Autoenrollment system takes a step closer to reality

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The long-awaited legislation to implement the Government's new pension autoenrollment system sets out for the first time how the new state body overseeing the scheme will operate, including its enforcement mechanisms.

Serious questions remain as to whether the scheme will be up and running by the new target start date of January 1, 2025, which is viewed as somewhat ambitious by many in the pensions industry.

However, while autoenrollment pensions to expand private sector coverage have been talked about for decades, the current Minister for Social Protection, Heather Humphreys, has gotten closer than any of her predecessors by publishing detailed legislation.

Plenty potential pitfalls lie ahead. Apart from the practical difficulties of getting the system in place in less than nine months, there is the possibility that a growing employer backlash against rising social costs associated with employment may postpone or dilute elements of the scheme yet again.

That said, the initial costs for the first three years are relatively low, at 1.5% from both employees and employers, and the political commitment to the scheme was underlined by the new Taoiseach Simon Harris, when he mentioned it in his first speech after his election.

There will also be a €1 State contribution for every €3 saved by employees, which will constitute an ongoing cost to the Exchequer each year. This is more generous than the current pension tax relief at the standard 20% rate of income tax, but less generous than the current top rate relief at 40% (although many on the top rate are more likely than standard rate taxpayers to be paying into a pension scheme already).

OPTING OUT

The broad parameters of the scheme remain largely unchanged from those announced two years ago. Employees (not the self-employed) aged between 23 and 60, earning over €20,000 per annum, who are not already paying into a pension scheme, will be automatically enrolled and can opt out after six months – although they will be re-enrolled after two years.

This raises the prospect of employees who are determined to remain outside of the scheme, by availing of every possible opportunity to opt out, being still forced to contribute six months every 2.5 years – provided they still meet the qualifying criteria.

Those opting out can receive a refund of their own contributions, but the employer and State contributions made on their behalf, as well any investment returns earnings while they are in the scheme, will continue in their personal pension pot until they retire.

NEW STATE BODY

A new State body, the National Automatic Enrolment Retirement Savings Authority (NAERSA) will act as a central processing authority, collecting contributions from employers, employees and the State, passing those contributions to investment funds and eventually paying out pensions from each individual's pension pot (which will follow them from employer to employer). NAERSA will contract out administration and investment services through open procurement.

The existence of this as a separate scheme from the employer is being cited by the Government as one of the benefits of the new system for employers, as they are saved the cost of setting up and administering their own pension scheme – while still benefiting from Corporation Tax deductions on the employer contributions they make to the scheme.

One of the largest providers of existing occupational pension schemes, Irish Life, has argued that employers with existing schemes should be allowed to automatically enrol employees in their own scheme, to avoid having most employees in an existing company scheme and some in the new AE scheme, which applies from Day One of employment.

However, it is open to employers to open up their company schemes to employees who currently do not qualify, if they wish to avoid different pension entitlements among their employees. Also, since NAERSA administers the scheme, there would be minimal administrative burden on employers.

Irish Life also criticised the inability to make Additional Voluntary Contributions (AVCs) under the new scheme, saying it could widen the pension gender gap.

The Department of Social Protection says that this is because the scheme is initially based on payroll contributions. But once it is bedded in, it is planned to allow AVCs also.

EXEMPTIONS

An exemption from the AE scheme exists for employees already paying into a pension scheme, which can be an occupational scheme or a private pension scheme like a Pension Retirements Savings Account (PRSA) or a Retirement Annuity Contract (RAC).

Initially this applies to all such schemes, regardless of contribution level. But the Bill provides that by Year Seven of the scheme, NAERSA, in consultation with the Pensions Authority, will set standards to ensure that these other schemes are at least as favourable as the AE scheme. These standards may be reviewed from time to time.

While most existing schemes have contribution levels above 1.5% from employer and employee (as AE will have for the first three years), this may be a bigger issue in a few years, as the contributions increase to 3% from each side from Year Four onwards, and to 4.5% from Year Seven and 6% from Year 10.

Similar issues have arisen with the Statutory Sick Pay (SSP) scheme, which applies if an existing sick pay scheme is inferior to the SSP as a whole, with the WRC having been asked to rule several times on whether an existing scheme is inferior to SSP or not.

SUPERVISION

The Bill published last week sets out the detailed arrangements for the new NAERSA, which will be a state body under the Department of Social Protection, whose staff will be civil servants, with their renumeration set by civil service structures and processes.

NAERSA will review the AE system not later than five years after it comes into operation. Section 43 of the Bill provides that this review will include: the contribution rates; the earnings threshold for enrolment; the ages for enrolment and opting in; the employment status of those to be enrolled; the range of AE provider services offered by the Authority; pension draw-down options; and any other matters directed by the Minister.

The Minister will have the power to accept or reject any such recommendations, subject to the agreement of the Minister for Public Expenditure for any changes affecting State spending.

The Pensions Authority is to prepare regular supervisory reports on the AE scheme, which is to be laid before the Houses of the Oireachtas.

INVESTMENT

Each of the investment management firms selected by NAERSA to manage AE members' funds will offer three funds with different risk ratings, which run from rating 1 for the lowest risk to rating 7 for the highest risk.

AE members can choose their risk level, but if they do not, a default strategy of risk ratings 5-7 is applied for those more than 15 years to retirement (at State Pension Age – currently 66), with ratings 3-4 for those from 5-15 years to retirement and ratings 1-2 for those with less than five years to retirement.

Apart from reaching retirement, funds can be paid out on death of the member, or due to incapacity or exceptional circumstances of ill-health (with the Minister to prescribe arrangements for the latter). If NAERSA refuses early access, the applicant can seek a review of this decision.

If eligibility for withdrawal of funds has been notified, but no application or withdrawal has been made for 15 years, the provisions of the Dormant Accounts Act apply.

Communication with scheme members is to be “digital by default”. Annual statements to members are to include figures for accrued retirement savings, projections based on pensionable age, contributions in the past 12 months and costs deducted in the same period.

ENFORCEMENT

Enforcement against non-compliance with the legislation is the responsibility of NAERSA, which shall appoint officers that can enter places of work, with either the consent of the occupier or a warrant.

These officers will be able to issue compliance notices, enforceable by District Courts, and fixed payment notices for amounts up to €5,000. Information on those on whom a fine or penalty has been imposed may be published by the Authority.

Also, cases can be brought to the Workplace Relations Commission (WRC) for alleged penalisation of employees for exercising their right to participate in AE.