
Kiwi Saver or Kiwi Slavers



Before you groan – oh god not another article on Kiwi Saver please take the time to read the content and see if you can answer the questions raised – with confidence.

So what does this report cover

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- **Employers point of view - Should I, Shouldn't I**
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 - Compulsory employer contributions - it had to happen didn't it
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Introduction

Whether you regard Kiwi Saver as a good or bad thing – you will be right. It will all depend on your attitude and outlook towards the scheme.

From an employers view point there are significant costs but also gains to be made as the scheme develops and the sooner these gains are understood the quicker you can make informed decisions on it. As the scheme is compulsory and has the backing of all the main political parties, all employers have to become involved – but at what level:

- The reactive approach of simply doing the bare legislative minimum and leaving everything else up to their employees.
- The proactive approach of getting involved and helping their employees save for their retirement through a variety of options, which could help with staff recruitment, retention and morale – and in the current labour market, is a very important issue.

By offering things like employer contributions, salary sacrifice, preferred providers etc you will (hopefully) be seen as being interested in your staffs welfare and adding value to them. This could be enough to differentiate you from other employers or become an employer of choice. While this will involve extra administration and payroll time and require the employer to advise employees on investments / schemes these can be kept to a minimum by having the right systems in place.

Who can join Kiwi Saver and Should I?

All NZ residents under the eligible age for NZ Superannuation or people legally entitled to be in NZ indefinitely.

All new employees and employees changing jobs from the 1st April 2007 aged between 18 and 65 are automatically enrolled. There are detailed rules covering “new jobs” which we will not cover in this article but we can supply these if you wish – please contact us.

Self-Employed, existing employees, non-employees and beneficiaries can join on a voluntary basis ie Opt in



Employers Point of View - Should I, Shouldn't I



What are my Obligations as an employer?

From the 1st July 2007 your main Kiwi Saver obligations include:

- You must offer Kiwi Saver in your workplace, unless you have been granted exempt status - ie you already have an approved superannuation scheme.
- To advise the IRD of all new employee's name, IRD No, and address, within 3 weeks of their starting work via a KS1 form - Kiwi Saver Enrolment Details, which is sent in monthly with your Employer Monthly Schedule.
- To provide new employees, or existing employers who request one, with a Kiwi Saver Employee Information pack which are available from the IRD.
- To deduct employees' contributions from their gross salary including taxable allowances and forward these to the IRD along with their PAYE. This applies for the first 14 days of employment – even if the employee opts out. Contribution rates are 4% or 8% of the pre tax wage; the employee chooses which rate by completing a KS2 form. If an employee does not do this then you should deduct at the default rate of 4%
- Ensure new employees' contributions start from their first pay – auto enrolment
- Refund any contributions deducted if they haven't been passed on to IRD when an employee opts out of Kiwi Saver - you should request the IRD do this directly to the employee rather than trying to put this refund through your payroll system
- Provide a Providers investment statement to all employees if you as an employer have chosen a preferred Kiwi Saver scheme.
- Accept and act on “opt out” requests (KS 10) and contribution holiday letters. It is vital that opt out requests are acted on immediately as an employee can only opt out between the 2nd and 8th week of starting work. And you must advise the IRD within the time of filing your next monthly PAYE schedule.
- Keep track of employees on contribution holidays and ensure their contributions restart on time.
- Keep all the required Kiwi Saver records.

Voluntary options include:

- Making voluntary employer contributions either directly to the scheme provider or through the IRD. Voluntary employer contributions are exempt from specified Superannuation Contributions Withholding Tax subject to a cap of the smaller of either the employee's contributions or 4% of their gross salary or wage.
- Choose an initial Kiwi Saver scheme for employees who have not chosen their own. Remember to provide an Investment Statement.

Compulsory Employer Contributions - it had to happen didn't it

- From the 1st April 2008 employers must contribute 1% of an employees gross wage if that employee has opted in.
- This sum increases by 1% per year for the next 3 years – at this stage!

- From 1st April 2008 employer contributions will no longer count towards the minimum contribution of the employees 4%
- The Government will reimburse employers for the cost of matching contributions, through a new tax credit capped at \$20 per week per worker (about \$1,040 per worker per year), and their contributions will also remain tax free under amendments introduced in 2006. The new tax credit will be paid to employers through the PAYE system by offsetting the credit against the employer's contribution and other PAYE liabilities, in order to minimise cash flow impacts and compliance costs.

Cullen has opted to take cash from employers' pockets and put it into employee's pockets.

Preferred Provider - Should I choose one for my workplace

By choosing a preferred provider for your employees you make the process a lot less hassle for new employees, as they will be given an investment statement upon starting employment

Usually this allows the investment option to be tailored to suit the needs of your business and employees. This is because there will usually be a larger range of products for members as opposed to default schemes. The six default providers are all cash and bonds investments – they are providing nothing that the ordinary person couldn't do for themselves.

Also the risk/return profiles can be matched to the individuals – a 25 year old is likely to want growth assets were a 50 year old would want more conservative options.

The main reasons for not choosing a provider are

- That it is the hassle free, safe option, which for most small business will be very tempting.
- The possible risks if the chosen provider underperforms or even fails – remember that while each provider must meet strict Government criteria there are no guarantees.

If you are going to choose a provider – take your time and choose one that you feel comfortable with. If you are just passing on information about Kiwi Saver to your employees or selecting a preferred Kiwi Saver scheme, you should not be liable as an investment advisor or promoter under the Investment advisor's Securities Legislation.

We recommend that you do not give financial advice to your employees – if you want to provide advice to your employees arrange for independent advice from a suitably qualified financial advisor. But remember they may have a vested interest in the advice they are giving you.

“Sorted” has a good checklist titled “ Advice Checklist “ on their website (www.sorted.co.nz) to assist you in selecting an Investment Advisor.

Existing Schemes

As very few employers have existing schemes and the issues surrounding these are complex we will not cover this topic in this update. If you require further information on this topic please contact us.

Penalties

Yes like anything the IRD administers there are penalties for getting it wrong. Penalties will apply in the following circumstances

- Failing to provide information to employees on Kiwi Saver
- Failure to deduct or incorrect Kiwi Saver contributions
- Penalties range from \$50 to \$250
- Any penalties are payable on the day your next PAYE payments are due.
- In addition to the above penalties late payment penalties and interest apply.

Redundancies

Again most employers do not have redundancy payments in their employment agreements. For those of you that do you should consider the impact of the compulsory employer contributions as you may well face a double hit, and for once it is not just the employer that pays. For employees who are members of Kiwi Saver, any redundancy payments will be subject to Kiwi Saver contributions both by the employee and, from 1 April 2008, the employer.

For employers who are thinking they may have to lay people off in the future this aspect of Kiwi Saver may encourage them to rush through any redundancies prior to 1 April 2008 to avoid this additional cost.

Impact on your wage bill

Employers need to factor in the recent increases in employee costs when deciding to employ extra staff and/or when doing their forecast over the next few years.

The main things to consider are

Extra weeks holiday – Increase in overall wage costs	2%
Full Employer Contributions – Increase in overall wage cost	4%



Remember that these are required increases, which may mean that there are no guaranteed productivity or efficiency gains to help offset these increases.

The government will have you believe that this additional cost is offset by the \$1,040 per annum/ per employee tax credit and the 3% drop in the company tax rate, however in reality:

- The \$1,040 would only cover an employee on a gross wage of \$26,000.
- The tax cut is a myth for most companies as once the profits are distributed to the owners they become taxed at their personal tax rates which will negate most savings – use our earlier article – “Tax Cuts – Myth or Reality”.
- The administration and compliance costs to the employer.

Overtime

Remember that your contribution will increase where workers work overtime eg if you pay time and a half your required contribution goes up 50% - to help manage this extra cost employers should review their overtime policies and procedures.

Wage Reviews

Employers will need to keep the cost of compulsory contributions in mind when considering wages reviews for staff – unfortunately in a lot of cases wage increases will end up going to the government via Kiwi Saver contributions rather than the employee as a wage increase.

When does Automatic enrolment does not apply

The automatic enrolment rules do not apply to:

- Casual and temporary employees employed under a contract of service for a period of 28 continuous days or less.
- ACC and paid parental leave recipients, private domestic workers or workers employed by exempt employers.
- Employees under 18 years or over 65 years of age.

Salary Sacrifice

What is it – it is an agreement between an employee and the employer that the employees gross remuneration is reduced and the employer instead contributes that gross amount into the employee's Kiwi Saver account.

The IRD have said that reorganising your pay this way was entirely legal and permitted by the current Tax Act and Kiwi Saver Act and was unlikely to be considered as tax avoidance. A stance that is interesting as prior to Kiwi Saver the IRD would not allow this type of structuring.

This gives employers an opportunity for significant benefits to be obtained from modest salary sacrifices, however note:

- The employer contributions are capped at the lesser of the employer's contribution or 4% of the employee gross remuneration.
- Officially, only contributions into Kiwi Saver accounts made by employers are tax-free.
- For there to be tax-exempt employer contributions to a Kiwi Saver scheme, there must be matching employee contributions

How does it work?

Employer contributions of up to 4% of an employee's salary can be exempt from tax. This means if a person contributes 4 per cent of their salary or wages to a Kiwi Saver scheme, the first 4 per cent of any contribution from their employer will be exempt from tax.

This tax benefit will inevitably produce requests from employees for "salary sacrifice" arrangements because the tax benefits available from a Kiwi Saver salary sacrifice are so much greater - in practical terms, as much as \$39 for every \$100 sacrificed for those on the top tax bracket.

Proceed with Caution

Implementing a salary sacrifice arrangement is not complex but care is required to ensure that it is effective and delivers the expected benefits. In most cases it will be possible to develop templates which employees considering a salary sacrifice arrangement can use to help them make a decision.

We strongly recommend that any salary sacrifice documentation be prepared or reviewed by suitably qualified people before it is made available to employees.

It is vital employees understand the downsides of salary sacrifice, some of these are:

- Resulting "downstream" effects of a salary sacrifice. These can include things like insurances calculated on salary (such as income protection insurance), liable parent payments, student loan repayment obligations, ACC benefits and redundancy payments.
- That a portion of their salary is "tied up" until retirement and if they apply for a contribution holiday, tax will be payable.
- Employee contributions are not exempt from PAYE.

To determine exactly how much salary to sacrifice to get the maximum tax break, multiply the employee's current salary by 0.0384615 to determine the amount to be salary sacrificed.

Important: It is not 4% of the gross remuneration – if this figure was used then part of the employer contribution would become liable for tax eg \$100,000 x (4% - 3.84615%) = \$153.85 that would be liable for tax – while it is not a lot the extra paperwork could be.

	<u>Pre Sacrifice</u>	<u>Post Sacrifice</u>	<u>Compulsory</u>
Gross Salary	100,000	96,154	100,000
Net Salary	69,730	67,745	69,730
Less: Employee Contribution 4%	<u>4,000</u>	<u>3,846</u>	<u>4,000</u>
In the Hand	65,730	63,899	65,730
Kiwi saver total			
Employee	4,000	3,846	4,000
Employer	<u>0</u>	<u>3,846</u>	<u>4,000</u>
	4,000	7,692	8,000
Total Cost to Employer	100,000	100,000	104,000
Total Value to Employee	69,730	71,591	73,730

As you can see from the above example the employee is better off under the sacrifice option and the employer is worse off under the Compulsory option (surprise surprise).

Once compulsory employer contributions reach their current maximum (4% by 1st April 2011) employees will be able to fully access this benefit without having to make a salary sacrifice.

As employers ready themselves for the introduction of KiwiSaver they should decide how they will respond to the inevitable requests from employees for salary sacrifice arrangements.

Employees point of view - Should I, Shouldn't I

Use the following to help assist your employees in their decision-making decisions.



What are my obligations as an employee

From the 1st July 2007 employees need to decide

- Whether to join a Kiwi Saver scheme (if an existing employee)
- Whether to opt out of Kiwi Saver (if automatically enrolled when starting a new job)
- Whether to choose their own Kiwi Saver scheme, or leave the choice to their employer or the IRD, who will allocate them to a default scheme.
- Whether to contribute 4% or 8% of gross salary or wages (including any employer contributions).

In addition employees can

- Transfer between schemes at any time however they can only belong to one scheme at a time
- After 12 months of contributing take a contribution holiday – see details under Employee Benefits.

Advantages / Benefits of belonging to Kiwi Saver

The main ones are:

Contributions Holidays

After 12 months in the scheme, Kiwi Savers may apply for a contributions holiday, where members are free to stop and start contributing. The minimum period for a contributions holiday is three months with the maximum period of up to 5 years. At the end of the holiday period, contributions will resume unless the employee applies for a further contributions holiday.

Mortgage Diversion

Kiwi Savers will be able to divert half of their contributions to mortgage repayments after contributing to Kiwi Saver for 12 months or more. Any Government and/or employer contributions cannot be diverted and the diversion can only apply to mortgage repayments on the family home. It cannot be applied to any other investment property.

This option is only available if their Kiwi Saver and mortgage provider offer it - which is not compulsory to.

Kick-start Savings

The government will kick start savings with a contribution of \$1,000 per member. This will be locked in until members are eligible for NZ Superannuation (currently 65 years old) or they have been in the scheme for five years which ever is the later.

First Home Deposit

After 3 years of savings the government will also offer a first home deposit subsidy of \$1,000 for each year of Kiwi Saver membership. This reaches a maximum of \$5,000 for five years. This deposit does not need to be repaid.

This assistance comes with certain eligibility criteria namely:

You cannot have owned any other land previously (in your capacity as a trustees is OK).
Regional house price caps will apply - these will vary depending on where you buy.
Household income limits will apply.

Contribution to Fees

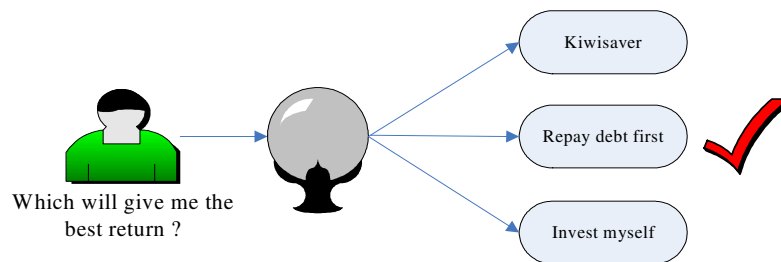
The government will pay \$40 a year into members' accounts to subsidise the fees charged by scheme providers.

Tax Credits

A new tax credit matching member's contributions at 100%, up to \$20 per week (about \$1,040 per year) from 1 July 2007.

Other Issues

- On death the balance of your Kiwi Saver account transfers under the terms of your will.
- At 65 your funds can be taken out as a lump sum or an annuity, tax-free.
- Funds in the scheme are not taken into account for accommodation supplements, but any funds previously withdrawn are.
- Locked in funds are not counted in asset testing for residential care subsidies



Disadvantages of joining Kiwi Saver

Contributions are locked up until you are eligible for NZ Superannuation or 5 years from commencement – whichever is the later. The only exceptions are first home purchase, financial hardship, serious illness and emigration. For younger workers this may seem like a lifetime away.

- Funds cannot be borrowed against or used as security.
- Contributions and Providers are not guaranteed.
- You maybe able to grow these funds better yourself
- Generally your funds are locked in until you reach 65.



Again Sorted have some great checklists to assist employees with their decisions – recommend they visit the site.

While many unions and employees are applauding the introduction of compulsory employer contributions, this fact I am sure will have an impact on the employers decision whether to hire new employees or use contract labour, particularly as the contribution rate can be increased at will by the government of the day.

With the current labour shortages, employers really have little choice but to accept the compulsory contributions but should the economy drop and the labour shortages ease what impact will these contributions have on wage rates and employers staff employment policies.

Useful Links

- www.kiwisaver.govt.nz
- www.ird.govt.nz/kiwisaver
- www.sorted.co.nz

Business Advice Limited

15 Norfolk Street, P O Box 915, WHANGAREI
Phone: (09) 430 2301, Fax: (09) 430 2303, Email: david@bizvice.co.nz
Website: bizvice@bizvice.co.nz

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