"IRISH PENSIONS -

AT A CROSSROADS"

A SUBMISSION BY

THE IRISH ASSOCIATION OF
PENSION FUNDS

TO THE PENSIONS BOARD

ON THE NATIONAL PENSION
POLICY INITIATIVE

IAPF

The Irish Association of Pension Funds

May 1997

CONTENTS

PART 1:

NATIONAL PENSION POLICY INITIATIVE SUBMISSION

1. INTRODUCTION

1.1 This submission sets out the response of the Irish Association of Pension Funds (IAPF) to the Consultation Document on the National Pensions Policy Initiative (NPPI) issued jointly by the Department of Social Welfare and the Pensions Board in February 1997.

1.2 The IAPF was established in 1973 and represents the interests of a broad cross-section of employers, trustees and practitioners who are involved in the operation of occupational pension schemes. The primary objective of the IAPF is to foster and enhance the interests of Irish pension schemes and of their members. The schemes which the IAPF represents have a total of nearly 200,000 members and an estimated asset base of IR£16 billion.

1.3 The submission is divided into 3 parts .

- Part 1 sets out the views of IAPF as to how best to achieve improved overall pension coverage in Ireland taking into account the issues raised in the Consultation Document.

- Part 2 sets out the response of IAPF, based on the broad strategy set out in Part 1, to the 43 specific questions in the Consultation Document.

- Part 3 contains the full results of market research commissioned by IAPF from Lansdowne Market Research as an input to its submission.

2. EXECUTIVE SUMMARY

Section 3 : Objectives and Criteria

2.1 The IAPF submission is based on the conclusions of the Pensions Forum convened by IAPF in March 1995 and on extensive consultations with its members on NPPI.

2.2 IAPF agrees with the objectives for a national pensions system which were set out in the Final Report of the National Pension Board. These require that the state provides directly through the state pension system an adequate basic income for everyone and facilitates and encourages supplementary provision on a voluntary basis.

2.3 To support these objectives the Pensions Board should be given responsibility, funded by the Exchequer, to promote a better understanding of pensions so that people can plan better for their future.

2.4 It is not appropriate to set specific goals for either the extent or the adequacy of pension coverage since there are a number of ways of making provision other than through formal pension plans. The Pensions Board should continue to monitor both formal pension scheme coverage and the income available to those reaching retirement age.

Section 4 : Current Arrangements

2.5 Currently the state pension represents 26% of National Average Earnings for a single person and 45% for a married couple. Over the last 10 years state pension increases have exceeded price inflation but have lagged behind wage inflation.

2.6 Ireland is not facing the demographic time bomb with which other countries have to contend:-

- Our demographics are more favourable as we have a lower ratio of pensioners to the working population.

- The level of state pensions in Ireland are generally lower than in other countries.

As a result Ireland has a unique opportunity for a long term partnership between state and occupational provisions which will provide a permanent and sustainable approach to retirement provision.

2.7 The tax treatment of pension funds is tax deferral, an approach which Ireland shares with most other OECD countries.

2.8 Any changes to the overall pensions system in Ireland should be cognisant of the long term desire for the harmonisation of pension provision throughout the EU.

Section 5 : Pension Coverage - Analysis and Key Conclusions

2.9 The IAPF has carried out a detailed analysis of retirement coverage having regard to the total resources available on retirement, comprising both formal pension provision and other assets and savings. This analysis is based on the following:-

- The ESRI 1996 Survey on Pension Scheme Coverage.
- Additional data on pension coverage in relation to income distribution.
- The market research commissioned by the IAPF from Lansdowne Market Research into Non-Pension Holder Coverage.

2.10 The Market Research disclosed a wide range of reasons for non coverage. The top three reasons common to all employment categories were affordability, administration charges and complexity.

2.11 The Market Research also indicated a wide variety of reasons for not participating in a formal pension scheme. These include not being able to afford to join, accepting the state pension as adequate, having alternative sources of income and considering that pension provision is something for the future. The research also revealed large numbers who indicated they did not understand pensions.

2.12 Having regard to the results of the coverage survey and the market research IAPF is proposing a three tiered approach to future pension policy:-

- An improvement in the state pension to look after those who cannot afford to make any further pension provision.

- The introduction of a new simplified pension system, Personal Retirement Accounts. This to be supported by an educational and promotional campaign, managed by the Pensions Board, to encourage pension provision.
- A simplification of the taxation and regulatory regimes for group schemes.

Section 6 : Reforming the State Pension System

2.13 As part of it's proposal for future pension policy IAPF proposes that the state pension (single persons rate) is increased to 35% of National Average Earnings over a 5 to 10 year period. This rate should also apply to social assistance pensions.

2.14 Pensions should then be maintained at this level through legislation.

2.15 IAPF considers that financing the proposal is well within the capacity of the Irish economy - over 40 years costs are projected to grow from 3.1% to 4.2% of GDP. The resultant costs are still significantly less than those in other developed countries.

2.16 The income redistribution inherent in PRSI (or tax) based financing of the improved benefits is consistent with social solidarity and addresses the "affordability" concerns of the lower paid as emerged in the market research.

Section 7 : Introducing Personal Retirement Accounts

2.17 IAPF's proposal includes the introduction of a new form of pension contract- the Personal Retirement Account (PRA). This is intended to be used for contributions from the self-employed, contributions from employers and employees buy out bonds and as an alternative option for AVCs.

2.18 The key features of PRAs would be as follows:-

- They would be set up either as insurance contracts or under trust.
- The accounts would be personal to the contributor, thus facilitating changes in employment status in a cost effective way.

- The tax treatment would be the same as for existing pension schemes including the facility to take up to one and a half times earnings as a tax free amount at retirement. In addition up to 50% of the accumulated fund could be withdrawn tax free at any time after age 50 to meet health related expenses or in the event of redundancy or severe financial hardship.

- PRAs could only be marketed by approved providers, usually financial institutions and other organisations who satisfy the conditions for approval including capital adequacy.

- The maximum contribution allowable, inclusive of contributions to other approved pension plans, would be 30% of taxable earnings (with higher limits for those over age 55).

2.19 The Pensions Board should be given the following additional responsibilities in respect of PRAs:-

- Authorising approved providers.

- Monitoring the investment vehicles permitted and making regulations in respect of the related investment risk.

- Overseeing the marketing of PRAs with appropriate powers to intervene should this become necessary.

Section 8 : Reforming Current Arrangements

2.20 IAPF proposes that the following changes should now made in the taxation and regulatory regimes governing approved pension arrangements.

- The maximum approvable benefits under approved pension schemes should in future be calculated by reference to the total period as a PRSI contributor. Some restrictions may then be needed in respect of “controlling directors”.

- It should be possible to retire at any time between 60 and 70 on the maximum approvable benefits.

- A new framework should be introduced to facilitate the interaction of group schemes and PRAs while protecting the position of the Revenue.

- The requirements in respect of early leavers should be improved to reduce the current vesting period from 5 years to 2 years and to provide preservation for pre 1991 service (with revaluation from 2006 in the case of defined benefit schemes). The Pensions Board should agree the setting up of a central register of deferred benefits and buy out bonds.

- It should be a requirement on the trustees of defined contribution pension schemes to provide an illustration of future expected benefits at 3 yearly intervals. The Pensions Board should specify the format of such illustrations.

- The requirements in respect of the "investment risk" and the "annuity risk" proposed for Personal Retirement Accounts should be extended to defined contribution schemes.

- The position of trustees in relation to investment decisions on defined contribution schemes and PRA's should be clarified by legislation.

2.21 IAPF also proposes that employers and the trade unions should seek ways to actively promote industry schemes as a cost effective way of extending pension coverage.

Section 9 : Assessment of Proposal

2.22 Overall the IAPF analysis shows that its proposal satisfies the various criteria which the Consultation Document proposed should be used to assess all proposals put forward in response to NPPI.

3. OBJECTIVES AND CRITERIA

3.1 The purpose of this Section is to set out the views of the IAPF on the objectives and criteria which should govern the development of future pensions policy in Ireland.

IAPF Pensions Forum

3.2 The IAPF convened a Pensions Forum in March 1995 to consider future pension issues. Over 50 participants, representing a wide range of pension interests, attended the Forum which was one of the early catalysts for the present debate.

3.3 The conclusions of the Forum, under a number of broad headings, were:-

Partnership

- *The partnership between state and occupational provision should be fostered.*
- *There is a need for a greater level of predictability in issues such as the tax treatment of pension funds, continued freedom of investment and the level and availability of state benefits.*
- *The full involvement of the social partners (employers, trade unions and the state) in the retirement planning process is vital.*
- *The position of the Pensions Board could, perhaps, be strengthened as the advisory body to the government on pensions issues.*

Flexibility

- *More research needs to be undertaken into an occupational pensions framework which caters better for job mobility and new work patterns.*

- *There was a broad agreement that it may be too narrow to focus solely on the provision of pensions. For instance, the growing need for long-term residential care may need to be factored explicitly into retirement planning.*

- *Greater attention should be paid to the interests of the ultimate consumer in the pensions process.*

- *The Revenue pensions regime could, in some circumstances, be an unnecessary barrier to flexibility.*

Education

- *There is a requirement for more research into the retirement needs of individuals in a more self-reliant society and the financial implications of demographic change for the State and occupational schemes.*

- *There is a need to generate a greater awareness of the importance of retirement provision by the younger members of the workforce.*

- *There is a need to persuade politicians of the importance of a stable long-term environment for retirement planning.*

- *There is a need to ensure that scheme members (particularly members of defined contribution arrangements) have a realistic expectations of emerging benefits.*

3.4 The conclusions of the Forum, supported through extensive consultation with the IAPF membership on NPPI, are the basis for this submission.

Objectives

3.5 In its Final Report the National Pensions Board stated:-

> *"Ideally, a fully developed national pension system is one which **enables** all residents in the state to acquire an income which allows them to maintain their established standard of living in the following circumstances:*
>
> - *attainment of retirement age,*
> - *long-term incapacity,*
> - *in the case of dependants, on the death of the income provider.*
>
> *This ideal is subject to the resources available for pension provision.*
>
> *At a minimum, the national pension system should **ensure** that any resident, in any of the above circumstances and who has no other income, should receive a state pension which is sufficient to maintain a basic standard of living."*

3.6 IAPF is fully in agreement with this as a statement of the appropriate objectives for a national pensions policy. Thus the role of the state - through which these objectives are delivered - is to provide directly through the state pension system an adequate basic income for everyone and to facilitate and encourage supplementary provision on a voluntary basis.

3.7 This approach is also consistent with that applied in other areas. For example, in response to employment, which is for most of the population a more immediate concern than pensions, the state has adopted the role of facilitating the widest possible opportunities for access to work while providing a fixed income for those who are unable, for whatever reason, to secure employment.

3.8 However, the IAPF believes that the successful achievement of the above objectives requires that resources are allocated to promote a better understanding of pensions so that people can plan better for their future. The Pensions Board, which has statutory responsibilities in the area of pension provision and policy, is ideally suited to take on this responsibility. An appropriate budget should be allocated for this purpose by the Exchequer since it would be inequitable that established pension schemes should be asked to meet this additional cost.

Pension Goals

3.9 The Consultation Document puts forward the view that " *progress towards the attainment of any set of goals relating to retirement income provision requires that they are agreed and clearly expressed*." It is also proposes that " *the goals that emerge should be expressed in terms of ends, not means."*

3.10 The IAPF supports the view that the emphasis should be on goals and not means. Formal pension arrangements will continue to have the major role in pension provision for the majority of the working population. However, any assessment of retirement provision must take into account the total resources available on retirement and not just those emerging from such arrangements. This is very relevant is analysing current pension coverage which is considered in detail in Section 5.

3.11 The stated objective requires that the income provided by the state should be adequate to provide a basic standard of living. It is necessary to establish what this level is, how it should be achieved and then maintained in the future. This is considered further in Section 6.

3.12 Because of the diversity of ways of providing for retirement IAPF does not consider that it is appropriate to establish targets for either the numbers to be covered by occupational pensions or the level of such coverage. It recommends, however, that the Pensions Board should continue to monitor coverage and that a new survey be introduced which looks at the income available to those reaching retirement age. This information will also be invaluable to the Board in promoting greater awareness of the need for pension provision.

Criteria

3.13 The Consultation Document sets out a number of criteria for assessing any options for improving overall pension coverage (which are repeated here for the sake of completeness).

Effect on Coverage:	The level of coverage, over and above state pension entitlement, varies widely across sectors of the community. Extending second pillar coverage is a major option for NPPI.

Adequacy of Benefits:	Merely extending trivial coverage to more people is of limited value. Equally, excessive benefits may be a waste of resources.
Protecting the Status Quo:	It would be important to ensure that the current structure, which broadly works well, is not unwittingly undermined or threatened. A lot of good coverage already exists.
Cost and Efficiency:	Value for money and administrative effectiveness can vary considerably between different systems.
Fiscal and Economic Impact:	There are short and long term effects on both national finances and competitiveness.
Robustness and Flexibility:	Changing a pension system is a very slow and complex process. The extent to which it can be easily adjusted to changing social and economic conditions may be important.
Solidarity:	There are implicit social contracts in the current system between government and citizens and between generations. These may or may not be felt appropriate in future.
Fairness:	People should feel they get a reasonable return for their contributions to different pillars and that there is fairness between different parts of society, such as, different income groups.
Labour market implications:	How pensions are provided can affect labour market participation and employment practices.

3.14 IAPF agrees that these are the appropriate criteria. Our proposals are assessed against these criteria in Section 9.

Summary

3.15 The IAPF submission is based on the conclusions of the Pensions Forum convened by IAPF in March 1995 and on extensive consultations with its members on NPPI.

3.16 IAPF agrees with the objectives for a national pensions system which were set out in the Final Report of the National Pension Board. These require that the state provides directly through the state pension system an adequate basic income for everyone and facilitates and encourages supplementary provision on a voluntary basis.

3.17 To support these objectives the Pensions Board should be given responsibility, funded by the Exchequer, to promote a better understanding of pensions so that people can plan better for their future.

3.18 It is not appropriate to set specific goals for either the extent or the adequacy of pension coverage since there are a number of ways of making provision other than through formal pension plans. The Pensions Board should continue to monitor both formal pension scheme coverage and the income available to those reaching retirement age.

4. CURRENT ARRANGEMENTS

4.1 This section describes, in general terms, existing pension structures highlighting points which are of particular relevance in the context of NPPI. It is not intended to be a complete and detailed description of the Irish pensions framework because this information is already included in the Consultation Document and elsewhere.

Overall Structure

4.2 In Ireland, as in most developed economies, there are 3 ways in which pensions can be provided - often referred to as the 3 pillars of pension provision. The key characteristics of these pillars are summarised in the following table:

		Financing		Delivery
Third Pillar	Private Provision	Advance Funding		DC
Second Pillar	Occupational Provision	Public Sector	Pay-As-You-Go	DB
		Private Sector	Advance Funding	DB but trend towards DC
First Pillar	State Provision	Pay-As-You-Go		DB

DB = Defined Benefit DC = Defined Contribution

State Provision

4.3 The first pillar is state provision through the social welfare system. This provides a flat rate pension payable from age 65. This pension is funded through Pay Related Social Insurance(PRSI) contributions. These contributions are payable by employers, employees and self employed individuals. The social welfare fund is supplemented, as required, by transfers from general taxation.

4.4 The maximum rate of pension payable with effect from June 1997 is as follows:

Table 4.4 Current State Pensions (Maximum Rate)

	Amount per Week
Single Person	£78[1]
Married Person (with an adult dependent under age 66)	£129

4.5 All private sector employees and all public and civil servants who take up employment after April 1995 are eligible for the above rate of benefits on a non means tested basis provided they satisfy the specified contribution requirements. Pensioners are also eligible for allowances for electricity, telephone rental, fuel during the winter months and, once they reach age 66, are also entitled to free travel on public transport. Many pensioners also qualify for a medical card which confers a free entitlement to almost all medical care.

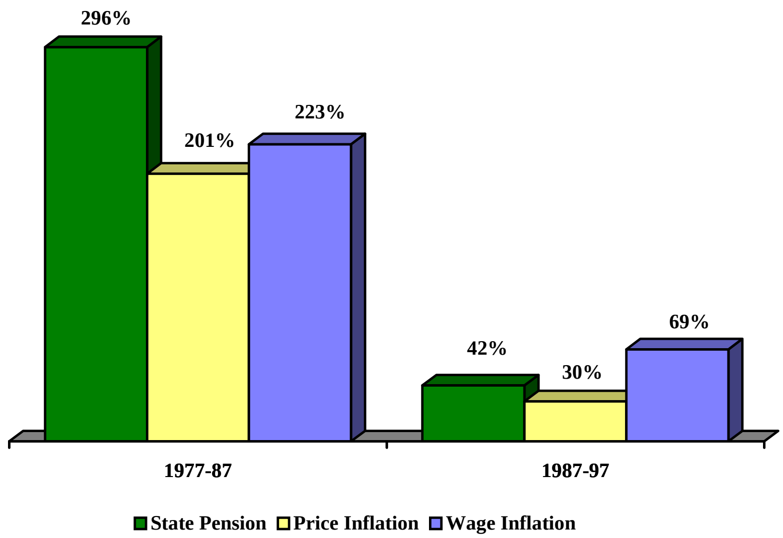
4.6 National Average Earnings (NAE) in June 1996 were £279.47[2] per week. Allowing on an approximate basis for wage inflation over the past 12 months the state pension currently represents 26% of NAE in the case of a single person and 45% in the case of a married couple.

State Pension Increases

4.7 The established practice is to increase state pensions as part of the annual government budget process. However there is no stated policy as to the rate of increase to be provided. The following table illustrates the rates of increase over the last 20 years relative to price and wage inflation.

[1] This is referred to in the remainder of this submission as the **state pension** when making comparisons.
[2] All Industrial Workers/All Industries

Table 4.7 Increases in State Pension Vs Price and Wage Inflation



Sources: CSO Statistical Bulletins, Department of Social Welfare, IAPF estimates

4.8 Over the period 1977 to 1987, during a period of relatively high inflation, the state pension increased at a rate in excess of both price and wage inflation. The position significantly changed in the following 10 years when the pension increased at a rate between price and wage inflation. The extent to which this was deliberate government policy is not clear.

State Pension - Financing

4.9 State pensions are funded on a Pay-As-You-Go basis and, as such, are vulnerable to future changes in the demographic balance between the working and retired populations. A review of the long term cost of state pensions, commissioned by the Department of Social Welfare, is currently being finalised. However it is clear from other studies[3] that Ireland does not have to contend with the demographic time bomb being faced by other developed countries with the consequent pressures on them to consider radical changes in their social security structures.

[3] Hughes (1997), Combat Poverty Agency (1997), Mc Carthy (1995)

4.10 There are two reasons for this:-

- Our demographics are more favourable as we have a much lower ratio of pensioners to the working population.
- The levels of state pensions in Ireland are generally lower than in other countries.

4.11 IAPF considers that our favourable position provides a unique opportunity for a long term partnership between state and occupational provisions which will provide a permanent and sustainable approach to retirement provision.

Occupational Provision

4.12 The second pillar of the system is occupational provision which can be organised either:-

- Through employer sponsored schemes established under the Finance Act 1972. Included within this category are employee funded additional voluntary contribution (AVC) arrangements. For convenience these schemes are referred to in this submission as **group schemes.**
- Through individual self-employed arrangements established under the Income Tax Act 1967. These are known as **retirement annuities** and are also open to employees who do not participate in a group scheme.

4.13 Group scheme benefits are, broadly speaking, provided on either of two bases:-

- Defined benefit where the employee's entitlement at retirement is based in some way on his/her salary or wages (often service related also). Typically the aim is to provide long term employees with a pension at age 65 of 2/3rds of salary or wages inclusive of the state pension.
- Defined contribution where the employee's entitlement at retirement is determined by the accumulated value of the contributions directly paid on the employees behalf.

Retirement annuities are invariably established on a defined contribution basis.

4.14 In recent years there has been a trend towards defined contribution arrangements for new group schemes, especially those with small numbers of employees. However, unlike other countries, there has not been a strong trend for established schemes to switch from defined benefit to defined contribution. This undoubtedly reflects strong employee and union resistance to any loss of the much greater certainty provided by defined benefit schemes and the less onerous regulatory environment in Ireland for such schemes.

4.15 It is essential that this support for established defined benefit schemes is maintained in any changes which result from NPPI.

Occupational Provision - Tax Treatment

4.16 The present system of pension fund taxation in Ireland is sometimes misunderstood. Contributions to pension funds are fully tax deductible and the funds themselves accumulate on a tax-free basis. However, this is balanced by the fact that the pension benefits emerging are fully taxed as income. In other words, the system operates on the basis of **deferred taxation** and not **no taxation**.

4.17 This tax treatment is consistent with the view which is reinforced in the Pensions Act that pension funding is a form of **deferred remuneration -** money which would otherwise have been paid as salary or wages is set aside to provide pensions on retirement.

4.18 Ireland shares this approach to pension fund taxation with most other OECD countries and clearly, based on the argument outlined above, its retention can be justified on equity grounds. Furthermore, the existing system encourages the development of occupational provision.

4.19 The issue of pension fund taxation was examined very thoroughly by the National Pensions Board in its report published in 1988. The Board concluded that:-

> *"We believe that the present tax treatment of pension funds is simple to understand and operate, is broadly equitable and clearly acts as a major encouragement to the establishment of funded occupational pension schemes."*

4.20 There are two entirely separate tax regimes governing group schemes and retirement annuities. There are considerable similarities between the two regimes and at a fundamental level both share the deferred taxation approach outlined above.

4.21 The main difference, however, between retirement annuities and group schemes, from a tax point of view, relates to limits. For retirement annuities the limit is defined in terms of a maximum contribution level. For group schemes the limit is defined in terms of maximum benefits (as a proportion of income at retirement) which the arrangement can provide without specific regard to the contributions required to fund those benefits (although there is a limit on contributions which individual employees can make). This difference is considered further in Section 8.

Occupational Provision - Regulation

4.22 The Pensions Act 1990 sets down a framework for the regulation and control of group schemes. The main areas covered by the Act are as follows:-

Disclosure of Information
Members are entitled to receive certain relevant information in relation to their pension scheme.

Trusteeship
The Act defines the role and duties of pension scheme trustees. Regulations also make provisions for members to participate in the selection of trustees.

Equality
The Act also implements the EU directive on the principle of equal treatment for men and women in occupational pension schemes.

Protection of Early Leavers
Under the Act all pension schemes are required to provide full vesting of acquired benefits for early leavers after a minimum period (usually 5 years) in respect of service after January 1991. In the case of defined benefit schemes the preserved benefit has to be revalued in line with price inflation (up to a maximum of 4% in any one year.)

Minimum funding standards
All defined benefit schemes are subject to a minimum funding standard which is monitored through the provision of a regular actuarial funding certificate . The base line for this standard is the value of the member’s statutory preserved benefits.

Private Provision

4.23 This consists of assets and savings which can be drawn upon to meet financial needs in retirement. It could thus be termed informal pension provision. While accepting that only a small proportion of these assets are likely to be used for retirement purposes, nonetheless it is interesting to compare the value of general assets in private hands with the aggregate value of pension funds.

Table 4.23 Pension Vs Non Pension Assets

	Value
Pension Funds	£19bn
Housing Stock	£54bn
Farms	£16bn
Other Assets	£27bn

Source: Consultation Document

EU Dimension

4.24 It is a long term objective that pension benefits across the EU will be harmonised. At present there are considerable obstacles to the process. These include different levels of state pension - in absolute terms and as a percentage of average earnings - and, as a result, different levels of occupational pensions. The coverage by occupational pension schemes ranges from being almost non-existent in some countries to almost 100% in others. Where there are occupational schemes there are various methods of funding. In some countries, e.g., Holland, schemes are generally funded as in Ireland but in others, e.g. Germany, pension liabilities are mainly covered by book reserves. Different vesting periods have already caused difficulties in relation to transfers of employees between countries.

4.25 All of this means that, despite theoretical freedom to work in other EU countries, there are formidable obstacles as a result of the pension arrangements. Any system introduced in Ireland should be cognisant of the long term desirability of harmonisation and should avoid, if possible, further barriers to this objective. The IAPF proposals have been put forward with this in mind.

Summary

4.26 Currently the state pension represents 26% of National Average Earnings for a single person and 45% for a married couple. Over the last 10 years state pension increases have exceeded price inflation but have lagged behind wage inflation.

4.27 Ireland is not facing the demographic time bomb with which other countries have to content:-

- Our demographics are more favourable as we have a lower ratio of pensioners to the working population.
- The level of state pensions in Ireland are generally lower than in other countries.

As a result Ireland has a unique opportunity for a long term partnership between state and occupational provisions which will provide a permanent and sustainable approach to retirement provision.

4.28 The tax treatment of pension funds is tax deferral, an approach which Ireland shares with most other OECD countries.

4.29 Any changes to the overall pensions system in Ireland should be cognisant of the long term desire for the harmonisation of pension provision throughout the EU.

5. PENSION COVERAGE - ANALYSIS AND KEY CONCLUSIONS

5.1 This Section sets out a detailed analysis of current pension scheme coverage, looks at the reasons why there are gaps in this coverage and, using the analysis, puts forward IAPF's proposal for future pensions policy.

5.2 The Consultation Document included a summary of current pension scheme coverage based on a survey commissioned from the ESRI. For its analysis IAPF has supplemented this survey in two areas. Firstly, for those not covered by occupational arrangements it is necessary to explore the reasons why this is the case. This was done by commissioning market research on Non-Pension Holder Coverage from Lansdowne Market Research. The full results of this research are set out in Part 3 of this submission. Secondly, IAPF obtained further information on coverage in relation to income distribution from the ESRI.

5.3 IAPF also considers that formal retirement provision through occupational arrangements must be considered in conjunction with less formal, but none the less significant, provision from other sources. In looking at such provision we have coined the phrase **total coverage**. This informal provision is difficult to measure accurately but it is too important to ignore in any assessment of pension provision.

Market Research - General Findings

5.4 The Non-Pension Holders Research was carried out in April 1997 by means of in-home face-to-face interviews of 704 members of the working population stratified by employment status and age. Full details of the survey results and methodology are set out in Part 3.

5.5 At an overall level one of the key findings of the survey was, when asked spontaneously for their reasons for not participating in a formal pension arrangement, that the main reason given was that they *"never thought about it"*. This is clear evidence that there is a need for more education on the importance of saving for retirement.

5.6 To explore non-coverage in a more structured way the respondents were asked which of a specified list of possible reasons applied in their own case. The results of this analysis are set out below:-

Table 5.6 Prompted Reasons for not belonging to a Pension Scheme

Reasons Suggested [4]	
I can't afford a pension scheme at the moment	75%
The charges involved in organising a pension are too high	64%
I don't really understand pensions	64%
I will have saved enough over the years for my retirement	54%
I am too young to worry about a pension	53%
The company I work for does not have a scheme	52%
I have only been working for a few years	49%
The state pension will be adequate enough for me	48%
I won't be able to get at the money in a pension scheme if I need it	47%
My husband's/wife's pension will be enough for both of us	35%
I can always sell the house/farm, business or some other asset to provide a pension	32%
I am not eligible to join my company's pension scheme	22%

Source: Lansdowne Market Research

5.7 The top 3 reasons (affordability, administration charges and complexity) are common across all employment categories and, to quote from the survey analysis, this strongly suggests that to achieve an increased pension coverage *"non pension-holders" need to be convinced that:-*

- *Pensions can be afforded, if they start early enough;*
- *Pensions do not impose too heavy charges;*
- *Pensions are not too complicated;*
- *Organising a pension is not too difficult."*

Other specific market research findings are commented upon further in the following paragraphs of this section.

[4] Combined Definitely Applies and Applies to Some Extent responses

Analysis of Coverage - Self Employed

Agricultural

5.8 The ESRI found that only 14,000 (12%) out of 119,000 farmers had formal occupational provision. The specific results of the market research for this group are:-.

Table 5.8 Self Employed Agricultural - Market Research Key Results

Specific reasons for not belonging to a pension scheme [5]		*Likely main source of retirement income*	
Retirement funded through sale of assets	65%	State pension	50%
State pension will be adequate	59%	Sale of assets	30%
Retirement savings inaccessible	56%	Pension Scheme	13%
		Partner's pension	6%
		Other	5%

Source: Lansdowne Market Research

5.9 These findings make sense intuitively. A farm does not stop producing income when a farmer retires. When the farm is passed on from one generation to the next there is usually an arrangement that a form of retirement income is paid to the retiring parent. Alternatively if the farm is leased outside the family it continues to produce an ongoing income. In more recent times there have also been generous EU retirement subsidies. Additionally the farming community has a high level of trust in and dependence on state pensions.

5.10 **On a total coverage basis it is IAPF's view that a high proportion of farmers, in practice, will have a reasonable income in retirement from various sources. Our research indicates that this figure could be in the region of 70,000 people (or approximately 60% of the total).**

Non agricultural

[5] These are the next most important reasons given after the general concerns in relation to affordability, administration charges and complexity.

5.11 Almost 58,000 (39%) out of a total of 146,000 of people in this category have formal occupational provision according to the ESRI Survey. It is reasonable to assume that the remaining 89,000 largely comprise sole traders, many of whom would justifiably claim that the business is their pension fund. The market research supports this conclusion.

Table 5.11 Self Employed Non Agricultural - Market Research Key Results

Specific reasons for not belonging to a pension scheme [5]	
Retirement funded through savings	65%
Retirement savings inaccessible	47%
Too young to worry about pensions	45%
State pension is adequate	45%

Likely main source of retirement income	
Sale of assets	33%
State pension	32%
Pension scheme	20%
Partner's pension	12%
Other	4%

Source: Lansdowne Market Research

5.12 The market research suggests that there is also a relatively high dependency on the state pension by this group.

5.13 This category also includes the new breed of mobile workers who, in a constantly changing labour market, move from job to job , switching as appropriate from employed to self employed status. It must be accepted that they are not well served by existing pensions framework which was designed for "a job for life" model of employment. This is an issue addressed in IAPF's proposal.

5.14 **It is IAPF's view, supported by research, on a total coverage basis that approximately 90,000 people in non agricultural self employment (or 60% of the total) will have a reasonable retirement income.**

Analysis of Coverage - Employees

[5] These are the next most important reasons given after the general concerns in relation to affordability, administration charges and complexity.

5.15 In order to estimate the total coverage for employees the results of the market research have been combined with the income distribution data provided by the ESRI to establish the extent to which this group relies on the state pension.

Part Timers

5.16 Coverage for this group, which numbers 87,000 is, not surprisingly, very low at 7,000(8%). Part time employees by definition have relatively low earnings. Based on the income distribution data supplied by the ESRI (see 5.25) IAPF estimates that current average earnings for this category are in the region of £100 per week. For these people the current state pension of £78 per week provides a replacement income of almost 80% of earnings.

5.17 In addition many part timers are only working to achieve short term financial targets such as an annual family holiday and has neither the need for nor the interest in pension provision, believing that a spouse or partner's retirement income will be adequate for their combined needs.

5.18 These conclusions are confirmed by the high proportion of part timers in the market research who believe that their likely main source of retirement income will either be the state pension or a partner's pension.

Table 5.18 Part Timers - Market Research Key Results

Specific reasons for not belonging to a pension scheme [5]	
Employer doesn't operate a scheme	68%
Only working for a few years	64%
State pension will be adequate	57%
Partners pension will be enough	50%

Likely main source of retirement income	
State pension	42%
Partner's Pension	31%
Pension Scheme	17%
Sale of assets	7%
Other	2%

Source:Lansdowne Market Research

5.19 IAPF believes that the pension needs of the majority of part timers can best be catered for through the current state pension system. To the extent that this is not perceived to provide an adequate level of pension it would be far more cost effective to increase the rates of payment than to ask the people concerned to

[5] These are the most important reasons given after the general concerns in relation to affordability, administration charges and complexity.

bear the disproportionately high administration costs inevitably associated with making relatively low contributions to an occupational arrangement.

Temporary Employees

5.20 According to the ESRI survey there are 56,000 people in this category, of whom only 6,000(11%) have made any pension provision. The results of the market research are:-

Table 5.20 Temporary Employees - Market Research Key Results

Specific reasons for not belonging to a pension scheme [5]		*Likely main source of retirement income*	
Only working for a few years	70%	State pension	35%
Too young to worry about pensions	60%	Pension Scheme	30%
Employer was not operating a scheme	55%	Partner's pension	17%
		Sale of assets	11%
		Other	3%

Source: Lansdowne Market Research

5.21 It is clear from the research that people in this category fall into two broad groups. Firstly there are those whose position is clearly temporary as they are in transition to more permanent employment. In the meantime formal pension provision is not an issue.

5.22 Secondly there are those whose temporary status is more long term and who require pension provision. Many of these will be in a similar position to part-timers for whom the state pension will provide an adequate replacement income. Nevertheless it must be recognised that the existing structures do not cater very well for persons in this category who wish to make provision for their retirement on a voluntary basis. The IAPF's proposal addresses this point.

Full Time Permanent Employees

5.23 Out of a total of 725,000 full time permanent employees 261,000(36%)[6] have no pension provision other than the state pension. The ESRI survey suggests

[5] These are the most important reasons given after the general concerns in relation to affordability, administration charges and complexity.

that the majority of these are employed by small indigenous companies (which have a poor record in relation to pension provision), are young and are relatively low paid. This is supported by the market research for this group, the key findings of which are:-

Table 5.23 Full Time Permanent Employees - Market Research Key Results

Specific reasons for not belonging to a pension scheme [5]		*Likely main source of retirement income*	
Employer doesn't operate a scheme	65%	State pension	36%
Retirement funded through savings	57%	Pension scheme	31%
Too young to worry about pensions	57%	Sale of assets	14%
Only working for a few years	54%	Partner's pension	11%
		Other	5%

Source: Lansdowne Market Research

5.24 Further analysis of the coverage data by income (see below) helps to throw further light on the true coverage situation for part time, temporary and full time permanent employees.

Income Distribution

5.25 Based on data from the ESRI Living in Ireland Survey and Hughes (1997) occupational pension coverage has been mapped against the actual distribution of income amongst the employed population in the table below:-

[6] This excludes 49,000 who are simply waiting to join their employer's pension scheme and, therefore, have a strong and reasonable expectation of occupational coverage in the near future.

[5] These are the most important reasons given after the general concerns in relation to affordability, expenses and lack of understanding.

Table 5.25 Distribution of Incomes - State and Occupational Coverage

Income Deciles	*Average Weekly Earnings*	*Existing State Pension* *as a % of Average Weekly Earnings*	*Occupational Coverage*
1st	£100	78%	3%
2nd	£146	53%	7%
3rd	£183	43%	20%
4th	£215	36%	41%
5th	£247	32%	52%
6th	£284	27%	58%
7th	£335	23%	72%
8th	£400	20%	78%
9th	£514	15%	89%
10th	£779	10%	89%

Sources: ESRI Living in Ireland Survey 1994, Department of Social Welfare, Hughes(1997)
Notes: Income data converted from hourly to weekly base on assumption of 40 hour working week: 10% income growth assumed between 1994-1997

5.26 Clearly, and not surprisingly, there is a high negative correlation between the state pension replacement ratio and the incidence of occupational coverage. The higher the replacement ratio the less occupational cover is needed. On the basis of this data it could be argued that the state pension does a reasonable job for those people in the bottom quartile of the income distribution. This covers 230,000 employees of whom 210,000 do not have any occupational provision. Allocating these on an approximate basis over the part time temporary and full time categories and factoring in the previous total coverage analysis in respect of the self employed results in the following overall analysis of total coverage.

Table 5.26 Total Coverage

	Total In Group	*Occupational Coverage ESRI Survey 000's*		*Estimated Total Coverage 000's*	
Self Employed					
Agricultural	119	14	12%	70	59%
Non-Agricultural	146	58	39%	90	62%
Total Self Employed	**265**	**72**	**27%**	**160**	**60%**
Employed					
Not yet eligible	49	0	0%	49	100%
Part-timers	87	7	8%	77	89%
Temporary	56	6	11%	36	64%
Full time permanent	725	463	64%	573	79%
Total Employees	**917**	**476**	**52%**	**735**	**80%**
Total At Work	**1182**	**548**	**46%**	**895**	**76%**

Sources: ESRI Survey, IAPF estimates

Analysis of Coverage by Age

5.27 The analysis to-date has focused on current levels of pension coverage. However pension coverage is dynamic and trends in the level of coverage are, in practice, heavily influenced by the changing age profile of the underlying population. Supplementary information on occupational pension coverage levels by age has been requested from the ESRI, through the Pensions Board, so that a detailed projection of likely future coverage levels can be made. At the time of preparation of this submission this information is not to hand and use has been made of the age based coverage estimates included in the Consultation Document as set out below:-

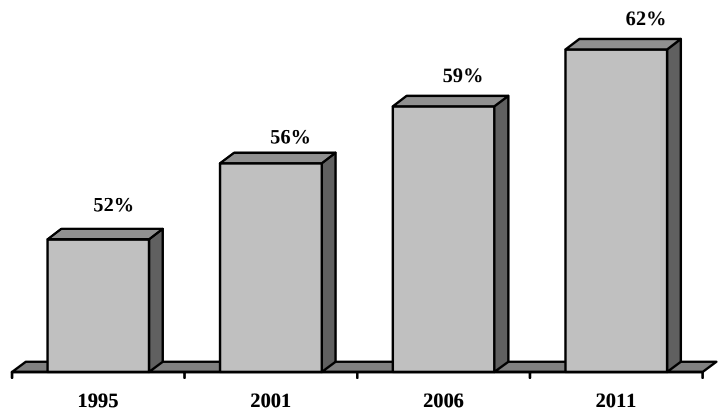
Table 5.27 Occupational Coverage by Age

Age band	*Coverage*
Up to 29	19%
30-39	65%
40-65	80%

Source: Consultation Document

5.28 Based on this information and labour force data the results of the projections carried out by the IAPF are set out in the table below.

Table 5.28 Projected Occupational Coverage over next 15 Years



Sources: Consultation Document, Labour Force Survey 1995, IAPF Estimates

5.29 This pattern of rising pension coverage is consistent with the market research findings. Of those respondents in the 18 to 24 age group 67% expect to start participating in a formal pension arrangement within the next 10 years and 52% of those in the 25 to 34 group expect to participate within the next 5 years.

Conclusions from IAPF Analysis - Future Pensions Policy

5.30 The first conclusion is that pension coverage in the fullest sense of the term is much greater than the 52% suggested by the ESRI survey - IAPF's estimates would suggest total coverage is in the region of 76%. Coverage is also likely to increase as the working population ages.

5.31 Notwithstanding these points it must be accepted that there is a problem. Barriers clearly exist to the further extension of occupational provision (formal or otherwise) to that section of the working population which needs it. The IAPF proposal set out in this submission addresses these barriers.

5.32 It is clear that no single solution will meet the needs of all those in the workforce. For this reason IAPF is proposing a three tiered approach to future pension policy:-

- An improvement in the state pension system to look after those who cannot afford to make any further pension provision. This involves both increasing the level of pension provided to achieve the minimum level of income recommended by the Commission on Social Welfare and maintaining the pension at this level in real terms.

- The introduction of a simplified pension contract - **The Personal Retirement Account -** to facilitate those who do not understand pensions or who believe the charges currently involved are too high. In view of the numbers in these categories who currently claim that they have no intention of ever participating in a pension scheme this initiative will have to be supported by a considerable education campaign to get across the message that easy, cost effective pension provision is both desirable and possible. Details are set out in Section 7.

- A simplification of the taxation and regulatory regimes for group schemes. This would ensure, inter alia, that pensions will be based more on a person's career rather than being job focused and would close any gaps in current disclosure requirements. Details are set out in Section 8.

5.33 Based on the analysis set out above IAPF does not believe that mandatory occupational provision is appropriate, principally because:-

- The improvements which are proposed in the state pension will, in themselves, meet the objective of ensuring an adequate basic retirement income for all.

- The state already operates a mandatory system. There are obvious inefficiencies in having two parallel mandatory systems.

- It could jeopardise the stability of existing second pillar arrangements.

Summary

5.34 The IAPF has carried out a detailed analysis of retirement coverage having regard to the total resources available on retirement, comprising both formal pension provision and other assets and savings. This analysis is based on the following:-

- The ESRI 1996 Survey on Pension Scheme Coverage.
- Additional data on pension coverage in relation to income distribution.
- The market research commissioned by the IAPF from Lansdowne Market Research into Non-Pension Holder Coverage.

5.35 The Market Research disclosed a wide range of reasons for non coverage. The top three reasons common to all employment categories were affordability, administration charges and complexity.

5.36 The Market Research also indicated a wide variety of reasons for not participating in a formal pension scheme. These include not being able to afford to join, accepting the state pension as adequate, having alternative sources of income and considering that pension provision is something for the future. The research also revealed large numbers who indicated they did not understand pensions.

5.37 Having regard to the results of the coverage survey and the market research IAPF is proposing a three tiered approach to future pension policy:-

- An improvement in the state pension to look after those who cannot afford to make any further pension provision.
- The introduction of a new simplified pension system, Personal Retirement Accounts. This to be supported by an educational and promotional campaign, managed by the Pensions Board, to encourage pension provision.
- A simplification of the taxation and regulatory regimes for group schemes.

6. Reforming the State Pension System

Overview

6.1 The purpose of this section is to develop IAPF's proposals for improving the pensions provided under the state pension system.

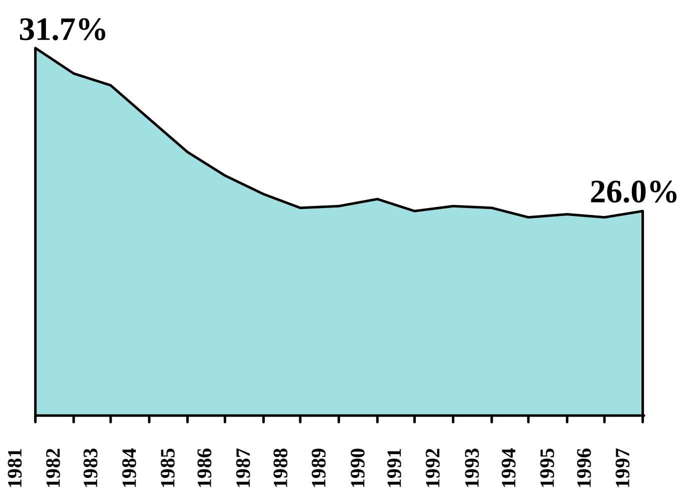
Commission on Social Welfare Recommendation

6.2 The Commission on Social Welfare (CSW) in its Report issued in 1986 recommended that all social welfare recipients should be entitled to what was described as a minimally adequate basic payment. Using a number of different methodologies it produced a series of estimates in the range £50 to £75 per week for a single person in 1985.

6.3 During 1996 the Department of Social Welfare asked the ESRI to review and update the CSW recommendations. The ESRI estimated that the updated range was then £75 to £96 per week. This in turn represents a range of 27.3% to 34.4% of National Average Earnings (NAE)[1]. It should be noted that this range is wider than in 1985

6.4 To place these recommendations in context the following table shows how state pensions have declined as a percentage of earnings over the last 15 years.

Table 6.4 State Pension as a Percentage of NAE



Sources: CSO Statistical Bulletins, Department of Social Welfare, IAPF estimates

[1] All Industrial Workers/All Industries

6.5 IAPF believes that pensioners should:-

- be ensured an adequate income in retirement.
- benefit from general improvements in economic prosperity.

and proposes, therefore, that state pensions should be increased to a level towards the top end of the updated CSW range. Ideally this should be done as early as possible but, recognising budgetary constraints, IAPF proposes that the increase should be phased in over a 5 to 10 year period.

6.6 The effect of IAPF's proposal is that the state pension will be increased gradually to 35% of NAE. In 1997 terms this represents a pension of approximately £100 per week. The maximum qualifying adult's allowance should be retained at 60 % of the personal rate.

6.7 IAPF does not see any merit in retaining a lower rate for social assistance (means tested) pensions and proposes, therefore, that the current maximum rates should be increased up to the level of the enhanced state pension over the same time scale.

6.8 The effect of this proposal over the range of actual incomes in the employed workforce is set out below:-

Table 6.8 Employees Income Distribution - Existing and Proposed State Pension

Income Deciles	*Average Weekly Earnings*	*Existing State Pension* *as a % of Average Weekly Earnings*	*Proposed State Pension* *as a % of Average Weekly Earnings*
1st	£100	78%	100%
2nd	£146	53%	69%
3rd	£183	43%	55%
4th	£215	36%	46%
5th	£247	32%	40%
6th	£284	27%	35%
7th	£335	23%	30%
8th	£400	20%	25%
9th	£514	15%	19%
10th	£779	10%	13%

Sources: ESRI Living in Ireland Survey 1994, Department of Social Welfare,
Notes: Income data converted from hourly to weekly base on assumption of 40 hour working week: 10% income growth assumed between 1994 and 1997.

Pension Increases

6.9 Having established a level of state pension which will achieve the goal of maintaining a basic standard of living it is essential to maintain the real value of this pension. There are two main options:-

- Index pensions to price increases as measured by the Consumer Price Index. While this has the merit of maintaining purchasing power it does not allow pensioners to share in future economy prosperity.
- Index pensions to the future growth in average earnings.

6.10 The difference between the two approaches is illustrated by the following table which shows, for different gaps between price and wage inflation, the variation in the pension payable as a percentage of NAE if the State pension were to be linked to price increases. Actual experience over the last 20 years has been that wage inflation has exceeded price inflation by approximately 2% per annum.

Table 6.10 Projected State Pension as Percentage of NAE

Rate of wage increases in excess of price inflation	*0%pa*	*1%pa*	*2%pa*	*3%pa*
***Base year*[1]**	35%	35%	35%	35%
5 years later	35%	33%	32%	30%
10 years later	35%	32%	29%	26%
15 years later	35%	30%	26%	22%
20 years later	35%	29%	24%	19%

6.11 On the basis of the above table IAPF considers that it will not be possible to sustain a system where pensions are solely linked to prices. In addition such an approach cannot be defended as socially equitable in the longer term since it does not allow pensioners to benefit from future prosperity. For these reasons IAPF strongly proposes increasing pensions in line with increases in average earnings.

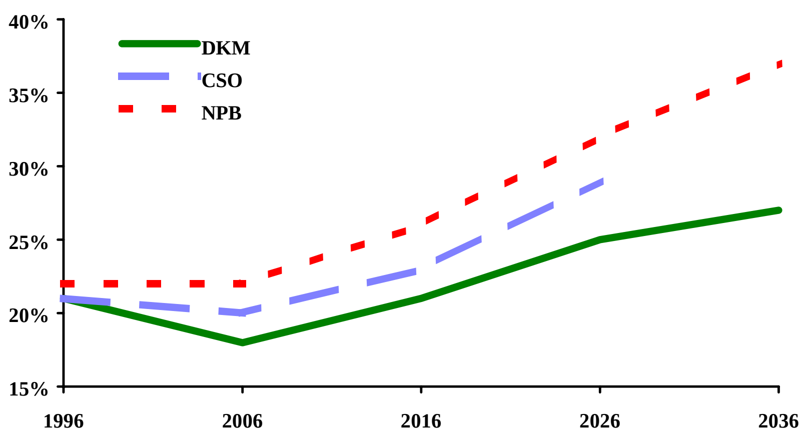
[1] The year the state pension reaches 35% of NAE.

6.12 Because of the importance of certainty IAPF also proposes that the commitment to maintain pensions in line with average earnings should be formalised in legislation.

Financing - Future Sustainability

6.13 In a Pay-As-You-Go environment a key driver of future state pension costs is the old age dependency ratio (the number of persons over age 65 as a percentage of the working population - defined as those between ages 20 to 64). Various projections of this ratio have been carried out in recent years with widely differing results as is illustrated below:-

Table 6.13 Old Age Dependency Ratios - Differing Projections



Sources: NPB Report(adjusted to achieve comparability), Consultative Document, CSO Population and Labour Force Projections

6.14 Further information will become available when the results of the current actuarial review of state pension costs are published. In the meantime, for the purpose of projecting future costs, IAPF has used the CSO projection as a base, representing as it does the middle ground between the alternatives available. Building on this data and making assumptions regarding future economic experience the table below sets out an approximate calculation of the emerging costs (as a percentage of GDP) of existing benefits (linked to prices or wages) compared to the IAPF proposal.

Table 6.14 Projected Cost of IAPF Proposal

	CSO Old age dependency ratio projection	Costs as a Percentage of GDP: Existing Benefits, Linked to prices	Linked to wages	IAPF Proposal
1996	21%	3.1%	3.1%	**3.1%**
2006	20%	2.2%	2.7%	**3.4%**
2016	23%	1.9%	2.9%	**3.7%**
2026	29%	1.8%	3.3%	**4.2%**
2036	32%e	1.5%	3.3%	**4.2%**

Assumptions	*Real GDP Growth*		*3% pa*
	Real Wage Growth		*2% pa*

Sources: CSO Population and Labour Force Projections (extrapolated to 2036), IAPF estimates.

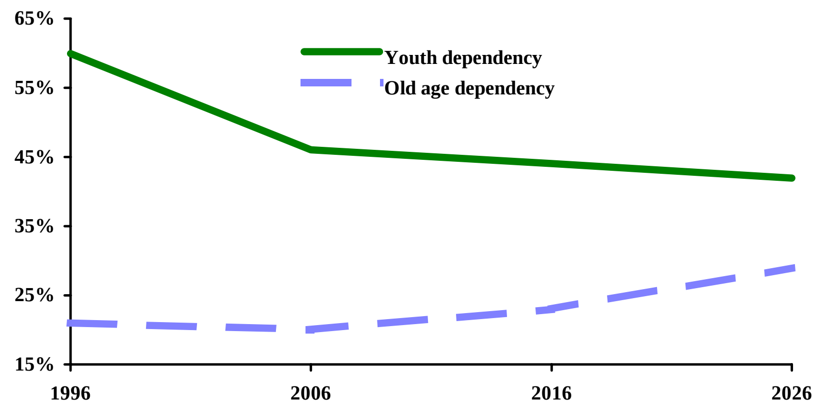
6.15 Based on this analysis IAPF, therefore, considers that it is well within the capacity of the Irish economy to absorb increased pension costs of the magnitude indicated. Should the projections prove to be too optimistic it should be remembered that there are a number of particular factors which may have the effect of offsetting or reducing the impact of any extra cost:-

- Over the last few years the Irish economy has experienced a faster rate of growth than almost all other developed countries. All indications are that this growth is set to continue into the foreseeable future.

- Extra state pension benefits will generate additional tax revenue.

- Increases in the old age dependency ratio will be offset by falling levels of youth dependency as illustrated below:-

Table 6.15 Youth Dependency Decline



Source: CSO Population and Labour Force Projections

6.16 Adopting the IAPF proposal is unlikely to damage our international competitiveness given the high benefit levels and less favourable demographic situation which tends to prevail in other countries. The analysis below which includes the cost of public service pensions confirms this point.

Table 6.16 Comparison of Projected State Pension Costs

	Ireland - IAPF Proposal	*UK*	*Germany*
1995	4.3%	4.5%	11.1%
2000	3.5%	4.5%	11.5%
2010	3.6%	5.9%	11.8%
2020	4.4%	6.2%	12.3%
2030	5.0%	7.8%	16.5%
2040	6.2%	8.5%	18.4%

Sources: Consultative Document, IAPF estimates

6.17 There is a debate starting about the merits of replacing PRSI contributions, in full or in part, by general taxation. IAPF does not have a view on the appropriate approach which is largely concerned with employment creation rather than pension provision.

Social Solidarity

6.18 The proposed increase in the level of the state pension overcomes one of the major barriers to increased pension coverage, especially amongst the low paid, identified by our market research - **affordability.** By financing an adequate pension through the PRSI system (or general taxation), in effect the less well off will be supported by more prosperous members of the community.

Summary

6.19 As part of it's proposal for future pension policy IAPF proposes that the state pension (single persons rate) is increased to 35% of National Average Earnings over a 5 to 10 year period. This rate should also apply to social assistance pensions.

6.20 Pensions should then be maintained at this level through legislation.

6.21 IAPF considers that financing the proposal is well within the capacity of the Irish economy - over 40 years costs are projected to grow from 3.1% to 4.2% of GDP. The resultant costs are still significantly less than those in other developed countries.

6.22 The income redistribution inherent in PRSI (or tax) based financing of the improved benefits is consistent with social solidarity and addresses the "affordability" concerns of the lower paid as emerged in the market research.

7. Introducing Personal Retirement Accounts

7.1 The purpose of this Section is to set out IAPF's proposal for a new form of pension contract, the Personal Retirement Account (PRA).

Background

7.2 In many respects the existing provisions for voluntary retirement provision - occupational pension schemes approved under the 1972 Act and retirement annuity plans approved under the 1967 Act - have worked well. Around 50% of the workforce (80 % of those over age 40) have some form of coverage and the majority of these are satisfied with their arrangements. There are, nevertheless, some desirable reforms and these are outlined in the next Section.

7.3 The market research carried out for IAPF has also shown that there is an identifiable section of the workforce who are not so well served by the present system. Broadly speaking these are employees in smaller companies where a company scheme is not provided and where the level of earnings involved does not make them a viable prospect for existing pension scheme providers.

7.4 There are also categories of workers where the irregular nature of their work makes it unlikely that they will ever become participants in pension schemes as they are currently structured.

7.5 In addition it is desirable to simplify the present treatment of retirement annuity plans and to introduce better controls on the sale of such plans.

7.6 To deal with these issues IAPF proposes the introduction of a new form of pension arrangement, the Personal Retirement Account (PRA). Structurally PRAs would be modelled closely on existing retirement annuities. They would be owned directly by the individual involved and would be set up as an insurance contract or under trust - with the trustee in this instance functioning mainly in a custodian capacity.

7.7 PRAs would be a pension vehicle for the following:-

- Self employed contributions including, possibly, existing retirement annuity contracts approved under the 1967 Act

- Employee and employer contributions as an alternative to group schemes. However where the employer was not willing to contribute employees could make contributions on their own.

- Buy out bonds, replacing the existing provisions in the case of new contracts after the date of introduction.

- AVC contributions as an alternative to the arrangements currently available.

7.8 An important aspect of PRAs is that they are owned by the individual account holder and the agreement of an employer, even one who has been making contributions, is not required when availing of the benefits and various other features. This gives a number of advantages:-

- The account is totally transferable between different employments and when moving from self employed to employed status (or vice versa). Thus it avoids both the complexity and the additional transaction costs usually associated with such changes.

- It will be flexible enough to cope with breaks in employment such as career breaks, family leave and even periods without employment.

Tax treatment

7.9 As an approved pension contract PRAs should qualify for the same general tax treatment as existing group schemes. This should include taking up to 150% of earnings at retirement as a tax free lump sum (which is also broadly consistent with the tax-free lump sum available in redundancy situations).

Allowable Contributions

7.10 Currently the maximum allowable contribution an individual can make under a retirement annuity is 15% of taxable earnings. The same limit applies to employee contributions, including AVCs in a group scheme context. This limit should be retained for PRA's.

7.11 An employer should also be allowed to contribute up to 15% of taxable earnings so that the maximum allowable contribution (when employers and employees contribute at the maximum) is 30% of taxable earnings.

Where applicable the limits are reduced by the contributions payable to all other approved pension contracts. As at present, the maximum limits should be increased in respect of those over age 55.

7.12 It is proposed, in line with developments in taxation in general, that the controls on maximum contribution limits and benefits at retirement should be predominately though self- assessment. Appropriate penalties for abuse, in line with those for other areas of the tax code, will be needed. The legislation should also include an onus on approved providers (see 7.19) and any professional advisers involved in PRAs to advise the Revenue if they suspect that any breach of the approval limits has occurred.

International Experience

7.13 Arrangements similar to PRAs are now a feature of pension provision in a number of countries.

7.14 They have been especially popular in the US where they are known as 401 (k) Plans. The tax treatment is similar to that for pension schemes in Ireland. An interesting feature is that withdrawals from the accumulated fund other than on death or retirement can be made in the event of severe financial hardship. It is also possible to borrow from the fund for house purchase. The facility addresses one of the reasons given in the market research for non coverage - that it is not possible to withdraw cash if and when it is needed. A more restricted form of this facility should be considered for Ireland (see 7.24).

7.15 The corresponding UK experience has been much less satisfactory with a series of disasters largely caused mainly by the option, provided under legislation, to use the contract to opt out of group scheme. IAPF strongly recommends that a similar options should not be made available in Ireland under any circumstances.

7.16 In addition to the problems caused by " opt outs" the UK market has experienced a lot of mis-selling, mainly as a result of unsustainable projections of future benefits. IAPF proposes that the Pensions Board should be given responsibility to oversee the marketing of PRAs and to make appropriate regulations in order to avoid similar problems

Annuity Risk

7.17 Most defined contribution pension schemes leave the annuity risk with the retiring member. This risk arises because the annuity rate used to convert the accumulated fund at retirement into a pension is variable, depending totally on interest rates at the time of retirement. In addition, because interest rates are low at present, the annuity rate is currently perceived to offer very poor value.

7.18 IAPF proposes that the retiring members should be free to keep the accumulated fund on deposit and draw down income only for a short period, say, 3 years, after retirement after which time annuity purchase would be obligatory. In addition IAPF is actively encouraging the life offices among its membership to introduce new products which cope better with fluctuating investment conditions around the time of retirement.

Approved Providers

7.19 The success of the introduction of PRAs depends in part on their being widely available. It is proposed, therefore, to introduce the concept of an approved provider. An approved provider should be an organisation, most likely a financial institution, which satisfies the conditions for approval set down by a regulatory body such as the Pensions Board or the Central Bank. These conditions must include capital adequacy and financial soundness.

7.20 Organisations other than financial institutions could apply to become approved providers provided they satisfy the various requirements including capital adequacy. Alternatively organisation such as trade unions and industry bodies could act as PRA sponsors, forming links with suitably qualified financial institutions.

The Role of the Pensions Board

7.21 In general it is proposed that the Pensions Board should have the same responsibilities in regard to PRAs as they have in regard to defined contribution pension schemes.

In addition the Board should have three further responsibilities:-

- Authorising approved providers if this role is not undertaken by another regulatory body (see 7.19).
- Monitoring the types of investment permissible under PRAs and ensuring, through disclosure regulations, that contributors are fully aware of the nature of the investment risk they are undertaking . This would apply as much to deposit contracts as to equity based ones since each, in its own way, carries an investment risk.
- Monitoring the marketing of PRAs to ensure the charges involved are clear and are fully disclosed. If experience suggests that this is not sufficient to protect contributions consideration will have to be given to allow the Pensions Board to control charges.

7.22 These responsibilities will impose new demands on the Pension Board's resources. It is proposed that these should be funded by a levy on all PRAs - in the early stages the cost should be borne by the Exchequer.

7.23 In carrying out this role the Pensions Board should have due regard to the existing consumer regulations including the various codes of practice applicable to members of the life assurance industry body, the Irish Insurance Federation.

Withdrawal Option

7.24 In order to further encourage additional private pension provision IAPF proposes that consideration should be given to allowing early cash withdrawals under PRAs of up to 50% of the then maximum tax free lump sum amount at any time after age 50 to meet the cost of any health related expenses that are not covered under any form of insurance or in the event of redundancy or serious financial hardship. Approval from the individual's Inspector of Taxes would be required in each case and the lump sum option at retirement would be reduced by the amount withdrawn.

Summary

7.25 IAPF's proposal includes the introduction of a new form of pension contract- the Personal Retirement Account (PRA). This is intended to be used for contributions from the self-employed, contributions from employers and employees, buy out bonds and as an alternative option for AVCs.

7.26 The key features of PRAs would be as follows:-

- They would be set up either as insurance contracts or under trust.
- The account would be personal to the contributor, thus facilitating changes in employment status in a cost effective way.
- The tax treatment would be the same as for existing pension schemes including the facility to take up to one and a half times earnings as a tax free amount at retirement. In addition up to 50% of the accumulated fund could be withdrawn tax free at any time after age 50 to meet health related expenses or in the event of redundancy or severe financial hardship.
- PRAs could only be marketed by approved providers, usually financial institutions and other organisations who satisfy the conditions for approval including capital adequacy.
- The maximum contribution allowable, inclusive of contributions to other approved pension plans, would be 30% of taxable earnings (with higher limits for those over age 55).

7.27 The Pensions Board should be given the following additional responsibilities in respect of PRAs:-

- Authorising approved providers.
- Monitoring the investment vehicles permitted and making regulations in respect of the related investment risk.
- Overseeing the marketing of PRAs with appropriate powers to intervene should this become necessary.

8. Reforming Current Arrangements

8.1 Existing pension structures, although they have served pension provision well, are beginning to show their age and IAPF believes that some reform of these structures, particularly in the taxation area, is appropriate to meet changing needs. This was one of the main conclusions of the Pensions Forum (see 3.2).

Suggested Group Scheme Reforms

Service used to Determine Maximum Benefits

8.2 Under existing Revenue Practice for group schemes the determination of maximum benefits is based on an employee's service in his/her last job immediately preceding retirement or leaving service. This is inconsistent with the philosophy of a **career rather than a job** based pension. IAPF would accept that in practice very few employees, even the most mobile, find that their benefits are restricted by this requirement. Also, a flexible approach has been taken by Revenue officials in interpreting existing rules in individual situations. Nonetheless the present situation does give rise to a lot of unnecessary complexity.

8.3 Therefore, IAPF proposes that benefits should, in future, be calculated by reference to a person's total period as a PRSI contributor. Some special provisions will be required to deal with those who, although in employment, were at some stage outside the scope of PRSI contributions. These include the self-employed prior to 1988, new public and civil servants prior to April 1995 and employees earning over a specified income limit up to the early 1970's.

8.4 In conjunction with the above the minimum periods of service required to qualify for Revenue maximum benefits (10 years in the case of pensions and 20 years in the case of lump sum benefits) should be retained even though the calculation is based on the aggregate period of PRSI service.

8.5 In practice the financial impact of the above change may be of little significance. In the vast majority of circumstances there would be no change in the overall maximum benefit limits. It follows that there would be little, if any, increase in the "cost" of existing tax reliefs. If it was a concern that those in a position to determine their own remuneration/pensions structure could abuse the new rules it may be appropriate to include some restrictions with regard to "controlling directors".

8.6 In summary, the main reasons for proposing a switch to PRSI based service are:-

- it is consistent with the changing nature of employment;
- it is easier for members to understand;
- it reduces complexity and, therefore, unnecessary administration expense;
- it creates a framework for the integration of PRAs and group schemes (see 8.10).

Retirement Age Flexibility

8.7 The current Revenue approval procedures require that a pension scheme has a specified " normal retirement age " - usually age 65. Where an employee wishes to retire earlier, which is a growing trend, the benefit approvable has to be proportionately reduced.

8.8 IAPF does not feel that this requirement reflects the reality of the current work place and it proposes instead that it should be possible to retire at any time between 60 and 70 on the maximum approvable benefits based on service completed at the date of retirement. Where retirement takes place earlier than age 60 the proportionate reduction should be based on a normal retirement age of 60.

8.9 This simplification has the further advantage that it is more easily understood and thus easier for employees to plan for early retirement. In conjunction with this change it should be made possible for employees to fund towards an earlier retirement age than 60 - under current rules this is not possible.

Integrating Group Schemes and PRAs

8.10 There are a number of possible ways, at an individual level, in which group schemes and PRAs will interact. A framework is needed to cater for such situations which, as far as possible, minimises complexity while at the same time protecting the position of the Revenue.

8.11 This is a highly technical subject. IAPF has done some initial work on how the regulatory framework might operate in a number of typical situations. This is described in Appendix 1. More work needs to be done and IAPF is willing to participate in any working group which may be established as part of NPPI to study this area.

Early Leavers

8.12 The National Pensions Board in its First Report made various recommendations regarding the treatment of early leavers. These recommendations were reflected in the Pensions Act 1990 which sets out a number of requirements in respect of defined benefit schemes :

- Obligatory vesting of preserved benefits after completion of 5 years pensionable service;
- Preservation of pensions in respect of future service which was introduced from January 1991. Since 1996 these benefits are also subject to revaluation at the lower of 4% per annum or the increase in the CPI.

8.13 The recommendations of the National Pensions Board are over 10 years old and in the meantime work practices and job mobility have changed significantly. The ESRI Survey shows that 45% of all pension schemes were established in the last 10 years. In addition IAPF's own benefits survey indicates that 63% of all members already provide benefits for early leavers in respect of pre 1991 service. As a result improvements in preservation in respect of pre 1991 service could now be done without imposing undue financial strain on pension funds. Specifically it is now proposed that:-

- The minimum vesting period should be reduced from 5 years to 2 years.
- Basic preservation in respect of pre 1991 service should be introduced immediately.
- The revaluation of these benefits should take effect from 2006 .

8.14 In the case of defined contribution schemes the current requirement is for employees to have an entitlement to the accumulated value of the contributions paid on their behalf after 5 years. In line with the improvement proposed for defined benefit schemes IAPF proposes that this period should be reduced to 2 years. The various proposals in relation to defined contribution disclosure (see 8.16) will also improve the position of early leavers.

8.15 It is also important to ensure that members receive any deferred benefits to which they are entitled. To facilitate this IAPF propose that the Pensions Board should agree with all providers of pensions a central register of deferred pensions and buy out bonds using PRSI numbers as a reference.

Defined Contribution Schemes - Illustration of Benefits

8.16 It is often difficult for members of defined contribution pension schemes to get a clear indication of the benefits that are being provided on their behalf. There are some practical problems such as agreeing what are appropriate assumptions regarding future investment returns. Nevertheless it is both necessary and possible to improve the present position.

8.17 IAPF proposes, therefore, that it should be a requirement on the trustees of all defined contribution schemes to provide an illustration at 3 yearly intervals of future expected benefits. The Pensions Board should specify the format of such illustrations including what assumptions are appropriate in regard to future investment returns.

Defined Contribution Schemes - Investment

8.18 The responsibilities of defined contribution trustees in the area of investment is a source of considerable concern at present. There seems to be an emerging consensus that legally (under trust law and the Pensions Act) trustees cannot delegate investment decision making entirely to a member without having regard to the appropriateness of the decisions then made. This places trustees in an invidious position as there is a lack of clarity as the degree to which they should be involved in the investment process and the extent of their potential liability.

8.19 IAPF strongly believes that this situation should be regularised by amending legislation empowering complete delegation and which in specific terms sets out the responsibilities of defined contribution trustees. A move in this direction is particularly urgent with the proposed introduction in the near future of PRAs - to ensure market stability it is essential that there should be a level playing pitch between PRA's and defined contribution schemes.

Industry Pension Schemes

8.20 In a number of countries there are very successful industry based pension schemes which were set up initially as a result of employee and trade union agreements in respect of a particular industry. The advantages of such schemes are low administration costs due to economies of scale and the absence of any great need to incur marketing costs. Transfers of employees between different employers - which is a common feature in some industries - is greatly facilitated since benefits are based on total service in the industry.

8.21 A similar successful scheme is operated in Ireland by the Construction Industry Federation. However there have been a number of attempts to set up arrangements for other industries which have not had much success. Even within the construction industry compliance is a big issue and many companies who should be participating do not in practice do so. A number of affinity groups have also set up arrangements for their members with varying levels of success.

8.22 IAPF considers that there is more scope for industry schemes as a way of improving overall pension coverage in a very cost effective way and it urges the employer representative bodies and the trade unions to explore ways to develop such coverage. Pending the outcome of such discussions IAPF does not have any specific proposals to make in regard to changes in the taxation or regulatory regimes which would facilitate such schemes.

Summary

8.23 IAPF proposes that the following changes should now be made in the taxation and regulatory regimes governing approved pension arrangements.

- The maximum approvable benefits under approved pension schemes should in future be calculated by reference to the total period as a PRSI contributor. Some restrictions may then be needed in respect of "controlling directors".

- It should be possible to retire at any time between 60 and 70 on the maximum approvable benefits.

- A new framework should be introduced to facilitate the interaction of group schemes and PRAs while protecting the position of the Revenue.

- The requirements in respect of early leavers should be improved to reduce the current vesting period from 5 years to 2 years and to provide preservation for pre 1991 service (with revaluation from 2006 in the case of defined benefit schemes). The Pensions Board should agree the setting up of a central register of deferred benefits and buy out bonds.

- It should be a requirement on the trustees of defined contribution pension schemes to provide an illustration of future expected benefits at 3 yearly intervals. The Pensions Board should specify the format of such illustrations.

- The requirements in respect of the "investment risk" and the "annuity risk" proposed for Personal Retirement Accounts should be extended to defined contribution schemes.

- The position of trustees in relation to investment decisions on defined contribution schemes and PRA's should be clarified by legislation.

8.24 IAPF also proposes that employers and the trade unions should seek ways to actively promote industry schemes as a cost effective way of extending pension coverage.

9. ASSESSMENT OF PROPOSAL

9.1 This Section sets out an assessment of IAPF's proposal against the nine criteria set out in the Consultation Document. This proposal is as follows:

An improvement in the state pension to look after those who cannot afford to make any further pension provision.

The introduction of a new simplified pension contract - Personal Retirement Accounts. This is to be supported by an educational and promotional campaign, managed by the Pensions Board, to encourage pension provision.

A simplification of the taxation and regulatory regimes for company pension schemes.

Criteria 1 - Effect on Coverage

9.2 IAPF's proposal for improving the state pension system will benefit all sectors of the community including current pensioners and the unemployed. Indexing future pensions to the growth in average earnings also ensures that pensioners will share in the future prosperity of the economy.

9.3 IAPF is also proposing the introduction of cost effective Personal Retirement Accounts, supported by an educational and promotional campaign, in order to further extend occupational coverage.

Criteria 2 - Adequacy of Benefits

9.4 Improving the level of state pensions and indexing pensions to future increases in average earnings will greatly improve the future pension expectation of those who may have to rely totally on such pensions to provide for their retirement.

9.5 IAPF's proposals to improve the position of early leavers will also ensure that persons who move between jobs will be guaranteed a better pension when they reach retirement.

9.6 The new requirements on disclosure will ensure that members of defined contribution pension schemes and Personal Retirement Accounts have a much better understanding of the benefits they can expect to receive at retirement and are thus in a better position to adjust their arrangements where appropriate

Criteria 3 - Protecting the Status Quo

9.7 The challenge posed by NPPI is to improve overall pension coverage, targeted as far as possible to areas of greatest need, while at the same time protecting the rights and expectations of those who have satisfactory occupational arrangements in place.

9.8 IAPF's proposal aims to achieve this by focusing on the areas of greatest need, the lower income groups and those who are not in pensionable employment. Most occupational pension schemes integrate the benefits provided with state pensions. For such schemes the additional costs involved in financing the higher levels of state pension will be offset to a degree by the corresponding reduction in the occupational scheme (the offset is not exact due to the redistributive nature of the PRSI system).

Criteria 4 - Cost and Efficiency

9.9 The most cost effective way of improving occupational coverage is by increasing the pensions payable under the state pension system. The additional administration expenses will be negligible and there is considerable saving in not have to introduce a new compliance structure.

9.10 IAPF is also concerned that some aspects of occupational provision are perceived to be unduly expensive. For this reason its proposal includes a new emphasis on the disclosure of charges.

Criteria 5 - Robustness and Flexibility

9.11 The overall approach adopted by IAPF is to support a **robust state pension system** and **flexible occupational arrangements**.

- Because by its very nature pension provision is long term IAPF would regard **robustness -** the extent to which the system can be sustained over time - to be one of the more important criteria. The proposal satisfies this criteria. Linking pensions to earnings means that the state pension system will retain an acceptance over a long period. On the other hand, if the more recent approach of linking pensions to prices is continued the perceived value of the pension will decline and there will inevitably be demands to recast the overall system.

- Retaining occupational pensions on a voluntary basis means that employers can retain some **flexibility** over future cost levels should the markets in which they operate become very competitive. Many multinational employers, who are among the best providers of occupational pensions, have stated publicly that this flexibility was one of reasons which attracted them to Ireland in the first instance.

Criteria 6 - Solidarity

9.12 The Consultation Document refers to implicit social contracts in the current system *between Government and citizens and between generations.*

9.13 IAPF is concerned that a continuation of the practice of indexing state pensions to prices increases will over time devalue the system since pensioners clearly have an implicit expectation that they will continue to share in the general prosperity of the economy. Legislating that pensions are indexed to increases in average earnings is probably the most effective way of ensuring that the system retains its credibility.

9.14 It is also implicit in the regulatory regime governing occupational schemes that the state has set up adequate arrangements to ensure that members receive the benefits which they have been led to expect. This is largely achieved through the various measures included in the Pensions Act 1990 and monitored by the Pensions Board. However IAPF's proposal includes a number of further safeguards which are considered desirable in the light of experience. These are set out in Sections 7 and 8.

Criteria 8 - Fairness

9.15 IAPF's proposals meet this criteria in a number of ways:

- The proposed improvement in the state pension system would be applied to existing pensioners including those in receipt of means tested benefits

- The proposal is designed to be most beneficial to those who are most in need of improved provision while causing the minimal amount of disruption to those (and/or their employers) who have taken steps to ensure that they are adequately provided for at present.

- Various additional safeguards are proposed to ensure that those making occupational provision do not lose any of the benefit through no fault of their own and, in particular, that they will not be penalised unduly by changing employment.

Criteria 9 - Labour Market Implications

9.16 Clearly any increased expenditure on pensions will add to the costs of Irish businesses. However the way this increase is financed will have a major bearing on the situation - the more of the increased cost which is borne from direct taxation the lower the direct impact.

9.17 The only significant increased cost involved in IAPF's proposals is the increase in the cost of financing the improved state pension; as indicated above IAPF has no objection in principle if some or all of the cost of state pensions is transferred to general taxation.

Summary

9.18 Overall the IAPF analysis shows that its proposal satisfies the various criteria which the Consultation Document proposed should be used to assess all proposals put forward in response to NPPI.

APPENDIX 1 - INTEGRATING PRAs AND GROUP SCHEMES

Scenario 1	***An individual leaving or retiring from a group scheme with PRA assets or deferred benefits under previous group schemes.***
Problem	***How should Revenue maximum benefits be determined?***
Proposed solution	Adapting current practice would suggest an approach whereby the test to be applied in such circumstances would be to calculate maximum benefits (based on completed PRSI service and earnings at the date of leaving) and then offset from this the value of previously accumulated PRA and group scheme benefits. While this is theoretically sound it is potentially very cumbersome from an administration point of view in terms of the volume of information which might need to be collected and the diversity of possible sources for it. To address this concern it is proposed that group scheme trustees should be allowed as a first step to apply a much simpler test which might be structured along the following lines:- • For defined benefit schemes that the value of the entitlements[1] is less than 30% of final earnings for each year of service with that employer. • For defined contribution schemes that total contributions have not exceeded 30% in any one year in the course of that employment. The 30% benchmark has been chosen because it conforms with the proposed contribution limits under PRAs. This new test in reality would apply in the vast majority of cases. If necessary the more sophisticated test described could still be applied. This solution is predicated on the assumption that employers would not be allowed to make contributions to PRAs and a group scheme at the same time. To limit potential for abuse application of the new simple test might be restricted in the case of “controlling directors”

[1] For leaving service benefits this value could simply be the transfer value amount. If immediate pension benefits are payable this value might be determined by applying a Revenue specified factor.

Scenario 2	An individual contributes to both a PRA and a group scheme.
Problem	How to ensure that 15% earnings limit is not breached?
Proposed solution	All personal contributions made under a “net pay” arrangement to either a PRA or a group scheme should be aggregated and shown explicitly on an employee’s P60. Individuals may apply to their Inspector of Taxes for relief on any after tax contributions paid directly into a PRA. It would be a relatively easy task for the Inspector to assess the merit of any such claim by reference to the P60 information for the same tax year. To facilitate this process approved providers would be required to provide a certificate of contributions paid at the end of each tax year as currently happens in the case of residential mortgages.

Scenario 3	An individual with PRA and group scheme benefits at retirement
Problem	How to ensure that overall tax free lump sum limits are not breached?
Proposed solution	This should be dealt with on a self assessment type basis. An individual should be made aware at the point of retirement of the maximum monetary amount involved. He/she can then draw this down from any source or combination of sources. Any authorised provider or set of group scheme trustees who are asked to pay an individual part of this lump sum would then have an obligation to inform that person’s Inspector of Taxes of the amount paid. It should then be a relatively simple task for that Inspector to ensure that the overall lump sum limit had not been breached particularly given that most people only retire once.

PART 2:

THE RESPONSE OF THE IAPF TO THE QUESTIONS IN THE CONSULTATION DOCUMENT

THE RESPONSE OF IAPF TO THE QUESTONS IN THE CONSULTATION DOCUMENT

1. ***What should be the overall objective for national pensions policy? You should express this as explicitly as you can.***

   IAPF agrees with the objectives for a national pensions system as set out in the Final Report of the National Pensions Board. These require that the state provides directly through the state pension system an adequate basic income for everyone and facilitates and encourages supplementary provision on a voluntary basis.

   Part 1 Reference: 3.5 to 3.12

2. ***Should judgements about pension adequacy be based on consumption needs rather than on income?***

   It would be difficult in practice to make judgements about adequacy given the wide variety of individual circumstances.

   Part 1 Reference: 3.10

3. ***How should assets be taken into account in assessing Second Pillar pension adequacy? Should some categories of assets be ignored?***

   The importance of assets as a way of making retirement provision is clearly shown by the market research commissioned by IAPF. However, there is no direct link between assets and adequacy because of the wide variety of individual circumstances. For this reason IAPF strongly believes that the overall system should retain a considerable level of flexibility to enable individuals to make provision appropriate to their own circumstances.

   Part 1 Reference: 5.8 to 5.27

4. ***What earnings base should be used in considering replacement rates - final earnings, earnings averaged over a period, or something else?***

   The objective is to maintain the pre retirement standard of living. On this basis final earnings should be based on earnings close to retirement. Averaging may be appropriate in circumstances where earnings fluctuate significantly.

5. ***Should State pensions be indexed to prices, wages or some other reference point, bearing in mind the financing costs?***

For the reasons set out in the submission IAPF believes it is essential that state pensions are indexed to wages.

Part 1 Reference: 6.9 to 6.12

6. ***The Pensions Act improved the position of early leavers. Should more be done? If so, what are the priorities?***

IAPF proposes that the current requirements in respect of early leavers should be improved by:-

- reducing the minimum vesting period from 5 years to 2 years; and
- providing preservation for pre 1991 service (revaluation from 2006).

The Pensions Board should also arrange the setting up of a central register of deferred benefits and buy out bonds.

Part 1 Reference: 8.12 to 8.15

7. ***Can the coverage and quality of disability cover be improved? Would changing the nature of the benefit help? Should permanent health insurance be catered for under the same regime to allow better integrated pension plans?***

In principal, IAPF has no difficulty in including disability cover within the taxation and regulatory regime covering occupational pension schemes. However, before doing this there are a number of practical issues to be considered, perhaps the most important of which is the situation where disability may only be temporary.

To make progress IAPF proposes that the Pensions Board should, once NPPI is completed, set up a working party to review the options and to make recommendations. IAPF would be willing to participate actively in this review.

8. ***Long term care provision is a growing concern especially at older ages. Should long term care be included within the same financial framework as pension schemes?***

IAPF is currently involved in a joint study of the options for long term provision with the Society of Actuaries in Ireland and the Irish Insurance Federation. When this study is completed we propose that it should be used as a basis for establishing a new policy in regard to long term care.

9. ***What is your overall view of the existing arrangements for retirement provision across society as a whole?***

Based on the analysis in Section 4 IAPF considered that the existing arrangements for retirement provision as a whole work well. However, there are a number of gaps and IAPF's proposal is designed to address these.

Part 1 Reference: 5.1 to 5.37

10. ***What should be regarded as desirable and realistic levels of Second Pillar coverage in the different sectors of the population (such as lower paid employees, other employees, the self-employed, those not at work. etc.)? You should comment on both the extent of coverage and its adequacy.***

IAPF does not consider that it is either practical or desirable to pre-determine the appropriate levels of the Second Pillar coverage in view of the wide variation in individual circumstances.

Part 1 Reference: 3.9 to 3.12

11. ***What new incentives or initiatives might encourage increased coverage? Who should be targeted?***

The IAPF proposal includes three new initiatives:-

- The Pensions Board to be given responsibility, funded by the state, to promote better pension provision. By definition this should be aimed at those sectors of the workforce where cover is lowest;
- The introduction of Personal Retirement Accounts in order to encourage voluntary provision among those who are not well catered for by the present system;
- Discussions between the employer bodies and the trade unions to promote the increased use of industry schemes.

Part 1 Reference: 5.32, S7

12. *What do you feel are the main reasons for non-coverage?*

IAPF has a concern that views on non-coverage are based on pre existing prejudice. For this reason it commissioned market research on Non-Pension Holder Coverage from Lansdowne Market Research. The results of this research are analysed in detail in Section 5 and form the basis of IAPF's proposals.

Part 1 Reference: S5

13. *What measures can be taken to improve coverage for atypical employees?*

IAPF considers that atypical employees can be most effectively catered for by an enhanced state pension system along the lines proposed and by the introduction of Personal Retirement Accounts.

Part 1 Reference: 5.15 to 5.26

14. *Are there areas where there is over-provision at present?*

IAPF does not consider that there are any areas of over-provision which require attention.

15. *Should tax benefits be available without limit, to fund high replacement rates, or should the allowable replacement rate fall with rising income?*

It follows from the response to the previous question that tax benefits should be available without limit. It is important to emphasise that what is involved is taxed deferral as the pensions ultimately payable are taxed as income.

16. *Is there a cost-effective distribution channel which could reach the smaller employers and lower income workers? If so, what is it and how could it be achieved?*

The most effective way of providing an adequate retirement income for lower income workers is through the enhanced state pension system proposed by IAPF. The introduction of Personal Retirement Accounts should also provide a cost effective way of making additional provision, especially if the proposal of IAPF in regard to disclosure of charges is implemented.

Part 1 Reference: S7

17. Should individuals be helped to choose a more appropriate level of investment risk? How?

IAPF proposes that the legal position in relation to the investment of defined contribution schemes should be modified and clarified. The Pensions Board should also specify that appropriate warnings should be included as to the implications of any particular investment policy for future benefits.

Part 1 Reference: 7.21, 8.18

18. How can the 'annuity risk' be better managed?

Retiring members should be free to keep the accumulated fund at retirement on deposit for 3 years. In addition, the IAPF is actively encouraging the development of new products to cope better with the risk.

Part 1 Reference: 7.17 to 7.18

19. What could be done to manage the employer's costs and workload in respect of regulation without relaxing standards?

Other than implementing the various proposals with regard to greater disclosure of information on charges IAPF does not consider that any further action is required.

It is important also that the Pensions Board carefully manages the cost of providing its services in order to ensure that these are done in the most cost effective way.

20. Are small defined contribution schemes too complex. How could they be simplified?

IAPF agrees that small defined contribution schemes can, under certain circumstances, be too complex, especially for small employers. This is one

of the reasons which led to the proposal to introduce Personal Retirement Accounts.

Part 1 Reference: S7

21. Are levels of administration costs an inhibiting factor for those considering pension provision? Would new vehicles help?

The market research carried out for IAPF identified high costs as an important factor in discouraging provision. For this reason IAPF proposes greater disclosure of charges for Personal Retirement Accounts.

Part 1 Reference: 5.6

22. What should be done to ensure defined contribution scheme members (or retirement annuity plan holders) understand the likely real value of their prospective benefits?

IAPF proposes that it should be a requirement on the trustees of defined contribution schemes and PRA's to issue a statement at least every 3 years showing the expected retirement benefits. The Pensions Board should specify the form of these statements.

Part 1 Reference: 8.16 to 8.17

23. Are there other aspects of efficiency, quality and consumer protection to be considered?

Other than those referred to in the Submission IAPF has no specific issues which it thinks should be considered.

24. Should pension provision be structured on the basis of each individual having their own personal entitlements or on the basis of a pension scheme member with dependants? What might be done about existing entitlements?

As the Consultation Document points out this debate is complicated with similar issues arising in the areas of taxation and the broader range of social welfare benefits. IAPF considers that pensions provision should not be considered in isolation.

25. In view of changing work patterns, do we need new pension vehicles based on the individual's career rather than on each particular job held? If so, what type of vehicle would you favour?

The need to be more responsive to changes in working practice is one of the key reasons behind the thrust of IAPF's proposal including, in particular, the introduction of Personal Retirement Accounts.

Part 1 Reference: S7, 8.2 to 8.6, 8.10 to 8.15

26. What specific issues need to be addressed arising from new work or remuneration practices?

IAPF's proposal is based on addressing all the relevant issues.

27. Is the current approach to "Normal Retirement Age" sustainable? Will greater longevity make it feasible, or desirable, for people to work longer?

IAPF's proposal includes a change in the existing regulations governing the calculation of maximum benefits to allow for "normal retirement" at any age between 60 and 70.

Having regard to the age structures of the Irish population IAPF does not see any need to facilitate and encourage persons to work beyond age 65 (although there should be no disincentives to do so).

It is possible that this is something which may need to be considered at some stage in the future.

Part 1 Reference: 8.7 to 8.9

28. What needs to be done, if anything, to deal with the consistently large amounts available for investment?

The issue of pension fund investment has been dealt with in a number of previous studies and IAPF is broadly satisfied with the present position. If the state wish to encourage greater investment within Ireland it could consider a greater degree of privatisation of state companies, an area where Ireland is now considerably behind most other developed economies.

29. In what broad directions do you consider future policy should move in order to minimise any problem of long term sustainability in overall pension provision across the First and Second Pillars?

It is necessary to strike the right balance between providing an adequate level of retirement provision in the short term and being able to sustain this approach in the long term. IAPF believes that its proposal is the appropriate way to achieve this.

30. Which features or approaches in these (or other countries) seem particularly worthwhile and practical for Ireland?

Where appropriate, IAPF has commented on the position in other countries in putting forward its proposals.

31. Should there be a mandatory element in Second Pillar provision? What should its objectives be?

For the reasons set out in the submission IAPF does not favour introducing a mandatory element in second pillar provision. Instead, the emphasis should be on having a satisfactory state pension system and enabling individual employees to make occupational provisions appropriate to their own circumstances.

Part 1 Reference: 5.33

32. What involvement should the State have in regard to pensions? How should it be organised?

The role of the State should be to provide a basic income for everyone through the state system and to facilitate and encourage supplementary provision on a voluntary basis.

Part 1 Reference: 3.5 to 3.8

33. To which broad initiatives would you give highest priority? Which should be discarded? Why?

IAPF is putting forward a three tiered approach in regard to future pension policy:-

- Improving the state pension.
- Introducing Personal Retirement Accounts; and

- Reforming the regulatory and taxation regimes for existing occupational pension schemes.

IAPF considers that all of these initiatives are equally important and must be taken together.

34. For each of the broad initiatives in which you see merit:

- ***What would represent a successful initiative?***
- ***What are the main practical issues?***
- ***How could it be improved?***

These are dealt with in Part 1 of the submission.

35. What other major initiatives should be considered?

IAPF does not consider that there are any further initiatives to be considered other than the comprehensive list set out in the Consultation Document.

36. What do you see as being a realistic sequence and timescale for the initiatives you would like to see carried out?

IAPF's proposal is as follows:-

- The commitment to increasing the state pension to 35% of NAE should be immediate; the increase is to be phased in over 5 to 10 years.

- Legislation to support indexation of the state pension to earnings should be brought in as soon as possible and not later than 1st January 1999.

- The introduction of PRAs and the various reforms to the taxation and regulatory regimes should also be brought in as soon as possible and not later than 1st January 1999.

37. Are there any other major issues you feel are essential to the development of national pensions system or have a bearing on the whole National Pensions Policy Initiative?

IAPF considers that all the major issues are set out in the Consultation Document and have been responded to in its submission.

38. What steps would you favour to improve the current arrangements? Do you feel that such improvements, on their own, would constitute sufficient action under this Initiative?

IAPF's proposals include a number of initiatives to improve the current arrangements. These are set out in detail in the submission and summarised in the Executive Summary.

39. In the context of a voluntary system, which groups should primarily be targeted?

The long term sustainability of the overall pensions system requires that each group should be targeted in relation to its own specific requirements. This is very much the basis behind IAPF's proposal which covers both extending pensions coverage to those who are not currently covered and improving coverage for those who are already making occupational provision.

Part 1 Reference: 5.30 to 5.32

40. Is there a risk that a mandatory Second Pillar would fail to reach parts of the target group? How could this be minimised?

IAPF does not support the introduction of a mandatory occupational pension. If such an arrangement was introduced IAPF considers that the most appropriate way of ensuring the maximum level of compliance would be to link the arrangements to the existing taxation/PRSI deduction system.

Part 1 Reference: 5.33

41. If a mandatory system were to be introduced, how should it be designed and regulated to get the best balance of cost and effectiveness?

IAPF believes that its proposal addresses in a more satisfactory way the various issues which might otherwise be addressed through a mandatory scheme.

Nevertheless if it was decided to introduce a mandatory scheme the key considerations must be as follows:-

- The approach adopted must cause minimum disruption to current occupational pensions.

- The scheme should be targeted to those who are currently not covered under occupational schemes.

- There should be the opportunity for full discussion on any proposals before they are recommended to the government.

42. How important are tax incentives and should they be altered to promote the voluntary system or to support a mandatory system?

IAPF emphasises that the tax treatment of occupational pension schemes represents tax deferral. Maintaining these arrangements is essential in order to protect both the current levels of coverage and to encourage additional coverage.

Part 1 Reference: 4.16 to 4.21

43. Should the State get directly involved as an occupational pension provider in some form? What issues does this raise?

There are already a significant number of pension providers which has led to a very competitive market. Accordingly, IAPF does not see any advantage for the state to get directly involved as a provider of occupational pensions.

Part 1 Reference: 3.5 to 3.8

PART 3:

MARKET RESEARCH

(as presented by Lansdowne Market Research)

MARKET RESEARCH

Methodology

- In-home face-to-face interviews were conducted in April 1997 with 704 members of the working population broken down as follows:-

Working Status	*Effective Sample*	*Universe*
Permanent full-time	176	310,000
Temporary full-time	105	50,000
Part-time temporary/permanent	167	80,000
Self employed (Non-agri)	128	89,100
Self employed (Agri)	128	103,800
Total	704	632,900

Management Summary

- The findings from this study indicate a wide range of issues as responsible for people not having, or being members of, a private pension scheme. Essentially, non-pension holders need to be convinced that:-

  – Pensions can be afforded, if they start early enough;
  – Pensions do not impose too heavy charges;
  – Pensions are not too complicated;
  – Organising a pension is not too difficult.

- Those who take the view that pensions cannot be afforded tend to express a higher degree of concern about virtually every issue involved in belonging to a pension scheme than those who are not worried about affording a pension scheme. Those who have a cost concern seem to be also particularly concerned about the charges involved in organising a pension, their lack of understanding of pensions and being able to get access to the money if needed. They also report that their length of time working is too short for them to be able as yet to afford a pension (this may be related to the anticipated natural growth of income as the individual acquires more work experience).

- Those who are **not** concerned about being able to afford a pension - who might be thought to possess a more studied resistance to pensions - cite different motives. They are most likely to refer to having saved enough money for their retirement and to rely to a greater extent on their husband/wife for pension provisions.

- Studied resistance to pension involvement can also be based on other motives. Two out of three farmers believe that selling the business/farm will support their retirement. The self-employed in non-agricultural occupations are also prone to this view.

- Part-time and temporary employees are inclined to look to their husband's/wife's pension as a means of support, beyond the quite well-known limits of the state pension. (This group contains a high proportion of women).

- Many permanent and temporary full-time employees talk of becoming involved in a pension scheme but almost 1 in 3 claim that they never will do so. For many non-pension holders in full-time employment, their perceived youthfulness also acts as a barrier. For this sizeable group, accumulated savings are also believed to provide support after retirement.

- Age is clearly a major influence on perceptions of the need for a private pension. For those under 25, pensions can very often seem to be a distant need. 4 out of 10 say that they will start participating in a scheme in 10 years or more - or never! Only 4 in 10 seem to be farsighted at this age - and the bulk of these are putting off the involvement process for at least five more years. (This means that many would-be pension contributors would only be commencing private arrangements in their late 20s).

- Those aged 25 -34 are more likely to fall into the 'within five years' category (putting off the "evil day" of participation) or to think they will never need a pension. This may be in part linked to changes of lifestage, due to marital or business-related factors. From 35 years of age onwards, resistance to involvement in private pension schemes increases: over 4 in 5 of those aged 50 - 65 who do not have a private pension as yet say that they never will. Again, these are related to the well-known factors alluded to earlier.

- In many ways, youthfulness is responsible for the next set of issues - not being working for very long, can't afford a pension scheme at the moment, I'm too young to worry about a pension. This is followed in terms of importance by relative complacency about financial requirements (don't understand pensions, husband/wife pension enough, the state pension would be enough). Finally, financial ignorance is the least important contributor to the motivated resistance to pension holding.

- Some fear of involvement in pensions can be detected. It would be very helpful for educational/information strategies to be directed at non-pension holders, so as to impress on them the need for pension provision.

- It would also be helpful to work with companies who do not, as yet, have pension schemes to provide this opportunity to those who currently slip outside the pension net.

- Furthermore, it is apparent that some sectors of the economy are under-provided for in terms of pension schemes. Retail/shops, construction/building and hotels/catering are especially notable, beyond the farming/fishing sector. Intriguingly, those working in Irish - owned private companies represent a high proportion of non-pension holders.

BIBLIOGRAPHY

Central Statistics Office (1995): Population and Labour Force Projections 1996-2026

Central Statistics Office (1996a): Labour Force Survey 1995

Central Statistics Office (1997): Statistical Bulletin March 1997

Combat Poverty Agency (1997): Welfare Implications of Demographic Trends

Commission on Social Welfare (1986): Report

Department of Social Welfare (1996): Statistical Information on Social Welfare Services 1995

Department of Social Welfare and Pensions Board (1997): Consultation Document - National Pensions Policy Initiative

ESRI (1996a): Occupational and Retirement Annuity Coverage 1995

ESRI (1996b): Poverty in the 1990s: Evidence from the Living in Ireland Survey

ESRI (1996c): A Review of the Commission on Social Welfare's Minimum Adequacy Rates

Hughes, G. (1997): Pensions, Savings and Tax Expenditures

IAPF (1996): Benefits Survey 1995

IAPF (1996): Pensions Forum Report

Kehoe, J. (1995): Social Security in Ireland - An Actuary's View

McCarthy, T. (1995): Ageing Populations and Pensions Systems: Time Bomb or False Alarm

National Pensions Board (1987): First Report of the National Pensions Board

National Pensions Board (1988): Report on the Tax Treatment of Occupational Pension Schemes

National Pensions Board (1993): Final Report - Developing the National Pensions System

Retirement Income Inquiry (1996): Pensions 2000 and Beyond.

Simplifying Pensions Group (1996): Pensions for All

World Bank (1994): Averting the Old Age Crisis