National Youth Council of Ireland

Submission on Green Paper on Pensions

By the National Youth Council of Ireland

Introduction

The National Youth Council of Ireland (NYCI) is the representative body for voluntary youth organisations.

NYCI functions to represent the interests of young people and youth organisations. NYCI's role is recognised in legislation (Youth Work Act) and as a Social Partner. The NYCI aims through its member organisations and its representative role to empower young people to participate in society as fulfilled confident individuals. The work of the Youth Council is based on principles of equality, social justice and equal participation for all. In achieving these aims the NYCI seeks the emergence of a society in which young people are valued citizens who can make a meaningful contribution to their community.

Background

The Green Paper on Pensions covers the background to the Irish Pension System and a broad range of issues related to social welfare, occupational, personal and public service arrangements.

Concern for the Pension system has arisen with the increasing debate over the changing demographics of Ireland. While Ireland currently has a younger population than most European Countries, over the longer term the impact of population ageing in this country will be considerable. According to new data, the number of people of working age for each person aged 65 and over will fall from 6 in 2006 to 2 in 2050. Taking into account the fact that a proportion of those of working age will not be in employment, the ratio of workers to people aged 65 and over in 2050 will be 1.5:1.(1)

Current analysis predicts that public pension expenditure will rise from 5% of GDP (6% of GNP) at present to 13% of GDP by 2050 (15% of GNP).

Rationale

NYCI recognises the long-term need for a greater take-up of private pensions by Irish workers, especially younger workers. The Government's target of 70% coverage has not been achieved and by 2005 only 55% of the workforce had a second tier pension.(2) Among those under 30, only 38.9% have a private pension.(3)

Given that all the data and analysis highlight the cost benefits of taking out a pension early in the working life, we believe that the Government should be encouraging young people to do so as soon as they start work.

The National Pensions Review Board expressed concern about "*coverage among those under 50 on medium and lower incomes in the private sector, especially women. The Board does not believe that property or other asset ownership is significant among this group*."(4)

Barriers to Pension uptake for Young People

Cost of living

Many young people today are struggling to make ends meet with our high cost of living. By contributing to a pension, a greater proportion of their earnings is diverted and locked up in funds that are not available to them for many years. For many young people this is not an option, as they are living on a month to month basis with little money available to them after everyday costs and bills are paid, to put away into savings or pension schemes. Many young people are struggling to save for a deposit on a house and would view property holding a more tangible investment as opposed a pension.

Lack of understanding of Tax benefits

Research conducted by Irish Life and Irish Permanent has highlighted the confusion which exists about the current tax based incentive for pension investing. Just 25% of respondents indicated that they totally understood the current tax relief regime for pensions. It would appear that the current tax incentive for pension savings has had little real impact on consumers. They believe it is overly complicated and confused and the confusion which surrounds that issue does nothing to encourage greater saving for pensions. This would appear to be even more indicative of young people's understanding of tax benefits as in a survey conducted by MRBI 59% of young people aged between 20-24 and 66% of young people aged from 25-34 felt the 'complexity of pension products' represented a barrier to increasing pension coverage in Ireland.

Possible Approaches to Pensions Development

The Green Paper on Pensions looks at models for supplementary pension reforms based on either enhancing the existing system of voluntary provision or on introducing mandatory or soft mandatory approaches. A rise in the social insurance pension combined with a rise in the statutory retirement age is also considered as an alternative to reforms based on supplementary pensions.

The four models, enhanced Social Welfare, voluntary, mandatory and soft mandatory are discussed below.

NYCI would support The Pension Board recommendation that "changes must not damage existing pension provision or worsen the existing position of any pension scheme."(5)

Enhanced Social Welfare

Increases to State Pension

Current State Pension provision does not provide for 'adequate pension' which refers to a level of pension payment that corresponds to income. NYCI would welcome and encourage increases to the current State Pension.

The values of the old-age contributory pension and the retirement pension were both €167.30 in 2004, which according to the OECD, is about 30% of average earnings (on the OECD measure of average earnings). (OECD 2007)

Conclusion:

Notwithstanding any enhancements in the State Pension there will continue to be a need for promotion of a greater take up of private pension schemes, particularly by younger workers.

Supplementary Pension Schemes - Options:

1. Enhancement of existing Private Pension System

The State encourages individuals to supplement the Social Welfare pension with private pension arrangements by offering tax relief on private pension provision. It is estimated that over half of those in employment are covered by supplementary pension arrangements.(6)

Supplementary Pension provision is recommended if individuals are to achieve a level of 'adequate pension' on retirement, however, the current level of supplementary pension coverage is a cause for concern. If maintained, it will result in a major fall in income at retirement for much of the population and for a significant minority, an unacceptably large fall, which may leave them at risk of poverty if they are solely dependent on first pillar pension.

Equity of Tax relief

ICTU reported in 2005 that the top 10% of earners earn 40% of the benefits of pension tax relief.(7) While a study by the ESRI found that 75% of tax relief for pensions went to the wealthiest 20% of the population. (8)

At present the Government is providing very generous pension tax relief which costs the exchequer **€2.9bn** per annum. It is important to highlight that those in the higher income groups benefit most from tax relief on pensions and the fiscal policy in this regard is inequitable in its current form. "*It is generally agreed that the object of tax relief must be to incentivise and support those less able to make pension provision and not necessarily to subsidise those who are in the strongest position to do so*." (9)

It is clear that Government needs to divert tax relief away from those who do not need it, and towards those who need support to start and maintain a second tier pension, in particular young people.

Once there is a more equitable system in place, it should be followed with increased coverage, thus resulting in a more beneficial and worthwhile investment for a greater proportion of people.

In the *National Pensions Review* report, the Pensions Board proposed changes to the taxation arrangements for voluntary private pension provision. The Board recommended that the State incentive for personal contributions to Personal Retirement Savings Accounts (PRSAs) be granted by means of a matching contribution of €1 for each €1 invested (subject to a maximum amount).

Employer contributions would continue to be treated as a business expense.

The Board also recommended that PRSA Contributors would be allowed to withdraw up to 30% of their accumulated funds tax free before the age of 45. At retirement over age 60, 20% of the balance could be taken tax free (rather than the current 25%).

Further consideration should also be given to the implementation of this for all other pension vehicles, according to the Board. *'A flat contribution matching rate means that all tax-payers receive the same level of support irrespective of their marginal rate.'* (10)

The Board also recommended that tax relief for other forms of supplementary pension provision be allowed at the higher rate for all personal contributions. This should be applied by the current method of granting relief at source or through a method of refundable tax credit, where appropriate.

Increasing access to standard PRSA's should be made possible by eliminating the requirement to prepare a fact-finding questionnaire at the point of sale.

Incentives for Young People to start up Private Pensions

Recommendation:
NYCI proposes that the amount which should be eligible for tax relief on private pensions should be reduced from €254,000 to €100,000 per annum. This measure would generate significant savings that could then be used to provide incentives to all those who are outside the tax net or on a 20% tax rate when they start a pension. This could be funded by reforming the current tax–relief on pension contributions. This would involve reducing the level of tax savings higher income earners can avail of on pension contributions

Recommendation:
A State incentive for personal contributions to Personal Retirement Savings Accounts (PRSAs) be granted by means of a matching contribution of €1 for each personal contribution of €1 invested and for PRSA contributors to be allowed a limited access to their funds before the age of 45. The facility to withdraw part of the fund will make this structure more attractive to younger savers. Savings made by reducing the level of tax savings higher income earners can avail of on pension contributions could also be used to fund this incentive.

Recommendation:
Tax relief for other forms of supplementary pension provision be allowed at the higher rate for all personal contributions. This should be applied by the current method of granting relief at source or through a method of refundable tax credit, where appropriate.

2. Mandatory Pension Schemes

NYCI would be opposed mandatory pensions for a number of reasons:

It would place an unfair burden on many young people who are already struggling to make ends meet with our high costs of living: many young people would consider it as tax by another name.

Mandatory Pensions would remove the right of citizens to choose how to manage their income and future financial planning.

Mandatory pensions would negatively impact on younger workers in particular as they are more likely to be earning less than older workers and therefore a greater proportion of their earnings would be diverted away and locked up in funds and not be available to them for many years.

In light of the history of uncompetitive practises in the financial services sector, there is a danger that by marking pensions mandatory, the Government will create a "captured market" where the banks/financial institutions will have little incentive to provide good value products and will abuse this situation with high charges and costs.

3. Soft Mandatory Pension Schemes

NYCI would encourage Government to consider the soft mandatory pension scheme as reviewed by The Pension Board. The 'Soft' mandatory option includes an 'opt out' feature and also access to pension funds before retirement. All those beginning employment would automatically be enrolled in the scheme and those already in employment would have the opportunity to join as well as those who are self employed.

Contribution	**Pensions Board**	**NYCI**
Employee Contribution	**5% of Income**	**3% of Income**
Employer Contribution	**2% of Income**	**3% of Income**
Exchequer Contribution	**2% of Income to a Maximum contribution of €750 p.a.**	**3% of Income**

Table shows soft mandatory scheme contributions as considered by the Pensions Board and contributions as suggested by NYCI

Contributors could cease contributions after three months' contributions had been made. All employees who would be eligible to join on commencement of employment would be allowed to recommence contributions at any time at one month's notice.

Recommendation:
NYCI feel that contributions from all parties should be set at an even rate, i.e. 3% from Employee, Employer and Exchequer. This would serve to lessen the burden on the individual employee and increase the responsibility on the part of the employer, savings made from reduced tax relief could go towards the increase of payment on the part of the exchequer.

By allowing an 'opt-out' option, NYCI feel that the Government would be offering young people the choice to start a pension early on in their career. It would also compel a young person into thinking about their future and we believe that if the benefits of starting a pension early were properly presented and explained, the vast majority would accept the offer.

Cost
The cost to the Exchequer of the proposed 'soft mandatory' scheme would depend on take up, however, if 100,000 joined the scheme on the average industrial wage for 2007 of €33,000, then the cost is estimated at €95 million. Although there may be considerable upfront support costs for Government as people are enrolled, these costs would fall as people opt out of the scheme. The overall cost would be considerably lower than the Mandatory option

Coverage
If people are automatically enrolled into a new scheme coverage rates will rise. Coverage in particular will rise for those on low incomes and young people, groups that traditionally have a very low pension uptake rate.

Adequacy
Pension adequacy would be determined by contribution rate to the scheme. The proposed UK soft mandatory system is designed to deliver 45% replacement rates for lifetime median earners. (11)

Recommendation:

If Government is serious about the pensions issue, it must provide a more equitable fiscal policy which benefits lower income groups and encourages them to invest in a pension which will safeguard them in their old age. NYCI believe the **Soft Mandatory Pension Scheme option would be of most benefit to the Irish working population and in particular, younger workers.**

Summary of NYCI Recommendations for Budget Reform

Enhanced Social Welfare

- NYCI would welcome and encourage increases to the current State Pension.

Private Pension System

- NYCI proposes that Government should provide a State incentive for personal contributions to Personal Retirement Savings Accounts (PRSAs) by means of a matching contribution of €1 for each €1 invested and for PRSA contributors to be allowed a limited access to their funds before the age of 45.
- NYCI proposes that the amount which should be eligible for tax relief on private pensions should be reduced from €254,000 to €100,000 per annum. This measure would generate significant savings that could then be used to provide incentives to all those who are outside the tax net or on a 20% tax rate when they start a pension.
- Tax relief for other forms of supplementary pension provision be allowed at the higher rate for all personal contributions. This should be applied by the current method of granting relief at source or through a method of refundable tax credit, where appropriate.

Mandatory Pension Schemes

- NYCI would be opposed mandatory pensions

Soft Mandatory Pension Schemes

- NYCI would encourage Government to consider a 'soft mandatory' system for pensions.

Footnotes:

1) P.1 Green Paper on Pensions, October 2007

2) Table 4.18 P.52 Green Paper on Pensions, October 2007

3) Response to Dail Question by Minister Martin Cullen, T.D. 6th November 2007

4) National Pensions Review, Report of the Pensions Board, 2005

5) National Pensions Review, Report of the Pensions Board, 2005

6) Green Paper on Pensions, Department of Social Protection, 2007.

7) ICTU, 2005

8) Pension Priorities: Getting the Balance Right, ESRI October 2007

9) Green Paper on Pensions, Department of Social Protection, 2007.

10) National Pensions Review, Report of the Pensions Board, P.85, 2005

11) P.125, Green Paper on Pensions, Department of Social Protection 2007