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# **The Save More Tomorrow™ plan can boost retirement savings in New Zealand**

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## **Abstract**

Save More Tomorrow is a retirement savings plan developed by Richard Thaler and Shlomo Benartzi that incorporates insights from Behavioural Economics. In this paper, we describe how the plan works and discuss how it can be used to increase retirement savings in New Zealand.

## **What is the retirement savings situation in New Zealand?**

Many New Zealanders are not saving enough for retirement. A Financial Services Council survey found that, on average, New Zealand retirees report a \$218 gap between their weekly income and the income they report that they need to live comfortably (Financial Services Council, 2018). The survey also projects that 18-34-year-old KiwiSaver members will end up with a \$205 gap between their weekly income in retirement and the income they say they will need to live comfortably. A Massey/Westpac survey found that only 40 percent of pre-retirees consider themselves well-prepared for retirement (Massey University, 2019).

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## **What is the Save More Tomorrow plan?**

Save More Tomorrow is a plan that helps people save for their retirement by taking into account people's psychological limitations. The plan was designed by Richard Thaler, who won the Nobel Prize in economics for his contributions to behavioural economics, and his collaborator Shlomo Benartzi (Benartzi and Thaler, 2004). It is implemented by an employer and works as follows:

1. Employees are enrolled in the plan by default,
2. they commit to using part of their future pay rises to increase their retirement savings contributions,
3. their contributions rise each year until they reach a pre-determined maximum savings rate, and
4. they can quit the plan at any time.

The plan takes advantage of three insights from behavioural economics.

### 1. Defaults influence behaviour

People procrastinate. Many would delay signing up for a plan even if, for example, it just involves filling out a form. Because enrolment in the Save More Tomorrow plan is the default, people's tendency to procrastinate does not prevent them from saving (for more on the power of defaults, see: Samuelson & Zeckhauser, 1988; Johnson & Goldstein, 2003). The option to stop the plan at any time preserves people's freedom to drop out of the plan if they, for example, can't afford to save.

## 2. People have self-control problems

People find it difficult to go to the gym, stick to diets and save for their retirement despite thinking that they should (Casari, 2009). Committing to save more in the future is easier than saving more right now, because one does not have to give anything up immediately.

## 3. People hate losses

People are much more upset about losses than they are about foregone gains (Kahneman & Tversky, 1979). Linking future savings to pay rises means that employees do not have to experience a reduction in their take-home pay – their disposable income only increases more slowly than it otherwise would have.

### **Does the Save More Tomorrow work?**

Thaler and Benartzi (2004) tested the Save More Tomorrow plan in three companies and found that it led to large increases in contributions to employees' 401(k) retirement plans (a retirement scheme in the US similar to KiwiSaver). In one company, for example, the savings rate of employees who joined the Save More Tomorrow program increased from 3.5 percent to 13.6 percent in only four years. The program was also popular among employees - in all three companies, few of them dropped out.

### **Can New Zealand employers use Save More Tomorrow to help their employees save more for their retirement?**

Two barriers hold New Zealand companies back from implementing the Save More Tomorrow plan as part of KiwiSaver. The first is an administrative burden. Currently, employees sign a [KS2 form](#) at the time their KiwiSaver rate is about to change and there is no option in the form to commit to future increases in saving. While it "*should be ok*" for employees to commit to

future savings increases “*as long as they give their request in writing,*” this would require some extra effort (E-mail correspondence with IRD, May 2019). Second, KiwiSaver members do not have the flexibility to increase their contributions by small amounts. At the moment, [contributions have to be 3, 4, 6, 8 or 10 percent](#). Employees who are contributing 4 percent, for example, would have to commit to a 2 percentage point increase, which often exceeds any pay-rises they might receive.

Employers could also instead use the Save More Tomorrow plan in a way that takes advantage of the financial incentives of KiwiSaver and allows for more flexibility. Employees have an incentive to contribute to KiwiSaver to reap government subsidies and employer matching contributions. However, it is difficult to withdraw from KiwiSaver, which limits the employees’ ability to react to unforeseen circumstances (see New Zealand Government, 2018). To consider the financial incentives and allow for more flexibility, employers could direct the minimum amount necessary for taking advantage of the financial incentives to KiwiSaver and invest the rest in an alternative, more flexible savings scheme (for a discussion on the tradeoff between incentives and flexibility, see: Tibshraeny, 2018).

### **What can the New Zealand Government do?**

The New Zealand Government can make it easier to implement automatic increases in KiwiSaver contributions and allow increases in smaller increments. KiwiSaver members could then show in their KS2 form whether and by how much they want their contributions to increase each year and what their maximum contribution rate will be. After the US removed similar barriers in their Pension Protection Act, pension providers offered plans with automatically increasing savings rates. The ability to offer this feature has, according to the estimates of Thaler and Benartzi (2013), increased annual savings in the US by US\$7.4 billion (a 0.33 percentage point increase in the 401(k) contribution rate).

The Government can also encourage research to test how well the Save More Tomorrow plan would work in the New Zealand context. For example, there are 60,000 public school teachers who often struggle to save enough for their retirement. The New Zealand Government can trial the Save More Tomorrow plan in collaboration with several public schools. If it works well, it can be rolled out to other public and private employers.

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