Inside the plan to defuse our pension timebomb

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For the first time, it appears a government is actually going to move on pension reform with a compulsory scheme for workers without pension plans of their own

It seems, that after many years of toying with pension reform, Ireland is finally getting a move on.

After years of governments discussing, reviewing and analysing Ireland's lack of pension coverage, last week finally saw some meaningful action.

In a bid to boost pension saving, the government has laid out its plans for a new pension scheme that people who do not have a pension will have to join, but will be able to opt out of if they want.

The proposed scheme will force employers to contribute to employee pensions and will also feature a state contribution. The move will see Ireland follow in the footsteps of other countries, such as Britain and New Zealand.

Proposals unveiled bythe Minister for Social Protection Regina Doherty last Wednesday outlined what's being considered for the proposed new automatic enrolment pension scheme, which will be phased in from 2022.

According to Doherty, automatic enrolment is "perhaps the most fundamental policy reform in a generation in terms of retirement savings provision".

In a nutshell, workers aged between 23 and 60 who earn more than €20,000 will be automatically enrolled and will have to pay 1 per cent of their salary into a pension from 2022. Employers will be obliged to match the contribution. Contributions will rise gradually over time, and by 2028 both employee and employer will pay in 6 per cent of salary.

On top of this, the state will provide some sort of incentive for retirement savers. The government's proposal is a little vague on exactly how this will work, but suggests a contribution equivalent to €1 for every €3 saved by employees.

But the government has stressed that nothing is set in stone just yet. Its auto-enrolment discussion paper, known as a 'straw man', will be the subject of a public consultation that runs until November. And within the document, some 50 questions are posed to tease out how the scheme should work.

For now, there are "no huge surprises", according to Bernard Walsh, head of pensions and investments with Bank of Ireland Investment Markets. "Anything to stimulate pension coverage is something we welcome," he said, adding that it was time for a new approach to boost pension saving.

"We've had the carrot of tax relief for a long time, so maybe it is time for the stick of automatic enrolment. It has worked elsewhere," Walsh said.

However, he raised concerns about the timeline, saying it will be another decade before contributions reach the target level under the proposed scheme. "I don't see why it will take so long to get it up and running," he said.

Doherty's department says that the "projected timeframe reflects the scale of such a programme".

FIGURING OUT THE DETAIL

Pension experts have broadly welcomed the proposals, acknowledging that the government is finally taking some action after years of discussion.

But there's a lot of ironing out to be done on the nitty-gritty of the plan, and how it will work in reality.

For example, the straw man paper mentions phasing in automatic enrolment from 2022 over a two-year period. According to Jerry Moriarty, chief executive of the Irish Association of Pension Funds (IAPF), it's likely that this could follow the model used in other countries.

"There's no great detail on the two-year phase-in period, but in the UK, they started with bigger employers first and then moved on to smaller ones," Moriarty said.

"They are also looking at building a clearing house model, where employers pay contributions to one central body," he said. However, there's little detail as yet on how much that will cost, and crucially, who will pay for it.

EMPLOYER ISSUES

For employers, the new scheme will bring extra cost and extra admin too.

Walsh cited a recent conversation with a hotelier who raised concerns about the "massive admin burden" the proposed system might create for those with a "transient workforce".

Moriarty agreed that this could be "tricky". He said that there are a number of scenarios which might prove awkward to administer, such as part-time workers with multiple jobs who have total income that brings them over the €20,000 entry point for the scheme.

Or, for example, people who do a lot of seasonal overtime, such as those working in the retail sector. "Will employers have to check at every payroll if someone is eligible to be enrolled? It would be confusing for employees too," Moriarty said. "It might be easier to check once a year, and enrol people if they are eligible at that point."

And, on this administrative headache of trying to figure out who to enrol, Ireland could do well to listen to others who have the benefit of hindsight.

In an interview with this newspaper last year, Helen Dean, the chief executive of Britain's National Employment Savings Trust (Nest), a government-backed auto-enrolment pension scheme introduced in 2012, spoke about what she'd do differently, given the chance.

"With the best of intentions, I think we designed in some policy complexity, that with the benefit of hindsight, is not that helpful," she said.

"An example would be we looked at auto-enrolment and created some criteria that define when someone is automatically enrolled. You have to be aged 22, you have to be earning over a certain amount. That seemed very logical from a policy perspective, but when you look at that from the point of view of the employer, who has to do a workforce assessment, that has made things very complicated.

"Many employers say they'd prefer to just automatically enrol everyone. Thinking about the operational implications for the employer, and the scheme, of some of the policy choices, and designing it from the outset to be as simple as possible, I think that would be the biggest lesson," she said.

ALREADY HAVE A PENSION?

Another matter that will require careful consideration is how to treat employees who already have a pension.

The Department of Social Protection say that the "system is intended to address the needs of those who are currently without supplementary retirement savings" and "will not impact on employees who already have pension coverage which meets, or exceeds, any minimum standards required by the system".

But what will happen if someone has a pension, but with contributions lower than the automatic enrolment scheme? "Where an occupational scheme has matching employee and employer contributions of say 3 per cent each, will they have to scale it up to reach the target contributions?" Walsh asked.

Moriarty said that in this scenario there are a number of options, such as "bring their own scheme to that level, or put everyone in the new one".

It's practical questions like this that will need to be considered in the months ahead, he said. "It can be figured out, but it needs to be addressed."

TALKING TAX

Another big talking point raised by the pension proposals is what lies ahead for pension tax relief, with experts scrutinising the government's proposed contribution under the scheme.

Currently, contributions to a private pension are subject to tax relief at the marginal rate.

According to Jim Connolly, head of pensions and technical services at Goodbody, the proposed state contribution under the new automatic enrolment scheme is "a fundamental departure from the way it works at the moment".

"For every €3 someone puts in, the government will put in €1," he said, adding that this effectively equates to relief of 25 per cent.

The IAPF's Moriarty said that "the worry is that this could be seen as a step towards reducing the tax relief".

Reducing tax relief on pension contributions would act as a disincentive to retirement saving, Walsh said. "And really that would be cutting the legs out from under this whole process."

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