Professional Insurance Brokers Association (PIBA) submission on the Green Paper on Pensions-May 2008

PIBA Recommendations

Advice and choice
PIBA believe that choice and advice should be maintained in any new system designed to enhance coverage. We would also point out that independent Brokers facilitate competition between providers thereby reducing costs, increasing fund performance and enhancing product design.

To illustrate the potential impact of such competition, assume a person aged 30 contributes €500 per month to a pension indexed at 5%, retiring at age 65. The impact of a 1% difference in investment performance is as follows:

5% p.a. investment performance	€553,000 fund
6% p.a. investment performance	€767,000 fund

In other words, there is a 39% increase in the fund as a result of a 1% increase in investment performance.

At an individual level, choice for the consumer leads to a more optimal selection of product and investment fund.

Any system of mandatory or soft mandatory coverage should guard against reducing such competition and choice in the provision of pensions.

Tax refliefs
Current pensions tax incentives play a key role in encouraging people to commit funds to long term pension savings vehicles, within a voluntary system.
Within a soft compulsory system (compulsory enrolment but voluntary opt out) tax incentives are key to encouraging people to stay enrolled and continue contributing.
Suggestions that a SSIA type tax credit system would work better with incentivising people to contribute to pensions arrangements than the current income tax relief method are wide of the mark in two important respects:

- The SSIA was a short term (5 years) vehicle where all funds (other than interest or gains) were returned tax free to the contributor after 5 years. By contrast in a pensions contract, a person may be contributing now but not get access to saved

funds for another 30 or more years, and then part of the benefits will be liable to income tax & Health Levy.

The motivational factors are entirely different as between short term savings and long term savings, and what worked for a 5 year savings plan (most of which were deposit based) is not necessarily going to work for a 30 year pensions savings product (which will likely be equity based).

- If tax credits were only to be allowed to pension savers at the standard rate, but emerging benefits at retirement (other than the amount which can be taken tax free) are to be taxed at marginal rate income tax, then the tax system will then act for many as a disincentive to contribute to a pension.

  In effect the pensions tax relief system would then become a form of taxation, in that a significant number of contributors would get relief on the way in at standard rate only (assuming the tax credit is set at standard rate) but would pay higher rate income tax & Health Levy on income taken from the vehicle in retirement.

With regard to suggested inequities in the current pensions tax relief system:

- The system already contains a substantial number of measures to limit and restrict the tax benefits of pension tax relief:
  - Age related limits, as a % of earnings, on tax relief on personal/employee contributions
  - A maximum earnings limit for tax relief on personal/employee contributions
  - A pension fund limit introduced in 2005, which penalises accumulation of retirement benefits/funds in excess of this limit
  - A minimum 3% pa drawdown for tax purposes has been introduced for Approved Retirement Funds (ARFs), starting on a phased basis in February 2008.
- Inequities, if they exist, can be solved by leveling up as well as leveling down.
- The greatest inequities in the current pensions system relate to the quality of benefits provided to different groups, rather than the level of tax relief provided. E.g. public sector employees enjoy unfunded defined benefit final salary pensions, which are then linked to salaries in retirement, with current and future generations of taxpayers footing the bill. However in contrast :
  - About 50 % of private sector defined benefit schemes are underfunded and may not pay out the benefits promised

- The average employer + employee contribution to defined contribution schemes is 11% of salary, which will never provide a pension even remotely close to what a similarly paid public sector employee will get in retirement.

PIBA therefore support either:

- The maintenance of the current pension tax relief granted on employee and employer contributions , or

- The granting of marginal rate income tax relief on all personal contributions to pension arrangements, combined with the maintenance of the current tax relief granted on employee contributions

Reducing red tape

The regulation of pensions regarding transfers to and from company schemes and other arrangements and maximum benefits should be simplified.

The regulation of providers and intermediaries should also be reviewed to remove burdensome regulation that adds little or no consumer protection (e.g. the certificate of benefit comparison for transfers from defined contribution pensions to PRSAs).

Insurance Mediation Regulations and the sale of PRSAs

There is a proposed exemption to the Insurance Mediation Directive Regulations 2005 that will, if passed, exclude insurance intermediaries who deal only with 'insurance policies' from the remit of the Investment Intermediaries Act 1995. However, an insurance intermediary who offers PRSAs through an insurance undertaking will continue to be subject to the dual regulation of the Investment Intermediaries Act 1995 and the Insurance Mediation Directive Regulations 2005 (because PRSAs (n) are listed as individuals instruments in the IIA, regardless of whether they have an insurance policy aspect or not). It is PIBA's contention that insurance Brokers who sell PRSAs through insurance undertakings should gain an equivalent exemption under the IIA. Otherwise, we feel that the sale of PRSAs will be deterred due to the fact that the regulatory environment would be anomalous as it would require the maintenance of a dual authorisation by insurance Brokers. PIBA has raised this issue with the Department of Finance; however, it is nonetheless appropriate to this review also given its potential to hamper pension provision.

Soft-mandatory pensions
PIBA supports the soft-mandatory approach described in the Green Paper as we feel that automatically entering people into a pensions scheme, while giving them the option to leave the scheme if they wanted, would be the most beneficial way of maximizing the current provision. It would also facilitate in surmounting people's "intertia" in joining the scheme. We believe this system can cut out on marketing costs and thus make it more viable for commercial providers to sell appropriate products. However, employers should be required to give a choice of providers or at least a selection is made from a minimum number of providers (reviewable every five years) or a Broker (who must deal with a least five insurers) would be appointed to recommend and manage the scheme.

We do not feel a mandatory approach to pension provisions would achieve the objective in the most efficient way. The State Pension is a simple low cost means of providing comprehensive pension provision and should not be interfered with by imposing an additional layer of mandatory pensions. The imposition of a mandatory pension regime might interfere with existing pension providers and might force people into pension provision where they might be better off saving for a mortgage or education.

Under a supplementary mandatory system, a key issue is the level of pension provision which the mandatory system would provide. There is a significant risk that whatever level is set will become the maximum or norm level of private pension provision for large sectors of the workforce, with no incentive for people to go beyond this level.

Therefore, if the level is set too low, the impact of the scheme is minimal in terms of improving pensions coverage. If set too high, affordability and loss of competitiveness issues arise for employers and the economy generally.

PIBA therefore believes a soft mandatory approach represents the best balance between coverage, the quality of the coverage, and affordability.

We believe in principle with allowing people to withdraw some of their fund before retirement, after a minimum contribution period for a deposit towards the purchase of a house as a means of encouraging, particularly young people, to make pension provision. We, at the same time, do have concerns that this would result in insufficient retirement funding-the very object of the process. There would be a definite need to impose limits on this option i.e. on the amount allowable for withdrawal and the purpose of the withdrawal. We would welcome further discussion on this.

Approved Retirement Funds
PIBA support the extension of the ARF option to all members of defined contribution occupational pension schemes, both:

- To act as an encouragement to employees to join such schemes and to make larger contributions to such schemes, and
- To remove the inequity in the current system whereby the ARF option for employees applies to AVCs, retirement annuities and PRSAs, but oddly not to benefits from a defined contribution occupational pension scheme. There is no logical reason to provide an employee with the ARF option if he contributes to a PRSA, but not to an occupational pension scheme.

The introduction of a 3% pa minimum ARF drawdown, for income tax purposes, deals with any tax inequity there may have been with funds transferred to an ARF or to the purchase of an annuity.

Long term care
This issue must be dealt with to properly address financial security in old age. Rules for funding in advance or taking sums (tax free) from retirement/ARF funds to cover this should be explored with a view to having a meaningful policy on providing financial security in old age.

Insurance against longevity
Deferred annuities purchased from an ARF should cover the risk of a pensioner outliving his/ her fund but they don't seem to be offered at present by Insurers.

Addressing long term care and longevity risk will free up the financial worries of people that often cause them to over conserve their funds in retirement to the detriment of the quality of life. We will discuss these concepts further if required by the Department.

Control of costs and charges
The Green Paper considers that mandatory or outright compulsion is an option for controlling costs/ charges associated with supplementary pension arrangements. PIBA is concerned that this would remove the need for advice from the market-"*the creation of simplified, compulsory products and arrangements don't require the provision of individual regulated advice to employers and individuals*."[1]

[1] 12.117 Green Paper on Pensions

A scheme run by the state would be very costly to implement and would result in an unimaginative, cumbersome and inflexible solution. We particularly believe that this approach would interfere inappropriately and inadvertently with the existing voluntary supplementary system and would result in unnecessary complexities. We also believe the absence of competition in such a system will reduce any gains over time.

Pensions Awareness/ Education

The public need to be educated on what provisions they should be making and why. This should form the basis of a strategic plan for government. This is especially important with increased life expectancy and the need for adequate provision for life. Education is key to making sure that people make adequate funding arrangements for retirement and that they are empowered to make informed decisions about their retirement funding.

"Your retirement income is at risk if you fail to keep up payments." This statement should be used on sales literature etc. as a means of promoting the significance of retirement funding. Equally the old adage "if individuals fail to plan, they plan to fail" should form a premise of pension promotion.

Providing that the security of products is not compromised, providers should be allowed more flexibility in the design of products. A more attractive product will increase coverage. Competition in the market place drives consumer choice and is to their ultimate benefit.

Public service employees have no difficulty in contributing to a pension scheme from the start of their employment. A similar culture needs to be cultivated in the private sector and the 'pensionable job' needs to me promoted as attractive and desirable.

Conclusion

In conclusion, we believe that competition, choice and advice should be at the heart of any new pension system. The current pensions tax relief system for contributions can encourage higher take up of pensions, when combined with a soft mandatory approach to private pension provision. The ARF option should be extended to all members of defined contribution pension arrangements, to encourage people to make higher pension contributions as well as to provide equity in the marketplace. Regulation should not impede the design of attractive products nor should it impede their sale. Education must be at the forefront of the strategic focus of the Government. These factors should result in a much higher participation of the general public in private pension provision and in the quality of such provision.