The Pension Commission

Aon's response to the consultation document on sustainable State Pensions into the future

At a glance…

Our response to the consultation can be captured in four simple points:

- Increased Flexibility
- Remove or increase the mandatory retirement age
- Auto Enrolment
- Commitment to the Total Contribution approach

Aon's focus is on our clients and their employees who will rely on the State Pension and Occupational Pension Scheme/Auto Enrolment models to provide them with an adequate income in retirement.

We have set out below how these four key factors can provide a sustainable and equitable State Pension model for future generations to come.

Why bring you this paper?

Employers who sponsor occupational pension schemes and their members need certainty on the State Pension Age, the rate of the State Pension and the terms and conditions relating to its funding and payment in order that they may plan and fund for supplementary pension provision.

Prepared for: Pension Commission
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Questions to Consider

What do you expect from State Pensions?

We see the State Pension as a key pillar to retirement provision. Occupational pension provision builds on this, so it is vital that the first pillar is **stable and certain**.

Our pre-retirement workshops cover, among other things, State Pension entitlements. Throughout our engagement with members approaching retirement we find that they tend to take it for granted that they will receive the State Pension. This is particularly so where their occupational pension is integrated with the State Pension. Those members would be aware of the State Pension rate and would feel that, given it has been incorporated into their benefit calculation, they will receive it for their lifetime once it comes into payment.

They would be less aware of the eligibility rules and it would be true to say that they struggle with understanding these.

To help members become aware of their entitlements the Department of Social Protection might consider the idea of making a benefit statement available every year showing State Pension accrued to date and that expected to accrue in the future. This could be added to the MyWelfare.ie portal.

Opportunity

The State Pension is a key pillar of retirement provision in Ireland and yet most members only focus on it as they approach retirement.

To help understanding and engagement an annual statement of entitlement should be made available via the MyWelfare.ie portal.

What concerns you with respect to current State Pension arrangements?

Sustainability - The pay as you go model for State Pensions means that the current generation of workers are paying for the pensions of the previous generation. The current generation therefore need to be confident that their pensions can and will be provided for by the next generation of workers. Given increases in longevity and projected demographic changes it has been well documented that the current State Pension model is not sustainable on cost grounds.

The future changes in State Pension Age that were introduced to address the cost issue were reversed last year. The concern here is that the current model is too open to political influence.

Income Gap - The recent proposed changes in State Pension Age, albeit that they have been reversed, often resulted in a gap between retiring from work and drawing the State Pension. This is an issue that needs to be addressed through flexible retirement options.

Education - Workers struggle to understand the rules regarding payment of the State Pension, especially where breaks in service arise. Providing them with simplified rules and easy access to their expected entitlements via an online portal (including FAQ/help guides) would benefit all parties and greatly assist their understanding.

Means testing – Members of occupational pension schemes are concerned that the value associated with increased retirement savings will be eroded by the future introduction of means testing of the State Pension.

How might we best finance sustainable State Pension arrangements into the future?

A more sustainable model whereby the State Pension Age was increased with the possibility of future further increases linked to longevity was introduced but subsequently repealed. We believe we should go back to this model but address some of the issues that arose by allowing the State Pension to be paid at ages other than the State Pension Age, i.e. suitably reduced if drawn earlier or increased if drawn later, and removing the mandatory retirement age or setting this at an age which is no younger than the State Pension Age .

Should the Commission recommend legislative changes to address gaps between retirement age?

Yes, we believe that mandatory retirement ages should be removed or set at an age which is no younger than the State Pension Age. In addition, earlier/later drawdown of the State Pension, with suitable reductions/increases being applied and within certain limits, should be facilitated.

What is the appropriate State Pension Age?

The previously provided advice says that age 68 is the appropriate age for Ireland and we would accept that, i.e. applicable in 2028 with 5-year reviews for sustainability as committed to in the Pensions Roadmap.

This is in line with international practice where developed countries (UK, Australia and Canada for example) have all increased their State Pension Age in the recent past.

How might we best ensure sustainable flexible retirement pathways, allowing for both early and later exits from the labour market?

We believe the best way is to build in flexibility by applying scales to reduce/increase State Pension entitlements based on earlier/later retirement.

Periodic reviews to assess sustainability (5-year reviews) will also be required with a commitment to fund shortfalls over the short term and not via long term "Pay As You Go" funding.

The factors used to adjust State Pensions would need to be reviewed as the State Pension Age and economic conditions change.

What are the best ways to fill any income gaps between retirement age and State Pension Age

The aim should be to remove the gap altogether. This can be done either by removing or increasing the mandatory retirement age or by allowing the State Pension to be drawn down at an earlier age, albeit reduced to allow for the longer expected payment. We believe that introducing both elements would best achieve the aim of removing the gap.

The introduction of increased flexibility for occupational pension arrangements may also assist in reducing the gap.

Suitable Reform Proposals

We believe that the State Pension Age needs to be increased to ensure that it can be maintained for future generations. We appreciate the previous issues that arose with this policy and would therefore propose that in addition to increasing the State Pension Age the following be introduced:

Removing or increasing mandatory retirement ages – this would remove the income gap for those who can and want to continue working;

Allow the State Pension to be drawn down earlier than age 66, albeit reduced for early payment, by those who cannot or do not wish to work until this age.

Ensure that the legislation is sufficiently robust that it cannot be amended/repealed as a matter of political expediency. Ideally, the responsibility for setting a sustainable State Pension policy within certain specified parameters should rest with an independent body so as to largely remove it from the political arena.

Progress the introduction of Auto Enrolment so that the dependency on the State Pension is reduced.

Conclusion

Our response to the consultation can best be summarised in the following points:

Increased Flexibility

Flexibility is needed that reduces the 'cliff edge' at retirement – this will allow older employees to choose a retirement age that suits their circumstances while permitting companies to manage their workforce and retain key expertise. This may require changes to pension legislation.

Provide for later and early retirement in the context of the State Pension subject to an appropriate adjustment. The full rate of the State Pension would be paid at State Pension Age with a percentage p.a. reduction/increase for earlier/later payment. The possibility of imposing a minimum retirement age, for example, an absolute age such as age 60 or a term before the attainment of State Pension Age such as 5 years beforehand could be considered.

There should be a minimum early retirement age applied to the State Pension so as to avoid a situation where a reduced pension reduces to a point whereby the pensioner would likely fall into poverty at a later age.

Removal of Mandatory Retirement Ages

Remove any mandatory retirement age requirement or set this at an age which is no younger than the State Pension Age. It would be important that any changes to the regulations relating to mandatory retirement ages and future State Pension Ages are flagged in advance and maintained into the future to give employers and workers the certainty they need to plan for retirement.

Appropriate State Pension Ages were set previously after having taken appropriate advice – see Pensions Roadmap. We believe that the State Pension Age should be linked to longevity with a sufficient notice period being given of any future change.

Auto Enrolment

Introduce an Auto Enrolment model with meaningful contributions to reduce the dependency on the State Pension over time.

Commitment to the Total Contribution approach

The commitment to the Total Contribution approach should be sustained and be protected from future political influence.