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**OLD AGE WEALTH DECUMULATION IN
NEW ZEALAND**

**LLM SEMINAR PAPER
LAWS 543: ELDER LAW**

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Abstract

This paper is a discussion about, and analysis of, old age wealth decumulation in New Zealand. The way that people acquire and dispose of wealth in New Zealand is very closely related to their age and stage of life, and as people enter into their elder years their income tends to slowly decrease as hours of work are reduced, and their expenditure slowly begins to increase as health and other support needs increase. In New Zealand the government plays a significant role in funding elder care, and has a series of levers which indirectly manage the rate at which wealth is decumulated. The purpose of this paper is to examine and critique some of the key levers that have been set by legislation and government policy that manage wealth decumulation in old age.

This paper argues that there is a tension that needs to be managed by the legislative and policy settings for wealth decumulation, which is that there is a social benefit in helping elderly people retain financial independence for as long as possible, but that there is also a benefit to the state if people pay for as much of their own care as possible.

Word length

The text of this paper (excluding abstract, table of contents, footnotes and bibliography) comprises approximately 7,500 words.

Subjects and Topics

Social Security Act 1964

New Zealand Superannuation

Asset management in old age

New Zealand Superannuation and Retirement Income Act 2001

I Introduction

This paper is a discussion about, and analysis of, old age wealth decumulation in New Zealand. The way that people acquire and dispose of wealth in New Zealand is very closely related to their age and stage of life, and as people enter into their elder years their income tends to slowly decrease as hours of work are reduced, and their expenditure slowly begins to increase as health and other support needs increase. In New Zealand the government plays a significant role in funding elder care, and has a series of levers which indirectly manage the rate at which wealth is decumulated. The purpose of this paper is to examine and critique some of the key levers that have been set by legislation and government policy that manage wealth decumulation in old age.

The first part of this paper outlines some of the key concepts and language that is used in this paper. This paper will then outline a model for conceptualising wealth accumulation and decumulation phases in New Zealand. The third part of this paper will analyse some of the key levers used by the government to manage the rate of wealth decumulation in old age. This paper then goes on to discuss the philosophical underpinnings of having social welfare for people who are elderly, and how those beliefs may change the way that people interact with the way that the state tries to control their rate of asset decumulation. The final part of this paper discusses and critiques some of the key assumptions underlying the way that asset decumulation is approached.

This paper argues that there is a tension that needs to be managed by the legislative and policy settings for wealth decumulation. The tension is that there is a social benefit in helping elderly people retain financial independence for as long as possible, but that there is also a benefit to the state if people pay for as much of their own care as possible.

II Key Concepts and Scope

The language ‘old age’ has been used in this paper because wealth decumulation is not necessarily tied to other signifiers of age. For instance, a person reaching the age at which a person is entitled to retire and receive government funding for that purpose will not necessarily stop working or begin decumulating wealth.

This paper uses some models for describing behaviour. There are some limitations to using these models because they are attempting to stereotype the lifestyle and health of a very broad range of people who happen to be over 65. It is likely that there will be some people who at 65 have health issues that make these models inappropriate. Equally there

are some people who at 90 are still actively travelling the world without any health issues. This paper uses these models as a way to try to understand the broader picture, but acknowledges that it does provide a very limited view.

Wealth decumulation in this context means a reduction of personal, financial wealth. As the focus of this paper is on wealth decumulation in old age, it does not regard other processes of wealth decumulation which are set in place by life events that would typically impact younger people. Examples of other life events that would also trigger a government mandated process of wealth decumulation but are outside of the scope of this paper are unemployment, long term illness, or entering full time study. The triggers, thresholds and rationale are quite different for each.

This paper does not discuss in detail the question of whether the state ought to be one of the main vehicles for elder care in New Zealand. A cultural critique of this paper would raise questions of whether there are other ways that society could ensure that people who are elderly have a high standard of welfare, for example by better supporting families to care for elderly people, or by developing a local community support model. The state as the main vehicle for elder welfare support is a reasonably individualistic approach which could be critiqued as being somewhat impersonal and clinical from a more collectivist tradition.

III Phases of Wealth Accumulation and Decumulation in New Zealand

A Introduction

There are phases of wealth accumulation and decumulation that align with different ages and stages. To understand and discuss these different phases, a model can be applied of three general phases. The three general phases are accumulation, holding, and decumulation.¹ These can be broadly be aligned to the three stages of retirement proposed by the Commission for Financial Capability (CFC);² discovery, endeavour and reflection.³ It is useful to align the two frameworks because the first framework helps to

¹ Johnson, Dianne, Worthington, Andrew, Brimble, Mark “Put it on the house: the promising, largely untapped potential for Australian home equity in retirement” (2014) 1 JASSA 34 at 34

² The Commission for Financial Capability is headed by the Retirement Commissioner. The Retirement Commissioner is empowered by the New Zealand Superannuation and Retirement Income Act 2001 Part 4.

³ Commission for Financial Capability “The Three Stages of Retirement” Commission for Financial Capability- Building Wealthy Lives <www.cffc.org.nz/retirement/the-three-stages-of-retirement/>

describe financial net outcomes, and the CFC framework describes other behaviour that drives the financial behaviour leading to those outcomes.

A useful diagram produced by the CFC that describes how money is spent throughout retirement is below. It shows the way that money is spent throughout retirement and also the level of income that people receive throughout retirement.

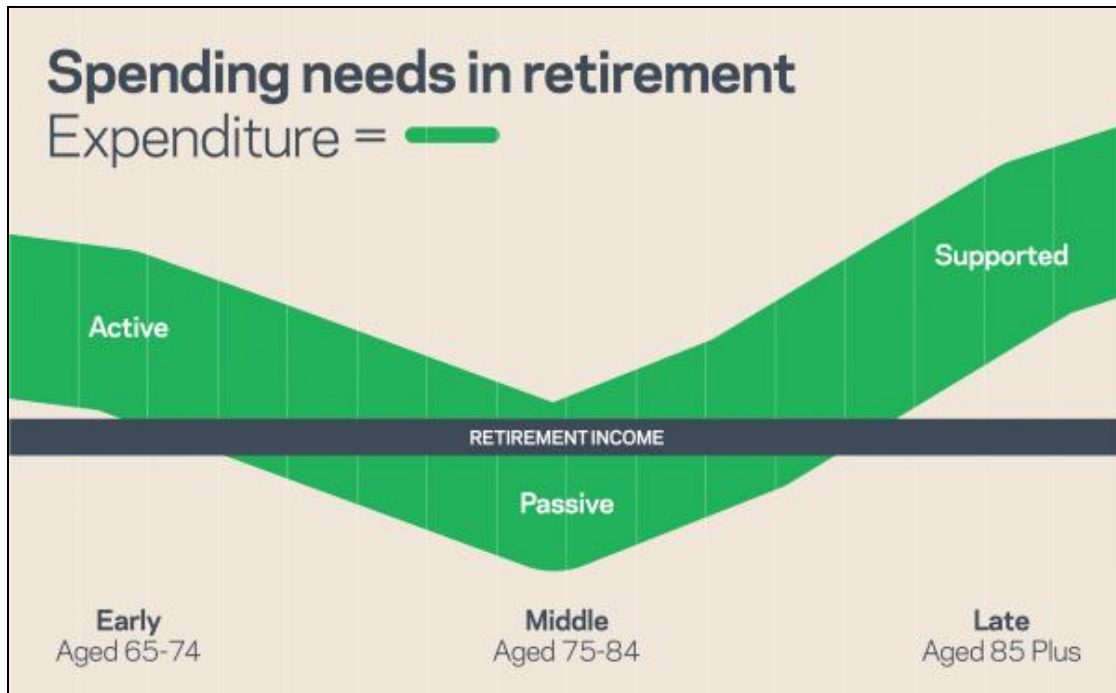


Figure 1- Spending needs in retirement (New Zealand Commission for Financial Capability)

B Accumulation

The accumulation phase does not align with the CFC framework because it generally takes place before retirement (although many people continue to accumulate wealth during retirement from investing). For the purpose of this paper, the accumulation phase describes the time that comes before retirement, when people are working and generating positive income. During the accumulation phase people are generally motivated, or encouraged, to save for their retirements in an attempt to smooth “the marginal utility of consumption across different time periods.”⁴

⁴ Aylit Tina Romm “The Effect of Retirement Date Expectations on Pre-retirement Wealth Accumulation: The Role of Gender and Bargaining Power in Married US Households” (2015) 36 JFEI 593 at 594

C Holding (Discovery and Endeavour)

The CFC framework describes the early stages of older age as the ‘Discovery’ stage. The category is intended to describe people aged 65-74, who may be working, retired or semi-retired. People within this category often have more time for leisure activities and are “physically and mentally capable of living a fairly active lifestyle.”⁵ It can be the most expensive phase of retirement because people want to do the things that they always wanted to do but never had time for, and live “the stereotypical retirement dream.”⁶ This means that the expenses arise from things like travel, new hobbies and new leisure activities. An important point to note is that many of the costs are discretionary and can be managed.

The ‘Endeavour’ stage describes ages 75-85, which characterises those years as a time where the pace of living slows down because energy levels dip and people tend to want to settle into a routine that gives comfort and security and is in general more easily sustainable.⁷

In this paper, the ‘Discovery’ and ‘Endeavour’ stages have been aligned with the holding phase because while there are costs of living that cause asset decumulation, many of those costs are discretionary and manageable. The decisions made about keeping a balance between maintaining wealth or maintaining quality of life are largely in the hands of the individuals, albeit within the constraints of their personal financial position pre-retirement, and in response to legislated and policy incentives.

D Decumulation (Reflection)

The ‘Reflection’ stage of life is intended to describe the lifestyle and spending needs of people aged 85+.⁸ It is characterised as the time of life when “health and finances may limit choice” and people become more dependent on help from others.⁹ The CFC describes two different paths financially that the ‘Reflection’ stage can take. This stage

⁵ Commission for Financial Capability “The ‘Discovery’ Stage” Commission for Financial Capability-Building Wealthy Lives < www.cffc.org.nz/retirement/the-three-stages-of-retirement/stage-one-65-74/>

⁶ Above n 5

⁷ Commission for Financial Capability “The ‘Endeavour’ Stage” Commission for Financial Capability-Building Wealthy Lives < www.cffc.org.nz/retirement/the-three-stages-of-retirement/stage-two-75-84/>

⁸ Commission for Financial Capability “The ‘Reflection’ Stage” Commission for Financial Capability-Building Wealthy Lives < www.cffc.org.nz/retirement/the-three-stages-of-retirement/stage-three/>

⁹ Above n 8

can be very low cost because the pace of daily life slows down to accommodate new physical and mental health limitations. However it can also be very high cost if people have many health issues or need support from professional carers.¹⁰

The 'Reflection' stage of life has been aligned with the decumulation phase in this paper because this stage of life can be financially characterised as a time when the cost of living increases substantially, but those costs cannot be managed in a way that helps to maintain wealth. A person who is in need of assistance, residential care or ongoing medical treatment does not have much choice about whether to use the services they need, or not. In this way it is quite different to the costs of the 'Discovery' stage.

E Conclusion

It is useful to understand the three stages of retirement, and align them to the life phases of wealth accumulation and decumulation. In reviewing how the law regulates and incentivises certain spending behaviours it is important to understanding the behaviour and needs of the people being regulated. Categorising the different stages of life can help us to analyse which behaviour is being, or should be, influenced at each stage.

The next part of this paper outlines some of the key ways that the government regulates and incentivises the spending behaviours of elderly people.

IV Government Levers Controlling the Rate of Wealth Decumulation

A Introduction

Government benefits and subsidies for older people can be viewed from two perspectives. From one perspective, benefits and subsidies can be viewed as the government providing benefits and a minimum standard of living for older people so that their personal savings do not run out too quickly. From the opposite perspective, the asset and income testing elements mean that material wealth is eroded until it meets the threshold for subsidy entitlement. Both of these perspectives are about government legal and policy settings controlling the rate at which older people decumulate their material wealth: not too fast, and not too slow.

¹⁰ Above n 8

This part of the paper outlines some of the main ways that the government manages the rate at which older people decumulate wealth. In New Zealand the government plays a central role in elder welfare. Kiwisaver is a government incentivised saving initiative¹¹ primarily targeting people in the accumulation phase of life, New Zealand Superannuation (NZ Super) is a benefit that all people over the age of 65¹² are entitled to regardless of other income.¹³ While living independently, there are many services that are subsidised (like health care and SuperGold Card benefits¹⁴) and access to some subsidies is asset or income tested. When living in residential care, the government subsidises the cost of certain minimum care requirements, subject to asset and income testing.

B Pre-Retirement Savings Incentives- KiwiSaver

KiwiSaver is a government incentivised saving initiative that is largely targeted at people in the accumulation phase of life.¹⁵ This outline of KiwiSaver will briefly explain the KiwiSaver initiative, the potential for it to increase personal retirement savings significantly through property ownership and investment funds, and limitations of the initiative.

The KiwiSaver scheme is retirement savings scheme which has three sources of contribution: personal, employer and government. When enrolled in the scheme, people have a percentage of their gross income deducted and deposited into their KiwiSaver account. The minimum personal contribution is 3% of gross income.¹⁶ Employers must match the personal contribution (up to 3% of the employee's gross income).¹⁷ The government makes a maximum annual member tax credit contribution of up to \$521.43 for active contributors.¹⁸

¹¹ KiwiSaver "What is KiwiSaver?" KiwiSaver Poua he Oranga
<<http://www.kiwisaver.govt.nz/new/about/>>

¹² New Zealand Superannuation and Retirement Income Act 2001, s 8

¹³ Ministry of Social Development "Getting other Income" Work and Income Te Hiranga Tangata
<www.workandincome.govt.nz/eligibility/seniors/superannuation/other-income.html>

¹⁴ SuperGold Cards are an entitlement card issued pursuant to the Social Security Act 1964 s 132A, and regulated by the Social Security (SuperGold Card) Regulations 2007. Holders of SuperGold cards can receive a range of discounts from businesses, government concessions including free off-peak public transport, and discounted services from the territorial local authority.

¹⁵ KiwiSaver Act 2006 s 3

¹⁶ KiwiSaver Act 2006 s 16

¹⁷ KiwiSaver Act 2006 s 101D

¹⁸ Income Tax Act 2007 s MK 4

People are automatically opted in to KiwiSaver when they start a new job, and must opt out within a six week window that begins two weeks after the start of employment, and ends eight weeks after the start of employment. Once a person is enrolled in KiwiSaver they cannot withdraw, but they can take a contributions holiday for up to five years. Funds can only be withdrawn before the person turns 65 under very limited circumstances.¹⁹

KiwiSaver funds are not guaranteed by the government.²⁰ They are instead privately run investment funds. People can decide which investment companies they want managing their funds, and the risk profile they would like their funds invested with.²¹

The explicit purpose of the KiwiSaver initiative is to help people to save for their retirement²² and this is delivered in two ways. The first is the reasonably straightforward approach where the personal KiwiSaver accounts have money deposited into them throughout the working life of people who are enrolled in KiwiSaver, and the amount in the account receives a compounding return on the investment. People may withdraw their saved funds from KiwiSaver when they reach the age of New Zealand superannuation entitlement.²³ This effectively means people who are enrolled in KiwiSaver from the beginning of their working lives will save 6% of their annual net income for retirement, which after 40 years of working will represent an amount that is significant when compared to each savers pre-retirement annual income.

The second way that KiwiSaver helps people to save for retirement is that the KiwiSaver contributions can be withdrawn early for the purchase of a first home. In New Zealand's historically buoyant housing market²⁴ this is essentially another type of retirement wealth saving opportunity. In New Zealand a comparatively high proportion of people's net worth is invested in property ownership²⁵ and home equity release products have the

¹⁹ KiwiSaver Act 2007 ss 9- 37

²⁰ KiwiSaver Act 2007 s 161

²¹ KiwiSaver Act 2007 s 45

²² Above n 11

²³ KiwiSaver Act 2007 Schedule 1 s 4

²⁴ The Treasury "New Zealand Economic Chart Pack Key New Zealand Macroeconomic and Financial Market Graphs" (2015) The Treasury at 12

²⁵ Mathew Arcus, Dr Ganesh Nana Intergenerational and Interfamilial Transfers of Wealth and Housing (Centre for Housing Research Aotearoa New Zealand, Wellington, 2005) at 10

potential to play a significant role in how people privately fund their retirement.²⁶ By making the saving from the KiwiSaver initiative available for first home purchases, the government is incentivising a secondary fund for directing retirement savings which takes the immediate form of mortgage repayments.

Both of these delivery models are government incentivised, privately administered saving schemes. It means that people are saving, and the risk profiles for retirement savings are diversified across different investment markets, and individuals are being incentivised to prepare for a future where they are not entirely dependent on the government for financial support in old age. However, it also means that personal retirement savings are closely tied to the performance of investment markets, and an ill-timed stock market and property market ‘bust’ cycle could erode all of the gains made by government intervention in the personal saving habits of New Zealanders.

It is also important to note that early research undertaken about the impact of KiwiSaver membership on expected retirement incomes suggests that the impact is negative or negligible, meaning that people are not saving much extra money, despite being enrolled in KiwiSaver.²⁷ As KiwiSaver is relatively new²⁸ this early data may not be indicative of the overall longer term impact of the initiative.

C NZ Super

NZ Super is a large part of the elder welfare support delivered by the New Zealand government. It is a universal pension. To be eligible for NZ Super, recipients must be aged over 65, and have lived 10 years in New Zealand since age 20, five of those years since turning 50.²⁹ People can continue to work while receiving NZ Super.³⁰ The amount of NZ Super that a person receives is determined based on whether they are in a married, civil union or de facto relationship or are single, and whether they live alone or in shared accommodation.

²⁶ Judith A. Davey “Home equity release products in New Zealand risks and opportunities: report to Retirement Commission / Judith A. Davey for the New Zealand Institute for Research on Ageing” (2007) New Zealand Institute for Research on Ageing at 21

²⁷ David Law, Grant M Scobie “KiwiSaver and the Accumulation of New Wealth” (2014) New Zealand Treasury Working Paper 14/22 at 22

²⁸ The initiative began in 2007

²⁹ New Zealand Superannuation and Retirement Income Act 2001 ss 8, 11

³⁰ Above n 13

From 1 April 2016 a single person living alone receives \$385 weekly, and people who are married, or in a civil union or de facto partnership each receive \$296 weekly (i.e. \$592 per week jointly). For comparison purposes, in New Zealand in 2016, a person working 40 hours a week on minimum wage (\$15.25)³¹ earns \$610 weekly. A person earning the New Zealand Living Wage³² (\$19.80)³³ earns \$792 weekly. The median income from wages and salaries in the year to June 2015 was \$882 weekly.³⁴

	NZ Super (Married, civil union or de facto person) from 1 April 2016	NZ Super (Single person living alone) from 1 April 2016	Minimum wage from 1 April 2016 (40 hours)	New Zealand Living Wage 2016 from 1 July 2016 (40 hours)	Median income from wages and salaries July 2014-June 2015
Weekly income per person	\$296	\$385	\$610	\$792	\$882

Based on this comparative information it is reasonably clear that for most people reaching the age of 65 NZ Super will be significantly less than the income that they are accustomed to living on. Even with a severe reduction in living standards, most people will need to supplement NZ Super with the wealth they have accrued in the course of their working life.

This is compounded by the impact of an increase in life expectancy. A female born in 1951 who turns 65 in 2016 has a life expectancy of 88.2-89.6.³⁵ This means that people

³¹ Minimum Wage Order 2016 s 4

³² The “New Zealand Living Wage” is an hourly rate set by the Family Centre Social Policy Unit and represents the hourly rate needed to pay for the necessities of life and participate as an active citizen in the community. It is based on a family unit of two working adults (one full-time and one part-time) with two dependent children. (<http://www.familycentre.org.nz/>)

³³ The Family Centre Social Policy Research Unit “Living Wage Aotearoa New Zealand 2016 Update” (2016) The Family Centre Social Policy Research Unit <https://d3n8a8pro7vhmx.cloudfront.net/nzlivingwage/pages/89/attachments/original/1456712781/Living_Wage_update_2016_FCSPRU_2.16.pdf?1456712781>

³⁴ Statistics New Zealand “New Zealand Income Survey: June 2015 quarter” (2 October 2015) Statistics New Zealand Tauranga Aotearoa <www.stats.govt.nz/browse_for_stats/income-and-work/Income/NZIncomeSurvey_HOTPJun15qtr.aspx>

³⁵ Statistics New Zealand “How long will I live?” (3 March 2016) Statistics New Zealand Tauranga Aotearoa <www.stats.govt.nz/browse_for_stats/health/life_expectancy/how-long-will-I-live.aspx>

who begin receiving NZ Super in 2016 will need to plan their retirement on the basis that their life savings will need to supplement their income for the next 25 years. This means that there is an incentive to carry funds for as long as possible in anticipation of having to make the savings last for a very long time.

When relying on NZ Super as the main source of income, there is an incentive to decumulate assets to maintain a standard of living, and at the same time keep a low rate of decumulation in anticipation of living for many more years and needing to smooth consumption over that time.

D Subsidies for Independent Living

There are also several subsidies that people over the age of superannuation entitlement can receive. Some are income and asset tested, and others are not. A non-comprehensive overview of the government subsidies and benefits available to older people is summarised in the table below. These benefits are not exclusively available to older people.

Universal Subsidies/ Benefits	Income and Asset Tested Subsidies/ Benefits
Super Gold Card ³⁶	Community Services Card ³⁷
Prescription Subsidy Card ³⁸	Disability Allowance (medical alarm rental and monitoring) ³⁹
High Use Health Card ⁴⁰	Temporary Additional Support (essential home telephone costs) ⁴¹
	Accommodation Supplement ⁴²
	Rates Rebate Scheme ⁴³
	Special Needs Grant ⁴⁴
	Home Help ⁴⁵

³⁶ Social Security (SuperGold Card) Regulations 2007 r 8

³⁷ Health Entitlement Card Regulations 1993 r 8

³⁸ Health Entitlement Card Regulations 1993 r 23

³⁹ Social Security Act 1964 s 69C

⁴⁰ Health Entitlement Card Regulations 1993 r 20

⁴¹ Social Security (Temporary Additional Support) Regulations 2005 r 6

⁴² Social Security Act 1964 s 61EA

⁴³ Rates Rebate Act 1973 s 3

⁴⁴ Special Needs Grants Programme 1998, pursuant to the Social Security Act 1964 s 124(1)(d)

These subsidies and benefits slow the rate of asset decumulation for older people, or can alleviate the effects of poverty, depending on the starting financial position of the older person. Universal entitlements cover local transport and, for people with higher healthcare needs, subsidies for prescriptions and medical appointments. The income and asset tested subsidies and benefits cover a wide range of services. The income thresholds for those subsidies and benefits are generally higher than the NZ Super payment amount, which means that in general, for a person whose sole income was NZ Super, the asset testing thresholds (if any) are most likely to determine eligibility. These subsidies mean that while living independently the rate of wealth decumulation is slower than what it would be without the subsidies.

E Subsidies for Residential Care

Residential care in this context means long term care in a hospital or rest home, when the older person will reside at the hospital or rest home.⁴⁶ Subsidies for residential care in New Zealand are means tested.⁴⁷ There are several eligibility requirements for the Residential Care Subsidy, but for the purpose of this paper the focus is on the financial means assessment element of eligibility.

There are two components of the financial means test, which are an asset test and an income test.⁴⁸ The asset test assesses the value of the assets belonging to the applicant and their spouse or partner and includes all assets that are capable of being sold, or any assets that were gifted⁴⁹ within the last 5 years⁵⁰ that exceeded the allowable gift value (\$6,000 each year).⁵¹ There are two thresholds for asset testing. The thresholds for the asset tests are \$218,973 (Threshold A)⁵² or \$119,915 (Threshold B).⁵³ The applicable

⁴⁵ Home Help Programme 2004, pursuant to the Social Security Act 1964 s 124(1)(d)

⁴⁶ Ministry of Social Development “Residential Care Subsidy” Work and Income Te Hiranga Tangata <www.workandincome.govt.nz/products/a-z-benefits/residential-care-subsidy.html>

⁴⁷ Ministry of Health “Long-term Residential Care for Older People- What you need to know 2012” (1 July 2012) Ministry of Health Manatū Hauora <www.health.govt.nz/system/files/documents/publications/long-term-residential-care-older-people-2012-jan16.pdf>

⁴⁸ Ministry of Health “Income and asset testing” (28 April 2016) Ministry of Health Manatū Hauora <www.health.govt.nz/our-work/life-stages/health-older-people/long-term-residential-care/income-and-asset-testing>

⁴⁹ Social Security Act 1964 Part 2 Schedule 27

⁵⁰ Social Security (Long-term Residential Care) Regulations 2005 r 8

⁵¹ Social Security (Long-term Residential Care) Regulations 2005 r 9

⁵² Social Security Act 1964 Part 1 Schedule 27 cl 1(2)

threshold is primarily chosen based on whether the applicant has a spouse or partner, and whether that spouse or partner also requires residential care.⁵⁴ The threshold represents the point at which the assets of the applicant have been decumulated to a level where the government begins paying for the minimum standard of residential care.

The income means assessment includes any income in the regular sense of the word, and also includes 50% of life insurance policy annuities received, 50% of superannuation schemes that are not NZ Super or overseas pensions, and any benefits received.⁵⁵ The annual income thresholds depend on a range of personal factors.

The detail of asset and income testing for eligibility for the Residential Care Subsidy is very important, because until a person has run out of assets and income down to the specified thresholds they must pay the maximum contribution for their own residential care.⁵⁶ The maximum contribution is set by a New Zealand Gazette notice and varies by territorial local authority. In July 2015 the lowest maximum weekly contribution was set at \$875.35 (in Otorohonga, South Waikato, Buller, Grey, Westland, Waimate, Waitaki, Clutha, Southland and Gore Districts) and ranged to the highest maximum weekly contribution of \$961.94 (Auckland City).⁵⁷ The maximum weekly contributions reflect the contract price for residential care agreed between District Health Boards and residential care providers in the Age-Related Residential Care Services Agreement (ARRCSA).⁵⁸ The ARRCSA sets out the minimum standards for residential care,⁵⁹ and residents can pay extra if they want goods or services that are not included in the agreement.⁶⁰

What this means is that people who have assets or income above the specified thresholds must pay for their own residential care, at a rate of at least \$875.35 per week until their assets or income fall below the thresholds. It means that long term residential care causes

⁵³ Social Security Act 1964 Part 1 Schedule 27 cl 1(3)

⁵⁴ Social Security Act 1964 Part 1 Schedule 27 cl 2

⁵⁵ Social Security Act 1964 Part 3 Schedule 27 cl 5

⁵⁶ Social Security Act 1964 s 140

⁵⁷ “Maximum Contribution Applying in Each Territorial Local Authority Region from 1 July 2015” (18 June 2015) 68 *New Zealand Gazette* 3619

⁵⁸ Ministry of Health “Maximum contribution questions and answers” (20 July 2007) Ministry of Health Manatū Hauora <www.health.govt.nz/our-work/life-stages/health-older-people/long-term-residential-care/maximum-contribution/maximum-contribution-questions-and-answers>

⁵⁹ Ministry of Health “Age Related Care Services Agreement” (2013) Ministry of Health Manatū Hauora <www.health.govt.nz/system/files/documents/pages/arrc-agreement-final-2013.pdf>

⁶⁰ Above n 58

rapid wealth decumulation which continues until the person leaves residential care or reduces their total wealth to the specified threshold. These legislative settings speed up the rate of wealth decumulation in what are likely to be the final years of an older person's life.

F Conclusion

This part of the paper has outlined some of the key legislative and policy settings that the government can control that encourage or require asset accumulation or decumulation. The NZ Super payment rates are set at a level where most people leaving full time employment will need to slowly supplement it to maintain their quality of life. Government subsidies for people over 65 make the daily costs of living independently less than for people under 65, and the increasing costs of healthcare less onerous. However the subsidies do not remove those costs entirely. These settings mean that while living independently the daily drain on savings is reduced and wealth is slowly decumulated over many years. However, upon reaching the point where long term residential care is required, the care subsidy thresholds are set in a way which rapidly erodes wealth that has been maintained until that point. This can be viewed as a way of exhausting the financial reserves of people to pay for their own care near the end of their lives. It is also a way of reducing the amount of intergenerational wealth transfer.

The next part of this paper will discuss some of the philosophical principles that underpin these legislative and policy settings.

V Philosophy of Wealth Decumulation

A Introduction

This part of the paper is an overview of the philosophy behind the government approach to managing the rate of asset decumulation for older people. The macroeconomic policy issue is that people are living for longer,⁶¹ the proportion of the population that is aged

⁶¹ Statistics New Zealand "How will New Zealand's ageing population affect the property market?" (23 April 2013) Statistics New Zealand Tauranga Aotearoa <http://www.stats.govt.nz/browse_for_stats/population/estimates_and_projections/ageing-population-property-market.aspx#evolving>

over 65 is increasing,⁶² and the question becomes: how do we pay for the ageing population, both in a private and public sense?

The way that the government manages the rate of wealth decumulation in part reflects public decisions about how much of the cost of old age should be privately borne, and how much should be publicly carried. The publically carried costs must be balanced in the annual government budget against competing priorities like education, maternity and child health care, economic development initiatives and national infrastructure investment.

This part of the paper outlines some of the rights and duties that underlie the way that the New Zealanders think and act about the question of who should pay for retirement. Those values underpin the way that people vote, and by extension the way that the New Zealand government sets its incentives and subsidies relating to elder welfare.

B Personal Responsibility- Libertarian and Individualistic Perspectives

One of the principles underlying the Social Security Act 1964 is captured in the succinct section title “personal obligation to pay for care”⁶³. Liberal individualistic societies are based to varying degrees on the principle that people are rational, utility maximising actors who are best placed, and ought, to make decisions for their own welfare and consumption smoothing. Under this conception, one element of people’s welfare includes decisions about funding their retirement. The way that people choose to act reveals their welfare preference decisions.⁶⁴

At the logical edges of this view that people are utility maximising rational actors, there would be no purpose for a social welfare system. Every person would choose their preferred distribution of expenditure over their lifetime, deciding whether to save and how much to save based on their preferences. There would be no requirement for people to pay taxes to support a welfare system. Instead, people would have a duty to save for their own retirement, and a failure to do so would be a calculated decision based on

⁶² Above n 61

⁶³ Social Security Act 1964 s 139

⁶⁴ Alan M. White “Credit and Human Welfare: Lessons from Microcredit in Developing Nations” (2012) 69 Wash & Lee L Rev 1100

maximising personal utility, and a risk assessment of how long the individual expected to live. This can be characterised as a “save as you go” model for funding retirement.⁶⁵

Relying on a concept of rational actors to pay for their own retirements is somewhat problematic because people are often overly optimistic about their future financial position,⁶⁶ and value the preferences of their current selves over their future selves.⁶⁷ It is also problematic because some people earn just enough to get by, and a failure to save is not expressing a preference against saving, but an inability to save due to insufficiency of income.⁶⁸ The real value of savings and investments can also be affected by circumstances that individuals cannot control, like inflation, economic downturns and low interest rates.

The New Zealand approach is not at the extreme end of this thought process. As previously discussed, NZ Super is universal and a failure to save during the accumulation phase does not spell destitution in the decumulation phase.

The purpose of the Social Security Act 1964 is to alleviate hardship, where people should use the resources available to them before using social security.⁶⁹ The first recourse for people seeking social assistance should be to their own resources, and pay for their own care where appropriate.⁷⁰ When applied to residential care subsidies, asset and income thresholds soften the general social security principle. Based on the relatively low weekly NZ Super payments that people who are over 65 receive, the current legislative settings appear to support a view that New Zealanders are prepared to fund their own retirement until their personal resources have been reduced to a point where state support is required. When the person who is elderly is living independently, the point where state support is required is represented by entitlement to additional income and asset tested subsidies and benefits. When the person who is elderly requires residential care, the point where state support is required is represented by entitlement to the Residential Care Subsidy.

⁶⁵ Andrew Coleman and New Zealand Treasury “To Save or Save Not: Intergenerational neutrality and the expansion of New Zealand Superannuation” (2013) Commission for Financial Capability- Building Wealthy Lives < <http://www.cffc.org.nz/assets/Documents/RI-Review-2013-To-save-or-save-not.pdf>> at 3

⁶⁶ Above n 64, at 1103

⁶⁷ Above n 64, at 1103

⁶⁸ Above n 64, at 1101

⁶⁹ Social Security Act 1964 s 1A

⁷⁰ Social Security Act 1964 s 1A

From a public funding perspective, these settings mean that older people are supported to be financially independent for as long as they live outside of residential care, but once entering residential care fund their own care to the greatest extent possible. This is good for public spending because it theoretically reduces the need for state financial intervention for people who are elderly and living independently, and also reclaims some of the wealth that NZ Super has enabled people who are elderly to retain throughout their retirement years.

From a private funding perspective, this can lead to three issues. The first is that this approach is not equitable between the successors of people who spent a large amount of time in residential care, and those who do not. The second issue is that it means that people who contemplate spending a large amount of time in residential care will also contemplate the possibility that their accumulated wealth will be eroded to pay for that residential care. In both cases, people who expect to leave a positive financial legacy for their successors and derive meaning from their ability to continue to provide for their successors, may choose instead to subvert the asset testing mechanisms that exist for public funding purposes. The third issue is that there may not be any intergenerational wealth transfers made, which, depending on the people involved and their expectations about making or receiving intergenerational wealth transfers, can have a significant personal impact.

The purpose of social security can be explained as a last recourse for when personal resources are exhausted, and a safety net to bridge the gap between theories of rational people and the reality of how people actually behave.

C Entitlement to State Support- Justifying the Subversion of Income Testing

There are alternative ways to explain the purpose and existence of social security. An alternative view is that people are entitled to state support during their retirement because they have paid taxes throughout their working lives which were used in part to support older people who were already retired, in a “pay as you go” funding model.⁷¹ In an implicit intergenerational social contract, people expect that in return the state will provide for them when they retire.⁷²

⁷¹ Above n 65

⁷² David Thomson “The Intergenerational Contract- Under Pressure From Population Ageing” in Eekelaar and Pearl (eds) *An Ageing World* (Clarendon Press, London, 1989) 369 at 371-373

A variant of this is when tax deductions are itemised on pay records by where each percentage of tax is being spent- people seeing an aggregated amount paid to the 'superannuation tax fund' may see this as an implicit promise that they will receive back the same amount that they put in, and regard that social funding as rightfully theirs.

This understanding of social welfare for people who are elderly can drive entirely different behaviours and beliefs. When people see state assistance as an entitlement, it can lead to people seeing their personal savings as additional to the requirements of paying for day to day life or intensive medical care. This may lead people to prioritise other uses of their wealth later in life, or to have expectations about how it will be used.

In particular, people may expect to make intergenerational wealth transfers so that their children or grandchildren have a better financial starting position in life. Under this framework of entitlement under an implied intergenerational contract, people may view it as reasonable to preserve their wealth in ways that subvert the rapid wealth erosion settings of residential care subsidies.

From a public funding perspective, a system where everyone expects the majority of their old age costs to be paid for by the state would be extremely expensive. In a scenario where everyone who has private assets has them obscured from asset testing for residential care subsidies so that they can take full advantage of the subsidies available, the cost of elder welfare borne by the state would increase. An increase in state funded residential care costs would mean that either a greater proportion of tax income would have to be dedicated to elder care and funding for other state services reduced to compensate for the increase, or that the amount of total tax income would have to be increased by raising taxes.

From a private funding perspective, approaching the funding of retirement from this perspective is much easier to plan for because the plan is that the state will do all of the planning on behalf of the individual. It also means that the ability to make intergenerational wealth transfers is safeguarded. It does however require a certain amount of forethought to obscure any assets above the asset testing threshold, and a certain amount of faith that the implied intergenerational contract will be honoured. It also means that the opportunity to gather personal wealth will be impeded by a lifetime of higher taxes.

It is worth noting that people may not appreciate how much support people who are elderly receive in terms of social security without access to other social security benefits

or subsidies. People can expect to live for 25 years after they turn 65,⁷³ which amounts to approximately \$500,000 received in the form of NZ Super. In the context of the amount people pay in tax over a lifetime this is a reasonably high return on investment even without regarding any additional benefits or subsidies. This rate of return is particularly good when all other taxpayer funded services that people receive throughout their lifetime like education, healthcare and infrastructure are paid out of those same taxes.

The table below shows some estimates at total tax paid over a working life. This is a estimate does not adjust for inflation, or career and income progression. Also, while life expectancy is increasing, not all people will live long enough to receive these welfare returns.

	Minimum wage from 1 April 2016 (40 hours)	New Zealand Living Wage 2016 from 1 July 2016 (40 hours)	Median income from wages and salaries July 2014- June 2015	\$100,000 annual income⁷⁴
Weekly income per person.	\$610	\$792	\$882	\$1,923
Lifetime income (52 weeks for 40 years).	\$1,268,800	\$1,647,360	\$1,834,560	\$4,000,000
Lifetime income tax paid based on flat 20% income tax rate.	\$253,760	\$329,472	\$366,912	\$800,000
Lifetime income tax paid based on flat 30% income tax rate.	\$380,640	\$494,208	\$550,368	\$1,200,000

D Analysis

The two approaches can be seen as having an equal net effect because under the more libertarian view people pay less tax and use those savings to fund their own retirements. In the implied intergenerational social contract view, people pay more taxes (or receive

⁷³ Above n 35

⁷⁴ 5.9% of New Zealanders earned \$100,000+ at the time of the 2013 Census <<http://www.stats.govt.nz/Census/2013-census/profile-and-summary-reports/quickstats-income.aspx>>

fewer other state services) and can rely on the state to maintain them in their old age. There is a difference in outcome, which is that, under the intergenerational social contract model, those who are wealthy ensure that their children retain that wealth, whereas under the libertarian model the wealth is redistributed into the economy generally. This means that the libertarian model penalises people who are low income earners throughout their lives, and the implied intergenerational social contract model helps maintain social financial inequality, where wealthy families keep their wealth through generations⁷⁵ while general taxpayers fund their retirement.

The New Zealand legislative approach is explicitly closer to the libertarian model of how old age should be funded. However, the behaviour of people within the system is also influenced by which model they personally subscribe to. When the state has welfare settings following a moderated libertarian model, it is best for the state and all taxpayers if people act consistently with that model. It is best for individuals to maximise their asset retention by subverting those legislated thresholds, which they may justify from a perspective of implied intergenerational social contract approach.

This response by individuals can create an apparent injustice: to those who consciously choose to follow the libertarian model and decide to pay their own way as much as possible out of a sense of civic duty or personal responsibility, and to those who do not have access to the financial and legal advice that would enable them to obscure their assets.

The incentives on the state and on individuals are misaligned so that there are perverse outcomes. In New Zealand has been estimated that there is at least one trust for every 18 people.⁷⁶ While there are many purposes for establishing a trust, it has been identified by the Law Commission that the residential care subsidy asset testing threshold “is often credited with creating a significant incentive for people to transfer assets to a trust.”⁷⁷ There are provisions that enable the Ministry of Social Development to “look through” trusts and count income and assets that have been transferred and gifted beyond the gifting limits prescribed in the legislation.⁷⁸ However provided the gifting limits have been followed, assets transferred to a trust can be excluded from asset testing.⁷⁹

⁷⁵ Above n 25 at 11

⁷⁶ Law Commission *Review of Trust Law in New Zealand: Introductory Issues Paper* (NZLC IP19, 2010) at 6

⁷⁷ Law Commission *Some Issues with the Use of Trusts in New Zealand* (NZLC IP20, 2010) at 12

⁷⁸ Above n 77 at 33, 34

⁷⁹ Above n 77 at 34

E Conclusion

This part of the paper has been an outline of two of the key ways that people and the state can approach the funding of retirement. The first is a moderated libertarianism, where people are expected to fund their own care as far as possible, but there is a social safety net available when needed. This is closest to the current legislative settings as illustrated by many of the higher value benefits and subsidies being income and asset tested, and by the NZ Super payment rate being somewhat below the median income of New Zealanders. The second is an approach where there is an implied intergenerational social contract where people are entitled after a lifetime of paying taxes to get out what they have put in over a lifetime.

People who subscribe to the second view may feel entitled to subvert the mechanisms of government settings because they have been contributing to the state social security fund for the length of their working lives. This subversion is good for preserving individual wealth, but has negative outcomes for the state, and inequitable outcomes for others who do not subvert the asset testing either by goodwill or lack of opportunity. One method for subverting asset testing mechanisms is the establishment of trusts.

VI Critique from Alternative Perspectives

A Introduction

This part of the paper critiques the existing legislative and policy settings, and the underpinning rationale, from the perspective of gender and socioeconomic status. As discussed earlier in the paper, the state is a large supplier of elder welfare support through a variety of mechanisms. These mechanisms are set so that private wealth is decumulated at a rate appropriate to the stage of life and level of independence that people have. This helps to prevent people from living in poverty while they are living independently. A shift happens in the financial settings when a person is no longer able to live independently and are living in care environments with a legislated minimum standard, and are therefore no longer at risk of living in poverty. This shift accelerates the rate at which wealth is decumulated because from a physical welfare perspective it does not matter if the person who is elderly has no wealth retained. This shift also reduces the cost to the state as far as possible in respect of each individual entering residential care.

This part of the paper critiques some of the underlying assumptions about the life accumulation cycles of the people who receive elder welfare support and services.

B Gender

From a perspective of gender, women generally live longer than men.⁸⁰ Women who have children are more likely to take prolonged career breaks to do work outside of paid employment than men who have children.⁸¹ Women earn less than men, due to the gender wage gap.⁸² There is also an increasing trend of women remaining single, or divorcing and becoming single,⁸³ which means that increasingly women may not have male partners with whom they can pool retirement resources to average out the gender inequalities.

These elements compound and mean that, in general, there is likelihood for women that they will retire without a comparable retirement nest egg to a man with a similar history of education, employment and children.⁸⁴ In an Australian study, women's median superannuation account balances were 47.6% of men's.⁸⁵ This means that women must live for longer on less.⁸⁶

While universal entitlement to NZ Super is a way of managing the risk of older women living in poverty, it does mean that single older women are unlikely to enjoy the same standard of living as single older men or people in mixed gender marriages, civil unions or de facto partnerships.

This is a systemic issue that should largely be addressed outside of the funding of elder care. However, while systemic changes are being made there is the ongoing issue that this inequality will affect many women for many years after a systemic change is made. The current system of elder welfare is based on a first principle of a personal responsibility to pay for as much of a person's own care as possible, and the NZ Super payment rates are

⁸⁰ Jo (Chau) Vu, James Doughney "Women and Superannuation: Work Until You Drop?" (2009) 4 JBSGE 41 at 42

⁸¹ Above n 78 at 46

⁸² Above n 80 at 42. In the New Zealand context, the gender pay gap in the public service in 2016 is briefly discussed at <<http://www.stuff.co.nz/national/politics/76151018/State-Services-Commission-reveals-gender-pay-gap-in-public-sector>>

⁸³ Above n 78 at 50

⁸⁴ Above n 78 at 46

⁸⁵ Above n 78 at 46

⁸⁶ Above n 78 at 46

set so that it must be heavily supplemented by the decumulation of personal wealth in order to maintain a comfortable lifestyle. This may not be appropriate in a context where many people in the retired population have significantly less accumulated wealth than others, due not to personal choice coming from a lifetime of unwise utility maximisation decisions, but stemming from gender inequality.

C Socioeconomic Status

A large focus of this paper has been the way that assets are decumulated. This assumes a certain amount of economic privilege in the subject population. Not all people reach retirement with funds accumulated that can supplement their NZ Super adequately to support them comfortably for 20 or 30 years after retirement. New Zealand has low rates of private saving⁸⁷ which suggests that either many people are unable to save because the cost of living meets or exceeds their income even during the accumulation phase, or that there is a widely held belief that elder welfare in New Zealand is funded under the implicit intergenerational social contract model. At the beginning of 2015 the average household debt in New Zealand represented 157% of the household's disposable income,⁸⁸ which is an increase from 78% at the beginning of 1995. Initiatives like KiwiSaver are explicitly linked to the idea that people should save for their retirement⁸⁹ but the slight negative effect that KiwiSaver has on total saving⁹⁰ suggests that the message is not being received.

While a wholesale approach of increasing the amount of money spent on NZ Super and other subsidies is an attractive option to people who have not been able to save throughout their working life, it is not necessarily appropriate for maintaining intergenerational equity. Through this lens however, the practice of transferring assets into trusts, or in other ways subverting asset testing mechanisms, can be viewed as particularly reprehensible. The practice could be viewed as enabling people who have had a lifetime of economic privilege to maintain that privilege for their successors, while funding their care out of the taxes of working people who are struggling to get by and make any savings at all.

⁸⁷ James Obben, Monique Waayer "New Zealand's old-age pension scheme and household saving" (2011) 38 International Journal of Social Economics 767

⁸⁸ Reserve Bank of New Zealand "Household Debt" (18 March 2016) Reserve Bank of New Zealand <http://www.rbnz.govt.nz/statistics/key_graphs/household_debt/>

⁸⁹ Above n 88

⁹⁰ Above at n 27

An issue that is reasonably problematic is that the people who make and critique the law are often working from an economically privileged position to start with. Similarly, people who try to subvert the asset testing mechanisms are also acting from a position of economic privilege, where it might not be clear to them that by exploiting a legal gap they are taking money that they do not strictly need, from people who do strictly need it. It can be difficult to identify privilege from a position of privilege.

D Conclusion

This part of the paper has briefly critiqued some of the underlying assumptions of this paper. In particular, through a lens of gender and socioeconomic status, there are issues with the way that the current legislative settings conceptualise the default person that these settings apply to.

VII Conclusion

This paper has been a discussion about government legislation and policies that manage the rate of asset decumulation for people aged over 65, in New Zealand. It aligned two frameworks to help describe the type of spending and saving behaviour that elderly people can be characterised as having at different life stages. This is useful for understanding the way that government subsidies are structured and target certain needs. The next part of this paper gave a high level overview of what government subsidies exist and what kind of behaviour they encourage.

This paper has argued that there is a tension that needs to be managed by the legislative and policy settings for wealth decumulation, which is that there is a social benefit in helping elderly people retain financial independence for as long as possible, but that there is also a benefit to the state if people pay for as much of their own care as possible.

This paper has then discussed some of the philosophical underpinnings to the way that the state and people interact with state funding of elder welfare, and the way that those underlying beliefs can drive behaviour. Under a more libertarian conception of why the state provides welfare support to people who are elderly, people who try to take full advantage of the safety net appear mercenary and unconcerned about the cost to society. From an implied intergenerational social contract perspective, people who do not act to maximise the return on the investment that they have made through years of paying taxes may appear to be acting inconsistently with their self interest. This is problematic because

it means that there is inequality of outcome depending on the way that people conceptualise the way that the state pays for their retirement.

In the final part of this paper, some of the underlying assumptions were critiqued from a lens of gender, and socioeconomic status. While making no recommendations, this part of the paper raises the issue that the broad settings that manage asset decumulation may be made with the life opportunities and patterns of a default person in mind who may not particularly representative of the elderly population.

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