

Clients of Watson Wyatt

Introduction

This submission is being entered by Watson Wyatt on behalf of a small group of clients who have met on several occasions over recent months with the sole purpose of considering the issues set out in the Green Paper on Pensions.

Watson Wyatt's involvement in this process has been entirely secretarial in nature, and the resulting views as expressed below are solely those of the clients concerned.

Availability of ARFs

The group supports the view that ARFs should be made available to the members of all DC pension arrangements. It was felt that ARFs should not be extended to members of DB arrangements.

Integration with State Pension

The group has concerns in relation to the impact of high state pension increases on the pensions provided by integrated schemes, particularly in the case of lower paid members. It is considered inequitable that members may pay contributions for a number of years on a pensionable salary greater than that used to calculate their pension. However, the group believes that it will be difficult to find a legislative solution suitable for all pension schemes and that it would be preferable for plan sponsors and trustees to develop their own scheme specific solutions in individual cases. On balance the group does not support a legislative response to this issue.

Tax incentives

The group considers that an SSIA type incentive structure is preferable to the current tax relief structure. It is felt that this should be a simple ratio (e.g. 1 for 1 or 1 for 2) for all regardless of marginal tax rate. It is accepted that this could involve some redistribution of tax relief away from those on the higher income tax rate. The principle that all members should receive the same incentive regardless of their marginal tax rate is supported. The group does not support the general concept of allowing members access to their funds before retirement as it is felt this might not materially improve coverage and could create a significant administrative burden. However, a new SSIA arrangement to encourage individuals to start making pension provision could be introduced. This would operate for a limited period of say 5 years. At the end of the savings term there would be a requirement to "roll over" a significant proportion of the accumulated fund into a pensions vehicle. The balance would be available for immediate consumption (or possibly rolled over with additional incentive). If an individual does not roll over the required minimum proportion the amounts contributed by the Exchequer would be clawed back.

Flexibility in Old Age

The group believes that Revenue practice should be amended to allow a phased commencement of pension but that this should not be a mandatory requirement for individual schemes.

Mandatory Pensions

The group believes that the most efficient way to deal with coverage/adequacy issues is to improve the State pension. While accepting that this would involve increases in employer and employee PRSI, it would be preferable to the establishment of a completely new structure requiring separate contributions from employer, company and Exchequer.

The group does not support the introduction of a mandatory scheme and sees it as a blunt response to headline coverage statistics which may not provide an accurate picture of the real adequacy/coverage problem. The group has significant concerns in relation to the impact of a mandatory system on existing provision; in particular that it would lead to a “race to the bottom,” initially for new hires but eventually followed by a more complete collapse to the mandatory level of provision. The administrative aspects of a mandatory system (e.g. the contracting out and certification arrangements for existing schemes and the measures that might have to be introduced to prevent a devaluation of existing arrangements) are also areas of significant concern.

Funding Standard

There is general acceptance among the members of the group that the funding standard should be a discontinuance standard as at present. However, it is felt that an alternative to annuity buy out for larger schemes (where buy out would not in any event be practical in the event of a winding-up) should be developed. The group also supports taking pension increases out of the liabilities to be assessed for funding standard purposes.

The group feels strongly that the current priority order is inequitable and unsustainable and there is support for a reordering of priorities to achieve a more equitable outcome for non retired members. In particular, the concept of employed and deferred members receiving their benefits without pension increases before pension increases for retired members is supported.

Security

It was felt that the Irish market is not sufficiently large to support a Pension Protection Fund and that the insolvency of a single large employer could undermine such a system. There were mixed views on the possibility of a debt on employer. It was concluded that such a measure could undermine future DB accrual (or could be used as an excuse for reducing or terminating future DB accrual) and should not be introduced.

Coverage

The group believes that broad coverage percentages as used at present may not provide an accurate view of the real extent of the coverage problem which may not be as great as is widely perceived and that more sophisticated analysis is required before adopting radical

solutions such as a mandatory scheme.

In particular:

Migrant workers who now represent a significant proportion of the labour force are often focused on repatriating earnings with a view to their eventual return home.

We have experienced increased participation of part-time workers in the labour force many of whom will have partners with adequate pension provision to meet their joint needs.

Individuals very often have savings and other non-pension assets to support them in their retirement.

The group questions whether it is appropriate at a policy level to target pension coverage as an important issue for such individuals. Would mandatory pensions represent a real advancement for such individuals given their priorities?

In summary, it is felt that a more sophisticated analysis of coverage statistics is required to identify the real areas of problem coverage. This should focus on coverage statistics for those over say age 35 with more than say 3 years service in their current employment. To the extent that coverage needs to be improved, measures should be focused on the specific areas of concern rather than the entire workforce.

Review of State Pension

The group's preferred response to the escalating cost of state pensions is to increase the state pension age and believes that it may be possible to do this more quickly than is suggested in the Green Paper. The group suggests that the following model would ease earlier transition (the specific percentages quoted are indicative, of course):

1. Immediately redefine the state pension age as age 70.
2. Increase the state pension to 50% of average industrial earnings from age 70
3. Continue to permit retirement from age 65 onwards with the current level of state pension (34% of average industrial earnings) at age 65 and with stepped increases up to 50% at age 70.
4. Over time gradually withdraw/restrict the early retirement option i.e. increase the minimum retirement age to 70 over a relatively long period.

In principle, the group suggests that any increase in the real level of State pension (as a percentage of average industrial earnings) should be available only to those who retire after the current minimum state pension age of 65.

Cost of Public Sector Pensions

The group believes strongly that the current public sector pension scheme is unsustainable. In particular, it is felt that the practice of granting pension increases on a parity with pay basis is completely unjustifiable and should be changed as soon as possible. The group believes that all new entrants to the public sector should join a different type of scheme – possibly a hybrid arrangement in order to reduce long term costs and introduce some element of pension risk sharing in the sector.

