to vesting of a contribution as it accrues in the context of many defined benefit schemes will be uncertain in its application – arguably, full vesting only occurs when an employee reaches retirement age and salary multiples for the defined benefit cease increasing. The appropriate criteria in this context is already legislated at section 25(2)(b) of the KiwiSaver Act in the context of exempt employers, where the reference is solely to the increase in value of a member's accrued benefit. ASFONZ submits that paragraph (ii) should be extended to recognise increases in benefits due to scheme reserves, and that paragraph (iv) be deleted as the concept of the amount accruing has already been captured.

10. ASFONZ does not support the proposed replacement of section 66 of the KiwiSaver Act, which will prevent employers from subsidising a part of their employees' minimum 4% contribution with effect from 1 April 2008, subject to transitional provisions for subsidy arrangements entered into prior to that date. Removing this ability limits the flexibility for employees to contribute towards KiwiSaver.

The concern of ASFONZ is that by removing the current ability for employees to contribute on (say) a 2 + 2 basis, access to KiwiSaver may be placed beyond reach of those employees unable to forgo the full 4% of salary required. Those on total remuneration packages that can only afford to forgo 4% of their package are also denied the additional benefit of a proportion of tax free employer contributions to their savings which are now to be reserved to those able to afford a contribution rate in excess of the 4% minimum, which appears contrary to the policy objective of encouraging saving for all. To encourage workplace savings to the maximum extent, ASFONZ would like to see the flexibility of the original provisions of the Act retained.

11. The proposed section 66A setting out transitional rules to move away from split employer/employee funding of the minimum contribution is confusing in its application. A simpler approach may be to refer straight to the proposed table at schedule 4. Regardless, the formula should recognise employer contributions funded from scheme reserves.
12. Section 206 of the KiwiSaver Act, providing relief for the Crown or any other person such as an employer being considered to provide investment advice, fails to extend that relief to investment broker obligations, leaving the position at least arguable that employers and the Commissioner should be treated as investment brokers when passing on contributions to providers. ASFONZ submits that clarification would be desirable to confirm that neither the Commissioner nor any employer is to be regarded as an investment broker for the purposes of the Investment Advisers (Disclosure) Act 1996 solely as a result of transmitting contributions to a provider as contemplated under the KiwiSaver Act.

13. Whilst section 81 of the KiwiSaver Act deals with amounts paid in excess of the required amount of a contribution, the Act is silent as to the requisite approach when a KiwiSaver enrolment is made in error or an ineligible person joins. The uncertainty created by this gap has given rise to much debate and analysis, and legislative clarity is desirable. To avoid complicating portfolio investment entity calculations that may arise if such memberships are treated as void, ASFONZ submits that a new provision should be inserted that allows a withdrawal benefit to be paid in respect of invalid enrolments, to be refunded via the Commissioner, notwithstanding the KiwiSaver rules or provisions of the relevant trust deed.

#### Part C –Related to the Superannuation Schemes Act 1989

14. Clause 239 extends section 9BAA to allow GA to consider transfers to other registered schemes without member consent in prescribed circumstances, notwithstanding the provisions of the trust deed. ASFONZ strongly supports this change.

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