



COMMISSION ON TAXATION
AN COIMISIÚN UM CHÁNACHAS

PART 10
TAX INCENTIVES FOR
RETIREMENT SAVINGS



Part 10:

Tax incentives for Retirement Savings — *consider how the tax system can encourage long term savings to meet the needs of retirement*

Section 1 is an introduction.

Section 2 describes the general context.

Section 3 summarises the tax treatment of the supplementary pension provision.

Section 4 sets out criteria to encourage long-term savings to meet the needs of retirement

Section 5 contains our review of options for tax relief.

Section 6 describes a new retirement savings scheme.

Section 7 contains a summary of our overall recommendations.

Section 8 deals with other issues related to the tax treatment of retirement provision.

Appendices 1 and 2 contain supplementary information.

Our recommendations in this Part are as follows:

10.1	The regime for non-funded pensions should be examined to identify the implicit tax cost to the Exchequer in the context of an equitable distribution of the tax expenditure on pensions.
10.2	The current tax relief for personal retirement provision should in the medium to long-term be replaced by a matching Exchequer contribution of €1 for each €1.60 contributed by the taxpayer.
10.3	The matching contribution approach should be accompanied by a kick-start provision involving a contribution of €1 for each €1 contributed by the taxpayer in the first, say, five years of pension provision by an individual.
10.4	The matching contribution should apply where an individual has relevant earnings including where, because of the level of his or her earnings, the individual is not liable to tax.
10.5	A soft-mandatory approach could make a significant contribution to increasing pension coverage and should be considered.
10.6	An employee's payslip should show the amounts contributed by the Exchequer to the employee's retirement savings.
10.7	A retirement savings scheme along the lines of the former SSIA scheme, that is easily understood and which involves an Exchequer contribution, should be introduced – the scheme is outlined in Box 10.16 of Part 10.
10.8	<ul style="list-style-type: none"> • As the annual earnings limit does not apply to employer contributions, there is a need to retain the standard fund threshold. • There should be a correlation between the annual earnings limit and the standard fund threshold, and the reduction in the annual earnings limit suggests that there should be a corresponding reduction in the standard fund threshold.
10.9	A lump sum taken on retirement should be liable to tax as follows: <ul style="list-style-type: none"> • An amount of up to €200,000 should be tax free. • The balance of the lump sum should be subject to tax at the standard rate of income tax.
10.10	The current tax relief rules should be reviewed to ensure that contributions and remuneration levels cannot be manipulated close to retirement to allow individuals to take advantage of unintended and inappropriate benefits.
10.11	Age-related limits on the amount of an individual's relevant earnings should continue.
10.12	The flexibility of an ARF should be extended to defined contribution occupational pension schemes.
10.13	Anomalies in the treatment of different retirement arrangements should be eliminated as far as possible.
10.14	The various ages specified in the legislation governing the time at which benefits may commence should be reviewed and conformed.

Section 1:

Introduction

1.1 The pensions remit

As part of our terms of reference, we were asked to consider how best the tax system can encourage long-term savings to meet the needs of retirement. Our examination is conducted within the context of the overall pensions system in Ireland, which is the subject of the Green Paper on Pensions¹, and two of our terms of reference in particular:

- Consider how best the tax system can encourage long term savings to meet the needs of retirement
- Review all tax expenditures with a view to assessing the economic and social benefits they deliver and to recommend the discontinuation of any which are unjustifiable on cost/benefit grounds

1.2 Saving for retirement

A State pension is provided through the social welfare system. The pension is intended to provide an adequate basic standard of living in retirement. In many cases the State pension is supplemented by private pension arrangements, generally through occupational pension schemes and personal pension plans, which are regulated by the State and are afforded support through the tax system.

Some people save to meet their retirement needs in other ways, for example through personal investments including real property. Home ownership can also be regarded as a part of the provision for retirement. The tax system affords relief on some, but not all, of these other savings mechanisms. People who are not high-rate taxpayers are less likely to avail of such savings mechanisms to accumulate assets.

1.3 Coverage and adequacy

The gap in coverage – whereby some individuals have limited capacity to save for retirement (or choose not to do so), and instead rely on the State pension to meet all of their needs – forms a backdrop to our deliberations. A key consideration in our examination of this issue is our changing demographics. By 2061, Ireland will move from an old-age dependency ratio of six people of working age to every one person aged 65 or over, to a ratio of 2:1 – in other words, just two people of working age to every one person aged 65 or over.

Unless there is more personal saving for retirement in the meantime, there is likely to be a significant gap in coverage. Various studies² have identified the gaps in pension coverage. We consider how best the tax system can contribute to closing those gaps by encouraging long-term savings to meet the needs of retirement.

Much work has already been done to identify the range of policy issues that need to be addressed and these are set out in the Green Paper on Pensions (2007). Section 7 of the Green Paper raises a number of options and poses a number of questions on incentives to encourage savings for retirement. We considered these and other options.

1 Green Paper on Pensions (2007)

2 OECD Economic Surveys: Ireland 2008 / Green Paper on Pension (2007) Section 3

There is no agreed methodology for measuring progress, nor is there any reliable means of gathering information in relation to the adequacy of retirement provision. However, the National Pensions Review found that there were a number of sources of data which might show a reasonable picture of the situation. The targets and adequacy of the National Pensions Review are set out in Box 10.1.

1.4 Market conditions

We share the general concern that a significant number of people in Ireland are not making adequate provision for their retirement. Our analysis and conclusions in this Part are informed by that concern. As regards our remit to consider the role of the tax system in encouraging people to make such provision, we are clear that the tax system alone will not address the problem – although it is now, and can continue to be, a part of the solution. There are also a number of equity issues in regard to the tax treatment of retirement savings and we took these into account.

We were mindful, in our deliberations, of the realities that the changed economic climate and the recent performance of pension funds is not making it easy for individuals to decide to invest in pension arrangements. In this Part of our Report, therefore, we are putting forward a model through which the tax system could make a contribution to encouraging people to save for their retirement and which addresses the equity principle.

One aspect of the model we present, that of giving a matching contribution, is appropriate to a more stable economic and retirement savings environment than exists at the time of publication of our Report. It is presented as a model for the medium to long term and as a contribution to the wider debate. A comprehensive examination of a range and mix of options and which is needed as a matter of urgency. The Green Paper on Pensions (and the impending White Paper) provides a timely framework for that debate.

Section 2: General context relating to retirement provision

2.1 National pension policy initiative

In 1998, the National Pensions Policy Initiative (NPPI) was published by the Pensions Board in conjunction with the Department of Social and Family Affairs. The NPPI set targets in relation to pension coverage and adequacy. These are set out in Box 10.1.

Box 10.1: NPPI targets

- The Board has come to a judgement that it would be reasonable to measure adequacy of gross retirement income from all sources (including lump sums and gratuities and other accumulated assets) against a benchmark of 50% of gross pre-retirement income subject to a minimum of 34% of average industrial earnings together with any associated adult dependant's allowance
- In summary, the Board considers that comprehensive achievement of an adequate level of income over a lifetime would involve an ultimate goal of some 70% of the total workforce over age 30 making, or having, supplementary pension provision. However, it will clearly take many years to reach that goal

The targets were reviewed in the National Pensions Review (NPR), which was published by the Pensions Board in October 2005. The view taken in the NPR was that the NPPI coverage and adequacy targets would not be met without some change to the existing voluntary pension system.

2.2 Towards 2016

In the Social Partnership agreement, Towards 2016, the parties agreed that all retired people should have adequate incomes; that the level of coverage of occupational pension schemes should be increased; and that the social partners would co-operate to promote improvements in the coverage of pension schemes towards the agreed NPPI target of 70% of the total workforce over age 30.

2.3 Programme for Government (2007-2012)

The Programme for Government 2007-2012 includes commitments relating to pension provision. These are set out in Box 10.2.

Box 10.2: Programme for Government 2007-2012

- Increase the basic State pension by around 50% to at least €300 per week by 2012
- Seek to develop imaginative proposals in the context of the Green Paper, and in consultation with the social partners, to provide an SSIA-type scheme in an effort to make supplementary pension provision more attractive to those on low incomes
- Aim to secure the target of at least 50% of pre-retirement earnings from all sources, including social welfare supports, private and occupational pensions, and savings and investments
- Remove anomalies identified in the pension system
- Ensure women are treated fairly in pension provision

2.4 The current arrangements regarding pension provision

The current arrangements regarding pension provisions are made up of two pillars. These are as follows:

The first pillar

The State pension comprises: a contributory pension for those who satisfy the PRSI contribution conditions, and a non-contributory pension, which is subject to a means test, for those who do not qualify for a contributory pension³. The State pension is intended to meet basic living needs.

The second pillar

This involves private pension arrangements intended to supplement the State pension. Supplementary provision is not mandatory. People are assisted through the tax system to make supplementary pension provision. Supplementary pension provision includes:

³ State pensions (transition) can be claimed at age 65 if the person is retired from full-time employment and satisfies social insurance contribution conditions. The State pension (contributory) can be claimed at age 66 or over, once social insurance contribution conditions are satisfied. The State pension (non-contributory) is a means-tested payment for people aged 66 or over who do not qualify for the State pension (contributory) based on their social insurance record.

- Occupational pension schemes: Provided in the public and private sectors, generally on a voluntary basis, by employers for their employees. Funded either jointly by employers and employees, or by the employer alone
- Personal pension schemes: Consist of retirement annuity contracts (RACs) (used mainly by the self-employed) and personal retirement savings accounts (PRSAs). They are voluntary⁴.

2.5 Occupational pension schemes

There are a number of types of occupational pension schemes as follows:

Defined benefit schemes

In the past⁵, the most common form of occupational pension scheme was a defined benefit scheme. Under this type of scheme, the pension and other benefits to be paid to members and their dependants are specified in the scheme rules, and are generally linked to final salary. The employer carries the investment and longevity risks⁶.

Defined contribution schemes

Another type of occupational scheme, the defined contribution scheme, is becoming more widely used. Under these schemes, the individual member's benefit is determined solely by reference to the contributions paid into the scheme, and the investment return earned on those contributions. The value of the pension at retirement depends on fund performance and interest rates at the time a pension annuity is purchased. In these schemes, the member bears the risk of investment performance by the fund.

Hybrid schemes⁷

Some more recent schemes combine elements of both the defined benefit and defined contribution approaches. A hybrid scheme is one that is neither a full defined benefit nor a full defined contribution scheme, but has some of the characteristics of each. In hybrid schemes, the risk is shared between the employer and the employee.

Table 10.1 sets out the numbers of schemes in each category.

4 In the sense that there is generally no obligation on individuals to effect any form of pension arrangements for themselves, or on employers to provide pension benefits for their employees (employers are obliged to offer a PRSA facility to their employees but are not obliged to contribute).

5 In substance, there have been no new defined benefit schemes. According to the Pensions Board, the registration of 237 new defined benefit schemes with the Board in 2008 should be seen in the context of 285 deregistrations in that year. Almost all of the new schemes were restructurings. The balance were schemes that had previously failed to register.

6 There is an overriding risk of the employer being unable to fund the scheme adequately due to solvency issues.

7 Examples of hybrid schemes would include: "career average" schemes, where the benefit offered is based on the average earnings throughout the member's entire career and "combination" schemes, where defined benefit applies to the first portion of a person's earnings and defined contribution applies to earnings above that portion.

Table 10.1 – Occupational pension schemes December 2008

Scheme size	Defined benefit		Defined contribution	
	No. of schemes	No. of members	No. of schemes	No. of members
Non group	29	29	68,504	68,504
1 to 50	749	12,660	21,330	89,277
51 to 99	156	11,511	332	22,952
100 to 500	230	53,097	222	41,338
501 to 1000	48	33,261	19	13,422
1001 +	59	469,364	17	36,704
Total	1,271	579,922	90,424	272,197

Source: The Pensions Board Annual Report and Accounts 2008

Note: Excludes AVC only, Death Benefit only, frozen schemes and schemes in wind-up. Hybrid schemes are not registered as a separate category.

2.6 Personal pension arrangements

Personal pension arrangements consist of RACs used by the self-employed and PRSAs. These contracts and accounts are similar to defined contribution pension schemes in so far as the investment risk lies solely with the individual who takes out the contract or account. Details are as follows:

Retirement annuity contracts (RACs)

An RAC is the formal name for what is normally called a personal pension. An RAC is a type of insurance contract approved by the Revenue Commissioners. The value of the ultimate benefits payable from the contract depends on the level of contributions paid, the investment return achieved, and the cost of buying the benefits. The total number of RACs is approximately 200,000⁸.

Personal retirement savings accounts (PRSAs)

PRSAs were introduced in 2002 as a flexible and portable pension product that can be used by everyone - employees, self-employed or unemployed. They are divided into standard and non-standard products. A PRSA is a long-term personal retirement account that enables a holder to save for retirement in a flexible manner. It is a contract between the account holder and a PRSA provider in the form of an investment account.

Like an RAC, the value of the ultimate benefits payable from the account depends on the level of contributions paid, the investment return achieved and the cost of buying the benefits. PRSAs are mainly vehicles for retirement savings for those who are not members of occupational pension schemes or those who make additional voluntary contributions (AVCs). Employers who do not provide an occupational pension scheme must provide access to a PRSA for their employees. Table 10.2 sets out the take-up of PRSAs since 2003.

Table 10.2 - Cumulative take up of PRSAs since 2003

Year	2003	2004	2005	2006	2007	2008
Standard Product	14,686	36,557	53,001	72,761	100,229	119,436
Non Standard Product	4,336	9,700	15,256	22,284	30,480	36,196
Total	19,022	46,257	68,257	95,045	130,709	155,632

Source: The Pensions Board Annual Report and Accounts 2008

Note: A standard PRSA is a contract that has a maximum administration charge of 5% on the contributions paid and 1% per annum on the assets under management. Investments are only allowed in pooled funds which include unit trusts and life company unit funds.

A non-standard PRSA is a contract that does not have maximum limits on charges and/or allows investments in funds other than pooled funds

2.7 Demographic considerations

Ireland's dependency ratio is six people of working age for every one person aged 65 or over. This dependency ratio is set to change dramatically in the coming decades:

- The overall size of the population is projected to reach approximately 6.5 million by 2050⁹
- The population share of those aged 65 and over is expected to more than double between now and 2050, from 11% to 28%. It is also likely that people will live longer
- In contrast, the population share of those of working age is projected to gradually decline during this period, from 69% to 57%
- The upward trend in the old-age dependency ratio implies that Ireland will move from having six people of working age for every older person, to two working for every one in retirement by 2050¹⁰

Because of these demographic considerations, the burden of providing the State pension in the longer term will increase, as lesser numbers of people will be working to support a greater number in retirement.

It is critical that provision is made for this eventuality. Individuals must be encouraged to make immediate and more adequate provision for their retirement. The available options include:

- Joining an occupational pension scheme, taking out a PRSA or entering into an RAC, all of which attract tax relief
- Accumulating other savings such as deposits, shares, bonds, fund investment, investment in property or in a business. While not all such savings are tax relieved, they could nonetheless contribute towards an adequate income in old age¹¹. These assets can, of course, be accessed at retirement, if they still exist, but they are not linked specifically to retirement because they can equally be accessed and used at an earlier stage. Consequently, they are not given further consideration here

9 Source Department of Finance projections based on CSO data.

10 Green Paper on Pensions Paragraph 3.4.

11 Home ownership also makes a contribution to retirement provision. A retired person who owns his or her own home, and whose mortgage has been repaid, will not have to incur the expense of providing a home. In addition, a person may be in a position to release some equity from his or her home. The tax system does not provide relief for home ownership in the context of provision for retirement. However, there are provisions within the tax system that support home ownership.

2.8 Gaps in retirement savings coverage

NPPI targets

The NPPI set out targets for first and second pillar pension coverage and adequacy. As Table 10.3 shows, progress has been slow in meeting the NPPI target for second pillar pension coverage of 70% of those in work aged between 30 and 65. That said, coverage has increased in recent years, and in 2008 stood at 61% of the target age group. Coverage under the private pension system has been measured at various points over the past decade.

Table 10.3 - Progress since 2002 towards NPPI supplementary pension coverage targets

		2002 CSO survey	2008 CSO survey	NPPI 2003	NPPI target ¹²
Pension coverage – all workforce		51%	54%	53%	60%
Pension coverage	Aged less than 30	36%	37%	34%	35%
	30 to 65	58%	61%	62%	70%
Pension coverage	Men	56%	56%	54%	59%
	Women	45%	50%	51%	61%
Pension coverage	Self-employed	44%	46%	36%	44%
	Employees	53%	56%	58%	64%

Source: National Pensions Review (2005). This table refers only to coverage and not to adequacy

While the above table illustrates that progress has been made towards reaching the NPPI targets, it is estimated that approximately one million people in the workforce still have no supplementary pension provision. Although there are differences between the CSO and NPPI figures, there remains a considerable gap between the 70% target and the 61% achieved.

2.9 Sectoral position

Annual surveys and updates¹³ undertaken by the CSO between 2002 and 2008 provide estimated breakdowns of pension coverage by economic sector, hours of work, occupation and company size. The broad patterns arising over that period are shown in Box 10.3.

12 To be achieved in the period after 2013.

13 CSO Quarterly National Household Survey: Pensions Module

Box 10.3: Patterns in pension coverage 2002-2008

- The sectors that had below-average coverage in 2002 showed similar patterns in 2008. The agriculture, construction, wholesale, retail and hotel and restaurant sectors are below the average occupational coverage level for employees, which is 56%. The self-employed (46%) show less variation by sector
- Part-time workers have lower than average coverage levels, as do employees of small companies
- Higher professional and technical occupations report higher than average coverage
- The public service pension schemes provide benefits on retirement for staff in the civil service, local authorities, Garda Síochána, the defence forces, the health and education sectors and in non-commercial State bodies. Employee coverage is close to 100% across the public service, with most new recruits, including atypical and part-time workers, becoming members of schemes¹⁴. This would suggest that coverage is lower in the private sector than the data in Table 10.3 would suggest, given that it is based on averages

2.10 Factors that contribute to less than adequate supplementary pension coverage

The reasons people do not save for retirement, despite the tax reliefs available, include some of the factors set out in Box 10.4, based on data compiled by the CSO¹⁵.

Box 10.4: Reasons why people do not save for retirement

- Never got around to organising a pension (32.5%)
- Cannot afford a pension (26.9%)
- No scheme available through work (8.4%)
- Other income source adequate (5%)
- Do not understand pensions (3.4%)
- Spouse's or partner's pension is sufficient (2.6%)
- Unable to access pension prior to retirement (0.9%)
- Other reason/do not know (20.3%)

Our consultation process revealed a number of other reasons that may contribute to less-than-adequate supplementary pension coverage. These include:

- Complexity
- Lack of transparency
- Lower income groups given lower level of tax relief on contributions
- Perceived lack of value of investment products
- Expectation that spouse's or partner's retirement income will be the main income source
- Lack of a consistent level of income
- Breaks in income
- Fund administration costs

¹⁴ This excludes commercial semi-State bodies. In addition, pension survey data is not broken down in such a way that would provide for a comparison between public and private sectors.

¹⁵ Quarterly National Household Budget Survey, December 2006

2.11 Gaps in adequacy of pension contributions

The National Pensions Review (2005) highlighted the difficulties involved in assessing the adequacy of pension contributions. There is no agreed methodology for measuring progress, nor is there any reliable means of gathering survey information in relation to the adequacy of contributions. However, the National Pensions Review found that there were a number of sources of data which, taken together, allowed it to build a reasonable picture of typical supplementary pension provision. The main findings are set out in Box 10.5.

Box 10.5: Findings of National Pensions Review (2005) on adequacy

- The majority of private sector defined benefit schemes will provide benefits greater than the NPPI target at retirement, for those who have spent most of their working life in the scheme. However, most people in the private sector do not remain with the same employer throughout their working lives
- The great majority of defined contribution scheme members are unlikely to have a retirement income equal to, or greater than, the NPPI target, irrespective of the length of time they are members of the scheme
- Additional voluntary contributions (AVCs) are increasingly likely as scheme members approach retirement. However, the typical contribution rate is unlikely to provide NPPI target benefits
- It is difficult to draw conclusions about adequacy from PRSA and RAC data, because of the lack of income data in the latter case, and because savers may have multiple contracts
- Inflation can erode the value of the benefits in retirement surprisingly quickly. For instance, over the 10 years to 2004, a period that would be considered to be one of comparatively low inflation, a pension of a fixed amount would have lost one quarter of its real value

Since the NPR was published, the position has been further exacerbated by the fall in value of pension assets. Ongoing volatility in world financial markets continues to be a source of serious concern for pension savings, many of which have suffered significant investment losses since 2007. It has been estimated by the Pensions Board that approximately 90% of all defined benefit schemes are underfunded and will not meet the requirements of the minimum funding standard. The unprecedented fall in the capital markets affects all forms of private pension provision, and will make achieving NPPI targets more difficult.

We are of the view that income adequacy in retirement can be improved by a package of measures that would encourage people to begin saving early and allow them to continue the saving habit during breaks in their career, in moving from one employment to another, or in switching to self-employment.

Section 3: Current tax treatment of supplementary pension provision

3.1 Introduction

Individuals are encouraged to supplement the State pension with private pension arrangements through tax relief on private pension provision. Just over half of those in employment belong to a

voluntary private pension scheme – see Table 10.3.

Support for supplementary pension provision in the tax system usually involves the deductibility for income tax purposes of contributions made to supplementary pension arrangements¹⁶. The income tax relief (subject to rules regarding caps and limits) is set out in Box 10.6.

Box 10.6: Relief for pension contributions

- Contributions made by employees under an approved occupational scheme are deductible for income tax purposes
- Contributions made by the employer to an approved occupational scheme are not charged to tax as a benefit-in-kind
- Payments made to a PRSA are deductible for income tax purposes
- Premiums paid under an RAC are deductible for income tax purposes

The Public Service Pension Levy is an amount deducted from the remuneration of public servants. All such amounts are deducted in calculating taxable income¹⁷.

In addition to the tax reliefs outlined in Box 10.6, income and gains generated by the investments held by the schemes are exempt from tax. Benefits payable on retirement are taxable, subject to an entitlement to take a tax-free lump sum.

For individuals in funded pension schemes, the overall aggregate earnings limit on tax relieved contributions for the purposes of calculating relief is €150,000 in 2009 (reduced from €275,239 in 2008). There is also a limit on the capital value of tax relieved pension benefits that an individual can draw down. This limit, known as the standard fund threshold is €5,418,085 for 2009 (unchanged from 2008).

The main features of the tax treatment of each arrangement available for supplementary retirement savings are described below and further information on each of these products is set out in Appendix 1.

From the description of the main rules and tax reliefs available, it is clear that there are anomalies in the tax treatment of the various arrangements. These are discussed in section 8 of this Part.

3.2 Occupational pension schemes

Contributions made by employees

Contributions made by employees are deductible for income tax and PRSI¹⁸ (including health contribution levy but excluding the income levy) purposes and tax relief is applied at the individual's marginal income tax rate. The amount of employee contributions that can be tax-relieved is limited to an age-related percentage amount of the employee's remuneration as follows:

16 There is no relief from the income levy in respect of supplementary pension provision

17 Financial Emergency Measures in the Public Interest Act 2009

18 The pension contribution takes place before income is taxed or subjected to PRSI. Consequently, an employee is not liable for PRSI or tax on the contribution and the employer is not obliged to pay employer's PRSI on that element of the employee's pay. The contribution is therefore not liable to:

- Employee tax (this can be at 41%, 20% or partly at each rate depending on the employee's income level)
- 8% employee PRSI (4% PRSI and 4% health contribution levy), and
- 10.75% employer PRSI

The relief would be reduced by 8% in the case of contributions made by an employee earning below €18,304 and by 3% in the case of an employee earning above €75,036 as these employees do not pay PRSI on such income but the health contribution levy is 5%. For illustrative purposes, we adopted a rate of 8% for PRSI (which includes the health levy).

Age Limit	% of Remuneration
Under 30	15
30-39	20
40-49	25
50-54	30 ¹⁹
55-59	35
60 and over	40

Tax relievable contributions are subject to an earnings cap of €150,000 per annum, with the result that the maximum annual tax relieved employee contribution is limited to €60,000 – i.e. €150,000 x 40% for an employee aged 60 or over. A contribution not allowed in one year may be carried forward and relief is allowed in subsequent years subject to the annual limit.

Additional voluntary contributions (AVCs)

Employees may make additional voluntary contributions (AVCs) into occupational pension schemes or PRSAs. AVCs are used to improve benefits over and above those provided by the scheme, while staying within limits set by the Revenue Commissioners. They are deductible for income tax and PRSI (excluding the income levy) purposes, and are tax relieved at the marginal income tax rate. The age-related percentage limits and earnings cap outlined above in relation to occupational schemes apply to aggregate employee contributions, including AVCs.

Contributions by employers

Contributions by employers into an employee's pension fund are not²⁰ charged as a benefit-in-kind on the employee. The age-related and earnings-related limits on tax relief for employee pension contributions do not impose a restriction on the level of employer contributions. The main control²¹ on employer contributions is the statutory rule which limits the size of the tax-relieved fund to one capable of providing a pension of two-thirds of final remuneration, subject to the overall standard fund threshold limit of €5,418,085.

Employer contributions are deductible in computing the income for tax purposes of the employer's business.

Investment income and capital gains of the pension scheme

Neither income tax nor capital gains tax is payable on any increase in value of a pension fund.

3.3 Personal pension arrangements - retirement annuity contracts

Contributions

Contributions to retirement annuity contracts are premiums payable on insurance policies taken out by an individual. All contributions are paid by the individuals. As with occupational pension schemes, contributions are deductible for income tax purposes and are tax relieved at the

¹⁹ The 30% earnings limit applies, irrespective of age, to specified sportspersons.

²⁰ Section 778(5) TCA.

²¹ The manner in which this rule is applied is elaborated in guidance notes issued by the Revenue Commissioners following consultation with the Society of Actuaries in Ireland.

individual's marginal income tax rate. Tax-relieved contributions are subject to the same age-related percentage limits, annual earnings cap, rules for carry forward of unused contributions and overall standard fund threshold limits as apply to occupational pension schemes. No benefit limits apply in the case of retirement annuity contracts.

Investment income and capital gains

Neither income tax nor capital gains tax is payable on any increase in value of an RAC.

3.4 Personal retirement savings accounts (PRSAs)

A PRSA is a contract between an individual and an authorised PRSA provider. It is a defined contribution arrangement. Employees and the self-employed, homemakers, carers and the unemployed – in fact every adult under age 75 can avail of a PRSA. There is no requirement to have taxable earnings in order to pay PRSA contributions. Tax relief is available for contributions of up to €1,525 per annum even if this exceeds the normal age-related income-based limit.

Contributions

Contributions to PRSAs are deductible for income tax and PRSI purposes²² (excluding the income levy) and are tax-relieved at the marginal income tax rate. Tax-relieved contributions are subject to the same age-related percentage limits, annual earnings cap, rules for carry forward of unused contributions and overall standard fund threshold limits as apply to occupational pension schemes. No benefit limits apply in the case of PRSAs.

Employers may also contribute but, in contrast with the position for occupational pension schemes, these contributions are treated as benefits-in-kind. They are also included within the age-related percentage limits and within the overall €150,000 earnings cap, for the purposes of tax relief. However, the employee is entitled to relief on the employer contribution as if it were a personal contribution. If combined employer and employee contributions exceed the limits, an unrelieved benefit-in-kind charge applies to the excess.

Investment income and capital gains of a PRSA

Neither income tax nor capital gains tax is payable on any increase in value of a PRSA.

Section 4: **Criteria to encourage long-term savings to meet the needs of retirement**

4.1 Context

This Section sets out the main issues that we took into account in considering the support given to retirement savings through the tax system, and how best the system can encourage long-term savings for retirement.

4.2 Principles

We established criteria against which any measure to incentivise long-term savings for retirement could be measured. These are set out in Box 10.7.

²² But contributions are not deductible for PRSI purposes (see Section 8) in the case of PRSAs taken out by the self-employed.

Box 10.7: Criteria for incentives to encourage long-term savings for retirement

Measures to incentivise savings for retirement should:

- Target the 'gap in coverage', i.e. those with low- to middle-incomes who are unlikely to have supplementary pension coverage
- Improve coverage for women and those with intermittent employment patterns
- Give relief in a way that concentrates the benefits on those with low- to middle-incomes
- Be sufficiently attractive to encourage such earners to participate
- Be fiscally sustainable for the Exchequer
- Not impose an excessive cost on participants
- Not impose an unreasonable administrative burden on employers, contributors or the State
- Avoid complexity, and be as simple and transparent as possible
- Not adversely impact on existing occupational pension arrangements

4.3 Equity in support given through the tax system to retirement saving

The tax system²³ gives the greatest level of support to pension provision by those with the highest levels of income, while those most in need get the least support. This is because in general:

- Those who can most afford to provide for retirement are given the highest level of support through the income tax system (€41 for each €100 saved)
- Those on modest incomes who pay income tax at the 20% rate get a lower level of support (€20 for each €100 saved)
- Those on low incomes who are not within the tax system get no support

It is not consistent with our guiding principle of equity that the tax relief for contributions by individuals to fund their pensions is given at differing rates and gives least support to those with the lowest income. We make recommendations later in this Part to equalise the tax relief for all contributions. However, it is important to be clear that in addressing this issue, we are only dealing with a limited aspect of equity i.e. considering how tax relief can be given in a fairer way in respect of contributions made by individuals.

Clearly, contributions are also made by employers and these also have an Exchequer cost. In the case of funded schemes, contributions have a tax cost in that the individual is not taxed on the contributions made by the employer to the pension fund. In the case of non-funded schemes (i.e. the employer does not contribute to a fund, but pays the pension out of its income during the employee's retirement), which are mainly in the public sector, there is no contribution and therefore no tax cost while the employee accrues the entitlement to the pension, but the employer incurs a liability to make a pension payment in the future.

In all cases, the individual receives a pension which has an explicit or implicit tax cost to the Exchequer. Therefore, in addressing the inequitable treatment of employee contributions, we are only dealing with one aspect of the Exchequer cost of pensions. We address the issue of employer funding to a certain extent through recommendations for a reduction in the standard fund threshold limit and prevention of manipulation of contributions or remuneration levels close to retirement.

However, we believe that the regime for non-funded pensions should be examined to identify the

²³ This is apart from PRSI relief.

implicit tax cost to the Exchequer in the context of an equitable distribution of the tax expenditure on pensions.

Recommendation 10.1

The regime for non-funded pensions should be examined to identify the implicit tax cost to the Exchequer in the context of an equitable distribution of the tax expenditure on pensions.

4.4 Tax deferral

Where a pension fund is drawn down in retirement, it is subject to tax. On this basis, some submissions to us argued that tax relief in respect of pension contributions is not in fact 'tax relief', but is 'tax deferral'. The tax treatment of pension provision is as follows:

- Contributions to approved occupational pension funds, PRSAs and RACs are tax deductible. In effect the income used to make the contribution is **exempt**
- Income and gains arising to the fund are **exempt**
- Draw downs from the fund are **taxable** (subject to a once-off tax free lump sum)

This treatment of exempt/exempt/taxable (or EET) is the norm in the EU.

Apart from the tax-free lump sum aspect, the argument regarding 'tax deferral' is as follows: income put into a fund to finance retirement provision is exempt from tax, as is any capital growth. In the absence of special rules, those amounts would be liable to tax. But when this money is drawn down in the form of a pension, it is income which is subject to tax. In this sense, pension provision can be regarded as tax deferral.

This is, of course, subject to some qualifications:

- The lump sum is tax free
- In many cases, the pension contributions are relieved at the higher rate of tax while the pension draw-down is taxed at a lower rate²⁴
- Where the pension is below the income exemption limits, no tax is payable
- There is a significant delay between the granting of tax relief and taxation of the drawdown
- Where the person is entitled to use an approved retirement fund (ARF) (see section 8.5 of this Part), any amount remaining in the fund (after any deemed distributions) is not taxable until the death of the individual, and then can be transferred to an ARF of the deceased's spouse without tax on the transfer
- Overall tax levels may increase or decrease over time

Should a recommendation to equalise State support for retirement provision by taxpayers liable to tax at different rates be adopted, the extent to which tax is deferred may change. Those on lower incomes may generally be granted tax relief at a rate greater than that which will apply to their pension. However, a proportion of high earners may find that a pension, based on 50% pre-retirement income, may be taxable at a higher rate than the rate of support applied to their funding contribution.

4.5 Improving provision for retirement – compel or encourage?

²⁴ In the case of a person who makes very high retirement provision, there is likely to be a closer match between the rate of tax relief and the rate of tax on draw down.

There are a number of approaches that can be taken to pension reform. Reforms can be based on a voluntary system, a mandatory system or a soft-mandatory system, as set out in Box 10.8.

Box 10.8: Approaches to pension reform

- A **voluntary system** involves encouraging long-term savings for retirement by way of tax incentives or direct contributions by the State to a pension arrangement
- A **mandatory system** requires a person to make contributions to a pension fund either through a social insurance system or mandatory private savings. It could be said that Ireland already has a mandatory occupational pension system, namely the contributory State pension funded through PRSI. One approach to pension reform would be to consider changes to that system. Another approach would be to allow the PRSI scheme to operate in parallel with a supplementary scheme which is itself mandatory
- A **soft-mandatory approach** to pension reform involves the mandatory introduction of a pension scheme by an employer and automatic enrolment of employees in the scheme, but with an option given to an employee to opt-out of the scheme after a period (this is the 'soft' aspect)

Our terms of reference in relation to retirement savings are that we should consider how best the tax system can *encourage* long-term savings for retirement. The question of whether pension provision should be mandatory is essentially a pension matter. On this basis, we focussed on how the tax system could encourage long-term savings in accordance with our terms of reference. Changes to the tax system may not on their own be capable of addressing the gaps in pension coverage and adequacy.

4.6 Mandatory approach: Pensions Board proposal

In its report entitled *Special Savings for Retirement (2006)*, the Pensions Board suggested a 'hybrid' model involving retaining the State pension and having a mandatory supplementary pension system. The proposal applies to all those at work who are not making supplementary provision and envisages increasing the State pension to 40% of gross average industrial earnings (GAIE) and having a mandatory supplementary system with the features set out in Box 10.9.

Box 10.9: Features of Pensions Board hybrid model

Eligibility	All employees and self-employed
Eligible income	All earned income between 125% and 500% of the increased State pension (between approximately €15,000 and €60,000 as at June 2006)
Benefit type	Defined contribution
Contribution rate	15% of eligible income
Exchequer contribution	5% (included in the 15% above). This would be in lieu of any employer and employee PRSI relief and of any employee tax relief on contributions ²⁵

25 The pension contribution is deducted before income is taxed. Therefore, an employee is not liable to PRSI or tax on the contribution and the employer is not obliged to pay PRSI on the contribution element of the employee's pay. Therefore the contribution element is not liable to 41% tax, 8% employee PRSI and 10.75% employer PRSI.

We consider that, because the proposed scheme is mandatory, it is not within our terms of reference and we do not examine it further. We believe that the approach is one that should be investigated as part of the Pensions Green Paper process. The proposal has some interesting characteristics and these are taken into account later in this Part.

4.7 International pension reform

Reforming pension systems is one of the biggest challenges facing most countries. Much has been done since the early 1990s across the OECD in an attempt to ensure the long-term viability of pension systems. There have been reforms in the UK which, like Ireland, has a long history of private pension coverage. In broad terms, the pension reform in other countries can be categorised as set out in Box 10.10.

Box 10.10: Pension reform in other countries

Mandatory private pensions as a substitute for part of public provision	South America, Eastern Europe, Central Asia and Sweden
Mandatory private pensions in addition to public pensions	Australia, Hong Kong, Italy, Norway and South Africa
Soft mandatory pensions in addition to public pensions	New Zealand
Cuts in public pension to leave a greater role for the private sector	Germany and Japan

Annex 13 sets out how some of the above countries have reformed their pension systems in response to the specific challenges they faced. These challenges included amending State provision to ensure long-term sustainability in the face of demographic change and encouraging long-term savings for retirement, by using mandatory or soft-mandatory systems.

4.8 The role of the tax system

The tax system already offers incentives to encourage retirement provision, by allowing contributions to occupational pension schemes, PRSAs and RACs to be deducted in calculating taxable income. While these incentives are widely used, there remains a gap in retirement savings coverage, particularly in the case of those with low to middle incomes.

An analysis of the 2004/2005 Household Budget Survey data shows that while middle to high-income individuals and households invest in private pensions, this is not the case to the same extent for low-income earners. Evidence from the UK suggests that although low- to middle-income individuals save, “they are not strongly influenced by the availability of tax relief”²⁶. The reason for this is that the benefits of tax relief are not as great for low-earners, who do not pay as much tax as high-earners. In addition to this, individuals with incomes below the taxable limits do not have any tax incentive to invest in pensions.

Whether an incentive can be introduced in the tax system that will encourage those who have not responded to existing tax incentives to begin to save for retirement is unclear. The Indecon Review of Potential Options to Encourage Increased Pension Coverage, which was prepared

26 Understanding Small Savers: Whyley and Kempson 2000.

in the context of the National Pensions Review, refers to the lack of evidence to suggest that tax incentives increase the overall level of savings. It cites the difficulties with understanding the benefits of pension arrangements, particularly in the case of those with low income. Factors contributing to this include:

- Tax incentives are complex and can be difficult to understand
- Low- to middle-income groups (who are traditionally low savers) pay lower rates of tax and so gain less from reduced tax liabilities
- The amount that people want to save is determined by a range of factors not linked to tax relief or rates of return, such as income and affordability

On the other hand, the ESRI Report *Pension Policy: New Evidence on Key Issues*²⁷, poses the question as to why participation is so low among low earners. It points to research which suggests that poor families will save if presented with financial incentives to do so.

This suggests that an explanation for low participation may be that tax incentives for retirement are less effective in low-income households. Tax deferral means little to people whose tax rate is low or zero. Where income is too low to allow for any savings, it is unlikely that they would respond to any incentive to start saving for retirement. In such a case the tax system will not provide a solution. Instead, retirement provision will need to be addressed through other support mechanisms.

In some cases, it may be that inertia rather than affordability is the reason for a person not having started to save for retirement and a soft-mandatory approach may be appropriate. This is developed in Section 5.

Tax incentives are offered in many countries to encourage retirement provision. The OECD Economic Survey of Ireland (2008, p.90) highlights international experience which suggests that tax incentives are likely to be more effective at raising savings if they are targeted at low- and middle-income earners, and if they are designed so that the incentives are easy to understand. It also points out experience in Australia, Canada and the United States which shows that households respond well to incentives presented as matching contributions from the government for each amount paid into retirement savings accounts. From this, it concludes that the high take up of special savings incentive accounts (SSIAs) by households in Ireland indicates they might respond to a system of matching contributions. But it goes on to say that it is unlikely that the same take up rate could be achieved for retirement accounts as for SSIAs, because pension funds must be committed for much longer periods.

We examine a number of approaches that might help to encourage more long-term saving for retirement and propose a combination of tax measures that, taken together, may contribute to addressing the issue. The focus of any new reliefs should be on those who are not currently saving for their retirement and on those who are not saving enough. Care is needed so as not to discourage those with existing savings for retirement from continuing to save. If any change were to encourage people to move from dedicated savings for retirement, which are inaccessible until retirement, to general savings which can be accessed at any time, the risk is that such savings would be drawn down before retirement. This could result in a fall in adequacy of retirement savings.

27 T. Callan, C. Keane, J.R. Walsh (2009) *Pension Policy: New Evidence on Key Issues*, Dublin: The Economic and Social Research Institute. Page 6.

Existing pension arrangements have been successful in attracting significant amounts of retirement savings. This success can be built on by the removal of anomalies in current tax treatment. Having a more consistent tax treatment of such arrangements should make the decision on which product to use a simpler one for taxpayers. Industry and regulators also have an important role to play in making pension and retirement products simple and understandable, and in actively marketing them.

Under the tax heading, there are two possible approaches:

- The first is for the Exchequer to grant tax relief for contributions along the lines of the current system. However, modifications to the system could encourage those most in need of retirement savings to save. This may involve giving increased tax relief to those on lower income levels. Such an approach should help low-paid workers, subject to them being in a position to avail of the relief. It would not help those outside the tax net. It may be possible to meet some or all of the extra costs involved by lowering the level of support for retirement savings given to those on higher levels of income
- The second is for the Exchequer to make a direct contribution to supplement what a person puts into retirement savings. This could involve putting in place a system to replace the existing tax relief system with respect to future pension contributions, or it could be something that supplements the existing tax relief system. This would help those outside of the tax net as well as low-paid employees - again subject to them being in a position to avail of the scheme

Section 5: Review of options for tax relief

5.1 Introduction

This Section sets out the options for reform that we examined. We looked at how equity might be improved and retirement savings encouraged while still providing an incentive for those liable to tax at the higher rate of income tax. The options we examined are:

- Relief for all at the higher rate
- A 'stepped' approach
- Relief for all at the higher rate for a short period only to kick-start retirement savings
- A matching Exchequer contribution combined with a kick-start approach

While the first three options have merit, we do not recommend them. We are recommending the option of a matching Exchequer contribution of €1 for each €1.60 contributed by the taxpayer. This would improve equity in that the same level of State support would apply to all and should encourage retirement savings by those on lower income levels. This, combined with a kick-start approach, is our recommended option. We asked the Department of Finance to cost these options – details of the Department's costings are in Appendix 2.

5.2 Option 1: Tax Relief for all retirement provision at the higher rate

5.2.1 Overview

This is the proposal in the Green Paper on Pensions (and originally proposed as one alternative in the National Pensions Review 2005) that all contributions towards supplementary retirement provision should qualify for tax relief at the higher rate. Under current rules, such contributions are deducted in calculating an individual's taxable income. The effect of this is that individuals liable to tax at the higher rate benefit most as income, which would otherwise be taxed at the higher rate, is sheltered from tax by the contribution. In the same way, individuals who are liable to tax at the standard rate get a smaller tax benefit²⁸. Individuals who are not liable to tax get no benefit under the tax system. This system of giving relief is regressive.

The Green Paper proposal is that, in the case of all forms of supplementary pension provision (other than PRSAs²⁹), tax relief for all personal contributions should be given at the higher rate.

The proposal refers to personal supplementary pension contributions. It does not cover contributions made by an employer on behalf of an employee.

The proposal seeks to incentivise individuals with low- to middle-income to start a pension³⁰. Many of these will not be liable to income tax at the higher rate but will either be paying tax at the standard rate or not be liable to tax at all. The proposal should act as an incentive to such individuals to make provision for their retirement. However, the reality remains that, in many cases, people may take the view that their current financial commitments make it impossible for them to save for retirement.

This option would not adversely affect those on higher levels of income who have been getting relief at the higher rate of tax because they would continue to get relief at that rate. It would improve equity between different categories of taxpayers by equalising the rate of tax on employee contributions between high and low levels of income.

5.2.2 Employer contributions

No change is envisaged to the existing treatment of employer contributions. Such contributions are not subject to tax on an employee as a benefit-in-kind. Consequently, there is a tax saving to the employee at his or her marginal rate. This would retain a degree of inequity between those taxable at the higher rate and others.

5.2.3 Limit existing tax reliefs to secure savings

The National Pensions Review recommendation for relief at the higher tax rate includes support for "a cap on incomes for pension contribution and benefit purposes but only if the derived savings are used to improve incentives for lower rate taxpayers and non-taxpayers". The details of the type

28 As the level of a person's income rises, some of their income will be exposed to the higher tax rate. Pension contributions would shelter income taxable at the highest rate of tax. In some cases, some income may be sheltered at the higher rate and some at the standard rate. Thus the effective rate of relief will be either the standard or higher rate or a combination of these rates.

29 For PRSAs the Green Paper proposes a matching contribution.

30 There is no official definition of what constitutes low to middle incomes. For our purposes, we have used as a base figure the amount of €34,000 which is broadly representative of average earnings. This is based on the figure of €32,730 for industrial earnings for 2007 contained in the CSO Earnings and Labour Costs (Table 9, page 15) publication. If we assume earnings growth of 3% for 2008 (based on the trend in the first three quarters of 2008), this gives an estimated industrial earnings figure for 2008 of €33,720 which, when rounded to the nearest €1,000, gives €34,000. Using the €34,000 guideline, it would be reasonable to assume that low income for an individual could be income up to, say, two-thirds of average earnings (i.e. €22,667), middle income could be up to, say, twice average earnings (€68,000) and high income could be income above that level.

or level of any cap are not specified. The annual earnings cap was reduced in Finance (No. 2) Act 2008 to €150,000. The Exchequer tax savings from that reduction in the cap could go some way to meet the cost of extending relief at the higher rate to all taxpayers.

Applying a cap to, or reducing the existing cap on, employee contributions, as a way to recoup some of the costs of this option might not be effective, as it could give rise to a change in behaviour by those affected.

There is a cap on employee contributions³¹, but there is no cap on the benefit-in-kind exemption for employer contributions to occupational pension schemes³². For PRSAs, the cap applies to both employer and employee contributions. If the cap on employee contributions was reduced, high-rate taxpayers might be able to avoid the measure by arranging for a reduced salary with lower employee contributions and higher employer contributions into the occupational pension scheme³³. If this happened, the cost of extending relief at the higher rate would be borne by the Exchequer.

One way of addressing this would be to introduce a cap on the exemption from the benefit-in-kind charge on employer contributions. This would make the provisions very complex for a number of reasons:

- Payments into a defined benefit pension scheme are made on a fund (rather than on a member) basis. Consequently, determining how much of any payment related to any particular member would be difficult to ascertain
- Even if it were possible to overcome this difficulty, it could give rise to problems in the case of employers who are required to make additional contributions to defined benefit pension funds that are under-funded. Unless specific exemption was to be introduced for such additional contributions, employees would pay tax on them as a benefit-in-kind

5.2.4 Soft-mandatory approach

An auto-enrolment approach could be considered under this option. This is a soft-mandatory approach to pension reform that involves the mandatory introduction of a pension scheme by an employer and automatic enrolment of employees in the scheme, but with an option given to an employee to opt-out of the scheme after a period (this is the 'soft' aspect).

5.2.5 Cost of providing tax relief at the higher rate

We asked the Department of Finance to cost this option. The Department's costings are outlined in Box 10.11.

31 Age related relevant earnings
 <30 15%
 Up to 40 - 20%
 Up to 50 - 25%
 Up to 55 - 30%
 Up to 60 - 35%
 >60 40%

Subject to an annual earnings cap of €150,000.

32 Subject to an overall control that a pension fund cannot exceed an amount sufficient to fund a pension of two thirds of final remuneration or €5,418,085 (the standard fund threshold), whichever is the lower.

33 Section 118B of the Taxes Consolidation Act 1997 ensures that salary sacrifice arrangements are subject to PAYE and PRSI. Tax Briefing Issue 70 specifies, as an example of such an arrangement, attempts to circumvent the limits imposed on personal contributions to pension schemes by foregoing salary and transferring the contributions from the hands of the employee to the employer.

Box 10.11: Cost of tax relief for all retirement provision at the higher rate

Additional cost for those already within the tax system and contributing to a supplementary pension (this is the 'deadweight' cost)	€91m
Additional cost if higher rate attracted more into supplementary pension schemes	€75m
Total	€166m
Additional cost if auto-enrolment were to apply ³⁴	€590m
Total	€756m

5.2.6 Advantages and disadvantages – relief for all retirement provision at the higher rate

The advantages of this option are that it equalises State support, encourages increased coverage in target groups without adversely impacting on existing contributors and builds on existing (and familiar) tax relief structures. It also meets the objective of maintaining employer involvement which is considered an important component in encouraging pension coverage. However, the disadvantages include overall cost (particularly if a soft-mandatory approach is adopted), possible deadweight cost and a lack of appeal to individuals outside the tax system. It might also cause employers to reduce their pension contributions for employees taxable at the standard rate, since employee contributions at the higher rate would be more tax efficient.

5.2.7 Conclusion

We see considerable merit in the option whereby relief for all retirement contributions would be granted at the higher rate. It could act as a strong incentive to those on lower levels of income, who have not been providing for their retirement to begin to do so. In addition, it would not disincentivise those on higher levels of income, who have been getting relief at the higher rate of tax, because they would continue to get relief at that rate. It would also improve equity as between the different categories of taxpayers.

However, we have concerns about the costs of this approach, particularly the costs of auto-enrolment. There are also deadweight costs associated with it. We took the view that this is likely to be the most costly of the options we considered.

On balance, we do not recommend this approach because of the potential cost of auto-enrolment.

5.3 Option 2: Stepped Approach

5.3.1 Overview

This section sets out another approach that could incentivise people to save for retirement. The approach is designed to maximise the incentive to save for retirement among those on low to middle incomes, who might otherwise get no tax relief, or only get relief at the standard rate. It does so by giving them tax relief at the higher rate of income tax.

It involves dividing retirement provision in any year into tranches. For the first tranche of contributions, tax relief would be given at the higher rate. For the next tranche of contributions, relief would be

34 This is the excess of the additional cost of auto-enrolment (€665m) over the cost of those attracted to save for retirement in the absence of auto-enrolment (€75m).

given at the standard rate. Above a level where it is considered that an incentive may not be justified, no tax relief would be given.

Those with higher incomes who currently receive relief for retirement provision at the higher rate would get less relief once the amount of their pension contribution exceeds the first tranche.

Unless new rules on employer contributions are implemented, a degree of unequal treatment would result. This is because those taxable at the higher rate would be in the best position to take advantage of the benefit-in-kind exemption.

5.3.2 Advantages and disadvantages — stepped approach

The advantages of this approach are that it equalises the State support, it should increase coverage in the target group and it reduces deadweight costs. The disadvantages are that it adversely impacts on some existing contributors and it would not be possible to apply it in conjunction with a kick-start approach.

5.3.3 Conclusion

The stepped approach could not be used in the same way as the kick-start option (described below) to encourage individuals to start providing for their retirement. This is because the stepped approach ensures relief at the higher rate will be available for the first tranche of retirement provision in each year and could not be restricted to the early years of saving. We have a concern that taxpayers would not invest in pension arrangements to the extent that tax relief is available at the standard rate.

Consequently, we do not recommend the introduction of a stepped approach.

5.4 Option 3: Tax relief for all retirement provision at the higher rate for a kick-start period

5.4.1 Overview

This is a modified version of Option 1 and would allow relief at the higher rate for a limited period of, say, five years. The relief at the higher rate would only be available for retirement savings by the individual in the limited period beginning with the first year in which such retirement savings are made. We considered it because:

- It should impose a smaller Exchequer cost than Option 1
- It has the potential to incentivise individuals to begin the savings habit (particularly if it could be restricted to individuals under a certain age)

Relief would be given at the higher rate for all pension contributions in the limited period. After this period, relief for retirement savings would be given at the taxpayer's marginal rate. That could be the higher rate of income tax or the standard rate, depending on the income and circumstances of the taxpayer. In the case of a taxpayer who is not subject to the higher rate of income tax, a sudden drop in relief at the end of that period could pose problems. This could be addressed by gradually stepping down the rate of relief over a further period of, say, two to three years.

This option should act as an incentive to individuals to commence providing for retirement. Giving tax relief at the higher rate for a limited period would be a significant contribution by the State towards getting taxpayers on low to middle-incomes to begin saving for retirement. Contributions

made early in a person's working life have a longer period to grow before retirement and so can give much greater value than those made later.

5.4.2 Costs

Even though this option is time bound, there would still be a significant cost to the Exchequer. However, the deadweight costs associated with Option 1 would be reduced as the additional tax relief would only apply to those who had been contributing to pensions for less than five years. The Department of Finance was unable to cost this option as there was no relevant data on which to estimate its cost.

5.4.3 Advantages and disadvantages — kick-start period

The advantages and disadvantages of this option are similar to those for Option 1. However, a significant disadvantage is that the equality of support ceases at the end of the five-year period.

5.4.4 Conclusion

We see merit in a kick-start period whereby relief for retirement contributions would be granted at the higher rate for a defined period. The option is focused on those who have not yet commenced saving for retirement and the time constraints should serve as an incentive to begin doing so. Limiting the relief to a specific period of time would also reduce the Exchequer cost of the proposal. However, the fact that the equal treatment of taxpayers would cease at the end of that period is unsatisfactory.

We do not recommend this approach in the context of relief at the higher rate. However, we recognise that a kick-start is likely to have a strong incentive effect and it is further considered in conjunction with the matching Exchequer contribution approach outlined in Option 4 below.

5.5 Option 4 — A matching Exchequer contribution

5.5.1 Overview

Under this option, contributions towards supplementary retirement provision would qualify for a matching Exchequer contribution of €1 for each €1.60 contributed by the taxpayer. The Exchequer contribution would be limited to the current age-related and earnings limits.

The impact of this approach is that individuals liable to tax at the higher rate would receive less Exchequer support than they do under current rules, while those liable at the standard rate would get greater support.

The matching contribution approach is a viable alternative to the options considered above, because it has the potential to incentivise those on lower levels of income, while still providing those on higher levels of income with reasonably generous support.

A matching Exchequer contribution of €1 for each €1.60 contributed by the taxpayer would incentivise individuals who are either paying tax at the standard rate or who are not liable to tax to make provision for their retirement. However, the reality remains that, in many cases, individuals in this situation may decide that, because of their other financial commitments, they cannot afford to provide for retirement.

Those with higher levels of income who, under current rules, receive relief at the higher rate for retirement provision would get less Exchequer support under this option. This could be a disincentive to save for retirement by way of pension arrangements.

5.5.2 The figures

Box 10.12 illustrates the current level of effective total Exchequer contribution made to taxpayers liable to tax at the standard and marginal rates.

Box 10.12: Current Exchequer contribution where pension contributions made

Example	Higher rate taxpayer	Standard rate taxpayer
Contribution made to a pension scheme by an employee	100	100
Employee gets -		
• tax relief of:	41	20
• relief from PRSI and the health contribution ³⁵	8	8
Employer gets PRSI relief of:	10.75	10.75
Exchequer contribution (in the form of reliefs given) is:	59.75	38.75
Savings by employee	49(41+8)	28 (20+8)
Savings by employer ³⁶	10.75	10.75
Amount in pension fund	100	100
Net cost to employee	51	72

Higher rate taxpayer

- In the case of a higher rate taxpayer, for every €100 contributed to a pension fund, the Exchequer will incur a cost of €59.75. This Exchequer cost is shared between the employee (€49) and the employer (€10.75). Thus from the point of view of the employee, for each €100 that goes into the fund, the State contributes €49, in the form of the reliefs given to the taxpayer. This is the equivalent of the State contributing €49 for every (net) €51 contributed by the taxpayer, or almost €1 for each €1 contributed by the taxpayer.

Standard rate taxpayer

- In the case of a standard rate taxpayer, for every €100 contributed to a pension fund, the Exchequer will incur a cost of €38.75. This Exchequer cost is shared between the employee (€28) and the employer (€10.75). Thus from the point of view of the employee, for each €100 that goes into the fund, the State contributes €28 in the form of the reliefs given to the taxpayer. This is the equivalent of the State contributing €28 for every (net) €72 contributed by the taxpayer, or roughly €1 for each €2.50 contributed by the taxpayer.

5.5.3 A matching contribution

We propose that, instead of the State contributing €1 for each €1 contributed by a high rate taxpayer and €1 for each €2.50 contributed by the standard rate taxpayer, it would make a matching contribution of €1 for each €1.60 contributed by the taxpayer in all cases. If this approach were to be adopted, the same level of State support would apply to all contributions.

³⁵ PRSI relief does not arise in all cases due to the employee PRSI ceiling of €75,036 – see footnote 28.

³⁶ If a matching Exchequer contribution applies, there will not be any employer PRSI relief

It would be difficult to give such support through the tax system under the net pay arrangement. We propose that it be given at source. Tax relief is given at source for mortgage interest and for medical insurance and it works well. It is operated by the service provider and is transparent. The Revenue Commissioners consider it feasible to give support in this way in the case of retirement provision but indicate that it would require a significant lead-in period to adapt to the new approach. It would mean that a person wishing to contribute €100 to his or her pension scheme would pay €62 to the pension scheme and the pension scheme would collect the €38 Exchequer contribution from the Revenue Commissioners.

5.5.4 Impact of moving to a matching Exchequer contribution

Box 10.13 shows the position of a higher rate taxpayer and a standard rate taxpayer under current arrangements and under the proposed arrangements.

Box 10.13: Comparison of current and proposed arrangements

	Current arrangements		
	High rate taxpayer	Standard rate taxpayer	Matching contribution
Contribution/amount in fund	100	100	100
Relief			
– Tax	41	20	
– PRSI, health contribution, levy	8	8	
Tax relief at source	–	–	38
Net contribution	51	72	62

5.5.5 Employer PRSI relief

A consequence of giving support by a matching contribution is that employer PRSI relief would cease to exist. That relief only arises because of the 'net pay arrangements' through which relief of pension contributions is effected. Where an employee makes contributions to a pension scheme the employer's PRSI is calculated on the remuneration net of employee pension contributions. If the employee makes a pension contribution, the employer makes a PRSI saving. If the employee makes no pension contribution, the employer makes no saving. It is arguable whether such a windfall gain should be available to an employer. Because there is no salary cap for employers' PRSI, the savings to the employer can be substantial. According to the Department of Finance, the Exchequer cost of employer PRSI relief for 2007 is estimated to be close to €185 million.

5.5.6 Impact on occupational pension schemes

In the case of occupational pension schemes, this option would standardise the Exchequer support of employee contributions. This would equalise the treatment of taxpayers and go some way towards helping to meet the Exchequer cost of providing the incentive for those on low and middle incomes.

Some inequity would remain unless corresponding changes were made to relief for employer contributions (through the benefit-in-kind exemption arrangements), because those taxed at the higher rate would benefit most from the benefit-in-kind exemption.

In addition, there could be behavioural changes in relation to new employment contracts, i.e. these could provide for less employee contributions and greater employer contributions. This is not a new issue. It is there already due to the reduction to €150,000 of the earnings related cap.

5.5.7 Impact on PRSAs and RACs

In the case of PRSAs and RACs, our proposal is that they also should get a matching Exchequer contribution rather than a deduction for tax purposes. On the basis of the above, the appropriate matching contribution would be €1 for each €1.60 contributed by the taxpayer.

The impact of the handling of an employer's contribution to a PRSA must also be considered. As is currently the case, the employer's contribution would be taxed as a benefit-in-kind at the employee's marginal rate - either the higher or standard rate depending on the employee's circumstances. The employer's contribution is effectively then an after-tax contribution by the employee and could qualify for the matching contribution.

5.5.8 Impact on those who are not liable to tax

Those who are not liable to tax because of the level of their income do not benefit from tax relief under current rules. In our view, the matching Exchequer contribution should apply to an individual who has relevant earnings, even where, because of the level of their earnings, they are not liable to tax. The matching contribution approach would not give Exchequer support to persons outside of the tax net because they have no income³⁷.

5.5.9 Exchequer costs related to this proposal

We asked the Department of Finance to cost this option. The Department's costings are set out in Box 10.14.

Box 10.14: Exchequer costs of giving relief for pension contributions at a matching contribution rate of €1 for each €1.60

Savings in respect of those already within the tax system and contributing to a supplementary pension	(€120m)
Additional cost if matching contribution attracted 10% more into supplementary pension schemes	€60m
Net savings	(€60m)
Additional cost if auto-enrolment were to apply ³⁸	€460m
Net overall cost	€400m

³⁷ This could arise in the case of individuals who stay at home for family reasons and have no income but are fully supported by, say, a spouse with a high income. On the one hand, it can be argued that such a person should be entitled to benefit. On the other, the underlying objective is to try to get people to provide for an income in retirement that is 50% of their pre-retirement income. As the person in this scenario had no pre-retirement income, an issue does not arise. The Retirement Savings Scheme in Section 6 addresses this issue.

³⁸ This is the excess of the additional cost of auto-enrolment (€520m) over the cost of those attracted to save for retirement in the absence of auto-enrolment (€60m).

5.5.10 Advantages and disadvantages – matching Exchequer contribution

The advantages of this option are that it equalises State support for retirement provision and makes it more transparent, it encourages increased coverage in the target group and it can combine effectively with a kick-start approach. A disadvantage is that it could disincentivise some existing contributors.

5.5.11 Kick-start period in conjunction with the matching contribution

The kick-start period, which was outlined in section 5.4 above, could be considered in conjunction with the matching contribution approach. This would involve:

- A matching Exchequer contribution of €1 for each €1.60 contributed by the taxpayer in respect of all retirement provision
- For the kick-start period, a matching Exchequer contribution of €1 for each €1 contributed by the taxpayer in the first, say, five years of pension provision

This would mean that a higher State contribution would be available for retirement savings in the five-year period beginning with the first year in which such retirement savings are made. After that period, the matching contribution would return to €1 for each €1.60 contributed by the taxpayer. This approach would give an incentive to all to begin providing for their retirement and encourage them to maximise provision in the first five years. This should help to embed the savings habit. The kick-start approach would be even more of an incentive to begin saving early if it could be restricted so that it only applied where the retirement savings commenced before, say, age 30³⁹. The compatibility of this with equality law would need to be examined.

We conclude that this matching Exchequer contribution option would improve equity and incentivise those with low- to middle-incomes to begin providing for their retirement. In addition, it could be combined in an effective way with a kick-start period in a manner that is equitable but also provides a strong incentive to begin retirement provision as early as possible.

Recommendation 10.2

The current tax relief for personal retirement provision should in the medium to long-term be replaced by a matching Exchequer contribution of €1 for each €1.60 contributed by the taxpayer.

Recommendation 10.3

The matching contribution approach should be accompanied by a kick-start provision involving a contribution of €1 for each €1 contributed by the taxpayer in the first, say, five years of pension provision by an individual.

Recommendation 10.4

The matching contribution should apply where an individual has relevant earnings including where, because of the level of his or her earnings, the individual is not liable to tax.

5.6 Soft-mandatory approach

An issue separate to the above options is the extent to which retirement provision could be made

39 This could apply by allowing the person concerned to apply to Revenue to commence the kick-start period at any time before age 30. This would ensure that the period would not be used up earlier when a young person, for example, may travel abroad after taking up employment.

mandatory. It would be possible to apply a soft-mandatory, or auto-enrolment, approach to any of the arrangements mentioned above. Under existing rules, employers are obliged to offer a PRSA to their employees where no employer-sponsored occupational scheme is in place. We understand that there has been a relatively small take-up by employees of this option.

Changing to a soft-mandatory approach would mean that employers would not only be compelled to offer the PRSA facility, but they would have to automatically enrol the employee in the scheme. The 'soft' aspect is that an employee would be entitled to opt out of the scheme later. The soft-mandatory approach has the advantage of using inertia in a positive way. In other words, instead of inertia having the effect of delaying a decision to start providing for retirement, the person concerned would be enrolled automatically in the system, and would have to make a decision and take action to opt out of the system. If adopted, it should have a positive impact on the number of individuals beginning the savings habit. In our view, this has the potential to increase pension coverage significantly.

There are a number of issues that would have to be considered in the case of a soft-mandatory approach. These include when an individual would be entitled to opt out of a scheme and the timing and extent of any refund of contributions made by an individual who opts out. These, however, are design features and not for consideration here.

In the event that a soft-mandatory approach was adopted, decisions would be required on a number of issues which have not been given further consideration here, including:

- Reducing the complexity of pensions so that they are more understandable and transparent
- The level of contribution that would apply on auto-enrolment
- Whether the employee only would be required to make the contribution, or whether the employer should also be obliged to contribute
- Whether an employer would be free to nominate the provider of the savings arrangement, or whether the employee would be given a choice, with a default option. If the employer were to be required to give a choice to employees, this would imply a considerable administrative burden. On the other hand, requiring an employee to take part in a scheme chosen by the employer might not be satisfactory
- Arrangements for re-enrolment at an appropriate time where an individual opts out

If a soft-mandatory approach were to be adopted, there may be a case for considering whether it would be possible to confine such an approach to individuals over say 25, subject to compatibility with equality laws. This would avoid putting an unnecessary administrative burden on employers in the case of younger employees, such as students engaging in holiday and part-time work. In addition, were a kick-start to apply, a young person in this position would then be able to avail of any kick-start option when they enter the workforce more permanently.

The question of introducing a soft-mandatory approach may be outside our terms of reference. Nevertheless, we are of the view that a soft-mandatory approach could make a significant contribution to increasing coverage and is something that should be considered.

Recommendation 10.5

A soft-mandatory approach could make a significant contribution to increasing pension coverage and should be considered.

5.7 Visibility of Exchequer contribution

Whichever of the above options is adopted, we consider that an employee's payslip should be required to show the amount contributed by the Exchequer to the employee's retirement savings. The 'net pay arrangement' which now applies is not fully transparent. A greater visibility of the State support for retirement savings is likely to increase awareness and act as an incentive to save.

Recommendation 10.6

An employee's payslip should show the amounts contributed by the Exchequer to the employee's retirement savings.

Section 6:

A retirement savings scheme

6.1 Introduction

This section examines the various components of a retirement savings scheme. This is effectively a special savings incentive account (SSIA) scheme, which involves a person opening an account to accumulate funds for use in retirement. It is envisaged that such accounts would be simple and straightforward. The approach is designed to address the issues raised in the CSO findings outlined in section 2.10 and in some submissions made to us. It would also address the objective in the Programme for Government to provide an SSIA-type scheme in an effort to make supplementary pension provision more attractive to those on low incomes. The approach is proposed to run in addition to the options considered in Section 5.

6.2 The SSIA scheme

A total of 1,170,208 SSIA accounts were commenced by individuals prior to the closing date of 30 April 2002. Approximately 1,085,000 SSIA accounts matured by the end of the scheme. 26.5% of persons who opened an SSIA did not already have a pension. The CSO Quarterly National Household Survey module on SSIA accounts gives the profile of all individuals over 21 who held such accounts. The data is set out in Box 10.15.

Box 10.15: Profile of individuals who held SSIA accounts

Broad occupational group	Population in these occupational groups ('000)	No of Accounts ⁴⁰	Percentage of occupational group with an SSIA account
Managers and administrators	310.3	178.0	57.4
Professional	223.6	162.8	72.8
Associate professional and technical	165.5	104.3	63.0
Clerical and secretarial	233.4	131.4	56.3
Craft and related	256.1	88.0	34.4
Personal and protective service	190.7	63.0	33.0
Sales	146.1	51.3	35.1
Plant and machine operatives	166.6	52.2	31.3
Other	178.0	41.7	23.4
Totals	1870.3	872.8	46.7

The survey also indicated that in the fourth quarter of 2005 the average monthly contribution to SSIA accounts stood at €217.04.

6.3 Cost of the SSIA scheme

The SSIA scheme ended in May 2007 and the full payout to SSIA account holders was in the region of €14.6 billion. This payout included original investment and Exchequer top-up. The cost to the Exchequer of the SSIA scheme, net of exit tax, from 2001 to 2006, was as follows:

Year	Cost €m
2001	71
2002	433
2003	532
2004	548
2005	597
2006	439
Total	2,620

40 Note the total number of accounts here is lower than the total number of SSIA's as the profile was limited to persons over 21 years of age.

6.4 The proposed retirement savings scheme

A scheme similar to the SSIA could have a role to play in complementing other retirement provision arrangements. Some of the target group may not be covered by these other arrangements:

- Some may not be in a position to take out a PRSA, and
- Some may be reluctant to take out a PRSA because of the perceived lack of transparency and complexity of existing pension arrangements

The scheme would not be a traditional pension product but a long-term savings product. The key attractions of such a scheme are as follows:

- It would be easily understood
- The Exchequer contribution would be transparent
- It should specifically incentivise those who are not liable to tax
- It would be attractive to those who may not be working or who feel that they cannot realistically avail of the other pension products
- Investment choices would be straightforward, and
- Because of the nature of the scheme, it should require regulation of a different order to a pension product and this should be less costly

It is not expected that there would be the same level of uptake of a scheme that has a much longer time horizon than the SSIA because of the general inaccessibility of funds until retirement age. Nonetheless, we are of the view that it would be an attractive facility that should be available in parallel with traditional retirement savings products. It should encourage the savings habit from an early age and it would enable those with broken employment patterns, those who are carers, those who take career breaks and those with low to middle incomes, who may not be able to benefit from traditional pension products, to get support from the State for their long term savings for retirement. There is likely to be a deadweight cost in the proposal in that it would cover some savings that would happen in the absence of an incentive.

6.5 Operation of the scheme

The various components that would make up a retirement savings scheme are set out in Box 10.16.

Box 10.16: Components of a retirement savings scheme

- The scheme would be open to all persons over 18 years of age and up to the age of retirement⁴¹ who are tax resident in Ireland for the year in which the contribution is made⁴²
- Its characteristics would make it less attractive to those who could avail of more conventional supports, which would limit access to the scheme
- A **matching Exchequer contribution** would apply. Based on the analysis in Section 5.5.2 we consider that an Exchequer contribution of €1 for each €2 contributed by the taxpayer would be appropriate. This would give less support than is given under the existing rules to a higher rate taxpayer for pension provision, but more support than is given to a standard rate taxpayer. It would give less than is proposed under the matching contribution option in section 5.5.3
- **Exclusions.**⁴³ We take the view that the matching Exchequer contribution should not normally apply for any year in which the person concerned is in an employment which is covered by a defined benefit pension scheme
- The scheme would have a **minimum savings level** to encourage continued investment. This could be set as low as €120 per annum to facilitate continued participation in the scheme by very low income groups and those with intermittent work patterns. This is considered important to maintain the saving habit
- **The scheme would have a maximum savings level.** We believe it was important as far as possible to discourage people currently contributing to more traditional pension schemes, from taking up this long term saving option. A limit on the amount that could be saved annually could be set by reference to a percentage of average industrial earnings. If the upper limit were, say, €3,300 per annum, a matching contribution of €1 for every €2 saved would mean that the taxpayer would be permitted to save €2,200 (two-thirds of that amount) and the State would make a one-third contribution (€1,100)
- **Employer involvement.** Employers should be involved in providing access to the retirement savings scheme and offering a salary deduction facility
- **Administration costs.** Because of the simplicity of the scheme and based on the experience of the SSIA scheme, administration costs are unlikely to be significant.
- **A range of investment options to be available.** Persons opening such accounts should be given a range of options with explanations that clearly show the consequences in terms of the level of risk for each option, such as putting money on deposit, investing in shares, funds and unit trusts. A default option would apply in the event of no election being made. The National Treasury Management Agency could have a role in the operation of the scheme.

41 The lack of consistency regarding retirement age issue is discussed in section 8.6.

42 If a person reaches retirement age and does not draw down the funds, they should be entitled to continue to benefit from the scheme until they reach a certain age – the appropriate age is not a decision for us. However, once the funds are drawn down, they should cease to be entitled to any further use of the scheme.

43 There are certain cases where defined benefit arrangements could be inferior to a defined contribution arrangement and these would need to be addressed.

- **Pre-retirement access to funds.** We believe that there should be some form of pre-retirement access⁴⁴ in the case of, for example, the purchase of a house as a principal private residence or serious illness. All matching Exchequer contributions related to the amount drawn down would be repayable in the event of such access. The potential for exceptional access to funds may increase the attractiveness of the scheme.
- **Returns on the savings, apart from the Exchequer contribution, would be taxable.** No tax would arise on the amount saved or on the State contribution. However, any other growth in the funds would be taxed. This could be done as follows:
 - Tax at the standard rate could be applied to the growth in funds each year as they arise. However, taxing as-you-go in this way would be complex other than in the case of simple deposit accounts, or
 - Instead of taxing as-you-go, a slightly higher tax rate could be applied to the growth on maturity or draw-down of the funds.
 - No further tax liability would arise on draw-down of the funds.

6.6 Exchequer costs

The Department of Finance has estimated that, if there was a 20% take-up of the scheme and a maximum contribution by all who took part, the Exchequer cost would be about €520 million per annum.

6.7 Benefit to the individual

If €2,200 were contributed each year by an individual and the Exchequer contribution was €1,100, then after 40 years, the total contributions made would be €132,000 in today's terms (ignoring any return earned). This is broadly equivalent to 10 years of the State pension – or, in annuity terms, it could increase income by €6,000 per annum for life, equivalent to 50% of the State pension (assuming an annuity rate of 5%).

6.8 Conclusion

A retirement savings scheme along the lines of the former SSIA scheme has attributes that could encourage long-term savings for retirement. The public familiarity with the SSIA scheme would make it attractive – even though the delay before funds can be accessed is much greater (for most people) than was the case with the SSIA's, and it would not be possible to have a general cut-off date for the opening of an account.

The scheme has the potential to increase retirement provision, particularly in the case of those with low to middle incomes and those with broken employment patterns. However, we also believe the scheme should be open to all (other than those in an employment which is covered by a defined benefit scheme), as limiting its availability would result in considerable administrative complexity. The scheme could be focussed on the target group by limiting it to a relatively low annual amount – this could be pitched at an appropriate percentage of average industrial earnings. The possibility of some pre-retirement access to funds should make the scheme attractive to younger people.

44 The main disadvantage of allowing pre-retirement access is that it would defeat the object of the scheme which is to accumulate funds for retirement. The main advantage is that a person may be more willing to commit to an account if they feel that in given circumstances they may have some access before retirement even if it involves partial repayment of the Exchequer contribution.

Another advantage of the scheme is that there would be no taxation of the amounts contributed by the saver or the Exchequer (as distinct from the growth in the funds) on withdrawal at retirement.

The scheme would not be sufficient on its own to meet the retirement savings needs but could make a valuable contribution, in parallel with other Exchequer supports, towards retirement provision.

Recommendation 10.7

A retirement savings scheme along the lines of the former SSIA scheme, that is easily understood and which involves an Exchequer contribution, should be introduced – the scheme is outlined in Box 10.16 of Part 10.

Section 7: Summary of our overall recommendations

7.1 Introduction

This section sets out a possible overall approach designed to incentivise:

- More people to save for retirement (i.e. increased coverage)
- People to save more for retirement (i.e. improved adequacy), particularly those at the lower income levels

7.2 Rebalancing of tax incentives for retirement provisions

Our recommendations have the potential to redistribute the tax expenditures on pension provision towards those on lower and middle incomes. This is consistent with our guiding principle of equity ensuring a more equitable incidence of taxation on all in society. It also accords with our principles that our proposals should be viable and flexible and our tax system should be one which is responsive to, and capable of changing in time with, our economic environment and economic profile.

We believe that the tax system cannot be viewed as a panacea to address the gaps in retirement provision. There are other areas of public policy where this issue will have to be addressed in a comprehensive way. However, we have looked at how the tax system can best encourage long term savings for retirement with a focus on those on low- to middle-incomes, who may not be in a position to benefit as much as others from tax relief on traditional pension arrangements. Our view is that there is not an obvious single answer under the tax heading. However, we believe that the following approach should contribute to an overall policy solution.

The approach contains three elements:

- **Retirement savings scheme:** The first element concerns a new savings account, structured on the lines of the SSIA, which would run in parallel with the other elements below. It would be widely available to facilitate further retirement provision. This would particularly facilitate those with atypical employment patterns and those not in employment and would enable them to continue saving for retirement. It would also encourage younger people to start saving earlier. The scheme would operate as outlined in Section 6.

- **Tax relief for personal pension provisions**
 - **Matching Exchequer contribution:** Given that the option of relief at the higher rate for all retirement provision is likely to have an unsustainable cost, the second element is that a matching Exchequer contribution would be given in respect of all personal contributions to pension arrangements at a rate of €1 for each €1.60 contributed by the taxpayer. This should incentivise those on lower incomes to provide for their retirement by giving them a higher level of support for pension contributions than they get under existing rules. Those who currently get relief at the higher rate would get less support. This would improve the equity of the system.
 - **High rate kick-start:** The third element is the high rate kick-start option outlined in Section 5. This would give additional support to all taxpayers in respect of contributions to pension arrangements for the first five years in which they make contributions. After that, they would revert to the normal support. This approach should provide a strong incentive to begin making provision for retirement.

Section 8: Other issues related to the tax treatment of retirement provision

8.1 Introduction

In this Section we consider a number of anomalies and issues in relation to the tax treatment of pensions.

8.2 The standard fund threshold

There are a number of limits on the tax relief for pension provision. One of these is the annual earnings limit, currently set at €150,000, on which tax relief for contributions can be based. Another is the limit on the capital value of the amount of tax relieved pension benefits that an individual can draw down. This limit, known as the standard fund threshold, is currently set at €5,418,085.

A limit on the overall size of an individual's tax relieved pension fund is appropriate and we are of the view that the standard fund threshold should remain. This is because pension contributions made by employers and benefits accrued in unfunded schemes are not subject to the annual earnings limit. If the standard fund threshold were to be removed, this would allow the annual contribution limit to be avoided by those who can switch from employee to employer pension contributions.

The standard fund threshold was introduced in 2005 and set at €5m. By 2008 it was €5,418,086. The annual earnings limit applying across all pension products was introduced with effect from December 2002 and set at €254,000. By 2008 it had been indexed to €275,239. For 2009 this limit was reduced to €150,000. We take the view that there should be a correlation between the annual earnings limit and the standard fund threshold and that any movement in the annual earnings limit should be accompanied by a corresponding movement in the level of the standard fund threshold.

Any change to the standard fund threshold would require transitional arrangements to cover, for example, those who may have already exceeded the revised threshold.

Recommendation 10.8

- As the annual earnings limit does not apply to employer contributions, there is a need to retain the standard fund threshold.
- There should be a correlation between the annual earnings limit and the standard fund threshold, and the reduction in the annual earnings limit suggests that there should be a corresponding reduction in the standard fund threshold.

8.3 Taxation of the lump sum

On retirement, an individual is entitled to take a part of his or her pension fund as a tax-free lump sum. Although the tax-free status of this lump sum is an arrangement of long standing, it is not possible to identify an objective rationale for it. The payment facilitates the transition from full pay to pension. Its tax-free status may provide an incentive to individuals to save for their retirement. On the other hand, the payment of a lump sum to some extent defeats the purpose of retirement savings, which is to provide income in retirement.

In general, we take the view that available Exchequer resources would be better used to enhance the incentives for those at entry level to retirement provision and believe that there is a case for subjecting the lump sum to some level of tax.

We accept that the prospect of some tax-free exemption of the lump sum is an additional incentive to make retirement savings. However, the level of exemption should be less than currently applies. The arrangements should be changed so that the lump sum, which is limited to 25% of the fund or 1.5 times final salary, is taxed as follows:

- A maximum €200,000 should be tax free
- The balance should be subject to tax at the standard rate of income tax

Examples:			
Final salary	€50,000	€100,000	€150,000
Maximum lump sum	€75,000	€150,000	€225,000
Tax free	€75,000	€150,000	€200,000
Taxable @ standard rate	-	-	€25,000
Tax @ 20%			€5,000

Recommendation 10.9

A lump sum taken on retirement should be liable to tax as follows:

- An amount of up to €200,000 should be tax free.
- The balance of the lump sum should be subject to tax at the standard rate of income tax.

8.4 Excessive contributions close to retirement

There are a number of controls in tax law relating to occupational pension arrangements:

- The earnings limit on an individual's tax relieved contributions is €150,000
- A limit on the tax-relieved pension fund that can be created by contributions to a fund capable of providing a pension of two-thirds of final remuneration, subject to the overall standard fund threshold limit of €5,418,085, and
- The age-related percentage limit on relievable contributions

Many individuals – employees, self-employed and proprietary directors – do not fund their pension arrangements at a sufficiently early stage of their working lives. They can therefore find themselves with inadequate pension funding and a short time-frame to address the issue. As we note below, the age-related limits on allowable pension contributions implicitly recognise that individuals may need, for *bona fide* reasons, to increase their level of contribution as they approach retirement. It is important that these individuals continue to make these contributions as otherwise their pensions would not be adequate. While limits and controls allow this to happen, they are, in some cases, used in an unintended way. This occurs where individuals can influence the amount of contributions (or the question of who pays them), as well as the final salary level. For example, large amounts may be contributed to a pension scheme by the employer in the years before retirement. This arrangement would include agreeing very high levels of remuneration in the final years, in order to maximise both the amount of pension that can be paid and the tax-free lump sum.

We take the view that a system which allows such arrangements is not appropriate and we recommend that the law should be changed to prevent their use.

Recommendation 10.10

The current tax relief rules should be reviewed to ensure that contributions and remuneration levels cannot be manipulated close to retirement to allow individuals to take advantage of unintended and inappropriate benefits.

8.5 Age-related limits

We considered whether age-related limits should be abolished so that young people would have the same opportunity as older people in terms of the proportion of their earnings that could be invested in retirement savings.

Under current tax law, there are age-related limits on the amount of retirement provision that can be made by an individual. These range from 15% of the remuneration of a person who is under 30 years of age to 40% of remuneration in the case of someone who is aged 60 or over. It can be argued that a younger person should be able to make the same level of tax relieved contribution as an older person. Certainly, having a single limit would simplify the system. However, abolishing the age-related limits would have disadvantages.

If all individuals were allowed to make tax-relieved contributions of up to 40% of their remuneration irrespective of age, individuals aged under 30 should not need that level of contribution to provide adequately for their retirement. This would not be an appropriate use of Exchequer funds. On the

other hand, if all individuals were only allowed to make tax-relieved contributions of up to 15% of their remuneration irrespective of age, a person aged over 55 would not be able to adequately provide for their retirement on that level of contribution given increases in longevity over the past few decades. The age-related limits reflect the level of investment likely to be required at each stage in life to provide for retirement. Unless there are higher levels of investment, older people who were late beginning retirement provision would be likely to have inadequate savings.

Age-related limits on the amount of an individual's relevant earnings should therefore remain.

Recommendation 10.11

Age-related limits on the amount of an individual's relevant earnings should continue.

8.6 Approved retirement funds (ARFs) and approved minimum retirement funds (AMRFs)

On retirement, the funds accumulated in a PRSA or an RAC may be used to purchase an annuity, or may be transferred to an ARF net of a tax-free lump sum⁴⁵. If the option to transfer the funds to an ARF is chosen then, unless the person concerned has an income of at least €12,700 per annum for life, €63,500⁴⁶ of the funds must be used to purchase an annuity or invested in an AMRF until age 75. An AMRF is similar to an ARF but has the effect of locking away capital until the individual concerned reaches 75 years of age. Income can be withdrawn from an AMRF but the original capital cannot. ARFs and AMRFs pay no tax on investment income or gains.

Withdrawals from an ARF are subject to income tax. When an individual dies, transfers or withdrawals of the funds in an ARF are regarded for tax purposes as being taxable income of the individual in the year of death. However, this does not apply when the funds in the ARF are transferred:

- To an ARF in the name of the spouse of the deceased in which case no tax is payable
- To a child, who is 21 or under, of the deceased (but a capital acquisitions tax liability may arise), or
- To a child who is over 21, when the transfer is taxed at the standard rate of income tax as a final liability.

There is an imputed 3% distribution on the market value of ARF assets on 31 December each year, where distributions of at least that amount were not otherwise drawn down from the ARF. This rule applies where the ARF owner is 60 years of age or over for the whole of the tax year, and where an ARF is set up after 6 April 2000. It does not apply to AMRFs.

Availability of ARFs in relation to retirement products

ARFs are currently available in relation to PRSAs and RACs. Except in the case of proprietary directors and holders of AVCs, they are not available in relation to occupational pension schemes. Submissions have suggested that ARFs should be available as an alternative to annuities to members of defined contribution occupational pension schemes. The submissions do not, however, call for them to be made available in the case of defined benefit schemes. If ARFs were to be made available in the case of defined benefit occupational schemes this could put pressure on the solvency of such schemes and could damage defined benefit pension provision – there is already evidence of considerable funding issues in relation to such schemes.

⁴⁵ In the case of a PRSA, the funds can be left in the PRSA.

⁴⁶ or, if lower, the amount of funds in the PRSA or RAC after taking the tax-free lump sum.

The flexibility of an ARF should be extended to defined contribution occupational pension schemes. We based this recommendation on the view that if it is appropriate to allow an ARF to be available in relation to a PRSA and RAC, and to proprietary directors in relation to their pension funds, members of the defined contribution occupational pensions should be allowed to benefit in a similar way.

Recommendation 10.12

The flexibility of an ARF should be extended to defined contribution occupational pension schemes.

8.7 Other anomalies

A number of anomalies in the tax rules relating to private pension arrangements came to our attention. The tax rules on pension provision are complex. The differences in the tax treatment of various arrangements⁴⁷ available can make the decision as to which product is most suitable unnecessarily difficult – there are simply too many variables to be considered. Some of the differences are warranted because of the nature of the products and the person for whom they are intended. However, in some cases, it is difficult to see the rationale for the differences in treatment.

Employer contributions

If an employer pays contributions to an individual's PRSA, the employer must report it to the Revenue Commissioners as a benefit-in-kind. The employee can claim immediate tax relief on these contributions, as if he or she had paid the contributions directly. In practice, a benefit-in-kind tax charge will only arise where the total contributions paid in any one year exceed the appropriate percentage (calculated by reference to the age of the contributor) of the annual earnings limit.

In contrast, employer contributions to occupational pension schemes are not taxed as a benefit-in-kind and are not subject to the €150,000 annual income limit.

Age limits for draw-down

The rules regarding retirement age vary depending upon whether a person contributes to an occupational pension scheme, a PRSA or RAC. Each occupational pension scheme, PRSA or RAC requires approval from the Revenue Commissioners in order to avail of the special tax treatment. To be approved, conditions must be met. As regards retirement age, the conditions are as follows:

- An occupational pension scheme must provide for retirement at a specified age, which in general is not earlier than 60 and not later than 70
- A PRSA or RAC must provide for withdrawals to begin not earlier than age 60 and not later than age 75

While there are operational differences between PRSAs, RACs and occupational pension schemes, the different retirement age ranges that apply should be reviewed with the objective of having more consistency. The upper retirement age in the case of occupational pension schemes should be 75, as is the case for a PRSA or an RAC.

In addition, the various ages specified in the legislation governing the time at which benefits must begin to be taken date back to 1972, and may warrant being reviewed and conformed in the

47 Occupational pension scheme, PRSA and RAC.

light of the increases in life expectancy since then.

Level of lump sum

Different rules apply to the amount of a tax-free lump sum that can be drawn down. In the case of occupational pension schemes, an employee is entitled on retirement to a maximum lump sum of 1.5 times final salary, irrespective of whether it is a defined benefit or a defined contribution scheme. For PRSAs and RACs, the limit on the lump sum is 25% of the amount in the fund on retirement. All schemes are subject to the overall lifetime cap on lump sums of 25% of the standard fund threshold.

While some of the issues identified are not tax issues, they are conditions that affect the availability of the tax benefits. The anomalies identified in the rules relating to retirement provision arrangements contribute to the view that the system is overly complex. Where anomalies make the choice of retirement savings product difficult, the decision to begin saving may be deferred.

Recommendation 10.13

Anomalies in the treatment of different retirement arrangements should be eliminated as far as possible.

Recommendation 10.14

The various ages specified in the legislation governing the time at which benefits may commence should be reviewed and conformed.

Appendix 1

Tax Reliefs to encourage supplementary pension provision

Irish measures to support saving for retirement (Pillar two)

	Occupational pension schemes (both DB and DC)	Personal retirement savings accounts (PRSAs) ⁴⁸	Retirement annuity contracts (RACs) ⁴⁹
Tax treatment of contributions			
Legislative reference	Sections 770 – 782 TCA	Sections 787A – 787L TCA	Sections 783 – 787 TCA
Open to	Employees only	All	Self-employed and individuals in non-pensionable employment
Employee contribution	Deductible at taxpayer's marginal rate (i.e. 20% or 41% depending on the level of the taxpayer's income)		
Employer contribution	No benefit-in-kind ⁵⁰	Taxed as benefit-in-kind ⁵¹	No employer ⁵² contribution
Tax relievability contribution limits allowed as a percentage of earnings ⁵³		Age	Relevant earnings
		< 30	15%
		Up to 40	20%
		Up to 50	25%
		Up to 55	30% ⁵⁴
		Up to 60	35%
		>60	40%
Annual earnings limit	€150,000	€150,000	€150,000
Funding limit	2/3rds of final remuneration ⁵⁵	None	None
Fund limit	€5,418,085	€5,418,085	€5,418,085

48 Long term savings account to assist in saving for retirement. Products jointly approved by Revenue and Pensions Board.

49 A standard contract approved by Revenue which may then be marketed; primarily to the self-employed.

50 Section 772 (3)(a) TCA. The main control on the overall level of employer contribution is the statutory rule which limits the tax relieved pension fund that can be created by contributions to a fund capable of providing a pension that does not exceed two-thirds of final remuneration or a fund agreed to the standard fund threshold, whichever is lower.

51 Introduced with the PRSA legislation in 2002 but the employee is entitled to tax relief on the contribution as if it has been paid directly by himself or herself.

52 All contributions are paid by the individuals themselves.

53 In the case of occupational pension schemes these limits apply to employee contributions only. However, for PRSAs the limits apply to the aggregate of both the employee and employer contributions

54 30% earnings limit applies, irrespective of age, to specified sportspersons

55 Subject to being reduced to 50% of final remuneration where tax-free lump sum taken.

	Occupational pension schemes (both DB and DC)	Personal retirement savings accounts (PRSAs)	Retirement annuity contracts (RACs)
Tax treatment of draw-down			
Access before retirement	None		
Age at which benefits must be drawn down	Normal retirement age 60 to 70	Normal retirement age 60 to 75	
Tax-free lump sum ⁵⁶	1.5 times final salary	25% of the fund	
Requirement to purchase annuity	In some cases	Optional: Approved Retirement fund ⁵⁷ (ARF) / Approved Minimum Retirement fund ⁵⁸ (AMRF)	
Approved retirement funds/Approved minimum retirement funds			
Ability to avail of ARF/AMRF	AVCs and proprietary directors	Yes	Yes
Management of funds	Must be managed by qualifying fund manager		
Tax treatment of funds	Income and gains are exempt in the fund. Withdrawals (known as distributions) are taxed at the individual's marginal rate and are subject to PAYE ⁵⁹ Imputed distribution ⁶⁰ : An ARF is deemed to make a notional annual distribution where sufficient actual distributions are not made.		
Tax treatment of funds on death	The amount payable to the deceased individual's estate is treated as income of the deceased for the year of assessment in which he or she dies. There are some exceptions: <ul style="list-style-type: none"> • A transfer to an ARF in the name of the deceased's spouse is exempt • A transfer to a child of the individual under 21 is exempt, but chargeable to capital acquisitions tax • A transfer to a child of the individual over 21 is taxed at the standard rate of income tax 		

56 Tax-free lump sum subject to lifetime limit of 25% of the standard fund threshold.

57 An ARF is a fund which pays no tax on its investment income or capital gains while the money is invested in it. However, if the money is withdrawn, it is subject to income tax at the individual's marginal rate.

58 An AMRF is similar to an ARF but has the effect of locking away capital until the individual reaches 75. Income can be withdrawn from an AMRF but the original capital cannot. The balance left after drawing down tax-free lump sum, or €63,000 if less has to be transferred to AMRF or used to purchase an annuity. However, an AMRF is not required if the individual is over 75, or has a pension or annuity of at least €12,700 for life.

59 But use of funds to purchase an annuity would not be taxable

60 Section 14 of Finance Act 2006 introduced a tax charge based on an "imputed distribution". The amount of the imputed distribution is 1% of the value of the assets in 2007, 2% of the value of the assets in 2008 and 3% for 2009 and subsequent years where the individual is aged 60 or over for the complete tax year.

Appendix 2

Department of Finance Costings

A: Relief for all individual pension contributions at the higher rate of income tax:

(i)	Additional Exchequer cost for those already within the tax system and contributing to a supplementary pension:	
1.	Employee contributions to Occupational Pension Schemes	
		€m
	Current cost ($€1.552\text{bn}^{61} \times 80\%^{62} \times 49\%^{63}$) + ($€1.552\text{bn} \times 20\% \times 28\%^{64}$) =	695
	Proposed cost ($€1.552\text{bn} \times 100\% \times 49\%$) =	<u>760</u>
	Extra cost:	65
2.	Individual contributions to RACs	
	Current cost: ($€1.084\text{bn}^{65} \times 90.5\%^{66} \times 41\%^{67}$) + ($€1.084\text{bn} \times 9.5\% \times 20\%^{67}$) =	423
	Proposed cost: ($€1.084\text{bn} \times 100\% \times 41\%$) =	<u>444</u>
	Extra cost:	21
3.	Contributions to PRSAs	
	Current cost: ($€200\text{m}^{68} \times 88.8\%^{69} \times 49\%$) + ($€200\text{m} \times 11.2\% \times 28\%$) =	93
	Proposed cost: ($€1.084\text{bn} \times 100\% \times 41\%$) =	<u>98</u>
	Extra cost:	5
	Total current cost =	1211
	Total proposed cost =	<u>1302</u>
	Total extra cost:	91 (say 90)

61 Employee pension contributions to Occupational Pension Schemes (OPS) for 2007 – per Revenue Commissioners P35 employer returns.

62 No breakdown of relief is available on contributions to OPS as between standard and higher rate taxpayers; relief at higher rate assumed for 80% of contributors but there is no scientific basis for this. If it was assumed that 70% of contributions were relieved at the higher rate and 30% at the standard rate, the extra cost of higher rate relief for all existing OPS members would be increased by about €30m and by a further €30m for each 10% "switch" in the assumption of the breakdown between higher and standard rate taxpayers contributing to OPS.

63 Made up of tax relief at higher rate of 41%, employee PRSI relief at 4% and health levy relief at 4%. Most employees pay PRSI at the "A" rate which also varies depending on an individual's level of income. In addition, employee PRSI does not apply to incomes above €75,036 per annum. A breakdown is not available of the PRSI contribution status of existing members of and contributors to pension schemes (or of the likely status of new members/contributors). A rate of 4% across the board has been used for the purpose of this exercise.

64 Made up of tax relief at standard rate of 20%, employee PRSI relief at 4% and health levy relief at 4%.

65 Latest RAC contribution figures from the Revenue Commissioners in respect of 2007.

66 Proportion of tax relief claimed at higher rate by contributors to RACs in respect of 2005 (latest year for which a breakdown is available); taken from info in PQ20745/08 as the proportion which the reduction in tax of higher rate taxpayers bears to the total tax reduction for RACs.

67 Contributions to RACs are almost exclusively made by self-employed individuals. PRSI and health levy relief is not available on pension premiums/contributions made by self-employed individuals operating outside of PAYE. Existing relief is confined to income tax relief. No breakdown available of contributors to PRSAs as between self-employed and PAYE taxpayers; so no adjustment made to PRSA costing.

68 Latest PRSA contribution figures from the Revenue Commissioners in respect of 2007.

69 Proportion of tax relief claimed at higher tax rate by contributors to PRSAs in respect of 2005 (latest year for which a breakdown is available) taken from info in PQ20745/08 as the proportion which the reduction in tax of higher rate taxpayers bears to the total tax reduction for PRSAs.

(ii)	Additional Exchequer cost if higher rate relief attracted more investment into supplementary pensions⁷⁰:
	Numbers in employment; 1.965m ⁷¹ X workforce not covered by pensions; 48% ⁷² X Additional take-up; 10% ⁷³ X pension contribution; €1,675 ⁷⁴ X 49% = <u>77</u> (say 75)
(iii)	Additional Exchequer cost if auto-enrolment were to apply⁷⁵
	Numbers in employment; 1.965m X workforce not covered by pensions; 48% X numbers in employment aged over 25 and under 65 years; 86% ⁷⁶ X pension contribution; €1,675 X 49% = <u>666</u> (say 665)

B: Replace tax and PRSI etc. relief for all individual pension contributions with a matching Exchequer contribution of €1 for every €1.60 of employee/personal contribution⁷⁷:

(iv)	Savings in respect of those already within the tax system and contributing to a supplementary pension:
1.	Employee contributions to Occupational Pension Schemes
	€m
	Current cost (€1.552bn X 80% X 49%) + (€1.552bn X 20% X 28% tax rate) = 695
	Proposed cost (€1.552bn X 100% X 38.46% ¹⁷) = <u>597</u>
	Saving: 98
2.	Individual contributions to RACs
	Current cost: (€1.084bn x 90.5% x 41%) + (€1.084bn x 9.5% x 20%) = 423
	Proposed cost: (€1.084bn x 100% x 38.46%) = <u>417</u>
	Saving: 6
3.	Contributions to PRSAs
	Current cost: (€200m x 88.8% x 49%) + (€200m x 11.2% x 28%) = 93
	Proposed cost: (€200m x 100% x 38.46%) = <u>77</u>
	Saving: 16
	Total current cost = 1211
	Total proposed cost = <u>1091</u>
	Total savings: 120

70 As the higher rate relief remains a voluntary incentive under this option, the costing provided can only be illustrative based on assumptions on take-up. In addition, while it would take time for any incentive to take effect, the estimated cost ignores this timing effect.

71 CSO labour market data for Q1 2009.

72 Pension coverage for workers aged between 20 and 69 has varied between 52% and 55% between Q1 2002 and Q1 2008, according to CSO QNHS data. This would leave the non-coverage percentages ranging from 48% to 45%. The higher (48%) figure has been used in this exercise.

73 Take-up assumed at 10% of workforce without pension cover. Cost would increase if higher % take-up assumed.

74 Assumptions required about average income level and contribution level of contributors; income level assumed at average industrial wage - €33,500 p.a. (latest estimate of average industrial earnings for 2008) and contribution level assumed at 5%. Pension contribution and estimated costs would be higher if it were decided that the contribution level should be higher and/or that the average income of the contributor would be higher.

75 There would be behavioural and timing impacts, among other impacts, arising from the introduction of auto-enrolment. These impacts are not reflected in these costings.

76 CSO labour market data for Q1 2009.

77 Tax and PRSI etc. relief at a rate of 38.46% on pre-tax pension contributions is equivalent to providing a direct Exchequer contribution of €1 for every €1.60 of post-tax pension contribution.

(v)	Additional Exchequer cost if higher rate relief attracted more investment into supplementary pensions:
	Numbers in employment; 1.965m X workforce not covered by pensions; 48% X Additional take-up; 10% X pension contribution; €1,675 X 38.46% = <u>61</u> (say 60)
(vi)	Additional Exchequer cost if auto-enrolment were to apply
	Numbers in employment; 1.965m X workforce not covered by pensions; 48% X numbers in employment aged over 25 and under 65 years; 86% X pension contribution; €1,675 X 38.46% = <u>522</u> (say 520)

C Auto-enrolment PRSA

Auto-enrolment has been included in the cost scenarios for higher rate relief and matching contribution set out above. In response to the specific issues and questions raised in the e-mail of 28 November 2008, the following is the position in relation to the assumptions made in providing the costings involved.

Employee opt-out and re-enrolment: No provision made for opt-out and re-enrolment.

Employees covered by scheme: Percentages of those at work aged between 25 and 64 and who have no pension coverage.

Level of employee contribution; contribution rate of 5% of earnings assumed.

Employee and Employer contribution: compulsory employee contribution only assumed. No employer contribution.

Refunds of contributions for opt-outs: no provision made.

D. Retirement Savings Scheme

Eligibility:	Anyone aged between 18 years and 64 years Tax resident in State for year in which contribution is made
Exclude:	All those who are covered by a Defined Benefit pension scheme in the year concerned
Employee Contribution:	Minimum saving level €120 Maximum saving level 10% Average earnings x 2/3 ⁷⁸
Exchequer contribution:	50% of employee contribution i.e. €1 for €2
Investment Type:	Range of options available
Access to Funds:	Limited pre-retirement access to funds

The scheme provides for State contributions to a retirement savings scheme in the form of a direct pay over by the Revenue Commissioners into an individual's savings account of an amount equal to 50% of the amount contributed by the taxpayer, subject to min/max contribution level by the individual

78 Maximum annual saving permitted under the scheme calculated at 10% (possibly too high at this level of income) of annual average industrial wage where employee contributes 2/3rds and the State 1/3rd.

Calculating maximum allowable contribution:

Average Industrial Wage = €33,000⁷⁹

€33,000 × 10% = €3,300 where employee can contribute 2/3 and State 1/3

=> MAX total savings level = €3,300

=> MIN total savings level = €180 (€120 employee + €60 State contribution)

Numbers eligible for scheme:

Population of the State aged between 18 and 64 = 2.9m⁸⁰

Total membership of Occupational Pensions = 797,370⁸¹

DB:DC = 2:1⁸² Defined Benefit number = 532,000 (531,580)

Number of people eligible to partake in the scheme 2.9m - 532,000

= 2,368,000

Estimation of Exchequer Cost based on the above figure (2,368,000):

5% Take Up = 118,400		Employee Contribution	Cost
Max Contribution	118,400 × €3,300 = €390,720,000	€260m	€130m
Min Contribution	118,400 × €180 = €21,312,000	€14m	€7m

10% Take Up = 236,800		Employee Contribution	Cost
Max Contribution	236,800 × €3,300 = €781,440,000	€521m	€260m
Min Contribution	236,800 × €180 = €42,624,000	€28m	€14m

20% Take Up = 473,600		Employee Contribution	Cost
Max Contribution	473,600 × €3,300 = €1,562,880,000	€1.04b	€521m
Min Contribution	473,600 × €180 = €85,248,000	€57	€28

79 Average industrial wage at Q2 2008; €33,423

80 Estimate based on CSO population figures released in August 2008.

81 Pensions Board Annual Report 2006.

82 Green Paper on Pensions (p.134) – ratio of DB to DC includes public sector schemes.

30% Take Up = 710,400		Employee Contribution	Cost
Max Contribution	$710,400 \times \text{€}3,300 = \text{€}2,344,320,000$	€1.56b	€783m
Min Contribution	$710,400 \times \text{€}180 = \text{€}127,872,000$	€86	€42m

47% ⁸³ Take Up = 1,112,960		Employee Contribution	Cost
Max Contribution	$1,112,960 \times \text{€}3,300 = \text{€}3,672,768,000$	€2.5b	€1.2b
Min Contribution	$1,112,960 \times \text{€}180 = \text{€}200,332,800$	€133m	€67m

The above costs are very tentatively estimated based on assumed savings contributions occurring in a full year. The estimates do not take account of the impact of withdrawals due to savers accessing funds or to the impact of any tax due on the accrued return on savings over the savings period

E. Abolition of employer PRSI relief in respect of employee pension contributions.

Latest figures from D/Social and Family Affairs indicate that the cost of employer PRSI relief on employee pension contributions is close to €185m (estimate for 2007).

83 CSO QNHS – Q4 2005. Almost 47% of those in employment had an SSIA. Unlikely that anything like this level of coverage would be achieved but costing included for illustrative purposes.