Green Paper Consultation response
May 2008

Introduction

This note outlines the views of Watson Wyatt (Ireland) Limited on how retirement provision in Ireland might develop over present and future generations. It is presented as a short overview of the key underlying themes we feel are most important in reviewing the pensions framework – we have not answered individually the questions set out for consideration in the paper. However, we will be happy to expand our thinking on any of the issues highlighted below.

(a) The role of the State in pension provision

Suggested actions:

- *Increase the current level of State benefits.*
- *Increase the State Pension Age.*
- *Introduce greater flexibility on when and how people can take their State benefits.*
- *Review public sector pensions on the grounds of cost.*
- *Separate policy setting and pension regulation bodies.*

Reasons:

One of the main drivers behind social welfare pension reform is to ensure adequate retirement provision for the population whilst retaining its affordability. Paying a higher benefit from a later age would be broadly cost neutral and would recognise that people are living longer as well as the increasing requirement for an adequate retirement pension.

Those who wish to work longer in later years should be supported and encouraged. Partial drawdown of benefits and greater flexibility surrounding retirement age would help to support this objective.

The cost of Public sector schemes should be fully quantified so that it can be factored into any comparison of aggregate remuneration relative to the private sector counterparts. In particular, the appropriateness and cost of providing pay related increases in retirement should be considered as part of this analysis.

Having two separate independent bodies, one for policy setting and implementation and the other for regulating the pension regime would avoid any potential conflicts. The objectives and role of each organisation would be clearly identifiable and each would be able to focus on its own priorities.

(b) How to increase pension coverage and adequacy

Suggested actions:

- *Greater emphasis on financial education – introduction of pension modules in secondary/tertiary education.*
- *Simplify current disclosure regime.*
- *Retain voluntary membership of private/public pension arrangements.*
- *Extend the ARF regime for all occupational pension schemes, subject to appropriate safeguards.*
- *Introduce greater flexibility surrounding retirement and purchase of annuities.*

Reasons:

There is no doubt that financial education is crucial to ensuring an adequate and secure retirement. There must be vehicles that allow individuals to plan carefully for retirement and understand exactly what benefits they could achieve, including a clear understanding of the tax benefits individuals receive. Creating awareness of pensions and making them a "strong brand" will surely enhance their attractiveness. Introducing a pension module as part of formal education, perhaps in transition year or in the first year of third level education, would help to ensure greater awareness and understanding.

Streamlined communications setting out the key messages, including risk versus return, are critical. It is questionable as to whether people understand what they are being told and whether the current disclosure regulations are too detailed.

The introduction of mandatory or soft mandatory pension arrangements creates the risk of higher unemployment or cost of goods, not to mention potential evasion techniques and "levelling down" from the Employers. There may also be further hindrance with the need for some test to ensure those current arrangements comply with the mandatory option. The current voluntary regime alongside a strong State provision is more suitable.

There is a need for greater flexibility on how one can use built up pension benefits at retirement. There should be a greater array of annuity options e.g. semi guaranteed annuities which have a discretionary performance related bonus on top. Being able to drawdown on partial pension benefits could be done through the extension of the ARF regime to all occupational pension schemes, but it would be important to ensure that appropriate safeguards are put in place, particularly in relation to defined benefit schemes.

(c) Minimum Funding Standard/Wind-up Priorities

Suggested actions:

- *Change the funding standard to a long-term basis, subject to specified benefits being fully covered on wind-up.*
- *Introduce a two tier system with a core accrued benefit protected for all members and remaining excess split appropriately.*
- *Change the priority orders in the event of wind-up.*

Reasons:

There is a conflict between the long-term funding of pension schemes and the need to cover the short-term potential wind-up liabilities. Meeting the funding standard implies member security for their benefits in the event of wind-up, but there are a number of reasons why it can be argued that this is not the case. Among other things, estimates of buy out costs are currently used but what they are is unknown in practice.

The Minimum Funding Standard is currently having a negative impact with market fluctuations very much determining whether it meets the standard or not and the burden of large contributions for the Employer over a short recovery period should the scheme fail the standard - a longer term basis would be preferable. By including a requirement to have full short-term protection for the core benefit referred to below, you would allow the funding of pensions to be dealt with in a more stable manner, while providing a very high level of security for the core entitlement.

There are anomalies and inequities with the current wind-up priorities. The entitlements of current pensioners, including those who have recently taken early retirement must be fully secured before any (non AVC) benefits are provided to active members and deferred pensioners below normal retirement age.

It would be fairer if a core accrued benefit was provided for all members as a first priority without any allowance for future pension increases – this is consistent with many other EU countries. The excess on top of the core benefit may be prioritised between non-pensioners and pensioners with the detail to be considered fully.