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New Zealand Superannuation and Overseas Pensions: Issues and Principles for Reform

The New Zealand Superannuation and Retirement Income Amendment Act 2009

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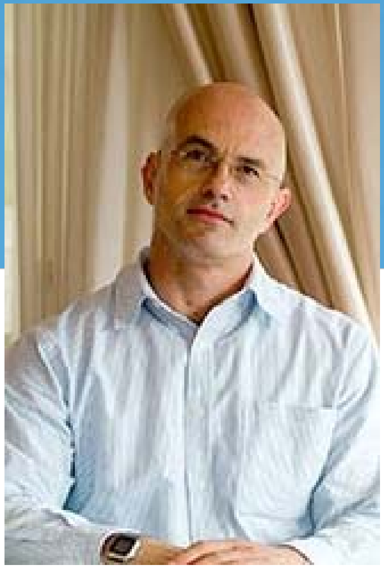

International Issues With Social Security

- If someone spends their working life in more than one country, they may encounter problems with pensions.
- These can arise in several areas:
  - They may be liable to contribute to a social security (pension) scheme in more than one country;
  - Their eligibility or entitlement to receive pensions in one (or both) countries may be reduced or terminated;
  - There may be problems for them receiving a full pension in the country they wish to retire in.

- One reason why cross-border pension issues are sometimes problematic and difficult to resolve is due to the wide variations found in the retirement income policies of different countries.
- For example, there may be different emphases upon Tier I and Tier II pensions and the way those pensions are funded and administered.

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- These differences tend make harmonisation of pensions arrangements across borders more difficult.
- Most countries are aware of the need for their pension schemes to accommodate individuals who migrate in/out during their working lives and incorporate some provision for those individuals although these may not necessarily address all disadvantages a migrant may face.

- Some countries supplement their domestic arrangements for migrants by entering into treaties (known as “social security agreements” or “SSAs”) with other countries to harmonise pension arrangements for individuals who have spent their lives between the two.

How Are These International Issues Dealt With Under NZS?

- The international interface of NZS is particularly important because NZ is a country with substantial migratory flows.
- Liability for social security contributions –This is not a major issue for NZS because it is funded from general taxation.

- Eligibility for NZS for those who migrate to NZ is dealt with under the 10 year residency rule. To get NZS, applicants require 10 years of NZ residency after the age of 20, 5 of which must be after the age of 50. (Note: Totalisation provisions under NZ's SSCs require certain overseas residency to count as NZ residency.)
- In addition, applicants must be "ordinarily resident" in NZ at the time of their application.

- If a migrant receiving NZS is eligible for an overseas pension that is similar to NZS, that pension is deducted from any NZS paid (deduction policy).

- If someone who has lived in NZ after the age of 20 but wishes to retire elsewhere, they *may* be able to receive NZS outside of NZ under the "portability rules". This is subject to 2 major provisos:
  - They must be ordinarily resident in NZ when they apply for NZS.
  - Their ability to receive NZS under "portability rules" may be affected by a SSA if they retire in one of 8 countries.

- The portability rules are in two parts:
  - Pacific Islands portability
  - General portability (applies to all other countries other than the Pacific Island ones).
- Pacific Island retirees can receive NZS at the full rate after 20 years NZ residency. (A proportional payment of NZS is available after 10 years residency.)

- Until 2009, NZS was payable in non-Pacific Island countries after 10 years of NZ residency but only at half rates (50%). There was no proportionality. (This has been changed from 2009.)
- Thus those retiring to the Pacific Islands received a more generous treatment than those retiring elsewhere.
- In both cases NZS is paid without any deduction of New Zealand tax.

- These NZS rules are relatively simple but can be arbitrary in their application and may give rise to major inequities.
- The NZS rules are over-ridden if a person retires to one of 8 countries with which NZ has concluded a SSA. This may not necessarily leave them better off or with a more appropriate treatment.

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Social Security Agreements

- The use of international treaties between two countries to harmonise and co-ordinate fiscal matters is a well established practice.
- It is very common for income tax and is becoming more common for social security and pension matters (at least for some countries).

- In the income tax area, such agreements (known as “double tax agreements”) generally work well to prevent double taxation for cross border transactions.
- SSAs have a more difficult task because of the wide variation in retirement income policies of different countries and the extent the state plays a role providing retirement income.

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How do these International Treaties Interact with Domestic Law?

- Under international law, international treaties are overrule (or are superior to) the domestic law of the two signatory states.

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- In the income tax arena, **double tax agreements** are usually designed to provide taxpayers with a better (or at least equal) treatment that a taxpayer would get under a country's domestic law.
- They are regarded as a "shield not a sword".
- Double tax agreements cannot create a tax liability when there is no underlying provision in the domestic law of one of the states.

- Unfortunately this principle does not appear to apply with SSAs.
- There are instances where some New Zealand SSAs can made a retiree worse off when compared to what they would be entitled to under New Zealand domestic law (general portability rules).

The 2009 Act

- In November 2009 the Government passed the *New Zealand Superannuation and Retirement Income Amendment Act* which changed the **general portability rules** for NZS.

- It did not change anything for those falling within the scope of the 8 SSAs, nor anything for those retiring in NZ with prior overseas residence or foreign pensions despite some earlier statements that some of these matters would be reviewed.
- Thus the scope of the changes under the 2009 Act are quite narrow.

What Changed With The 2009 Act?

- Under the earlier general portability rules, NZS could be paid outside of NZ after 10 years residency but only at half rates (50%).
- That has now changed so that the amount paid outside NZ is determined by the number of years the superannuitant has lived in NZ between the ages of 20 and 65.

- Full payment of NZS outside of NZ is now possible if the superannuitant spent 45 years of their working life in NZ.
- Residency after 65 years no longer counts for general portability but still does for Pacific Islands portability.

- The existing Pacific Island portability rules were not changed and retires can still receive NZS at full rates after 20 years residency.
- What is changed is that retirees to the Pacific Islanders can now apply for NZS from outside New Zealand, which is not permitted for those falling within the general portability rules.

- NZS continues to be paid free of NZ tax overseas. This may mean a superannuitant retiring overseas may enjoy a larger pension than if they had retired in NZ.
- There may be in future some changes to this tax treatment for those who go on an extended overseas trip but do not take up residence in another country.

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Are These Changes An Improvement?

- YES and NO.
- The new formula for general portability is much fairer outcome for those who have worked all their lives in NZ between 20-65 years.
- Reduces the amount payable to elderly migrants retiring outside of NZ when they have contributed little (if anything) during their working lives.

- But still does not address the issue that NZS is paid free of NZ tax which may result in a larger net pension.
- It enhances the privileged status for Pacific Island retirees.
- Does nothing for retirees suffering a disadvantage under one of NZ's SSAs – particularly Australia.

- It addresses only one of the international problems with NZS despite acknowledgment by the Select Committee that there were others.

Other Developments

- Although not linked in any way to the 2009 Act, another important development in 2009 was the negotiation of a new DTA with Australia.
- This DTA (like most of NZ's DTAs) contains an article governing the taxation of pensions (both public and private) between Australia and NZ.

- Under this new DTA, NZ and Australia will mutually recognise the tax-exempt status of each other's private (non-government) pensions.
- This means a NZer can take a private pension to Australia (i.e. one payable by the GSF) and it will now remain tax-free in Australia. The reverse also applies.

- These changes will reduce tax impediments for Australian retirees to move to NZ especially those with substantial Australian superannuation interests.
- Australian occupational pensions are not subject to deduction under section 70 despite being heavily subsidised by the Australian taxpayer.

Remaining Problems

- The 2009 Act did not address a number of major problem areas:
  - That the Australian (and UK) SSCs may make someone worse off than the general portability provisions.
  - NZers retiring in Australia are penalised (over any other country) but provides incentives for Australians to retire in NZ and collect NZS when they have never contributed to the NZ tax base.
  - It does not change anything for retirees who bought overseas pensions to NZ that are deducted from NZS.

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- Fails to address inconsistencies in the application of the deduction policy;
- Continues to provide a privileged position for Pacific Islander retirees;
- Does not address the fiscal risks to NZ in the Australian SSC.

- It is strange why changes to improve the general portability provisions were given such a priority while Parliament deliberately avoided addressing other inequities.
- The changes made will benefit a relatively small number of retirees.