CHARTERED ACCOUNTANTS IRELAND

# Submission to The Pensions Commission

## Public Consultation on sustainable State Pensions into the future

9 March 2021

**This submission is being made on behalf of the members of Chartered Accountants Ireland by email to ConsultPC@pensionscommission.gov.ie**

## About Chartered Accountants Ireland

Chartered Accountants Ireland ("the Institute") is a membership body representing over 29,500 influential members throughout the globe, including almost 20,000 members based in Ireland. Our role is to educate, represent and support our members. Our members work in senior positions in practice and industry. We work with governments and businesses to raise awareness of the importance of sound financial advice, and we have had an active voice in addressing issues of relevance to our members over the past number of years.

Chartered Accountants Ireland was established as the Institute of Chartered Accountants in Ireland by Royal Charter in 1888. Its activities and those of its members are governed by its Byelaws and by Rules relating to professional and ethical conduct. Chartered Accountants Ireland is governed by a Council and it is responsible for determining policy and monitoring its implementation. Council is led by the Officer Group and supported by the Management Team and staff. A number of committees with voluntary member involvement also play a key role.

## Introduction

Chartered Accountants Ireland ('the Institute') agrees that a review of the sustainability of the State Pension in Ireland is urgently needed. In that regard we welcome this consultation process.

The Institute has responded to the prior Government consultations on Supplementary Pension Reform and the Strawman Public Consultation: Process for an Automatic Enrolment Retirement Savings System for Ireland.

Our responses therein stated that there was an inadequate level of income post-retirement for many workers and for many this would mean living on the poverty line. We proposed that any automatic enrolment (auto-enrolment) scheme introduced be efficient, transparent, and cost-effective for all stakeholders, particularly employers, and deliver on its core objective of increasing pension coverage, but without introducing needless complexity, eroding tax incentives for retirement saving or replacing the State Pension. We also advocated that the State Pension should reflect a changing work and policy environment and be flexible enough to deal with these changes.

In a survey of our members carried out in February and March 2021 for the purposes of the current consultation on the State Pension, our members again raised concerns about the sustainability of the current State Pension, and the requirement for clear and coherent government pensions strategy with adequate lead-in time for any changes to allow workers to plan for the long-term.

Issues of pension age, eligibility criteria, contribution rates, pension calculation and pension payment ranges should be addressed to ensure that the system is sustainable for the taxpayers of the future whilst ensuring dignity and security of those in retirement.

Our responses to some of the questions posed in the consultation document are below.

To summarise, we believe that:

- The Government must set out a clear, consistent long-term strategy, particularly in terms of future State Pension Age increases, and any significant changes should be communicated 10 years in advance.
- Reform to the State Pension Age cannot take place without commitment and action to increase private pension coverage. Automatic enrolment should be introduced in Ireland for private sector workers.
- Mandatory retirement should be abolished to afford workers the choice to work or retire as long as they desire to.
- The Benefit Payment for 65-year-olds should continue for those retiring at 65 years of age until they reach State Pension Age.

The current arrangements for pension provision in Ireland may not guarantee an adequate level of income post retirement for many workers, primarily because of demographic changes. The gap between public and private sector employees in terms of pension funding remains wide and this position is unsustainable. All employees in the public sector have some form of pension while almost 40 percent of private sector workers have made no provision for their retirement. Those employees without provision are likely to rely on the State pension in retirement, which is around €13,000 per annum. This would put them on the poverty line.

One approach to solving this problem is to promote greater levels of private pension provision. Chartered Accountants Ireland believes that reforms to the State Pension cannot take place without parallel reforms to increasing private pension coverage in Ireland to enable workers to avoid living their retirement in poverty.

## An Appropriate State Pension Age

It is well known that the Government faces a great challenge in funding the State Pension as the population continues to age. Census 2016[1] in Ireland shows that there are almost 638,000 individuals over 65 years of age in Ireland: up 19 percent in 5 years.

**The spend on the State Contributory Pension was €2.7 billion in 2007, increasing to €5.2 billion in 2018**[2]. This represents an increase of 98 percent.

The majority of respondents to our survey said that the State Pension Age should not increase beyond the current 66 years. For many, this means a working life well in excess of 40 years. And for many, staying in the work force until State Pension Age is reached is not an active choice, rather a necessity in order to stay out of poverty.

Many workers in the State make a considerable tax contribution throughout their working life through payments of income tax, PRSI and other various levies. These workers deserve to have certainty about their retirement age.

Determining the appropriate age at which a person can access a State Pension is complicated by several factors, not least increased life expectancy for some as well as variations in the typical health of the population.

The State Pension Age and access to the State Pension should also reflect that living longer does not necessarily mean being in full health and capable of working at the same capacity as before. People who are in poor health when approaching the current pension age should be provided with access to an early State Pension (like in some other EU countries) for example.

Increasing the State Pension Age from the current 66 years is unlikely to entirely relieve the financial burden on the State. Workers who are required to retire at 65 years can claim the Benefit Payment for 65-year-olds if certain conditions are met and this payment continues until that person reaches the State Pension Age. **The maximum weekly Benefit Payment is €203 which, compared to the State Pension weekly payment of €248.30, is not significantly lower**[3].

Furthermore, the Benefit Payment for 65-year-olds will only bridge the gap between retirement age and State Pension Age provided adequate alternative private arrangements are in place. Solely relying on this payment will mean living below the poverty line.

Increasing the State Pension age without also addressing the issue of contractual retirement ages will further widen this gap as will the low levels of private pension coverage.

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[1] Census 2016 Report, Central Statistics Office
[2] Department of Social Protection, Social Insurance Fund, Financial Statements
[3] The Department of Social Protection, www.gov.ie

## Adjusting the State Pension Age

Chartered Accountants Ireland believe that any changes made to the State Pensions Age should be done incrementally, and that a clear long-term government policy should be adopted to create certainty for workers, particularly those approaching retirement. Certainty and transparency are of paramount importance for future pensioners and that was evident in the responses to our survey.

All workers need sufficient time to prepare for a new change in State Pension Age; therefore, we feel that a clear, coherent long-term government policy with substantial lead-in time is required before any changes are made. Respondents to our survey are seeking a minimum of 10 years' notice for individuals affected by changes to their State Pension age in order for individuals to adjust and manage their lives to new circumstances.

For example, the pension age in Ireland is now 66. People currently aged 56 are planning to begin drawing the State Pension in 10 years' time (when they reach the age of 66). For example, if the Government plans to increase the State Pension Age beyond 66, it should give affected workers 10 years' notice of this change, i.e., it should immediately inform workers aged 56 that they will not be able to rely on the State Pension until they turn 67 years (i.e., for another 11 years).

The Stage Pension Age should not increase by more than one year at a time. Subsequent increases should be set out in the same way as described above, always giving workers 10 years' notice of any change that will affect them.

According to research by the Finnish Centre for Pensions[4], the average State Pension Age across the EU is 65; in some countries the retirement age is linked to increased life expectancy, but clear policy is set out several years in advance. In Belgium, for example, the current retirement age is 65 for those retiring on or before 31 January 2025, increasing to 66 years for those retiring between 1 February 2025 and 31 January 2030 and 67 years for those retiring on or after 1 February 2030. In Croatia, the current retirement age for men is 65 years (62 years for women) and this will rise to 67 years in 2038. For women in Croatia, the retirement age will be 65 years in 2030 and 67 years by 2038. In Malta the current retirement age is 63 years, gradually rising to 65 years in 2027.

In the UK, the State Pension age for men and women will increase to 67 years between 2026 and 2028.

A consistent messaging and clear communication given well in advance will allow people to fairly plan for their retirement.

The Government should also develop its communication strategies, making the most of digital technologies, to ensure there is a clear plan for communicating future changes to the State Pension Age, and to aid with broader financial and later-life employment planning.

## Working beyond retirement age

The reality for many private sector workers is that they have made insufficient provision for their pension, and therefore they may wish to continue working beyond the normal retirement age of 65 years (in many cases) to guarantee an adequate retirement income. Those individuals should be allowed

[4] Finnish Centre for Pensions, Report on International Comparisons, Retirement Ages, 2020

continue to work if they wish to, and to be able to continue to make PRSI contributions beyond the current allowed age of 66 years.

70 percent of Chartered Accountants Ireland members surveyed stated that the requirement in employment contracts that require workers to retire at a certain age – often set at 65 – should be abolished. This would allow workers to continue to earn and save, thereby likely reducing their reliance on the State Pension at retirement age. It would also reflect the fact that many people are beginning their careers later than in the past, so have shorter careers in which to contribute either to a private pension plan or to the State Pension via PRSI contributions.

Workers can request to receive a contribution statement showing a summary of social insurance contributions received up to the end of the last tax year as well as any credits received. This online record requested via MyGovID is not a forecast of the State Pension. It would be useful for workers, particularly those approaching retirement to be able to see in real time (via an App or otherwise), the PRSI contributions made to date and what this translates to in terms of expected State Pension. This would enable workers to plan and may in fact encourage voluntary PRSI contributions to help qualify for the State Pension. Removing the age limit of 66 years by which to make PRSI contributions would also be helpful.

## Financing a sustainable State Pension system

The Tax Strategy Group[5] estimated in September 2020 that the net cost to the Exchequer of keeping the State Pension Age at 66 years over the next 5 years – rather than increasing it to 67 years on 1 January 2021 – is on average €400 million per annum. Over the period 2021–2025, the cumulative cost would be over €1.9 billion.

The most recent Actuarial Review of the Social Insurance Fund (SIF)[6] projected that in the medium to long term, pension related expenditure will continue to be the predominant component of SIF expenditure, rising from 70 percent in 2016 to circa 80 percent in 2071. This projection was estimated based on the State Pension Age rising to 67 on 1 January 2021 and 68 on 1 January 2028.

Our members are of the view that the increasing cost to the Exchequer to fund the State Pension should be financed through taxation, with increased rates of employer and employee PRSI contributions. Workers should also be allowed to pay PRSI beyond the currently allowed 66 years if they continue to work.

The combined employee and employer PRSI receipts for 2019 were in the region of €12.2 billion (€12.11 billion in 2020) which is about 16 percent of the total tax take[7]. A combined PRSI rate of 15.05 percent is paid in respect of most (PRSI Class A) employees. Self-employed persons who earn €5,000 or more in a contribution year are liable for PRSI at the Class S rate of 4 percent, subject to a minimum payment of €500.[8]

Provisional estimates from the Tax Strategy Group[9] for a 0.5 percent increase in the rates of PRSI would raise in the order of €377m in employee contribution revenues on a single year basis, with a similar amount being raised if employer PRSI was increased at the same level. This contribution could

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[5] Tax Strategy Group 20/05 Social Protection Package – Budget 2021 Issues
[6] Actuarial Review of The Social Insurance Fund 31 December 2015
[7] Revenue Commissioners Annual Report 2019
[8] PRSI Contribution Rates – Advance Notice for 2021 Guide, gov.ie
[9] Pay Related Social Insurance Tax Strategy Group – 19/06 July 2019

be put towards the €400 million per annum net cost to the Exchequer of maintaining the State Pension Age at the current age of 66.

It should be noted, however, that Irish social insurance contribution rates are in general significantly lower than those charged in other countries[10], and therefore consideration could be given to a phased increase in PRSI contribution rates over a 10-year period with each annual increase in the order of 0.25 percent.

For example, Employer's PRSI has gradually increased since 2018 to incorporate the National Training Fund levy. The Government, as part of Budget 2018, decided to raise the rate of the National Training Fund levy by 0.1 percent in 2018 to 0.8 percent, thereby increasing Employers PRSI to 10.85 percent. As part of Budget 2019, the levy was raised by a further 0.1 percent and by 0.1 percent in 2020[11]. Employers PRSI is now 11.05 percent. This approach to incrementally increasing PRSI by small percentages sets a precedent for how PRSI could be adjusted.

## Maintaining current tax relief

Many workers who currently contribute to a pension receive marginal rate tax relief. According to the Statistics and Insights from the First Year of Real-Time Payroll Reporting (2019 tax year)[12], 30 percent of all employees are making regular contributions to their pensions, and the gross income point which most employees make a pension contribution is between €40,000 and €45,000. Based on today's living standards, these individuals are not considered 'high earners.' Furthermore, the report said that 65 percent of the estimated incomes of those in retirement are less than €20,000 per annum (excluding the State Pension).

If tax relief was to be reduced for workers making regular pension contributions, there is a much-reduced incentive for them to save for their pensions, potentially increasing the risk that they reduce their pension contributions. This reduced level of saving would mean that such individuals have lower pensions in retirement which in some cases could lead to greater demands on the State Pension in the long term.

An adequate pensions system requires encouragement by government to help people save for their retirement. Tax incentives help to do this. If these incentives are reduced, individuals, particularly the lower and 'squeezed-middle' earners, may consider it not worthwhile to contribute to their pension. This will push more individuals into the bracket that will depend on the State pension.

We are also of the view that auto-enrolment should be introduced to relieve the burden on the State to be the sole provider of pensions for many workers (see below).

## Increasing private sector pension coverage

Chartered Accountants Ireland is strongly in favour of the Government's proposal to implement automatic enrolment in a timely, but phased manner. The recent Government announcement on the delayed introduction of auto-enrolment until at least 2023 is unacceptable, and reform is long overdue

[10] Department of Employment Affairs and Social Protection, PRSI Tax Strategy Group 19/06 – July 2019
[11] Department of Education and Skills, National Training Fund Expenditure Report 2019
[12] Statistics and Insights from the First Year of Real-Time Payroll Reporting (PAYE Modernisation) report, Revenue Commissioners

– the OECD[13] informed the Government in 2014 that urgent reform was needed. Similar models have been introduced in New Zealand[14] and UK[15] and both countries have reported increased private pension coverage as a result.

The lack of private pension provision has been on the agenda of various governments in Ireland over the past 20 years and the only solution to which the State has given serious consideration is to make people work longer. This approach is simply unsustainable. Auto-enrolment is a viable answer as it

incentivises people to save, reduces the risk of people entering poverty in retirement and reduces the reliance on the State Pension. The combined result in the long-term will be savings for the State.

We do not want to see auto-enrolment replace the State pension and any proposed changes to the State pension need to be properly consulted upon in a transparent manner and operate in tandem with increasing private pension coverage.

## Fair Reform

As noted already, the State Pension age reform should take into consideration the effect of increasing life expectancy on those contributing to the State Pension and those in receipt of it. Chartered Accountants Ireland believes that this reform should be structured to ensure that the costs of improving longevity are shared fairly between the generations and provide increased certainty around how State Pension age will change in future.

Fiscal planning for old age in Ireland is a challenging and complex issue that involves multi-faceted solutions. The State Pension system in Ireland, as it currently stands, compounds, and exacerbates many socio-economic inequalities that simply continue into old age, such as the cumulative disadvantage that accrues for some groups such as those with low levels of education, and in low income and insecure jobs, and inequalities within the system regarding gender.

For example, the way entitlement to a pension from the State has been based on social insurance contributions ties pension entitlements to an individual's labour market participation history. This has historically resulted in lower pension payments (and sometimes no pensions at all) for people (mainly women) who have spent extended periods away from the labour force raising families or caring for elderly family members. There is an onus on the Government to develop and reform pensions policy that is both gender-sensitive and takes account of these inequalities.

## Conclusion

To conclude, Chartered Accountants Ireland believes that the Government must set out a clear, consistent long-term strategy, and any significant changes in the State Pension Age in particular should be communicated 10 years in advance. We believe that reform to the State Pension Age cannot take place without commitment and action by the government to increase private pension coverage among workers in Ireland.

Mandatory retirement should be abolished to afford workers the choice to work or retire as long as they want to and the Benefit Payment for 65-year-olds should continue for those retiring at 65 years of age until they reach State Pension Age.

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[13] OECD, Review of Pensions System in Ireland, 2014
[14] Ministry of Social Development, KiwiSaver: A Model Scheme
[15] Department for Work & Pensions, Automatic Enrolment evaluation report 2019, February 2020