

*Response to the*

*Strawman Public Consultation Process for an  
Automatic Enrolment Retirement Savings System  
for Ireland*

*from the*

**Irish Association of Pension Funds**



# IAPF Response to a Strawman Public Consultation for an Automatic Enrolment Retirement Savings System for Ireland

## Introduction

We welcome the publication of the Strawman as an important step in moving closer to the introduction of an Auto-enrolment system in Ireland. We believe this is needed in order to improve pensions coverage and the adequacy of pensions savings in Ireland. It will be one of the most important developments in Irish pensions policy and therefore it is crucial that it is implemented in a manner that will achieve its objectives. There are many pension schemes in existence in Ireland that work hard to achieve good outcomes for their members and we have drawn on their expertise and experience in providing our view on the Strawman. Many of these schemes already have auto-enrolment in operation or, indeed, mandatory membership.

We are pleased to provide our input to the process. We have also provided input to the consultations on the State Pensions, DC Master Trusts and Supplementary Pensions Reform.

## Administrative Arrangements and Organisational Approach

### 1. Is the rationale for use of a CPA sound?

We can understand the rationale in achieving a pot-follows-member approach and to minimise the involvement of employers.

We recognise that the successful design and implementation of a CPA will be instrumental in ensuring a positive experience for employers and members alike. It will make it easy for employers to remit contributions to a single source and not multiple providers.

The CPA would promote the auto-enrolment system and oversee minimum standards

### 2. What are the potential strengths and weaknesses of a CPA structure? Do you believe that the CPA model proposed can be improved? If so, how?

A properly run CPA could have several strengths. It would centralise the contribution collection and allocation functions, which would ensure consistency, a measure of State oversight, a lack of duplication and could potentially lead to cost efficiencies.

Having the State involved in these functions may also reinforce public confidence in the system. The weakness is the political risk element. If the CPA is to be set up properly, it will require considerable private sector expertise, which must be bought in sooner rather than later, and not through some lengthy and counterproductive public procurement process.

Defined contribution administration is quite complex. There are very significant levels of transactions that need to be carefully tracked to ensure the right contributions are being collected and applied to the right accounts and invested in the correct funds. As well as the recording of these transactions, the money needs to be moved in a safe and timely manner. The movement of employees between employers and fluctuating earnings add complexity to the system with contributions expected and paid often changing from the previous payroll.

It is unlikely that the skills required to establish a system that can deal with these issues is within the current public sector systems infrastructure. Therefore, if the State is committed to establishing a viable CPA, it will need to hire a very senior executive with the relevant experience and expertise to lead the establishment of the CPA by Q1 2019 at the latest. That individual will also need to be free to hire a team of experienced people at some point in early to mid-2019 to start work on the development of the systems and infrastructure needed to operate the CPA properly when it is due to go live.

Obviously, an appropriate administration system will also need to be set up, and here some form of public procurement process will no doubt need to be undertaken, but that is a longer-term decision.

Another potential weakness of a CPA structure is the current lack of definition as to what exact functions the CPA will be carrying out, by comparison with the AE Registered Providers. In the strawman consultation document, the division of functions between the two is not very clear. A lack of clarity risks duplication of effort, time and costs being expended on managing the interface between the CPA and the AE Registered Providers, as opposed to on the delivery of the administration services themselves.

Therefore, if the CPA structure is to be used, it must be done properly and based on seconding or hiring individuals in who are the best available, very similar to the hiring of Professor Tom Keane to lead the National Cancer Strategy, or the establishment of other agencies considered to be critical such as the National Asset Management Agency. If the CPA does not draw on the best practice and expertise available in the market, it will fail, and that failure could undermine the entire auto-enrolment system. The cost of setting up such an infrastructure is likely to be considerable and should not be underestimated.

We are concerned that the development of the CPA will become very costly and time-consuming and has the potential to delay the introduction of auto-enrolment. There is no indication in the consultation document of the likely cost of establishing the CPA, the envisaged ongoing costs or the timetable for getting it established. It is difficult, without this, to make a judgment on the overall benefit of it and the likelihood of success. The experience in the UK of NEST is that, while its impact has been very positive, it was set up at a significant cost that will take some time to be paid back.

### 3. [If you don't agree with the CPA model, can you suggest alternatives?](#)

Much of the rationale is about setting standards and it is possible that this could be achieved without the need for a CPA acting in an ongoing administrative capacity. For example, providers could only be authorised to receive auto-enrolment contributions where they can demonstrate that they can meet those standards. There could be other means of ensuring a pot follows member approach e.g. such as making that a default requirement unless a member specifies otherwise.

4. Have you suggestions for how the operating costs of the CPA could be covered?

Should the State decide to establish and run a CPA, there is strong agreement among our membership that it should pick up the associated costs and, in particular, the set-up costs. If the aim of the CPA is to minimise the costs to the member and administration burden on the employer, while still providing a commercially viable proposition for providers, it seems passing on the costs to the members/providers may be counterproductive. Therefore, if the CPA is established with a clearly defined remit these costs may be small relative to the overall gain to the State in having an adequately covered population and adequately funded pension system in the long run.

As an alternative the cost could be reflected in the charges as part of the overall cost of the system. This would mean that an element of the maximum charge levied by providers would include the costs of the CPA, an entity over which they would have no control. We are concerned that this could deter potential providers and limit competition.

5. Is the use of commercial providers for the provision of retirement savings options the right approach?

It is difficult to see a viable alternative. The pension system in Ireland already has a well-developed infrastructure. Using this may be the most effective and least costly way of implementing an AE system. The use of multiple providers and the carousel model will provide sufficient competition to ensure standards are to the level established by the CPA.

There may be some non-commercial providers such as existing pension schemes that would operate on a not-for-profit basis. The other alternative is for the State to assume this role and associated responsibilities. This would involve developing and implementing new capabilities. This would bring additional risk to the timely and efficient establishment to the AE system and would require significant investment.

6. Is it appropriate to limit the number of approved AE Registered Providers, as proposed, in order to provide economies of scale and drive down unit costs?

There is some basis in the rationale to limit the number. However, as the market is relatively small, commercial realities will dictate how many providers would actually be interested in participating.

7. If so, is the maximum figure proposed of four providers about right? Or should it be more or less, and if so, why?

It is difficult to put a precise number on it but four seems like a good compromise.

8. Are there alternatives that can achieve the economies of scale required other than to select a limited number of providers by open tender?

Setting standards that providers would have to meet in order to be authorised could also achieve a similar result. In a small market there are likely to only be a limited number of providers interested or capable of delivering the services and scale required. There is a danger that using a tender process could delay the implementation and create more legal risk for the State.

9. What do you believe is the optimum governance structure for Registered Providers and why? (e.g. Master Trust or insurance-based contract providers).

The trust system imposes obligations on trustees such as the need to act in the best interest of the members. In addition, it would align the regulatory structure of Master Trusts to the current regime. It is worth noting that it is more difficult to have a similar fiduciary duty in contract arrangements.

10. Where a member elects not to choose a provider and fund option, is it appropriate to allocate them to the default fund of one of the AE Registered Providers on a carousel basis, or is there a better alternative you would suggest?

If relying on members to make the choice, that would be appropriate. General experience would indicate that most members will not make a choice. We therefore agree that the default approach makes sense.

11. What is an appropriate maximum limit on the level of administration/investment management fees?

The recent IAPF DC survey indicated an average fee level of 0.41% on the scheme's default strategy. However, that was a relatively small number of schemes and within that number the fees ranged from 0.05% to 1%. In almost all of those responses the schemes also indicated that the employer paid all of the administration costs and many other costs. Therefore, the only fee applied to the members is the investment management charge. The additional costs met by the employer ranged from .166% to 2% of the fund, with the majority above 0.2%.

Finally, we believe the proposed fee of 0.50% will be a challenge if the full cost of administration is to be borne within that fee. We expect that there will be a very large number of very small DC pots removing the economies of scale often associated with group schemes. This could lead to charges in the range of 0.5-1% of AUM, depending on the services being offered to members.

We also believe that the administration and investment charges should be separated, with either a separate maximum charge for each or, at least, disclosure of each. Ongoing administration and investment management services are very different and there is no obvious reason to bundle them together. Separating them would ensure there can be better comparisons between providers and also that the providers are focusing sufficiently on both elements. This is currently required for some products under PRIPS.

It is also important to focus not only on the level of the fee but on the value being offered for that. For example, a lower fee may mean administration standards are compromised or investment strategies are restricted which may result in lower outcomes for members.

12. What is the appropriate timeframe between each tender round (e.g. 5, 7, 10 years) and why?

Assuming a tender process, it may need to be a long period in order to ensure there is sufficient interest among providers at the outset. With contributions starting at a low level and a proposed cap on charges it is likely to be some time before providers would make a return on their initial investment.

Therefore, we propose an initial appointment of 7-10 years with providers being replaced due to issues such as a short-fall in service standards, performance, solvency and conflicts.

13. Do you think the proposed timeframe for the roll-out of AE is reasonable and achievable?

We have concerns that building the CPA and utilising a tender process could lead to delays in the proposed timeframe, unless work on establishing the CPA commences immediately. Momentum will be essential and, therefore, use of existing technologies and industry expertise will both ensure delivery and minimise costs.

14. Do you believe that employees should select their preferred provider or should employers be required to select a Registered Provider on their behalf?

We understand the rationale that many of the employers will be very small and the process is designed to be simple for them. Furthermore, having the account linked to the member rather than an employer choice would facilitate portability by making it easier to adopt a pot-follows-member approach. However, it should also be recognised that many members may not be in a position to or want to make a choice, so the option of allowing (not requiring) the employer to choose might be helpful, for passive members. An employer may, for example, believe that a certain provider is a good fit for their workforce.

### Target Membership

15. Should there be a lower/upper earnings threshold triggering automatic enrolment?

It is appropriate that there would be a lower limit as there will be a point at which individuals will not be able to afford to save, long-term savings cannot be their priority, or the State Pension would provide an adequate replacement income. Establishing what that level is will be difficult as it will vary significantly depending on individual circumstances. It is also the case that the level of replacement income that will provide adequacy for an individual on a higher salary will not be the same for someone on a lower salary.

Consideration needs to be given to segments of the population who work multiple jobs. Using a minimum salary as opposed to a total income model may inadvertently exclude this grouping. This will impact particular segments of the population more than others, most notably women. As women, in general, are less financially prepared for retirement we believe the inclusion of those in multiple jobs needs a solution. We believe this issue is also more likely to extend to ethnic minorities.

We do not see why there should be an upper earnings threshold if the system is to achieve its objective of allowing people to adequately replace their income in retirement.

16. If so, is the proposed earnings threshold of €20,000 p.a. above which members will be automatically enrolled into the system appropriate? If not, what would you propose as the earnings threshold and why?

It would appear to be a reasonable amount. However, it would be important to research those earning below that amount to determine whether the State Pension would provide an adequate replacement income. It is also possible that people earning below that amount may be working part-time and in more than one job, where their combined earnings would take them above the threshold. It should also be determined whether that cohort have the same likelihood of qualifying for a full State Pension as people earning higher amounts.

17. Do you agree with the proposal to review the earnings threshold on a five yearly basis? If not, what adjustment process would you propose?

The operation of the earnings limit should be reviewed at a general level at least every five years. However, we suggest that the threshold should increase automatically in line with earnings or some pre-determined method at, for example, budget time.

A five year review period risks a substantial reduction in income as opposed to annual incremental changes. Also, a five year review may mean potential members miss out on pension contributions for a longer period than is necessary.

18. Should there be a lower/upper age threshold for automatic enrolment?

We believe that there should not be a lower age threshold. The easiest time to get someone to start in a pension plan is when they first join an employer. Where it happens automatically, their first salary payment becomes the benchmark for how they spend or save. We have some concern that by starting later there will be a much more noticeable drop in their take home pay (particularly when contributions are at 6%) and this will cause resentment which could ultimately lead to more opt-outs.

It is appropriate to have an upper age limit but we would question whether 60 is too low as anyone being enrolled at 60 in 2022 would have at least 7 years of savings.

19. If so, are the proposed age thresholds appropriate? If not, what would you propose as the age thresholds and why?

We suggest that auto enrolment takes place on joining the workforce with no lower age threshold and the upper threshold should be 5 years before State Pension Age.

20. Should employees outside of the age/earnings criteria triggering automatic enrolment be able to opt-in?

Yes, we believe that would be appropriate.

21. How should those with more than one source of employment be treated?

It should be possible to link employments through PPS numbers. If the rationale for not enrolling people below the threshold is that they have sufficient replacement income from the State pension, that will not hold true for people with more than one small income which in aggregate exceeds the threshold.

22. Do you agree with the approach proposed for self-employed people? If not, what modifications would you propose?

Pension coverage for self-employed is lower than the overall coverage rate. It is also essential that the designation of self-employed is correct. It is difficult to consider a different approach as the self-employed comprise so many different types of roles. However, the importance of saving for retirement should be highlighted and promoted to the self-employed.

23. Should people outside of the workforce (e.g. carers, homemakers) be eligible to opt-in? If so, suggest how that might work in terms of contributions, etc.

Yes. Where they are not earning a salary there could be a maximum monetary amount that they can pay which would also benefit from the State contribution. The UK Auto-enrolment system facilitates non-earners contributing.

24. Should all eligible members be enrolled immediately on commencing employment?

Yes, for the reasons already stated. [See above]

25. Should members of existing pension schemes be allowed to transfer into the AE system?

As both systems will co-exist and as employees will move from employers with AE to those with stand-alone schemes, there will be many members who have benefits in both systems. There may be a case for allowing someone to transfer in deferred benefits if they want to consolidate their pension savings. However, if someone is an active member of an existing scheme that provides equivalent benefits, it is difficult to see any basis on which they should be allowed to opt-out of that scheme and transfer to the AE system.

26. Do you agree with the approach to starting with a low level of contributions increasing on a phased basis to a higher level over a period of six years? If not, what approach would you propose and why?

It is reasonable that contributions are phased in so that individuals and employers can prepare for the impact. It is also important that there is a set schedule for increases to the ultimate level and that this happens in accordance with the schedule. Six years may prove to be too short a timeframe, but we await the outcome of the economic assessment.

27. Do you agree with the proposed contribution levels? If not, what contribution levels would you propose and why?

The contribution levels seem reasonable in order to achieve the objective of adequacy. However, it should be noted that 6% of earnings, without tax relief, is a big deduction from net salary for an individual. It may be wiser to set maximum employee contributions at 4% or 5% of net salary. Our most recent survey of DC scheme contribution rates showed average employee contributions were 5.4%. Where there is tax relief on these, the impact on take-home pay would be significantly less than a 6% contribution with no tax relief.

The paper does not consider how earnings would be determined. Many employees will have fluctuating elements to their salaries such as overtime, allowances or bonuses. If these are to be included, it will add to the complexity of the system as contributions will be changing and whether an individual should be enrolled might differ from one pay period to another. This issue needs to be carefully considered and is one of the more complex areas of the UK system.

28. Should there be an upper threshold on qualifying earnings along the lines described in the Strawman or should qualifying earnings be uncapped?

It is our view that qualifying earnings should be uncapped. The system is designed to provide adequate replacement income and, therefore, savings to achieve this should be facilitated. There are already limits in place such as the Standard Fund Threshold that place an upper limit on retirement savings.

29. Should the Irish AE system incorporate a ‘disregard’ such as used in the UK’s AE system whereby earnings between £0 and £6,032 are not subject to a contribution requirement? If so, why do you believe a ‘disregard’ should apply and at what level?

It is important that the system is as simple as possible to administer and understand. Including a disregard will only add to the complexity.

30. Should employer matching contributions be required for those outside the automatic enrolment age/earnings trigger criteria, who choose to opt-in?

No, this would make it very difficult for employers to plan and budget. Once the parameters have been set and they assume those are the people who need to be auto-enrolled, the employer should not be obliged to match contributions for others. They may however do so on a voluntary basis and this should be facilitated.

31. Do you agree with the Strawman approach to State incentives – i.e. a potential State bonus top-up based on matching member contributions with a payment of €1 for every €3 they save?

We believe the proposal adds further complexity to the overall system. The current system of tax relief at marginal rate is designed to only tax individuals when they have the use of their money. The tax neutrality of the current EET system can be somewhat skewed by the fact that there are more favourable taxes for pensioners that mean some people will not stay in the same tax bracket post-retirement and by the payment of tax-free cash. However, the majority of people will be in the same tax bracket and pay tax at the same rate as that on which they received relief. While most people may not understand tax relief, it can be explained in a way that shows it as a State contribution. This is how it has been communicated in the UK. Even though tax relief has continued at marginal rate under the UK system, it is communicated as a Government top-up.

Introducing a separate top-up and the possibility of all payments from auto-enrolment being tax-free would introduce a whole new level of complexity and allow for the possibility of arbitrage in the system. This has the potential to undermine the existing system which does already account for 50% of the workforce. It is also likely that, as people change jobs, they will have mixed benefits between the auto-enrolment system and stand-alone schemes. Calculating their retirement benefits from all sources will become more difficult.

32. What level of top-up or State incentive would you propose?

Continue the current system of marginal rate relief.

33. If you don’t agree with the ‘top-up bonus’ approach what type of incentive would you propose?

Continue the current system of marginal rate relief.

34. Is it appropriate to cap State incentives? If so, what should be the value of this cap?

The current caps that are in place in terms of maximum contributions allowed and a Standard Fund Threshold are adequate.

35. Do you agree with the suggested approach to limiting the AE Registered Providers to offering three 'standard choice' DC savings options with one fund acting as the default?

There is merit in limiting the number of choices as too much choice can lead to confusion. However, the choice of the types of alternative funds that providers can offer should not be overly prescribed in order to allow providers to differentiate and offer different types of funds. The characteristics of the default strategies should be relatively prescriptive to ensure individuals allocated on the carousel system end up in similar funds.

36. If not, what retirement savings options do you consider should be provided?

Providers should be free to make funds available, outside of the default, that they have particular expertise in. These could range, for example, from ESG funds to higher risk or Infrastructure funds.

37. An alternative to conventional DC is the target benefit approach – do you believe that a target benefit approach merits consideration as one of the 'standard choice' options for the AE Registered Providers?

No, target benefit approaches are relatively unproven and add to the complexity and cost.

38. Do you agree with the approach to provide for maximum annual management and investment charges at 0.5% of assets under management?

There is merit in having a maximum charge, but the overall focus should be on providing value for money and the best outcome for members. A maximum charge that is too low may just restrict the services offered to members and result in sub-optimal investment strategies. It may also be worth considering whether a higher charge is more appropriate at the outset until the system builds the type of scale required to justify lower charges. Consideration should also be given to having a different maximum charge in the default fund to the others offered.

Finally, a 0.5% charge is probably too low for full administration and investment management – this depends on the level of administration the CPA is doing, but a hard ceiling should probably be avoided in the tender process. It may be more appropriate to have a range of charges that providers would have to comply with.

39. If not, what approach to management and investment fees would you propose?

An alternative would be to allow providers to determine the charging structure and that becomes a weighted factor in the tendering process.

40. Do you agree with the proposal to allow members switch between funds?

Yes, although it is not clear if members would also be allowed to switch between providers and how this would be processed.

41. Do you agree with the concept of a minimum compulsory membership period and that six months is an appropriate minimum period?

Yes.

42. What is your view on an opt-out window of two months in months seven and eight of membership?

While it seems like a rational approach designed to minimise opt-outs there is a possibility that having such a limited period could inadvertently increase opt-outs. Knowing that this is the only window available to opt-out might encourage people to opt-out who might otherwise stay in the system if they thought they could opt-out at any time or at other occasions.

43. Do you agree that people who opt-out should be automatically re-enrolled after a defined period (e.g. three years)?

Yes.

44. Do you agree with the concept of allowing members to take a period of Saving Suspension? If so, are there specific conditions that should attach to such suspensions?

While this sounds reasonable, we believe it could be very difficult to administer in practice. In countries where suspensions are possible, the result can often be that large numbers of people end up not making regular savings.

45. Do you agree with the approach which sees employer and State contributions retained/credited to the CPA to contribute to its costs, in the case of member opt-out?

We find it difficult to see why employers should contribute to the costs of the CPA in this way. It will be arbitrary as some employers might have much higher opt-out rates than others, and so will get no benefit for the contributions they have made. While it is reasonable for employers to contribute to the retirement savings of their employees, it would also be reasonable that they have those contributions returned to them where the employee decides to opt-out.

46. Do you agree that Registered Providers should provide a standard range of investment/ draw-down options?

Yes. As the whole premise of the system is based on people not making choices it is important that this is carried through to retirement.

47. Should members be allowed to allocate their accumulated fund across all of these post-retirement options?

Yes, subject to the caveat in the answer to the next question.

48. Should members be required to invest a minimum proportion of their accumulated fund in a lifetime annuity (pension)? If so, in what circumstances?

Yes. We believe there is a strong case for a guaranteed lifetime income, although not necessarily an annuity. It would allow members to have the comfort of knowing they have some form of longevity protection and make them less concerned about over spending their savings. It also helps alleviate issues that may arise when members no longer have the cognitive ability to make financial decisions. However, the income could be deferred, only coming into payment at e.g. age 75. There may be particular provisions required to reverse this in cases of ill-health or terminal illness.

49. Do you agree that the appropriate age to grant access to the retirement draw-down products is the State pension age? If not, what age would you suggest?

Yes, but we also need to recognise and facilitate the requirement for phased retirement and the need for members to drawdown their pension pot to supplement reduced ongoing earned income.

50. Do you agree that early access to accumulated retirement savings should be provided on the grounds of ill health and enforced workplace retirement? If so, under what conditions and from what age?

Yes. Not everyone will be in a position to continue to work until State Pension Age and it is important that those people have access to their savings. The grounds outlined of ill-health and enforced workplace retirement both seem appropriate and should not be age limited.

### **Issues Not Covered**

One issue not dealt with in the consultation is the interaction with existing schemes.

Firstly, where an existing scheme has voluntary membership, there will be employees who have not joined the scheme and will, presumably, have to be auto-enrolled. A decision will need to be made as to whether these can be auto-enrolled in the current scheme or in the auto-enrolment system.

Secondly, the Strawman states that auto-enrolment will apply to those not currently in pension schemes. Presumably, however, there will need to be some check as to whether the existing scheme is of an equivalent standard to the auto-enrolment alternative (as indicated in the Strawman). This may not be straightforward as schemes can have complex contribution options and salary definitions. For example, many schemes offer matching contributions so while employees may not have availed of an option that would be equivalent to the auto-enrolment contribution levels, it may be available to them. This area needs to be thought through carefully.

There should be consideration given and investment deployed to leveraging the use of technology to drive a world class solution to Auto Enrolment for Ireland. Businesses, small, medium and large are also increasingly shifting their computing needs and corporate applications from their own servers to the cloud and globally recognized service providers which can provide a cost-effective way to manage and secure data.

There is an opportunity to develop systems infrastructure to support:

- Easier administration and connection of information
- Use of PPS number to allow funds to follow member and dashboard availability for auto enrolled members to track their savings as they move across different employments
- Self-Serve portals and leverage BOT technology to support basic queries
- Leverage encryption technology to ensure safe access from different devices while complying with GDPR rules
- Ease of portability for members
- Mechanism/platform to support member communication
- Automated Controls (preventative) for changes and data transfers
- Easy options to top up pension savings