Excerpt from "The Complete KiwiSaver"

Chapter 7: The young — and the not so young

The rules of KiwiSaver — and how to play the game to win — are quite different for those under 18. And while the rules are the same for everyone aged 18 to 64, there are some special considerations for those who are ten years or less from NZ Super age.

Under-18s and turning 18

Who: Anyone under 18, their parents, grandparents or anyone else who would like to help them

Every New Zealand child, even newborns, can join KiwiSaver. But the rules for under-18s differ in the following ways:

- They are not automatically enrolled when they get a new job.
- They don't get the member tax credit of up to $1,043 a year from the government.
- Compulsory employer contributions do not apply – although some employers are kind enough to contribute anyway.

Under-18s do, however, get the same $1,000 kick-start as everyone else. And, if they are working and not on a contributions holiday, 2% of their pay will go into KiwiSaver.

The only way for under-18s to join KiwiSaver is by directly approaching a provider. It's a good idea to sign children up as soon as possible — to get the kick-start while the going is good and to let the returns on that money compound over the years. However, I suggest that you choose a provider that requires little or no initial contribution and then no further contributions.

Why? There's not a lot of point in relatives making contributions to an under-18's KiwiSaver account. With no tax credits or compulsory employer contributions, the scheme does not hold the advantages it does for adults. By all means save for the young, but do it in a more flexible non-KiwiSaver account from which the child can later withdraw the money for education, setting up a business, travel or any other purpose. You might also want to set money aside elsewhere so you can put it into your child's KiwiSaver account when she or he turns 18. More on this shortly.

As noted, if a young person has a job, either when they sign up or later on, 2% of their pay will go into their KiwiSaver account — unless they have belonged for more than a year and take a contributions holiday. KiwiSaver employee contributions are taken out of pay even if the young person is not paying PAYE because they are a primary or secondary school student who expects to earn less than $2,340 a year. (For more on the PAYE exemption, go to www.whatstax.govt.nz and click on 'Your first job').

Should a parent encourage their child to take contributions holidays? Some people say the child is in the same situation as their parents — it's not a good idea to contribute to their account because of the lack of incentives and the inaccessibility of the money. But there are several counter arguments:

- Putting aside 2% of their pay from their very first job can set up a habit they will probably be thankful for later on. Anyone who saves 2% of their pay for all or most of their life should end up fairly comfortably off in retirement. (It might mean you won't feel obliged to leave them an inheritance!)

- People who start participating in a savings plan, such as KiwiSaver, often find themselves taking a new interest in their investments, and learning something about markets — such as the relationship between risk and return. There's no reason that this learning shouldn't start in childhood.

- A teen can be getting lined up for the first home subsidy and the right to withdraw KiwiSaver money to buy a first home. To be eligible for the subsidy, you have to contribute to KiwiSaver for at least three years. At publishing time the government hadn't yet decided whether that period can start before age 18. And realistically most people aren't ready to buy a first home before they are 21 anyway. But some are. In any case, a child who is contributing to KiwiSaver before turning 18 is probably more likely to continue to do so after 18 — at which point she or he certainly can be lining up for the home subsidy. (See 'Help with buying a first home' on page 120)

- In most cases, earnings of under-18s are not large amounts anyway. If your child baulks at losing access to 2% of their pay, you might want to simply make that up to them by boosting their pocket money.

Which type of fund should a child invest in? That depends on whether you think she or he is likely to take advantage of the first home subsidy and, if so, in how many years. Broadly, if it's ten or more years away — or if you think the child won't buy a house in New Zealand at all — the child will probably accumulate the most over the years if you invest in a fund with more shares and/or property. But if a home purchase might be less than ten years away, a lower-risk fund is a good idea. For more on this, see Part 3.

Some people worry that if a child receives the $1,000 kick-start and then little or nothing more is contributed to the account, fees are likely to reduce the balance over the years - possibly to zero. But while some reduction in the account is quite possible – if fees are higher than after-tax returns - it's highly unlikely the balance would get anywhere near zero. I asked providers how they expected their funds would perform with minimal contributions. For their responses, see 'The minimal KiwiSaver' on page 218)

If you want information about KiwiSaver to give to older children, Inland Revenue has published a nine-page brochure called 'KiwiSaver: A guide for children and young people'. You can download it from www.kiwisaver.govt.nz - go to 'KiwiSaver forms and services' then to 'KiwiSaver forms and guides', scroll down and click on the guide. Or you can ring 0800 257 773, and ask for it to be mailed to you. (It's an automated service, but it seems to work. Have your IRD number handy.) My only reservation about the guide – or at least the version available at publishing time - is that early on it says, 'Once you've joined, you can't opt out' and doesn't immediately mention contributions holidays. This could unnecessarily scare someone off, as an employee's commitment is actually only for one year — and for non-employees it's less than that.

'But my kids might hate me for signing them up'

Some parents are reluctant to sign up their children for KiwiSaver, as they fear it will commit the children to something they don't want. Indeed, there has been considerable misleading information about this in some media.

My response: You children are more likely to be mad with you for not signing them up. They will have missed out on the $1000 kick-start, plus accumulating returns on it over the years. And in most cases they can get that money without ever putting in any of their own – or their parents' – money.

People often don't realise just how little commitment there is in KiwiSaver. Many providers will let children – as well as other non-employees - join KiwiSaver with zero contributions. And once the child starts work, they can take repeated contributions holidays for the rest of their lives if they wish.

Looking at it more positively, signing up kids for KiwiSaver will get them past the "first year barrier". The fact that KiwiSaver employees have to contribute from their pay for 12 months before they can take a contributions holiday could put off some young adults from joining. But if they have got their first year of membership over and done with before they ever work, they can take contributions holidays whenever they wish after that, and then contribute whatever amount suits them.

Also, knowing a few young people, I reckon many simply wouldn't get around to joining KiwiSaver themselves after they turn 18 – or would opt out if they are automatically signed up. But if they are already in, and they understand how the scheme works, they're more likely to contribute as adults, picking up tax credits and perhaps employer contributions as well as the chance to get a $3,000-$5,000 first home subsidy.

I bet, for thousands of young people, KiwiSaver will start them on a stronger financial path than they would otherwise take.

Not too taxing

If you are considering signing up a child for KiwiSaver, you'll be pleased to know that you won't have to fill out tax returns each year. For adults and children alike, taxes are taken care of by the provider. But you will have to get the child an IRD number if she or he doesn't already have one. To get a number, ring 0800 377 774; or go to 'Forms and guides' on the home page of www.ird.govt.nz, or go to a PostShop or AA Centre. Ring the PostShop or AA Centre first to find out what documents you need to take with you.

When a child turns 18

On a teenager's 18th birthday, the whole KiwiSaver game changes. Tax credits and compulsory employer contributions begin, so the young person will gain plenty from contributing up to $87 a month or 2% of their pay. If your child is not working at that point, they will benefit greatly if you contribute the $87 a month (or $1,043 a year) for them.

For more information about children, see 'The minimal KiwiSaver' on page 218 and 'More about children' on page 221.

Footnote: If you are a child or teen, I apologise for addressing your parents rather than you in this section. For younger children, obviously the parents make most of the decisions. But if you are old enough to read this, I hope you have a big part in making the decisions about your KiwiSaver account.

55 to 64-year-olds

Who: Everyone aged 55 to 64, regardless of employment status

KiwiSaver is particularly attractive if you are in your 50s to 64, so it's a pity that many people in that age group seem reluctant to join. Some say they can't be bothered, as they'll soon collect NZ Super. But you can gain thousands of extra dollars of retirement money for little effort or input. Others say they won't join because they have already saved enough for retirement. But that's no excuse! You can always give your KiwiSaver gains to charity. (See 'I've already saved enough for my retirement' on page 91.)

There are two extra advantages for older KiwiSavers:

- Unlike younger people, you are not tying up your money for many years.
- The average annual returns on the money you put into KiwiSaver are really high — and considerably higher than for younger people investing in the same fund — even though your investment can be low risk. (For an explanation of why the returns differ with age, see 'Different for the young' on page 66)

Everyone has to be in KiwiSaver for at least five years, so if you join after your 60th birthday, you won't gain access to your money until after your 65th birthday. For example, a 64-year-old won't gain access until he or she is 69. And while for everyone else the tax credit, first home subsidy and compulsory employer contributions stop once they reach NZ Super age, for those who join after 60 the incentives will continue until five years after they sign on. Note that the day you turn 65 you are ineligible to join, so 64-year-olds should make sure they get in while the going is good.

Total in KiwiSaver account after five years

For employees, we assume they and their employer each contribute 2% of their pay, and their income grows by 3% a year.

	With return of 3% after fees and tax	With return of 8% after fees and tax
Employee earning $25,000	$9,200	$10,500
Employee earning $50,000	$17,200	$19,500
Employee earning $100,000	$28,300	$32,000
Non-employee contributing $20/week	$12,300	$13,900

How much money is in it for you? If you are a non-employee and you're short of money, you can contribute nothing, and receive the $1,000 kick-start. After five years, hopefully you will end up with somewhat more than $1,000. Not bad for no input from you! But a much better idea is to contribute up to $1,043 a year, which will be matched by the government. At the $1,043 level, if you are in KiwiSaver for five years, you will have put in a total of $5,215 and the government will have put in $6,215. If you invest conservatively, getting an average return after fees and tax of 3%, you'll end up with about $12,300.

That's terrific. If you were saving the same amount but the government wasn't helping you out, you would need a return of more than 36% a year to get to $12,300. And returns like that come only if you take massive risks and are lucky. But with KiwiSaver you can get the equivalent of that return with low risk, simply because the government's contributions are so generous. It's such a good deal that it's well worthwhile to dip into other savings, if necessary, to make your contributions.

Employees also receive employer contributions. That means that generally they do even better over five years, as our table shows. The exception is people on lower incomes, who would build up a lower total because they contribute less - unless they top up their account to maximise the tax credit. (For account growth over periods longer than five years, see 'How fast your KiwiSaver account will grow' on page 70)

Why do I assume you'll invest in a conservative fund? Most experts would advise that because you have only five to ten years before you can spend your savings, there's too big a chance that you'll lose some money in a riskier fund over such a short period. In any case, if your time horizon is relatively short, making a higher average return makes surprisingly little difference to total savings. Take, for example, our non-employee above who ends up with $12,300 in a fund earning 3%. If he or she were in a fund earning 8%, the total would be about $13,900. Why so small a difference? The money is being gradually drip-fed into the KiwiSaver account, so quite a lot of it is there for only a short time. And even the first dollars are there for only five years. Compounding just doesn't have much time to work its magic.

Generally, then, for people aged more than 55, a conservative or balanced fund would be a wise choice. There are, though, two exceptions to this:

- If you have other retirement savings, you should consider your KiwiSaver investment in light of those other investments. You might, for instance, regard your KiwiSaver account as a bit of a fling, investing in a risky fund in the knowledge that if it doesn't work out you have plenty of other savings to fall back on.
- If you plan not to spend your KiwiSaver money until you are in your late 70s or 80s, you might have 20 or 30 years to play with, and so you are in a position to take more risk. Note, too, that investing in shares and/or property gives you more protection against unexpected inflation over the long term.

In retirement

As stated above, when you reach NZ Super age or five years after joining KiwiSaver — whichever comes later — the government incentives and compulsory employer contributions cease. But of course your employer can continue to contribute if it wishes. You, too, can keep putting in money or stop — whatever suits you.

What about taking money out? You can withdraw the lot on the first day you have access to it, or leave it in the account for as long as you like. I suspect many people will take part of the money in lump sums, perhaps for travel or projects, and part in regular payments. Some providers are more helpful with this than others. See 'Retirement-related issues' on page 292.

For help in working out how much to save for retirement, and how much spending you are likely to have in retirement, see the Retirement Commission's website, www.sorted.org.nz

Better you than the grandkids

If for whatever reason you are reluctant to join KiwiSaver but you would like to contribute regularly to KiwiSaver accounts for your under-18 grandchildren, think again. As explained above, under-18s don't get tax credits, but you do! You could help your grandchildren more by joining KiwiSaver yourself and contributing the money to your own account, attracting the tax credits.

Once your tax credits stop, you could then transfer the money to the grandkids — making sure you do it gradually enough not to have to pay gift duty (don't give away more than $27,000 a year). I suggest, though, that you don't transfer the money to their KiwiSaver accounts. Better to put it in other savings accounts, so they can access it for tertiary education, setting up a business or paying for their OE.