Sustainable State Pensions into the Future

Recommendations to the Pensions Commission

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STRONGER TOGETHER

CONGRESS

Irish Congress of Trade Unions

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Introduction

The Irish Congress of Trade Unions (Congress) is pleased to accept the invitation from the Pensions Commission to share our recommendations on sustainable State Pensions into the future.

Congress is the representative body for 44 unions and the largest civil society organisation on the island of Ireland. We represent the interests of some 700,000 workers and their families in all sectors of the economy both in the Republic and Northern Ireland.

Congress has long advocated for income support for working people in retirement. The 1908 Old Age Pension Act is one of the earliest and most far-reaching social achievements of the trade union movement. It has benefited generations. However, public pension provision is today under threat from successive governments' policy response to population projections and a pay-as-you-go financing model whereby social insurance contributions from current workers are used to pay the pensions of those who are now retired.

An ageing population is a feature of all advanced economies. Congress recognises the considerable challenges population ageing presents for decision-makers, as revenue and expenditure are adversely affected. Pension expenditure is both the largest component of age related expenditure and the expenditure component where the largest increase will occur over the coming decades.[1] To mitigate the significant implications for the public purse and to safeguard the sustainability of the State Pension, it is government policy to 'Support Fuller Working Lives.'[2] That is, to increase employment rates for older workers by means of both carrot and stick measures, but primarily through increasing the pension age.

1 Department of Finance (2018) *Population Ageing and the Public Finances in Ireland* p.17
2 Government of Ireland (2018) *The Roadmap for Pension Reform 2018-2023* p.36

While increases in the pension age are taking place in most rich countries, the 2011 Social Welfare and Pensions Act put Ireland on course to have the highest pension age in the OECD in 2028, despite having the youngest population in Europe.[3] Increasing the pension age represented the biggest cut to the social safety net for working people. The Act was vigorously resisted by Congress, and we continued to raise public awareness of this injustice to workers over the following decade. On the eve of the planned increase in the qualifying age to 67 coming into effect, the issue became the most important deciding factor for voters, after health and housing, in the 2020 general election.[4] Support has not waned. The most recent Red C monthly political tracker poll for the Business Post shows 66 per cent of all voters support retaining the pension age at 66. This opinion is highest among 18-34 year olds, suggesting the 'intergenerational fairness' argument for the increase does not have the support of almost seven in ten (69 per cent) of the intended target.[5]

Following on from a commitment under the new Programme for Government, the planned increase to age 67 years in January 2021 and to 68 years in January 2028 was repealed as part of the Social Welfare Act 2020, and a Pensions Commission was established to:

- Develop a range of options for government to consider in order to address the sustainability of the State Pension and the Social Insurance Fund in terms of pension age, eligibility criteria, contribution rates, pension calculation methods and pension payment rates;

- Examine how private sector employment contracts specifying retirement ages below the State Pension Age may be impacting on the State's finances and pension system; and

- Consider how people who have provided long-term care for incapacitated dependants can be accommodated within the State Pension system.

The Commission on Pensions is due to report its findings, options and recommendations to the

Minister for Social Protection by June 30. To assist the Commission in its considerations, a public consultation was launched on the sustainability of State Pensions into the future.

The key issues for Congress in respect to the State Pension (Contributory) are set out in our reply to the Commission's six questions. Given the limited time allowed for observations, the issues raised below are not exhaustive.

3 The 2011 Act legislated to discontinue the State Pension (Transition) from 2014, increase the qualifying age for State Pensions to 67 in 2021 and to 68 in 2028. Thereafter changes in the age would be linked to changes in life expectancy.
4 UCD-RTÉ-TG4-Irish Times-Ipsos MRBI (February 2020) *Election 2020 Exit Poll*
5 Red C-Business Post (February 2021) *Opinion Poll Report*

1. What do you expect from State Pensions?

The Irish pension system is a combination of three 'pillars' of pensions provision – a publicly managed first pillar consisting of a basic contributory and non-contributory pension, a second pillar consisting of occupational pensions and a third pillar of personal provision consisting of private pension plans and financial investments individually purchased and funded. The pillars provide 'tiers' of income protection to reduce risk and improve total retirement income. See Table 1. This multi-pillar approach is common in OECD countries, but with differences in the balance of pension provision between pillars.

In Ireland, the policy objective of the first pillar is *poverty alleviation* - keeping workers out of poverty in retirement. Entitlement to the State Pension (Contributory) is based on an applicant's social insurance contribution history, is unrelated to past or ongoing earnings and the eligibility age is 66. A means-tested State Pension (Non-Contributory) is available for applicants who do not qualify based on their contribution record. The standard personal rate of payment is €248.30 per week and, in keeping with the dependency based structure of the welfare system overall, a means-tested €222.50 top-up is paid for a dependent spouse or partner, marginally above the poverty line for a couple (discussed later). Because it is paid at a flat-rate, the State Pension replaces a high level of earnings for low-paid workers, but the replacement value declines as the earnings level rises leaving middle and high-income earners exposed to a drop in their pre-retirement living standards in old age.

Not only does Ireland lack a pay-related State Pension, it is the only OECD country lacking a mandatory occupational pension for its workforce. Consequently, coverage is low with just one in three

Table 1: Pillars and Tiers in Pensions Systems[1]

Tiers	Public pillar	Occupational pillar		Personal pillar
	State	Social partners	Employer	Individual
Third (topping up)				Savings or private pension
Second (income replacement)	Pay-related pension	Collective agreement	Company plan	
First (minimum income)	Basic pension or social assistance			

1 McCashin, A (2019) *Continuity and Change in the Welfare State: Social Security in the Republic of Ireland* p208

workers in the private sector and half of all workers actively saving for retirement in a workplace or private pension.[6] To address this, the introduction of a quasi-mandatory scheme is currently in the planning. In our submission on the design of this new 'auto-enrolment' scheme, Congress recommended that auto-enrolment retirement savings (a minimum 14 per cent of gross earnings) be publicly managed, in place of the four commercial pension providers proposed by Government, and that the draw-down take the form of the old Pay-Related Benefit. That is, for a 20-year period from the early 1970s a pay-related supplementary benefit was paid in addition to unemployment, disability, injury and maternity benefit. Not only would adopting our recommendation have the effect of transforming the State Pension (Contributory) from a basic pension, so that pensioners not only avoid poverty but also maintain their pre-retirement standard of living, the significant profits from managing auto-enrolment investments could be deposited into a National Pensions Reserve Fund (discussed later) to support the future sustainability of the State Pension, instead of being handed over to private companies.

The high numbers of workers exclusively reliant on the State Pension for income in retirement heightens the importance of achieving its objective to protect against poverty. The previous Government committed to benchmark the payment rate at 34 per cent of average annual earnings, and to index link future increases in the pension to increases in prices and wages by the end of 2018. This would have had the immediate effect of increasing the standard rate to €263 (discussed later). Moreover, such reform would provide pensioners with greater income certainty on the value of their pension and is essential to safeguard the State Pension against displacement by the new auto-enrolment scheme over time. Congress calls on Government to deliver on its commitment.

Congress recommends maintaining the State Pension as the bedrock of the pension system.

Congress recommends auto-enrolment contributions be publicly managed and paid out as a pay-related top-up benefit on the State Pension (Contributory) to auto-enrolled workers.

Congress further recommends that the significant profits from managing auto-enrolment investments be deposited into a National Pensions Reserve Fund to pre-fund future State Pensions.

Congress calls on Government to deliver on the commitment to benchmark and index link the State Pension payment rate without further delay.

6 CSO (2020) *Pension Coverage Survey 2019*

2. What's working with current State Pension arrangements?

Poverty Alleviation

The official at-risk-of-poverty line is set at 60 per cent of median household income, adjusted to take account of family size and composition. Households with income below this threshold are at risk of experiencing poverty. Whether they experience poverty will depend on a number of factors, including the degree to which the income is below the threshold; the length of time on a low income; possessions and assets, especially one's own home.

Improvements in the State Pension and secondary welfare supports by successive governments over the last two decades have halved the at-risk-of-poverty rate for pensioners from one in five (20.1 per cent) in 2005 to one in ten (11 per cent) today. People over 65 today have a lower risk of experiencing poverty compared to the population as a whole (14 per cent).

An alternative to measuring poverty as relative to other people's income, is the VPSJ Minimum Essential Standard of Living (MESL). This measures the adequacy gap between welfare payment rates for different household types and the expenditure needed to enable a life with dignity, at a minimum acceptable standard that members of the public agree nobody should be expected to live below. While pensioner couple households reliant on the State Pension (Contributory) demonstrate income adequacy, pensioners living alone have greater vulnerability to income inadequacy. Due to the lack of public transport and the resulting additional €67 average weekly cost for running a car, a pensioner living alone in rural Ireland in 2020 had a significant income shortfall of €47.24 per week.[7]

Congress recommends adequate public transport for rural areas be a Government priority and it recognised as essential for allowing all pensioners realise the value of Free Travel in order to enable income adequacy when dependent on the State Pension.

Coverage

Since 1961, when a contribution-based State Pension was first introduced, public pension coverage has gradually grown, with married women, high earning professionals, farmers, the self-employed, part-time workers and new public servants fully incorporated in the social insurance system by the mid-1990s.[8]

By 2019, there were over 526,000 people in receipt of one of the State Pensions – 431,224 receiving the State Pension

7 VPSJ (2020) *MESL Pension Household Types* (Rural) https://www.budgeting.ie/download/pdf/sw_pen_r-2020.pdf (Urban) https://www.budgeting.ie/download/pdf/sw_pen_u-2020.pdf

8 From 1973 women retained their social insurance record on marriage without having to first prove their connection to the labour market i.e. make contributions for six months after marrying. In 1974 income limits for non-manual workers were abolished. Social insurance coverage was extended to the self-employed in 1988; part-time workers in 1991, and new public servants in 1995.

(Contributory) and 94,854 received the State Pension (Non-Contributory),[9] representing 78 per cent of the population aged over 65.[10]

At the same time the State Pension has become more complex with lots of qualifying conditions that are not easily understood and not always fair (discussed later). However, some of the newer provisions have been instrumental in improving coverage. For example, crediting contributions to workers who are temporarily inactive through, for example, illness or unemployment or providing full-time care, has preserved the social insurance record of many workers, women in particular, and thus their future pension entitlement (discussed later). Similarly, income disregards, while particularly complex, result in over 70 per cent of applicants who have insufficient contributions to qualify for the State Pension (Contributory) qualifying for the means-tested State Pension (Non-Contributory) at the maximum payment rate, which is 95 per cent the value of the full contributory pension.[11]

The planned changeover to a new formula, the so-called Total Contribution Approach, for calculating applicant's State Pension (Contributory) entitlement will simplify the pension and eliminate existing anomalies and inconsistencies (discussed later).

Congress agrees in principle with adopting a Total Contributions Approach and calls on Government to deliver on its commitment to introduce.

9 Department of Social Protection (2020) *Annual Report 2019* p.18
10 CSO (2019) *Population Estimates by Age Group, Sex and Year*
11 Oireachtas Joint Committee on Social Protection (July, 2017) *Review of State Pension (Contributory)* p.6

3. How best to accommodate those who provided long-term care for most of their working lives?

Credited Contributions

Credited social insurance contributions, commonly referred to as 'credits', are awarded to insured workers not in a position to make paid contributions due to sickness, invalidity, unemployment, maternity, caring, participating in specified training schemes, strikes and other miscellaneous circumstances. The objective of credits is to preserve a worker's insurance record and their future entitlements by covering gaps in income from employment, for a limited duration.

A 10-year/ 520 contributions limit on credits for *non-caring* contingencies over an applicant's working life is planned in the upcoming changeover to a new formula, the so-called Total Contribution Approach, for calculating the State Pension (Contributory) payment rate. Government is proposing that from 2022 applicants must have at least 40 years/ 2080 contributions in total to qualify for the full weekly payment.[12] Those with fewer than 40 years/ 2080 contributions will receive a pro-rata payment i.e. 1/40th of the standard rate for each year/ 52 contributions.

Back in 1996 a Homemakers Scheme was introduced for workers, overwhelmingly women, exiting employment to provide care. Each full year spent caring is disregarded when calculating the rate of payment, up to a 20 years limit. Under the Total Contributions Approach, the Homemakers Scheme will be replaced with a new HomeCaring Credit which will also provide up to 20 years/ 1040 credited contributions to State Pension (Contributory) applicants providing full-time care to children under age 12 or to a sick or incapacitated person of any age.

Congress notes that the proposed new HomeCaring Credit:

(i) Will have no limit on backdating caring periods, unlike the existing Homemakers Scheme which does not recognise periods before 1994.

(ii) The retention of the 20 years/ 1040 credits for caring duties is a significant improvement on the 10 years/ 520 credits cap Government had originally committed to implement.[13]

(iii) The 20 years/ 1040 credits limit is comparatively favourable to the length of caring periods allowed for pension purposes in other EU member states.

12 The number of contributions that will be required to received the full weekly payment rate under the Total Contributions Approach is still to be finalised.

13 Government of Ireland (2010) *National Pensions Framework* Dublin: The Stationery Office p.23

Congress further notes that certain categories of public servants, who have no entitlement to the State Pension (Contributory) and who have taken time out of the workforce to provide care, are not awarded similar credits for pension purposes. Consequently, their occupational pension can be less than a full State Pension, in contrast to the guaranteed floor built into the public service sick pay scheme.

Congress acknowledges the planned HomeCaring Credit as reasonable provision for preserving the pension entitlement of workers taking time out of employment to provide full-time care.

Paid Contribution Test

However, in order to qualify for any contributory benefit, including the State Pension (Contributory), applicants must have a minimum number of paid contributions in order to meet the 'paid contribution test'. This ensures no applicant is awarded any social insurance benefit based wholly on credits.

Under legislation passed in 1997 which came into effect in 2012, applicants for the State Pension (Contributory) must have at least 10 years/ 520 paid contributions over their working life i.e. they don't have to be consecutive years, to qualify.[14] Applicants who reached pension age before 2012 and after 2002, required a minimum 5 years/ 260 paid contributions.

The doubling of the paid contribution test disqualified applicants, mostly women, who would previously have qualified for a State Pension (Contributory) based on their insurance record. Family carers, mostly mothers, of children with complex needs are unlikely to ever return to insured employment. Applicants unable to meet the paid contribution test can instead apply for a non-contributory pension, but it is means-tested on both their and their spouse's income and capital. However, over 70 per cent do qualify at the full weekly payment rate which is over 95 per cent the value of the State Pension (Contributory).[15] For long-term carers in a high income or asset rich (e.g. farm) household, a more beneficial option is to claim as a dependent of their spouse, which is up to 90 per cent the value of the standard rate of the State Pension (Contributory), as this is based on the spouse's insurance record and the dependent's means. While both options provide carers with a pathway to a pension they both fail to recognise caring as a contribution.

In contrast, in the UK the paid contribution test was discontinued in 2010. That is, applicants now receive 1/35th of the standard rate for every 52 contributions, whether a paid contribution or credit. Such a measure allows more women, and long-term carers in particular, to qualify for a pension in their own right, instead of as a dependent, and does not distinguish between a contribution from employment or for caring.

Congress recommends abolishing the paid contribution condition for the State Pension (Contributory) for applicants providing long-term care.

14 Prior to 2002, a minimum 3 years/ 156 paid contributions were required to qualify.
15 Oireachtas Joint Committee on Social Protection (2017) *Review of State Pension (Contributory)* p.6

4. What concerns you with respect to current State Pension arrangements? AND

5. What specific policy, provision or other changes are needed to make State Pensions sustainable into the future?

Qualifying Age

When the State Pension (Contributory) was first introduced in 1961, the qualifying age was 70. A Retirement Pension, later renamed the State Pension (Transition), was also introduced to bridge the gap for workers aged 65 who had retired and met the qualifying social insurance conditions. Throughout the 1970s, the pension age was gradually reduced to 66, which left the transition pension effective for just one year.

In 2014 the State Pension (Transition) was discontinued in the first of three incremental changes to increase the qualifying age to 68 by 2028. This has had profound implications for the finances and dignity of many workers when they turn 65.

i. Forced retirement

Congress has actively contributed to the Workplace Relations Commission's Code of Practice on Longer Working, welcomed the Irish Human Rights and Equality Commission's retirement and fixed-term contract guidelines and legislation allowing public servants to work to age 70 on existing terms and conditions. We view these as positive developments for those workers *choosing* to continue to work beyond their mid-60s.

However, existing measures have proved inadequate for far too many workers wanting to remain in their job after the specified retirement age in their employment contract. To rectify this Congress is calling for an amendment of Section 34(4) of the Employment Equality Act. The amended Section 34(4) would include a new paragraph, reading as follows:

> 34(4) Without prejudice to *subsection* (3), it shall not constitute discrimination on the age ground to fix different ages for the retirement (whether voluntarily or compulsorily) of employees or any class or description of employees if —
>
> (a) it is objectively and reasonably justified by a legitimate aim, and
>
> (b) the means of achieving that aim are appropriate and necessary.
>
> *Provided that discrimination on the age ground shall be taken to occur where an employee is required to retire from his or her employment at an age which is earlier than the pensionable age, without his or her agreement or, unless otherwise required in a particular case by any enactment.*
>
> *"pensionable age" means the pensionable age as defined in the Social Welfare Consolidation Act 2005"*

It is wholly unacceptable for Government to pursue a policy of increasing the pension age while failing to make associated adjustments in employment law for workers willing and able to continue working. Indeed, the previous Government committed to: "consider the merits of restricting the capacity to use mandatory retirement provisions relative to the prevailing State pension age" by the end of 2018 should existing provision not result in greater employee flexibility to work beyond 65.[16] Congress calls on Government to deliver on its commitment without further delay. Not only would such reform protect the income of these workers, it protects the sustainability of the Social Insurance Fund to have benefits paid out for a shorter period.

Congress recommends an amendment to the Equality Employment Act making it illegal to force a worker to retire at an age earlier than the age at which the State Pension is generally available.

16 Government of Ireland (2018) *The Roadmap for Pension Reform 2018-2023* p.38

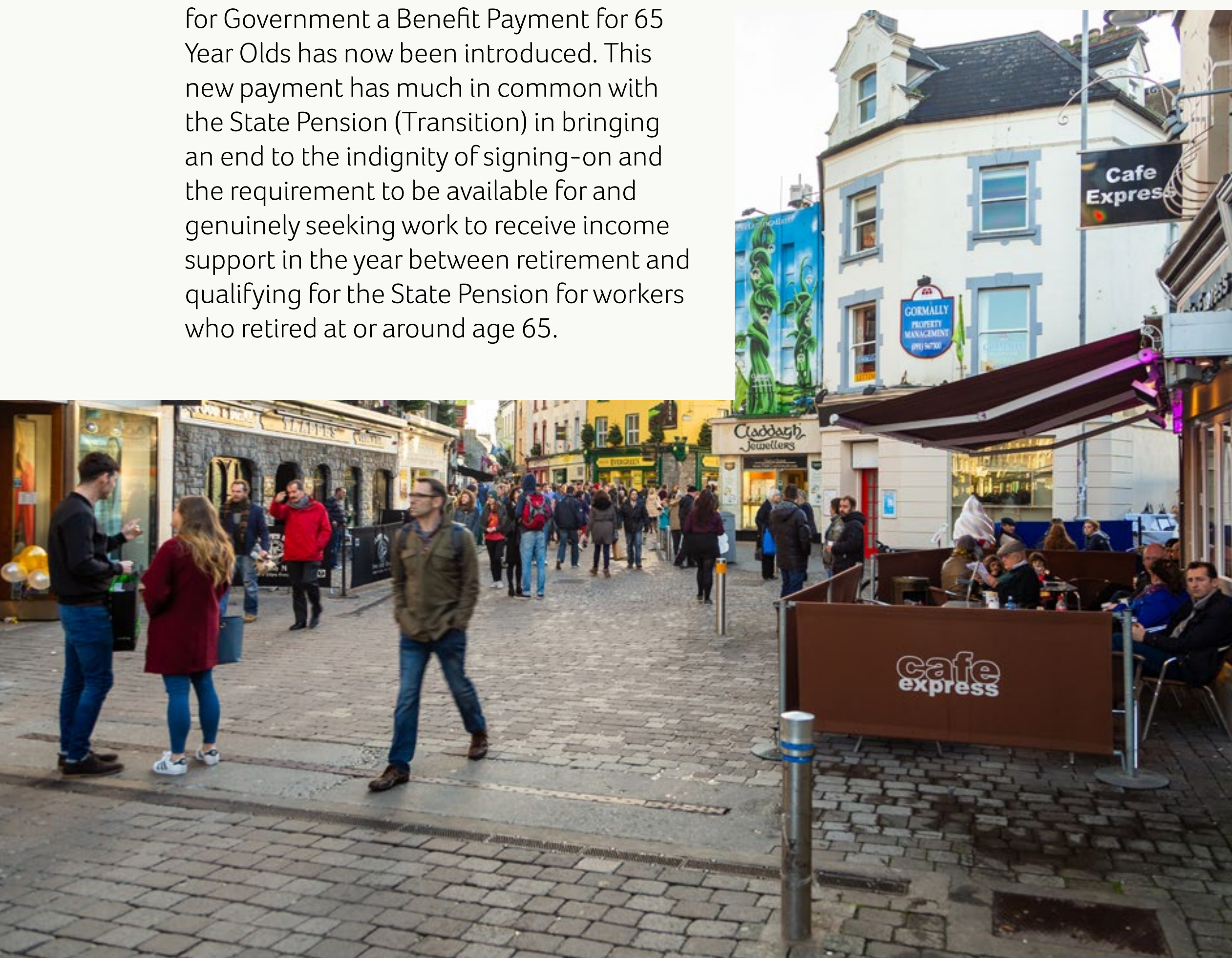
ii. State Pension (Transition)

While some workers will choose to extend their working life, and we support them in that, Congress is gravely concerned with the impact of the decision to abolish the State Pension (Transition) on other workers. The two options left open to workers physically unfit and financially compelled to continue in employment, after up to 50 years workings, was to find alternative employment or to claim a jobseeker's payment until they qualified for the State Pension at 66. This became a major issue in the 2020 general election campaign.

Under a commitment in the Programme for Government a Benefit Payment for 65 Year Olds has now been introduced. This new payment has much in common with the State Pension (Transition) in bringing an end to the indignity of signing-on and the requirement to be available for and genuinely seeking work to receive income support in the year between retirement and qualifying for the State Pension for workers who retired at or around age 65.

However, unlike the State Pension (Transition), it is *not* paid at the same rate as the State Pension (Contributory). Instead, it is set at the same rate as Jobseeker's Benefit at €203 per week i.e. €45.30 per week / €2,355.60 per annum less than the State Pension. This leaves low income retirees who do not have a supplementary pension dependent on a subsistence benefit that is significantly below the poverty line.

Congress calls on Government to align the Benefit Payment for 65 Year Olds payment rate with the State Pension (Contributory).



iii. Flexible pension age

Unlike Ireland, the State Pension in some EU member states recognises the young age at which workers can enter employment and also workers in physically arduous occupations who are unlikely to be physically capable of working in their trade into their 60s.

For example, in Germany the qualifying age for the statutory pension is 65, gradually increasing to 67 years over a transition period from 2012 to 2029. However, workers who entered full-time employment at 18, straight out of school, and have made contributions every year since are eligible for the State Pension at 63 without any deductions in the payment rate. Also, a special 'fast accrual' provision allows mine-workers retire at the earlier age of 61 on 25 years contributions. Similarly, in Italy, under the 2018 'quota 100' plan, workers are eligible for the State Pension once the sum of their age and contribution years is equal to 100 – if they are 62 years old and have paid 38 years of contributions, for example.

This previous Government proposed providing workers with the option to defer receipt of their State Pension (Contributory) on an annual basis when they reached pension age. In return, an actuarial adjustment will be applied to increase the payment rate they receive when the pension is drawn down. Congress supports in principle this proposal and urges Government to act to deliver on this commitment.

Congress recommends introducing a lower pension age for workers who entered full-time employment at a young age and have a long contribution record.

Congress calls on Government to commit to undertaking an assessment of the merits of introducing a fast accrual provision in the State Pension (Contributory) for specified occupations.

Congress supports the provision in principle to enable workers defer receipt of their State Pension (Contributory) and calls on Government to deliver this reform without further delay.

Indexation

Ireland is unusual in setting the State Pension payment rate in the budget without use of a formula.

The previous Government committed to rectify this by way of benchmarking the pension at 34 per cent of average annual earnings, and automatically linking future payment increases to increases in prices and wages (whichever has the greater growth that year) by the end of 2018. This 'double-lock' would have the effect of ensuring the gap between those retired and those in work would not widen and

that pensioners' income would not be eroded by the gradual increase in the cost of living. This is particular important given the large numbers for whom the State Pension is their only source of income. Congress also views indexation as essential for safeguarding the State Pension against displacement over time by the move auto-enrolment scheme. Pegging the pension to 34 per cent average annual earnings would also have the immediate effect of increasing the standard rate by a €15 per week - from €248 to €263.[17]

Congress supports in principle the Government commitment to provide pensioners with greater income certainty on the value of their pension via benchmarking and the indexation, and calls on Government to deliver this measure without further delay.

Congress views the proposed target of 34 per cent average annual earnings to be a floor below which the value of the pension will not fall and not as a ceiling above which it cannot exceed, as finances allow.

Calculation Method

Under the existing 'yearly averaging' method for calculating the applicant's payment rate, which has applied to the State Pension (Contributory) since its introduction in 1961, a key qualifying condition is their average number of social insurance contributions per year.

The yearly average is calculated by dividing the number of total contributions by the number of years making contributions i.e. from the date the applicant first enters employment to their last contribution year before pension age. Yearly averages are grouped into rate bands and each band has a corresponding rate of payment. Applicants with a low yearly average receive a lower pension.

A significant anomaly arises with yearly averaging where a long gap outside of the labour market reduces the yearly average, which in turn reduces the rate of payment. A second inconsistency is that two people with the same total number of contributions can be awarded different rates due to differences in the length of time over which the contributions were made. Similarly, a person with a high number of contributions can get the same rate or less than another person with significantly fewer contributions. These anomalies have worsened since 2012 when two new rate bands were introduced and the rate paid for yearly averages of less than 40 contributions was lowered.

The previous Government committed to replacing the yearly average method with a new formula, the so-called Total Contribution Approach by Quarter 3 of 2020. Calculating an applicant's payment rate using the Total Contributions Approach will eliminate existing anomalies and inconsistencies in that the totality of contributions – as opposed to the timing of them – determines the payment rate.

Congress agrees in principle with adopting a Total Contributions Approach for calculating an applicant's payment rate and calls on Government to deliver on its commitment to introduce this.

17 (26 June 2020) Annual Earnings and Labour Costs https://www.cso.ie/en/releasesandpublications/er/elca/earningsand-labourcostsannualdata2019/

Congress recommends a sufficient phase-in period whereby the option to calculate the payment rate under the averaging or total contributions method remains in place for the medium term to avoid any adverse impact on applicants now at an age where they can do very little to improve their contributions record and who have a reasonable expectation that their future State Pension entitlement would not change significantly.

Auto-enrolment

One-third of current workers, 35 per cent, have no occupational pension and/or private pension arrangements to supplement their income from the State Pension and are exposed to a significant drop in their living standards when they retire.[18] This policy failure is rooted in the lack of a legal obligation on employers to contribute to an occupational pension and is further compounded by a pension system, including the application and value of tax incentives, that is overly complex and is not sufficiently understood to encourage pension saving among middle-income earners.

In response, the previous Government committed to introducing a quasi-mandatory occupational pension by the end of 2022, which will compel employers to include non-pensioned staff earning above a threshold into a retirement saving scheme and to make minimum contributions. Low-income employees will be able to opt-in on a voluntary basis. Workers can choose to opt-out following a minimum period of participation in the new 'auto-enrolment' scheme.

However, progress has been stalled and the roll-out will not now begin until at least 2023.

In our submission on the design of auto-enrolment, Congress recommended that retirement savings be publicly managed, in place of the four commercial pension providers proposed by Government. Instead of handing over the significant profits from managing auto-enrolment pension pots to private companies, they would be deposited into a National Pensions Reserve Fund (discussed later) to contribute to the future financing of the State Pension. The draw-down should be paid out to auto-enrolled workers in the form of a pay-related top-up benefit on the State Pension (Contributory).

Congress agrees in principle with the introduction of auto-enrolment as a means of increasing income adequacy for retirees and employer responsibility to contribute to their workers' retirement savings and calls for early discussions with the social partners to agree the timing of its introduction.

Congress recommends auto-enrolment savings be publicly managed and the profits deposited into a National Pensions Reserve Fund to contribute to the financing of the State Pension.

Congress further recommends the draw-down be paid out to auto-enrolled workers in the form of a pay-related top-up benefit on the State Pension (Contributory).

18 CSO (Jan 2020) *Pension Coverage Survey 2019*

Financing

i. Pay-as-you-go model

The debate on the sustainability of the State Pension into the future is largely based on the fact that it is not pre-funded. Rather than save or invest social insurance contributions, the contributions from current workers are used to pay for the pensions of current pensioners. This pay-as-you-go financing model is weakened by an ageing population. Government population projections suggest the pensioner-to-worker dependency ratio is set to double over the next 30 years. That is, while there are currently around five people of working age for every person aged 65 or over, by 2050 this ratio is projected to be just over two (discussed later).

Back in 2001, the Government did establish a public investment fund - the National Pensions Reserve Fund (NPRF), with the goal of supplementing the pay-as-you-go financing model from 2025. The NPRF was started with the privatisation proceeds of Telcom Eireann and added to with annual deposits form Government equivalent of one per cent of GNP. In Ireland, the Exchequer only contributes to the State Pension if the accumulated surplus in the Social Insurance Fund is exhausted and its income insufficient to meet its in-year liabilities.[19] However, in 2009 NPRF assets were used to help fill the large gap in the public finances and it was finally abolished in 2013.[20] The target for the NPRF was €140 billion by 2025 which was projected to cover 25 per cent of the State Pensions liability and the cost of public sector pensions.[21]

Ireland must capitalise on our less immediate demographic challenge and our lower relative pension expenditure to restart pre-funding the State Pension into the future. As discussed above, Congress recommends the profits from publicly managing auto-enrolment investments should be deposited into a new NPRF, instead of being handed over to private pension providers as currently planned.

Congress recommends Government commits to re-establishing a funding mechanism to pre-fund pension expenditure into the future.

ii. Contribution rates

The debate on the sustainability of the State Pension into the future has almost exclusively focused on the cost of pensions to be paid out of the Social Insurance Fund, while ignoring the revenue coming in - contribution rates. This is all the more surprising when one considers that in all other circumstances when a pension scheme is in difficulty, workers alone are not expected to shoulder the shortfall. Employers are also expected to contribute to addressing the deficit.

Employee taxes on labour and social insurance in Ireland are close to the OECD average. On the other hand, employer contributions are markedly lower than average (discussed below). Equally, on a

19 An Exchequer contribution was required every year since the Social Insurance Fund was established in 1952, bar 15 of those years when it was in surplus (1997-2007 and 2016-2019 inclusive).
20 The NPRF was criticised for making the public finances look worse in that the 1 per cent transfer of GNP reduced the funds available for current expenditure, both public and private.
21 Somers, M (2007) *Irish Pensions* p.11

per person basis taxation, including social contributions, levied on the self-employed is relatively low in Ireland.

The self-employed pay a 4 per cent rate of social insurance, subject to earning above €5,000 per annum, compared to the standard 15.05 per cent rate paid in respect to most PAYE employees – comprising of 4 per cent payable by the employee and 11.5 per cent by their employer. Historically, the self-employed only qualified for a narrow range of benefits which was the justification for their smaller contribution. But this is no longer the case. Following changes by the previous Government, access to invalidity, jobseekers, parental, paternity, and treatment benefits was extended to the 350,000 self-employed contributors without any corresponding increase in their social insurance contribution. That is, the self employed are now covered for approximately 93 per cent of the value of all benefits paid out of the Social Insurance Fund in return for a contribution 11 percentage points lower than that made in respect of employees.[22]

The State's advisory body, the Tax Strategy Group, proposed that consideration be given in budgets 2020 and 2021 to adjusting the self-employed social insurance contribution rate to that of the standard rate of employer social insurance (i.e. 11.05 per cent) incrementally over four budgets.[23] Table 2 sets out their provisional estimates of the yield to the Social Insurance Fund following such increases.

Congress recommends Government adopts the Tax Strategy Group proposal to adjust the self-employed social insurance contribution to align with the level of benefits they can access.

Table 2: Provisional Estimated Yields from Proposed Increases in Self-Employed PRSI

Rate	Full Year Yield € millions
Current Rate of 4%	550
Increase to 5.75% from January year 1	780
Increase to 7.5% in from January year 2	1,000
Increase to 9.25% in year 3 from January year 3	1,250
Increase to 11.05% in year 4 from January year 4	1,500

22 Tax Strategy Group (2020) *PRSI for Self-Employed Workers* 20-4 p.5
23 *Ibid* p.11

6. Sustainable Reform Proposals

Fiscal Policy

The long-term sustainability of the pension system and indeed broader fiscal sustainability are functions of the economy's long-run growth potential, which is, in turn, a function of all aspects of fiscal policy. As such, any attempt to assess the sustainability of the pension system without incorporating a full analysis of all aspects of actual and potential revenue raising and actual and potential government spending decisions is fundamentally flawed.

i. Revenue raising

The previous Government failed to deliver on a commitment to review social insurance contribution rates by the end of 2018. Following on from a new commitment under the Programme for Government, a Commission on taxation and welfare is now due to be established.

Analysis carried out by the NERI shows Ireland to have significant areas of under-taxation when compared to similar European economies and total government revenue to be lower than in the EU as a whole.[24] In 2018, Ireland had a revenue shortfall of 3.1 percentage points of output (GNI* basis) or €6 billion. To the extent that we can consider Ireland 'low tax', it is in relation to the taxation of labour, most notably payroll taxes and social contributions.[25] Ireland's Implicit Tax Rate (ITR) on labour income is 32.9 per cent and below the EU-27 average of 38.2. However, drilling down into our topline figure shows that the ITR on employees in Ireland (24.1 per cent) is actually above the EU average (21.1 per cent). The shortfall is in relation to employer contributions, where the ITR on employers in Ireland (8.8 per cent) is just half of the EU-27 average (17.1 per cent).

Congress recommends Government align employer contributions with the EU average.

24 Goldrick-Kelly, P. Mac Flynn, P. McDonnell, T (2020) *Reformation Tax and Spend in the United Kingdom and the Republic of Ireland* NERI Working Paper Series 67:2020

25 Taxes on consumption generate yields that are similar to EU average, while the yields from capital taxes exceed EU averages. This is explained by Ireland's very high capital share of national income (the potential tax base), which is in turn a function of multinational tax planning and decoupled from real economic activity in Ireland, Goldrick-Kelly et al (2020) *ibid*

ii. Demographic projections

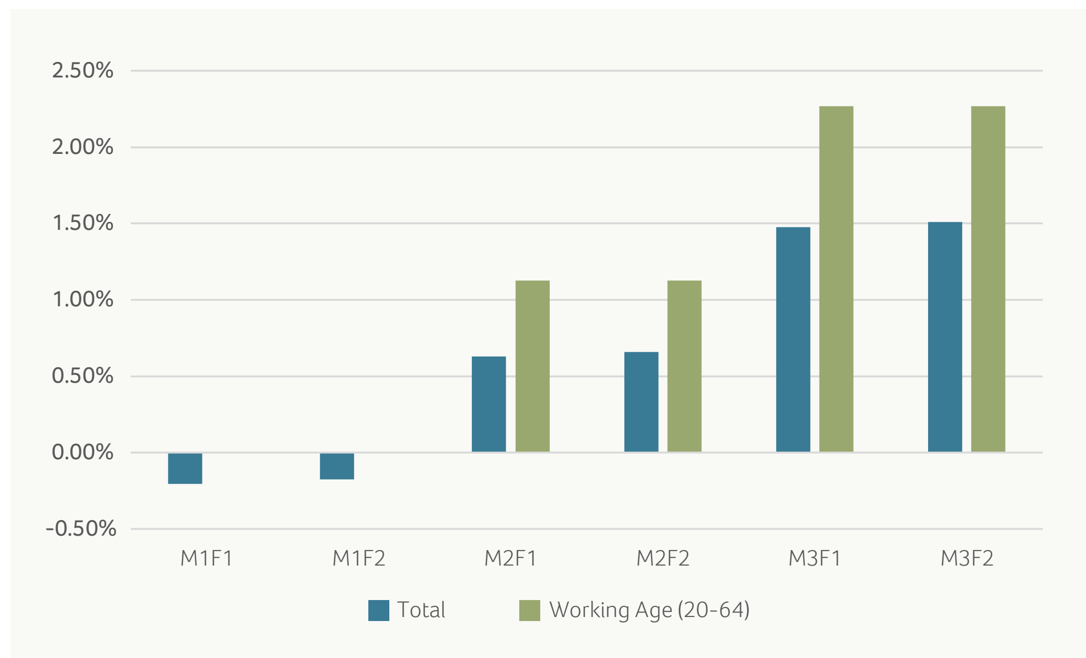
Projections relating to the fiscal impact of demographic changes, particularly in the area of State Pension sustainability, are sensitive to assumptions made about life expectancy, fertility and migration.

While there is broad agreement about the general trend in the first two factors - that life expectancy will increase and fertility rates will decline - there is far less agreement about the extent of migration into Ireland. This is significant because migrants are more likely to be younger than the population as a whole.

Increased migration therefore implies a larger working age population with positive implications for the sustainability of the State Pension and Social Insurance Fund.

This can be demonstrated with reference to the four years of data following the latest population projections in 2016. In 2020, the prime working age cohort (between 20 and 64) was larger in reality than under any projection scenario. In aggregate, the scenario closest to real observed data was modest fertility accompanied by high net migration (M1F2).

Chart 1: Percentage difference between real population and projection estimate 2020



The M1F2 is the scenario with highest ratio of working age people to school age and elderly cohorts and the second highest regarding the elderly in 2051. This would imply a significantly more optimistic picture in sustainability terms relative to more pessimistic projections (including the central M2F2 projection used in most analyses) – and mean a greater number of working age people supporting pension entitlements, particularly when combined with policy to increase workforce participation (discussed later).

The net positive fiscal impact of immigration on the sustainability of the State Pension, via expanding the contribution base to help to cover existing and new pension claims, is not lost on other OECD countries who face an increasing demographic strain. This underscores the importance of Ireland continuing to be a desirable destination for workers and a welcoming country for current and future migrants to relocate.

Congress recommends Government recognises the relationship between immigration, the contribution base and the future sustainability of the State Pension in the design of immigration policies.

iii. Productivity and public services

Any analysis of fiscal sustainability would be fundamentally incomplete and therefore inherently flawed if it did not adequately consider the potential impact of fiscal policy on an economy's long-run productivity growth and output growth.

Long-run economic growth is endogenously linked to fiscal policy decisions. This means that the sustainability of the State Pension is not

independent of other aspects of state revenue raising and government spending. It is true that productivity has been in decline in many advanced economies in recent years. However, this development is itself connected to fiscal policy. In particular, there was a decline in public investment and public R&D in many countries, especially in the wake of the financial crash. It is not inevitable that the period of lower productivity growth will continue.

We know that long-run per capita output is determined by: (A) the proportion of the working-age population as a percent of the total population, (B) the percent of the working age population working for pay or profit, (C) the average number of hours worked per person working and, (D) the average output per unit of hour worked (i.e. labour productivity). Analysis carried out by the NERI makes clear that best way to sustain productivity growth is to increase investment in education and

skills, particularly in early years learning; to increase investment in the production, diffusion and use of new ideas, and to increase investment in productivity enhancing infrastructure.[26] These are all aspects of fiscal policy.

In addition, the early years are the most important for human capital development, and external factors, like poverty, can have extremely damaging and lasting effects on human capital. This means that even social transfers, to the extent that they reduce poverty, can influence long-run economic growth. Finally, fiscal policy can influence the employment rate and hours worked through tax policy and/or by removing barriers to employment. For example, our female employment rate is second lowest among 12 peer EU countries. This is little surprise. Childcare costs, relative to wages, are the highest in the EU for lone parents and second highest for couples.[27] Improving the availability and reducing the cost of childcare would have a positive impact on the percentage of the working age population in employment and the average number of hours worked.

Congress recommends increased investment in productivity enhancing infrastructure and its importance recognised by Government for the future sustainability of the State Pension.

26 McDonnell, T (2015) *Cultivating Long-Run Economic Growth in the Republic of Ireland* NERI Working Paper Series 31:2015
27 European Commission (2020) *Key Data on Early Childhood Education and Care in Europe 2019*

Summary and Conclusions

The key issues for Congress in respect to the State Pension (Contributory) are as follows:

I. *Congress recommends maintaining the State Pension as the bedrock of the pension system.*

II. *Congress recommends auto-enrolment contributions be publicly managed and paid out as a top-up on the State Pension (Contributory).*

III. *Congress further recommends that the significant profits from managing auto-enrolment investments be deposited into a new National Pensions Reserve Fund to pre-fund future State Pensions expenditure.*

IV. *Congress recommends adequate public transport for rural areas be a Government priority and it recognised as essential for allowing all pensioners realise the value of Free Travel in order to enable income adequacy when dependent on the State Pension.*

V. *Congress acknowledges the planned HomeCaring Credit as reasonable provision for preserving the pension entitlement of workers taking time out of employment to provide full-time care.*

VI. *Congress recommends abolishing the paid contribution condition for the State Pension (Contributory) for applicants providing long-term care.*

VII. *Congress recommends an amendment to the Employment Equality Act making it illegal to force a worker to retire at an age earlier than the age at which the State Pension is generally available.*

VIII. *Congress calls on Government to align the Benefit Payment for 65 Year Olds payment rate with the State Pension (Contributory).*

IX. *Congress recommends introducing a lower pension age for workers who entered full-time employment at a young age and have a long contribution history.*

X. *Congress calls on Government to commit to undertaking a review to assess the merits of introducing a fast accrual provision in the State Pension (Contributory) for physically arduous occupations.*

XI. *Congress supports in principle the Government commitment to allow workers defer receipt of their State Pension (Contributory) for a higher payment rate and calls on Government to deliver on its commitment without further delay.*

XII. *Congress supports the Government commitment to provide pensioners with greater income certainty on the value of their pension via benchmarking and the indexation, and calls on Government to deliver on its commitment without further delay.*

XIII. *Congress views the proposed target of 34 per cent average annual earnings to be a floor below which the value of the pension will not fall and not as a ceiling above which it cannot exceed, as finances allow.*

XIV. Congress agrees in principle with adopting a Total Contributions Approach for calculating an applicant's payment rate and calls on Government to deliver on its commitment to introduce this without further delay.

XV. Congress recommends a sufficient phase-in period for the Total Contributions Approach whereby the option to calculate the payment rate under the averaging or total contributions method remains for applicants now at an age where they can do very little to improve their contributions record and who have a reasonable expectation that their future State Pension entitlement would not change significantly.

XVII. Congress recommends Government commits to re-establishing a funding mechanism to partly fund future State Pension expenditure.

XVIII. Congress recommends Government adopts the Tax Strategy Group proposal to adjust the self-employed social insurance contribution to align with the level of benefits they can now access.

XIX. Congress recommends Government align employer contributions with the EU average.

XX. Congress recommends Government recognises the relationship between immigration, the contribution base and the future sustainability of the State Pension in the design of immigration policies.

XXI. Congress recommends increased investment in productivity enhancing infrastructure and its importance recognised by Government for the future sustainability of the State Pension.

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