Commission on Public Service Pensions

Final Report

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14 November 2000

Mr Charlie McCreevy TD
Minister for Finance
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Upper Merrion Street
Dublin 2

Dear Minister

I have the honour to submit to you, on behalf of the Commission on Public Service Pensions, our Final Report which we have prepared in accordance with the terms of reference given to us.

Yours sincerely

Professor Dermot McAleese
Chairperson

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Acknowledgements

The preparation of this Report has involved a significant input from a range of people and organisations which the Commission is pleased to acknowledge.

The Commission wishes to record its gratitude to Conor McGinn of the Department of Finance who acted as Secretary of the Commission since its inception. The work of a Secretary of a Commission is very demanding. A voluminous amount of correspondence has to be dealt with, meetings have to be arranged and agendas worked out. There is an incessant stream of ongoing requirements for information and back-up research. Most demanding of all is the task of drafting and re-drafting chapters first for the Interim Report and then for this Final Report. The Final Report is a lengthy tome by any standard. Each chapter has been carefully scrutinised and re-scrutinised. Our Secretary's skill, diligence and creativity made a profound impression on all members of the Commission. In his commitment to the work of the Commission and his effectiveness in assisting us to accomplish it, he exemplified the best qualities of a public servant. We were fortunate to have him as Secretary.

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Executive Summary

1. Introduction

1.1 The Executive Summary of the Final Report of the Commission on Public Service Pensions is structured as follows:

1. Establishment of the Commission and overview of the main issues examined in the Report.
2. Analysis of the Commission's terms of reference: the present and future cost of public service pensions, claims for improvements in existing scheme benefits, changes in the working environment, conditions of employment and operational requirements of the public service.
3. Examination of existing public service pension scheme arrangements: (i) pension terms, (ii) management, administration and communication, and (iii) financing arrangements.
4. Review of occupational pension arrangements in the private sector and in the public service in other countries.
5. Proposed criteria for assessing public service pension arrangements and consideration of whether or not the public service should adopt a radically different pension structure.
6. Presentation of the Commission's analysis, conclusions and recommendations in relation to public service pension terms.
7. Presentation of the Commission's analysis, conclusions and recommendations in relation to pension scheme financing, management and communication systems.
8. Final conclusions.

The full list of Commission recommendations follows this summary.

1.2 The structure of the Executive Summary does not correspond directly with that of the Report. However, cross references to the Report are made throughout. References to Sections and Paragraphs within the Executive Summary itself are given in italics.

Background (Chapter 1)

1.3 The Commission on Public Service Pensions was established in February 1996 to examine and report on the occupational pension arrangements of public servants. The Commission made an Interim Report in August 1997; we now present our Final Report. This is the first comprehensive examination of pensions for the public service since the foundation of the State.

1.4 The formal terms of reference of the Commission were:

To examine and report on the pension terms of public servants employed in the Civil Service (non-industrial and industrial), Defence Forces, Gardaí, Education, Health and Local Authority Services, having regard to

(1) the present and future costs arising under the schemes financed by the Exchequer;

(2) claims for improvements in existing scheme benefits, including claims for voluntary early retirement;

(3) changes in the working environment and conditions of employment of public servants since the schemes were introduced; and

(4) the operational needs of the Services concerned.

Developments during the review period

1.5 Reference to the Commission was made in the two National Agreements concluded during the period of our review. *Partnership 2000* (1997) and the *Programme for Prosperity and Fairness* (2000) both stated that, insofar as the public service was concerned, no claim for the introduction of pension schemes or for improvement of existing schemes should be submitted or processed further pending the report of the Commission.

1.6 In November 1997, as part of an announcement on the payment of pension increases arising out of restructuring deals made under the *Programme for Competitiveness and Work*, the Government stated that policy in relation to any future restructuring deals would be determined in the light of the recommendations in the Commission's Final Report.

1.7 The Report of the Pensions Board on the National Pensions Policy Initiative, *Securing Retirement Income* (May 1998), set out a strategy for future pensions development in Ireland and made a number of major recommendations for change to give effect to the strategy. These included recommendations in relation to the target rate of Social Welfare pension and basis for its future indexation, the establishment of an explicit mechanism to fund part of the future cost of Social Welfare pensions, the introduction of a new pensions vehicle to be known as Personal Retirement Savings Accounts (PRSAs), simplification of the tax regime for pensions, and various changes to occupational pension provision. Many of these recommendations have been accepted by the Government and are currently in the process of implementation, while others are still under consideration.

1.8 In July 1999, the Minister for Finance, Charlie McCreevy TD, announced the Government's decision to set aside an annual provision of 1% of GNP to pre-fund part of the future cost of Social Welfare and public service pensions and, in addition, to allocate a tranche of the proceeds of the Telecom Éireann flotation to supplement the annual allocations. The Minister stated that he hoped to have the necessary legislation for pensions pre-funding in place by the middle of 2000 and that, in the meantime, the appropriate sums would be set aside in 1999. He noted that there were major policy issues to be determined in legislating for pensions pre-funding, and that he looked forward to the pending report of the Commission on Public Service Pensions in that context. The relevant legislation, the National Pensions Reserve Fund Bill, 2000, was published in June 2000.

1.9 In addition to the reference noted at *Paragraph 1.5*, the *Programme for Prosperity and Fairness* stated that following Government consideration of the Report of the Commission, a Working Group of the public service unions, relevant Government Departments and other appropriate bodies would be established to advise on the implementation of the relevant Government decisions with a view to introducing, as quickly as possible, any proposed changes in public service pension arrangements, including those for low paid workers.

1.10 A number of legislative changes which have been implemented or are in the course of development – arising from the National Pensions Policy Initiative and otherwise – will have implications for the wider pensions environment in which occupational pension schemes, including public service schemes, operate. These include the establishment of a framework for PRSAs and the implementation of new pension flexibilities in the 1999 and 2000 Finance Acts which apply to the self-employed and to certain other groups, as well as to additional voluntary contribution (AVC) schemes. The ongoing nature of these changes means that the full implications for existing pension schemes is not yet fully apparent. Therefore, for the purposes of our Report, the Commission has proceeded on the basis that these pension changes will not have any *direct* implications for large defined benefit occupational pension schemes, including those in the public service.

Commission's approach

1.11 The Commission established at an early stage that we did not have any role in adjudicating on matters being processed under the industrial relations machinery. In considering our terms of reference, we interpreted our main objective as securing the viability and stability of public service pension arrangements over the long-term. We determined that a broad-based approach was necessary so as to address issues that were encountered across the whole public service. This enabled the Commission also to place demands for change in public service pensions in the context of new thinking about the role of the public service (the Strategic Management Initiative), about the evolution of pensions in Ireland (the National Pensions Policy Initiative) and abroad, and developments in the private sector.

Identification of major issues (Chapters 2 and 11)

1.12 On the basis of submissions received from interested parties (see *Paragraph 2.6*), the views of the relevant Government Departments and agencies, specific issues which were referred to us for examination, and our own deliberations, the Commission decided to focus on the following issues:

(i) securing the long-term viability and stability of public service pensions;

(ii) managing the growth in pension costs;

(iii) retirement age and early retirement;

(iv) pensions increase policy;

(v) integration with State Social Insurance benefits and low levels of occupational pension;

(vi) pensions and atypical employment;

(vii) pension scheme flexibility;

(viii) dependants' benefits;

(ix) other issues relating to pension terms;

(x) funding public service pensions;

(xi) transparency in pension costs and liabilities;

(xii) management, administration and communication.

1.13 Items (i) and (ii) are central to the Commission's strategy for a new public service pensions framework, and underpin our recommendations as a whole. The Commission's analysis and recommendations on items (iii)-(ix) are presented below in *Section 6* dealing with public service pension terms, while items (x)-(xii) are addressed in *Section 7*, which deals with pension scheme financing, management and communication arrangements.

Overview of recommendations

1.14 The package of measures recommended by the Commission represents an integrated strategy aimed at securing the long-term viability and stability of public service pensions. It addresses, in particular, the following key aspects:

- the growth of long-term pension expenditures;
- the issue of retirement age and claims for early retirement;
- the need for transparency in public service pension costs within government management and financial systems;
- the requirement that the pensions system should be compatible with the current and changing nature of public service employment and should be capable of adapting to future change;
- the pension situation of employees who are in receipt of relatively low levels of pay at retirement, with particular reference to integration with State Social Insurance benefits;
- the need for extending choice with respect to level of pension and age of retirement;
- the advantages and disadvantages of establishing a pension fund to meet in full or in part the growing pensions bill; and
- the need for better communication to scheme members of their pension entitlements and of the value of those entitlements.

2. Analysis of Commission's terms of reference

2.1 In this Section, the Commission considers the present and future cost of public service pensions, claims for improvements in existing scheme benefits, and changes in the working environment, conditions of employment and operational requirements of the public service.

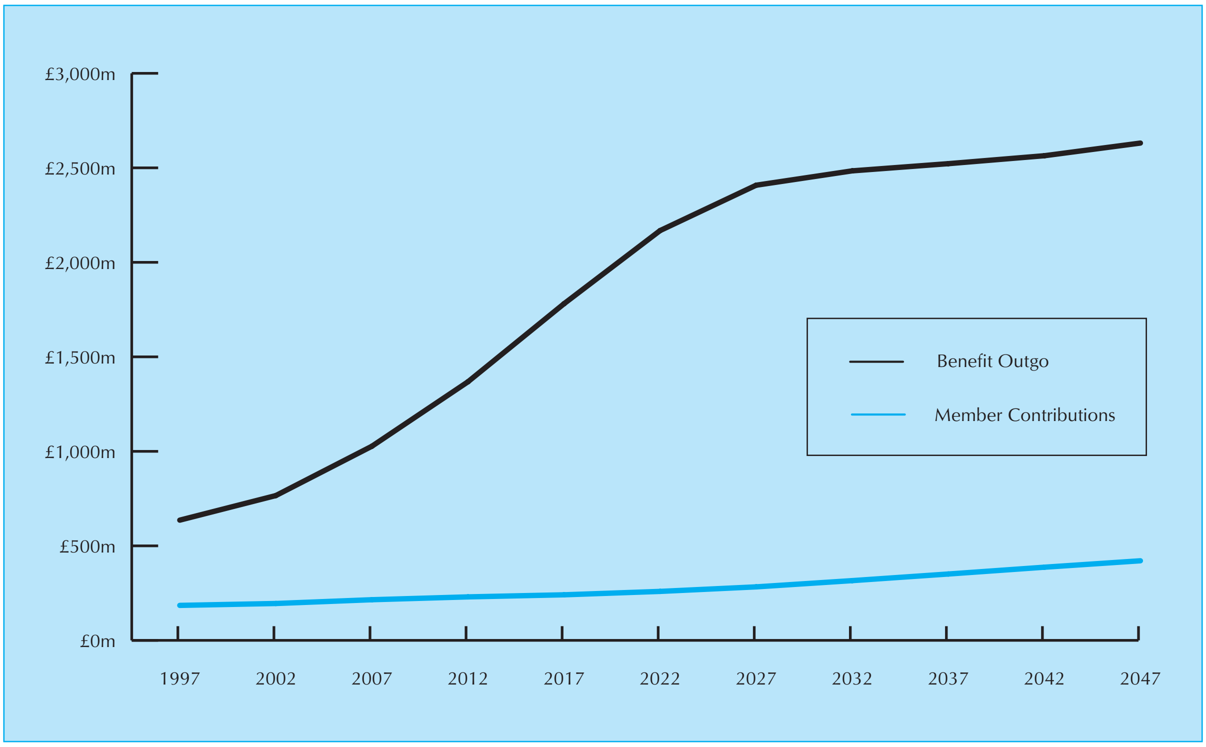
Present and future cost of public service pensions (Chapters 6 and 10)

2.2 The Commission considered that ascertaining the true cost of public service pension terms and carrying out a detailed projection of future pension costs were key requirements of our terms of reference. Comprehensive actuarial costings would enable the State to better manage its long-term commitments, bring greater transparency into pension costs, and allow proper evaluation of possible changes to benefit terms.

2.3 The main findings of the Commission's review of public service pension costs are summarised below:

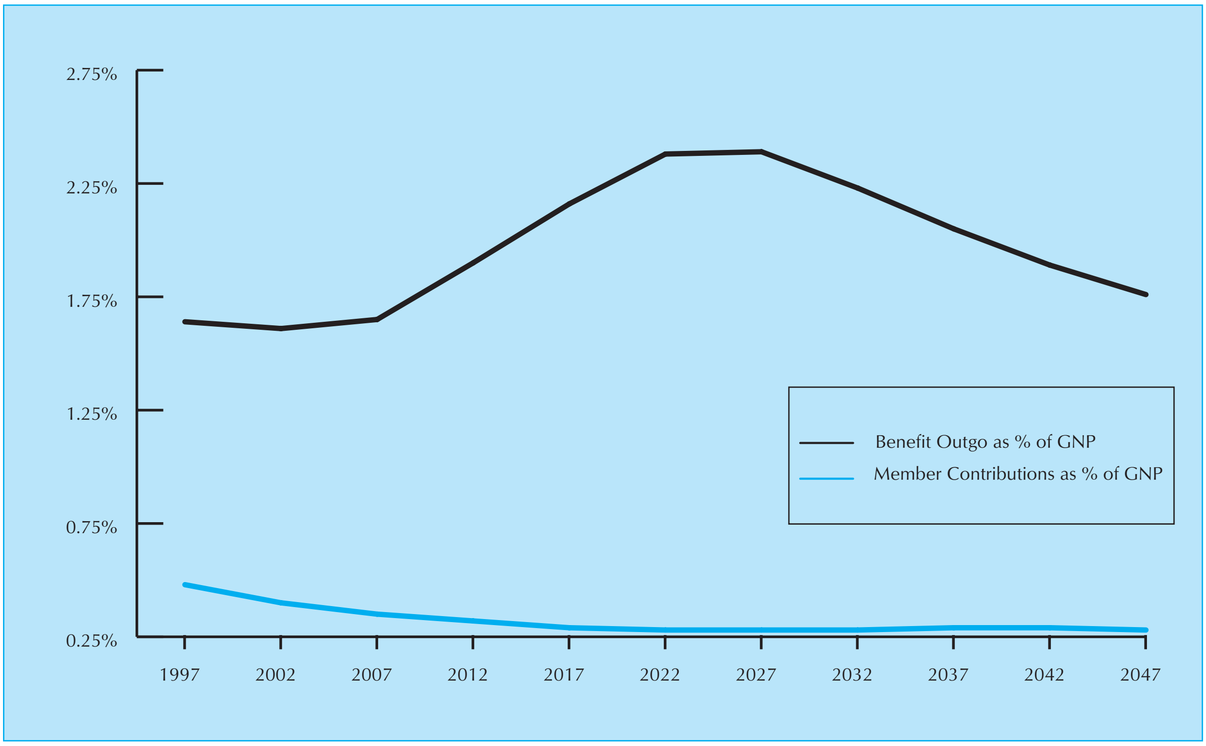
- in constant (1997) price terms, the existing level of gross benefit expenditure, £636 million (€807 million) in 1997, is expected to more than double over the next 15 years to £1,368 million (€1,737 million) in 2012, and to almost quadruple over the next 30 years to £2,408 million (€3,058 million) in 2027. The projected development in pensions expenditure and contributions is shown in Table 1:

Table 1: Projected development of cashflows for public service pensions — 1997 to 2047



- for the 20 years after 2027, benefit expenditure is projected to display limited growth, with the reduction in the rate of growth partially attributable to the effects of integration with the State Social Insurance pension for post-April 1995 entrants (taking into account the increased cost of Social Insurance pensions, the *overall* impact on the Exchequer of extending full PRSI to public servants is expected to be broadly neutral);
- as member contributions will increase at a slower rate than gross benefit expenditure, net benefit expenditure (i.e. the difference between benefit payments and contribution income) is projected to increase at a higher rate than the rate of increase in gross benefit expenditure over the period to 2047;
- the main factors in the expected growth in public service pension costs include the increase in public service numbers which occurred during the 1970s and early 1980s, improvements in benefit terms and in pension scheme coverage, increases in public service pay relative to price inflation, and the impact of increased life expectancy;
- expressed as a percentage of GNP, gross benefit expenditure is projected to remain relatively static for the 10 years to 2007, and then to increase steadily from 1.6% to a peak of 2.4% of GNP in around 30 years' time. Thereafter, benefit expenditure will return gradually to a level of approximately 1.8% of GNP by the middle of the century; the development in pensions expenditures and contributions as a percentage of GNP is shown in Table 2;

Table 2: Future projected benefit expenditure and member contributions as a percentage of GNP



- expressed as a percentage of pensionable pay, gross benefit expenditure is projected to grow from 16% of pay to around 38% of pay in 2027, before falling somewhat to 30% of pay in 2047;
- it has been estimated that if the additional pension costs in the year 2027 were to be incurred in 1998 and financed through taxation, it would require an increase of 2p on the standard rate of tax and 3p on the top rate of tax;
- the value in 1997 of the State's accrued liabilities in respect of public service pension schemes was estimated at approximately £20 billion (€25 billion);
- new entrant rates (the contribution rates which would be required to fully fund the pension benefits of a new employee over the period of employment) varied considerably between sectors and groups within the public service, ranging from 8% to 30% of pensionable pay. The degree of variation in the rates reflected the benefit terms and conditions applying to each group (e.g. earlier retirement ages result in higher new entrant rates), the promotional salary scale assumed (the rates are higher where significant salary increments and/or career progression can be expected), assumed average age at entry, etc. It was calculated that benefit scales for groups with special pension terms cost up to twice as much as the standard civil service benefit scale.

2.4 The Commission considered the evolving cost of public service pensions to be a matter of serious concern. The growth in pension costs will occur at a time when the effects of demographic ageing generally will begin to impact upon the cost of Social Welfare and health care provision. Against this cost backdrop, it is essential to evaluate carefully any further commitments that would add to the growth in future pension costs. The funding of public service pensions would not, of itself, reduce the cost of pension schemes, except to the extent that the returns on the monies lodged to the fund would be greater than the returns which the Government would otherwise have obtained (a comparison that is difficult to quantify conclusively). However, it is clear that part-funding future pension costs could play a valuable role in *smoothing* the cost profile and thereby stabilising the fiscal and tax environment in future years.

2.5 The appropriate response to the evolving cost of public service pensions, in the Commission's view, is:

(i) to find ways of smoothing the expected peak in costs, including the use of pension funding;

(ii) to limit any recommended scheme improvements to cost neutral changes, or to cost increasing changes considered absolutely necessary for operational reasons or on grounds of equity and fairness, with a view to preventing as far as possible any net enlargement of the rise in the pensions bill;

(iii) to estimate the impact on long-term costs of all major suggested changes in pension terms;

(iv) to permit as much individual flexibility as possible, consistent with the overall framework of the pensions system, in order to allow employees to provide for benefit improvements by means of personal contributions (the new flexibility to be facilitated through better communication systems);

(v) where a disimprovement in benefit terms is considered necessary, to confine the change to new entrants only, while having due regard to intergenerational equity.

Claims for improvements in existing scheme benefits (Chapter 2)

2.6 The Commission received submissions from 105 interested parties, including unions and staff associations, pensioner representative associations, individual public servants, former public servants, pensioners, representatives of employers, pension funds and the pensions industry generally. The Commission met with 17 parties who made submissions. In addition to the above, a number of specific issues were referred to the Commission for examination, while a range of pension and retirement issues were raised in the *Report of the Commission on Nursing* (July 1998).

2.7 Claims for improvements in scheme benefits were categorised by the Commission. They are addressed in *Section 6* below under the following headings:

- retirement age and early retirement;
- pensions increase policy;
- integration with State Social Insurance benefits and low levels of occupational pension;
- pensions and atypical employment;
- pension scheme flexibility;
- dependants' benefits;
- employee contributions;
- notional added years.

2.8 Many other points were raised in submissions and the Commission has endeavoured in the Report to address as many as possible of those that came within the terms of reference.

2.9 Claims for benefit improvements arise from:

- a desire for improved pension terms;
- the changing nature of the employment environment;
- comparisons between the different pension terms of various groups within the public service;
- the wish to address perceived inequities and anomalies; and
- a desire for more flexibility.

2.10 Such claims draw attention to the dilemma faced by the Commission under our terms of reference, namely, the difficulty in addressing in a satisfactory way the competing objectives of having regard to the present and future costs arising under the schemes (as considered above) and the claims for improvements in existing scheme benefits.

2.11 The integrated package of measures recommended by the Commission aims to address the major issues which we have identified, including claims for benefit improvements, while having regard to the need to manage the evolving cost of public service pensions.

Changes in operational requirements, working environment, and conditions of employment of public servants (Chapters 7 and 12)

2.12 The basic principles of public service pension arrangements were laid down in the nineteenth century. Pension terms were designed to accommodate the generally accepted view of public service employment at that time. Employment was *for life*, commenced usually well before age 20, and the employee worked within the one area of the service until retirement at about age 60. At this stage, the employee was considered unable to continue working because of old age or infirmity and a reduced maintenance-type payment, or pension, was made by the employer.

2.13 Changes in the nature of the public service affect the continuing validity of these basic principles and assumptions. The process of modernisation of the public service must be considered in this regard. If the public service is to undergo a process of significant change in the future, corresponding reform of pension arrangements may be necessary. Pension terms must not be a barrier to change and should be capable of adapting to the developing work situation. Thus, it is important to determine whether a process of gradual reform rather than a more radical overhaul of the pensions system is necessary. We address this further in *Section 5*.

2.14 The main trends of change which the Commission identified in the public service and which we considered relevant in our review of public service occupational pension arrangements were:

- increasing age of entry, trend towards shorter service, and more mobile work force;
- growth of atypical employment;
- ensuring pensionability of atypical employment;
- more frequent breaks in service;
- employee interest in retiring earlier than the norm;
- emphasis on delivery of service and management of performance;
- changes in pay determination.

2.15 The Commission concluded that while there may be developments in the existing model of public service employment by virtue of changes which might be expected in pay determination systems, greater variety in future work patterns, and increased mobility between the public service and the private sector, the majority of public servants will continue to be employed under the traditional framework in the medium- to long-term. The implications for public service pension arrangements of the developments listed are considered further below.

2.16 Data presented in the Report (see Chapter 7) suggest that public servants are retiring earlier from full-time employment and that the average level of service at retirement is falling. In addition, the number of early retirements on grounds of ill health appears quite high in some parts of the public service.

2.17 A number of responses to increasing longevity and improvements in health and educational resources have been implemented in several OECD countries. These include encouraging working beyond retirement age, more flexible working arrangements at older ages, replacement of the fixed point of retirement with gradual/phased retirement, ensuring availability of job opportunities for older workers and that they are equipped with the necessary skills and competence to take them. In relation to pay-as-you-go public old-age pension systems (state social security systems as well as public service occupational schemes), reforms have usually included increases in the standard age of entitlement to public pensions and the introduction of greater flexibility in the age at which benefits can be accessed subject to actuarial adjustment.

3. Existing public service pension arrangements

3.1 In this Section, the Commission examines existing public service pension arrangements under three headings:

(i) pension terms;

(ii) management, administration and communication; and

(iii) financing.

Public service pension terms (Chapter 3)

3.2 Most public servants are in modified class for the purposes of Pay Related Social Insurance (PRSI) — they pay a lower rate of PRSI than other employees and are not eligible for a range of State Social Insurance benefits, including pensions. Under public service occupational pension schemes, public servants earn or *accrue* retirement pension and lump sum for each year of pensionable service at a rate of one-eightieth and three-eightieths, respectively, of the amount of final salary and pensionable allowances. An upper limit of 40 years' pensionable service applies. Thus, maximum pension is one-half, and maximum lump sum one-and-a-half times, the amount of final salary and allowances. This form of pension scheme is known as a *defined benefit final salary* structure. Public service pensions are increased in line with changes in the pay of serving public servants.

3.3 For the majority of public servants in modified PRSI class, an employee pension contribution of $6\frac{1}{2}$% of remuneration applies (5% contribution for main pension benefits and $1\frac{1}{2}$% contribution towards dependants' benefits). Some groups are not subject to an explicit contribution for main pension benefits. However, for pay determination purposes, it has been accepted in a number of arbitration findings that an implicit contribution is made through salary being set at a lower level to take account of pension benefits.

3.4 For most public servants, retirement is available as an option on reaching a minimum age of 60. Public servants may retire at an earlier age in the case of ill health, or on foot of organisational restructurings, reductions in staff numbers, or on grounds of efficiency. The maximum retirement age is 65.

3.5 There is a separate contributory scheme to cover payment of pension to spouses and children in the case of the death-in-service or death after retirement. A death gratuity is also payable under the main pension scheme in the case of death-in-service.

3.6 The main variations from this general picture are in the area of retirement age. For example, Gardaí may retire at age 50 with 30 years' service and with each year after 20 counting as double. Retirement at age 55, with various service conditions, applies in the case of other categories such as teachers. The Defence Forces also have special early retirement arrangements and a very different form of pension scheme.

3.7 A further variation is in the area of classification for Social Insurance purposes. While most public servants are in modified class PRSI, a significant number are in full class PRSI. They pay the same rate of PRSI as private sector employees and are entitled to receive State Social Insurance pensions. Accordingly, their occupational pensions (and pension contributions) are *integrated* or *coordinated* to take account of the Social Insurance benefits payable (see *Paragraph 6.45*). The number of public servants whose occupational pensions and contributions are subject to integration will increase as a result of the Government decision that all public servants appointed on or after 6 April 1995 should be in full PRSI class.

3.8 Schemes for the purchase of notional service and AVC schemes provide opportunities for individual public servants to *top up* their pension benefits within the limits laid down by the Revenue Commissioners. The two sets of arrangements work in very different ways: under the purchase scheme, the public servant agrees to buy a specified number of added years of notional service, thereby increasing the total period of pensionable service for the calculation of pension benefits under the occupational pension scheme; under the AVC arrangement, the public servant makes contributions for investment in an individual fund which, at retirement, is used to provide additional benefits.

3.9 In the current socio-economic context and with today's increasingly mobile and flexible work environment, some of the basic principles and assumptions underlying public service pensions (see *Paragraph 2.12*) might appear outmoded and overly rigid. Over the past 20 or 30 years, certain pension modifications have been made with the aim of providing the necessary adaptability and flexibility required in a modern public service. In assessing public service pension terms, the Commission considered their appropriateness for the future, the internal consistency and fairness of terms, including fairness as between different public service groups, and the need for employee choice and flexibility within the pensions framework.

Management, administration and communication (Chapter 4)

3.10 In some parts of the public service, the pension scheme is small and is specific to a particular company or organisation; in others, it is a large *umbrella* type scheme applying to the sector as a whole. Thus, there are a large number of schemes and a wide range of organisations involved in different aspects of their administration. Notwithstanding the complexity of these structures, it appeared to the Commission that on the basic requirement of any pension administration system — paying pensions in the correct amount and on time — public service pensions are administered reasonably efficiently and effectively across all parts of the public service.

3.11 However, there are deficiencies in the system. Foremost among those, in our view, is the lack of proactive communication of the pension scheme. The focus of pension administration and personnel sections has traditionally been the calculation of benefits at the point of retirement and on death-in-service. Insufficient effort is made to communicate benefit entitlements to employees during service, to appraise them of options to enhance their pension, and to open up retirement choice. In addition, scheme documentation is not kept up to date in some parts of the public service.

3.12 The fragmented structure of public service pensions, involving a large number of independent schemes, can present problems for the management and negotiation of pension terms. Also, questions arise as to the effectiveness of the appeal mechanisms available under public service schemes.

Arrangements for financing of public service pension schemes (Chapter 5)

3.13 The majority of public service occupational pension schemes are financed on a pay-as-you-go basis, with the annual cost of pensions being met from current revenues. Thus, the liabilities are secured by the Government and its ability to tax. In contrast, private sector companies and commercial state companies operate a pre-funding system, setting aside funds and investing them to meet future liabilities as and when they arise. In Chapters 5 and 23, we examine the arguments for and against pay-as-you-go and funding. These are summarised below.

3.14 The arguments in favour of pay-as-you-go include the following:

- the State's permanent and continuing commitment to discharge its obligations as they arise adequately meets the primary objective of funding in the private sector, viz to provide a secure basis for the pensions of employees;
- pay-as-you-go is easy to operate and the administrative costs are low;
- pay-as-you-go is in keeping with the Government's budgetary system generally;
- pay-as-you-go facilitates transferability of service within the public service (in most cases, no transfer payments need to be made when a public servant moves from one public service scheme to another).

3.15 The arguments in favour of funding include:

- funding, unlike pay-as-you-go, makes advance provision for future liabilities;
- the real cost of pensions is immediately obvious under a funding arrangement. Thus, the long term effect of increases in the number of personnel covered and/or improvements in pension terms (which may have only a minor impact on costs under a pay-as-you-go system in the short term) is immediately apparent to the parties concerned;
- contribution rates for a pension fund would bring home to members of schemes the value of their pension entitlements and to employers the real cost of recruitment;
- funding would give a more stable profile of costs to the Exchequer over time compared with pay-as-you-go.

3.16 The financing of public service pension schemes is closely related to the question of accounting for pension costs under government financial management systems. The existing cash-based approach is consistent with pay-as-you-go. The charge to the accounts each year is in respect of actual pension scheme expenditures on pensions, lump sums, etc. No entry is made in respect of the accruing cost of pensions for staff currently in service, i.e. to recognise the future cost of pension benefits earned or accrued for that year. In addition, no record is maintained of the pension liability in respect of the past service of serving public servants and of pensioners.

3.17 The shortcomings of the cash-based approach include:

- existing systems fail to highlight the long-term cost of pensions and of decisions which would have long-term pension cost implications, e.g. additional recruitment, improvements in pension terms, etc.;
- because they report only the current cash cost of pensions, they convey a false impression of the affordability of pension schemes and benefits;
- they fail to bring home to employers and employees the true cost of early retirement;
- the failure to report the full cost of public service pension benefits impacts adversely on the value which employees place on those benefits.

4. Occupational pensions: private sector and abroad

4.1 In this Section, the Commission reviews occupational pension arrangements in the private sector in Ireland and in the public service in other countries and compares them with public service pensions in Ireland. Recent developments in occupational pensions are discussed and relevant future trends identified.

Private sector (Chapter 8)

4.2 Public service pensions have in the past acted as a catalyst in the development of occupational pension arrangements in the private sector. In many countries, the State was the first to make provision for its employees to cater for their old age or infirmity. The idea of occupational pensions spread to other sectors, and was encouraged by governments through the creation of favourable conditions for the financing of pensions, above all, by favourable tax treatment. In many ways, public service schemes as they developed were taken by the private sector as models of what good occupational pension schemes might provide.

4.3 The Commission's conclusions on a comparison of pension terms in the public service with large Irish private sector schemes are as follows:

(i) pension scheme coverage for permanent employees is considerably higher in the public service than in the private sector;

(ii) in the public service, the earliest age of retirement is age 60 for the vast majority of employees (the latest is age 65). In the private sector, the normal retirement age is 65 for over three-quarters of the schemes of large firms, but almost all allow members to retire earlier, usually with their benefits being subject to some form of actuarial reduction;

(iii) in the public service, AVC schemes, if available, are generally set up at the behest of individual unions; in the private sector, almost all large firms make provision for AVCs;

(iv) most pension schemes for large firms in the private sector are defined benefit, as are public service schemes (see *Paragraph 3.2*). However, there is an increasing trend towards defined contribution schemes (this form of pension scheme is explained at *Paragraph 5.13*) for new entrants to private sector companies, particularly in the case of newly created schemes, but also, to a lesser degree, in the case of already existing schemes;

(v) most private sector defined benefit schemes operate a 60ths accrual rate with provision for commutation (i.e. conversion of a portion of pension into tax-free lump sum), while public service schemes have separate 80ths-based accrual rates for pension and lump sum. When allowing for the more favourable pensions increase policy of public service schemes (see item (vi)), the value of a public service pension is normally greater than that of a private sector pension;

(vi) pension increases in the public service are based on increases in the pay of serving staff, while increases in the private sector are often discretionary or in some cases no increases are given. Where increases are given in the private sector, they are usually based on changes in the Consumer Price Index, subject to a cap of between 3% and 5% per annum.

4.4 Public service pension schemes have been adapted to changing circumstances over a long period of years to encourage public servants to remain in the public service for the whole of their working lives. They do this by offering more favourable pension terms than are generally available in the private sector. This ensures that the average public servant has a higher probability of being covered, of receiving better benefits, and of such benefits maintaining their purchasing power.

4.5 However, moving beyond a static comparison of terms, it is clear that private sector pension schemes have had to adapt more to the changing social and economic environment and to developments in the labour market. Furthermore, private sector schemes, supported by better communication and administrative systems, offer a wider range of flexibility and retirement choice (generally at full cost to the member) than is available in the public service.

Public service schemes in other countries (Chapter 9)

4.6 The Commission examined public service pension arrangements abroad under a number of headings. Special attention was given to the experience of countries such as the UK, Germany, Sweden and the Netherlands. Trends in the reform of pension arrangements in these countries were studied in detail.

4.7 The Commission concluded as follows:

(i) with a number of countries moving to increase the age of retirement, the normal retirement age for public servants in Ireland may now be considered amongst the lower of those applying to public servants in Europe;

(ii) most countries operate defined benefit pension schemes for their public servants, although a small number have been moving to a defined contribution or hybrid pension scheme design either for certain categories of public servants or for new entrants generally;

(iii) maximum pension benefits, expressed as a percentage of pensionable remuneration, would seem, on average, to be higher in many European countries, but this must be qualified on the basis that the figure for pensionable remuneration used in those countries (based on an average of the final three years' pay, for example) may be lower than that used in public service schemes in Ireland;

(iv) retirement with immediate payment of pension from a minimum retirement age is permissible for public servants in most countries (but not in Ireland), usually subject to actuarial reduction;

(v) it is normal practice to apply special retirement and pension terms to certain groups facing particular operational requirements, e.g. police, fire service;

(vi) most public service schemes are separate and distinct from the state social security system, with members having no entitlements under the latter. Integration applies in most countries where public servants are covered by the state social security system;

(vii) pensions are generally increased by reference to the Consumer Price Index, or by a combination of cost of living and adjustments in line with salaries for serving staff. Ireland applies increases by reference to pay only, which appears to be a more favourable system compared with many other countries. A much less favourable system of pension increases applies in public retirement plans in the US;

(viii) with some notable exceptions, most countries finance public service pensions on a pay-as-you-go basis;

(ix) compared with Ireland, it would appear that many countries devote greater resources to the administration of pensions and to the communication to members of benefit details and retirement options.

4.8 In a widely based review such as this it is difficult to draw firm conclusions. Each country has its own distinctive historical, social and economic characteristics. These help to determine the relative importance of the public service within the economy, the processes for determining pay and conditions for public servants, and the state social security system, all of which combined impact upon the public service pension system in each country.

5. Criteria for a public service pensions framework and pension scheme design

5.1 In this Section, we identify the objectives for public service pensions and develop a set of principles or criteria which a new public service pensions framework should be capable of meeting. Alternative pension structures are examined in order to determine whether a move to a radically different pension structure is necessary or whether instead it is preferable to reform the existing defined benefit structure.

Goals for public service pensions (Chapter 13)

5.2 In the Report, the Commission identifies separately the concerns of public servants and pensioners, on the one hand, and of the State and public service employers, on the other, on the basis of submissions and meetings with the relevant parties. On the face of it, these different concerns are difficult to reconcile. However, the Commission noted points of overlap between both sets of concerns, as set out below.

5.3 Both parties accept the view that the State as an employer should offer good pension schemes to its employees, and that the schemes should be credible, secure and stable. Employers wish to ensure that their employees are protected adequately against the contingencies of death or ill health and can anticipate a reasonable standard of living in retirement. For their part, employees need to be confident that they and their dependants will be financially secure in the event of death or ill health and will have a reasonable source of income in retirement.

5.4 Both agree that pension terms should be applied to all public servants under a consistent set of principles. Differences in treatment between public service groups should be based insofar as possible on objective, verifiable, operational criteria, and these should be subject to regular review and updating.

5.5 The need for pension terms to be adaptable and flexible is accepted by employers and employees. Increasingly, public service employers are adopting new approaches to employing personnel in order to deliver on the standards of service and quality expected under the Strategic Management Initiative and the requirements of public service reform. Equally, many employees, particularly female employees, find that atypical forms of work, e.g. part-time or temporary working, meet their needs through the additional personal flexibility they offer. Accordingly, there is an acceptance that pension schemes should raise no unnecessary barriers to the introduction of change desired by both employers and employees and, in particular, that they should be capable of catering for atypical forms of employment.

5.6 For employees, the desire for flexibility extends to choice within the pension system itself — for example, in relation to early retirement, dependants' benefits, and improving pension benefits generally. For their part, employers would be willing to facilitate the offer of additional pension flexibility, provided that there was no additional cost to the pension scheme, that the administrative costs were reasonable and that the new facilities did not become a barrier to mobility either within the public service or between the public service and the private sector.

5.7 Employers and employees have a shared interest in ensuring that pension schemes do not result in a distortion of preferred work choices. Employees might wish — for reasons of choice but also of health — to adjust their work towards less operationally demanding duties or to work reduced hours in the lead up to retirement, without unduly affecting their pension rights. This could suit management too. However, the present pension system, with its focus on final pay, has the effect of encouraging public servants to work longer and/or more unsocial hours towards the end of their careers in order to boost pension benefits. This may be in the interest of neither the employee nor of the service concerned.

5.8 Both employers and employees require that pension terms are applied transparently and fairly. There is a shared interest in having a pension system that is efficiently administered, with changes in pension arrangements effected without undue disruption and confusion. Scheme provisions, including benefit entitlements and options which may of their nature be quite complex, should be actively communicated in as simple and straightforward a manner as possible, and unnecessary complexity in pension schemes should be eliminated.

5.9 Both parties accept that pensions should be financed in a balanced way between employers and employees. Both would wish to minimise the risk that the benefits promised might not be delivered due to the cost reaching a level which became unaffordable to the taxpayer. They would be willing to consider some form of advance funding — through the investment of employee and employer contributions in an independently controlled fund — on the basis that this would help promote the robustness and long term viability of benefit promises.

5.10 In conclusion, employers, employees, and pensioners have a common interest in securing the long term viability and stability of public service pension schemes. Equally, they wish to have in place pension arrangements that are affordable, fair, flexible and transparent, and that can be justified to the wider public who must ultimately finance them.

Criteria for a public service pensions framework

5.11 Having considered carefully the views of all interested parties, the Commission concluded that public service pension arrangements should be assessed on the following criteria:

- ***adequacy:*** the State, as a good employer, should offer comprehensive and adequate pension schemes to its employees, taking account of pension terms and arrangements available in the private sector, and in public sectors in other countries at a similar stage of economic development;
- ***viability:*** benefits promised should be affordable to the taxpayer and reasonable in relation to the country's capacity to pay;
- ***flexibility:*** pension structures should be capable of dealing with the position of the low paid, part-time employees, contract workers, and those with variable earnings. They should also be capable, insofar as possible, of offering choice to public servants in relation to their pensions package and retirement decisions;
- ***fairness:*** fairness in pension terms means that differences in treatment between groups should be based on clear objective criteria, and that pension terms are seen to be applied transparently and correctly in all cases;
- ***cost:*** the long-term development of pension costs should be known and prepared for in advance. The consequences for pension costs of decisions in relation to recruitment, early retirement, improvements in benefit terms, etc. should be clearly costed and made transparent.

Alternative pension structures (Chapter 14)

5.12 The Commission considered the question of whether a completely new pensions model for the public service should be proposed as an alternative to reforming the existing structure.

5.13 Different pension structures were examined. The examination included the defined contribution structure which, as noted at *Paragraph 4.3*, is becoming increasingly prevalent in the private sector. A defined contribution scheme is one in which the member's benefits are determined by reference to:

- the contributions made, less charges levied;
- the investment return received on those contributions; and
- annuity rates at the time of retirement.

We considered the advantages and disadvantages of each structure, together with the arguments for retaining the existing defined benefit model.

5.14 Pension scheme structure should form an integrated component within the overall employment model. We concluded (see *Paragraph 2.15*) that, while there will be greater variety in future work patterns, increased employee mobility, etc., the majority of public servants will continue to be employed under the traditional framework in the medium- to long-term. For this reason, the Commission recommends retention of the existing pensions structure. However, reforms — as outlined in *Section 6* below — are necessary to make the existing structure better capable of adapting to changing circumstances and of delivering the flexibilities required.

5.15 Pension structures should not be fixed, but should be capable of change. If changes in the employment framework for the public service turn out to be radically different to those anticipated, or should cost and other pressures faced by pension schemes increase dramatically, then it may be found necessary at some future date to replace the defined benefit structure with a more flexible and transparent defined contribution (or hybrid) pension scheme. The Commission believes that the analysis has been carried out to implement such a scheme alteration were it to be considered necessary.

6. Analysis and recommendations in relation to public service pension terms

6.1 This Section summarises the analysis, conclusions and recommendations on public service pension terms (see *Paragraph 1.12*). Some members of the Commission expressed reservations in relation to certain of the recommendations. These are marked "*(R)*" below.

Retirement age and early retirement (Chapter 15)

6.2 The Commission's terms of reference required us to have particular regard to claims for early retirement. It is clear that there has been an increasing demand for early retirement facilities across the public service and amongst certain groups in particular. For many, a desire for early retirement has merged over time with claims for enhanced pension terms which apply to a number of groups for operational reasons. In some cases, early retirement is sought as an option within the pension scheme, one that might not actually be taken up. We reached the view in our Interim Report that it was not immediately clear that the demand for early retirement (i.e. with no actuarial reduction of pension to cater for the longer period over which it will be paid) was sustainable on grounds of cost, operational requirements, practice in the private sector, increased longevity, and trends in public service retirement arrangements abroad.

6.3 The determination of what is a reasonable and fair retirement age is a complex and difficult task. There are many conflicting interests at stake. The diversity of employment within the public service — with a range of different operational requirements — means that it is not possible to apply a uniform approach to retirement age. Employees and employers have different perspectives based on their own needs and experience and these can change significantly over time. For example, existing retirement ages were generally established at a time when both life expectancy and the work environment were very different to what they are today. Accordingly, some employers would argue that special pension terms are no longer appropriate in certain areas due to changes in the nature of a profession, while some employees would contend that their work environment has so significantly altered over time that special terms should be extended to other groups.

6.4 In our consideration of retirement age and early retirement in the public service, we had regard to a number of factors:

- historical basis for present arrangements;
- staff claims in relation to retirement and early retirement;
- desire for retirement flexibility;
- operational considerations;

- macro-economic and labour market considerations;
- improvement in health and life expectancy;
- cost to pension schemes;
- retirement age in the Social Welfare system;
- retirement age in the private sector;
- retirement age in the public service abroad.

6.5 Having examined these factors, we make a series of recommendations in our Report, as detailed below, on the normal retirement age for public servants, voluntary early retirement, and the special retirement provisions applicable to certain groups for operational reasons. We also address a number of related matters, including flexibility in working arrangements, and phased retirement.

6.6 The decision to leave formal employment is one of the most important decisions which an employee will make; accordingly, we consider that appropriate supports should be made available to underpin that process.

6.7 The Commission considers that employees should be provided with regular and comprehensive information on their entitlements and the retirement options available to them. Structured programmes of retirement planning and counselling should be initiated so as to raise the issue with individuals well ahead of their retirement and to provide information on the options open to them.

(Paragraph 15.15.4 of the Report)

6.8 The Commission considers that a more flexible approach to working and retirement would encourage public servants who would otherwise retire early to remain in public service employment for longer. New flexibilities might include, for example, working at a lower level of responsibility, part-time working, the facilitation of reduced working of unsocial hours prior to retirement, and the re-employment of retired personnel having required skills and expertise.

6.9 In our view, the proposal of the Civil Service Inter-Departmental Committee on Work Sharing to expand the scope of the job-sharing scheme to a wider range of attendance patterns (to be known as work-sharing) addresses much of the above. The new scheme is currently being finalised and will, presumably, be extended to other parts of the public service. Our recommendations below, if implemented, would dovetail with this more flexible approach to working, particularly in the lead up to retirement.

6.10 We recommend that changes be made to pension terms to enable public servants who wish to do so to work at a lower level of responsibility prior to retirement without unduly affecting their pension rights. Individuals should be allowed to freeze benefits based on the salary/allowance point immediately prior to changing work pattern, and to separately accrue benefits based on the lower salary/allowance point for the period served in the new work pattern.

(Paragraph 15.15.8)

6.11 We recommend in Paragraph 22.9.14 of the Report a change in the pensionability rule for variable allowances so that averaging would cover the best three years' allowances in the last ten, rather than the allowances received in the final three years of service. This change would address the position of employees who might prefer to work fewer unsocial hours close to retirement without unduly affecting their pension rights. Apart from facilitating public servants who wish to have greater flexibility prior to retirement, this change would also meet some of the concerns of management in this regard.

6.12 In a context of ongoing labour shortages, some relaxation of the abatement of pension rules should be made in order to facilitate the re-employment of public servants with required expertise/skills on a contract basis after retirement. *(R)*

(Paragraph 15.15.12)

6.13 Improved retirement choice for public servants could be achieved by allowing individuals the opportunity to make personal contributions towards the cost of retiring early.

6.14 We recommend the introduction of *cost neutral early retirement*. This would allow public servants aged 50 and over (aged 55 and over, in the case of new entrants) to retire with immediate payment of benefits, subject to actuarial reduction to cater for the longer period over which the benefits would be paid. *(R)*

(Paragraph 15.15.14)

6.15 Public servants would have recourse to the Scheme for Public Employees' Additional Retirement Savings (SPEARS) (see *Paragraph 6.72*) as a well designed, cost-effective, and adaptable facility providing for genuine retirement choice. SPEARS would enable public servants to help offset part of the reduction in scheme benefits resulting from a decision to opt for cost neutral early retirement.

6.16 There have been substantial improvements in life expectancy since public service pension schemes were introduced in the middle of the nineteenth century, and current projections are that it will continue to improve further in the years ahead.

6.17 Reflecting this change, we recommend that the age of retirement for new entrants with standard pension terms should be changed from age 60–65 to a single retirement age of 65, with consequential changes in the retirement ages for groups which have special retirement terms for operational reasons (see *Paragraph 6.33*). *(R)*

(Paragraph 15.15.17)

6.18 Early retirement (other than on an actuarially reduced basis) gives rise to substantial additional pension costs. Given the objective of minimising the growth in future pension costs, it is clear that early retirement should be implemented with circumspection. However, there are situations and cases in which early retirement may be the appropriate management option.

6.19 The Commission recommends that early retirement provisions should be made available — at an individual/group level — to cater for organisational restructurings, reductions in staff numbers, and as part of new performance management systems to be introduced in the public service. The existence of these provisions and the conditions applying to them should be clearly stated in pension scheme documentation provided to public servants. In view of the cost of early retirement, we recommend that it should be used only where other reasonable avenues — such as retraining and redeployment, flexible working, etc. — have been considered.

(Paragraph 15.15.19)

6.20 However, we consider that there is need for further provision, particularly in light of the arguments presented in submissions and in our meetings with interested parties.

6.21 Accordingly, we recommend the introduction of an additional early retirement facility, called *Approved Early Retirement*. Early retirement under this facility would be available in respect of public servants aged 55 or over (aged 60 or over in the case of new entrants) with 20 or more years' service who consider that they are unable to make a fully satisfactory contribution and where management accept that their early retirement would improve the general level of efficiency and effectiveness of the service in question. It would be initiated either by management or the individual public servant, and would be subject to agreement by both parties. Pension benefits under Approved Early Retirement would consist of the immediate payment of pension and retirement lump sum with no actuarial reduction.

(Paragraph 15.15.21)

6.22 In light of the significant cost which early retirement imposes, the Commission recommends that an annual quota of Approved Early Retirements be set and that all applications across the public service be assessed at a central level. We suggest below (see *Paragraph 7.14*) that alternative arrangements should be examined which would involve departments or organisations meeting the additional capital cost of early retirement from within their own resources.

(Paragraph 15.15.22)

6.23 We recommend that a review of the Approved Early Retirement facility should be carried out in five years' time, having regard to its efficacy in addressing the needs of management and staff, the level of take-up, and the development and implementation of new systems to monitor performance in the public service, including early retirement provisions (see *Paragraph 6.19*).

(Paragraph 15.15.23)

6.24 As part of their respective restructuring agreements reached under the *Programme for Competitiveness and Work*, a number of limited retirement and early retirement initiatives were agreed for teachers and nurses. These initiatives were to operate on a pilot basis, subject to annual quotas, and would be reviewed in the light of our Final Report.

6.25 The Commission recommends that the limited retirement initiatives for teachers and nurses should be continued for a further five years, and that they be included in the review referred to at *Paragraph 6.23*.

(Paragraph 15.15.25)

6.26 The Commission considers that the high incidence of early retirement on grounds of ill health in certain parts of the public service is a matter of concern — in terms of the effect on pension costs, the impact upon the individuals affected, and the consequences of the loss of experienced and qualified employees from the public services in question.

6.27 Accordingly, we recommend that a review should be carried out of procedures followed in processing ill health early retirements across the public service, with the aim of developing a consistent approach and to identify best practice.

(Paragraph 15.15.27)

6.28 We acknowledge the work of occupational health units in helping individual public servants to address difficulties which they are experiencing in their work, particularly the debilitating effects of adverse stress and burnout.

6.29 A range of additional actions should be taken to address factors which have potentially negative effects on the health and performance of individuals. These include identifying and addressing the most prevalent causes of adverse stress where they occur in various public service occupations (e.g. under-resourcing, excessive work loads), developing and extending occupational health services to address health and welfare issues, and the effective use of redeployment, accompanied by retraining.

(Paragraph 15.15.29)

6.30 The Commission accepts that it is necessary for operational reasons for certain public service groups to be subject to lower retirement ages than the norm, and as a consequence to have enhanced pension terms.

6.31 For the application of special terms to be justified, it should be possible to demonstrate that it is an absolute prerequisite that all employees in the group are required, as the central feature of their employment, to maintain throughout their period of service a consistently high work capacity, defined in terms of physical capability, alertness, and speed of response so as to be able to respond quickly and effectively to an operational emergency, and that the application of lower retirement ages is a reasonable means of determining work capacity.

6.32 In assessing the position of public service groups in light of this requirement, the Commission considered operational requirements and environmental conditions, the historical basis and development of current arrangements, and practice in the private sector and in comparable employments in the public service of other countries.

6.33 Based on the information available to the Commission, and taking into account our recommendation to raise retirement ages for new entrants to the public service generally (see *Paragraph 6.17*), our specific recommendations on the application of special terms for operational reasons are as follows:

(i) new entrants to those parts of the psychiatric services where special terms currently apply should in future have standard pension terms; there should be no change in the special terms (i.e. doubling of service on serving in excess of 20 years, and retirement on reaching age 55) of personnel currently employed in the psychiatric services;

(ii) new entrants to the Garda Síochána should be subject to a minimum retirement age of 55 and should be retained beyond that age, to a maximum retirement age of 60, subject to meeting certain minimum standards of health and fitness on an annual basis; there should be no change in the special terms as they are applied to members of the Garda Síochána currently in service;

(iii) in the case of the prison service, the optional facility to retire between ages 50 and 55 on achieving 30 years' service should not apply to new entrants; the new Prisons Board should examine whether, in light of developments in operational requirements in the prison service, special terms in their entirety (i.e. retirement between ages 55 and 60, and doubling of service on serving in excess of 20 years) should be removed;

there should be no change in the special terms as they are currently applied to personnel now in employment;

(iv) in the case of the fire service:

(a) new entrant Firefighters should continue to be subject to a retirement age of 55, with service in excess of 20 years doubled for pension purposes;

(b) new entrant officers, who have the option to remain in employment until age 65, should have standard pension terms;

(c) new entrant Firefighters who are subsequently promoted to non-operational positions should have standard pension terms, but should receive a higher pensions credit for the period served as Firefighters (this is known as *uniform accrual*);

(d) there should be no change in special terms as they are currently applied to all serving personnel;

(v) new entrant teachers should have standard pension terms; the provision whereby teachers may retire between age 55 and age 60 (on achieving 35 years' service) should continue for all serving teachers (the limited retirement initiative for teachers is addressed in *Paragraph 6.25*);

(vi) new entrants to the Defence Forces should have special pension terms more in line with the special terms which apply to certain other public service groups, consistent with current personnel policy (see Chapter 21 of the Report);

(vii) having regard to the available information, and in light of the range of other recommendations made in relation to retirement age and early retirement, the Commission does not recommend the extension of special pension terms to any other public service group. *(R)*

(Paragraph 15.15.33)

6.34 The purpose of the Commission's recommendations in relation to retirement age and early retirement — which we believe are essential to ensure internal equity and fairness in pension arrangements for the future — is to arrive at a situation where increased flexibility in pension and working arrangements is available to all public service groups, and where departure from standard pension terms occurs only where it is considered absolutely necessary for operational reasons. The recommendations in relation to special pension terms focus upon the retirement terms of new entrants; thus, the entitlements of serving staff members would not be affected in any way.

Pensions increase policy (Chapter 16)

6.35 The maintenance of the value of pensions over time is an important element in the terms of a pensions scheme. Pension increases in the public service are currently determined on the basis of *pay parity*, that is, in line with the pay of the grade in which the retired public servant once served. This has proven an advantageous arrangement for the pensioner, mainly because pay has increased at a consistently higher rate than price inflation. However, a number of issues have arisen in relation to existing pension increase arrangements. They include:

- **pay parity in the context of a changing approach to pay determination:** in an environment in which pay determination systems increasingly reward change and modernisation, and where there is wide variation in the rates of pay increases granted to different groups, the tracking of salary of the grades from which pensioners have retired may be seen as less appropriate;

- **administrative difficulties:** many practical difficulties have arisen in the implementation of pay parity, for example, the problem of continuing links with specific grades that have over time been amalgamated with other grades or regraded, dealing with lengthening or shortening of pay scales, etc.

6.36 Pension increases represent a significant component in the cost of pensions. Obviously, the more favourable the pensions increase policy, the greater the cost. Pension schemes in the private sector which pay pension increases (some schemes do not) usually base them on changes in the Consumer Price Index (CPI), subject to a cap of between 3% and 5% per annum. Public service schemes in other countries regularly raise pensions in line with price inflation. Pay parity is less common as a basis for adjustment in public service schemes abroad.

6.37 The Commission considers that a change in pensions increase policy is necessary to address the issues raised above. In formulating our recommendations, we had regard to a range of factors:

- commitment to increase pensions;
- Government statements on pension increases;
- employee contributions and pension increases;
- pay parity and restructuring agreements;
- administrative considerations;
- cost;
- pension increases in the private sector;
- pension increases in the public service abroad.

6.38 The Commission considers that pension increases in line with changes in the CPI would represent the minimum provision required for the maintenance of the standard of living of public service pensioners. We also believe that some link to broader pay increases remains highly desirable. In most schemes, the formal position is that the grant of increases in pension is at the discretion of the Minister for Finance. The Commission acknowledges the possibility that in the absence of any change now to secure pension increase arrangements into the future, pressures might arise, perhaps in a time of straitened financial circumstances, to move to a system of CPI-related pension increases.

6.39 The Commission notes the arguments made on behalf of many pensioners and employees that pay parity represents a benefit to which they have contributed and that public servants have consistently placed a greater importance and value upon good pension benefits than have employees in the private sector. With the changing nature of pay determination in the public service, and in the absence of any change to pensions increase policy, the practical difficulties, disputes, and delays in finalising pensions increases which have arisen in the past will continue.

6.40 In an environment in which pay determination systems increasingly reflect commitment to public service change and modernisation, the tracking of salary of the grades from which pensioners have retired may be seen as less appropriate for pension increase purposes.

6.41 For these reasons, the Commission considers that an alternative system of increasing pensions, based on an average of pay increases in the public service as a whole, would be more appropriate to this changing environment, and that in light of the substantial benefit which pay-related pension increases represents, should be made subject to an additional contribution by public servants towards the cost involved.

6.42 Accordingly, the Commission recommends that a CSO Public Service Earnings Index should be developed (along the lines set out in Paragraph 16.5.6 of the Report) for calculation twice-yearly of a single rate of pay-related increase to be paid to all public service pensioners. The implementation of the index should involve consultation with public service employers, unions and pensioner representatives. In view of the value to public servants of a guaranteed system of pay-related pension increases, the Commission recommends that all serving public servants should make an additional explicit 1% contribution of remuneration or net remuneration, as appropriate, towards the cost of pay-related pension increases. We also recommend that the State should explicitly guarantee the new system of pension increases by means of legislation and through the establishment of a Public Service Pension Fund to meet the full cost of pension increases (see *Paragraph 7.11*). *(R)*

(Paragraph 16.6.5)

6.43 The Commission believes that the new system of pay-related increases, supported by an employee contribution and a pension fund, would represent an affordable, administratively straightforward and equitable pension increase system. Given the uncertainty which characterises existing arrangements, the new system should strengthen confidence as to the continuation of pay-related pension increases into the future.

6.44 As discussed in *Section 7*, we recommend that the 1% contribution towards the cost of pension increases, when it is introduced, should be lodged to the Public Service Pension Fund. The Public Service Earnings Index should be developed with a view to its implementation after the completion of the current *Programme for Prosperity and Fairness*.

(Paragraph 16.6.8)

Integration with State Social Insurance benefits and low levels of occupational pension (Chapter 17)

6.45 Integration applies in the case of public servants in full PRSI class. Occupational pension is calculated on the basis of net pensionable remuneration, i.e. pensionable remuneration less a Social Welfare offset of twice the rate of Old Age (Contributory) Pension (OACP). For a public servant with 40 years' service, this ensures that the combination of occupational pension and OACP is equivalent to 50% of pensionable remuneration. Employee contributions are calculated on the basis of net remuneration, i.e. remuneration less twice the rate of OACP.

6.46 In integrated private sector schemes which have a 60ths accrual rate (with commutation to provide retirement lump sum), the Social Welfare offset is usually $1\frac{1}{2}$ times the rate of OACP. Applying this lower offset gives essentially the same result as under public service integrated schemes after allowing for the difference in accrual rates.

6.47 Integration is a central feature of public service pension schemes and of the majority of defined benefit schemes in the private sector. It is also the practice in many other countries. Integration ensures the provision of an occupational pension which, when combined with the Social Welfare pension, is both reasonable by reference to pensionable pay and the period in employment, and affordable to both employees and employers. In effect, integration avoids *double pensioning* that tranche of income which is already *pensioned* by the employer's and employee's PRSI contributions. The Commission accepts that integration is a fundamental component in the public service pensions framework and is strongly of the view that it should be continued.

6.48 However, in certain circumstances, the effect of integration (with its flat rate deduction) can be to produce a very low or zero rate of occupational pension. In the public service, the relatively low levels of pay and career progression applicable to many groups who have traditionally been subject to integration contribute to this effect. Several groups met the Commission and forcefully communicated their members' dissatisfaction with this outcome.

6.49 It must be recognised that a number of factors — not just the operation of integration — contribute to the lower rates of occupational pension experienced by these groups compared with other public service groups. These include lower average levels of service at retirement and generally lower levels of pay at retirement.

6.50 The Commission acknowledges that the current final salary defined benefit pension structure for the public service works particularly to the advantage of those experiencing relatively beneficial career and salary progression. On the other hand, there is a perception amongst those in full PRSI class retiring on relatively low levels of pay that the occupational pension is poor *value for money* and that their work in the public service is inadequately reflected in their pension.

6.51 Clearly, the complete abolition of integration (which, in relative terms, would benefit the groups particularly affected by this issue the most) would result in a significant increase in pension benefits, as well as in the cost of public service pension schemes. We could not recommend such an approach. Apart from the impact on future costs, it would represent a radical recasting of the public service pensions framework. In our view, the removal of integration would impact upon the long-term viability of existing schemes, perhaps to the point where future governments might consider replacing them with defined contribution schemes.

6.52 The Commission examined the arguments for and against making an adjustment to integration for employees who are in receipt of relatively low levels of pay at retirement. We considered the possibility of adjusting the calculation formula in a targeted way for the benefit of those directly affected, in the context of retaining the existing public service defined benefit pension structure.

6.53 Having decided that such a change is necessary, the Commission recommends that, in order to enhance the pension position of public servants in full PRSI class and subject to integration and who retire on relatively low levels of pay, the operation of integration in all public service schemes should be amended through the introduction of a new pension calculation formula as follows:

> Pension to be calculated using accrual rates of:
>
> 1/240th for pensionable remuneration below three times the rate of OACP, and
>
> 1/80th for pensionable remuneration in excess of this limit.

(Paragraph 17.6.5)

6.54 This formula would result in an increased occupational pension in the case of those retiring on pensionable remuneration of less than three times the rate of OACP (i.e. £15,028 (€19,082) per annum based on the May 2000 OACP rate of £96 (€122) per week), and an unchanged occupational pension for those retiring on pensionable remuneration above this limit. The Commission considers that such a cut-off level is appropriate in current circumstances having regard to the salary maxima of the various grades for whom the issue of integration and low levels of occupational pension was raised. In our view, the improvement in the pension calculation formula recommended, which is to be financed in full by the State, meets the concerns of public servants retiring on relatively low levels of pay. It would, of course, be open to individual employees to make additional contributions to SPEARS (see *Paragraph 6.72*) as a means of further improving their pension situation.

6.55 The Commission recognises that a case could be made to increase the contribution rate of some or all public servants in order to recover at least part of the cost of the proposed change. However, we decided not to recommend accordingly.

6.56 In its report, *Securing Retirement Income*, the Pensions Board recommended that the rate of OACP should be increased to 34% of average industrial earnings over a five to ten year period. The Commission is conscious that if this target rate is reached, the salary point which it is recommending as the cut-off point for the calculation of improved rates of occupational pension would be equal to 102% of average industrial earnings. The Commission considers that, even though the adjustment to occupational pension tapers off very steeply as pay rises towards the cut-off point, such a high cut-off point might prove hard to justify. There are questions of principle and indeed of the cost of the proposed adjustment formula that would need to be reviewed at the point of implementation.

Pensions and atypical employment (Chapter 18)

6.57 Atypical working has always been a major part of public service employment. It is not clear that the numbers in atypical employment are set to increase substantially in the future, but new arrangements are currently being introduced which could have a significant impact on the position. In any event, there is now a strong emphasis on ensuring pensionability of all forms of atypical employment, particularly part-time employment.

6.58 The Commission recommends that public servants in temporary and part-time work should be granted access to public service pension schemes, provided that they are in regular or quasi-permanent employment and, in the case of part-time employees, that they work a certain minimum number of hours per week.

(Paragraph 18.6.1)

6.59 At present, most part-time public servants are found in areas where full PRSI applied prior to the 1995 change. When considering the extension of pension terms to part-time employees, the question of integration and low levels of occupational pension arises.

6.60 There are two possible approaches to integration for part-time employees. One method is to calculate the part-timer's actual service at retirement (i.e. to add together all the hours, days and years the person has worked) and apply this service to the full time remuneration for the position (less the Social Welfare offset of twice the rate of OACP). This is known as *pro rata integration*. The other method is to take the actual remuneration of the part-timer at retirement (less the Social Welfare offset) but to treat each year in which he or she has worked (regardless of the actual time put in) as a full year of service for pension purposes. This is known as *full integration*. The public service currently applies the latter approach (although the pensions of job-sharers are based on pro rata integration). From the perspective of the employee, full integration gives a less favourable level of occupational pension than pro rata integration.

6.61 If the OACP were not payable and therefore integration were not involved, both methods of determining pension for a part-time employee would give the same result. However, the calculations give different results with integration because the OACP is flat rate (i.e. unlike the occupational pension it is not service-based).

6.62 The Commission gave careful consideration to the question of the pension terms to be applied to part-time employees, in particular, the question of integration. For a number of reasons, including:

- the blurring of the distinction in the public service between job-sharing and part-time working,
- the general implications of the European Commission's Part-time Work Directive and of recent decisions of the European Court of Justice in relation to direct and indirect sex discrimination, and
- the need to accommodate atypical forms of working for socio-political reasons,

the Commission considers that occupational pensions for part-time public servants should be calculated on the basis of pro rata integration.

6.63 Accordingly, the Commission recommends a change in the form in which integration is applied to part-time public servants from full to pro rata integration; this modification in scheme terms would result in improved occupational pensions for such employees (the change in the operation of integration recommended at *Paragraph 6.53* would impact on the pension calculation of any part-time employees where the amount of notional full-time pensionable remuneration was less than three times the rate of OACP).

(Paragraph 18.6.7)

6.64 The Commission believes that the effect of this recommendation would be to facilitate the pensionability of part-time employment within the existing benefits structure and to achieve a practicable system for treating atypical service.

6.65 The Commission recommends that discussions should take place between public service unions and employers in order to arrive at a reasonable and equitable approach to the calculation of death gratuity and spouses' and children's benefits for part-time public servants. These discussions should take account of practice in private sector pension schemes and of the existing approach of public service schemes in relation to job-sharing, part-time, and contract public servants, as well as giving appropriate weighting to each individual's pattern(s) of employment. Insofar as possible, the principle of pro rata benefits should apply. In addition, particular regard should be had to the commitments entered into by the Social Partners in relation to the promotion of family friendly policies.

(Paragraph 18.6.12)

6.66 At present, public service schemes do not allow preservation of pension benefits where service at time of leaving is less than five years. Thus, other than death-in-service cover, and the refund of employee pension scheme contributions (if any), individuals with contracts of employment of less than five years could not expect to benefit from their scheme membership.

6.67 The Commission recommends that the period of reckonable service required to qualify for preserved benefits under public service schemes should be reduced from five to two years, in line with the recommendation of the Pensions Board in the National Pensions Policy Initiative. We believe this change should apply to serving staff only from a current date.

(Paragraph 18.6.13)

Pension scheme flexibility (Chapters 12 and 19)

6.68 The Commission believes that public servants should have the opportunity to provide for enhanced pension benefits and to plan in relation to the age at which they would like to retire. With the increasing age of entry to the public service, more frequent breaks in service, and widespread interest in early retirement, there is likely to be a growing demand in the future for a well designed, cost-effective, and adaptable facility which would allow public servants to contribute towards improved pensions and a package more suited to their individual circumstances. For the State, the requirements of any such facility are cost, administrative convenience, and the minimisation of any possible exposure under the legal and regulatory framework applying to the facility.

6.69 Existing arrangements for the provision of member choice are the schemes for purchase of notional service and additional voluntary contributions (AVCs). We describe these briefly at *Paragraph 3.8*.

6.70 Purchase of notional service has the advantages that it is designed to be self-financing and that it provides certainty in relation to the benefits purchased. Its disadvantages are its strict eligibility requirements, inflexibility as regards benefits purchased and pricing anomalies. AVCs have the advantages of flexibility, external funding, good communication and promotion. Their disadvantages include the uncertainty of benefits, administrative charges and fragmentation of schemes across the public service. The level of take-up of AVC schemes would appear to be high, particularly when compared with the take-up under the purchase schemes.

6.71 The Commission examined the introduction of a new scheme which would represent a drawing together of the two existing arrangements, but in a way which would address some of the shortcomings of both.

6.72 Accordingly, the Commission recommends the introduction, in consultation with the public service unions and having regard to the position of existing AVC schemes, of a single AVC-type scheme for the public service as a whole. We recommend that this scheme should be established and operated broadly along the lines envisaged in Chapter 19 of our Report, and called the Scheme for Public Employees' Additional Retirement Savings (SPEARS). SPEARS should include a savings account facility and a lump sum death benefit facility. In addition to providing the options available under existing AVC schemes, SPEARS should incorporate a new purchase arrangement to enable the use of the savings account at, or prior to, retirement to purchase an amount of public service pension, which would be increased in line with public service pensions generally.

(Paragraph 19.10.4)

6.73 We recommend that the structure of SPEARS (AVC, group PRSA, or other) should be decided once the framework for PRSAs has been put in place. However, in the event that the scheme were set up initially as an AVC under trust deed, we recommend that the independent trustees of the scheme should include representatives of public service unions and employers. It might be considered desirable to convert SPEARS into a group PRSA in due course and this matter should be decided by the State at the appropriate time, in consultation with the public service unions.

(Paragraph 19.10.5)

6.74 The Commission recommends that existing schemes for the purchase of notional service should be phased out, the precise period involved to be determined by the State, in consultation with the public service unions, based on the level of take-up of the schemes in comparison with the new SPEARS option.

(Paragraph 19.10.6)

6.75 SPEARS should include an option at retirement to use any or all of the retirement lump sum to purchase additional pension.

(Paragraph 19.10.7)

6.76 We recommend that the State should consider meeting part of the administrative cost of SPEARS, in particular, the cost of promoting the scheme, in the context of the phased removal of the schemes for purchase of notional service.

(Paragraph 19.10.8)

6.77 The Revenue limits can have an important impact on the pension benefits which an individual can fund towards, including early retirement. While not formally coming within our terms of reference, we would suggest that consideration should be given to introducing greater flexibility into the operation of these limits. We note that greater simplification in the tax treatment of pensions is recommended in the National Pensions Policy Initiative.

Dependants' benefits (Chapter 20)

6.78 The spouses' and children's pension schemes are a key component in public service pension arrangements. They provide an important social and financial benefit to the families of deceased members. The benefits of the schemes, taken in conjunction with the gratuity payable on death-in-service, are reasonable when compared with dependants' benefits of public service schemes in other countries and with schemes in the private sector.

6.79 The *original* widows' and orphans' contributory pension schemes were introduced for male public servants in most parts of the public service between 1968 and 1971. In general, the schemes were extended to include female public servants from 1981 onwards. At the time of their original introduction and subsequent extension to include female public servants, membership of the schemes was made automatic for new entrants and optional for those who were then in service. This approach was agreed with the public service unions. Most groups, with the exception of teachers (other than VEC teachers), have availed of two options to join the schemes.

6.80 For a variety of reasons, a number of serving public servants, both male and female, declined to join the *revised* and/or original spouses' and children's contributory pension schemes

This was a public service-wide phenomenon. A range of submissions received by the Commission sought a new option to join the schemes.

6.81 The Commission gave careful consideration to the arguments involved. On balance, we have decided not to recommend a further general membership option across the public service as a whole. We would be particularly concerned about the major additional costs which a new option would impose, given that it would almost certainly be availed of by those who would either have an immediate entitlement or a high expectation of benefit at a later stage. We would be concerned also that a further option would weaken the integrity of the schemes, leading to pressure for individuals to enter and leave at will. Such a development could undermine fundamentally the financing of the schemes.

6.82 However, the Commission accepts that in a number of cases, perceptions of injustice may have arisen as a result of the exercise of past options not to join public service spouses' and children's pension schemes. We consider that some means should be introduced to allow for a review of these cases, but subject to certain conditions.

6.83 The Commission recommends that a limited appeals process for spouses' and children's scheme membership options be established to examine individual cases and to allow appeals that meet any one of the following criteria:

(i) where there is no evidence that an option was provided to the individual public servant in the first place;

(ii) where there is medical evidence to indicate that the person making the decision not to join the scheme was of sufficiently unsound mind not to appreciate the consequences of his or her decision;

(iii) where a member of the original scheme declined to join the revised scheme in circumstances where there would have been no reasonably foreseeable adverse financial consequences for the individual (in terms only of his or her scheme contributions) had he or she instead opted to join the revised scheme.

(Paragraph 20.3.26)

6.84 The Commission considers that an option to join spouses' and children's schemes in the case of teachers (other than VEC teachers covered by the LGSS) should proceed on the basis of the management offer made at the Teachers' Conciliation Council (i.e. an option to join the revised schemes is to be offered to national and secondary teachers in the original schemes). *(R)*

(Paragraph 20.3.28)

6.85 Under public service spouses' and children's schemes, a spouse's pension may only be paid to the legal spouse of the member. This arrangement reflects the constitutional imperative to protect the family based on marriage. Given that many family units are not based on marriage, and in light of pensions practice in the private sector, the Commission decided to examine the question of payment of spouse's pension to non-marital partners. We looked first at the position under the Constitution, which unlike the case in the private sector, is particularly relevant for the State as sponsor of occupational pension schemes.

6.86 The *Constitutional Review Group* stated that the present emphasis of Article 41 of the Constitution is the protection of the rights of the family as a unit rather than the protection of individuals resulting from a family relationship. This approach, the Group argued, presented significant difficulties if the definition of the family unit were to be extended beyond the family based on marriage, due to the uncertainties of defining what constitutes a family at any given time.

6.87 The Group recommended that a revised Article 41 should retain the pledge to protect the family based on marriage, but that an amendment should be made so as to make it clear that this pledge should not prevent the Oireachtas from providing protection for the benefit of family units based on a relationship other than marriage.

6.88 Revenue rules in relation to occupational pension schemes permit the payment of a survivor's pension to a co-habiting partner on the basis that the person was wholly or substantially dependent financially on the employee or was so dependent at the time of the employee's death. In practice, we understand that the existence of dependency is recognised where two people are sharing a household, as financial *interdependence* is the determining factor, i.e. where a second income has been relied upon to maintain a certain standard of living prior to the member's death.

6.89 The Commission is sympathetic to the argument that a spouse's pension should be payable to the surviving partner of a public servant where the two parties were living together as husband and wife prior to the member's death, and where financial interdependency can be shown to have existed.

6.90 Taking these considerations into account, we recommend that the existing provisions of public service spouses' and children's schemes should be modified to allow payment of a survivor's pension to a financially dependent partner in circumstances where there is no legal spouse and where a valid nomination has been made. We would suggest that the system of nomination to be introduced on foot of this recommendation should provide for regular review, preferably as part of the annual issue of the statement of pension entitlements (see *Paragraph 7.32*). We would envisage that the nomination form would seek details on the nature and extent of the financial dependency and that it would state that documentary evidence of financial dependency would be required should the member predecease his or her partner. We consider that the form should also state that a nomination, assuming there was no legal spouse, would not be binding on the scheme administrators, and that a pension would not be paid where there was no valid nomination. *(R)*

(Paragraph 20.4.9)

6.91 The approach which we recommend would ensure that (i) the constitutional imperative not to penalise marriage would be respected by continuing to favour the family based on marriage over any other type of arrangement, (ii) there would be absolute certainty that survivor's entitlements would be payable to the legal spouse where the member was legally married, and (iii) pension scheme administrators would have discretion to pay a survivor's pension to a partner in circumstances where the member was not married.

6.92 This approach would prohibit payment of survivor's pension to a non-marital cohabiting partner in circumstances where the public servant was married at time of death, but separated. In such a case, the survivor's pension would continue to be payable to the legal spouse. We are of the view that should there be constitutional change in this area, the matter should be considered again by employers and unions.

6.93 The Commission makes a series of other recommendations in relation to dependants' benefits. These are included in the List of Recommendations.

Employee contributions (Chapter 22)

6.94 In assessing public service pension arrangements, it is necessary to take into account the contributions, whether implicit (see *Paragraph 6.102*) or explicit, being made by individual public servants towards the cost of their pension benefits, including the role of pensions within the salary determination process.

6.95 The majority of public service occupational pension schemes in Ireland (covering about three-quarters of all pensionable public servants) involve an explicit contribution, although this fact does not appear to be widely recognised outside the public service.

6.96 Since 5 April 1995, most new entrants to the public service pay contributions at a *nominal rate* of $6\frac{1}{2}$%, 5% for the main pension scheme, and $1\frac{1}{2}$% for the spouses and children's scheme. The *actual rate* of contribution is calculated as 3% of remuneration plus $3\frac{1}{2}$% of net remuneration (i.e. remuneration less twice the rate of OACP).

6.97 Given the application of a uniform contribution rate, it is clear that the employee contribution does not reflect the variation in the value of the pension package between different public service groups, as indicated by the new entrant rate (see Table 6.8 in the Report). An alternative approach would involve the application of a separate rate of employee contribution for each group relative to the value of the pension package applying to that group. For example, it might be decided that employees pay one-third of the estimated cost of the pension benefits.

6.98 However, the existence of a wide variety of employee contribution rates would be administratively complex, while the introduction of such a system in the first place would be a difficult and time-consuming task. In addition, the question of adjusting pay rates would arise. A further complication with *group-specific* contribution rates is that there would be no limit to the extent to which the *"groups"* might tend to splinter. There would also be a concern that such an approach would be destabilising from an industrial relations perspective.

6.99 While there may be a logic to *group-specific* contribution rates, which are the practice in some public service schemes abroad, the Commission considers that, on balance, it would be preferable to continue the application of a standard rate of employee contribution for new entrants across all public service groups.

(Paragraph 22.2.10)

6.100 Over time, as a consequence of our recommendation at *Paragraph 7.15*, there could be future variation in rates reflecting changes in pension terms negotiated for particular groups.

6.101 In *Paragraph 6.42,* the Commission recommends the introduction of an additional 1% contribution towards the cost of pay-related pension increases.

6.102 In a number of arbitration findings in the past, a deduction has been made when setting the pay of certain civil service grades and, by extension, of other public service grades having a direct pay linkage with those grades to reflect the difference in contribution arrangements and the more favourable pension terms applying in the civil service compared with the private sector. This latter deduction would not appear to have applied uniformly in other arbitration findings, nor was it applied to other public service grades. It is not possible to say with certainty that such a deduction continues to exist in what has been — through the effect of national pay agreements and restructuring agreements — a significantly different pay determination environment.

6.103 We recommend that to the extent that any future pay determinations for public service grades are carried out by means of a comparison with equivalent positions in the private sector, any adjustment which might be made to reflect the value of public service relative to private sector pension arrangements should take into account the employee contribution being made by the public servants concerned.

(Paragraph 22.2.14)

6.104 A significant number of public servants who took up employment prior to 6 April 1995 do not currently pay an explicit main scheme contribution, or pay a contribution of less than 5%. It has been strongly argued in a small number of submissions that an explicit main scheme contribution of 5% should be introduced for these public servants and that salaries and pensionable allowances should be uplifted accordingly.

6.105 The Commission gave careful consideration to this issue. We were concerned particularly about the cost implications of the proposed change which in the context of our projections of the future cost of public service pensions would be difficult to justify. In other parts of our Report where we noted differences in pension terms as between two separate groups which could not be justified by reference to operational or other reasons, we recommended that the difference in treatment should be removed for new entrants. Insofar as differences in employee pension contribution arrangements are concerned, this outcome has already been achieved as part of the April 1995 change to introduce full PRSI for all new entrants to the public service. For these reasons, the Commission is unable to recommend the introduction of explicit pension contributions and consequent uplifting of salary for the groups affected. *(R)*

Notional added years (Chapter 22)

6.106 The granting of notional added years of pensionable service to certain public servants in professional, technical and other grades is a particular feature of public service pension schemes. The notional added years are intended to compensate for the inability of individuals in such positions to qualify by maximum retirement age for a *full pension* based on 40 years' service.

6.107 The growth of pensions coverage in the private sector coupled with more extensive transfer and preservation arrangements means that many individuals have already accrued pensionable service before they take up public service employment. Moreover, there is more scope for individuals to make additional pension provision for themselves than in the past through the notional service schemes and various AVC arrangements. The introduction of SPEARS would further improve this position. It is also relevant that the added years schemes were introduced for public service groups at a time when the majority of public servants had limited Social Insurance coverage; this is no longer a factor for future entrants, given the extension of full PRSI to all public servants.

6.108 The Commission considers that the schemes of notional added years are a crude instrument for the purposes of addressing recruitment difficulties. They are not designed to be responsive to the needs of the relevant areas of the public service at the time of recruitment. We believe that pay would be a more appropriate and responsive recruitment incentive.

6.109 Having weighed the considerations for and against, the Commission is of the view that the schemes of notional added years are no longer appropriate as a component in public service pension arrangements and, accordingly, recommends their abolition for new entrants. In that context, consideration should be given to the offer of other forms of recruitment incentive.

(Paragraph 22.3.12)

Other pension terms (Chapter 22)

6.110 The Commission makes a series of other recommendations in relation to public service pension terms. These are included in the List of Recommendations.

7. Analysis and recommendations in relation to financing, management and communication arrangements

7.1 In *Section 7*, we summarise our analysis, conclusions and recommendations in relation to pension scheme financing, transparency in pension costs, and pension scheme management and administration.

Partial funding of public service pensions (Chapter 23)

7.2 Some of the major arguments in favour of pay-as-you-go and funding are summarised at *Paragraphs 3.14* and *3.15*, while the use of funding as a means of smoothing the future cost profile of public service pensions is raised at *Paragraph 2.4*.

7.3 The Commission is not convinced of the need to fully fund public service pensions in line with private sector practice. The basic reason for establishing a pension fund in the private sector – to provide security of benefits – does not apply in the public service where the State is the ultimate guarantor of benefits. In addition, the economic arguments in favour of funding are less than conclusive. Finally, the introduction of full funding would do nothing to address the expected peak in public service pension costs and would limit, to an unreasonable extent, the budgetary flexibility available to future governments.

7.4 Nevertheless, we are aware of the major advantage of funding, particularly in bringing transparency into pension costs. With the existing pay-as-you-go approach, benefits, not costs, tend to become the main focus of attention. In a funded system, the contribution rates would bring home to public servants the value of their pension entitlements and the costs of improving them, while the State, too, would become more conscious of the real cost of recruitment. We make recommendations below on the introduction of greater transparency in pension costs under government financial systems. However, we would suggest that if public service pension costs were allowed escalate beyond existing projections, a move towards full funding might be deemed necessary as a more effective means of control.

7.5 The Commission sees definite advantages in the idea of partially funding future pension costs. We welcome the Government decision of July 1999 (see *Paragraph 1.8*) to pre-fund part of the future cost of Social Welfare and public service pensions. This initiative will help to smooth the pensions bill in the future, thereby averting destabilising shifts in future government taxation/spending patterns. In addition, it ensures diversification of state expenditure at a time when the economy is at or near full employment and revenue is buoyant. Finally, as we have argued, funding (whether full funding or part funding) represents an effective approach to ensuring greater transparency and discipline in the management of public service pension costs.

7.6 The Government decision of July 1999 envisaged the setting up of two funds, one for Social Welfare pensions and one for public service pensions, while the National Pensions Reserve Fund Bill published in June 2000 provides for a single fund to cover both sets of liabilities. However, in the press statement accompanying the publication of the Bill, the Minister for Finance indicated that the legislation could be amended at a future date to provide for two funds if, following our Report and following the necessary consultation process about the Report's recommendations, there were agreement between all parties that there should be separate funds.

7.7 A partial fund for public service pensions could be structured as either a government budgetary reserve fund or a private sector type pension fund. The former would have the advantages of simplicity, ease of establishment, and lower cost of administration. The latter would have the advantages of integrity and cost discipline in a pension scheme context.

7.8 The type of fund selected would have implications for the ownership and management structure of the fund and, indeed, for the question of whether or not an employee contribution to the fund would be appropriate. A budgetary reserve fund would clearly form part of the public finances and, once established, it would be for the Government to decide on its deployment, subject to legislation. It is difficult to envisage on what basis an employee contribution might be sought for such a fund.

7.9 On the other hand, a public service pension fund could be seen as separate from government, being jointly secured by public service employers, serving public servants, and former public servants for the purposes of paying a particular pension scheme benefit. A direct employee contribution would reinforce the independence of the fund from government, in terms of its perception and in reality. In these circumstances, there would be a strong case for creating an independent Board of Trustees or Directors which would act in the same way as pension fund trustees in the private sector and would comprise employer, union and pensioner representatives.

7.10 In *Paragraph 6.42*, we recommend that the existing policy of pay-related pension increases should be continued, subject to the making of an additional 1% contribution by public servants towards the cost involved. We also recommend that the contribution should be lodged, along with an employer contribution, to a new pension fund which would in due course be made responsible for meeting the total cost of pension increases.

7.11 Accordingly, we recommend that as part of the process of introducing the new 1% employee contribution, the public service pensions element in the proposed National Pensions Reserve Fund should be adapted to a separate properly constituted pension fund for pension increases, structured on the basis set out in Paragraph 23.5.42 of our Report. As we discuss in the Report, the periodic and lump sum contributions for such a fund would be broadly of the same order as those implied for public service pensions under the Government's pre-funding initiative, while there would be a different profile of fund payments as between the two approaches, reflecting the different drawdown mechanisms involved.

(Paragraph 23.9.8)

Transparency in pension costs and liabilities (Chapter 24)

7.12 We outline the existing cash-based systems of accounting for public service pension costs and the shortcomings of these systems at *Paragraphs 3.16-3.17*. At present, because they are financed on a pay-as-you-go rather than a funded basis, public service pension costs are recognised in government accounting systems only when the pension benefits ultimately become payable, thereby disregarding the accruing cost of pensions for serving employees. Decisions about the recruitment of employees, improving benefit terms, making new allowances pensionable, increasing pensions coverage, as well as early retirement, have obvious pension cost implications but, usually, the full extent of these costs will only impact at some future point. Often, the department or agency which gives rise to the additional pension cost is different to that which must meet that cost in due course. Thus, as the pension cost does not affect its bottom line there is little incentive for the employer concerned to manage and control the increase in costs.

7.13 In order to address these deficiencies, the Commission recommends the adoption of an accruals-based approach to accounting for pension costs under government financial systems. We recommend that implementation of accrual accounting for pension costs should take account of the framework proposed in our Report (see Section 24.4) and be addressed in the context of ongoing reforms to government financial management systems.

(Paragraph 24.6.2)

7.14 Accrual accounting would help to make pension costs more fully transparent, and would bring to bear some of the disciplines associated with funded pension schemes. In practical terms, it could enable departments and agencies to be given greater flexibility to make decisions having long-term pension implications, on the basis that the costs involved would be met from within their own resources. For example, the recruitment of new employees would mean having to pay for the accruing cost of their pension benefits, as well as salary and PRSI costs; the cost of granting a pensionable allowance to an individual would include the consequent cost of pensioning the allowance; and the capital cost of early retirement would be met in advance by the relevant department or organisation.

7.15 The Commission also recommends that in future negotiations on changes to pension terms for any public service group or for the public service as a whole, actuarial costings of the proposed changes, specifically, the impact on contribution rates, should be obtained from the Public Service Pensions Office (see *Paragraph 7.22*). It would then be a matter for management and unions to agree how the increase in contribution rates would be apportioned as between employers and employees.

(Paragraph 24.6.4)

7.16 We recommend that actuarial reviews of public service pension schemes and of the Public Service Pension Fund should be carried out on a regular basis, ideally every three years.

(Paragraph 24.6.5)

Reforms to management, administration and communication systems (Chapter 25)

7.17 The Commission comments in *Paragraphs 3.10-3.12* on the areas in which we consider improvement is necessary in current public service pensions management, administration and communication arrangements.

7.18 The management, administration and communication of occupational pension schemes is a complex and technical area. In many of the larger funded private sector schemes, standards of service provision and administration are being continuously updated, driven by a range of factors such as the changing regulatory environment, developments in information technology, employee interest, and an increased emphasis on occupational pension as a valuable feature of employment. In some cases, pension schemes are outsourcing their administration functions.

7.19 Public service schemes have not experienced these developments to any significant extent. One of the consequences of the pay-as-you-go system is a pensions administration system that is geared primarily towards the calculation and payment of pension, rather than the provision of management information on pension costs or the communication of benefit entitlements and scheme options to serving employees. This has had implications for the resourcing of pension administration units across the public service.

7.20 Having considered the implications for the management and administration of pension schemes of the overall set of initiatives which we are recommending, we propose a new structure for the management and administration of public service pensions. One of the most important tasks to be addressed by the new structure is to plan the introduction of a new computerised pensions administration system capable of linking pension data across all public service employments. Such a system would provide the management information required for pension costing as well as the data at individual level which are necessary for effective pension communication systems.

7.21 The Commission recommends that the question of amalgamating closely similar public service schemes or of creating a single occupational pension scheme for all public servants should be examined as part of the implementation of new management and administration structures.

(Paragraph 25.3.8)

7.22 We recommend the introduction of a new centralised structure for the future management and administration of public service pensions. The structure would involve four groups or parties: the Minister for Finance, an Inter-Departmental Committee on Public Service Pensions, a Public Service Pensions Office (PSPO), and a number of Pension Support Units.

(Paragraph 25.4.1)

7.23 Representatives of the public service unions and of the PSPO could be asked to join the Inter-Departmental Committee. The expanded committee might then exercise a general role in relation to staff side pension claims, as well as considering other proposals affecting public service pension arrangements. The expanded committee might be titled the *Public Service Pensions Partnership Committee*.

7.24 The objective of the Pensions Partnership Committee would be to ensure that the wider implications, including the long-term cost implications, for all public service pension schemes of a proposed change in pension terms in any one area of the public service were fully considered, and that the basic principles of the public service pensions framework were not compromised as a result of the change. It would not be intended that the Pensions Partnership Committee form part of the standard industrial relations machinery.

7.25 The Commission notes that under the *Programme for Prosperity and Fairness (PPF)*, a Working Group of the public service unions, relevant Government Departments, and other appropriate bodies is to be established to advise on the implementation of the relevant Government decisions arising from our Report with a view to introducing, as quickly as possible, any proposed changes in public service pension arrangements, including those for low paid workers. The Commission hopes that through that process the full range of pension issues addressed by this Report can be dealt with. The Commission envisages that the Working Group should have completed its task by the expiration of the *PPF*.

(Paragraph 25.4.7)

7.26 The Commission recommends that all parties should agree to forward claims under consideration to the PSPO for costing. This would facilitate implementation of our recommendation at *Paragraph 7.15*.

(Paragraph 25.4.8)

7.27 The Commission considers that if a Public Service Pensions Partnership Committee were to be established along the lines set out in *Paragraph 7.22*, it should not become effective until the *PPF Working Group* has completed its task.

7.28 The Pension Support Units would be responsible for ensuring correct recording of data on the pension entitlements of serving public servants, the setting up of new pension cases, provision of scheme documentation, and answering queries from individual public servants and pensioners. The Units, along with the PSPO, would implement the new pensions IT/database strategy developed by the PSPO.

7.29 As outlined above, the Commission believes that a move to a centrally coordinated information and management system is necessary to address the various deficiencies which we have identified. However, we would emphasise that local input and responsibility on the part of departments and organisations would be essential to ensure the success of the new system.

7.30 In our view, the most pressing requirement in relation to pensions administration is to plan the introduction of a computerised pensions administration system for the recording of pensionable service, pensionable pay and allowances, and other relevant pension data.

7.31 We recommend the development of a specialised, computerised pensions administration system, and that introduction of the new system should be overseen by the interdepartmental committee and implemented by the PSPO, with appropriate expert assistance.

(Paragraph 25.5.4)

7.32 Consistent with our recommendations in relation to pension flexibility, we recommend the implementation of an active policy of pension scheme communication, involving the provision of user friendly documentation, an annual statement of pension entitlements, and a statement of the options available to public servants to improve their overall level of benefits and to plan for their retirement (including information on SPEARS).

(Paragraph 25.5.6)

7.33 We have suggested that questions arise as to the effectiveness of the appeal mechanisms available under public service schemes. We consider that a more transparent and independent appeals system would be to the benefit of scheme administrators and aggrieved parties.

7.34 Accordingly, we recommend the appointment of a suitably qualified individual — supported by an executive to be provided by the Minister for Finance — as an external ombudsman for public service pensions. Account should be taken of the existing remit of the Public Service Ombudsman in implementing this recommendation. In the event that a National Ombudsman for Pensions is appointed who it is intended should have a remit in relation to all pension schemes, consideration should be given to subsuming the functions of the ombudsman for public service pensions into those of the National Pensions Ombudsman.

(Paragraph 25.6.3)

8. Conclusions and overview of recommendations and impact on costs (Chapter 26)

8.1 Assessing the financial implications of the Commission's recommendations is an unusually complex task. Some proposals would add to pensions expenditure (benefits), others would reduce it, and the different proposals have different time profiles. Some of our proposals would affect expenditure in the short-term only and are rapidly self-liquidating through the passage of time, others could have enduring long-term implications for the pensions bill that are impossible to quantify precisely. For example, the Commission is confident that our recommendations on pensions administration, taken in their entirety, would introduce a more flexible and more effective way of dealing with public service pensions that could have a significant long lasting impact on pensions expenditure, on productivity in the public service and through these on overall economic performance. But exact estimation of this impact is obviously impossible. Where appropriate, specific recommendations have been costed, and the broad methodology of such costing exercises is explained in the Report.

8.2 In Table 3, we illustrate the broad impact of the Commission's main recommendations in terms of their impact on costs and savings, both in the short- and long-term.

Table 3: Assessment of impact of main recommendations on cost of public service pensions

Short-term costs	Short-term savings
Approved Early Retirement New integration formula Pensions for part-timers Funding of pension increases Pensions administration	1% contribution for pension increases

Long-term costs	Long-term savings
Approved Early Retirement New integration formula Pensions for part-timers Pensions administration	Increase in retirement age Changes in special terms Removal of professional added years 1% contribution for pension increases Improved administrative efficiency Funding of pension increases

8.3 A number of the Commission's recommendations would not have any direct implications for the future cost of pension benefits. For example, use of the Public Service Earnings Index as the basis for calculating future rates of pension increase would not result in any change in the overall cost of pension increases in the long-term; however, it would reduce administrative costs by allowing departments and agencies to pay a single rate of increase automatically to all pensioners, rather than having to examine the particular implications of each pay agreement for different pensioner groups. The recommendations in relation to cost transparency and pension scheme management and administration would increase the cost to the State of administering pension schemes, but should also contribute to improved management of schemes and to better communication of scheme entitlements. Also, the development of SPEARS would likely give rise to additional costs, particularly if the State decided to meet part of the scheme's promotional costs. However, this must be balanced against the administrative costs which the State currently bears in relation to the schemes for purchase of notional service.

8.4 Certain scheme recommendations might appear to represent benefit improvements, but at a wider level could also realise savings. For example, there would be an additional capital cost to the State for each individual availing of the Approved Early Retirement facility. However, the terms of the new facility require employers to establish that each early retirement would improve the general level of efficiency and effectiveness of the service in question. Clearly, this aspect of the facility would have to be carefully monitored and controlled if it is not to give rise to additional costs.

8.5 The recommended introduction of a 1% contribution towards the cost of pension increases offers a real long-term saving in future pension costs.

8.6 The recommendations of this Report have implications for all parties having an interest in public service pensions — the Government, public service employers, trade unions, pensioner associations, individual public servants and pensioners — as well as for the taxpayer. They may also have implications for the commercial state sector, the private sector and for the overall competitiveness of the economy generally. The recommendations which we make are the fruits of a comprehensive examination of Irish public service pension schemes, a detailed evaluation of scheme structures and benefits, and a considered analysis of how best to reconcile the legitimate concerns of the major stakeholders. Against this background, we are satisfied that the recommendations represent an integrated and cohesive long-term strategy for public service pensions, and we would place particular emphasis on the importance of maintaining the integrity and cohesion of the package of measures outlined in the Report. We are aware that, taking account of the range of entitlements currently applicable to serving staff in the public service, the changes which we propose — primarily in respect of new entrants — are less beneficial in some respects, and more beneficial in others, but it is essential that the balanced nature of our recommendations be recognised and respected.

8.7 This is a time of increasing pressure and of cutbacks in pension terms in many Western economies. The public service pension bill, financed on a pay-as-you-go basis out of general revenues, is a matter of general concern. Ireland's public service pensions are no exception. However, because the overall demographic situation is more favourable than in other countries, the national finances will be in a stronger position than others to cope with the consequences of ageing for some time. It is important that this breathing space is put to constructive use. The Commission is confident that our recommendations will help secure the long-term viability and stability of public service occupational pension schemes in Ireland.

List of Recommendations

Some members of the Commission expressed reservations in relation to certain of the Commission's recommendations. These are marked accordingly.

Chapter 15 — Retirement age and early retirement

1. The Commission considers that employees should be provided with regular and comprehensive information on their entitlements and the retirement options available to them. Structured programmes of retirement planning and counselling should be initiated so as to raise the issue with individuals well ahead of their retirement and to provide information on the options open to them.

2. We recommend that changes be made to pension terms to enable public servants who wish to do so to work at a lower level of responsibility prior to retirement without unduly affecting their pension rights. Individuals should be allowed to freeze benefits based on the salary/allowance point immediately prior to changing work pattern, and to separately accrue benefits based on the lower salary/allowance point for the period served in the new work pattern.

3. We recommend that in a context of ongoing labour shortages, some relaxation of the abatement of pension rules should be made in order to facilitate the re-employment of public servants with required expertise/skills on a contract basis after retirement.*

4. We recommend the introduction of *cost neutral early retirement*. This would allow public servants aged 50 and over (aged 55 and over in the case of new entrants) to retire with immediate payment of benefits, subject to actuarial reduction to cater for the longer period over which the benefits would be paid.*

5. We recommend that the age of retirement for new entrants with standard pension terms should be changed from age 60-65 to a single retirement age of 65, with consequential changes in the retirement ages for groups which have special retirement terms for operational reasons (see Recommendation 13).*

6. The Commission recommends that early retirement provisions should be made available — at an individual/group level — to cater for organisational restructurings, reductions in staff numbers, and as part of new performance management systems to be introduced in the public service. The existence of these provisions and the conditions applying to them should be clearly stated in pension scheme documentation provided to public servants. In view of the cost of early retirement, we recommend that it should be used only where other reasonable avenues — such as retraining and redeployment, flexible working, etc. — have been considered.

7. We recommend the introduction of an additional early retirement facility, called *Approved Early Retirement*. Early retirement under this facility would be available in respect of public servants aged 55 or over (aged 60 or over in the case of new entrants) with 20 or more years' service who consider that they are unable to make a fully satisfactory contribution, and where management accept that their early retirement would improve the general level of efficiency and effectiveness of the service in question. It would be initiated either by management or the individual public servant, and would be subject to agreement by both parties. Pension benefits under Approved Early Retirement would consist of the immediate payment of pension and retirement lump sum with no actuarial reduction.

8. In the light of the significant cost which early retirement imposes, the Commission recommends that an annual quota of Approved Early Retirements be set and that all applications across the public service be assessed at a central level. In Paragraph 24.5.3 of the Report, we suggest that alternative arrangements should be examined which would involve departments or organisations meeting the additional capital cost of early retirement from within their own resources.

9. We recommend that a review of the Approved Early Retirement facility should be carried out in five years' time, having regard to its efficacy in addressing the needs of management and staff, the level of take-up, and the development and implementation of new systems to monitor performance in the public service, including early retirement provisions.

10. The Commission recommends that the limited retirement initiatives for teachers and nurses should be continued for a further five years, and that they be included in the review referred to at Recommendation 9.

11. We recommend that a review should be carried out of procedures followed in processing ill health early retirements across the public service, with the aim of developing a consistent approach and to identify best practice.

12. A range of additional actions should be taken to address factors which have potentially negative effects on the health and performance of individuals. These include identifying and addressing the most prevalent causes of adverse stress where they occur in various public service occupations (e.g. under-resourcing, excessive work loads), developing and extending occupational health services to address health and welfare issues, and the effective use of redeployment, accompanied by retraining.

13. Based on the information available to the Commission, and taking into account our recommendation to raise retirement ages for new entrants to the public service generally (see Recommendation 5), our specific recommendations on the application of special terms for operational reasons are as follows:

(i) new entrants to those parts of the psychiatric services where special terms currently apply should in future have standard pension terms; there should be no change in the special terms (i.e. doubling of service on serving in excess of 20 years, and retirement on reaching age 55) of personnel currently employed in the psychiatric services;

(ii) new entrants to the Garda Síochána should be subject to a minimum retirement age of 55 and should be retained beyond that age, to a maximum retirement age of 60, subject to meeting certain minimum standards of health and fitness on an annual basis; there should be no change in the special terms as they are applied to members of the Garda Síochána currently in service;

(iii) in the case of the prison service, the optional facility to retire between ages 50 and 55 on achieving 30 years' service should not apply to new entrants; the new Prisons Board should examine whether, in light of developments in operational requirements in the prison service, special terms in their entirety (i.e. retirement between ages 55 and 60, and doubling of service on serving in excess of 20 years) should be removed; there should be no change in the special terms as they are currently applied to personnel now in employment;

(iv) in the case of the fire service:

(a) new entrant Firefighters should continue to be subject to a retirement age of 55, with service in excess of 20 years doubled for pension purposes;

(b) new entrant officers, who have the option to remain in employment until age 65, should have standard pension terms;

(c) new entrant Firefighters who are subsequently promoted to non-operational positions should have standard pension terms, but should receive a higher pensions credit for the period served as Firefighters (this is known as *uniform accrual*);

(d) there should be no change in special terms as they are currently applied to all serving personnel;

(v) new entrant teachers should have standard pension terms; the provision whereby teachers may retire between age 55 and age 60 (on achieving 35 years' service) should continue for all serving teachers (the limited retirement initiative for teachers is addressed in Recommendation 10);

(vi) new entrants to the Defence Forces should have special pension terms more in line with the special terms which apply to certain other public service groups, consistent with current personnel policy (see Recommendation 34 below);

(vii) having regard to the available information, and in light of the range of other recommendations made in relation to retirement age and early retirement, the Commission does not recommend the extension of special pension terms to any other public service group.*

Chapter 16 — Pensions increase policy

14. The Commission recommends that a CSO Public Service Earnings Index should be developed (along the lines set out in Paragraph 16.5.6 of the Report) for calculation twice-yearly of a single rate of pay-related increase to be paid to all public service pensioners. The implementation of the index should involve consultation with public service employers, unions and pensioner representatives. In view of the value to public servants of a guaranteed system of pay-related pension increases, the Commission recommends that all serving public servants should make an additional explicit 1% contribution of remuneration or net remuneration, as appropriate, towards the cost of pay-related pension increases. We also recommend that the State should explicitly guarantee the new system of pension increases by means of legislation and through the establishment of a Public Service Pension Fund to meet the full cost of pension increases (see Recommendation 47).*

15. We recommend that the 1% contribution towards the cost of pension increases, when it is introduced, should be lodged to the Public Service Pension Fund. The Public Service Earnings Index should be developed with a view to its implementation after the completion of the current *Programme for Prosperity and Fairness*.

Chapter 17 — Integration with State Social Insurance benefits and low levels of occupational pension

16. The Commission recommends that, in order to enhance the pension position of public servants in full PRSI class and subject to integration and who retire on relatively low levels of pay, the operation of integration in all public service schemes should be amended through the introduction of a new pension calculation formula as follows:

> Pension to be calculated using accrual rates of:
>
> 1/240th for pensionable remuneration below three times the rate of OACP, and
>
> 1/80th for pensionable remuneration in excess of this limit.

Chapter 18 — Pensions and atypical employment

17. The Commission recommends that public servants in temporary and part-time work should be granted access to public service pension schemes, provided that they are in regular or quasi-permanent employment and, in the case of part-time employees, that they work a certain minimum number of hours per week.

18. We recommend a change in the form in which integration is applied to part-time public servants from full to pro rata integration; this modification in scheme terms would result in improved occupational pensions for such employees (the change in the operation of integration recommended in Recommendation 16 would impact on the pension calculation of any part-time employees where the amount of notional full-time pensionable remuneration was less than three times the rate of OACP).

19. The Commission recommends that discussions should take place between public service unions and employers in order to arrive at a reasonable and equitable approach to the calculation of death gratuity and spouses' and children's benefits for part-time public servants. These discussions should take account of practice in private sector pension schemes and of the existing approach of public service schemes in relation to job-sharing, part-time, and contract public servants, as well as giving appropriate weighting to each individual's pattern(s) of employment. Insofar as possible, the principle of pro rata benefits should apply. In addition, particular regard should be had to the commitments entered into by the Social Partners in relation to the promotion of family friendly policies.

20. The Commission recommends that the period of reckonable service required to qualify for preserved benefits under public service schemes should be reduced from five to two years, in line with the recommendation of the Pensions Board in the National Pensions Policy Initiative. We believe this change should apply to serving staff only from a current date.

Chapter 19 — Pension scheme flexibility

21. The Commission recommends the introduction, in consultation with the public service unions, and having regard to the position of existing AVC schemes, of a single AVC-type scheme for the public service as a whole. We recommend that this scheme should be established and operated broadly along the lines envisaged in Chapter 19 of the Report, and called the Scheme for Public Employees' Additional Retirement Savings (SPEARS). SPEARS should include a savings account facility and a lump sum death benefit facility. In addition to providing the options available under existing AVC schemes, SPEARS should incorporate a new purchase arrangement to enable the use of the savings account at, or prior to, retirement to purchase an amount of public service pension, which would be increased in line with public service pensions generally.

22. We recommend that the structure of SPEARS (AVC, group PRSA, or other) should be decided once the framework for PRSAs has been put in place. However, in the event that the scheme were set up initially as an AVC under trust deed, we recommend that the independent trustees of the scheme should include representatives of public service unions and employers. It might be considered desirable to convert SPEARS into a group PRSA in due course, and this matter should be decided by the State at the appropriate time, in consultation with the public service unions.

23. The Commission recommends that existing schemes for the purchase of notional service should be phased out, the precise period involved to be determined by the State, in consultation with the public service unions, based on the level of take-up of the schemes in comparison with the new SPEARS option.

24. SPEARS should include an option at retirement to use any or all of the retirement lump sum to purchase additional pension.

25. We recommend that the State should consider meeting part of the administrative cost of SPEARS, in particular, the cost of promoting the scheme in the context of the phased removal of the schemes for purchase of notional service.

Chapter 20 — Dependants' benefits

26. In Recommendation 51 below, we recommend that, for reasons of administrative efficiency, consideration should be given to drawing up a single public service occupational pension scheme and/or rationalising the large number of separate schemes currently in existence. We recommend that spouses' and children's schemes should be included in that process. Furthermore, we do not see that there is a value in maintaining spouses' and children's schemes separately from main pension schemes.

27. The Commission recommends that a limited appeals process for spouses' and children's scheme membership options be established to examine individual cases and to allow appeals that meet any one of the following criteria:

(i) where there is no evidence that an option was provided to the individual public servant in the first place;

(ii) where there is medical evidence to indicate that the person making the decision not to join the scheme was of sufficiently unsound mind not to appreciate the consequences of his or her decision;

(iii) where a member of the original scheme declined to join the revised scheme in circumstances where there would have been no reasonably foreseeable adverse financial consequences for the individual (in terms only of his or her scheme contributions) had he or she instead opted to join the revised scheme.

28. The Commission considers that an option to join spouses' and children's schemes in the case of teachers (other than VEC teachers covered by the Local Government Superannuation Scheme) should proceed on the basis of the management offer made at the Teachers' Conciliation Council (i.e. an option to join the revised schemes is to be offered to national and secondary teachers in the original schemes).*

29. We recommend that the existing provisions of public service spouses' and children's schemes should be modified to allow payment of a survivor's pension to a financially dependent partner in circumstances where there is no legal spouse and where a valid nomination has been made. We would suggest that the system of nomination to be introduced on foot of this recommendation should provide for regular review, preferably as part of the annual issue of the statement of pension entitlements (see Recommendation 56). We would envisage that the nomination form would seek details on the nature and extent of the financial dependency and that it would state that documentary evidence of financial dependency would be required should the member predecease his or her partner. We consider that the form should also state that a nomination, assuming there was no legal spouse, would not be binding on the scheme administrators, and that a pension would not be paid where there was no valid nomination in place.†

30. The Commission recommends the removal of the provision which requires a spouse's pension to cease on grounds of remarriage or cohabitation.‡

31. The Commission recommends that the Article 15(5) pension payable in certain circumstances under the Garda Síochána Pensions Order, 1981 to spouses of deceased members of the Force should be discontinued in the case of new entrants to the Force.

32. The Commission recommends that where a dependent child is orphaned and both parents are members of the same spouses' and children's scheme, two children's pensions should be payable. We note that the cost of any change would be minimal.

33. We recommend that an appropriate system for nomination of death gratuity should be introduced into public service pension schemes. It should provide for annual review of the nomination as part of the annual issue of the statement of pension entitlements. Preferably, and subject to legal advice, this change should be introduced by means of primary legislation in order to ensure that due regard is had to the property rights of the spouses of public servants.

Chapter 21 — Defence Forces Pension Schemes

34. The Commission makes the following recommendations in relation to the design of a new pension scheme for new entrants to the Defence Forces:

(i) consistent with our recommendation for the public service schemes generally, the pension scheme should have a defined benefit final salary structure, integrated with the Social Insurance system. Pension and lump sum should be based on final remuneration (integrated as appropriate) and service at retirement;

(ii) maximum retirement ages would be as laid down under the personnel policy and maximum pension would accrue over a period of 30 years. However, the Commission recommends that pension should not be payable earlier than age 50. Preservation of pension benefits should apply in the case of personnel who, having two or more years' service, leave service earlier than age 50;

(iii) on retirement/discharge earlier than age 50 there should be an appropriate severance arrangement in certain circumstances. This should only be made available on a limited and selective basis in the light of specific personnel and operational requirements;

(iv) allowances in the nature of pay should be included in the definition of pensionable remuneration, consistent with policy in other public service pension schemes;

(v) the same general pension provisions should apply to officers and enlisted personnel;

(vi) in line with our recommendations on pension contributions generally (see Section 22.2 of the Report), the pension contribution should be 3% of remuneration, plus $3\frac{1}{2}$% of net remuneration (this already applies to officers commissioned after 6 April 1995);

(vii) as a separate matter, we consider that the existing provisions in relation to occupational injuries under the Army Pensions Acts should be examined, having regard, particularly, to the many substantial changes which have taken place since their introduction;

(viii) new entrants to the Army Nursing Service and the Chaplaincy Service should have standard public service pension terms and retirement ages.

35. The Commission recommends that the new pension schemes for new entrants should be drawn up as soon as possible, with appropriate consultation involving the Defence Forces' representative bodies. Furthermore, the Commission recommends that, having regard to the advantageous nature of the existing Defence Forces Pension Schemes considered in the round, no fundamental modifications to the pension terms of serving personnel should be made.

Chapter 22 — Other issues relating to pension terms

36. While there may be a logic to *group-specific* contribution rates, which are the practice in some public service schemes abroad, the Commission considers that, on balance, it would be preferable to continue the application of a standard rate of employee contribution for new entrants across all public service groups.

37. We recommend that to the extent that any future pay determinations for public service grades are carried out by means of a comparison with equivalent positions in the private sector, any adjustment which might be made to reflect the value of public service relative to private sector pension arrangements should take into account the employee contribution being made by the public servants concerned.

38. Having weighed the considerations for and against, the Commission is of the view that the schemes of notional added years are no longer appropriate as a component in public service pension arrangements and, accordingly, recommends their abolition for new entrants. In that context, consideration should be given to the offer of other forms of recruitment incentive.

39. The Commission recommends that (apart from the special rules applying to organisations covered by the Public Service Transfer Network) public service schemes should operate the same arrangements as apply to private sector occupational schemes generally in relation to the accepting of transfer payments in respect of previous employments.

40. In view of the increasing numbers entering the public service in Ireland who have served previously in the UK public service, we recommend that the relevant authorities here take up with the relevant authorities in the UK the question of amending the respective transfer schemes so as to enable individuals who have built up pension entitlements in the public service in one jurisdiction to have the benefit of those entitlements transferred to the other jurisdiction and given appropriate credit for the purposes of the pension scheme applicable in the other jurisdiction. We recognise that any such arrangements could only be made where there was an agreement to operate them on a reciprocal basis and that the arrangements would have to reflect the overall parameters of the schemes. (In practice therefore, it is likely that any such changes would only apply in relation to future transfers and that the service credit would be the actuarial equivalent of the accrued entitlements.)

41. The Commission recommends that in the context of further public service reforms which would have the effect of removing points of difference between established and non-established type employment in the public service, the pension terms for non-established employees (new entrants) should be amended to bring them into line with those of established employees (new entrants).

42. We recommend that the reckoning of variable pensionable allowances under the *three-year averaging rule* should, subject to any necessary adjustment or amendment of the Revenue limits, be changed to an average of the variable pensionable allowances received in the best three consecutive years in the ten years preceding retirement, as uprated to the date of retirement in line with the Public Service Earnings Index (see Recommendation 14). Averaging would not apply in this way in cases in which salary on promotion had effectively taken the place of allowances received in the ten years preceding retirement, or where the allowances in question had been incorporated into the pay scale. There would be no change in the averaging rules as applied to salary.

43. We recommend that, as a general principle, pension terms and provisions which now appear outdated or which add to the complexity of pension schemes without conveying any significant advantage in terms of efficacy, fairness or cost should be deleted or modified as appropriate

44. The Commission recommends that compound interest in the case of refund of marriage gratuities, payment of outstanding employee contributions, and recovery of financial loss to the Exchequer should be reduced from a rate of 6% per annum to a rate of 4% per annum from a current date, and that the rate should be reviewed as a matter of course.

45. We recommend the introduction of a provision enabling marriage gratuities to be repaid over a fixed period of time (say, no more than 10 years) on the basis of regular deductions from salary, rather than by specific minimum instalments such as one month's gross pay. In such situations, compound interest would continue to be applied to the reducing balance.

46. We recommend that, where it might be deemed appropriate, there should be an option to consider the introduction of funded defined contribution type schemes on a basis that was mutually acceptable to the organisations concerned and to the relevant public service unions. The rates of contribution by employer and employees should be designed so as to provide benefits which are comparable with standard public service pension benefits. Public servants in such schemes who subsequently move to areas of the public service where defined benefit pension terms apply should have the option of transferring the balance on their defined contribution accounts into SPEARS (if introduced) or the main pension scheme.

Chapter 23 — Partial funding of public service pensions

47. We recommend that as part of the process of introducing the new 1% employee contribution, the public service pensions element in the proposed National Pensions Reserve Fund should be adapted to a separate properly constituted pension fund for pension increases, structured on the basis set out in Paragraph 23.5.42 of the Report. As we have shown, the periodic and lump sum contributions for such a fund would be broadly of the same order as those implied for public service pensions under the Government's pre-funding initiative, while there would be a different profile of fund payments as between the two approaches, reflecting the different drawdown mechanisms involved.

Chapter 24 — Transparency in pension costs and liabilities

48. The Commission recommends the adoption of an accruals-based approach to accounting for pension costs under government financial systems. We recommend that implementation of accrual accounting for pension costs should take account of the framework proposed by the Commission (see Section 24.4 of the Report) and be addressed in the context of ongoing reforms to government financial management systems.

49. The Commission recommends that in future negotiations on changes to pension terms for any public service group or for the public service as a whole, actuarial costings of the proposed changes, specifically, the impact on contribution rates, should be obtained from the Public Service Pensions Office (see Recommendation 52). It would then be a matter for management and unions to agree how the increase in contribution rates would be apportioned as between employers and employees.

50. We recommend that actuarial reviews of public service pension schemes and of the Public Service Pension Fund should be carried out on a regular basis, ideally, every three years.

Chapter 25 — Reforms to management, administration and communication systems

51. The Commission recommends that the question of amalgamating closely similar public service schemes or of creating a single occupational pension scheme for all public servants should be examined as part of the implementation of new management and administration structures.

52. We recommend the introduction of a new centralised structure for the future management and administration of public service pensions. The structure would involve four groups or parties: the Minister for Finance, an Inter-Departmental Committee on Public Service Pensions, a Public Service Pensions Office, and a number of Pension Support Units.

53. The Commission notes that under the *Programme for Prosperity and Fairness* (*PPF*), a Working Group of the public service unions, relevant Government Departments, and other appropriate bodies is to be established to advise on the implementation of the relevant Government decisions arising from our Report with a view to introducing, as quickly as possible, any proposed changes in public service pension arrangements, including those for low paid workers. The Commission hopes that through that process the full range of pension issues addressed by this Report can be dealt with. The Commission envisages that the Working Group should have completed its task by the expiration of the *PPF*.

54. The Commission recommends that all parties should agree to forward claims under consideration to the Public Service Pensions Office for costing. This would facilitate implementation of Recommendation 49.

55. The Commission recommends the development of a specialised, computerised pensions administration system, and that introduction of the new system should be overseen by the interdepartmental committee and implemented by the Public Service Pensions Office, with appropriate expert assistance.

56. Consistent with our recommendations in relation to pension flexibility, we recommend the implementation of an active policy of pension scheme communication, involving the provision of user-friendly documentation, an annual statement of pension entitlements, and a statement of the options available to public servants to improve their overall level of benefits and to plan for their retirement (including information on SPEARS).

57. We recommend the appointment of a suitably qualified individual — supported by an executive to be provided by the Minister for Finance — as an external ombudsman for public service pensions. Account should be taken of the existing remit of the Public Service Ombudsman in implementing this recommendation. In the event that a National Ombudsman for Pensions is appointed who it is intended should have a remit in relation to all pension schemes, consideration should be given to subsuming the functions of the ombudsman for public service pensions into those of the National Pensions Ombudsman.

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* *Reservations were entered in relation to these recommendations by Senator Joe O'Toole, Ms Rosheen Callender and Mr Dan Murphy.*

† *A reservation was entered in relation to this recommendation by Mr Joe McGovern and Mr John Cullen.*

‡ *A reservation was entered in relation to this recommendation by Mr Joe McGovern, Mr John Cullen and Ms Anne Vaughan.*

Reservation by Senator Joe O'Toole, Rosheen Callender and Dan Murphy

1. We were unable to reach agreement with the other members of the Commission on certain aspects of the Final Report of the Commission.

2. Our signatures to the Final Report are, therefore, subject to the reservations set out hereunder.

3. We consider that most of the report and the recommendations set out in the report are valuable contributions to the whole debate on Public Service Pensions, and the development of policy thereon.

4. In particular, we welcome the thrust of the Report which, while acknowledging the significant increase in pension costs over the period ahead, places considerable emphasis on securing the terms of Public Service Pensions for current and future pensioners and eschews alternative approaches which might have called the benefits into question in the future as has happened in the case of certain other countries when confronted by similar problems.

5. Some of the individual Recommendations are particularly valuable. In this regard, we would make particular mention of:

- the retention of a defined benefit pension structure;
- the improvements in the occupational pensions of lower-paid public servants as a result of the adjustment recommended in ''integration'';
- the extension of pension coverage to atypical workers;
- the introduction of a new ''AVC-type'' Scheme (''SPEARS'') to provide for greater flexibility in relation to pensions, lump sums, retirement ages, etc.;
- the establishment of a fund to guarantee post-retirement pension increases;
- improvements in administration and, in particular, the development of better systems for recording service details and communications to members.

6. However, there are some significant recommendations which we cannot support.

Retirement Ages

7. We cannot agree to the Recommendation that standard retirement ages should be increased. The current standard retirement ages of 60 to 65 years are not out of line with those applying *de facto* in the Private Sector or in the Public Services of other countries. In addition, the Social Insurance Retirement pension is payable at age 65.

8. While we can see the desirability of increasing the age at which some public servants actually retire, we consider that this would be most effectively achieved by providing incentives for staff to stay in employment, e.g. by being able to accrue more than 40 years' service for pension purposes. This would achieve the purpose of encouraging staff to stay in service without imposing a new and higher retirement age on a compulsory basis for all. In our view, the aim should be to provide greater flexibility by giving public servants a greater degree of choice in relation to their retirement age.

9. In the case of public service groups with special retirement terms, we are not satisfied that the Commission has been in a position to carry out a substantive and effective examination of the appropriateness of these special terms in current circumstances and, therefore, we are not in a position to support these recommendations. It seems to us that, if there is a view on the part of employers that some of these special terms should be reviewed in the light of current circumstances, then that is an issue they need to discuss with the Trade Unions representing such staff. Trade Unions, in turn, would be better placed to engage in such discussions after the introduction of ''SPEARS'' and other provisions enabling public servants to provide for special terms on an individual basis.

10. In addition, the failure of the Commission to recommend that public servants (on standard terms) who have completed 40 years' service should be allowed to retire on full pension without having attained 60 years of age, when put in conjunction with the fact that service over 40 years is not recognised for pension purposes, is a serious shortcoming in the Recommendations of the Commission.

Proposed 1% Contribution

11. While we welcome, in general terms, the recommendations for the establishment of a Public Service Pensions Index and the recommendation, through the use of this mechanism, for the maintenance of the system of pension increases by reference to the pay increases of serving staff, we are opposed, at this stage, to the proposal that this should be associated with an explicit contribution of a further 1% of pensionable pay. As we see it, this is an issue which would be best left over for consideration in the context of the Pay Reviews by the Benchmarking system set out in the *Programme for Prosperity and Fairness*.

Dependants' Benefits

12. As regards dependants' benefits, while we can see the difficulty of offering a further general option for staff (and others) to join the Spouses' and Children's Scheme, we consider that any group who have not had a second option should be afforded same now, as a final option, on the same terms as applied in other cases.

Contributory and ''Non-Contributory'' Schemes

13. The Commission has noted that the vast bulk of Superannuation Schemes in the Public Service are contributory schemes which involve a staff contribution of 5% of pay for personal pension. In the case of those schemes which are ''non-contributory'', there is an implicit contribution of 5% which is arrived at by reducing the pay of the staff involved to a gross figure which is 95% of the rate applicable to corresponding grades in contributory schemes. This applies now only in the case of staff recruited before 1995. The effect of the schemes being ''non-contributory'' is that the pension entitlements are also 5% less than those of their counterparts who are in explicitly contributory schemes. This is a glaring anomaly and one which we consider that the Commission should have removed by recommending that the ''non-contributory'' schemes should be converted into explicitly contributory schemes and uprating the gross salary accordingly.

Reservation by Joe McGovern and John Cullen

Dependants' Benefits

1. Unlike private sector schemes, the spouses' and children's schemes in the public sector are statute based. As such it would be inappropriate to introduce provisions in those schemes which move ahead of the law generally on family units based on marriage. The recommendations of the Constitutional Review Group are being considered by an all-party Oireachtas Committee and the Commission should not anticipate any legislative proposals from that Committee.

2. The provision which requires spouses' pensions to cease on remarriage or cohabitation should be retained, consistent with the provisions relating to the Social Welfare widow's/widower's contributory pension.*

* Anne Vaughan also supported this reservation.

Glossary of principal terms used

The main sources used for the pension related definitions below are The Pensions Board, *Trustee Handbook* (1998), Finucane K. and Buggy, B., *Irish Pensions Law and Practice* (1996), and Kenny, P., *Understanding Pensions: The Friendly Guide to Pension Schemes* (1994).

Abatement	The practice of reducing the rate of occupational pension to take account of salary payable on employment subsequent to retirement, or other occupational or state pension entitlements.
Accruing Pension Cost	Represents the cost to be met at some future date of the pension benefits earned by the employees during the period of account.
Accrued Pension Liabilities	The present value of all pension liabilities accrued to a specific date using the generally accepted principle that pension benefits should accrue over the period of employment or scheme membership giving rise to these benefits.
Accrual Rate	The rate at which rights build up for each year of pensionable service in a defined benefit scheme, e.g. 1/80th and 3/80ths for pension and lump sum respectively in the public service.
Accrual Accounting	Method of accounting which records expenditure as it is incurred (as opposed to when it is paid) and income as it is earned (as opposed to when it is received).
Actuarial Assumptions	In a defined benefit scheme, assumptions such as those relating to investment return, price inflation, salary increases, mortality and morbidity, which the actuary employs in carrying out an actuarial valuation or other actuarial calculation.
Actuarially Reduced Pension	A provision which enables pension and lump sum to be paid earlier than normal retirement age. Benefits are reduced because (i) fewer contributions have been paid and those which have been paid have been invested for a shorter period and (ii) the payment of the pension starts earlier, the average expectation of life is longer, leading to a longer period of payment.
Actuarial Valuation/Review	An investigation by an actuary into the ability of a pension scheme to meet its pension promise. This has two purposes. Firstly, the actuary will calculate a recommended contribution rate which will allow the scheme to meet its future liabilities. Secondly, it is needed so that the actuary can establish the ability of the existing assets of the fund to meet its accrued

	benefits and complete an actuarial funding certificate. In unfunded public service schemes, an actuarial review focuses primarily on cashflow projections, i.e. an estimate of pensions outgo and contribution income for future years on the basis of actuarial assumptions.
Added Years	See *Notional Added Years*.
Additional Voluntary Contributions (AVCs)	The extra contributions which an occupational pension scheme member can decide to make to an external financial institution, with the aim of increasing his or her retirement and/or death benefits. AVCs are often provided for in a separate scheme from the main pension scheme.
Annuity	Series of payments made at specified intervals for life, for a stated period of time, or until a specified event occurs; it is usually secured by the payment of a single premium to an insurance company.
Appropriation Account	An end of year account of a department's spending of the moneys voted by the Dáil, which compares the Supply Estimate (down to subhead level) with actual payments made and receipts brought to account and explains any substantial differences.
Atypical Employment	Employment other than on a full-time permanent basis, i.e. part-time, temporary, contract or seasonal employment.
Bridge Jobs	Part-time or temporary employment that create a more gradual transition from full-time work to retirement.
Cash Accounting	The primary system of government accounting which aims to record cash receipts and cash payments actually received and paid during the period of account. This is the alternative to an accruals system of accounting.
Commutation	The replacement of a series of future pension payments by an immediate lump sum. The exchange of pension for immediate cash is regulated by the Revenue Commissioners.
Conciliation and Arbitration Schemes	Conciliation and Arbitration schemes are agreed between management and unions for the purpose of dealing with claims and proposals relating to the salaries and other emoluments and the conditions of service of employees.
Constant Price Terms	In the actuarial review of public service pensions presented in this Report, benefit outgo and contribution income projections have been prepared in constant (1997) prices.

	This means that any trends in the projections exclude the impact of future price inflation.
Contributory Scheme	A pension scheme which requires contributions from active members.
Coordination	Term sometimes used in place of integration in public service pension schemes; see *Integration.*
Deferred Benefits	Term sometimes used in place of preserved benefits; see *Preserved Benefits*.
Defined Benefit Scheme	A scheme in which the pension and other benefits which will be paid to the member and/or the member's dependants are clearly stated or defined in the scheme rules. Where the benefits are based on salary at retirement, it is known as a Final Salary Scheme.
Defined Contribution Scheme	Also known as a Money Purchase Scheme. A scheme where the rate of contribution (employer and, if contributory, member) is defined and where the member's pension is determined solely by reference to the contributions paid into the scheme by or on behalf of the member and the investment return earned on those contributions.
Dependants' Benefits	Benefits provided to the dependants of a pension scheme member in case of death while in employment or death after retirement. In the public service, dependants' pensions are usually provided under separate schemes to the main pension schemes, known as spouses' and children's contributory pension schemes. In the case of death-in-service, a death gratuity is payable under the main pension schemes.
Disclosure of Information Regulations	Regulations issued under the Pensions Act, 1990 requiring the disclosure of specified information about pension schemes and their benefits to interested parties.
Discount rate	For funded pension schemes, the discount rate is the expected future rate of investment return that will be achieved on the pension scheme's assets.
Early Leaver	A person who leaves employment before retirement age. An early leaver having more than five years' service is usually entitled to preserved benefits.
Early Retirement	The retirement of a member with immediate retirement benefit before normal pensionable age. The benefit may be reduced because of early payment. See also *Actuarially Reduced Pensions* and *Ill Health Early Retirement.*

Emoluments/Allowances	Benefits in cash or in kind which are additional to basic salary, e.g. allowances for the conditions under which work is done such as shift premia or higher duties.
Employee Contributions	Contributions made by an employee under a contributory pension scheme.
Established Civil Servants	Civil servants recruited following the holding of a competition by the Civil Service Commission. They are permanent employees and their employment can only be terminated by Government.
Fast Accrual	See *Special Terms*.
Final Remuneration	See *Pensionable Remuneration*.
Final Salary Scheme	See *Defined Benefit Scheme*.
Funding	The provision in advance for future pension liabilities by setting aside money in a trust, which is separate from the employer's business, to finance the payment of benefits when they arise.
Hybrid Scheme	A scheme which combines the features of two or more pension structures. For example, the scheme might provide for some benefits to be calculated on a defined benefit basis and the balance on a defined contribution basis.
Ill Health Early Retirement	Retirement on medical grounds before normal pensionable age. The benefit payable in these circumstances may be enhanced. In the public service, the enhancement consists of an award of notional service of up to 10 years (usually, six and two-thirds years), calculated by reference to the length of actual service given and potential service to retirement.
Integration	The system of taking into account all or part of the benefits payable by the State under the Social Insurance system. The most common method of operating an integrated pension scheme is by salary offset — in public service schemes, the deduction of a Social Insurance offset of twice the rate of OACP is done before calculating pension benefits.
Life Expectancy	The average period that a person at a specific age, in a known state of health, may be expected to live, derived from statistics for the population at large. Of particular relevance in the actuarial review of pension schemes.
Marriage Gratuity	Gratuity awarded in lieu of any other pension benefit to a public servant who resigns on, shortly before, or within two

years after the date of marriage, providing he or she was appointed from a competition advertised prior to 1 February 1974.

Model Schemes

Issued by the Department of Finance as a basis for drawing up pension schemes and scheme amendments by public service bodies and state companies so as to conform with the Civil Service Pension Scheme.

Modified PRSI Class

Special lower rate of PRSI applicable to the majority of public servants who as a result have limited Social Insurance cover and are not entitled to Social Insurance pensions. With effect from 6 April 1995, newly appointed public servants are in full PRSI class and are entitled to the full range of Social Insurance benefits.

Money Purchase Scheme

See *Defined Contribution Scheme*.

National Pensions Policy Initiative (NPPI)

The objective of NPPI, which was jointly sponsored by the Pensions Board and the Department of Social, Community and Family Affairs, was to facilitate national debate on how to achieve a fully developed national pension system and to formulate a strategy and make recommendations for actions needed to achieve this system. The Pensions Board report on the Initiative, *Securing Retirement Income*, was published in May 1998.

Net Remuneration

Under public service schemes, this is defined as current salary plus pensionable emoluments less twice the maximum rate of Social Insurance OACP to a single person with no dependants. Part of employee contributions are calculated on net remuneration.

Net Pensionable Remuneration

Pensionable salary plus pensionable emoluments at date of retirement less twice the maximum rate of Social Insurance OACP payable to a single person with no dependants. Net pensionable remuneration is used in the calculation of retirement pension under public service schemes. It is adjusted upwards for the calculation of spouses' and children's pensions by deducting once rather than twice the maximum rate of OACP.

New Entrant Contribution Rate

In the context of unfunded public service schemes, the percentage of salary plus pensionable allowances which it is estimated (based on actuarial assumptions) would be required to fund the existing pension benefits for typical new entrants to the public service. The rate reflects the terms and conditions applying to the new entrant and is inclusive of member contributions.

Nomination	The naming by a member of a person or persons to whom he or she wishes any death benefit to be paid in the event of his or her death. This will not usually be binding on the trustees. Also called a Wishes Letter.
Non-Contributory Scheme	A scheme which does not require contributions from active members, i.e. the employer is liable for all the contributions needed to support the scheme.
Non-established Civil Servants	Civil servants employed in a whole-time capacity by a Government Department or office who are not established civil servants. They are often employed in a situation where the long-term necessity of a particular position is not obvious, or where it is deemed desirable that personnel should undergo a trial period in a non-established capacity before being appointed in an established capacity. Non-established civil servants may be dismissed by the Minister of the relevant department.
Normal Retirement Age	The age by reference to which the normal retirement date is determined.
Notional Added Years	Any years of pensionable service added to actual service for the purpose of calculating pension scheme benefits. Normally used to describe the additional years of pensionable service awarded to professional, technical or specialist public servants for pre-recruitment qualifications and/or experience. (See also *Purchase of Notional Service* and *Ill Health Early Retirement*.)
Notional Fund	Mechanism sometimes used by unfunded schemes to facilitate the charging of public service employers for the accruing pension costs of their employees.
Occupational Pension Scheme	This is formally defined in the Pensions Act as a scheme which is approved under the 1972 Finance Act, or the 1976 Income Tax Act, or whose approval has been applied for to the Revenue Commissioners. The term *Occupational Pension Scheme* is generally used to distinguish job-related pension schemes from State Social Welfare Schemes.
Officer/Non-Officer	The terms *officer* and *non-officer* have particular legal implications in the local authority structure — the two classes of employees are broadly equivalent to established and non-established civil servants.
Old Age (Contributory) Pension (OACP)	A pension payable from age 66 under the Social Insurance system as a result of the payment of the appropriate level and number of PRSI contributions.

Pay Parity	The principle generally followed in public service schemes where pensions are increased in line with the pay of serving public servants.
Pay-as-you-go	The method of financing the cost of scheme benefits out of the employer's cash flow, where no advance funding of benefits is made. This is often the approach adopted to finance occupational pension schemes run by the State.
PCW Restructuring Agreements	Agreements made under the local bargaining element of the *Programme for Competitiveness and Work*.
Pension Scheme Structure	The structure of benefits and contributions under an occupational pension scheme — see *Defined Benefit*, *Defined Contribution*, and *Hybrid Scheme*.
Pension Terms	The rules and conditions which govern the payment of pensions under a pension scheme.
Pensionable Emoluments (Allowances)	In public service schemes, Pensionable Emoluments include allowances in the nature of pay, but do not include overtime, gratuities, or expense payments. Pensionable Emoluments are averaged over the final three years of service.
Pensionable Remuneration	The aggregate of pensionable salary and pensionable emoluments.
Pensionable Salary	In public service schemes, the salary payable on the last day of pensionable service, except in case of promotion in the final three years of service, in which case salary is averaged over the final three years of service.
Pensionable Service	The period of service which is taken into account for the purpose of calculating pension benefits. In the public service, pensionable service may include service purchased under the purchase scheme, notional added years, and service transferred from other public service employments, etc.
Pensions Act	The Pensions Act, 1990, as amended, is the principal legislation under which occupational pension schemes are regulated.
Pensions Board	The statutory body established under the Pensions Act to monitor and supervise the operation of the Pensions Act and pension developments generally.
Preservation	The granting by a scheme of preserved benefits, in particular, in accordance with minimum requirements specified by the

	Pensions Act. Preservation has been available in public service schemes since the mid 1970s.
Preserved Benefits	Benefits payable at a future date to or in respect of a member who has left the scheme prior to normal retirement age. Where preservation applies under a public service scheme, all pensionable service is covered. Certain restrictions apply in the case of schemes covered by the Pensions Act.
Personal Retirement Savings Account (PRSA)	PRSAs, as recommended under the NPPI, are to be a new type of pension vehicle aimed at meeting the needs of a flexible labour market. A PRSA will be an investment account owned by an individual which will hold units in investment funds. It will be managed by an approved PRSA provider and may be transferred from one provider to another. It is expected that PRSAs will be available as a pension option from 2001.
Pro Rata Pension Benefits	A formula which produces a pension for a part-time employee proportionate to the hours worked of a full-time employee, e.g. a part-time employee working half the hours of a full-time employee will accrue a pension entitlement which bears the same relationship to that of a full-time employee as the number of hours worked, i.e. one-half.
Public Service	The public service comprises the civil service, the local authorities, the health services, the Defence Forces, the Garda Síochána, the education sector and non-commercial state-sponsored bodies.
Public Sector	The public service plus the commercial state companies.
Purchase of Notional Service	Self financing scheme which enables a public servant, subject to certain conditions, to purchase additional years of service by reference to a shortfall in maximum pensionable service of 40 years at retirement age.
Remuneration	The aggregate of salary plus emoluments.
Restructuring Agreements	See *PCW* Restructuring Agreements.
Retained Benefits	A term used by the Revenue Commissioners to denote retirement or death benefits in respect of an employee's earlier service with a former employer or an earlier period of self-employment. These may have to be taken into account in computing maximum approvable benefits.
Revenue Rules/Limits	The benefit and contribution structure to be complied with for the purposes of securing approval of the pension scheme

	by the Revenue Commissioners under the Finance Act, 1972. (A summary of the principal requirements is set out in Appendix 12.1.)
Scheme for Public Employees' Additional Savings (SPEARS)	Single AVC-type scheme recommended for the public service as a whole (see Chapter 19).
Social Insurance/ Social Security System	State system which provides an income support system to cover insured workers for a variety of life contingencies for which they would otherwise find it difficult, if not impossible, to provide on an individual basis. Entitlement to such benefits is derived by virtue of payment of an appropriate number of PRSI contributions.
Social Welfare Offset	See *Integration*.
Social Welfare System	A term used to describe the overall welfare system comprising Social Insurance, Social Assistance and universal payments such as child benefit.
Special Terms	In a number of areas in the public service enhanced pension terms apply for operational reasons. In most cases, this involves *fast accrual*, i.e. doubling years of service in excess of 20 thus enabling a person to qualify for maximum pension entitlement after 30 years. A lower maximum retirement age than the norm usually applies.
Spouses' and Children's Pension Scheme	See *Dependant's Benefits*.
Standard Pension Terms	Used in a public service context to denote the pension terms applied to the generality of public servants (i.e. annual accrual rates of 1/80th and 3/80ths for pension and lump sum, retirement at age 60-65, etc.).
Strategic Management Initiative	A process of structural reform of the public services commenced in February 1994 which addresses three key areas: the contribution public bodies can make to national development, the development of a customer focus for the public service, and the effective use of resources.
Supplementary Pension	Under public service schemes, a supplementary pension is payable in respect of periods during which the pensioner is not employed in any capacity which involves a Social Insurance contribution and, due to causes outside his or her control, fails to qualify for Social Insurance benefit or qualifies for benefit less than the maximum personal rate of OACP.
Transfer of Service	The transfer of benefit entitlements from one occupational scheme to another following a change in employment.

Transfer Payment	A payment from one pension scheme to another, or to an insurance company to purchase a buy-out bond, in lieu of the benefits which have accrued to the member under the scheme. In this form, it specifically refers to transfers made under the preservation requirements of the Pensions Act.
Trustee	An individual or company which alone or jointly becomes the legal owner of property to be administered for the benefit of someone else (the beneficiaries), in accordance with the provisions of the document creating the trust and the provisions of trust law generally and the Pensions Act. Under the Pensions Act the term *trustees of a pension scheme* has a broader meaning which enables administrators of scheme not established under trust (such as public service schemes) to be covered within the definition.
Unfunded Scheme	An arrangement or benefit where no advance financial provision has been made (see *Pay-as-you-go*).
Unsocial Hours Allowances	Payments made to certain public service groups as an addition to salary in respect of attendance at night, weekends, and public holidays.
Vesting Date	In the context of a pension fund, the vesting date marks the commencement of the pension fund's liability to meet the future cost of the pension benefits which are earned or accrued after the commencement date.
Vesting Period	This is the period of time a person must be in membership of a pension scheme before being eligible to qualify for pension benefits. In the public service, the vesting period is five years.
Voluntary Early Retirement (VER)	An arrangement sometimes offered to allow employees volunteer to retire earlier than the normal age of retirement, usually without actuarial reduction of benefits. Sometimes enhancement of accrued pension entitlements is offered. VER schemes have been used in the public service as a means of reducing staff numbers and to facilitate restructuring. See also *Early Retirement*.
Vote	A coherent area of government expenditure which is the responsibility of a single Government Department or office which is in turn accountable to the Dáil for the expenditure shown.

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PART I

Introduction

CHAPTER 1

Introduction

1.1 Introduction

1.1.1 The Commission on Public Service Pensions was established in February 1996 to examine and report on the occupational pension arrangements of public servants. The Commission made an Interim Report in August 1997; we now present our Final Report.

1.1.2 This Chapter sets out the background to the establishment of the Commission. It lists a number of issues which were referred to the Commission and details other relevant developments occurring during the review period. Finally, it outlines the approach and procedures followed by the Commission in carrying out our deliberations and identifies the main issues addressed in the Report.

1.2 Background

1.2.1 The establishment of a Commission on Public Service Pensions was announced by the Government in a joint Government/ICTU Statement on 13 July 1995. The Commission's membership and terms of reference were announced by the Minister for Finance, Ruairi Quinn TD, on 11 February 1996.

1.2.2 The Commission was established at a time when a number of public service groups were seeking improvements in their pension arrangements and concern was growing generally about the emerging cost of public service pension schemes. The Commission's Report represents the first comprehensive examination of pensions for the public service since the foundation of the State. At the present time, there are approximately 203,000 pensionable public servants — employed in the civil service, prison service, local authorities, Garda Síochána, Defence Forces, education and health sectors, and non-commercial state-sponsored bodies — and approximately 77,000 public service pensioners.

1.2.3 The formal terms of reference of the Commission were:

To examine and report on the pension terms of public servants employed in the Civil Service (non-industrial and industrial), Defence Forces, Gardaí, Education, Health and Local Authority Services,[1] having regard to

(1) the present and future costs arising under the schemes financed by the Exchequer;

(2) claims for improvements in existing scheme benefits, including claims for voluntary early retirement;

(3) changes in the working environment and conditions of employment of public servants since the schemes were introduced; and

(4) the operational needs of the Services concerned.

[1] It was later clarified by the Department of Finance that the Commission's terms of reference extended to include the non-commercial state-sponsored bodies.

1.2.4 The Commission's membership was as follows:

Professor Dermot McAleese (Chairperson), Whately Professor of Political Economy, Trinity College Dublin

Dr Brian Aylward, Personnel Director of Irish Cement Ltd., and past Chairman of the Irish Association of Pension Funds

Ms Rosheen Callender, National Equality Secretary, SIPTU*

Mr John Cullen, Assistant Secretary, Department of the Environment and Local Government

Mr Brian Geoghegan, Director of Economic Affairs, Research and Information, IBEC

Mr Eamonn Heffernan, Director of Mercer Ltd., and Chairperson of The Pensions Board†

Ms Anne Maher, Chief Executive of The Pensions Board†

Mr Joe McGovern, Assistant Secretary, Department of Finance

Mr Dan Murphy, General Secretary, Public Service Executive Union

Senator Joe O'Toole, General Secretary, Irish National Teachers Organisation

Ms Anne Vaughan, Principal Officer, Department of Social, Community and Family Affairs

* Ms Rosheen Callender was nominated to the position previously filled by Mr Brendan Hayes, Regional Secretary, SIPTU, who stepped down from the Commission in mid-1997.

† Mr Eamonn Heffernan and Ms Anne Maher were appointed to the Commission as experts in a personal capacity.

1.2.5 The members of the secretariat to the Commission were:

Mr Conor McGinn (Secretary), Assistant Principal, Pensions Section, Department of Finance

Mr Cathal Sheridan, Higher Executive Officer, Pensions Section, Department of Finance

The Commission and secretariat were assisted by

Mr John Reilly, Actuary and Principal Officer, Department of Finance

Mr Damian Smyth, Assistant Principal, Superannuation Section, Department of the Environment and Local Government

1.3 Referral of specific issues to the Commission

1.3.1 A number of specific matters were referred to the Commission by the Department of Finance over the course of our deliberations:

(i) an agreement as part of the *Partnership 2000* negotiations that the Minister for Finance would, as a matter of urgency, request the Commission to examine the specific issues raised by SIPTU in relation to the pension arrangements of non-officer grades in the Eastern Health Board and Dublin voluntary hospitals and to issue an interim report not later than 1 July 1997 (*letter of 7 January 1997*);

(ii) a request by the Labour Court that the Commission give priority to the nurses' pension claims (*letter of 18 February 1997*);

(iii) a request by the Civil Service Inter-Departmental Committee on Work Sharing that the Commission examine the pension implications of a proposal for job-sharing for those over age 55 having a minimum of 30 years' service (*letter of 8 May 1997*);

(iv) a request by the Government for a report by 30 October 1997 on the Commission's considered views of the most appropriate method for applying pension increases in relation to restructuring type deals under the *Programme for Competitiveness and Work (letter of 21 July 1997*);

(v) claims for early retirement by laboratory assistants, ambulance personnel, and radiographers (*letter of 14 December 1998*).

1.3.2 We stated in response to items (i), (ii), and (v) that the claims in question would be amongst those examined under the terms of reference. We added that the Commission did not have any role in adjudicating on matters being processed under the industrial relations machinery. The Commission presented an Interim Report to the Minister for Finance on 12 August 1997 which considered *inter alia* items (i) and (ii).

1.3.3 In response to item (iv), the Commission commented that a considerable amount of work would be necessary in order to arrive at a common view on the best way forward on the large range of interdependent issues coming within the terms of reference. Until that point was reached, it would not be possible to agree recommendations on any specific aspect of the pensions system. We also referred to preliminary comments made in the forthcoming Interim Report.

1.3.4 In relation to item (ii) above, the Commission received a letter dated 12 February 1998 from the Commission on Nursing outlining the concerns of nurses and midwives in relation to retirement issues.

1.4 Other developments during the review period

1.4.1 Reference to the Commission was made in the two National Agreements concluded during the period of our review. *Partnership 2000* (1997) and the *Programme for Prosperity and Fairness* (2000) both stated that, insofar as the public service was concerned, no claim for the introduction of pension schemes or for improvement of existing schemes should be submitted or processed further pending the report of the Commission.

1.4.2 In November 1997, as part of an announcement on the payment of pension increases arising out of restructuring deals made under the *Programme for Competitiveness and Work*, the Government stated that policy in relation to any future restructuring deals would be determined in the light of the recommendations in the Commission's Final Report.

1.4.3 The National Pensions Policy Initiative was launched by the Department of Social Welfare and the Pensions Board in October 1996 and, in addition, it was formally incorporated by *Partnership 2000* in early 1997. The objective of the Initiative was to facilitate national debate on how to achieve the aim of a fully developed national pensions system which would enable all residents in the State to acquire an income to allow them to maintain their established standard of living in retirement. The Initiative culminated in a report from the Pensions Board to the Minister for Social, Community and Family Affairs entitled *Securing Retirement Income* (1998). This report sets out a strategy for future pensions development in Ireland and contains a number of major proposals and recommendations for change to give effect to the strategy. Many of its recommendations have been accepted by the Government and are currently in the process of implementation. Some others are still under consideration. Crucially, the Board recommends a target rate for Social Welfare pensions, making substantial efforts to preserve the real level of these pensions, a funding mechanism in relation to the Social Welfare pension, and a large number of innovations that will enable the potential of an established voluntary Second Pillar to be developed and extended.

1.4.4 In July 1999, the Minister for Finance, Charlie McCreevy TD, announced the Government's decision to set aside an annual provision of 1% of GNP to pre-fund part of the future cost of

Social Welfare and public service pensions and, in addition, to allocate a tranche of the proceeds of the Telecom Éireann flotation to supplement the annual allocations. The Minister stated that he hoped to have the necessary legislation for pensions pre-funding in place by the middle of 2000 and that, in the meantime, the appropriate sums would be set aside in 1999. He noted that there were major policy issues to be determined in legislating for pensions pre-funding, and that he looked forward to the pending report of the Commission on Public Service Pensions in that context. The relevant legislation, the National Pensions Reserve Fund Bill, 2000, was published in June 2000.

1.4.5 In addition to the reference noted at Paragraph 1.4.1, the *Programme for Prosperity and Fairness* stated that following Government consideration of the Report of the Commission, a Working Group of the public service unions, relevant Government Departments and other appropriate bodies would be established to advise on the implementation of the relevant Government decisions with a view to introducing, as quickly as possible, any proposed changes in public service pension arrangements, including those for low paid workers.

1.4.6 A number of legislative changes which have been implemented or are in the course of development — arising from the National Pensions Policy Initiative and other developments — will have implications for the wider pensions environment in which occupational pension schemes, including public service schemes, operate. These include the establishment of a framework for a pensions vehicle to be known as Personal Retirement Savings Accounts (PRSAs) and the implementation of new pension flexibilities in the 1999 and 2000 Finance Acts which apply to the self-employed and to certain other groups, as well as to additional voluntary contribution (AVC) schemes. The ongoing nature of these changes means that the full implications for existing pension schemes is not yet fully apparent. Therefore, for the purposes of our Report, the Commission has proceeded on the basis that these pension changes will not have any *direct* implications for large defined benefit occupational pension schemes, including those in the public service.

1.5 Commission's approach and outline of Final Report

1.5.1 The Commission established at an early stage that we did not have any role in adjudicating on matters being processed under the industrial relations machinery. In considering our terms of reference, we interpreted our main objective as securing the viability and stability of public service pension arrangements over the long-term. We determined that a broad-based approach was necessary so as to address issues that were encountered across the whole public service. This enabled the Commission also to place demands for change in public service pensions in the context of new thinking about the role of the public service (the Strategic Management Initiative), about the evolution of pensions in Ireland (the National Pensions Policy Initiative) and abroad, and developments in the private sector.

1.5.2 The Commission's approach involved the following steps, which correspond broadly with the seven Parts of the Report:

I. Identification of major pension issues

II. Review of public service occupational pension schemes and costs

III. Review of occupational pensions in the private sector and abroad

IV. Analysis and assessment of public service pension arrangements

V. Criteria for a public service pensions framework and pension scheme design

VI. Recommendations

VII. Conclusions and overview of recommendations and impact on costs.

Each of these steps is summarised below.

Part I. Identification of major pension issues

1.5.3 Part I of the Report (Chapters 1-2) presents a brief overview of the main issues examined by the Commission. These were identified on the basis of submissions received, referrals to the Commission (see Section 1.3), and the Commission's own deliberations. Given the Report's main objective — securing the long-term viability and stability of public service pensions — it was deemed essential as a preliminary step to estimate the growth in pension costs, analyse the reasons for their increase, assess their medium- to long-term effect and, finally, devise strategies for managing these costs. Thus, the full list of issues examined in this Report, which are to a large degree inter-related, is as follows:

(i) securing the long-term viability and stability of public service pensions;

(ii) managing the growth in pension costs;

(iii) retirement age and early retirement;

(iv) pensions increase policy;

(v) integration with State Social Insurance benefits and low levels of occupational pension;

(vi) pensions and atypical employment;

(vii) pension scheme flexibility;

(viii) dependants' benefits;

(ix) other issues relating to pension terms;

(x) funding public service pensions;

(xi) transparency in pension costs and liabilities;

(xii) management, administration and communication.

1.5.4 Chapter 2 examines each of the major issues in some detail. Many other points were raised in submissions and the Commission has endeavoured to address as many as possible of those that came within the terms of reference.

Part II. Review of public service occupational pension schemes and costs

1.5.5 Part II (Chapters 3-7) consists of a review of public service occupational pension schemes. It details the pension terms applying in each area of the public service, reviews their history, and outlines the administration, management, communication and financing arrangements of public service schemes. It presents a full actuarial review of public service pensions and considers the implications for pension schemes of changing operational requirements, work environment, and conditions of employment of public servants.

1.5.6 The actuarial review of public service pension schemes indicated that in constant (1997) price terms, the existing level of gross benefit expenditure, £636 million (€807 million) in 1997, is expected to more than double over the next 15 years to £1,368 million (€1,737 million) in 2012, and to almost quadruple over the next 30 years to £2,408 million (€3,058 million) in 2027. The Commission considered that these figures represented a very significant increase in pension costs and that while they were unlikely to place an intolerable strain on the economy — as a percentage of GNP they will rise from 1.6% to 2.4% over the period in question — they were a serious cause of concern.

Part III. Review of occupational pensions in the private sector and abroad

1.5.7 Part III (Chapters 8-9) reviews occupational pension arrangements in the private sector in Ireland and in the public service in other countries and compares them with public service pensions in Ireland. Recent developments in occupational pensions are discussed, where relevant, and trends for the future identified. Particular aspects of pensions practice are highlighted for further consideration in the context of the Commission's recommendations.

Part IV. Analysis and assessment of public service pension arrangements

1.5.8 In Part IV (Chapters 10-12), there is a fuller analysis of existing public service pension arrangements under a range of headings: the evolving cost of public service pensions; the adequacy and fairness of current pension arrangements; the consequences for pension schemes of changing operational requirements, work environment, and conditions of employment of public servants, and the need for flexibility in pension terms.

Part V. Criteria for a public service pensions framework and pension scheme design

1.5.9 Part V (Chapters 13-14) identifies the shared objectives for public service schemes based on a review of the individual concerns of the major stakeholders — employees and pensioners, public service employers and the Government.

1.5.10 The Commission proposes a set of criteria for public service pensions under the headings of adequacy and comprehensiveness, viability, flexibility, fairness and cost.

1.5.11 We also examine alternative pension structures to determine whether a move to a new pension structure (e.g. defined contribution or hybrid scheme) is necessary or whether existing structures might continue to be used, adapted as appropriate.

Part VI. Recommendations

1.5.12 In Part VI (Chapters 15-25), the Commission recommends a range of measures in relation to public service pension terms, and to pension scheme financing, management, and communication systems. These measures represent, in our view, an integrated strategy aimed at securing the long-term viability and stability of public service pensions. They address, in particular, the following key aspects:

- the growth of long-term pension expenditures;
- the issue of retirement age and early retirement;
- the need for transparency in public service pension costs within government management and financial systems;
- the requirement that the pensions system should be compatible with the current and changing nature of public service employment and should be capable of adapting to future change;
- the pension situation of employees who are in receipt of relatively low levels of pay at retirement, with particular reference to integration with State Social Insurance benefits;

- the need for extending choice with respect to level of pension and age of retirement;
- the advantages and disadvantages of establishing a pension fund to meet in full or in part the growing pensions bill; and
- the need for better communication to scheme members of their pension entitlements and of the value of those entitlements.

Part VII. Conclusions and overview of recommendations and impact on costs

1.5.13 In addition to presenting the Commission's final conclusions, Part VII (Chapter 26) of the Report contains an overview of our recommendations and of their implications for public service pension costs.

1.6 Commission procedures

1.6.1 The procedures adopted by the Commission are detailed in this Section.

Regular Commission meetings

1.6.2 The first meeting of the Commission was held on 21 March 1996. The Commission met on 53 occasions in total, including a number of 2-day meetings and a series of meetings with parties who made submissions. We held our final meeting to approve this Report on 6 October 2000.

1.6.3 A Steering Committee of the Commission (Ms Anne Maher, chair, Dr Brian Aylward, Ms Rosheen Callender, Mr Eamonn Heffernan, and Mr Joe McGovern) was established to guide and oversee the implementation of the actuarial project on public service pension costs together with other pensions consultancy work required by the Commission. The Steering Committee met on 17 occasions.

Invitation of submissions

1.6.4 The Commission placed an advertisement for submissions in the national press in September 1996 and made available guidelines for submissions to interested parties. Submissions were received from 105 parties. We present an overview of the issues raised in Chapter 2. The Commission met with 17 parties who made submissions.

Contact with government departments and public service agencies

1.6.5 The Commission sought the views of, and met with, the six government departments having direct responsibility for the pensions of major public service groups — the Departments of Finance, Education and Science, Health and Children, Environment and Local Government, Defence, and Justice, Equality and Law Reform. We also sought and received submissions from two of the larger non-commercial state-sponsored bodies, Teagasc and FÁS.

1.6.6 Information on public service pension arrangements, their historical development, data on serving public servants and public service pensioners, etc. was obtained by direct contact with the Department of Finance, other government departments, and public service agencies.

1.6.7 Briefing on ongoing industrial disputes in certain areas of the public service in relation to pensions matters was obtained from the Department of Finance.

Consultancy projects

1.6.8 The Commission engaged consultants — the Economic and Social Research Institute, Irish Pensions Trust Actuarial Services Ltd., and Mercer Ltd., Actuaries and Consultants — to carry out a number of expert studies. These are detailed in Appendix 1.1. The Commission recommends that the principal Actuarial Report quantifying existing and future public service pension costs (November 1997) should be published and that the other consultancy reports should be made publicly available.

1.6.9 The actuarial review and subsequent actuarial reports were deemed essential to a proper consideration of the issues within the Commission's remit and formed the bedrock around which we based much of our work. Accordingly, considerable time and effort was devoted to this project. The actuarial review was untypical of such exercises in the private sector due to the scale of the project, the unavailability of reliable data in certain areas, and the fact that the primary objective of the review was a projection of future cashflows. These factors imposed considerable demands, particularly in terms of supervising the collection of the basic data essential for the review. The Commission Steering Group which supervised the project was required to provide input in relation to the selection of the actuarial assumptions to determine the precise cost projections, and to agree the format of the presentation of the results of the projections.

1.6.10 The findings and conclusions of each of the consultancy reports are quoted or summarised at the appropriate points in the Report.

Information on public service pension arrangements in other countries

1.6.11 We obtained information on public service pension arrangements abroad by reviewing relevant reports and by making direct contact with officials in each of the countries considered. The experience of a number of countries in public service pensions matters was considered to be of particular value. Delegations from the Commission and secretariat visited Germany, the Netherlands, Sweden and the UK.

Interim Report

1.6.12 As noted at Paragraph 1.3.2, the Commission made an Interim Report to the Minister for Finance in August 1997. This was published in November 1997. The Report included a preliminary examination of the cost of public service pensions, reviewed current pension terms, analysed submissions received and outlined changes in operational requirements, the working environment and conditions of employment of public servants. The Report also discussed current financing and administrative arrangements for public service pensions. It gave a preliminary review of public service pension arrangements in other countries, including recent developments abroad, and reported on a comparison carried out by the ESRI between public service pension arrangements and those applying in the private sector.

1.6.13 The Interim Report concluded with the Commission's preliminary assessment of the issues examined, which were primarily those referred to us by the Minister for Finance during the first half of 1997 (see Section 1.3). We noted that it would be inappropriate to recommend changes in public service pension arrangements in the absence of reaching overall conclusions as required under the terms of reference.

1.6.14 The Final Report includes material already published in the Interim Report.

1.7 Conclusion

1.7.1 This Report aims to provide a coherent and integrated strategy for the future of public service pensions in Ireland. Our recommendations have implications for all parties having an interest in public service pensions — the Government, public service employers, trade unions, pensioner associations, individual public servants and pensioners — as well as for the taxpayer. They may also have implications for the commercial state sector, the private sector and for the overall competitiveness of the economy generally.

1.7.2 This is a time of increasing pressure and of cutbacks in pension terms in many Western economies. The public service pension bill, financed on a pay-as-you-go basis out of general revenues, is a matter of general concern. Ireland's public service pensions are no exception. However, because the overall demographic situation is more favourable than in other countries, the national finances will be in a stronger position than others to cope with the consequences of ageing for some time. It is important that this breathing space is put to constructive use. The Commission is confident that our recommendations will help secure the long-term viability and stability of public service occupational pension schemes in Ireland.

APPENDIX 1.1

Consultancy projects carried out on behalf of the Commission on Public Service Pensions, 1996-2000

No.	Title of Project	Consultant	Date commissioned	Date of completion
1	A Comparison of Pension Arrangements in the Civil Service and large Private Sector Firms	ESRI	January 1997	June 1997
2	Actuarial Review of Public Service Pensions	IPT	January 1997	November 1997
3	Actuarial Review of Impact of Changes to Pension Scheme Terms	IPT	January 1997	December 1997
4	Review of Alternative Structures	Mercer Ltd.	May 1998	July 1998
5	Supplementary Actuarial Information	IPT	March 1998	October 1998
6	Additional Voluntary Contributions/ Purchase of Notional Service	Mercer Ltd.	December 1998	May 1999
7	Further Actuarial Review of Impact of Changes to Pension Scheme Terms	Mercer Ltd.	April 1999	October 1999

CHAPTER 2

Overview of Main Issues and Concerns

2.1 Introduction

2.1.1 Under our terms of reference, the Commission was required to have regard to claims for improvements in existing pension scheme benefits. Accordingly, the Commission invited submissions from interested parties and wrote to a number of government departments and agencies in order to help us identify the main issues and concerns regarding public service pensions. A number of specific issues were referred to the Commission for examination (see Section 1.3). Having analysed the responses and referrals received, met with a number of interested parties and departments, and carried out our own deliberations, the Commission decided to focus on the following issues:

- (i) securing the long-term viability and stability of public service pensions;
- (ii) managing the growth in pension costs;
- (iii) retirement age and early retirement;
- (iv) pensions increase policy;
- (v) integration with State Social Insurance benefits and low levels of occupational pension;
- (vi) pensions and atypical employment;
- (vii) pension scheme flexibility;
- (viii) dependants' benefits;
- (ix) other issues relating to pension terms;
- (x) funding public service pensions;
- (xi) transparency in pension costs and liabilities;
- (xii) management, administration and communication.

2.1.2 The issues are inter-related. Issues (i) and (ii) are central to the Commission's strategy for a new public service pensions framework, and have an obvious impact on our approach to the other issues listed. In this Chapter, we give a brief outline of the issues and of our main recommendations on each.

2.1.3 A summary of the issues raised in submissions from interested parties and a listing of submissions received are contained in Appendix 2.1. The submissions of government departments are summarised in Appendix 2.2. Finally, the pension and retirement issues raised in the final report of the Commission on Nursing (1998) are detailed in Appendix 2.3.

2.2 Securing the long-term viability and stability of public service pensions

2.2.1 To a large degree, securing the long-term viability and stability of public service pensions goes to the heart of the Commission's approach to our terms of reference. In submissions received from unions and public servants, pensioner representative associations, and individual pensioners, the Commission detected a certain unease about the financial underpinning of public service pensions and about the long-term viability of the existing pensions system. There was a general concern that the effects of demographic ageing generally, which will affect Ireland later than other European countries, would impact at some future date upon the ability of the Government to deliver on its pensions promises in respect of its former employees.

2.2.2 The integrated package of measures recommended by the Commission aims to secure a public service pensions framework which is capable of enduring over the long-term. In our view, it addresses the major issues which have been identified, and has regard to the need to manage the evolving growth in public service pension costs in the years ahead.[2]

2.3 Managing the growth in pension costs

2.3.1 The key to securing the long-term future of public service pensions is the management of evolving pension costs. In our deliberations on this issue, we were conscious of the impact of demographic change which will result in a significant increase in the cost of Social Welfare and health care provision over the next 50 years.[3] Public service pension costs are, similarly, projected to increase during this timeframe, but will peak earlier, in about the third decade of this century.

2.3.2 The Commission asked consultants to carry out a full actuarial valuation of public service pension schemes. The results of the valuation are presented in detail in Chapter 6. The main factors which contribute to the growth in public service pension costs are:

- the major increase in recruitment to the public service in the 1970s and early 1980s;
- improvements in benefit terms and in pension scheme coverage;
- the increase in public service pay levels relative to price inflation; and
- the impact of increased life expectancy.

2.3.3 The Commission's terms of reference required us to have regard to the rise in pension costs in formulating recommendations for changes in the pension system. We were extremely concerned at the estimated rise in the size of the public service pensions bill which will see the existing level of gross benefit expenditure, in constant (1997) price terms, more than double over the next 15 years (i.e. by 2012) and almost quadruple over the next 30 years (i.e. by 2027), after which time further growth will be limited.

2.3.4 The *affordability* of the escalating pensions bill was considered by the Commission. We concluded that, in an absolute sense, the costs are affordable, as the extra public service pensions costs will amount to less than 1% of GNP at its peak. We considered that this was unlikely to constitute an intolerable strain on national finances.

2.3.5 However, the peak in pension costs could prove problematic for the following reasons:

- pension costs will rise very steeply as a percentage of public service pensionable pay, from 16% in 1997 to around 38% in 2027. An increase of this scale could possibly lead

[2] Reservations were expressed by some members of the Commission in relation to several of the recommendations. These are marked *(R)* for the purposes of this Chapter.

[3] In the general population today, there is one person aged 65 or over for every five persons of working age; demographic projections indicate that, by the middle of this century, the ratio will have changed significantly to over one pensioner for every two persons of working age (The Pensions Board (1998), *Securing Retirement Income,* p. 66).

to pressure to scale back pension benefits, much as happened in other countries over the past number of years;

- the cost projections are based on assumptions about the existing level of benefits and conditions of entitlement. If pension terms were to be improved substantially, or if coverage of pension schemes were to be extended, the cost of pensions would rise proportionately.

2.3.6 For these reasons, the Commission has felt it necessary to highlight the cost implications of the present pensions system. In this respect, Ireland is no different from many other European countries.

2.3.7 At the same time as the pension bill is rising and concern over the growth in costs is increasing, there are several factors tending to push pension costs up even further:

- there are pressing demands by several parties for improved pension terms, notably early retirement, added years of notional pensionable service, and preferential treatment of certain types of part-time or low paid work. These demands originate from two sources — trade union claims and judgements of the European Court of Justice based on interpretations of EU legislation;
- some cost pressures have been prompted by changes in the working environment. Promotion is increasingly related to performance at work instead of seniority. The more demanding work environment, while improving productivity, at the same time makes early retirement or working at a reduced pace a more attractive option for many employees. The demand for part-time work and job-sharing is rising. Social legislation has had the effect of raising the pension costs associated with such work practices;
- life expectancy is increasing. According to some estimates, it will rise by one year every decade,[4] hence the pension cost per person is already rising, even disregarding the demand for early retirement. For example, a female retiring at age 65 now has a life expectancy of 17 years — if this rose to 20 years by 2026, the pensioner would be drawing a pension for 20 years, an increase of 18%;
- public service numbers continue to grow (over the period 1995—2000, the public service has grown by around 20,000). Increases in the number of public servants has the single greatest effect on public service pension costs.

2.3.8 The above factors place further upward pressure on a public service pensions bill that is already rising rapidly. The problem is that the costs of changes in pension terms and commitments become apparent only in the long run; because the short-run budgetary implications are quite often modest, it is difficult to convey the full impact of the long-term effects to the parties having an interest in public service pensions.

2.3.9 The Commission was also conscious of the difficulty in making special pension arrangements in particular parts of the public sector. Unlike the private sector, the scope for flexibility in response to special individual needs is limited by the tendency for changes in pension terms in one part of the public sector to have implications for employees and pensioners in other

[4] Projections by the Central Statistics Office (using a base year of 1996) indicate that life expectancy at age 65 will rise by one year every decade for females and 0.7 years every decade for males (see Paragraph 7.4.4). A number of commentators have suggested that life expectancy could be significantly higher than existing projections (see for example, Willets, R., ''Mortality in the Third Millennium'', paper presented on 26 January 2000 to the Society of Actuaries in Ireland).

parts through comparability claims. This feature of the public service limits the amount of discretion that can be exercised in dealing with individual cases that were drawn to the Commission's attention in the submission process.

2.3.10 The Commission was, therefore, presented with the difficult task of proposing ways of approaching these two mutually opposing objectives: moderating the huge rise in costs, on the one hand, and responding in a constructive way to long-standing demands for improved pension terms on the other.

2.3.11 The Commission's basic approach to this dilemma has been:

(i) to find ways of smoothing the expected peak in costs, including the use of pension funding;

(ii) to limit any recommended scheme improvements to cost neutral changes, or to cost increasing changes considered absolutely necessary for operational reasons or on grounds of equity and fairness, with a view to preventing as far as possible any net enlargement of the rise in the pensions bill;

(iii) to estimate the impact on long-term costs of all major suggested changes in pension terms;

(iv) to permit as much individual flexibility as possible, consistent with the overall framework of the pensions system, in order to allow employees to provide for benefit improvements by means of personal contributions (the new flexibility to be facilitated through better communication systems);

(v) where a disimprovement in benefit terms is considered necessary, to confine the change to new entrants only, while having due regard to intergenerational equity.

2.4 Retirement age and early retirement

2.4.1 Union claims arise from:

- a desire for improved pension terms;
- the changing nature of the employment environment;
- comparisons between the different pension terms of various groups within the public service;
- the wish to address perceived inequities and anomalies; and
- a desire for more flexibility.

Such claims draw attention to the dilemma faced by the Commission under our terms of reference, namely, the difficulty in addressing in a satisfactory way the competing objectives of having regard to the present and future costs arising under the schemes (as considered above) and the claims for improvements in existing scheme benefits.

2.4.2 At present, the maximum retirement age for most public service groups is age 65, with the majority being able to retire from age 60 with no reduction for early payment of pension. Other groups have special retirement terms, in the form of lower retirement ages, usually with enhanced pension benefits. Various groups of public servants have sought different forms of early retirement, whether through the extension of special retirement terms, or via other forms of early retirement, at minimal or no cost to the individual.

2.4.3 Simultaneous with the above developments, greater numbers of national and international bodies and commentators have been pointing to the cost impact upon occupational schemes of improvements in life expectancy which means that pensions must be paid for a longer period of time. The expected growth in the ratio of pensioners to active employees will increase the cost impact of pensions upon the economy as a whole. These factors, some would argue, point to the need to raise, rather than lower, the average age at which people retire from the labour force.

2.4.4 Apart from demands for early retirement, the Commission recognises that the view of retirement generally has been changing. Retirement no longer implies an end to a person's income earning and productive capacity, and many retirees seek to find alternative employments, including part-time and consultancy working. In addition, many retirees continue to contribute productively by means of voluntary, community or other unpaid work.

2.4.5 In light of these developments, the Commission is recommending a range of options and facilities which would allow those who wish to do so to avail of early retirement at full cost to themselves, or to reduce their work commitments within the public service prior to retirement. To support these recommendations, we propose the introduction of a well designed, cost-effective, and flexible additional voluntary contribution (AVC) type facility which would allow individuals to fund in advance towards genuine retirement choice (see Section 2.8). We believe that the introduction of a wider range of retirement options, together with improved management of factors impinging upon the health and performance of public servants (including the promotion of the valuable contribution of occupational health units) would help address many of the underlying concerns of individual public servants.

2.4.6 The Commission also examined the introduction of a retirement facility called *Approved Early Retirement*. Early retirement under this facility would be available to public servants aged 55 or over with 20 or more years' service who consider that they are unable to make a fully satisfactory contribution, and where management accept that their early retirement would improve the general level of efficiency and effectiveness of the service in question. It would be initiated either by management or the individual public servant, and would be subject to agreement by both parties. Pension benefits under Approved Early Retirement would consist of the immediate payment of pension and retirement lump sum with no actuarial reduction.

2.4.7 A number of recommendations are made in relation to the special retirement terms of certain groups. The purpose of these recommendations — which we believe are essential to ensure internal equity and fairness in pension arrangements for the future — is to arrive at a pensions system where departure from standard retirement terms occurs only where it is considered absolutely necessary for operational reasons. The recommendations focus upon the retirement terms of new entrants; thus, the entitlements of serving staff members would not be affected in any way. *(R)*

2.4.8 Also under this heading, reflecting the continuing improvement in life expectancy in Ireland, we are recommending an increase in the age of retirement for new entrants to the public service to age 65. There would be consequential changes in the retirement ages for groups which have special retirement terms for operational reasons. *(R)*

2.4.9 Finally, the Commission acknowledges the central importance of planning for retirement. The decision to leave formal employment is one of the most important decisions which any employee will make. To assist employees in their retirement planning, the Commission considers that they should be provided with regular and comprehensive information on their entitlements and the retirement options available to them. Structured programmes of retirement planning and counselling should be initiated so as to raise the issue with individuals well ahead of their retirement and to provide information on the options open to them.

2.5 Pensions increase policy

2.5.1 In the public service, pensions are increased in line with pay increases paid to serving employees. Pensions increase policy is obviously a major issue, most immediately for those currently in receipt of pension. It has been topical over the past number of years, principally in relation to the question of whether the pay increases contained in restructuring agreements under the *Programme for Competitiveness and Work* should be passed to pensioners. While the Government in its decision of 4 November 1997 has decided this matter for the present, it has stated that policy for future restructuring agreements will be determined in light of the Commission's Report (see Paragraph 1.4.2).

2.5.2 Aside from the restructuring agreements, pensions increase policy is an important and costly aspect of public service pension terms and merits specific examination by the Commission. A number of submissions have commented on the favourable pension increase arrangements enjoyed by public servants in comparison with the private sector (where pensions are, at best, increased in line with price inflation).

2.5.3 On the basis of our analysis of the issues arising in relation to existing pensions increase policy, the Commission formed the view that an alternative system of increasing pensions, based on an average of pay increases in the public service as a whole, would be more appropriate to this changing environment, and that, in light of the substantial benefit which pay-related pension increases represents, increases should be made subject to an additional contribution by public servants towards the cost involved. *(R)*

2.5.4 The Commission also believes that the State should explicitly guarantee the new system of pension increases by means of legislation and through the establishment of a public service pension fund for pension increases, into which the additional employee contribution would be paid (see Section 2.11).

2.6 Integration with State Social Insurance benefits and low levels of occupational pension

2.6.1 Public servants paying the full rate of PRSI will normally be entitled to the State Social Insurance pension as well as an occupational pension. Integration is the practice followed to ensure that the occupational pension scheme takes account of the entitlement to the Social Insurance pension by adjusting the benefits ultimately payable by the scheme as well as the contributions made towards the cost of the scheme. Where a public servant has 40 years' service, this will result in a combination of occupational pension and personal rate of Social Insurance Old Age (Contributory) Pension (OACP) which is equal to the target replacement ratio of one-half of pensionable remuneration (the same percentage as for a public servant paying the lower modified rate of PRSI, who is not entitled to a Social Insurance pension). This is a standard feature of public service occupational pension schemes as well as pension schemes in the private sector. Integration also operates in many other countries.

2.6.2 Two major issues arise in relation to the operation of integration between public service occupational pension schemes and the Social Insurance system, viz the effects of integration where pensionable remuneration is comparatively low and the separate but related question of pension arrangements for part-time employees.

2.6.3 In our Interim Report, the Commission commented that notwithstanding the major issues of cost and comparability with public servants paying modified PRSI, it was clear that the effect of integration can be to produce a very low or zero rate of occupational pension. The lower levels of pay applicable to many groups who have traditionally been subject to integration contribute to this effect.

2.6.4 In this Report, the Commission examines the arguments for and against making an adjustment to integration for employees who are in receipt of relatively low levels of pay at retirement. We consider the possibility of adjusting the calculation formula in a targeted way for the benefit of those directly affected, in the context of retaining the existing structure of public service occupational pension schemes.

2.6.5 Having decided that such a change is necessary, the Commission recommends that in order to enhance the pension position of public servants in full PRSI class who are subject to integration and who retire on relatively low levels of pay, the operation of integration in all public service schemes should be amended through the introduction of a new pension calculation formula. This formula would result in an increased occupational pension in the case of public servants whose pensionable remuneration is less than three times the rate of OACP.

2.7 Pensions and atypical employment

2.7.1 Traditionally, public service occupational pension schemes were geared to meet the requirements of the permanent public servant who entered the public service usually well before age 20 and continued in employment until age 60-65, having at retirement close to maximum service for pension purposes. This reflected the public service employment model in effect during the nineteenth century when the schemes were introduced and which continues to be the norm for many public servants in employment or being recruited today.

2.7.2 Atypical working has always been a major part of public service employment. It is not clear that the numbers in atypical employment are set to increase substantially in the future, but new arrangements are currently being introduced which could have a significant impact on the position. In any event, there is now a strong emphasis on ensuring pensionability of all forms of atypical employment, particularly part-time employment.

2.7.3 The Commission considers that employees in temporary and part-time working should be granted access to public service occupational pension schemes. Employees should be in regular or quasi-permanent employment and, in the case of part-time employees, work a minimum weekly number of hours.

2.7.4 At present, most part-time public servants are found in areas where full PRSI applied prior to the Government decision to extend full PRSI status to all public servants recruited on or after 6 April 1995. When considering the extension of pension terms to part-time employees, the question of integration and low levels of occupational pension arises.

2.7.5 There are two possible approaches to integration for part-time employees. One method is to calculate the part-timer's actual service at retirement (i.e. to add together all the hours, days and years the person has worked) and apply this service to the full-time remuneration for the position (less the Social Welfare offset of twice the rate of OACP). This is known as *pro rata integration*. The other method is to take the actual remuneration of the part-timer at retirement (less the Social Welfare offset) but to treat each year worked (regardless of the actual time worked) as a full year of service for pension purposes. This is known as *full integration*. The public service currently applies the latter approach (although the pensions of job-sharers are based on pro rata integration). From the perspective of the employee, full integration gives a less favourable level of occupational pension than pro rata integration.

2.7.6 The Commission gave careful consideration to the question of the pension terms to be applied to part-time employees and, in particular, the question of integration. We recommend a change in the form in which integration is applied to part-time public servants from full to pro rata integration. This will result in improved occupational pensions for such employees.

2.7.7 We believe that the effect of this recommendation would be to facilitate the pensionability of part-time employment within the existing benefits structure and to achieve a practicable system for treating atypical service.

2.8 Pension scheme flexibility

2.8.1 It was clear from submissions received and from the Commission's meetings with interested parties that public servants today take a much stronger interest than heretofore in their pension benefits. There is objective evidence for this in the numbers availing of schemes of AVCs in certain parts of the public service. With the increasing age of entry to the public service, more frequent breaks in service, and widespread interest in early retirement, there is likely to be a growing demand in the future for a facility to allow public servants to contribute towards improved pensions and a package more suited to their individual circumstances.

2.8.2 For the State, the requirements of any such facility are cost, administrative convenience, and the minimisation of any possible exposure under the legal and regulatory framework applying to the facility. The Commission examined the possibility of streamlining existing arrangements for the provision of member choice, and recommends the introduction of an alternative arrangement to be known as the Scheme for Public Employees' Additional Retirement Savings (SPEARS). As a single plan operating throughout the public service, we believe that SPEARS would represent a well designed, cost-effective and adaptable facility to enable public servants to contribute towards enhanced pensions choice, including planning for early retirement, at least possible cost to themselves.

2.8.3 We recommend also the implementation of an active policy of pension scheme communication to facilitate the provision of genuine retirement choice (see Paragraph 2.13.4).

2.9 Dependants' benefits

2.9.1 The Commission considers that spouses' and children's contributory pension schemes are a key component in the public service pensions framework. The value of the schemes to public servants was reflected in the submission process. As one of the most frequently raised topics, individuals and unions sought a further option to join the schemes for those employees who, in most cases, had on two previous occasions decided not to take up a membership option. The

Commission examined the arguments involved, but decided, on balance, not to recommend a further general membership option across the public service as a whole. However, we accept that in a number of cases, perceptions of injustice may have arisen as a result of the exercise of past options not to join public service spouses' and children's pension schemes. We consider that some means should be introduced to allow for a review of these cases, but subject to certain conditions.

2.9.2 A range of other issues were raised under this heading, including the recognition of common-law relationships for pension purposes. On this point, we recommend that the existing provisions of public service spouses' and children's schemes should be modified to allow payment of a survivor's pension to a financially dependent partner in circumstances where there is no legal spouse and where a valid nomination has been made. *(R)*

2.10 Other issues relating to pension terms

2.10.1 The Commission examined and makes recommendations on a number of other issues relating to pension terms, many of which were raised in the submission process. They include:

- employee contributions;
- notional added years;
- portability of pensions/preservation of service;
- pension terms on ill health early retirement;
- pensionability of allowances: consequences for pensioners;
- differences in pension terms between established and non-established type employees;
- pension scheme coverage for certain professional and other groups.

2.11 Funding public service pensions

2.11.1 There are two main approaches to financing pension schemes, *pay-as-you-go,* where pension costs are met from current revenue, and *pre-funding*, where funds are set aside and invested to meet future liabilities as and when they arise. The majority of public service pension schemes are financed on a pay-as-you-go basis. In the private sector, the primary reason for establishing a company pension fund is to secure benefit entitlements independently of the continued existence or otherwise of the company in question. The State is in a very different situation. Its pension liabilities in respect of current and former employees are secured by the Government and its ability to tax. Furthermore, pay-as-you-go is in keeping with the Government's budgetary system generally, and is the approach adopted by most of our EU partners.

2.11.2 However, there is a lack of transparency about the real cost of pensions under the pay-as-you-go system (see also Section 2.12). In addition, there is no recognition of accrued pension liabilities for past service. Thus, it can be argued that Ireland's national debt is actually higher than the reported figure by £20 billion, or €25.4 billion (i.e. the total of accrued public service pension liabilities in 1997, as estimated in our actuarial review). In a funded system, the contribution rates would bring home to public servants the value of their pension entitlements and the costs of improving them, while the State, too, would become more conscious of the real cost of recruitment.

2.11.3 It is also argued in favour of funding that higher investment returns obtained on a State pension fund's assets compared with the returns that would result from the Government's alternative usage of the monies would make the ultimate long-term cost of pensions more affordable. However, this is a comparison that is difficult to quantify conclusively.

2.11.4 A major concern for the Commission has been how to address the very significant growth in long-term pension costs. As indicated in Section 2.5, we recommend a move to partial funding, with contributions to be set aside and invested to meet the future cost of pension increases. If implemented, this funding approach — which would require substantial resources in the years ahead — would serve to smooth the expected peak in future pension costs.

2.11.5 We have estimated that the periodic and lump sum contributions which would be required for such a fund would be broadly similar to the scale of contributions to which the Government has committed itself under its July 1999 pre-funding initiative (see Paragraph 1.4.4).

2.12 Transparency in pension costs and liabilities

2.12.1 At present, because they are financed on a pay-as-you-go rather than a funded basis, public service pension costs are recognised in government accounting systems only when the pension benefits ultimately become payable, thereby disregarding the accruing cost of pensions for serving employees. Decisions about the recruitment of employees, improving benefit terms, making new allowances pensionable, increasing pensions coverage, as well as early retirement, have obvious pension cost implications but, usually, the full extent of these costs will only impact at some future point. Often the agency, department, or body which gave rise to the additional pension cost will be different from that which must meet that cost in due course. Thus, as the pension cost does not affect its bottom line there is little incentive for the employer to manage and control the increase in costs.

2.12.2 For this reason, the Commission recommends the adoption of a new accounting framework with the objective of extending greater transparency into pension costs and liabilities. We are not in a position to recommend a detailed system of accounting for pension costs as we believe that this must be done in the context of ongoing reform in government financial management systems under the Strategic Management Initiative. However, we would suggest that the framework for improved transparency in pension costs proposed would facilitate better management of the continuing evolution of public service pension schemes, and would be consistent with the thrust of reforms under the financial management component of the Strategic Management Initiative.

2.12.3 In order to enhance the visibility of accruing public service pension costs, we believe that it would be appropriate if a statement on the cost of the pension earned in the previous year were included in the annual benefit statement issued to each individual public servant (see Paragraph 2.13.4).

2.12.4 Finally, the Commission considers that proposed changes to pension terms in the future should be actuarially costed and that agreement should be reached between public service employers and unions about how any additional cost, in terms of an increase in contribution rates, should be met. The costings should be prepared by the Public Service Pensions Office (see Paragraph 2.13.5).

2.13 Management, administration and communication

2.13.1 The management and administration of occupational pension schemes is a complex and technical area. In many of the larger funded private sector schemes, standards of service provision and administration are being continuously updated as a result of a range of factors such as the changing regulatory environment, developments in information technology, employee interest, and an increased emphasis on occupational pension as a valuable feature of employment. In some cases, pension schemes are outsourcing their administration functions.

2.13.2 By contrast, public service schemes have not experienced these developments to any significant extent. One of the consequences of the pay-as-you-go system is a pensions administration system that is geared primarily towards the calculation and payment of pension benefits, rather than the provision of management information on pension costs and the communication of benefit entitlements and scheme options to serving employees. This has had implications for the resourcing of pension administration units across the public service.

2.13.3 The Commission recommends the development of a specialised, computerised pensions administration system across the public service. The new system should be capable of linking pension data across the public service, communicating information on individual pension entitlements, and delivering the management information required for pension costing.

2.13.4 The Commission also recommends the implementation of an active policy of pension scheme communication, involving the provision of user-friendly scheme documentation, annual benefit statements, and details of the options available to public servants to improve their overall level of benefits and to plan for their retirement. Such a policy would involve a close interlinkage with the new scheme for the provision of member choice, SPEARS (see Section 2.8).

2.13.5 Having considered the implications for the management and administration of pension schemes of the overall set of initiatives being recommended by the Commission, we propose a new structure for the management and administration of public service pensions. We recommend the introduction of a centralised structure involving the Minister for Finance, an Inter-Departmental Committee on Public Service Pensions, a Public Service Pensions Office (PSPO), and a number of Pension Support Units.

2.13.6 The Commission's recommendations, taken as a whole, have the objective of establishing a single, consistent set of pension terms for all public servants, which is also capable of adaptation to meet local operational requirements. For the future, it will be essential to ensure that the wider implications, including the long-term cost implications, for all public service pension schemes of proposed changes in pension terms in any one area of the public service are fully taken into account. It should also be established that any proposed changes are consistent with the basic principles underpinning the public service pensions framework. This combination of measures would, in our view, assist the parties in effectively managing the continuing evolution of public service pension arrangements.

APPENDIX 2.1

Summary of submissions received from interested parties

1. Introduction

1.1 An advertisement was placed in the national press in September 1996 inviting submissions on issues to be examined by the Commission. Guidelines for submissions were issued. Submissions from public service employers were received separately (Appendix 2.2 deals with submissions received from government departments).

1.2 Submissions were received from 105 parties, including unions and staff associations, pensioner representative associations, individual public servants, former public servants, pensioners, representatives of employers, pension funds and the pensions industry generally. The parties who made submissions are listed at the end of this Appendix. The Commission met 17 parties who made submissions.

1.3 Submissions addressed the following matters:

1. ***Cost of public service pensions***
2. ***Pension terms***
   - retirement age and early retirement;
   - reckoning of past service;
   - pensions increase policy;
   - integration of occupational pension schemes with State Social Insurance benefits;
   - pensions and atypical employment;
   - additional voluntary contributions/purchase of notional service;
   - spouses' and children's schemes;
   - added years of notional service;
   - pensionability of overtime and allowances;
   - ill health early retirement.
3. ***Management and administration***
   - financing arrangements for public service pensions;
   - administration;
   - portability of pensions/preservation of service;
   - Revenue rules;
   - other issues.

1.4 These and other issues are examined and discussed in this Report. A brief summary of each issue is given below.

2. Cost of public service pensions

2.1 A number of union submissions argued that the current cost of public service schemes (net of employee contributions) was not excessive by comparison with other employments where reasonable pension benefits were provided. Some unions pointed out that the overall cost of occupational pensions would be reduced over time through the operation of integration with the State Social Insurance system arising from the extension of full PRSI cover to all new entrants to the public service. Other submissions argued that any improvements to be made to pension scheme terms should be done on a cost neutral basis. It was also suggested that pension contributions should be set at levels commensurate to the benefit to be received, i.e. that they should reflect the new entrant contribution rate.[5]

3. Pension terms

Retirement age and early retirement

3.1 At the time of the Commission's establishment, early retirement was the subject of claims by a number of public service groups, including teachers and nurses. The importance of early retirement for staff interests was confirmed in the submissions received from unions and individual employees and in the presentations made by those whom the Commission met. A number of different early retirement arrangements were proposed (with particular variations in the case of those groups which already had retirement provisions different from those applying generally in the public service):

- introduction of *fast accrual* schemes in which all service greater than 20 years would count as double, coupled with an earlier minimum retirement age. This scheme would be similar to that applying currently to Gardaí, personnel employed in the psychiatric services, Firefighters and Prison Officers. Early retirement was sought particularly for personnel in shift-based employment and/or those who considered themselves to be in hazardous or stressful occupations;
- improvement in pension terms for groups which already have fast accrual terms and lower retirement ages for operational reasons;
- a more flexible approach to retirement to enable employees to retire at any age between 55 and 70, with a pension based on actual service to be paid immediately. In addition, as a means of addressing the suddenness of transition between work and retirement, employees might be allowed work half-time prior to retirement, and get pro rata pension credit. A number of other forms of flexible or phased retirement were proposed.

3.2 Arguments made in favour of a change in retirement age and the introduction of early retirement included:

- comparability with public service groups which have special pension terms and retirement earlier than the public service norm;
- the impact of stress and burnout. It was argued that serving public servants have to deal with a changing work environment, the introduction of new technology, and the various consequences of societal change, and that these pressures and the pace of change impact more strongly upon some groups than on others.

3.3 Several employer and pensions industry submissions argued against a reduction in retirement ages and the extension of early retirement provisions on the grounds of cost and the impact of increased life expectancy. Others took the view that early retirement should only be allowed on

[5] We discuss new entrant contribution rates in Paragraphs 6.2.8-6.2.10 and Section 6.6 of the Report.

a cost neutral basis, i.e. that pensions should be actuarially reduced to take account of the fact that they would be paid over a longer period of time.

Reckoning of past service

3.4 Concern was expressed about the requirement, on being appointed to a permanent public service position, to pay pension contributions in respect of all past service and, in particular, the application of compound interest if amounts due were not paid within a prescribed period.

3.5 A number of points were also raised regarding the repayment of marriage gratuities. The impact of compound interest on the amount to be repaid was the main concern.

Pensions increase policy

3.6 In public service schemes, pensions are generally increased in line with the pay of serving public servants. This is known as *pay parity*. Submissions received from unions and pensioner associations sought continuation of pay parity. They made particular reference to restructuring/productivity type agreements in relation to pay and conditions of service (such as those provided for under the *Programme for Competitiveness and Work*). It was argued that these agreements did not break the link between pensioners and serving employees for pension increase purposes. A number of other submissions suggested adoption of a policy of increasing pensions in line with changes in the Consumer Price Index (CPI), which is the approach in the private sector and in the public service schemes of a number of European countries.

Integration of occupational pension schemes with State Social Insurance benefits

3.7 Public servants paying the full rate of PRSI and consequently entitled to receive the Old Age (Contributory) Pension (OACP) have their pension benefits (and contributions) integrated with the Social Insurance pension. The calculation of pension benefits takes account of the Social Insurance pension by deducting an amount of twice the rate of OACP from pensionable remuneration. In the case of public servants who retire on relatively low levels of pay, including part-time employees, the effect of integration can be to produce a very low or zero rate of occupational pension. The payment of lump sum is not affected, as it is calculated on the basis of pensionable remuneration.

3.8 Union submissions argued that all employees should have an entitlement to a reasonable level of occupational pension. They suggested a number of amendments to the integration arrangements, viz:

- the introduction of a minimum level of occupational pension;
- the exemption of a certain amount of pay from the integration process.

3.9 Other points raised under the heading of integration included:

- dissatisfaction at the reduction of pension at age 65 for enlisted personnel in the Defence Forces on qualifying for Social Insurance pensions;
- the non-payment of a supplementary pension to employees in full PRSI class who retire before age 65 and who subsequently take up other employment.

3.10 Pension industry and employer submissions argued for continuation of existing integration arrangements.

Pensions and atypical employment.

3.11 Many submissions argued for membership of pension schemes to be extended to part-time public servants. A difficulty raised was the question of integration with the State Social Insurance system (as outlined above). An employee will qualify for the full rate of OACP under the Social Insurance system if he or she earns more than £30 per week and fulfils the PRSI contribution requirements. Under public service pension arrangements, integration is applied in the same way for part-time employees (where pensionable) as it is for full-time employees, with the result that, on retirement, many part-time employees receive a very low or zero rate of occupational pension.

3.12 In addition to the suggestions listed at Paragraph 3.8 above, a further union proposal was the introduction of a supplementary pension scheme specifically designed for part-time employees, with a pro rata abatement of State Social Insurance entitlements.

3.13 The exclusion of temporary employees from many pension schemes was also raised by a number of unions.

Additional voluntary contributions/purchase of notional service

3.14 The possibility of using additional voluntary contributions as a means of introducing greater choice and flexibility for members of pension schemes was raised in submissions. Pensions industry representatives argued that a range of unnecessary restrictions applied under existing arrangements. A number of points were made concerning the cost of purchase under the schemes for purchase of notional service.

Spouses' and children's schemes

3.15 For most groups of public servants, there are separate spouses' and children's contributory pension schemes to provide for payment of survivors' pensions in the case of death-in-service or death after retirement. These schemes are of relatively recent origin. In each case, membership of the schemes was optional for those in service at the date of introduction and automatic for all new entrants. In general, the schemes were offered to male employees in the period 1969–71, and to female employees in 1981, while in 1984, revised schemes were offered to members of existing schemes and to those who had previously opted not to join (different dates applied to different groups). Submissions from unions, pensioner representatives and individual public servants sought to have a further option to join the various schemes. The main groups covered by submissions included civil servants, teachers and members of the Defence Forces. For certain groups, the question of a new membership option affected female public servants particularly. The submissions argued that when the schemes were originally offered they were not properly explained, and that individuals opting not to join did so in ignorance of the possible future consequences. They also referred to the impact of ongoing social developments, such as the introduction of judicial separation and divorce, and the changing position of women in society.

3.16 Other issues were raised under this heading, including the possibility of refunding contributions for those who are single at retirement, and a proposal to allow for the nomination of non-marital partners to receive spouses' pensions.

Added years of notional service

3.17 Several submissions argued that there were anomalies in the various schemes for awarding added years of notional pensionable service to those in professional, specialist or technical positions in different parts of the public service.

Pensionability of overtime and allowances

3.18 Pensioner associations argued that where particular allowances had been made pensionable from a specific date, the consequent increase in pension should have applied not only to allowance holders who retired on or after that date, but also to those who had retired before that date. The position of Garda Síochána and Defence Force pensioners, in particular, was raised.

3.19 The calculation of pension in relation to variable allowances, such as unsocial hours payments, was raised, particularly, the *averaging rule*, under which variable allowances received in the final three years are averaged for the purposes of calculating pensionable remuneration. It was suggested that this arrangement placed undue pressure on employees to work extra unsocial hours close to retirement when they might prefer to work less, and that it disadvantaged employees who became unable to work unsocial hours due to ill health.

3.20 The pensionability of overtime payments was sought in a number of submissions.

Ill health early retirement

3.21 Some submissions sought improvements in the pension terms applying on early retirement in case of ill health. It was suggested, for example, that the five year service requirement to qualify for an ill health early retirement pension should be lowered to two years.

4. Management and administration

Financing arrangements for public service pensions

4.1 Submissions proposed the advance funding of public service pensions or the creation of a partial fund to meet the expected increase in pension costs. Many suggested that a move to full funding of public service pensions was not practicable. Others argued against pre-funding and sought the retention of the existing pay-as-you-go approach.

Administration

4.2 Submissions raised the need for better communication to individual public servants of their benefit entitlements and of the pension scheme choices available to them. In addition, it was suggested that an independent pensions body should be established to oversee public service pensions.

Portability of pensions/preservation of service

4.3 Conditions affecting the portability of occupational pensions between the public service and the private sector were raised in a number of submissions. Unions representing nurses and teachers argued that work in the public service abroad, particularly in the UK, should be transferable for pension purposes.

4.4 The introduction of preservation of service in the early 1970s was raised, in particular, the fact that public servants resigning before 1 June 1973 had no entitlement to preserved benefits from age 60, even though they had the requisite service.

Revenue rules

4.5 A range of issues were raised in relation to the tax limits laid down by the Revenue Commissioners in relation to occupational pension schemes. It was argued, for example, that the limit on employee pension contributions qualifying for tax relief should be increased from its current level of 15% of salary.

Other issues

4.6 Issues other than those outlined above included:

- the question of converting non-contributory schemes into contributory schemes, with consequent uprating of pay levels. It was argued that this was appropriate as it had already been acknowledged that an implicit contribution is paid in the form of lower salary levels;
- a proposed increase in the gratuity payable in case of death-in-service;
- the lack of pension scheme coverage for certain groups, e.g. many part-time employees;
- the compulsory membership of public service pension schemes. It was suggested that public servants should be allowed to opt out of occupational schemes and to contribute to personal pension plans, as is permitted in the UK;
- a reduction in the minimum period of service required to qualify for pension from five years to two years;
- the payment of higher pension to those who remain in service until maximum retirement age;
- the standardisation of pension terms, e.g. the removal of the difference in retirement ages between established and non-established civil servants.

Submissions received (excluding government departments)

Note: An asterisk (*) denotes that the Commission met with the party concerned.

Agency for Personal Service Overseas
Amalgamated Transport and General Workers Union
Association of Assistant Secretaries and Higher Grades
Association of Garda Sergeants and Inspectors*
Association of Garda Superintendents
Association of Higher Civil Servants*
Association of Retired City and County Accountants
Association of Retired Commissioned Officers of the Permanent Defence Force*
Bentley, John
Brennan, Anthony
Brennan, Rose
Brennan, Thomas
Burke, Pat
Byrne, Hugh
Carr, Thomas
Carrol, John
Casey, Deirdre
Chambers, Bernadette
Civil Service General Council Staff Panel
Corcoran, William
Coroners Association of Ireland
Craven, Agnes
Creamer, Christopher
Crimmins, John
Crowley, Josephine
Cullen, Frank
Dooley, Imelda
Doyle, Patrick
Duane, Fionnuala
Dublin Corporation Retired Officers' Association
Duffy, Michael
Fallon, Michael
Gallagher, John
Garda Representative Association*
Garda Síochána Pensioners Association*
Garda Federation
Glavin, Patrick
Glynn, Marcella
Graham, John
Hanley, John
Hearne, Michael
Hempenstall, James
Hickson, John
IMPACT*
Irish Association of Investment Managers*
Irish Association of Older People

Irish Association of Pension Funds*
Irish Insurance Federation
Irish Medical Organisation
Irish National Teachers Organisation, Teachers Union of Ireland, and Association of Secondary Teachers of Ireland (Joint Submission)*
Irish Nurses Organisation*
Irish United Nations Veterans Association*
Irwin, Dermot
Kavanagh, Catherine
Kevany, Rosemary
Kirby, Jim
Kneeland, Brian
Local Government Staff Negotiations Board
Malone, Tom
Marrinan, Ann
McCulloch, David Gerard
McHenry, Elizabeth
McInerney, James
McMahon, Sheila
Meagher, Marie
Moloney, Frank
Mullarkey, Thomas
National Building Agency Ltd.
National Safety Council
Nunan, Michael
O'Boyle, Anna
O'Ceilleachair, Sean
O'Hegarty, Diarmuid
O'Neill, Ann
Organisation of National Ex-Servicemen and Women*
Pensions Board, The
Permanent Defence Force Other Ranks Representative Association*
Phillips, Jim
Power, Laurence
Psychiatric Nurses' Association of Ireland
Public Service Executive Union*
Purcell, Matt
Quaid, Charles
Retired Civil and Public Servants Association*
Roche, Frederick
RTÉ
Ryan, Margaret
Savage, May
Scanlon, Michael
Scott, Augustine
SIPTU — Dublin Region Public Sector
SIPTU — Local Authorities' Branch
SIPTU*
State Solicitors Association

Stewart, Jim
Teachers Union of Ireland – Limerick Colleges Branch
Trinity College, Dublin*
Turner, Michael
University College Galway
Walsh, Celine

A small number of parties requested that they be excluded from the published list of submissions.

APPENDIX 2.2

Summary of submissions received from government departments

1. Introduction

1.1 The Commission invited submissions from government departments in May 1997. The departments contacted were Finance, which administers the Civil Service Pension Scheme and has the main policy role in relation to the conditions of service of public servants and in relation to the public finances generally, and the Departments of Defence, Health and Children, Environment and Local Government, Education and Science, and Justice, Equality and Law Reform, which have primary operational responsibility for the public services referred to in the Commission's terms of reference.

2. Department of Finance

2.1 At the outset, the Department of Finance suggested that while the Commission would need to consider claims for improvement in existing benefits, such claims should be examined only as part of an in-depth assessment of the continued appropriateness of existing provisions. The best approach, in the Department's view, might be to first consider what pension provisions should ideally apply in the public service, and to then assess claims for improvements in benefits in the light of these *ideal* arrangements.

2.2 In devising a possible ideal scheme, the department suggested that regard should be had to the following:

- the existing provisions and the basis upon which they were developed;
- the operational and manpower policy requirements of the public service;
- the short- and long-term implications for Exchequer costs and national competitiveness;
- the reasonable expectations of employees — in terms of what a new recruit to the public service might reasonably expect a *good* employer to provide;
- current practice elsewhere in this country and abroad; and
- other factors such as ease and efficiency of administration, internal equity, and the respective roles of occupational pension schemes, the Social Welfare system, and the facilities available to individual employees to enhance their scheme benefits.

2.3 The Department noted that standard public service terms were intended to cater primarily for a *traditional career* — full-time employment with 40 (or more) years of unbroken service either within the one area or within a closely related group of areas, e.g. within the civil service or within the local authority service. The Department suggested that the Commission would have to consider, amongst other things:

- the significant growth in atypical employment expected in the public service;
- evolving EU case law in the equality area;
- the possibility of greater career mobility;
- the removal of an upper age limit for the recruitment of most public servants; and
- the likely opening up of public service positions to citizens of other EU member states.

2.4 While the Commission's terms of reference required it to have regard to the present and future costs arising under the schemes financed by the Exchequer, the Department argued that it was essential that this aspect of the Commission's terms of reference be considered in the wider context of national competitiveness of the private and commercial state sectors. Given the projected growth in public service pension costs, it was imperative to avoid further increases, including those which would follow from improvements in existing terms.

2.5 The Department suggested that claims from public sector groups for improvements in their pension terms were not, in general, driven by practice in the private sector but on a claimed comparability with other public service groups who had enhanced terms. Accordingly, it was vital to ensure that non-standard terms should only apply where they were warranted by the operational requirements of the service concerned.

2.6 The Department expressed satisfaction with aspects of the current arrangements, such as income replacement ratio, integration, standard accrual rates (whereby maximum pension entitlements were accrued after 40 years' pensionable service), amount of death gratuity, etc., but suggested that the Commission might wish to consider whether, given improvements in life expectancy, the existing minimum and maximum retirement ages should be increased. The Department asked whether it was reasonable to retain minimum and maximum retiring ages, and if so, whether a five-year difference between both was appropriate.

2.7 The submission expressed concern about a range of other matters, including:

- the concept of a minimum pension as sought by some public service unions in the context of the integration of pension benefits with the State Social Insurance system;
- the continuing need for the various forms of professional added years arrangements;
- existing arrangements for abatement of pension where a public servant is re-employed after retirement; and
- the beneficial nature of *Injury Warrant* terms, which provide benefits to or in respect of civil servants who, through no fault of their own, are killed or injured while performing their duties.

2.8 On the question of pension increases, the Department stated that it was reasonable to protect an individual's pension at retirement. It noted that increasing pensions in line with changes in the Consumer Price Index would be less costly than the existing policy of pay parity. The Department asked whether pay parity was appropriate in a context where pay increases may have been granted to a particular group of employees on foot of changes in their duties and responsibilities given that the emphasis on linking pay increases to changes in the nature and responsibilities of jobs was likely to be accentuated in the future.

2.9 The Department suggested that current pay-as-you-go financing arrangements for pensions should be examined. The Department argued that even if formal funding was not introduced, there was an urgent need to put in place more transparent systems of accounting which would clearly and quickly identify existing pension liabilities and the impact on those liabilities of increases in numbers or improvements in terms.

2.10 Under the general heading of early retirement, the Department considered redundancy, under-performance, and special terms. The Department noted that under the pay-as-you-go system, the true cost of early retirement was not readily apparent, and pointed to the private sector approach of paying in advance the capital cost associated with early retirement decisions.

2.11 As regards the special terms which apply to such groups as Gardaí, Prison Officers, Psychiatric Nurses, etc., and which were originally introduced with a view to maintaining operational effectiveness by maintaining a younger age profile than normal because the work was predominantly of a physical or dangerous nature, the Department asked whether such terms were still appropriate in today's environment, where people were living longer and the working environment had changed considerably.

2.12 Where it might be argued that a justification for special terms remained, it was not clear to the Department that the existing systems were the most effective way of achieving the stated objective. For example, a purely voluntary system involving early retirement might achieve the objective of lowering the age profile but the organisation could still be disadvantaged because the personnel who left might be more competent than many of those who remained. The Department suggested that a more targeted approach should be adopted.

2.13 As a minimum, the Department argued, it was difficult to see merit in the extension of special terms to groups for whom such arrangements were not considered appropriate or necessary when living conditions and life expectancy were not as good as they are now.

2.14 In arriving at its conclusions, the Department noted, the Commission would have to take into account the accrued rights of serving personnel.

3. Department of the Environment and Local Government

3.1 The Department of the Environment and Local Government argued that the key issues in determining the appropriate approach to the future financing of public service pensions were:

- the extent of the emerging liabilities;
- the prospects and expectations for economic growth in the period up to the time expenditure is expected to peak and beyond;
- the impact which such growth might have on the State's ability to maintain a pay-as-you-go system;
- the alternative funding models and mechanisms which might be considered;
- the view that, taking account of accrued liabilities, a full funding strategy was impractical. The Department favoured the establishment of a partial or reserve fund in which member contributions could be invested;
- the need for transparency in pension costs irrespective of the funding model adopted.

3.2 In relation to the impact of changes in the working environment and conditions of employment of public servants since public service pension schemes were first introduced, the Department considered that:

- there was a need to examine the special provisions from which certain groups benefit such as
    - professional added years;
    - early retirement/*fast accrual* schemes;

- this was particularly important given that work practices had changed considerably over the years, with much greater account being taken of health and safety considerations. As a consequence special terms of these groups would continue to be targeted by others seeking improvements in their pension arrangements;

- the principle should be adopted that fast accrual terms should only apply in situations where the personnel concerned were obliged to retire early, either as part of the conditions of employment or where the employer required some flexibility in certain cases. They should not be retained where early retirement was merely an option and there was an entitlement to remain in public service employment until age 65;

- it was essential that pension arrangements be less restrictive so as to enable new work practices to be implemented within a *pensions friendly* environment in order that pension rights were protected and, where circumstances dictated, enhanced.

4. Department of Health and Children

4.1 The Department of Health and Children made a number of points in its submission:

- the cost of pension schemes would continue to rise because of the increase in the numbers of staff employed in the health service particularly as a result of its expansion in the 1970s;

- the establishment of a pension fund in respect of new entrants to the service would appear to make sense. However, it was difficult to see how existing employees and pensioners could be accommodated without a substantial injection of Exchequer funding to meet pension costs and the accrued benefits of serving staff;

- in the context of reorganisation/rationalisation of services, it was important from the perspective of cost effectiveness that management should be in a position to offer personnel deemed to be surplus to requirements the option of voluntary early retirement (VER). In addition, in cases of under-performance, there were good arguments on grounds of efficiency and effectiveness for enabling management to offer the option of VER — this was recognised with the introduction of the pilot early retirement scheme for nurses aged 55 and over with 35 years' service;

- the mental health service had witnessed the greatest change in its working environment. The change was marked by a shift from a psychiatric institution-based service to a community-based one which was integrated with other health services. As a consequence, some consideration was being given to reviewing the pension terms held by Psychiatric Nurses. A draft General Scheme and Heads of a new Mental Health Bill were considered and approved by Government (1996). In relation to superannuation, the draft provided that the more favourable superannuation conditions applicable to existing officers and employees registered under the 1945 Act would not be altered (i.e. the right to retire with immediate payment of pension from age 55, having a minimum of 30 years' service, with doubling of service for service in excess of 20 years). However it stated that the superannuation entitlements of personnel appointed after the enactment of the legislation should be determined in accordance with a collective agreement with any recognised trade union or staff representative association concerned;

- given the budgetary constraints within which the public health service operates and the need to ensure cost-effective use of all resources in a manner consistent with service needs, there was a case for reviewing traditional work practices with a view to introducing the flexibility necessary in order to facilitate the deployment of staff in response to service requirements. In order to make atypical employment arrangements more acceptable and attractive, officers as well as non-officers should be allowed to reckon part-time service for pension purposes.

5. Department of Education and Science

5.1 The Department of Education and Science submission provided the following:

- an overview of the education environment and the role of teachers;
- an outline of the role of the Department of Education and Science in relation to pensions;
- a summary of the primary and secondary teachers' pension schemes, including revisions made under the *PCW* agreement;
- an outline of the teachers' early retirement scheme as agreed with unions under the terms of the *PCW* agreement;
- key statistical information.

6. Department of Defence

6.1 The Department of Defence submission noted that a review of the existing superannuation arrangements for military personnel was being undertaken to take account of the recommendations of the *Gleeson Commission* (1990). The review was considering amongst other things:

- military manpower policy requirements;
- the superannuation terms in other public service areas;
- cost effectiveness and value for money.

6.2 Other points made in the Department's submission included:

- while the Department had no preference regarding the method of financing public service pensions, it suggested that given the emerging and projected costs for public service pensions, there might be a case for some funding arrangement, at least in respect of employee contributions and perhaps matching employer contributions;
- the operational requirements of the Defence Forces were considered to be of paramount importance; the most critical features were:
  - the need for young physically fit personnel;
  - adequate turnover of personnel;
  - continuous recruitment;
- the Department suggested that pay parity was the fairest pension increase mechanism;
- abatement of pension should be considered in the case of personnel who retire early with immediate pension from areas like the Defence Forces and who subsequently take up employment elsewhere in the public service.

7. Department of Justice, Equality and Law Reform

7.1 The main points of the Department of Justice, Equality and Law Reform submission were as follows:

- the financing of pensions should be open and transparent. Accordingly, the Department would support the open recognition of pension liabilities and expenditures within Government accounting systems;
- Garda, Sergeant, and Inspector ranks had claims before the Garda Síochána Conciliation Council to increase the age of retirement from age 57 to 60. Garda management were not in favour of extending the retirement age because of its impact on recruitment and the effect on the motivation and morale of officers seeking to advance through the ranks;
- in relation to the operational needs of the service, it was argued that a young and energetic force was essential at ground level. While health and life expectancy had improved since the introduction of these retirement provisions, the operational and manpower arrangements were as important as ever. In this respect, it was very debatable whether the level of fitness of Gardaí in their late 50s would be sufficient to meet the demands of policing at ground level. It was considered that the fast accrual pension scheme helped maintain an effective age profile, particularly at operational level;
- the physical nature of the work of Prison Officers, it was argued, might be used to justify their right to retire on full pension after 30 years. However, the Department could not say whether this was the most appropriate arrangement. In the absence of detailed analysis, the Department would have reservations about recommending the continuation of the status quo or recommending significant change. Any such analysis should examine amongst other things the justification of providing for retirement on maximum pension at 30 years for grades whose work did not involve full-time contact with prisoners;
- reference was also made to a claim for fast accrual terms for Probation and Welfare Officers, i.e. to qualify for maximum pension on the completion of 30 years' service.

APPENDIX 2.3

Extract from the final report of the Commission on Nursing (1998)[6]

Retirement Initiatives

1. The claim in relation to early retirement for nurses (other than psychiatric nurses) and midwives was considered by an Adjudication Board during the negotiations on pay and conditions of nurses and midwives in early 1997, which was then considered by the Labour Court. The Board and the Labour Court recommended that all of the arguments be considered by the Commission on Public Service Pensions (CPSP) in the context of its terms of reference. However, in the interim, the Labour Court recommended the implementation of a limited initiative from January 1997 to address the immediate situation of nurses and midwives (other than nurses and midwives who already enjoy enhanced superannuation terms), who find the demands of the profession are such that they are no longer able to function at the level of professional performance they themselves and management require (LCR15450). The Court recommended that:

- an early retirement facility be introduced for nurses and midwives, aged 55 or over with at least 35 years' service, subject to a number of criteria which would underpin the delivery of a consistently high quality nursing service, limited to a quota of 200 per annum, to operate on a pilot basis pending the report of the CPSP; and
- the introduction of a pre-retirement initiative to facilitate nurses and midwives in reducing the amount of actual service commitment in the years immediately preceding their retirement. Nurses and midwives, aged 55 or over, who have 20 years' whole-time service and who do not otherwise enjoy enhanced superannuation benefits, may make application to work on a job-sharing basis for a maximum of three years prior to retirement, with the three years in question, or other lesser period, to reckon as full-time service for superannuation purposes. A quota not exceeding 600 applications was set for the initial three years operation of the scheme with up to a maximum of 300 applications being approved in year one.

2. It appears that there is generally a low uptake of the scheme. By early 1998 approximately 11 applications were made for early retirement and 16 applications for the pre-retirement scheme.

Commission on Public Service Pensions

3. The Commission on Public Service Pensions was established in February 1996 with the following terms of reference:

> *"to examine and report on the pension terms of public servants employed in the Civil Service (non-industrial and industrial), Defence Forces, Gardaí, Education, Health and Local Authority Services, having regard to:*
>
> *(1) the present and future costs arising under the schemes financed by the Exchequer;*
>
> *(2) claims for improvements in existing scheme benefits, including claims for voluntary early retirement;*
>
> *(3) changes in the working environment and conditions of employment of public servants since the schemes were introduced; and*
>
> *(4) the operational needs of the Services concerned."*

[6] Government of Ireland, *Report of the Commission on Nursing: A blueprint for the future* (1998), pp. 180-1.

The Commission on Public Service Pensions submitted an interim report to the Minister for Finance in August 1997.

4. The Commission considers that The Public Services Pension Commission (CPSP) in its examination of the totality of pension issues within the public service is in a better position to examine the difficult and complex pensions/retirement issues identified as being of concern to nurses and midwives during the consultative process. For this reason the ***Commission wrote to the CPSP outlining in detail the concerns of nurses and midwives in relation to retirement issues. The Commission understands that the CPSP is considering these issues within the context of its terms of reference.***

Options to Increase Pension Entitlement

5. The Commission was concerned that, during the consultative process, many nurses and midwives appeared unaware of the options available to them to increase their pension entitlement. These options may be availed of at the individual initiative of a nurse or midwife. Nurses and midwives need to take individual responsibility for planning their retirement. It is important for every nurse and midwife to understand what their pension/retirement entitlements will be, based on their work pattern and the level of pensionable service which they can expect to have, at retirement age. The options available to nurses and midwives to increase their pension entitlement include the purchase of notional service (to a maximum of 40 years) or the purchase of AVCs. The option most suited to an individual will depend on her or his circumstances. However, details in relation to the purchase of notional years or additional voluntary contributions should be available from either the personnel section within a health service provider or a nursing trade union. ***The Commission considers that health service providers have a responsibility in assisting nurses and midwives to plan their retirement by prompting discussion and making available information on the retirement and pension options which are readily available.***

PART II

Review of Public Service Occupational Pension Schemes and Costs

CHAPTER 3

Existing Public Service Occupational Pension Arrangements

3.1 Introduction

3.1.1 In Part II of the Report, we set out public service pension terms in detail and review the administration, management, and financing arrangements of public service pension schemes. We present a full actuarial review of public service pensions and consider the implications for pension schemes of changing operational requirements, work environment and conditions of employment of public servants.

3.1.2 In this Chapter, the Commission details the various occupational pension schemes applying in the public service. We outline the historical development of public service pension arrangements and set out the pension terms applying under each scheme. We pay particular attention to scheme development in the civil service and the local authorities because, historically, these schemes have been the standard reference or model for most other public service schemes (and, perhaps because of this, better information is available for both schemes).

3.1.3 Table 3.1 summarises the membership, pensioner numbers, and cost of pension schemes across the eight major sectors of the public service in 1997 (see Appendix 3.1 for more detailed statistics). The cost of public service pensions is examined in detail in Chapter 6.

Table 3.1: Summary of public service pension scheme numbers, pensioner numbers, and total annual pension costs for 1997

Sector	Estimated total no. of members	% of total scheme membership	Estimated total no. of pensioners	Estimated total annual pension cost*	
				Ir£ (m)	*Euro (m)*
Civil Service	29,058	14%	13,903	87	*110*
Local Authorities	23,993	12%	16,017	59	*75*
Education	56,149	28%	15,022	147	*186*
Garda Síochána	10,746	5%	5,492	58	*74*
Prison Officers	2,476	1%	252	2	*3*
Defence Forces	13,098	7%	11,129	57	*72*
Health Service	59,779	29%	13,367	85	*108*
NCSS Bodies	7,920	4%	2,000	14	*18*
Total	**203,219**	**100%**	**77,182**	**509**	***646***

* Excluding the cost of gratuities and lump sums.

3.1.4 Public service pension terms have changed considerably over the last 30 years in response to changing needs and requirements. The introduction of spouses' and children's pension schemes and a preservation of service facility are just two examples of the system's ability to respond to an obvious need. On the other hand, it will be seen that the essential principles on which public service pension schemes are based — some of which may now seem anachronistic — have remained fundamentally unchanged since the schemes were first introduced in the nineteenth century.

3.2 Overview of public service pension terms

3.2.1 Before examining individual schemes in detail, we summarise below the main features of public service occupational pension arrangements. Pension schemes in the public service are *defined benefit* schemes — the pension benefits payable are specified or defined in the rules of the scheme. Thus, the scheme member knows the calculation formula which will determine the level of benefits due at retirement. Furthermore, public service schemes are *final salary* defined benefit schemes — the benefits formula is based on the level of remuneration at the date of retirement.[7] Under the *defined benefit final salary* structure, for each year of pensionable service, a public servant will earn or accrue a retirement pension of 1/80th of pensionable remuneration, or of net pensionable remuneration in the case of a public servant in full PRSI class (see Paragraph 3.3.58), and a retirement lump sum of 3/80ths of pensionable remuneration. We examine other forms of pension structure — including defined contribution schemes — in Chapter 14 of the Report.

3.2.2 Table 3.2 sets out a general summary of standard public service pension scheme terms. In the summary, certain differences in terms between public service groups or individuals have been ignored.

3.2.3 The main variations from this general picture are in the area of retirement age. For example, Gardaí may retire at age 50 with 30 years' service and with each year after 20 counting double. Retirement from age 55, with various service conditions, applies in the case of other categories such as teachers. The Defence Forces also have special early retirement arrangements and a very different form of pension scheme.

3.2.4 A further variation is in the area of classification for State Social Insurance purposes. Most public servants are in modified class PRSI — they pay a lower rate of PRSI than applies to employees generally and do not qualify for a range of Social Insurance benefits, including pensions. A number of public servants are in full class PRSI — they pay the same rate of PRSI as other employees and, because they are entitled to Social Insurance pensions, their occupational pensions (and pension contributions) are subject to integration. The number of public servants whose occupational pensions and contributions are subject to integration will increase as a result of the Government decision that all public servants appointed on or after 6 April 1995 should be in full PRSI class.

3.2.5 The variations in terms between groups will become apparent in the following outline of pension terms in each part of the public service.

[7] Except where promotion or a personal change of salary took place in the final three years of service, in which case a three-year average applies.

Table 3.2: Standard public service pension terms[8]

Access	Automatic scheme membership for all permanent and many atypical employees
Eligibility for benefits	5 years' service (no minimum for death-in-service)
Pensionable service	Wholetime, temporary, part-time and job-sharing (pro rata), transferred, notional, and purchased service
Maximum service	Limit of 40 years
Retirement age	Age 65, optional from age 60
Pensionable remuneration	Final pay (averaged over final 3 years, if recently promoted) plus pensionable allowances (averaged)
Retirement pension	1/80th of pensionable remuneration per year of pensionable service up to a maximum of $\frac{1}{2}$ pensionable remuneration
Retirement lump sum	3/80ths of pensionable remuneration per year up to a maximum of $1\frac{1}{2}$ times pensionable remuneration
Integration (if full PRSI)	Pension calculation: pensionable remuneration is offset by twice the single rate of Old Age (Contributory) Pension (OACP)
Part-time employees	Each year worked (part-time) is treated as a full year's service; if full PRSI, integration is applied to actual remuneration, as above
Spouses' and Children's Scheme (S&C)	Spouse receives $\frac{1}{2}$ of member's pension ($\frac{1}{2}$ of potential pension to age 65 if death-in-service or following ill health retirement); children's pensions
Ill health benefits	Immediate benefits based on actual service plus up to 10 added years
Death-in-service	Gratuity of 1-$1\frac{1}{2}$ times pensionable remuneration, plus S&C pensions, if applicable
Contributions	5% main scheme, $1\frac{1}{2}$% S&C scheme (if full PRSI, part of contribution based on remuneration less OACP offset)
Early leaver (having five years' service)	Benefits preserved and payable from age 60, uprated in line with salary increases
Transfer of service	Between public sector organisations/groups
Early retirement	Not normally available before age 60
Retention beyond age 65	Infrequent; no reckoning of service beyond age 65
Options to individual to enhance pension	(i) Purchase of notional service at full actuarial cost; (ii) union-sponsored AVC schemes
Pension increases	In line with salaries (pay parity)
Financing of schemes	Pay-as-you-go cost met from annual revenues

[8] It is assumed that this is a public service scheme where an explicit main scheme contribution applies, and that the individual concerned is a member of the relevant spouses' and children's contributory pension scheme.

3.3 Civil service

Historical development of the Civil Service Pension Schemes[9]

3.3.1 The system of occupational pension provision now in place dates from a number of different pension arrangements in the eighteenth century which provided for the needs of British civil servants in their old age. These were formalised in nineteenth century legislation. No fund was ever established for civil service pensions, although an individual member contribution was introduced for a time. The first Superannuation Act devoted exclusively to pensions was in 1834. The 1859 Superannuation Act consolidated earlier changes in the Civil Service Pension Scheme. It fixed the pension accrual rate as 60ths of final salary after 40 years' service and provided for early retirement on grounds of ill health. A minimum retirement age of 60 was established on foot of an 1857 Commission of Enquiry report which concluded, *inter alia*, that at this age productivity often begins to decline due to old age or infirmity.

3.3.2 Legislation passed in 1909 introduced lump sum benefits[10] on retirement based on 30ths of pensionable remuneration and changed the accrual rate for pension from 60ths to 80ths to give a pension of one-half of pensionable remuneration plus lump sum after 40 years' service. Maximum lump sum of $1\frac{1}{2}$ times pensionable remuneration was payable after 45 years' service. The 1909 Act also introduced a death-in-service gratuity equal to the amount of annual pensionable remuneration, subject to a minimum of five years' service, and made provision for the payment of a balancing gratuity where death occurred shortly after retirement. The 1909 changes applied to male civil servants only. The Superannuation Act, 1914 provided that the death-in-service entitlement should be calculated as the more favourable of the amount of annual pensionable remuneration or the amount of lump sum which the civil servant would have received if he had retired on the grounds of ill health on the day of his death. The British administration granted increases to pensions in payment under the Pensions (Increase) Act, 1920.

3.3.3 Few changes were made to the pension scheme in the early years of the new State. Pensions (Increase) Acts were passed in 1950 (the first time public service pensions were increased by the Irish administration), 1956, 1959, 1960 and 1964. The Pensions (Increase) Act, 1964 provided for future indexation of pensions by means of Statutory Instrument instead of an Act of the Oireachtas.[11]

3.3.4 The 1909 changes were extended to female civil servants in 1954. The Superannuation Act, 1956 allowed civil servants to allocate part of their pension in favour of pensions for dependants. When Social Insurance Old Age (Contributory) Pensions were introduced in 1961, public servants with established civil service type pension entitlements were excluded from cover because their pension schemes were regarded as affording them adequate income protection on retirement.

3.3.5 The Superannuation and Pensions Act, 1963 introduced transferability of service within the public service and made available in limited form the granting of added years of notional service for those appointed to professional grades in the civil service (this was subsequently widened in an *ad-hoc* scheme formalised in 1985).

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[9] Material in this section is drawn from Hughes, G., *The Irish Civil Service Superannuation Scheme*, ESRI (1988), Appendix 1.

[10] It would seem that the purpose of changing the pension accrual rate to eightieths was to facilitate the introduction of the death-in-service gratuity (See Rhodes, G, *Public Sector Pensions*, George Allen & Unwin Ltd, 1965, pp. 21-22).

[11] The pensions covered by this provision are listed in the Schedule to the Act. They include the National Schools and Secondary Teachers' Superannuation Schemes, Garda Síochána pensions, civil service pensions, local authority and harbour authority pensions, and pensions payable by any body established by the Oireachtas. The most recent regulations made under the Act date from 1984, and there is a backlog of regulations to be made for the period since then.

3.3.6 A Committee on Post-Retirement Adjustments in Public Service Pensions was established in September 1964 and reported in March 1965. The Committee recommended that pensions should be increased in line with changes in the Consumer Price Index. However, in the 1969 budget, the Minister for Finance announced his decision in principle to adopt pay parity — i.e. to increase pensions in payment in line with salary increases — and to move towards it over a number of years. (A detailed note on the history of pension increases in the public service is given in Appendix 16.1.)

3.3.7 The Pensions (Abatement) Act, 1965 modified existing abatement provisions. With abatement, pension is reduced so that when added to the remuneration of any new position to which a pensioner is appointed, the sum is no greater than the remuneration of the position from which the pensioner retired. Prior to 1965, abatement applied in respect of civil service pensioners appointed to any position across the public service as a whole; following the 1965 Act, it was confined to appointments within the civil service only.

3.3.8 With effect from 23 July 1968, a contributory pension scheme was introduced to give pensions to widows and orphans of deceased civil servants. The scheme, known as the Civil Service Widows' and Orphans' Contributory Pension Scheme,[12] was put on a legislative basis by means of Statutory Instrument in 1977. A non-contributory *ex-gratia* widows' and orphans' scheme was introduced in respect of civil servants who retired or died before the effective date of the contributory scheme. Up until 1981, female civil servants were excluded from the widows' and orphans' scheme.

3.3.9 Prior to 1970, non-established civil servants had no occupational pension coverage. With effect from 1 January 1970, a non-contributory pension scheme was introduced for such employees. As non-established civil servants were in full class PRSI, unlike established civil servants, the scheme was subject to integration with the Social Insurance system. A contributory widows' and children's pension scheme for non-established state employees was introduced from 1 December 1978. Both of these schemes have operated and continue to operate on an administrative basis.

3.3.10 Certain changes in the Civil Service Pension Scheme were introduced with effect from 1 June 1973 arising from a joint management/staff working party report which was endorsed by the General Council under the Scheme of Conciliation and Arbitration for the civil service. These included:

- an increase in the fraction used in calculating retirement lump sums and death gratuities from 1/30th to 3/80ths per year of service, thereby providing for maximum lump sum of $1\frac{1}{2}$ times pensionable remuneration after 40 years instead of 45 years;
- the reckoning of service in days rather than completed years;
- the reckoning of prior part-time service;
- the grant of added years on ill health early retirement;
- a reduction in the qualifying period for retirement benefits from ten to five years;
- the abolition of the minimum qualifying period (five years) for death gratuity and widows' and children's pension in case of death-in-service;

[12] As a result of the 1973 joint management/staff working party report, the terms of the Widows' and Orphans' Contributory Pension Scheme were widened and the title changed to the Widows' and Children's Contributory Pension Scheme.

- the abolition of the *break-in-service* rule in relation to the reckoning of prior service (previously, if an employee had a break in service, the earlier period did not reckon for pension purposes);
- preservation of pension rights after five years' service for those in employment on or after 1 June 1973 (see Paragraph 3.3.44);
- the purchase of notional added years at the officer's expense (this was implemented in a Department of Public Service Circular in 1979).

Many of these changes were given legislative effect in the Civil Service Superannuation Regulations, 1980 drawn up under the Superannuation and Pensions Act, 1976 (see Paragraph 3.3.14).

3.3.11 The *marriage bar* which required women to resign from the civil service on marriage was removed with effect from 31 July 1973.

3.3.12 In 1974, the upper income limit applying to the insurability of non-manual workers under the Social Insurance system was abolished with the result that a large cohort of employees, including many public servants, were brought into full Social Insurance for the first time while many other public servants (who had been above the income limit) came into the lower rate of modified insurance for the first time.

3.3.13 In 1975, in line with the 1969 commitment to pay parity, provision was made for automatic increases in pensions from 1 July each year in line with increases in salaries in the civil service. This was later amended to increase pensions from the same effective date as that of increases applied to salaries of civil servants.

3.3.14 The Superannuation and Pensions Act, 1976 enabled the Minister for Finance to make pension schemes in respect of the public service, to amend or repeal certain provisions of the Superannuation Acts, 1834 to 1963, and certain other enactments, and to make provision for related pensions matters.

3.3.15 In 1981, the Widows' and Children's Contributory Pension Scheme became the Spouses' and Children's Contributory Pension Scheme when it was extended to include all female civil servants appointed on or after 1 June 1981. Female civil servants appointed prior to that date were given the option to join. In 1984, the scheme was revised to cover all children of a member, regardless of the member's marital status, and to include the spouses of post-retirement marriages. More restrictive provisions for refunding contributions were introduced as a means of financing these improvements. The option to join the revised scheme was extended to all civil servants, whether in the existing scheme or not, and to all pensioners and surviving spouses of pensioners in respect of whom the option to join the original scheme had been given.

3.3.16 Job-sharing and career break schemes were introduced in 1985 and 1986, respectively.

3.3.17 In 1987-88, a limited voluntary early retirement scheme was introduced and ran for a number of years with the objective of reducing numbers in the civil service[13] (this was later extended to other areas of the public service).

[13] Approximately 1,250 civil servants availed of the scheme (this figure excludes industrial non-established civil servants), which represented 4.2% of all serving civil servants on 1 January 1988.

3.3.18 In 1987, the Government decided that enhanced pension benefits should be granted to Secretaries of Departments coming within the remit of the Top Level Appointments Committee (TLAC) who reach the end of their seven year terms before age 60 or who are required to retire at age 60 or between 60 and 65.

3.3.19 Arrangements to allow civil servants to avail of union-sponsored additional voluntary contribution (AVC) schemes to enhance their pension benefits were introduced in 1987 (as an alternative to the scheme for purchase of notional added years).

3.3.20 In 1995, the Government decided that all established civil servants (and public servants generally) appointed on or after 6 April 1995 should be in full PRSI class, thus giving them an entitlement to State Social Insurance pensions. Integration of contributions and benefits apply as part of the new pension arrangements.

3.3.21 New entrants from open competitions held since 1997 for the grades of Administrative Officer, Third Secretary, and Executive Officer are appointed on a one year contract basis subject to assessment during the period of contract. At the end of this period, should they be deemed satisfactory, they are offered an established position on probation. If they are judged not to be satisfactory, their appointment is terminated.

Coverage of Civil Service Pension Scheme

3.3.22 Employment in the civil service (including the prison service) comprises 15% of total public service employment. There are two main categories of position in the civil service: established and non-established personnel. **Established** civil servants are those recruited by means of competitions held by the Civil Service Commission. They are permanent employees and their employment can only be terminated by the Government. A certificate of qualification must have been issued under Section 26 of the Civil Service Commissioners Act, 1956 or a person must be deemed under Section 27 of that Act to possess such a certificate.

3.3.23 **Non-established** civil servants are those employed in a wholetime capacity by a government department or office who are not established civil servants and in respect of whom special pension arrangements have not been made.[14] This definition covers certain employees who are not civil servants in the strict legal sense, e.g. civilian employees attached to the Defence Forces (who number about 1,200) and manual employees in Garda stations. Non-established civil servants may be recruited in the same way as established personnel; however, appointments to certain positions such as Services Officer, etc., may be made by individual departments. They are often employed in a situation where the long-term necessity of a particular position is not obvious, or where it is deemed desirable that personnel should undergo a trial period in a non-established capacity before being appointed in an established capacity. Non-established civil servants can be dismissed by the Minister of the relevant department.

3.3.24 The Civil Service Pension Scheme is set out in the Superannuation Acts, 1834 to 1963, the Superannuation and Pensions Act, 1976, various Statutory Instruments made under those Acts, and circulars issued by the Department of Finance.[15] There are separate main schemes and spouses' and children's schemes for established and non-established civil servants. We set out the

[14] Department of Finance, "Superannuation Handbook: A Guide to the Superannuation Provisions applicable to Civil Servants" (Revised, 1998), Part 2, Chapter 3.
[15] During the period 1973-87, the Department of the Public Service had primary responsibility for the Civil Service Pension Scheme.

pension terms for both groups below. The variation in terms arising out of the extension of full PRSI to entrants appointed after April 1995 is shown separately.

3.3.25 Membership of the main pension scheme is automatic for all established civil servants.[16] Membership of the spouses' and children's contributory pension scheme is automatic for all civil servants appointed in an established capacity after 31 December 1968, in the case of male civil servants, and 31 May 1981, in the case of female civil servants. The scheme was optional for civil servants appointed in an established capacity before those dates.

3.3.26 On appointment, non-established civil servants automatically become members of the non-established pension scheme, with the exception of temporary civil servants appointed under certain short-term non-renewable contracts (see Paragraph 3.3.27). Membership of the spouses' and children's contributory pension scheme is automatic for all male non-established civil servants made pensionable under the main scheme after 30 November 1978, and for all female non-established civil servants made pensionable after 31 May 1986. The scheme was optional for those pensionable before those dates.

3.3.27 Temporary non-established civil servants appointed on short-term contracts are generally admitted to the pension scheme on the basis that:

- such appointments, even if it is not specifically stated, are often renewable; and
- death-in-service cover is provided by inclusion in the scheme.

In a small number of cases, non-established civil servants who are not admitted to the pension scheme are paid an addition of up to 11% of salary with which to make their own personal pension arrangements.

3.3.28 Atypical employees are not generally recruited to the civil service, although as already noted, temporary employees have been appointed as non-established civil servants in the past. Recently, panels have been set up for the appointment of temporary and part-time established civil servants at the grades of Clerical Officer, Executive Officer and Administrative Officer. In the future, temporary requirements among these grades may be met in the first instance from the new atypical panels. With changes to the job-sharing and career break schemes, there will be resulting staffing gaps which will be filled with temporary part-time employees.

Pension terms of established civil servants appointed prior to 6 April 1995

3.3.29 On retirement on age, ill health or redundancy grounds, an established civil servant, having at least five years' pensionable service, qualifies for:

(i) a **pension** of 1/80th of pensionable remuneration per year of pensionable service subject to a maximum of one-half of pensionable remuneration; and

(ii) a **lump sum** of 3/80ths of pensionable remuneration per year of pensionable service, subject to a maximum of one-and-a-half times pensionable remuneration.

3.3.30 **Retirement age** is 65, although a civil servant may retire with immediate payment of pension benefits at any time after age 60 (with no actuarial reduction to allow for the longer period over which the pension will be paid).

[16] Traditionally, membership of the scheme has applied to civil servants who are capable of giving five years' pensionable service by age 65 on the basis that this is the minimum period required to qualify for retirement benefits.

3.3.31 Pensionable remuneration includes salary and pensionable emoluments. Salary is defined as the actual rate of salary held on the last date of pensionable service, except where there has been a promotion or a personal increase in salary in the last three years of service, in which case it is calculated as an average over those three years. If a civil servant is job-sharing at retirement, pensionable salary is based on the salary which would have been payable if he or she had been working in a full-time capacity. Pensionable emoluments include allowances in the nature of pay, but do not include overtime, gratuities, or expense payments (see also Paragraphs 22.9.8-22.9.15). Pensionable emoluments are averaged over the final three years of service (this is known as the *three-year averaging rule*).

3.3.32 Pensionable service includes actual paid service as an established civil servant, paid temporary service, service transferred from elsewhere in the public sector under the Transfer of Service Scheme, notional service granted in certain circumstances, and any additional service purchased by the civil servant under the purchase scheme. Job-sharing service reckons as half of full-time service. Total pensionable service cannot exceed 40 years.

3.3.33 There is provision to grant **notional added years** (maximum ten years) for professional civil servants under Section 6 of the Superannuation and Pensions Act, 1963 and for professional, technical and specialist civil servants under the *ad hoc* added years scheme, which was introduced in 1985. The latter scheme, amended in 1997, is more commonly used than the former. Generally, these arrangements apply where it is not possible to appoint a person before age 25 because of the particular experience/qualification requirements of the position. We set out further details on the grant of notional added years in Section 22.3.

3.3.34 A civil servant may qualify for **ill health early retirement benefits** arising from permanent disability, provided he or she has at least five years' pensionable service. Pension and lump sum are calculated as outlined above, except that account is taken of an additional period of notional service of up to ten years (usually, six and two-thirds years), calculated by reference to the length of actual service given and potential service to retirement age. In certain very limited circumstances a special higher rate of pension (Injury Warrant) may be payable to a civil servant who is forced to retire because of injury sustained in the performance of official duties, or to his or her spouse and children where the injury results in death.

3.3.35 A civil servant appointed from a competition advertised prior to 1 February 1974 who has at least five years' actual reckonable service prior to marriage, and who resigns from the civil service on or shortly before marriage, or within two years thereafter, may apply for the award of a **marriage gratuity**, which would be in lieu of any other civil service pension benefit. The amount of the gratuity is one month's pay for each year of reckonable service (pro rata for part of a year) up to the date of marriage, subject to a maximum of 12 months' pay.

3.3.36 If **reappointed**, the civil servant may elect to refund the marriage gratuity, and in doing so, all prior service will be aggregated with subsequent service for pension purposes. Refunds may be made (in instalments, if desired) during service, or by deduction from final pension awards. Compound interest — at the rate of 6% per annum — is charged on refunds made by civil servants who are reappointed in the normal course (e.g. through a competition of the Civil Service Commission). No interest is charged in the case of civil servants reinstated through statutory provisions pertaining to widowhood or non-support by spouses (reinstatement is no longer available since 1996).

3.3.37 **Secretaries General** of government departments appointed by TLAC (see Paragraph 3.3.18) who reach the end of their seven year term before age 60 may, with the agreement of the Government, be allowed the option of early retirement with enhanced pension benefits. The enhanced benefits consist of an award of up to ten added years and a special severance gratuity of six months' salary on the terms specified in Sections 6 and 7 of the Superannuation and Pensions Act, 1963. These arrangements are normally granted subject to special abatement conditions should the individual concerned subsequently be appointed, below age 65, to any public sector position following retirement.

3.3.38 There is provision for **early retirement** for reasons of **improving efficiency and economy** and **on abolition of office** under the Superannuation and Pensions Act, 1963 and the Superannuation Act, 1909. Pension benefits are paid immediately and up to ten notional added years may be included in pensionable service. A special severance payment of up to one-half of salary may be paid. These terms have been used relatively infrequently. The terms available under the civil service voluntary early retirement (VER)[17] scheme are less beneficial, as the maximum added years award is seven years, and is confined to those with more than 20 years' service. Under the VER scheme, a severance gratuity of three weeks' pay per year of potential service to age 65 (subject to a maximum of 27 weeks' pay) is payable as an alternative to an added years award.

3.3.39 A **short service gratuity** is payable where a civil servant retires on grounds of permanent incapacity having at least one but less than five years' pensionable service. The gratuity is one-twelfth of pensionable remuneration for each year of reckonable service (with pro rata entitlement for part of a year). In addition, if the civil servant has a minimum of two years' reckonable service, a lump sum equal to 3/80ths of pensionable remuneration multiplied by the number of years of reckonable service is payable (with pro rata entitlements for part of a year).

3.3.40 On **death-in-service**, a death gratuity is payable to the legal personal representative (if less than £15,000, the gratuity is paid direct to the person who appears to be beneficially entitled to it). The gratuity is a minimum of the amount of pensionable remuneration or, if greater, the lump sum that would have been payable if the civil servant had retired on ill health grounds on the date of death (subject to a maximum of $1\frac{1}{2}$ times pensionable remuneration).

3.3.41 A **balancing gratuity** is paid where a civil servant dies shortly after retirement and where the total amount of lump sum and pension paid up to the date of death is less than the annual amount of pensionable remuneration at time of retirement. The gratuity is equal to the amount of the shortfall and is payable to the legal personal representative.

3.3.42 **Spouses' and children's pensions** are also payable on death, provided the civil servant was a member of the spouses' and children's pension scheme (or where the *ex gratia* widows' and children's pension scheme applies, in respect of those who retired or died before 23 July 1968). Where the civil servant dies after retirement in the normal course, the spouse's pension is one-half of the pension in payment on the date of death. Where the civil servant dies in service, or dies subsequent to retirement on ill health grounds, the spouse's pension is one-half of the retirement pension that would have applied had the civil servant served to age 65.

3.3.43 A pension equivalent to one-sixth of the deceased's entitlement is payable in respect of

[17] The VER scheme operated on a general basis in the civil service in the period from mid-1987 to the end of 1988 (see Paragraph 3.3.17). Since then, it has been offered in a small number of instances where officers were deemed surplus to requirements.

a dependent child, defined as a child under the age of 16, a child between the age of 16 and 22 in full-time education or vocational training, and a child with a disability (who may qualify for a child's pension for life). A higher rate of child's pension (one-third of the deceased's pension entitlement) is payable where no spouse's pension is being paid. A maximum of one-half the deceased's pension applies to the total amount of children's pensions payable.

3.3.44 **Preservation of benefits** applies to any established civil servant who resigns prior to age 60 (on or after 1 June 1973) having at least five years' service. Under preservation, accrued pension entitlements are *frozen* at the time of leaving service and can be claimed on reaching age 60. Benefits are based on pensionable service and pensionable remuneration at the date of leaving, the latter uprated by pay increases applied to the former civil servant's grade since the date of leaving. A preserved death gratuity is payable if death occurs before age 60. Assuming membership of the spouses' and children's scheme, pensions may also be payable to the member's dependants. A preserved pension and lump sum may be paid where the individual becomes incapable of working before age 60. In all circumstances, preserved entitlements are based on actual accrued service only.

3.3.45 As an alternative to preservation, if a former civil servant takes up employment in another area of the public sector, he or she has the option under the **Transfer of Service Scheme** to transfer the period of pensionable service to the new pension scheme (usually without the necessity for a transfer payment between the two schemes). If the civil servant has less than five years' service on leaving, and does not transfer service to another public sector organisation, his or her contributions under the spouses' and children's contributory pension scheme are refunded.

3.3.46 **Pension increases** are applied in line with, and with effect from, the operative date of any relevant pay increases. Pensioners benefit from all general pay increases and, in general, from special pay increases which apply to their former grade as a whole. The pensions increase policy is set out in more detail in Appendix 3.2.

3.3.47 Established civil servants appointed before 6 April 1995 do not make an explicit **contribution** under the main pension scheme. However, for pay determination purposes, it has been accepted in a number of arbitration findings in the past that an implicit contribution is made through salary being set at a lower level to take account of the benefits payable under the pension scheme (we discuss this matter in Section 11.9). An explicit periodic contribution of $1\frac{1}{2}$% of remuneration is made in respect of membership of the spouses' and children's contributory pension scheme. A further contribution of 1% of pensionable remuneration is made by deduction from retirement lump sum or death gratuity in respect of each year of pensionable service for which periodic contributions have not been made (this applies only in respect of married civil servants).

3.3.48 A scheme for **purchase of notional service** was introduced for civil servants serving in an established capacity on or after 1 April 1979. The scheme was revised in 1990. Subject to certain conditions, it enables civil servants to purchase additional years of service by means of periodic or lump sum contributions. Appropriate actuarial tables are applicable. The scheme is intended to be self financing. Further details of the scheme are provided in Section 12.10.

3.3.49 **Additional voluntary contributions** (AVCs) — in the form of union-sponsored schemes — were first approved by the Department of the Public Service in a letter to Personnel Officers dated 19 February 1987. As an alternative to the purchase scheme, AVCs enable additional pension benefits to be obtained by means of payments to an outside agency in circumstances where there would be a shortfall of service at retirement or where ultimate pension benefits would fall short of the limits set by the Revenue Commissioners. AVCs can also be used to enhance death-in-service cover. Further details are contained in Section 12.12.

3.3.50 Section 1 of the Pensions (Abatement) Act, 1965 provides for the **abatement of pension** of civil service pensioners who are re-employed in the civil service; abatement does not apply on employment elsewhere in the public service. Under this provision, the pensioner's total income from pay and pension should not exceed the salary which would have been payable had the civil servant not retired. The Minister for Finance may waive the abatement if it is in the public interest to do so, e.g. if there are no practical alternatives for carrying out a particular body of work. The section only applies to civil service appointments; it does not, for example, apply to persons employed on a fee-paid basis. However, it is the general policy in fixing fees in such cases to pay a reduced amount to take account of the pension wherever practicable.

3.3.51 **Allocation of pension** — introduced in the Superannuation Act, 1956 — enables a civil servant at retirement to surrender part of his or her pension to provide a separate pension for a nominated beneficiary, usually a spouse and/or dependent relative. The allocated pension is determined by standard actuarial factors. Once the allocation is made, the retired civil servant's pension is payable at the reduced rate, i.e. less the deduction of the amount surrendered for the duration of the payment of pension, even if the nominated beneficiary predeceases the retired civil servant. The allocation facility was introduced at a time when there was no spouses' and children's scheme in place; however, since the latter was established, it has rarely been used.

3.3.52 Prior to 1994, **forfeiture** of entitlement to pension benefits applied in the case of civil servants who (for whatever reason) were dismissed from their posts, or resigned so as to pre-empt dismissal. With effect from 1 January 1994, however, such former civil servants retain their entitlement to pension benefits (preserved, if they are under age 60), subject to the provision that in cases involving financial loss to the Exchequer, the amount of the loss, plus interest, is recouped by deduction from the benefits payable.

3.3.53 Under a 1995 provision, **compensation** is payable in the case of delays of more than one year in payment of pension benefits due. Compound interest based on changes in the Consumer Price Index is applied to the amount of benefit outstanding.

Pension terms of established civil servants appointed on or after 6 April 1995

3.3.54 The terms set out above apply to established civil servants who are in modified (Class B) PRSI. New entrants appointed as established civil servants on or after 6 April 1995 are in full (Class A) PRSI and their pensions are integrated with the State Social Insurance system. The purpose of integration is to take account of Social Insurance benefits in making up a portion of replacement income at retirement. Integration applies to both pension and contributions. Lump sum is unaffected.

3.3.55 Where a person is appointed direct to a position from another part of the public service where he or she had been in modified PRSI class immediately before appointment or from a non-established position in the civil service[18] which had been held continuously since before 6 April 1995, the pension arrangements for modified PRSI class civil servants described above will apply.

[18] Non-established civil servants were already fully insurable under the Social Welfare Acts prior to the April 1995 change. A condition of service for those employed before 6 April 1995 is that should they subsequently be appointed to established positions, their PRSI status changes to the lower modified rate.

3.3.56 Where an established civil servant in full PRSI class has previous service in the public service in respect of which he or she has paid modified PRSI contributions, a once-off option may be exercised at any time up to the date of retirement in favour of:

- aggregating all such prior service with future service under the pension terms applying to civil servants in full PRSI class; or
- retaining all preserved pension benefits in respect of the previous service, in which event only the future service would be governed by the new terms.

3.3.57 The main differences in the arrangements for civil servants in full PRSI class compared with those for civil servants in modified PRSI class are:

- an explicit main scheme contribution applies. The contribution comprises $3\frac{1}{2}$% of net remuneration (as defined in Paragraph 3.3.58) in respect of pension and $1\frac{1}{2}$% of remuneration in respect of lump sum. A separate contribution rate of $1\frac{1}{2}$% of remuneration applies in respect of the spouses' and children's contributory pension scheme;
- the salary scales of new entrants are uplifted to 20/19ths of the salary scale applicable to civil servants in modified PRSI class;
- pension is calculated on the basis of net pensionable remuneration (as defined in Paragraph 3.3.58), while the lump sum or death gratuity is calculated on the basis of pensionable remuneration (as defined in Paragraph 3.3.31 above).

3.3.58 **Net remuneration** is defined as current salary plus pensionable emoluments, less twice the maximum rate of Social Insurance Old Age (Contributory) Pension (OACP) payable to a single person with no dependants. **Net pensionable remuneration** is defined as salary plus pensionable emoluments at date of retirement, less twice the maximum rate of OACP payable to a single person with no dependants. The deduction is sometimes known as the *Social Welfare offset*. In the case of spouses' and children's benefits, the calculation of net pensionable remuneration is adjusted upwards by means of deducting once rather than twice the maximum single rate of OACP.

3.3.59 The total pension (occupational pension plus OACP[19]) payable to a civil servant in full PRSI class is the same, after 40 years' service, as that payable to a civil servant in modified PRSI class (i.e. 50% of pensionable remuneration). To take an example, where a civil servant in full PRSI class retires after 40 years' service and is in receipt of a salary of £25,000 at retirement (assuming there are no pensionable emoluments), pension is calculated as in Table 3.3.

Table 3.3: Pension for a civil servant in full PRSI class retiring with pensionable remuneration of £25,000 and 40 years' service

Net pensionable remuneration:	£25,000 – (2 × £5,009)[20] = £14,982
Occupational pension:	£14,982 × 40/80 = £7,491 per annum
Total pension:	£7,491 + £5,009 (OACP) = £12,500 per annum (i.e. 50% of pensionable remuneration)

[19] This excludes any additional amount which may be payable in respect of qualifying adult or child dependants.
[20] OACP (May 2000) = £96 × 52.18 weeks = £5,009.

3.3.60 A **supplementary pension** is payable in respect of periods during which the pensioner is not employed in any capacity which involves a Social Insurance contribution and, due to causes outside his or her control, fails to qualify for Social Insurance benefit or qualifies for such benefit at less than the maximum personal rate of OACP. The rate of supplementary pension will be sufficient to bring the occupational pension to the rate which would have been payable had it been based on pensionable remuneration instead of net pensionable remuneration.

Part-time civil servants

3.3.61 While there are no formal pension terms in place for part-time established civil servants in full PRSI class, it is envisaged by the Department of Finance that pensionability will be conditioned as follows:

(i) the part-time civil servants concerned must be in regular, quasi-permanent employment (including wholetime temporary, regular temporary or seasonal workers, etc.);

(ii) they must be working a minimum of 8 hours per week where the full-time equivalent week is 39 hours;

(iii) full integration of actual pensionable remuneration with the Social Insurance OACP in the case of one part-time job must apply — but subject to appropriate adjustment in the case of more than one part-time job to ensure that the total Social Welfare offset is not more than twice the personal rate of OACP;

(iv) each year of part-time service must count as one year's service;

(v) there must be an appropriate adjustment to actual pensionable remuneration where hours vary substantially during service.

Prison Officers

3.3.62 Prison Officers are civil servants and so are covered by the Civil Service Pension Scheme. The Superannuation (Prison Officers) Act, 1919 made certain changes to pension terms to take account of the much higher standard of physical efficiency required of a Prison Officer all through service and the extra strain of working in a prison environment. These changes enabled Prison Officers to retire on or after age 55 (rather than age 60) with their service in excess of 20 years counting as double in the calculation of pension benefits (thus, maximum benefits are payable after 30 years' actual service). The maximum retirement age is set at age 60. The terms were amended in 1983 to allow Prison Officers the option of retiring from age 50 with immediate pension provided they had 30 years' actual service in the prison service.

Non-established civil servants

3.3.63 Non-established civil servants, including industrial civil servants, civilian employees attached to the Defence Forces, and manual employees working in Garda stations, have broadly the same pension terms as established civil servants paying full class PRSI, with the following exceptions:

- there is no pension contribution under the main scheme;
- the contribution rate under the spouses' and children's contributory pension scheme is $1\frac{1}{2}$% of net remuneration rather than of remuneration, as in the case of established civil servants in full PRSI class. Net pensionable remuneration is not readjusted when calculating spouses' and children's pensions, unlike the position set out at Paragraph 3.3.58;

- the retirement age is 65/66 years, with no provision to retire at an earlier age other than on grounds of ill health;
- non-established civil servants are not eligible for the award of professional added years;
- the death-in-service arrangements are similar to those for established civil servants, with the exception that where the deceased was married, there is discretion to pay the death gratuity to the spouse, rather than to the legal personal representative;
- *compassionate gratuities* are payable to part-time non-established civil servants who have worked for ten or more hours per week and have completed five years' service. They are payable on retirement after age 60 and are calculated at the rate of one week's pay for each year of service up to 15 years, and two weeks' pay for each subsequent year, subject to a maximum of 78 weeks.

3.4 Local authorities

Historical development of the Local Government Superannuation Scheme

3.4.1 The Minister for the Environment and Local Government has responsibility for the Local Government Superannuation Scheme (LGSS), which is governed by the Local Government (Superannuation) Act, 1980. Schemes made under the 1980 Act are subject to the consent of the Minister for Finance.

3.4.2 The LGSS has its origins in the Union Officers' Superannuation (Ireland) Act, 1865. That Act provided for the grant by Poor Law guardians of annual allowances not exceeding two-thirds of salary at retirement/resignation to wholetime officers[21] of Poor Law unions in Ireland, with the consent of the Poor Law Commissioners. Officers had to be at least 60 years of age and retirement/resignation had to be on the grounds of permanent infirmity or old age. The terms of the Act were later extended to cover other officers, and a definition of local authorities was introduced. The first pension scheme which provided benefits to non-officer grades appears to have been the Dublin Corporation Superannuation Act, 1905. (As indicated above, non-established employees in the civil service were not made pensionable until 1970.)

3.4.3 A series of Acts followed which modified, but did not alter substantially, the above provisions. A major change was made in the Local Government (Superannuation) Act, 1948, which forms the basis for the present pension arrangements. Under the Act, a contributory code for both officer and non-officer grades was introduced and the accrual rate for pension was changed from 60ths to 80ths for officers, thus providing for a maximum pension of one-half of pensionable remuneration after 40 years. Provision was made also for the payment of a lump sum at the rate of 1/30th of pensionable remuneration per year of service up to a maximum of $1\frac{1}{2}$ times pensionable remuneration after 45 years. These changes were in line with changes previously made in the Civil Service Pension Scheme. The pension entitlements of non-officers continued to accrue on the basis of 60ths with a maximum pension entitlement of two-thirds of pensionable remuneration after 40 years' service. Provision for payment of death gratuities was introduced under the 1948 Act for both officers and non-officers.

3.4.4 The Local Government (Superannuation) Act, 1956 replaced earlier pension provisions. The Act improved substantially the pension conditions of non-officer grades in a number of ways,

[21] The terms *officer* and *non-officer* have particular legal implications in the local authority structure. The two classes of personnel are broadly equivalent to established and non-established civil servants (see also Paragraph 3.4.8).

in particular, by making eligibility for pensionable status in any case subject to a single objective requirement of a minimum of 200 service days in a single financial year.

3.4.5 A revised local authority scheme was introduced on an administrative basis in 1977. The purpose of the scheme was essentially to bring it into line with changes which had been introduced in the civil service with effect from June 1973 (see Paragraph 3.3.10), and to take account of the fact that non-officers were fully insurable under the Social Welfare Acts. The changes implemented in respect of non-officers included the replacement of the 60ths accrual rate with an 80ths accrual rate for new entrants, and the introduction of integrated pension arrangements with effect from May 1977. Under the latter, pension continued to be based on pensionable remuneration for service prior to the cut-off date, but net pensionable remuneration was used for service after the cut-off date. Preservation of benefits for all local government personnel was also introduced from this time.

3.4.6 The Local Government (Superannuation) Act, 1980 enabled the detailed arrangements governing the pensions of local authority staff to be set out in statutory form. Over 30 schemes have been made under this legislation, the latest being the Local Government (Superannuation) (Consolidation) Scheme, 1998 which consolidates and updates the provisions of all earlier Acts and schemes. It covers all aspects of local government pension arrangements, such as personal pension benefits, spouses' and children's pensions, transfer of service, and the purchase of notional service. A number of circular letters also apply.

Pension terms of local authority officers and employees

3.4.7 Reflecting the historical development of local authority structures in Ireland, the LGSS has applied to the personnel not just of the local authorities but also of the Health Boards and Authorities, Vocational Educational Committees (VECs), Institutes of Technology, and certain local government and health corporate bodies. In total, the scheme has provided for the pensions of about 37% of public service employees. Employment in the local authorities themselves comprises about 12% of public service employment. Recently, responsibility for the pensions of vocational teachers has been transferred to the Department of Education and Science and the transfer of the remaining pension functions of VECs and Institutes of Technology is under active consideration. In addition, consideration is being given to transferring the pension arrangements for Health Boards and statutory health bodies to the Department of Health and Children.

3.4.8 The LGSS covers two categories of personnel: officers and non-officers. While there is no simple definition of either category, generally, local authority officers are engaged in administrative, technical, and professional duties, while non-officers are engaged in manual work. Different rules of admission apply to both groups:

- membership is automatic for **officers** appointed to permanent positions or under contract to temporary wholetime positions where the contracts of employment are potentially renewable (prior to 1 January 1998, only permanent wholetime officers could become members);
- membership is automatic for **non-officers** on completion of 130 days' service in a calendar year, with no minimum number of service days needed in subsequent years.

3.4.9 On being made pensionable, officers are required to pay contributions for any previous temporary (including part-time) service they may have accrued. Those in full PRSI class pay contributions owed on a current salary basis, i.e. for each year of temporary service, a contribution level equivalent to current rates must be paid. Officers in modified PRSI class pay for any temporary service on an historic salary basis, i.e. contributions owing are determined by reference to the appropriate salary at the time of temporary employment. In the latter situation, an officer has three years from notification of the amount due to pay the outstanding contributions. Failure to do so within this period results in the application of compound interest, the rate of which is determined by whether the period of service was before or after 31 December 1983. In the former instance a rate of 7% applies, and in the latter a rate of 6% applies.

3.4.10 The payment of contributions for previous temporary service is different in the case of non-officers as there is no requirement to make such service reckonable for pension purposes. However, the automatic entry into the scheme after 130 days' service means that should a non-officer opt to pay the appropriate contributions for such past service, the amount owing will be small. Payment is determined on an historic rather than a current salary basis. If the contribution is not paid within an agreed period, the service is deemed to be non-pensionable. In practice, it would appear that most non-officers choose to make reckonable all previous temporary service.

3.4.11 As in the civil service, marriage gratuities may be repaid in order to reckon service given prior to leaving on marriage. Compound interest, at the rates set out in Paragraph 3.4.9, is charged in the case of re-employments in the normal course occurring after 27 May 1977. Personnel re-employed following widowhood are required to repay the original gratuity only, i.e. no compound interest is applied.

3.4.12 Local Authority Managers have broadly similar terms to Secretaries General in the civil service appointed by TLAC (see Paragraph 3.3.37).

3.4.13 Apart from the above, officers and non-officers covered by the LGSS have, with the following exceptions, the same pension terms as established and non-established civil servants, respectively:

- non-officers may retire between the ages of 60 and 65, whereas non-established civil servants must retire at age 65/66;
- in the case of officers retiring from posts designated as *professional* under the Local Authority (Officers and Employees) Act, 1926, an addition of up to one-third is made to reckonable service, subject to a maximum of ten years, where retirement takes place after 60 years of age — this is a less restrictive form of the *notional added years* applying in the civil service (see Paragraph 3.3.33);
- the changes introduced into the civil service scheme with effect from 1973 (see Paragraph 3.3.10) apply in the LGSS automatically for new entrants from June 1978, and subject to option for personnel in service between May 1977 and May 1978;
- persons who became pensionable before 1 February 1995 have the option on resigning to take a refund of main scheme and spouses' and children's scheme contributions for service given prior to that date, as an alternative to preserving benefits or transferring service;
- it was agreed in 1996 that part-time non-officer grades would be admitted to the LGSS on an optional basis (subject, generally, to the terms set out at Paragraph 3.3.61). Contributions and benefits are integrated;

- a main scheme pension contribution of 5% of pay applies in respect of all personnel. Part of the contribution is integrated for non-officers (post-May 1977 service) and for officers appointed on or after 6 April 1995;
- given that a 5% pension contribution already applied, no uprating of salary took place when full PRSI was introduced in respect of officers appointed on or after 6 April 1995;
- in February 1996, a minimum death gratuity of £12,000 was introduced for non-officers. It is indexed in line with pay increases and is paid on a pro rata basis in the case of part-timers;
- personnel employed in the psychiatric services, principally Psychiatric Nurses, who come under the LGSS and are registered under the 1945 Mental Treatment Act, have the option to retire at age 55, and must retire at age 65. Service in excess of 20 years' counts as double, and so maximum benefits are payable after 30 years' service;
- Fire Officers and Firefighters have similar pension terms to those applying in the psychiatric services, except that Firefighters are generally required to retire at age 55 (Fire Officers may remain in service until age 65).

3.5 Health service

Historical development of pension schemes in the health service

3.5.1 The structure of the modern health system is based on the 1970 Health Act which established eight Health Boards and set out how the health service was to be managed, structured, operated and financed. Today the acute services are administered by distinct hospital systems – the voluntary public hospitals, hospitals set up as corporate bodies,[22] and the Health Board hospitals. Some of the voluntary public hospitals are partly owned by religious orders, run by boards of governors and administered by boards. All but a minor part of the current hospital expenditure is met by public funds with the exception of private hospitals – some of which are also nurse training schools. Services for people with a mental disability are mainly provided by voluntary organisations.

3.5.2 It would appear that health service personnel first became pensionable under the local authority superannuation code, which had its beginnings in the Union Officers' Superannuation (Ireland) Act, 1865 (see Section 3.4). The provisions of the 1865 Act were applied to medical officers of Poor Law unions (and of dispensary districts of such unions) by the Medical Officers' Superannuation (Ireland) Act, 1869. Pension terms were similar to those applying to civil servants. Special pension terms applied to persons working in asylums – these date as far back as the 1909 Asylum Officers' Superannuation Act, and perhaps earlier. Special terms continue to apply in respect of officers and employees registered under the 1945 Mental Treatment Act.

3.5.3 The LGSS applies to personnel employed in hospitals coming under the auspices of the Health Boards and most health corporate bodies. Thus, the LGSS covers the vast majority of health service personnel. However, discussions have taken place between the Department of Health and Children and the Department of the Environment and Local Government concerning the transfer of future responsibility for the administration of pensions in respect of those health service employees covered by the LGSS.

[22] These include Beaumont Hospital, St James's Hospital and St Luke's Hospital, all funded by the Eastern Regional Health Authority.

3.5.4 In the past, voluntary hospitals had no pension schemes for their staff. The Voluntary Hospitals (Officers) Superannuation Scheme, 1969 (VHSS) as amended in 1977 now covers such hospitals as the Mater, St. Vincent's, and Crumlin.

3.5.5 The Nominated Health Agencies Superannuation Scheme, 1986 (NHASS) covers 19 different agencies. Both the VHSS and NHASS are run centrally by the Department of Health and Children.

3.5.6 The main categories of personnel employed in the health service are:

- nursing (general and public health);
- psychiatric nursing;
- medical and dental;
- paramedical;
- management and administration;
- maintenance and technical;
- support services.

3.5.7 Other than the LGSS, the formal pension schemes applying in the health service are:

- Voluntary Hospitals (Officers) Superannuation Scheme, 1969 (as amended in 1977) and the Voluntary Hospitals (Officers) Spouses' and Children's Contributory Pension Scheme, 1986;
- Voluntary Hospitals (Non-Officers) Superannuation Scheme, 1985 and the Voluntary Hospitals (Non-Officers) Spouses' and Children's Contributory Pension Scheme, 1986;
- Nominated Health Agencies Superannuation Scheme, 1986 and the Spouses' and Children's Contributory Pension Scheme, 1986.

These are non-statutory schemes.

Pension terms of personnel employed in the health service

3.5.8 The pension terms of health service personnel are broadly similar to those applying to civil servants and to local authority personnel, with the following exceptions:

- officers and employees registered under the 1945 Mental Treatment Act (principally Psychiatric Nurses) who come under the LGSS may retire after age 55. Pensionable service in excess of 20 years is doubled, up to a maximum of 30 years' actual service (40 years' pensionable service). Health service personnel working in the psychiatric services who are covered by pension schemes other than the LGSS do not have special pension terms;
- all officers (apart from non-consultant hospital doctors — see Paragraph 3.5.11) who are employed in a temporary capacity are excluded from membership of the respective pension schemes. It should be noted, however, that the employing authorities are examining the question of extending pension scheme coverage to temporary personnel employed on potentially renewable contracts (such a change has already taken place in the LGSS — see Paragraph 3.4.8);

- all personnel (apart from some medical practitioners) covered by the NHASS are in full PRSI class. With effect from 6 April 1995, all new entrants covered by the LGSS and VHSS are in full PRSI class, while officers in service before that date are in modified PRSI class;
- given that a 5% pension contribution already applied, no uprating of salary took place when full PRSI was introduced in respect of officers appointed on or after 6 April 1995.

3.5.9 Personnel covered by the LGSS who are appointed to permanent positions subsequent to earlier service which was non-pensionable are required to pay outstanding employee contributions in order to make this service pensionable. Under the VHSS and NHASS, the payment of outstanding contributions in such a situation is optional. Under the LGSS, those in modified PRSI class generally have three years to pay contributions which are owing. After this, compound interest is applied on the outstanding balance (see Paragraph 3.4.9). In the VHSS, compound interest applies from the outset on contributions owing. Personnel covered by the LGSS and VHSS on a full PRSI basis since 6 April 1995 pay outstanding contributions on a current salary basis.

3.5.10 Nurses have been entitled to reckon the period of training for pension purposes on the basis that it constituted actual paid service. However, with the recent change of status of training as a result of the introduction of the Bachelor of Nursing Degree programme, this will no longer be possible.

3.5.11 Non-consultant hospital doctors have for some time been covered by the LGSS and VHSS. Full pension entitlements were extended to this group notwithstanding the wholetime temporary nature of their employment.

3.5.12 Under the 1997 restructuring agreement reached with nurses under the *Programme for Competitiveness and Work (PCW)*, two new retirement initiatives were agreed and have been implemented. These comprise a pre-retirement initiative whereby nurses may opt to job-share at age 55 and retire at age 60 with full pension credit for the job-sharing service, and a limited early retirement initiative. Both initiatives are subject to an annual quota. They are operating on a pilot basis and are to be reviewed in the light of the Commission's Final Report. Further details of these initiatives are given in Appendix 3.3.

3.6 Education sector

3.6.1 The education sector, which makes up about 28% of total public service employment, includes teachers, lecturers, and non-teaching personnel in schools, VECs, special schools, universities, Colleges of Education, Institutes of Technology and other education bodies. There are separate pension schemes for each area; the principal schemes are detailed below.

3.6.2 Teachers comprise the largest group in the education sector, representing about 24% of total public service employment. There are three separate pension schemes, the National School Teachers' Superannuation Scheme, the Secondary Teachers' Superannuation Scheme and the Vocational Teachers' Superannuation Scheme. A range of changes to teachers' pension terms were made as part of the 1997 restructuring agreement between management and teachers under the *PCW*, including the introduction of a pilot early retirement initiative (see Paragraph 3.6.24).

3.6.3 Apart from the facility to retire on or after reaching age 55 having 35 years' service (see Paragraph 3.6.9), there are a number of general differences between the pension terms of civil servants and of teachers. These include:

(i) maximum retirement age for a teacher is the end of the school year following his or her 65th birthday;

(ii) unions and management did not agree to revise the spouses' and children's schemes for national and secondary teachers in line with the 1984 changes in the civil service scheme (see Paragraph 20.3.5). VEC teachers did have this option as part of the implementation of the 1984 changes under the LGSS;

(iii) a main scheme contribution of 5% of pay applies (integrated as appropriate);

(iv) primary and secondary teachers have the option to purchase notional years of service by reference to age 60 or age 65 while most public servants with standard pension terms must purchase added years by reference to age 65 only;

(v) the civil service working party changes introduced with effect from June 1973 (see Paragraph 3.3.10) were implemented for national and secondary teachers in 1977; thus, preservation of pension benefits applies in respect of national and secondary teachers in service on or after 30 June 1977, rather than 1 June 1973 as in the civil service.

National teachers — historical development of pension scheme

3.6.4 The National School Teachers' Superannuation Schemes are made under the Teachers' Superannuation Act, 1928 and the Teachers' Superannuation (Amendment) Act, 1990. The principal scheme is the National School Teachers' Superannuation Scheme, 1934, as amended.

3.6.5 The original pension scheme for national teachers was set up under the National School Teachers' (Ireland) Act, 1879. It provided for the granting of pensions or gratuities to any *classed* teacher, i.e. principal and assistant teachers in model or ordinary national schools, but not including Lay Assistants or the subsequently established Junior Assistant Mistresses (they were made pensionable under the 1934 scheme). The Act also provided for the establishment of a pension fund out of which all pensions were to be paid. The basis of the fund was provided by a capital sum of £1.3 million set aside from the Irish Church Fund, the interest on this sum at the rate of 3% per annum being paid into the fund. Actuarial valuations of the fund were made regularly during the early period, but less frequently thereafter. Each of these valuations, with the exception of one made shortly after establishment, disclosed a deficiency. Various grants were made to the fund to maintain its solvency. In 1914, new teacher contributions ranging from $3\frac{1}{2}$% to 5% of pay were introduced. These were fixed at 4% of pay in 1921 and continued at that rate up until 1934. It was estimated that the deficit in the scheme by 1934 was close to £5 million.

3.6.6 The Government decided in 1934 that the new pension scheme for national teachers would be non-contributory and that it would take on the full responsibility of meeting the cost of teachers' pensions. Because of the additional financial burden to the State, the salaries of serving teachers were reduced by 9% (the net reduction was 5% as teachers were no longer paying the 4% contribution). The new scheme provided for continuation of an existing facility for national teachers to retire on or after age 55 once they had accrued 35 or more years' service.

3.6.7 While the legislation provided for the establishment of a pension fund, this was intended to be a nominal fund only, and the scheme's pension commitments have since been met from monies voted annually by the Oireachtas.

3.6.8 The pension scheme remained non-contributory up until 1968. On foot of a recommendation by the Tribunal on Teachers' Salaries (the *Ryan Tribunal*), a common contributory salary scale was introduced for all teachers. Secondary teachers already paid a pension contribution of 5% of pay. The introduction of a similar contribution for national teachers and payment of the same salary scale as for secondary teachers had the effect of uprating the national teachers' non-contributory scale by 1/19th.

National teachers — pension terms

3.6.9 Basic pension terms for national teachers are similar to those applying in the civil service. However, there is an option for national school teachers to retire with immediate payment of pension and lump sum on or after age 55, provided they have completed 35 years of pensionable service.[23]

3.6.10 Membership of the main pension scheme is automatic for national school teachers in pensionable teaching service, i.e. fully qualified teachers who are appointed to permanent or temporary wholetime posts in national schools. Membership of the spouses' and children's contributory pension scheme is automatic for male teachers appointed after 30 June 1969 and female teachers appointed after 31 May 1981 and was optional for teachers who were appointed before those dates.

3.6.11 Recent changes under the teachers' *PCW* agreement make provision for the pensionability on an ongoing basis of part-time service in primary schools provided it is deemed to be quasi-permanent. A teacher who is timetabled at the outset of the school year for specific class contact time of at least 2 days per week for the full duration of the school year in any one school will be regarded as in quasi-permanent employment. In addition, more extensive arrangements are being introduced for the payment of contributions in respect of certain part-time service (e.g. substitute teaching) given prior to pensionable service — more restrictive arrangements were first permitted in 1991.

Secondary teachers — historical development of pension scheme

3.6.12 The Secondary Teachers' Superannuation Schemes are made under the Teachers' Superannuation Act, 1928 and the Teachers' Superannuation (Amendment) Act, 1990. The principal scheme is the Secondary Teachers' Superannuation Scheme, 1929, as amended.

3.6.13 The scheme was established initially on a funded basis. The fund was valued once, in 1934, when it was found to have accrued a deficiency of £344,000 with contributions paid by teachers and schools being sufficient to meet only two-thirds of the liability in respect of new entrants. The Department of Finance sanctioned the discontinuance of the fund from 1 January 1984, with pensions and lump sums being paid since then from the Second-Level and Further Education Vote. The contribution rates at the time the scheme was set up were 4% of pay for teachers and 2.5% of pay for the employing school. The teachers' contribution was increased to 5% of pay under Section 13 of the 1951 Secondary Teachers' Superannuation (Amendment) Scheme, and the employer's contribution was increased to 5% of pay under Section 16 of the

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[23] In computing the 35 years, credit for pre-service training is allowed; a teacher with four or more years' training is allowed two years' credit; a teacher with three years' training is allowed one year's credit. The credited years do not count for benefit purposes.

1956 Secondary Teachers' Superannuation (Amendment) Scheme. The employer's contribution continues to be payable but is calculated on the *basic salary* only. Basic salary is the amount of the teacher's salary for which the school is responsible. Since the introduction of the Common Basic Scale on 1 July 1968, basic salary amounts to £400 per annum. In practice, in the case of the vast majority of schools, the Department pays both incremental salary and basic salary. The amount of the basic salary together with the associated pension contribution and PRSI contributions is offset against capitation grants due to schools.

Secondary teachers — pension terms

3.6.14 The Secondary Teachers' Superannuation Scheme applies to teachers in secondary, community and comprehensive schools.

3.6.15 Until recently, the scheme was identical in most respects to the national teachers' scheme; however, it differed in two important areas:

- secondary teachers were eligible only to retire between ages 60 and 65 (they did not have the national teachers' option to retire from age 55, having 35 years' service); and
- membership of the scheme was optional (in 1997, about 80% of secondary teachers were members of the pension scheme).

3.6.16 These have now changed as a result of the implementation of the teachers' restructuring agreement under the *PCW*. Secondary teachers now have the option to retire from age 55 provided they have at least 35 years' service, and membership of the pension scheme is automatic for new entrants appointed to eligible service on or after 1 March 1996.

3.6.17 Secondary teachers who are not members of the pension scheme pay the full rather than the modified rate of PRSI, and so are entitled to receive State Social Insurance benefits. Following the change in Social Insurance status of new entrants to the public service, all secondary teachers (whether in the pension scheme or not) appointed on or after 6 April 1995 are in full PRSI class. Teachers who were eligible for admission to the pension scheme prior to 1 March 1996 may on application be admitted to membership of the scheme from a date not earlier than 15 months prior to the date of application for membership. Those opting to join the main pension scheme are required also to join the spouses' and children's contributory pension scheme.

3.6.18 Prior to the *PCW* agreement, membership of the Secondary Teachers' Superannuation Scheme was open only to registered teachers serving in secondary schools in permanent or temporary wholetime posts and to permanent teachers serving in community and comprehensive schools. However, under the new arrangements, membership of the scheme is now open, with effect from 1 August 1996, to all teachers in secondary, community and comprehensive schools who are employed on a permanent or quasi-permanent basis (i.e. timetabled at the outset of the school year for specific class contact time of at least nine hours per week for the full duration of the school year in any one school) provided they are fully qualified, are capable of giving at least five years of actual pensionable service by the end of the school year in which they reach age 65, and have satisfactory health.

3.6.19 In reckoning pensionable service, unless the teacher retires from part-time service or dies while in part-time service (see Paragraph 3.6.20), part-time service given from 1 August 1996 is reckoned in the proportion which the weekly hours worked bear to wholetime service of 22 hours weekly. Part-time service for which contributions have been made (see Paragraph 3.6.21), and which was given before 1 August 1996, is reckoned as half of comparable wholetime service.

3.6.20 Where a teacher retires from part-time service or dies while in part-time service, pension benefits are related to actual salary at retirement or death, whichever is appropriate, and to pensionable service, where the teacher is given one full year's credit for each year of part-time service. An appropriate adjustment may be made where hours vary substantially during service. In circumstances where a teacher dies in part-time service, potential pensionable service for the purpose of a spouses' and children's pension is counted in full years from the date of death. As part of the teachers' *PCW* agreement, these provisions are to be reviewed in the light of the Commission's Final Report.

3.6.21 Once admitted to the scheme, a teacher has the option to pay contributions in order to make pensionable certain service given prior to the effective date of admission. The service must have been given as a fully qualified secondary teacher. All previous wholetime service may be made pensionable in this way and part-time service may be made pensionable in respect of:

- each school year where the teacher had at least half of comparable wholetime service in that year; or
- each week during the school year where, not having had a minimum of half of comparable wholetime teaching service in the school year, the teacher had at least nine hours' teaching service in that week.

Part-time service may not be made pensionable in this way until contributions have been made in respect of all reckonable wholetime service. Where wholetime service comes to more than five years, contributions must be made in respect of a minimum of five years' service.

3.6.22 The rate of contribution for such reckonable service is $1\frac{1}{2}$% of remuneration and 5% of net remuneration. It is open to the teacher to make payment of the appropriate contribution either immediately by way of a lump sum based on current remuneration, or at retirement. An option to pay immediately must be exercised within 12 months of formal admission to the pension scheme. Where payment is made at retirement, the appropriate contribution is deducted from the retirement gratuity and is based on remuneration immediately prior to retirement.

Vocational teachers — pension terms

3.6.23 Until recently, pensions of vocational teachers were covered by the Local Government Superannuation Scheme (LGSS). The scheme was open to officers, including teachers, employed by VECs since the date of their establishment in 1930. Following the *PCW* agreement, the LGSS has, in relation to vocational teachers, become the Vocational Teachers' Superannuation Scheme, 1998 (VTSS) by virtue of the Vocational Education Superannuation Schemes (Transfer of Departmental Administration and Ministerial Function) Order, 1998. This order transfers responsibility for vocational teachers' pensions to the Department of Education and Science. Pension terms are essentially the same as those applying under the LGSS, but with a number of provisions specific to the case of teachers (as modified under the *PCW* agreement). These are as follows:

- the qualification criteria for membership of the scheme are the same as those applying to secondary teachers except that vocational teachers are eligible for membership even where they are not capable of giving at least five years' pensionable service by the end of the school year in which they reach age 65 (under the VTSS, teachers with less than the potential for five years of pensionable service are eligible to receive payment of a death gratuity if they die in service; however, a spouses' and children's pension is not payable);

- there is an option to retire from age 55, provided the teacher has a minimum of 35 years' service (in reaching the threshold of 35 years, credit for pre-service training is given);
- unlike the case of national and secondary teachers, the revised spouses' and children's pension scheme (see Paragraph 3.6.3 (ii)) was introduced in respect of vocational teachers as part of its general introduction under the LGSS;
- under the *PCW* agreement, temporary wholetime service and part-time service of a quasi-permanent nature is, with effect from 1 September 1996, pensionable on an ongoing basis; a teacher who is timetabled at the outset of the school year for specific class contact time of at least nine hours per week for the full duration of the school year by any one VEC will be regarded as in quasi-permanent employment during that year;
- provisions in respect of reckoning part-time pensionable service given from 1 September 1996 and pension arrangements in case of retirement or death while in pensionable part-time service are the same as for secondary teachers;
- special provisions apply to the payment of contributions in respect of service, including part-time service, given in an otherwise pensionable capacity prior to the effective date of admission to the scheme.

Limited pilot early retirement initiative for teachers

3.6.24 A limited early retirement scheme was agreed as part of the *PCW* restructuring agreement reached between the Department of Education and the teachers' unions in early 1997. It applies on a pilot basis to national, secondary and vocational teachers. The scheme involves three strands:

Strand I	Teachers with not less than 15 years' wholetime or pensionable service who are consistently experiencing professional difficulties in their teaching duties;
Strand II	Teachers aged 55 years or more who, having served for a minimum of 20 years, wish to retire and whose school management verifies that such retirement would provide an opportunity to enhance the education service provided by the school by facilitating change such as the introduction of new skills and curriculum review;
Strand III	Teachers in posts surplus to requirements which will not be filled and who cannot readily be redeployed.

3.6.25 Special retirement terms, involving the granting of added years in certain circumstances and immediate payment of pension with no actuarial reduction, apply. The full details of the scheme are set out in Appendix 3.4. Strands I and III are subject to an overall quota of 150 retirements per year. Strand II is subject to an overall quota of 250 retirements per year. Priority is given to older teachers under all three strands where the number of applications exceeds the quota. All applications for early retirement under Strands I and II of the scheme are processed by an *Early Retirement Advisory Committee* (*ERAC*) which makes recommendations to the Minister for Education. Under the agreement, the pilot scheme is to be reviewed in the light of the Commission's Final Report.

Non-teaching personnel in schools and VECs

3.6.26 Pension terms in respect of non-teaching personnel (clerical support staff and school caretakers) in schools and VECs are generally equivalent to civil service terms. It would appear that not all such employees (some of whom work on a part-time basis) are members of a pension scheme.

Third level education — historical development of pension schemes

3.6.27 In the past, the academic, administrative, and technical staffs of many third-level colleges were covered by separate pension schemes operated by the colleges or institutions in which they were employed. Most such bodies now operate a single scheme for all employees. For historical reasons, the five older universities,[24] have pension funds. The employer contribution to these funds is provided from monies made available through the Higher Education Authority (HEA). These schemes are only partially funded in that, while main scheme benefits are formally funded, pension increases continue to be financed on a pay-as-you-go basis (see Paragraph 5.2.5). Pension terms differ in certain aspects from public service norms, e.g. notional added years facilities tend to be more favourable than apply elsewhere in the public service and, in a number of universities (e.g. TCD and NUIM), early retirement subject to actuarial reduction is available from age 50.

3.6.28 The Department of Education and Science has operational responsibility for the pension scheme of the Colleges of Education for National Teachers. The Department has also a regulatory and financing role in relation to the pension schemes of the College of Home Economics. The National College of Art and Design which is funded via the HEA has a non-funded pension scheme that corresponds with public service standard terms. This is also the case with the University of Limerick and Dublin City University.

Third level institutions — pension terms

3.6.29 Notwithstanding the caveat above, standard pension benefits for those in third level education are basically similar to those applying in the civil service. The majority of staff are covered by non-contributory main schemes and contribute $1\frac{1}{2}$% of pay for membership of spouses' and children's contributory pension schemes. For new entrants taking up service on or after 6 April 1995, a 5% contribution applies under the main pension schemes, in the same way as for established civil servants (see Paragraph 3.3.57).

3.6.30 In TCD, academic and administrative personnel employed on a contract basis where there is a reasonable expectation of two years' employment are admitted to a defined contribution scheme, rather than to the standard defined benefit arrangements. Generally, employees and employers each pay a scheme contribution of 5% of salary. On subsequent appointment to permanent positions in the university, transfer values can be used to purchase service within the defined benefit scheme. A number of the other universities operate similar arrangements.

3.6.31 Up to ten notional added years are provided as a matter of course to academic staff in most universities. In practice, TCD, UCD and NUIM also grant added years to administrative personnel. This is in contrast to other parts of the public service where such a facility is confined to professional and specialist grades.

3.6.32 Section 25(7) of the Universities Act, 1997 requires that universities prepare and submit new pension schemes for approval to the HEA with the consent of the Ministers for Education

[24] Trinity College Dublin (TCD), National University of Ireland Maynooth (NUIM), University College Galway (UCG), University College Dublin (UCD) and University College Cork (UCC).

and Science and Finance. Section 25(8) of the Act preserves existing pension entitlements of employees serving at the commencement date of the Act. The HEA has written to the universities asking them to submit draft schemes which conform to public service norms. Proposals from the universities are currently under consideration.

3.6.33 Management and administrative personnel employed by the VECs and by the Institutes of Technology are currently covered by the LGSS and so have the same pension terms as apply in the local authority sector. Teachers and lecturers in Institutes of Technology are also currently covered by the LGSS but, under the *PCW* agreement, it has been agreed that teachers and lecturers employed on a temporary wholetime or quasi-permanent basis will be pensionable on an ongoing basis with effect from 1 September 1996. It has since been decided by the Government that, subject to agreement on the resources involved, all of the functions exercised by the Minister for the Environment and Local Government in regard to VEC and Institute of Technology pensions should be transferred to the Minister for Education and Science. Arrangements for the transfer are currently being made.

Other education bodies

3.6.34 The Department of Education and Science also has a regulatory and financing role in relation to the pension schemes of the following bodies:

- National Council for Educational Awards;
- National Council for Vocational Awards;
- HEA;
- Dublin Institute for Advanced Studies;
- Institiúid Teangeolaíochta Éireann;
- Royal Irish Academy of Music.

3.7 Permanent Defence Forces

Pension schemes of the Permanent Defence Forces

3.7.1 The Defence Forces (Pensions) Acts, 1932 to 1975 empower the Minister for Defence, with the consent of the Minister for Finance, to make pension schemes to provide retired pay, pensions and gratuities for and in respect of members of the Permanent Defence Forces. The terms and conditions for the grant of pension, etc., are contained in the Defence Forces (Pensions) Schemes, 1937 to 1994.

3.7.2 Membership of the main pension schemes applies to all personnel (commissioned officers, enlisted personnel, and members of the Army Nursing Service and the Chaplaincy Service) from the date of joining the Permanent Defence Forces.

3.7.3 Membership of the spouses' and children's contributory pension scheme is automatic for male officers commissioned after 31 December 1970 and female officers commissioned after 31 December 1984 and was optional for officers serving before those dates. In the case of enlisted personnel, membership of the spouses' and children's pension scheme is automatic for male personnel enlisted after 31 January 1978 and female personnel enlisted after 31 December 1984, and was optional for those serving before those dates.

3.7.4 The Defence Forces Pension Schemes represent a distinct pension code which is quite different from the codes applicable elsewhere in the public service. Distinctive features of the schemes include provision for the immediate payment of pensions and gratuities regardless of age after relatively short periods of service (five years for gratuity only, and 12 years for pension and gratuity, in the case of officers; three years for gratuity only, and 21 years for pension and gratuity, in the case of enlisted personnel) and the absence of provision for the preservation of benefits.

3.7.5 Unlike most other public service pension schemes, the Defence Forces schemes are generally not directly pay-related in that many of the benefits (pensions, in particular) are not directly based on pay at date of retirement, but are flat rates based on rank, service in rank, and overall service. Pensions in payment are generally revised in line with movements in the pay of serving personnel.

3.7.6 Members of the Permanent Defence Forces are not insured for Occupational Injuries Benefits under the Social Welfare Acts. Instead, they are covered by the Army Pensions Acts, which constitute a military occupational injuries code. Disability pensions may be granted under those Acts to retired officers and enlisted personnel suffering from permanent disablement due to injuries or wounds attributable to military service or due to disease arising from overseas service with the United Nations. The level of pension depends on the degree of disablement assessed by the Army Pensions Board, which is the statutory body appointed to adjudicate on pension applications. Under taxation legislation, all disability pensions under those Acts are exempt from income tax. Provision is also made for the grant of allowances to the dependants (including spouses and children) of deceased military personnel where death was attributable to service. Where a person is eligible for payments under both the Army Pensions Acts and the Defence Forces Pension Schemes, the payment under the schemes is generally subject to abatement.

3.7.7 There is no explicit contribution to the main pension scheme, except in the case of officers commissioned on or after 6 April 1995, who are in full PRSI class. A 5% contribution was introduced for these officers in the same way as for established civil servants (with consequent uprating of salaries by 1/19th) — see Paragraph 3.3.57. A contribution of $1\frac{1}{2}$% of remuneration applies to officers who are members of the spouses' and children's contributory pension scheme. For enlisted personnel, the spouses' and children's scheme contribution is $1\frac{1}{2}$% of four times the amount of basic spouse's pension plus addition for Military Service Allowance.

Commissioned officers

3.7.8 There are three broad service categories for the purposes of pension benefits:

- officers with five or more but less than 12 years' service who qualify for gratuity (without pension) of 20 days' pensionable pay at date of retirement for each year of qualifying service;
- those with between 12 and 20 years' service who qualify for pension and gratuity, both at flat rates, depending on rank and service. Under the schemes, the minimum pension for a person retiring as a Captain after 12 years' service is about 20% of maximum regimental pay, plus addition for Military Service Allowance (MSA);[25]

[25] Military Service Allowance (MSA) was introduced to compensate Defence Forces personnel for the special disadvantages associated with military life. It is paid on a continuous basis to all personnel up to and including the rank of Colonel (with the exception of those in training or in full-time third-level education). On foot of a recommendation by the *Gleeson Commission*, 1990, MSA is reflected in the pensions and gratuities of personnel retiring since August 1990.

- those with 20 or more years' service who qualify for flat-rate pension depending on rank, service in rank and overall length of service and for flat-rate gratuity depending on rank.

All benefits are calculated by reference to the number of completed years of qualifying service and are payable immediately on retirement, regardless of age.

3.7.9 The qualifying period for maximum pension of 50% of maximum regimental pay (plus addition for MSA) varies according to rank and service, but can be attained long before an officer reaches maximum retirement age. For example, a Commandant may qualify for maximum pension at around age 40 to 42, while the normal retirement age for that rank is 56. Where maximum flat-rate pension is less than 50% of the maximum regimental pay for the rank (e.g. for a Captain), the pension is increased to the latter amount. Conversely, where pension is greater than 50% of the maximum regimental pay for the rank (e.g. for a Lieutenant-Colonel), the pension is reduced to the latter amount, but only if the officer was promoted to his or her retiring rank on or after 1 January 1986.

3.7.10 The maximum retirement lump sum of $1\frac{1}{2}$ times pay (plus addition for MSA) is payable only on retirement within two years of the maximum retirement age, which varies according to rank and ranges from age 54 for a Captain to age 63 for a Lieutenant-General. However, in the case of an officer with 20 or more years' service who serves to within four years of maximum retirement age for the rank, the maximum flat-rate retirement gratuity is progressively increased on the basis of one-third of the difference between the flat-rate gratuity and $1\frac{1}{2}$ times pay (plus addition for MSA) at retirement, for each completed year of service during the five year period preceding retiring age, subject to a maximum of $1\frac{1}{2}$ times pay (plus addition for MSA) at retirement.

3.7.11 In the case of officers commissioned on or after 6 April 1995, who are in full PRSI class, integration of personal and survivors' pensions with the Social Insurance system applies in line with arrangements applicable to established civil servants in full PRSI class.

3.7.12 Under the schemes, certain officers such as doctors, engineers, and pilots who are paid extra remuneration in respect of their specialised duties are categorised as special service officers for pension purposes. The extra remuneration is reflected in the calculation of pay-related gratuities, while fixed percentage additions are made to the standard rates of pension. Medical and Dental Officers qualify for a 20% addition to pension, while other categories such as engineers, pilots and chemists qualify for a 10% addition.

3.7.13 Subject to certain conditions, long-service increments introduced under the *PCW* restructuring agreement for officers are reckonable for pension purposes in the case of Captains and Commandants retiring after 1 October 1994 and Lieutenant Colonels retiring after 1 January 1998.

3.7.14 An officer with at least one but less than ten years' service who is compulsorily retired on medical grounds qualifies for an enhanced service gratuity of 30 days' pensionable pay for each complete year of service. No pension is payable. Where service is greater than ten but less than 20 years, he or she qualifies for a higher pension than would be payable if retiring voluntarily, in addition to a flat rate gratuity. Where service is 20 years or more, the standard rates of pension and gratuity apply, but the maximum retirement gratuity of $1\frac{1}{2}$ times pensionable pay is payable somewhat earlier.

3.7.15 There is no minimum service requirement for the payment of death gratuity. On death-in-service, a gratuity of a minimum of one year's pensionable remuneration is payable to a relative of the deceased (if married, usually his or her spouse and/or children). A maximum gratuity of up to $1\frac{1}{2}$ years' pay is payable depending on length of service.

3.7.16 The contributory spouses' and children's pension scheme for officers is essentially the same as that applying elsewhere in the public service. The spouse's pension is normally one-half of the deceased's actual pension, except where the officer dies in service or after retirement on medical grounds (in which case, the pension is half what the deceased would have received on serving to normal retirement age). In all cases, the maximum spouse's pension payable is one-quarter of the deceased's uprated pensionable remuneration.

Enlisted personnel

3.7.17 Enlisted personnel qualify for immediate gratuity (without pension) on retirement with three or more and less than 21 years' service. They qualify for both immediate pension and gratuity after 21 years' service (or after 12 years if discharged on medical grounds) regardless of age in every case. Maximum benefits are payable after 31 years' service, while maximum retirement age is 60.

3.7.18 Pension consists of a basic flat rate pension (which varies according to rank) in respect of 21 years' service, together with an addition to basic pension of 40% of the rate of MSA. An additional increment in respect of each year of service in excess of 21, up to an overall maximum of 31 years, is also payable, while the addition for MSA is increased from 40% to a maximum of 50% of the allowance (payable after 31 years' service). A retirement gratuity of 25 weeks' pay (plus addition for MSA) is payable after 21 years' service, and the maximum gratuity is 45 weeks' pay after 31 or more years' service.

3.7.19 Minimum pension after 21 years' service represents between 36% and 39% of maximum pay (plus addition for MSA) depending on rank, while the maximum after 31 years' service ranges from 47% to 53% of maximum pay.

3.7.20 Enlisted personnel pay PRSI at Class H, and so are fully insured for all benefits under the Social Welfare Acts, except Occupational Injuries Benefits (see Paragraph 3.7.6).

3.7.21 The 21 year pension (plus addition for MSA) is payable to a pensioner during his or her lifetime, but the additional increment for service in excess of 21 years and the supplementary 10% of MSA cease to be payable when the pensioner becomes entitled to Social Insurance Retirement Pension (at age 65), or OACP (at age 66). The withdrawal of the additional increment is in accordance with the principle of integration of occupational benefits with Social Insurance benefits in the case of employees who are fully insured under the Social Welfare Acts. However, the method used in the case of enlisted personnel is, in effect, a partial form of integration, and differs from the standard method applicable in other public service employments.

3.7.22 Certain forms of extra remuneration are reckonable for pension purposes. These payments are fully reckonable in the calculation of pay-related gratuities, while an addition of 3% of the standard rates of pension is payable in respect of each additional payment.

3.7.23 A modified service pension and a service gratuity are payable where discharge is on medical grounds and service is 12 or more but less than 21 years. Benefits are calculated on a proportionate basis by reference to the standard pension and gratuity applicable to 21 years' service.

3.7.24 There is no minimum service requirement for payment of death gratuity. On death-in-service, a gratuity of one year's pensionable remuneration is payable to a relative of the deceased (if married, usually his or her spouse and/or children).

3.7.25 The contributory spouses' and children's pension scheme for enlisted personnel is essentially based on schemes applicable elsewhere in the public service. The spouse's pension is one-half of the 21 year pension appropriate to the rank of the deceased.

Members of the Army Nursing Service and the Chaplaincy Service

3.7.26 The pension arrangements of members of the Army Nursing Service (ANS) and the Chaplaincy Service are quite different from those of officers and enlisted personnel. For example, no gratuity is payable in addition to pension, and there is no provision for the payment of survivors' benefits. Generally, benefits are determined by reference to pay and service on retirement.

3.7.27 Where service is five years or more but less than 20 years, a gratuity of one month's reckonable pay is payable for each year of service, subject to a maximum of one year's pay in the case of the ANS, and 19 months' pay in the case of the Chaplaincy Service.

3.7.28 The minimum qualifying period for pension is 20 years (or ten years if retired on medical grounds) and maximum pension is payable after 30 years' service. Pension is based on 1/60th of reckonable pay at date of retirement for each year of service. An additional 1/60th is payable for each year of service in excess of 20, subject to a maximum pension of 2/3rds of pay after 30 years' service. There are no minimum age limits to qualify for pension or gratuity and maximum retirement age for both services is 65 years.

3.7.29 Benefits are non-contributory, except in the case of persons appointed on or after 6 April 1995 (in full PRSI class), in respect of whom a 5% pension contribution applies.

3.8 Garda Síochána

Historical development of the Garda Síochána Pension Scheme

3.8.1 The terms and conditions of the pension schemes applicable to members of the Garda Síochána are set out in the Garda Síochána Pensions Orders, 1925 to 1981, and agreements made under the Garda Síochána Conciliation and Arbitration Scheme.

3.8.2 Members of the Garda Síochána have special pension terms which differ from standard public service terms. These special terms take account of the need to maintain a younger and more physically capable workforce able to give a better service and suited to the rigours of policing. This approach is a long-standing one and was reflected in the Constabulary (Ireland) Act, 1908, which provided the basis for the current arrangements. The *Ross Commission*, 1920, reporting on the Royal Irish Constabulary and Dublin Metropolitan Police, recommended the adoption of the *Desborough Commission* view that all ranks be entitled after 25 years' service to retire on pension of one-half of annual pensionable pay, and after 30 years' service to retire on a pension at the rate of two-thirds of pensionable pay.

3.8.3 After the establishment of the Garda Síochána in 1922, the Garda Síochána (Temporary Provisions) Act, 1923 and the Garda Síochána Act, 1924 enabled the Minister for Justice, with the sanction of the Minister for Finance, to authorise the grant and payment of pensions or gratuities to members of the Garda Síochána and to their widows, children and dependants. Unlike the rest of the public service, provision for widows' pensions always existed in the Garda code. The Garda Síochána Pay Order, 1924 provided for the annual deduction of $2\frac{1}{2}$% from the pensionable pay[26] of every member of the Force as a contribution to the general pension charge of the Garda Síochána. This contribution rate was reduced to 1.75% of pay for male Gardaí in the early 1970s when the widows' and children's contributory pension scheme was being introduced.

3.8.4 The Garda Síochána Pensions Order, 1925 maintained the special pension terms which continue to apply today. It also established a compulsory retirement age of 63 for members in the rank of Chief Superintendent and below. The retirement age was reduced for members recruited after 1952 to age 60 for the Chief Superintendent and Superintendent ranks, and to age 57 for the Inspector, Sergeant and Garda ranks. The retirement age for Assistant/Deputy Commissioners has recently been reduced to age 60. The Garda Commissioner now has pension terms equivalent to civil service Secretaries General appointed by TLAC (see Paragraph 3.3.37).

3.8.5 In 1965, provisions were introduced to allow female Gardaí to retire from age 50 after at least 25 years' service. The reduction in contribution rate from $2\frac{1}{2}$% to 1.75% of pay in the early 1970s (see above) was not applied to female Gardaí, as they were not then covered by the widows' and children's contributory pension scheme. That scheme was extended to female Gardaí in the early 1980s.

3.8.6 Pension terms for male and female members of the Force were equalised in June 1983. Female members were offered the pension terms applicable to male members (including the 1.75% contribution rate), while male members were offered the terms applicable to female members (including the $2\frac{1}{2}$% contribution rate). Male and female members recruited after this date are conditioned to retirement from age 50 having 30 years' service, and pay the 1.75% standard contribution rate.

3.8.7 In 1983, Garda Síochána Arbitration Board Report No.15 recommended that a series of allowances, including rent allowance, be made pensionable. The Board recommended that the commencement date be 1 October 1982. It was decided at the time that pensions in payment prior to the commencement date would not receive the benefit of the pensionability of these allowances.

3.8.8 Under the *PCW* agreement with the Garda associations, unsocial hours allowances — night duty, Saturday, Sunday and public holiday allowances — were made pensionable for members of the Garda Síochána who retired on or after 1 January 1993. The pensionability of these allowances was not extended to pensions in payment prior to this date.

Pension terms of members of the Garda Síochána

3.8.9 Members of the Garda Síochána may retire on or after age 50 if they have 30 years' actual service in the Force, with service in excess of 20 years being doubled. Thus, maximum pension is payable after 30 years' actual service. Maximum retirement age is 57.

3.8.10 Membership of the main pension scheme is automatic for all members of the Garda Síochána. Membership of the spouses' and children's contributory pension scheme is automatic

[26] The $2\frac{1}{2}$% contribution seems to date from the mid-1800s when local police pension funds were being established throughout the United Kingdom (Rhodes, A, *Public Sector Pensions*, 1965, p. 59).

for male Gardaí attested (i.e. appointed following completion of training) after 31 December 1971, and for female Gardaí attested after 30 June 1984. Membership was optional for those attested before those dates.

3.8.11 A special pension is payable where a member is incapacitated due to an injury received in the execution of duty without the member's own default. A statutory scheme of compensation also applies. A special survivor's pension is payable where the member is killed in the performance of his or her duty.

3.8.12 Members of the Garda Síochána who are attested on or after 6 April 1995 are in full PRSI class and are subject, generally, to the same pension calculation and contribution arrangements as apply to newly appointed established civil servants (see Paragraph 3.3.57). The 5% periodic contribution rate (integrated as appropriate) for new entrants replaced the existing rate of 1.75%, and the salary scale and the rates of pensionable allowances which are subject to periodic contributions (i.e. rent allowance and unsocial hours allowance) were uprated accordingly.

3.8.13 Where the surviving spouse of a deceased member would qualify for the maximum rate of Social Insurance Widow(er)'s Contributory Pension based on both his or her own and the deceased member's Social Insurance contribution record, only one pension is payable by the Department of Social, Community and Family Affairs. In such cases, an equivalent pension may be paid by the Department of Justice, Equality and Law Reform under Article 15(5) of the Garda Síochána Pensions Order, 1981. Such pension is paid in addition to any award under the spouses' and children's scheme. This additional spouse's pension is examined in more detail in Paragraphs 20.5.10-20.5.17.

3.8.14 In most other respects, members of the Garda Síochána have the same pension terms as established civil servants.

3.9 Non-commercial state-sponsored bodies

3.9.1 Separate pension schemes (usually, a main scheme and a spouses' and children's contributory pension scheme) apply to each of the non-commercial state-sponsored bodies. In general, these schemes are based on *model schemes* issued by the Department of Finance (see Paragraph 4.2.8) and offer the same pension terms as apply to civil servants. The largest schemes, in respect of FÁS, Forfás, and Teagasc, include approximately half of the public service employees in this area. A number of the older bodies, including FÁS, Forfás and CERT, operate pension funds. In some cases, the relevant funds relate to employees who were transferred on the winding up of organisations where pension funds had already existed (e.g. AnCO, IDA). As with the funded university schemes (see Paragraph 3.6.27) the cost of pension increases is not funded in advance and is met on a pay-as-you-go basis.

3.9.2 Enhanced pension terms apply to certain full-time board members and to those in equivalent positions under the schemes of a number of non-commercial state-sponsored bodies (generally, retirement is between age 60 and 65). Maximum pension of one-half of pensionable remuneration is accrued after 24 years; maximum lump sum in such schemes is $1\frac{1}{2}$ times pension rather than salary. However, individuals appointed to these positions who previously served elsewhere within the public sector may, if more favourable to them, have the standard 40 year pension arrangement applied, thus entitling them to a lump sum of up to $1\frac{1}{2}$ times salary rather than $1\frac{1}{2}$ times pension. Members who have their appointment terminated (other than for stated misconduct), or are not re-appointed on expiration of their period of office, are entitled to immediate pension and lump sum where they have accrued more than five years' service. Preservation of benefits applies only in case of voluntary resignation having five or more years' service. The schemes involved include:

- Competition Authority — Chairman and Members
- Labour Court — Chairman and Members
- Environmental Protection Agency — Directors
- Bord Pleanála — Chairman and Members

3.10 Conclusions

3.10.1 In this Chapter, the Commission has reviewed the historical basis of current pension provision in the public service. We have outlined the detailed pension provisions applying in each area of the public service. It will be seen that, given the current socio-economic context and today's increasingly mobile and flexible work environment, some of the basic principles and assumptions underlying public service pensions might appear outmoded and rigid. However, over the past 20 or 30 years, certain pension modifications have been made with the aim of providing the necessary adaptability and flexibility required in a modern public service. The Commission considers below the continuing appropriateness of current pension terms in the changing public service, the internal consistency and fairness of pension terms, including fairness as between public service groups, and the need for employee choice and flexibility within the pensions framework.

3.10.2 At this stage, the Commission is in a position to make a number of general points about public service pension schemes:

- while there is variation in scheme terms, a broad similarity in pension structures now exists across the public service as a result of an ongoing process of standardisation. The only area where there is any significant divergence from the norm is the Defence Forces;
- a number of public service groups have lower retirement ages for operational reasons, and receive enhanced pension terms as a result. The rationale for these terms is not clear in all cases. We examine this matter more closely in Chapter 15;
- the Commission is very much in favour of retaining the broad uniformity which underpins public service pension schemes. However, we see the provision to the individual of greater choice and flexibility on a cost neutral basis as a very important part of our agenda;
- existing pension arrangements derive from a time when life expectancy was much lower and work environments were significantly different from what they are now. It can be argued that schemes should be changed to better reflect the requirements of today's society;
- although they have made greater provision for part-time and temporary employment in recent years, it is questionable whether public service pension schemes cater adequately for this important component in public service employment.

APPENDIX 3.1

Pension scheme coverage in the public service (1997)

Sector/Scheme (i)	Coverage	Active Members	Pensioners	Annual Pension Cost (ii)
				Ir£ (m)
Civil Service Pension Scheme	Established Civil Servants (excl. Prisons)	25,667	8,055	81.0
	Prison Officers	2,476	252	2.2
	Non-Established and Industrial Civil Servants	3,391	5,848	5.5
Local Government Superannuation Scheme (Local Authorities)	Officers	8,914	3,084	26.5
	Employees	15,079	12,933	32.6
Local Government Superannuation Scheme (Health Service personnel)	Officers/Employees	40,218	11,544	74.0
Voluntary Hospitals Superannuation Scheme	Officers/ Employees	13,661	1,823 (incl. NHASS)	11.3 (incl. NHASS)
Nominated Health Agencies Superannuation Scheme (NHASS)	Officers/ Employees	5,900		
National Teachers Superannuation Scheme	National Teachers	21,040	6,990	77.4
Secondary Teachers Superannuation Scheme	Secondary Teachers	16,986	2,998	29.4
Local Government Superannuation Scheme (VECs, Institutes of Technology)	Vocational Teachers, Lecturers and Non-Teaching Staff	9,883	2,134	15.9
Various university schemes	Lecturers/Administrative/ Secretarial	7,240	2,700	23.7
Others in education sector	Teaching and Administrative Personnel	1,000	200	0.5
Defence Forces Pension Schemes	Officers and Enlisted Personnel	11,884	11,129	57.0
Civil Service Pension Scheme	Civilian Employees	1,214		
Garda Síochána Pension Scheme	Garda Síochána	10,746	5,492	57.7
Non-commercial state-sponsored bodies (various pension schemes)	Employees	7,920	2,000	14.0
Total		**203,219**	**77,182**	**508.7**

Source: Commission on Public Service Pensions, ''Actuarial Review of Public Service Pensions'' (November 1997), Report prepared by IPT Actuarial Services Ltd.

Notes:

(i) There are separate spouses' and children's schemes in respect of each public service group.
(ii) The costs represent annual pension expenditures in 1997 (employee contributions have not been netted off), excluding the cost of gratuities and other non-recurring payments.

APPENDIX 3.2

Pension increases under the Civil Service Pension Scheme[27]

(i) Since 1986, civil service pensions have been increased in line with relevant pay increases applicable to serving staff, and such pensions increases are effective from the same dates as the pay increases. The increases are effected on an administrative basis initially, and are later given statutory effect by means of regulations made under the Pensions (Increase) Act, 1964. Summary details of these arrangements are as follows.

(ii) All **general** pay increases (e.g. general increases under national pay agreements such as the *Programme for Competitiveness and Work (PCW)* or previous similar agreements concluded between the social partners) are applied to civil service pensions as a matter of course.

(iii) **Special** payscale increases (i.e. increases pertaining to specific grades or posts) are also applicable to pensions subject to the following conditions:

(a) the increase must apply to all staff serving in the grades or posts concerned;

(b) assimilation of serving staff to the revised pay scales must be on the basis of ''corresponding points'' (i.e. not on ''starting pay on promotion'' or ''regrading'' terms);

(c) the increase must not have been awarded in consequence of a substantial restructuring or alteration of duties which, in effect, constitutes regrading of the posts or grades concerned;

(d) the increase must not have been awarded in respect of increased productivity from serving staff;

(e) the increase must be a permanent feature of the pay scale.

(**Note**: The restrictive conditions outlined above have given rise to particular difficulties in the case of special payscale increases under the *Programme for Competitiveness and Work Agreement*, which have been largely awarded in respect of restructuring, increased productivity and alterations in duties. In the case of these increases, the Government has, exceptionally, decided that pending the report of the Commission on Public Service Pensions, certain permanent increases in pay scales arising from *PCW* restructuring deals may be applied to retired personnel, **subject to a minimum increase of 3%**.)

(iv) In applying pensions parity, a former officer who had not reached the maximum of his/her pay scale by the time he/she retired is **not** subsequently deemed to advance along the incremental scale in respect of periods after retirement. Thus, for example, the pension of an officer who resigns 6 months after reaching the 6th point on a 9-point salary scale will (subject to paragraph (v) below) be revised by reference to the 6th point of that scale.

(v) Where a post or grade is abolished, the normal practice is to base the pension of an employee who has retired from that post or grade on the scale point of an existing grade which is closest to the point held at retirement by the former employee. Future increases

[27] This Appendix reproduces Section 19 of Department of Finance, ''Superannuation Handbook: A Guide to the Superannuation Provisions applicable to Civil Servants'' (Revised, 1998).

in the former employee's pension are then based on pay increases applicable to the grade concerned. Where a post is upgraded or downgraded subsequent to the date of an officer's retirement, the pension is increased by reference to the pay he/she would have had if he/she had remained in the post, but ignoring the upgrading or downgrading which occurred after the retirement.

(It should be noted that a post is not treated for this purpose as being downgraded solely because, for example, there is a change in the method of pay determination for serving staff. A post would only be regarded as being downgraded for this purpose if, for example, the change involved a reduction in the duties and responsibilities of the post and the person serving at the time of the downgrading retained the original salary rate on a personal basis — i.e. only a future appointee would be subject to the lower salary rate. If the change did not have these characteristics, pensions increases of staff who retired before the change would generally continue to be determined by reference to the salary rate of the serving staff.)

(vi) If a retired officer has allocated portion of his/her pension to another person *[see Paragraph 3.3.51]*, pay increases are applied to the notional full pension, which is then reallocated in the proportions determined by the former officer at the time of his/her retirement.

(vii) Where a retiree is awarded a pension based on **net pensionable remuneration**, which takes account of the rate of Social Insurance pension paid on the date of his/her retirement, such a pension is not recalculated in full (taking account of changes in the Social Insurance pension) on the occasion of a pay increase. In such cases, the officer's occupational pension, when calculated at retirement, is expressed as a percentage of full pay at that time — e.g. 30% of scale pay — and pension increases are based on changes in scale pay, without regard to changes in Social Insurance pension rates.

(viii) Where a pension is based on pensionable remuneration which includes pensionable emoluments, the element in the pension which reflects the emoluments is increased by reference to general pay increases only.

(ix) If:

(i) an emolument which was not hitherto pensionable becomes pensionable, or

(ii) a new pensionable emolument is introduced

with effect from a specific date, officers who have retired prior to that date do not benefit from such developments.

APPENDIX 3.3

Retirement initiatives agreed between the Department of Health and Children and the Nurses' Unions under the *PCW* restructuring agreement (1997)

1. Pre-retirement initiative

Nurses aged 55 or over who have a minimum of 20 years' wholetime service and who do not otherwise enjoy enhanced pension benefits may qualify to work on a job-sharing basis for a maximum of five years prior to retirement, or such lesser period as may apply until they reach age 60, with the five or lesser number of years in question to reckon as full-time service for pension purposes.

A quota not exceeding 600 applications applies during the initial three-year operation of the scheme, with up to a maximum of 300 applications to be approved in the first year.

The scheme is intended to benefit both individual nurses and their employers where nurses are no longer capable of coping with the stresses and demands of nursing on a full-time basis. The scheme operates on a pilot basis pending review in the light of the Final Report of the Commission on Public Service Pensions.

2. Limited early retirement initiative

A limited early retirement initiative is available in respect of nurses aged 55 or over with at least 35 years' service who find the demands of the profession such that they no longer feel they can operate at the level of professional performance they themselves and management require. The facility operates as follows:

- nurses in this category are eligible for immediate pension;
- the scheme is subject to a number of criteria;
- an annual quota of 200 applies;
- the scheme operates on a pilot basis pending the Report of the Commission on Public Service Pensions.

APPENDIX 3.4

Limited early retirement scheme agreed as part of the restructuring agreement reached between the Department of Education and Science and the Teachers' Unions (1997)

1. **Strand I** — Applies to teachers with not less than 15 years' wholetime or pensionable service who are consistently experiencing professional difficulties in their teaching duties.

Subject to certain provisions, pension entitlements are as follows:

- a teacher with 35 years or more of actual pensionable service is granted pension based on actual reckonable service;
- a teacher with less than 35 years of actual pensionable service is awarded pension based on actual reckonable service enhanced by the grant of added years; the grant of added years is 25% of actual reckonable service, subject to the lesser of five years or potential service to age 65, and also subject to an aggregate maximum of actual service and added years of 35 years.

2. **Strand II** — Applies to teachers aged 55 years or more who, having served for a minimum of 20 years, wish to retire and whose school management verifies that such retirement would provide an opportunity to enhance the education service provided by the school by facilitating change such as the introduction of new skills and curriculum review.

Pension entitlements are as follows:

- a teacher aged 55 with 35 years or more of reckonable pensionable service is granted pension based on actual reckonable service;
- a teacher aged 55 with less than 35 years of reckonable pensionable service is awarded pension based on actual reckonable service, enhanced by the grant of added years equal to whichever is the least of (a) two years, or (b) potential service to age 65, or (c) the service required to give total reckonable service of 35 years.

3. **Strand III** — Applies to teachers in posts surplus to requirements which will not be filled and who cannot readily be redeployed.

Pension entitlements are as follows:

Teachers with at least five years of pensionable teaching service have an option of either:

(i) immediate pension and lump sum based on actual (and purchased) pensionable service, enhanced by the award of added years at the rate of 35% of actual reckonable service, subject to

(a) added years not exceeding the lesser of seven years or potential service to age 65; and

(b) total service for pension and lump sum purposes being subject to a maximum of 40 years;

or

(ii) immediate pension and lump sum based on actual (and purchased) pensionable service, subject to the standard 40 year limit, with no added years award, but with a severance gratuity at the rate of three weeks' pay per year of potential service to age 65 (subject to a maximum of 27 weeks' pay).

4. Strands I and III are subject to an overall quota, in aggregate, of 150 retirements per year. Strand II is subject to an overall quota of 250 retirements per year. Priority is given to older teachers under all three strands where the number of applications exceed the quota.

5. All applications for early retirement under Strands I and II of the scheme are processed by an *Early Retirement Advisory Committee* (*ERAC*) which makes recommendations to the Minister.

6. The Scheme operates on a pilot basis pending review in the light of the Final Report of the Commission on Public Service Pensions.

CHAPTER 4

Management, Administration and Communication

4.1 Introduction

4.1.1 In this Chapter, we outline the management, administration and communication arrangements for public service pension schemes. We identify and discuss a number of issues which have arisen under these general headings. Our recommendations on these issues are presented in Chapter 25. We deal with the financing of public service schemes separately in Chapter 5.

4.1.2 In some parts of the public service, the pension scheme is small and is specific to a particular company or organisation; in others, it is a large *umbrella* type scheme applying to the sector as a whole. Thus, there are a large number of schemes and a wide range of organisations involved in different aspects of their administration.

4.1.3 Notwithstanding the complexity of these structures, it appeared to the Commission that on the basic requirement of any pensions administration system — paying pensions in the correct amount and on time — public service pensions are administered reasonably efficiently and effectively across all parts of the public service.

4.1.4 However, there are deficiencies in the system. Foremost amongst these, in our view, is the lack of proactive communication of the pension scheme. The focus of pension administration and personnel sections has traditionally been the calculation of benefits at the point of retirement and on death-in-service. Insufficient effort is made to communicate benefit entitlements to individual employees during service, to appraise them of options to enhance their pension, and to open up retirement choice. In addition, scheme documentation is not kept up to date in some parts of the public service.

4.1.5 There are deficiencies too in the recording of information, even basic service data. There is little use of modern information technology to formally record pensionable (or potentially pensionable) service with different employers, which is the norm in most private sector schemes. Part of the explanation for this may lie in the pay-as-you-go approach to financing public service pensions and the often limited resourcing of pension administration sections. Apart from creating problems for the valuation of pension liabilities and the estimation of future cashflows, the limited recording of service makes it difficult for individual public servants to calculate their full pension entitlements so that they can better plan for retirement.

4.2 Parties involved in administering and managing public service pensions

4.2.1 The main parties carrying out the day-to-day administration of pensions are the six government departments which operate the schemes for the major public service groups, as shown in Table 4.1.

Table 4.1: Administration of public service pensions

Department	Public service area
Finance	Civil service
Environment and Local Government (LGSS)	Local authorities, health service, VECs, etc.[28]
Health and Children	Health service
Education and Science	Teaching & support personnel
Defence	Defence Forces
Justice, Equality and Law Reform	Garda Síochána

4.2.2 In addition, a large number of public service bodies, including universities and non-commercial state-sponsored bodies, administer their own pension schemes, sometimes with assistance from outside pension consultants.

4.2.3 At a broader level, the primary brief for pensions policy, the financing of pensions, and the negotiation of changes to pension terms rests with the Department of Finance. We review the role of each party below. A more detailed note on existing pension administration arrangements is provided in Appendix 4.1.

4.2.4 The existence of separate pension schemes and administrative structures reflects the different strands of historical development of the public services. In recent times, there has been a growing centralisation and standardisation of approach, particularly as regards pension terms.

Department of Finance

4.2.5 The Department of Finance, through its Pension Section, administers the Civil Service Pension Scheme, with payment of pension benefits being carried out by the Paymaster General's Office. The Department has a major role in developing pensions policy for the public sector as a whole — in relation to pension terms and the financing of pension schemes — and in wider public service pensions management. It deals with union claims for changes to pension terms through the Civil Service Conciliation and Arbitration Scheme. It advises on the management response to pension claims elsewhere in the public service. It sanctions the payment of pension increases. It contributes to the development of national and EU policy on pensions matters generally and assesses the implications for public service schemes of new legislation and of relevant court judgements, both at domestic and European level. The Department also plays an active role in developing pension solutions to changing employment conditions and working requirements in different parts of the public service.

[28] The administration of pensions under the Local Government Superannuation Scheme is carried out by the individual local authorities, Health Boards, VECs, etc. The Department of the Environment and Local Government maintains an overall co-ordination and support role.

4.2.6 The other pension functions of the Department of Finance include:

- the formal approval of pension schemes, which are usually drawn up as Statutory Instruments based on a *model scheme* (see Paragraph 4.2.8) and requiring the signature of the Minister concerned and of the Minister for Finance;
- the provision of advice to departments and agencies on individual pension cases, and the granting of sanction in cases in which the Department has a formal role (e.g. approval of ill health retirements by civil servants, teachers, and members of the Garda Síochána);
- making decisions on appeal cases under pension schemes where the Minister for Finance is given a role as final arbiter; and
- the approval of AVC schemes for the civil service and other parts of the public service.

In addition, the Chief Medical Officer, who is attached to the Department, provides medical opinion on ill health retirement applications for civil servants and teachers.

Other government departments

4.2.7 The government departments which operate the other large public service pension schemes carry out the range of administrative duties discussed below.

4.2.8 These and other departments are also involved, with the Department of Finance, in approving pension schemes and modifications to schemes of public service bodies and state companies coming under their aegis. These schemes and revisions are generally drawn up in line with *model schemes* issued by the Department of Finance, which replicate the provisions of the Civil Service Pension Schemes. Departments also have some pension responsibilities relating to their own civil servants.

Other public service bodies

4.2.9 Other public service bodies — including hospitals, schools, universities and non-commercial state-sponsored bodies — are involved, to a greater or lesser degree, in the management and administration of pensions for their employees, whether under an umbrella scheme for the sector as a whole, or under a stand-alone scheme specific to themselves. Pension funds are used to finance the pension costs of a small number of schemes. In some cases professional pension consultants are employed to handle parts of the administration and/or to advise on changes to pension terms.

4.3 Adequacy of existing administration and communication systems

4.3.1 We discuss the adequacy of existing management and administration arrangements for public service pensions in this and the following Section under the headings:

- processing of pensions;
- pension administration for serving public servants;
- communication;
- appeals;
- development of pensions policy;
- negotiation of pension claims.

As noted previously, we consider the financing of pension schemes separately in Chapter 5.

Processing of pensions

4.3.2 Under this heading, we include the processing of pension calculations, the payment of pensions, lump sums, and gratuities, the implementation of pension increases and the payment of arrears.

4.3.3 It would appear to the Commission that the processing of pensions is carried out reasonably efficiently and effectively across all public service schemes. New pension cases are set up correctly and pension benefits are paid promptly. In most cases, pension increases, which are based on increases in pay of serving public servants, are paid within a reasonable period of the effective date of the relevant pay increases (although difficulties in relation to restructuring agreements have given rise to delays — see Section 11.8). Pensioners' queries are dealt with efficiently, and in some areas, personnel from the relevant pension sections meet with pensioner association representatives from time to time to discuss pensioners' concerns.

4.3.4 While a number of substantive issues have been raised by pensioner associations — and these are discussed elsewhere in this Report — it would appear that, in general, pensioners and their representative associations are broadly satisfied with the level of service which they receive from scheme administrators.

Pension administration for serving public servants

4.3.5 For serving public servants, the administration of pensions includes the recording of service and contributions, the processing of employee pension options (e.g. purchase of notional service, use of AVCs, payment of outstanding contributions in respect of prior service), dealing with public servants who leave employment before retirement age, and the transfer of pensionable service between public service organisations.

4.3.6 In general, existing administrative systems would appear to be capable of providing adequately for public servants who serve for their full career in centralised parts of the public service (e.g. civil service, Garda Síochána, Defence Forces) and have maximum pension entitlements at retirement age. The main administrative requirements arise at point of retirement when pension entitlements are being calculated. The recording of service is straightforward, although, increasingly, there may be breaks in full-time service due to career breaks or job-sharing.

4.3.7 It would appear that existing systems are less capable of addressing the needs of employees who have worked in non-centralised parts of the public service (e.g. the local authorities, and the education and health services). The main difficulty is the tracking of service, including temporary, part-time, and training-type employment, where a number of different employers may be involved. In many cases, computerised payroll/personnel systems have not been designed to record pensionable service. As a further complication, the reckoning of certain service may be at the option of the individual, subject to payment of outstanding contributions. Sometimes, the option is exercised only at retirement. Where there is prior service in another part of the public service, a formal transfer of service must be arranged for that service to be made reckonable in the calculation of pension with the final employer (see Paragraph 4.3.8). In many cases, a full calculation of pensionable service is only carried out at retirement or in the case of death-in-service.

4.3.8 Service may be transferred between public service bodies by means of the *Public Service Transfer Network*,[29] which facilitates mobility throughout the public service. However, the process of transferring service can be cumbersome, involving the verification of earlier service with previous employers and the assessment of any outstanding contributions (in some cases, a transfer value must be paid).

4.3.9 We note in Section 7.2 that the number of public servants taking up employment at older ages is increasing. Thus, it can be expected that many public servants will be interested in options to improve their pension, whether through the purchase of notional service or AVC schemes. We discuss both options in Chapter 12, where we identify certain deficiencies in current arrangements.

4.3.10 In addition to the requirements placed upon pension scheme administrators arising from the factors discussed above, there are ever increasing demands upon existing systems as a result of greater numbers of queries from individuals about their pension entitlements generally and as a consequence of the new pension provisions of the family law legislation in relation to judicial separation and divorce.[30]

4.3.11 In many public service areas/organisations, responsibility for different aspects of pension administration rests with different sections or units. For example, *Personnel Section* may be responsible for recording service, *Pay Section* for pay history and pension contributions, and *Pension Section* for technical aspects of the pension scheme. There may be little ongoing contact between these sections in the overall coordination of pensions administration. In some decentralised areas (e.g. local authorities/health service), most of the day-to-day responsibility for queries and the processing of employee options rests with the local personnel section. Given the increasing complexity of the pensions environment, it must be asked whether employees are being provided with the appropriate level of expert assistance and advice, and whether existing administrative structures represent the most efficient and effective method of administering pensions across the public service as a whole.

4.3.12 To conclude, difficulties arising from inadequate tracking of pensionable service and the lack of computerised pension systems became very apparent to the Commission when the actuarial review of public service pensions was being undertaken. Given deficiencies in the data available, it was necessary to prepare samples and estimates for particular public service groups. Many schemes did not maintain a central record of individuals with deferred or preserved pension entitlements. The Commission considers that this situation is far from satisfactory. Apart from creating an obstacle to assessing future pension costs, the lack of easy access to pension and service records on a centralised basis hinders those employees who make the effort to ascertain their own personal pension entitlements and to plan accordingly.

Communication

4.3.13 The Commission views communication as an important component in the proper administration and management of pension schemes. Communication includes the provision of:

[29] For legal reasons there are in fact two such networks – one dealing with transfers between bodies neither of which is a local authority and the other covering cases where the transfer is either to or from a local authority. We refer to the Civil Service Transfer of Service Scheme in Paragraph 3.3.45.

[30] The Family Law Act, 1995 and the Family Law (Divorce) Act, 1996 require that pension rights must be taken into account by the court where, following a judicial separation or divorce, the parties to the marriage apply to the court for one or more of the various orders prescribed under the Acts for the purposes of financial settlement (The Pensions Board, *Trustee Handbook* (1998), p. 65).

- information on accrued occupational pension entitlements and, where relevant, on State Social Insurance entitlements;
- options to improve pension entitlements;
- options to part-finance the cost of retiring early;
- annual report and general information on the pension scheme;
- replies to queries from employees and pensioners;
- information as required in family law cases.

4.3.14 Under the disclosure regulations of the Pensions Act, 1990, pension schemes (including those in the public service) are required to prepare annual reports and to provide these automatically to qualifying trade unions and, on request, to scheme members, prospective members, and to their spouses. As part of this process, schemes are obliged to inform members of the availability of their annual reports. A person leaving employment with an entitlement to preserved benefits (*early leaver*) must be provided automatically with a statement of his or her entitlements and of the rules applying to payment. For new entrants, basic information on the scheme (eligibility, contributions, benefit details, etc.) must be provided automatically within a certain minimum period of joining. The constitution of the scheme should be made available for inspection. Where serving members seek it, the scheme must provide details of personal entitlements, including survivors' benefits, contribution and service history, etc. On retirement or death, information must be provided on the amount of benefits payable, options relating to these benefits, and the rules governing continued payment of pension and how the amount of pension might subsequently be altered.

4.3.15 It is not clear to the Commission that all public service schemes have sufficient resources to provide a satisfactory level of communication to public servants in relation to their pension scheme and individual benefit entitlements. The case of early leavers is a particular concern.

4.3.16 While the quality of scheme information may have improved over the last number of years, partly as a result of implementation of the Freedom of Information Act, 1998, it would appear that, for some schemes, information booklets are not regularly updated to cover the most recent developments. The fact that the formal constitution of certain schemes may be in the form of a series of Acts and Statutory Instruments can make it difficult for employees to exercise their right of inspection. This difficulty is compounded in a number of instances by the fact that the actual drawing up of relevant regulations is often in arrears.

4.3.17 In the report on the National Pensions Policy Initiative*, Securing Retirement Income*, the Pensions Board recommended that schemes should automatically provide annual statements to scheme members. These statements, in addition to giving personal benefit information (personal accrued amount and prospective level of pension), would address points relating to Social Welfare pensions. The Board accepted that where there were large numbers in the same grade — such as in the public service — it might be necessary to issue *grade statements* rather than personalised statements, at least initially.[31]

4.3.18 Apart from formal compliance with the disclosure requirements of the Pensions Act, the Commission is in favour of active communication of benefit entitlements and of options to

[31] The Pensions Board, *Securing Retirement Income* (1998), pp. 177-8.

improve benefits so that employees can take a more active role in planning for their retirement. We discuss this further in Chapter 19.

4.3.19 We consider that there are major shortcomings in current communication systems for public service schemes. Greater resourcing of this aspect of pensions administration will be necessary, particularly in the context of our recommendations for the future direction of public service pensions.

Appeals

4.3.20 Most decisions relating to entitlements under public service occupational pension schemes flow directly from the relevant schemes (which are usually in the form of Statutory Instruments) and there is limited or no discretion in applying case law and precedent to individual cases. As regards appeals and complaints, it would appear that the general line adopted by scheme administrators is that if a particular matter does not come within the remit of the scheme, it cannot be accommodated without amending that scheme. It would seem that many individual complaints may actually relate to settled pensions policy, for example, in relation to the cut-off date for the introduction of preserved benefits, reckoning of non-pensionable allowances, etc.

4.3.21 The Commission notes that public service pension schemes are subject to the following formal appeal/complaint mechanisms:

- recourse to the Public Service Ombudsman (in relation to cases of maladministration);
- the Freedom of Information Act, which gives a statutory right to obtain reasons for decisions and access to relevant papers;
- a formal system of appeal, generally available under public service schemes, to the relevant Minister and, in some cases, to the Minister for Finance.

4.3.22 In addition, there are a number of other avenues which enable public servants and pensioners to draw attention to what they consider are unsatisfactory decisions in relation to their pension entitlements. These include political representations, parliamentary questions, and representations by unions and pensioner organisations.

4.3.23 As a result, the general view amongst scheme administrators would appear to be that any individual complaints which have a substantive element of justification are normally resolved in favour of the pensioner, sometimes on the *benefit of the doubt* basis. However, a number of submissions received by the Commission suggested that there was need for an independent pensions body to consider cases involving a dispute or appeal.

4.3.24 We note that the formal appeal system referred to in Paragraph 4.3.21 involves the appropriate Minister (in some cases, in consultation with the Minister for Finance) acting in a quasi-judicial way, making a determination on an individual case where the public servant or pensioner has invoked the right to appeal the employer's determination of his or her pension or prospective pension entitlements.

4.3.25 We would suggest that questions arise as to the effectiveness of this form of appeal. It would appear that the departmental staff who are involved in processing appeals are often those who advised on how to handle the cases in the first instance. While complainants ultimately have recourse to the courts as a last resort, it can be argued that a more transparent and independent appeal system would be to the benefit of scheme administrators and aggrieved parties as a more effective means of addressing concerns raised.

4.3.26 The Public Service Ombudsman's Office has outlined the essential criteria for a good internal complaints system. We summarise these below.

Accessible	Simple instructions about how to make a complaint should be made available. This should clearly identify the designated complaint handlers and explain how they will operate.
Simple	The various stages in the complaint handling process should be kept to a minimum with each stage in the process clearly identified.
Speedy	Targets should be set for acknowledging receipt of complaints and the completion of their examination.
Fair and Independent	Complaints not resolved by the original decision maker should be examined objectively by persons not involved with the original decisions or actions. The examination should have regard not only to the rules governing the scheme but also to considerations of equity and good administrative practice.
Confidential and Impartial	All complaints should be treated in confidence.
Effective	The complaints system should have the authority to address all the issues giving rise to the complaint. Where the examination finds that the fault lies with the public body, the system must have the power to provide appropriate redress.
Flexible	Where rules are necessary to ensure consistency, too much rigidity should be avoided and there should be a degree of discretion given to those involved in the system to adjust to changing needs.[32]

4.3.27 Measured against these criteria, appeals mechanisms in public service pension schemes would appear to fall down in a number of respects.

4.4 Management of pensions across the public service

4.4.1 The management of public service pension schemes across the public service as a whole involves managing the overall financing of pensions (see Chapter 5), developing pensions policy, and negotiating changes to scheme terms with the public service unions. While there is an obvious link between policy development and the negotiation of change, we consider them separately below.

Development of pensions policy

4.4.2 Pensions policy includes assessing the implications for, and representing the concerns of, public service schemes in relation to legislative changes proposed at national level (e.g. Pensions Act, Family Law Acts) and at European level (e.g. Directives in the area of equality in pension schemes), as well as the impact of relevant court judgements in the domestic courts and in the European Court of Justice. It also involves the implementation of necessary scheme modifications arising from legislative developments and court decisions.

4.4.3 As we have shown in Chapter 3, public service pension schemes are usually provided for in primary legislation and drawn up in the form of Statutory Instruments. They are financed on a

[32] The Ombudsman, *An Example of a Code of Good Administrative Practice*, pp. 9-11.

pay-as-you-go rather than a funded basis, which is the approach of occupational pension schemes in the private sector. This combination of factors has, in the past, given statutory public service occupational pension schemes a special status *vis-à-vis* occupational pension schemes generally. For example, unfunded public service schemes do not require approval by the Revenue Commissioners under the Finance Act, 1972. In addition, public service schemes are exempt from certain of the regulatory requirements of the Pensions Act in relation to occupational pension schemes.

4.4.4 However, developments over time have tended to blur this distinction, and nowadays, private sector and public service occupational pension schemes are usually treated in similar fashion for the purposes of national and EU policy and legislation, as well as by the courts. At the European Court of Justice, it has been found that even though public service pension schemes are drawn up in statutory form and are financed by the State, they should nonetheless be considered, like private sector occupational pension schemes, as coming within the scope of Article 119 of the *Treaty of Rome* dealing with pay, rather than as statutory schemes of social security (which are outside the scope of that Article).[33] This judgement confirms the view of public service occupational pensions as deferred pay and so negotiable between unions and management. In conclusion, it is clear that public service occupational schemes no longer enjoy a special status, and must now be considered in the context of occupational pension schemes generally.

4.4.5 The main policy issues currently impacting upon public service pension schemes in common with all other occupational pension schemes are as follows:

- equality;
- access to pension schemes for part-time and contract employees;
- disclosure of information to scheme members;
- pension provisions of Family Law legislation;
- mobility of workers across Europe.

4.4.6 The central co-ordinating role of the Department of Finance ensures an integrated approach to pensions policy issues across the public service. The *model schemes* (see Paragraph 4.2.8) are updated regularly to reflect current legal requirements and developments in public service pensions policy.

4.4.7 As the discussion above indicates, the range of issues affecting pensions, some of which are quite complex, has widened considerably in recent years. As a consequence, and with increasing regulation of occupational pension schemes, the Commission considers that it is becoming more difficult for public service pension schemes to keep abreast of current developments. There are no structures to bring together public service pension scheme administrators and policy makers to discuss developments on a regular basis. We would suggest that this has probably acted as an inhibiting factor in progressing change.

4.4.8 Because of the existence of separate pension schemes, any amendment to pension terms which is required on foot of new legislation or the outcome of a court case has to be implemented separately for each scheme, subject to the approval of the Department of Finance. This may take

[33] Case C-7/93 ABP v Beaune (judgement of 28 September 1994, paragraph 23).

a long period of time. The Commission notes that in many cases changes in pension terms are operated on an administrative basis pending the formal updating of schemes in due course.

Negotiation of pension claims

4.4.9 Changes to pension scheme terms usually involve negotiations with the public service unions, e.g. the 1973 civil service working party changes (see Paragraph 3.3.10); some of these negotiations may form part of wider negotiations on pay and conditions.

4.4.10 Public service pension terms are amended relatively infrequently. Changes may be proposed by the public service unions. They are often raised first as claims in the civil service context and negotiated with the Department of Finance under the civil service conciliation machinery. Thereafter, many of these changes are negotiated under separate conciliation processes in the other sectors of the public service, sometimes involving some of the same personnel, on both sides of the table, who were involved in the civil service negotiations. Some examples are the spouses' and children's pension scheme (first introduced in the civil service in 1968 and subsequently extended to other areas), the revised main pension scheme terms (introduced with effect from June 1973 in the civil service and extended to the LGSS and teachers' schemes in 1977), the purchase of notional service schemes, the revised spouses' and children's pension schemes, and the professional added years schemes.

4.4.11 In some cases, claims may be lodged initially in the local authority, health or education sector, often in relation to issues that are more relevant in those sectors than in the civil service, e.g. part-time working, the reckoning of past service, etc. As well as participating at working party level in the context of civil service pensions, the Department of Finance forms part of the management teams under the Teachers' Conciliation Council, the Local Government Superannuation Scheme Conciliation Committee, and the Garda Síochána and Defence Forces' Conciliation and Arbitration Schemes.

4.4.12 Under public service conciliation and arbitration schemes, pension terms are conciliable but not arbitrable (except by agreement). Thus, if there is disagreement between management and unions regarding a particular pensions claim, there is no agreed procedure for its determination by an outside party.

4.4.13 Recent amendments to the terms of the Industrial Relations Acts have given employees in the local authority and Health Board areas access to the Labour Court and the Labour Relations Commission and future pension claims for such employees will fall to be dealt with in those fora rather than under the traditional conciliation process.

4.4.14 As already indicated, not all changes to pensions terms emerge directly from the industrial relations process. Other developments can have a direct and binding influence on public service pension terms, e.g. the Government decision to introduce full PRSI for all new entrants to the public service, national pensions legislation (e.g. the Pensions Act), and European Court decisions (such as those in the equality area).

4.4.15 While changes to scheme terms are often implemented first on an administrative basis, they invariably require a formal change to the terms of each individual pension scheme affected (see Paragraph 4.4.8). The Commission notes that this can be a cumbersome process. As changes must be negotiated separately for each scheme, it can result in different implementation dates for different schemes, which can be a source of grievance for any individuals affected.

4.4.16 Table 4.2 outlines a range of recent modifications to public service pension scheme terms, giving the source of the change and the schemes affected in each case.

Table 4.2: Recent changes in public service pension scheme terms

Item	Source of change	Date	Schemes affected
Pension splitting in Family Law cases	Family Law Acts	1995-96	All
Full PRSI for new entrants—integration	Government decision	1995	Most[34]
Access to pension schemes for part-time and temporary employees	European Court of Justice judgements, EU Directives, policy development	c 1997	Potentially all
Pensionability of Garda Síochána unsocial hours payments	*PCW* agreement (part of wider package of pay and conditions)	1994	Garda Síochána
Pilot early retirement initiative for teachers	*PCW* agreement (part of wider package)	1996	Teachers
Pilot early retirement initiative for nurses	*PCW* agreement (part of wider package)	1996	Nurses
Minimum death gratuity	LGSS negotiations	1996	LGSS
Change in upper age limit for children's pension	Civil Service Working Party	1997	Civil service (potentially all)

4.4.17 Notwithstanding the coordinating role of the Department of Finance, it would seem to the Commission that the existence of different industrial relations structures, with independent arbitration in some cases, creates a potential for changes in pension terms to be implemented in one part of the public service without full consideration being given to their possible impact on other public service schemes.

4.5 Conclusions

4.5.1 The Commission considers that existing arrangements for administering and managing public service pension arrangements, while deficient in certain respects, ultimately fulfil their objective of paying pensions in an efficient and effective manner. Some of the difficulties faced by the administrative systems, such as the establishment of comprehensive scheme databases and better communication procedures, are capable of resolution with greater resourcing and usage of appropriate information technology. We believe that given the defined benefit structure of the pension schemes and the fact that standard terms apply across most of the public service there is no reason why public servants should not be provided with good quality information on their pension benefits.

[34] Schemes covering public service groups which were in full PRSI class prior to the 1995 change — e.g. non-established civil servants — were unaffected by the change.

4.5.2 A significant feature of the pension system is the growing centralisation of approach, particularly in relation to pension terms. This has been assisted to a great degree by the widescale use of *model scheme*s across the public service. We believe that uniformity of pension terms is a valuable tool in managing pension schemes, as it can act as a restraining influence in certain situations where the concession of an improvement in terms in one sector of the public service could have widespread financial repercussions across the public service as a whole. The other side of the coin, however, is that the knock-on effects of a concession can ripple right across the system very quickly and with considerable expense.

4.5.3 This move towards a more centralised approach raises the question of how the measures recommended by the Commission later in this Report will be implemented. It is clear that, on a global scale, the Commission's recommendations will involve a set of initiatives which will impact upon all pension schemes in a way which requires effective, integrated, and coordinated management and administration systems. We discuss this matter further in Chapter 25.

APPENDIX 4.1

Current public service administration arrangements

Introduction

1. There is no standard model for the administration of public service pensions. Some schemes are managed centrally (e.g. the national and secondary teachers' schemes, the Defence Forces' schemes and the Garda Síochána scheme) whereas others are managed locally (e.g. the Local Government Superannuation Scheme). The civil service scheme combines both methods in that most departments have devolved responsibility for pensions administration while the Department of Finance operates the scheme for the remaining departments.

2. Pension management and administration arrangements for the larger public service groups are outlined in the following paragraphs.

Civil service

3. Service and contribution records for each individual civil servant are maintained by the employing department. Those departments with devolved responsibility, e.g. the Department of Agriculture, Food and Rural Development, calculate the pension entitlements of their staff while the Department of Finance carries out this function in respect of other departments. The Department of Finance calculates pension increases for all pensioners. It has computerised some of its pensions administration, e.g. pensions payroll and calculation of benefits, but many operations, e.g. pension increases, are done manually. There is little computerisation of pensions administration in other departments.

4. Departments are required to refer some of the more difficult pension cases, principally involving professional added years or options to purchase notional service, to the Department of Finance for decision.

5. Changes to pension terms in the civil service are discussed between the Department of Finance and the civil service unions, initially at the General Council of the Civil Service Conciliation and Arbitration Scheme, and are usually referred to a joint management/staff working party (which meets four times a year).

6. Informal meetings and contacts take place from time to time between pensioner representatives and the Department of Finance to discuss matters such as pension increases and pension payment arrangements.

7. Pensions Section in the Department of Finance comprises 15 employees. Of these, eight are involved in administrative duties, and nine in policy formulation. In addition, 12 employees in the Paymaster General's Office are involved in the payment of civil service pensions.

Local authorities

8. The Department of the Environment and Local Government exercises an overall policy, support and guidance role in relation to the Local Government Superannuation Scheme (LGSS) but leaves the administration of the scheme to the local authorities themselves (there are 29 County Councils, 10 Corporations, and 49 Urban District Councils). To assist local authorities and to standardise practice, the Department has developed a number of initiatives over the years, principally an expert computer system. While this has helped to overcome inconsistencies, experience to date would suggest that some authorities, particularly the smaller ones, continue to have difficulties in administering what can be very complex provisions. In some authorities, it would seem that the computer system either is not operated at all or is used for very limited purposes. The computer system comprises—

- an information element which contains all the relevant scheme rules and documentation; a help desk; and a step by step process for the determination of reckonable service; and
- databases which store all relevant service and contributions data, calculate the benefits when they become due, and produce benefit statements.

The system is being upgraded at present.

9. All aspects of administration, including record management and the payment of pension awards, are dealt with locally and pension payments are met from the authorities' own resources and charged to their programme accounts.

10. The Minister for the Environment and Local Government has an appellate function in relation to LGSS pensions.

11. Changes to the LGSS have, to date, been dealt with by a committee representing management and staff interests under the aegis of the Local Government Management Services Board. The Department of Finance is represented on this committee. Now that all local authority staff have access to the Labour Court and the Labour Relations Commission, the role of the committee may be re-examined.

12. Pensions Section in the Department of the Environment and Local Government comprises nine employees, seven of whom deal with the LGSS, with the remaining two responsible for the pension entitlements of the Department's own staff. In addition, personnel employed by the local authorities are directly involved in the administration of the pension scheme.

Health service

13. The pension arrangements for the health service come within a number of distinct schemes. The Health Boards are covered by the LGSS which is administered by the Department of the Environment and Local Government (see above), while the voluntary hospitals and nominated health agencies come within the Voluntary Hospitals Superannuation Scheme (VHSS) and the Nominated Health Agencies Superannuation Scheme (NHASS), respectively, and are administered by the Department of Health and Children. In contrast to the LGSS, the VHSS and the NHASS are managed centrally with all the day-to-day functions, such as the calculation and payment of pensions, being carried out by the Department of Health and Children. There is not a high level of computerisation.

14. Changes to the pension arrangements for health service personnel arise from negotiations conducted under the aegis of the Health Service Employers Agency.

15. Negotiations are ongoing in relation to the transferring of the pension arrangements for relevant health service personnel from the LGSS to the Department of Health and Children.

16. Pensions Section in the Department of Health and Children comprises nine employees. Most of the work is of an administrative/payment nature. Personnel in the Health Boards, voluntary hospitals, etc. are also involved in the administration of pensions.

Education sector

17. All records relating to the service, pay, contributions, etc., of national and secondary school teachers are maintained centrally by the Department of Education and Science. Individual schools do not have any pension functions. The verification of past service and charging of arrears of contributions is handled by the Department, as is the calculation of pension entitlements. The scheme administration is not computerised, with the exception of the pensions payroll (for the national teachers' and secondary teachers' schemes) and the downloading of service details from the payroll system (national teachers).

18. Responsibility for the pensions of vocational teachers was transferred to the Department of Education and Science from the Department of the Environment and Local Government in September 1998. The Vocational Teachers' Superannuation Scheme is administered locally by the Vocational Education Committees, with the exception of payment of awards which is the responsibility of the local authorities. The Department of Education and Science exercises the same policy and support role in relation to vocational teachers' pensions as the Department of the Environment and Local Government does in relation to the pensions of local authority staff.

19. Changes to the teachers' pension schemes are made arising from agreement at the Teachers' Conciliation Council (the Department of Finance is represented on the management side of the Council). Some changes are made outside of the Conciliation Council, with the consent of the Department of Finance.

20. Teachers' Pensions Section in the Department of Education and Science comprises 27 permanent employees and 10 temporary employees. Most of the work is of an administrative/payment nature.

21. The Department of Education and Science also administers separate pension schemes in respect of the Colleges of Education and clerical and support staff in schools.

22. In the case of universities and a range of other education bodies, there are a number of stand-alone pension schemes which are administered in full by the body in question. Finance is made available by the Higher Education Authority (HEA) or by the Department of Education and Science. Some of the older Universities (e.g. UCD, Trinity, Maynooth and UCC) have pension funds and the HEA provides finance for the employer contributions to the fund, plus the cost of pension increases. Changes to pension scheme terms — usually in line with changes in the larger public service schemes — are negotiated locally, in agreement with the Department and the Department of Finance.

Defence Forces

23. All records relating to the pension entitlements of Defence Forces personnel are kept centrally by the Department of Defence. The Pensions Unit of that Department calculates and pays the pension entitlements when they become due. The pensions administration system is a manual one with the exception of pensions payments, which are computerised.

24. Changes to the pension arrangements for Defence Forces personnel arise from negotiations under the Defence Forces' Conciliation and Arbitration Scheme, at which the Department of Finance is represented.

Garda Síochána

25. The calculation and payment of Garda pensions are carried out by the Department of Justice, Equality and Law Reform. Service records are provided by the Garda authorities. There is little computerisation apart from the pensions payroll.

26. Changes to the pension arrangements for the Garda Síochána arise from negotiations under the Garda Síochána Conciliation Council, at which the Department of Finance is represented.

27. Ill health retirement and complex cases are referred to the Department of Finance.

28. Pensions Section in the Department of Justice, Equality and Law Reform comprises nine employees. Most of the work is of an administrative/payment nature.

Non-commercial state-sponsored bodies and other public service bodies

29. There are separate pension schemes for each of the non-commercial state-sponsored bodies coming under the aegis of a range of government departments. There are many such bodies and schemes — over 100 bodies participate in the Public Service Transfer Network. The largest schemes are in respect of FÁS, Teagasc, Forfás, Enterprise Ireland, the Central Fisheries Board and the Blood Transfusion Service Board.

30. Practically all of the schemes of these bodies conform to the *model schemes* developed by the Department of Finance and the degree of divergence between schemes is relatively small.

31. While a small number of the older non-commercial state-sponsored bodies have pension funds (e.g. FAS), most operate on a pay-as-you-go basis. Some avail of the services of private sector pension administrators and advisors.

32. Changes to pension scheme terms — usually in line with modifications introduced in the larger public service schemes — are negotiated locally, in agreement with the parent department and the Department of Finance.

CHAPTER 5

Financing and Accounting Arrangements for Public Service Pension Schemes

5.1 Introduction

5.1.1 In this Chapter, the Commission outlines current financing and accounting arrangements for public service pensions and evaluates the appropriateness of these arrangements in the changing public service environment. We also present a preliminary discussion of the pre-funding of public service pension schemes as a means of better managing future pension costs.

5.2 Current financing and accounting arrangements

5.2.1 The majority of public service occupational pension schemes are financed on a pay-as-you-go basis, with the annual cost of pensions being met from current revenue. Thus, pension liabilities are secured by the Government and its ability to tax. In contrast, private sector companies and commercial state companies operate a pre-funding system, setting aside funds and investing them to meet future liabilities as and when they arise.

5.2.2 The pay-as-you-go method of financing pensions reflects the cash accounting approach which has traditionally underpinned government accounting systems. Under this approach, the annual charge for pensions in government accounts is in respect of the cost of pensions and lump sums of public servants who have retired or died in service during the year in question, as well as the cost of pensions already in payment. Unlike funded schemes, there is no charge or adjustment made in respect of the accruing cost of pensions, i.e. the cost to be met at some future date of the pension benefit earned by serving staff *as pensionable service is completed*. In addition, current government accounting systems do not contain any record of the pension liability in respect of the past service of serving public servants and of pensioners.

5.2.3 In the civil service, the cost of pensions is met from a central Superannuation Vote which is administered by the Department of Finance; thus, departmental Appropriation Accounts do not contain any pension charges for serving civil servants. Different arrangements apply to other public service groups (see Appendix 5.1); for example, the pay-as-you-go cost of Defence Force pensions is met from the Army Pensions Vote, while the cost of local authority pensions is charged to the accounts of each individual local authority (and is not identified in the accounts of the Department of the Environment and Local Government).

5.2.4 Usually, pension contributions received from employees are recorded under the Appropriations-in-Aid heading of the appropriate Vote, rather than netted off against pension payments.[35]

[35] Taking the example of the health service, total pension contributions by serving employees in 1997 were equivalent to about 60% of total pensions expenditure that year (see Tables 6.4 and 6.5).

5.2.5 A number of universities and non-commercial state-sponsored bodies operate pre-funded pension arrangements. In the case of the universities, the Higher Education Authority (HEA) provides 15% of pensionable payroll annually to cover pension costs. This money is invested by the respective funds and, along with investment returns and employee contributions, is used to pay pensions. Pension increases are financed separately with a further 5% (approximately) of pensionable payroll being paid annually by the HEA to cover such costs. The universities and/or their agents have complete autonomy in the areas of investment and investment policy and no Exchequer/HEA controls or monitoring are in place.

5.2.6 Pension costs for the public service as a whole go largely unreported in government financial statements, although an expenditure figure was included in the Budget 2000 tables.[36] In 1997, according to the Commission's actuarial review (see Section 6.4), the total expenditure on public service pension schemes was £636 million (€807 million). The total of employee contributions received was £185 million (€235 million). In comparison, assuming an average new entrant rate[37] of 19% of pensionable remuneration, which is inclusive of the employee contribution, the accruing cost of pensions for serving staff for 1997 is estimated at £780 million (€990 million).

5.2.7 The Department of Finance produces a regular analysis of the Exchequer pay and pensions bill, the most recent of which relates to the period 1995-2000.[38] Local authority pay and pension costs are excluded. The Exchequer pay and pensions bill covers:

(i) the actual cost to the Exchequer of the pay and pensions of civil servants, teachers, members of the Garda Síochána and the Defence Forces;

(ii) the amounts which are included in respect of pay and pensions in grants to Health Boards and other health agencies (such as voluntary hospitals), universities and other third level colleges, and non-commercial state-sponsored bodies; and

(iii) the cost of employer PRSI contributions.

Employee pension contributions are netted off the gross figure. A separate table shows a sectoral breakdown of the Exchequer pensions bill, indicating the percentage year-on-year growth in net pension expenditures.

5.2.8 The Commission would question the usefulness of the table for the management of pension costs. The increase in pension expenditures reported in any year reflects, mainly, the number of retirements which have taken place during the year, and the cost of pension increases for those then in receipt of pensions. Both factors are effectively outside the control of decision makers. In reality, the actual incurring of pension costs has taken place at a much earlier stage.

5.3 Pay-as-you-go versus funding

5.3.1 There are two basic approaches to financing pensions: pay-as-you-go, where pension costs are met from current revenue; and pre-funding, where funds are set aside and invested to meet future liabilities as and when they arise.

[36] Department of Finance, *Budget 2000*, Table E, p. 171.

[37] The new entrant rate represents the contribution (as a percentage of pensionable remuneration) which would be required to fully fund the accruing cost of current public service pension terms for serving staff — see Paragraphs 6.2.8-6.2.10 and Section 6.6. Pensionable remuneration in 1997 is estimated at £4,087 million (€5,189 million).

[38] Department of Finance, "Analysis of Exchequer Pay and Pensions Bill 1995-2000" (June 2000).

5.3.2 The arguments generally made in favour of the *pay-as-you-go* system include the following:

- the State's permanent and continuing commitment to discharge its obligations as they arise adequately meets the primary objective of funding in the private sector, viz. to provide a secure basis for the pensions of employees;
- pay-as-you-go is easy to operate and the administrative costs are low;
- pay-as-you-go is in keeping with the Government's budgetary system generally;
- pay-as-you-go facilitates transferability of service within the public service (in most cases, no transfer payments need to be made when a public servant moves from one public service scheme to another).

5.3.3 The arguments made in favour of *funding* include:

- funding, unlike pay-as-you-go, makes advance provision for future liabilities;
- the real cost of pensions is immediately obvious under a funding arrangement. Thus, the long-term effect of increases in the number of personnel covered and/or improvements in pension terms (which may have only a minor impact on costs under a pay-as-you-go system in the short-term) is immediately apparent to the parties concerned;
- contribution rates for a pension fund would bring home to members of schemes the value of their pension entitlements and to employers the real cost of recruitment;
- funding would give a more stable profile of costs to the Exchequer over time compared with pay-as-you-go.

5.3.4 The Commission notes that a number of the arguments in favour of funding have to do with the need for transparency in pension costs. This brings up the related question of the accounting for pension costs in government financial management systems, a matter we discuss in Section 5.4 following.

5.3.5 The question of funding, or of partially funding, public service and Social Welfare pensions was recently considered by the Government in the context of the report of the Budget Strategy for Ageing Group.[39] The Group had been asked to bring forward specific proposals, in the light of present and prospective substantial budget surpluses, designed to ease the longer term budgetary burden of the Exchequer's liability for Social Welfare and public sector employee pensions implicit, respectively, in the prospective ageing of the general population and of public servants. The review of the Social Welfare liability was in line with the recommendation of the Pensions Board in *Securing Retirement Income* (1998) that steps should be taken to establish an explicit mechanism to fund, at least partially, the prospective substantial growth that is projected to occur in Social Welfare old age pensions, if they are increased in line with real earnings.[40]

5.3.6 As a result of these deliberations, the Minister for Finance announced on 23 July 1999 that the Government had decided to provide resources on a planned basis to secure future pensions, setting aside an annual provision of 1% of GNP (then estimated at £520 million for 1999) to pre-fund part of the future cost of Social Welfare and public service pensions. The Minister added that the Government had also decided to allocate a tranche of the proceeds of the flotation of Eircom (then Telecom Éireann) to supplement the annual allocation.

[39] Department of Finance, "Report of the Budget Strategy for Ageing Group" (July 1999).
[40] The Pensions Board, *Securing Retirement Income* (1998), p. 110.

5.3.7 In its report, the Budget Strategy for Ageing Group had estimated that even if all Exchequer receipts arising from future privatisations of state bodies were allocated to pre-fund future Exchequer liabilities, these, together with the annual allocation proposed, would be sufficient to fund about 40% only of the extra pension and health costs which the Exchequer would face over the decades ahead. Accordingly, the Group recommended that:

- the annual pre-funding allocation should be established as a non-discretionary budget item, to be met each year regardless of economic, budgetary or other circumstances;
- there should be periodic reviews of the actuarial position of the funds and an associated automatic requirement to adjust either the amount of annual funding assigned to, or the basis on which draw-down may be made from, each fund consistent with the outcome of each actuarial review of the long-term viability of the funds.

5.3.8 The Government acknowledged in its statement of July 1999 that there were major policy issues to be determined in legislating for pensions pre-funding and that these would be considered in the drawing up of the necessary legislation. Reference was made to the upcoming report of the Commission on Public Service Pensions in that context. The relevant legislation, the National Pensions Reserve Fund Bill, 2000, was published in June 2000.

5.3.9 The Commission's analysis and recommendations on the funding of public service pensions, taking into account the relevant economic arguments as well as the implications of the Government's pre-funding initiative, are set out in Chapter 23.

5.4 System of accounting for public service pensions

5.4.1 The financing of public service pension schemes is closely related to the question of accounting for pension costs. In this Section, the Commission discusses the limitations in the treatment of pension costs under the existing cash-based approach. We also review developments generally in the reform of government financial management systems, which have implications for the reporting of pension costs.

5.4.2 As outlined above, government pension costs are financed on a pay-as-you-go basis. Accounting for pension costs has traditionally followed this method of financing; thus, only actual cash outgo and member contributions received are recorded in government financial systems.

5.4.3 The shortcomings of a purely cash-based approach to accounting for government pension costs and liabilities are outlined below:

- it fails to highlight the long-term cost of pensions, which is expected to increase substantially over the next 20 years. In particular, cash accounting fails to capture the long-term cost of management decisions to improve pension terms, extend scheme coverage, and to recruit additional employees. In the case of recruitment, for example, there would actually be a short-term pension saving through increased employee contributions (however, the eventual cost of pensions for these employees would far outweigh the value of the contributions received);
- it conveys a false impression of the affordability of pensions — it makes no sense in accounting terms to relate the actual cost of pensions in payment to the employee contributions received from serving staff;

- existing systems fail to bring home to employers the true cost of decisions to retire employees early on grounds of ill health, restructuring, or efficiency. In private sector funded schemes, employers are often required to pay in advance to the pension fund the additional capital cost arising from an early retirement (or to use a fund surplus to finance the early retirement);
- because of the above deficiencies, it becomes difficult to delegate to departments and agencies responsibility for important categories of management decision making in accordance with the modernisation of the public services under the Strategic Management Initiative (see Paragraph 7.5.2);
- by failing to report the full cost of pensions — particularly that portion being borne by the employer — existing systems impact adversely on the value placed on pensions by employees. This can lead on occasion to the pursuit of unsustainable pension claims such as in the area of early retirement;
- because they give no recognition to the accruing cost of pensions and of accumulated pension debt, current arrangements are open to criticism by international organisations such as the World Bank, the IMF and the OECD. In its 1998 Article IV consultation report on Ireland, the IMF urged the authorities to take the opportunity afforded by buoyant economic conditions to incorporate at least the full accruing cost of public service pension liabilities in future budgets.

5.4.4 The Commission considers that implementation of the following measures would help address these problems (we take these up further in Chapter 24):

- provision for regular actuarial reviews of public service schemes;
- actuarial valuations to be carried out on proposed changes to scheme terms; and
- changes to government financial management and reporting structures to record accruing pension costs in a more transparent way.

Reform of government financial systems

5.4.5 The annual departmental Appropriation Accounts are prepared primarily on the basis of cash-based receipts and payments.[41] The accounting system records the movement of cash in and out of the Department, i.e. those receipts and payments actually received and paid during the period of account. Under this system, the accounts for any particular year include, but do not distinguish between, cash required to meet liabilities outstanding at the end of the previous year plus cash required to meet liabilities incurred and falling due for payment in the current year. They do not provide for liabilities incurred in the current year but which are not expected to mature for payment until the following year.

5.4.6 The cash basis of accounting used by government departments differs from the system used in the commercial sector which is known as the *accrual system*. With accrual accounting, revenues are taken into account when due, even if not received, and expenditures are charged in the account when liabilities are incurred, whether payment is made in the accounting period or not. The system also allows deferral of expenses so that resources consumed during an accounting period can be identified. This facilitates the matching of costs with outputs. In relation to pensions, the general approach, subject to certain qualifications (see Paragraph 24.2.4), is to

[41] Much of the material in Paragraphs 5.4.5 and 5.4.6 is taken from Department of Finance, *Public Financial Procedures: An Outline* (1990), p. 42.

ensure that the operating costs of providing retirement benefits to employees are recognised in the accounting periods in which the benefits are earned by the employees. Financial statements are prepared separately for the pension fund.

5.4.7 Until recently, the cash-based accounting system has been considered appropriate for government accounting purposes because its simplicity enables the annual Appropriation Accounts to be prepared more easily and because it fits in well with the requirements of parliamentary control. However, over the past few years, in keeping with the emerging focus of the Strategic Management Initiative (see Section 7.5), the emphasis of the accounting system has moved on from simple compliance with spending limits to measuring achievement and recording full costs. In this respect, following a review of departmental financial management systems completed in 1994, it was decided to introduce some important aspects of accrual accounting into the Appropriation Accounts (the accounting for pension costs remained unchanged).

5.4.8 In 1995-96, a pilot project involving the introduction of a comprehensive system of accrual accounting was carried out by the Department of Transport, Energy and Communications (now Department of Public Enterprise). The project involved the production of financial statements with accompanying notes and conforming as closely as possible to Statements of Standard Accounting Practice (SSAPs)[42] and Financial Reporting Standards (FRSs) as issued by the Accounting Standards Board at that time. Fundamentally, with some exceptions, the accounting policies which were adopted were no different in most respects to those adopted by public limited companies. The Department produced financial statements for 1995 and 1996 according to the new accounting policies.

5.4.9 Accounting for pension costs was a key aspect of the new system. The project noted that the pension scheme applying to civil servants employed by the Department was unfunded and that actual pension costs arising from the scheme were the responsibility of, and paid for by, the Department of Finance on a pay-as-you-go basis. While the Department of Transport, Energy and Communications did not incur pension costs and was not responsible for their actual payment, it was responsible for the staff that generated these costs. Accordingly, it was considered important, in calculating the full staff costs of the Department, to include a figure for pension liability.[43]

5.4.10 Thus, a notional charge for the accruing cost of pensions was recorded in the Department's Operational Statement. The charge was based on an actuarial valuation of the pension liability for pensionable service of the existing staff of the Department accrued over the year, calculated at 20.2% of the total salary cost. The estimated unfunded pension liability was not included in the financial statements, but was disclosed separately as a note to the financial statements.

5.4.11 In 1996, the Government established a Working Group on Financial Management with the objective of mapping out a comprehensive set of proposals for radically overhauling existing financial procedures. This was in response to the critique of existing financial management and controls in *Delivering Better Government* which attributed the problems in the management of

[42] Financial Reporting Exposure Draft (FRED) 20 proposes substantial change from the existing SSAP 24, *Accounting for Pension Costs*. The main changes are: (i) in measuring pension scheme assets, a move from using an actuarial basis to using market values, (ii) a move from using the expected rate of return on the scheme assets to a rate that reflects the characteristics of the liabilities, (iii) a move from gradual recognition of actuarial gains and losses in the profit and loss account to immediate recognition in the statement of total recognised gains and losses (iv) and as a consequence of (iii), the balance sheet to show a pension asset or liability equal to the recoverable surplus or deficit in the scheme.

[43] Department of Transport, Energy and Communications, *Introduction of Accruals Based Accounting Project Report* (1996), p. 44.

the public finances to inadequate systems, characterised as overcentralised, short-term in orientation and more concerned with control of inputs than with efficient and effective delivery of outputs.

5.4.12 The report of the Working Group, *Financial Management in a Reformed Public Service* (1999), was accepted by the Government. The Report made recommendations under a series of headings — multi-annual budgeting, delegation of financial authority, administrative budgets, and the development of a generic model for an enhanced financial management system based on an accrual accounting approach.[44]

5.4.13 The Commission considers that full inclusion of pension costs within the new financial management systems being developed — and, in particular, the introduction of an accruals-based approach to accounting for pensions — would bring a much-needed transparency into this largely unreported part of government costs and liabilities. The Commission's further deliberations and recommendations in this regard are set out in Chapter 24.

5.5 Conclusions

5.5.1 Financing and accounting are important elements in current public service pension arrangements. The Commission is conscious of developments which are already underway, including the pre-funding of part of future Social Welfare and public service pension costs, and the modernisation of government financial systems. Against this backdrop, the Commission's objectives in relation to the financial accounting for public service pensions are as follows:

- securing the long-term financial base for public service pension schemes;
- ensuring that there is an acknowledgement of the real cost of existing pension provision on an ongoing basis, i.e. ensuring transparency of pension costs; and
- creating an awareness and understanding of the medium- to long-term effects of additional recruitment, pension improvements, early retirement packages, etc.

5.5.2 We believe that the introduction of an accruals-based approach to accounting for public service pensions, broadly along private sector lines, would offer a number of advantages. From the perspective of cost discipline, an accruals approach would ensure that the real cost of pensions would be charged to the accounts of the department or organisation which had primary responsibility for the delivery of a particular public service. It would foster an awareness of the medium- to long-term effects of additional recruitment, improvements in pension terms, and of early retirement. In our view, this would enhance the overall management of pensions at a time of escalating costs. In addition, the employer contribution would bring home to employees in a transparent way the true cost and value of a public service pension.

[44] Financial Management Working Group, *Financial Management in a Reformed Public Service: Report of the SMI Working Group on Financial Management to the SMI Implementation Group* (1999).

APPENDIX 5.1

Current arrangements for meeting the cost of public service pensions

1. Civil service

The cost of expenditure on civil service pensions is met from a central Superannuation Vote administered by the Department of Finance. Employee contributions are recorded under the Vote's Appropriations-in-Aid heading.

2. Local authorities

Expenditure on pensions under the LGSS is financed by each local authority and is charged to its programme accounts. Expenditures are financed from a combination of the local authority's resources, which includes grants from the Department of the Environment and Local Government, community and service charges, and employee pension contributions.

3. Health service

Health Boards and certain health corporate bodies come under the aegis of the LGSS and, therefore, like the local authorities, meet the cost of their own pension expenditures on an ongoing basis. Costs are financed by employee contributions — which are retained by the Health Boards — and grants from the Department of Health and Children. The Voluntary Hospitals Superannuation Scheme and the Nominated Health Agencies Superannuation Scheme are financed in a similar way.

4. Teachers' pension schemes

Pension payments in respect of national school teachers are met from the First Level Education Vote of the Department of Education and Science. Employee contributions are recorded under the Vote's Appropriations-in-Aid heading. The Second Level and Further Education Vote of that Department provides for all payments made under the Secondary Teachers' Superannuation Schemes and recoups local authorities for the pension payments they make in respect of teachers and other staff of Vocational Education Committees and Institutes of Technology. Employee contributions are recorded as Appropriations-in-Aid.

5. Universities

A number of the universities operate funded pension schemes from which pensions are paid. The funds are financed from grants made by the Higher Education Authority (HEA). Pension increases are financed separately by the HEA.

6. Defence Forces

Pensions for Defence Forces personnel are met centrally from the Army Pensions Vote of the Department of Defence. Employee contributions are credited to Appropriations-in-Aid.

7. Garda Síochána

The payment of pension awards is met centrally by the Garda Síochána Vote of the Department of Justice, Equality and Law Reform. Employee contributions are recorded as Appropriations-in-Aid.

8. Non-commercial state-sponsored bodies

Most of the non-commercial state-sponsored bodies' pension schemes are unfunded. The cost of pensions is met from a combination of employee contributions and grants from the Exchequer. A small number of pension schemes are funded under arrangements broadly similar to those of the universities.

CHAPTER 6

Cost and Actuarial Review of Public Service Pensions

6.1 Introduction

6.1.1 The Commission considered that ascertaining the true cost of public service pension terms and carrying out a detailed projection of future pension costs were key requirements of our terms of reference. Until now, no full actuarial costing of public service pensions had ever been carried out.[45] While it had been generally acknowledged that pension costs would rise significantly over the long-term, there had been no accurate measure of the extent of the increase. The Commission decided that comprehensive actuarial costings were needed to enable the State to better manage its long-term pension commitments, to bring greater transparency into pension costs and to allow proper evaluation of possible changes to benefit terms.

6.1.2 In January 1997, the Commission contracted actuarial consultants, Irish Pensions Trust Actuarial Services Ltd., to undertake an actuarial review of public service pension schemes. The primary objective of the review was to prepare a projection of gross benefit expenditure and contribution income (cashflow projections) for each public service group and for the public service as a whole on the basis of existing pension terms, together with an actuarial valuation of the accrued pension liabilities of the State in respect of all public service pension schemes. A further objective was to estimate the contribution rates (new entrant rates) required to finance the benefits of typical new entrants to the various parts of the public service.

6.1.3 In this Chapter, the Commission presents the findings of the actuarial review.[46] We consider the factors behind the growth in public service pension costs. Finally, we discuss the scale of future pension costs and examine the implications for the State and for the taxpayer.

6.2 Methodology and assumptions used

6.2.1 There are a number of ways to measure the cost of a pension scheme. The easiest is to establish the current pay-as-you-go cost. This is the actual gross expenditure on pensions, death gratuities, and lump sums in any year. Contributions received from scheme members can be offset to give a net cost figure. The main drawback of this method is that it takes no account of future outgoings and contributions. There are other more comprehensive measures which capture the future cost profile:

- *cashflow projections*, which estimate the pensions expenditure and contribution income for future years on the basis of actuarial assumptions;

[45] The results of preliminary work on the costing of public service pension schemes was published in a paper, ''Public Sector Pension Provision'', presented to the Society of Actuaries in Ireland on 23 November 1995 by J. Joyce, J. Reilly and R. Smythe. It is to the credit of the authors of the paper that their projections are very much in line with the conclusions of the Commission's own actuarial review. An earlier partial review of public service pension costs (civil service, Garda Síochána, teachers and Defence Forces) was carried out by the Operations Research Section of the Department of the Public Service (October 1986).

[46] Commission on Public Service Pensions, ''Actuarial Review of Public Service Pensions'' (November 1997), Report prepared by IPT Actuarial Services Ltd.

- the *valuation of accrued liabilities*, which is a measure of the pension benefits accrued — for both pensioners and serving staff — over the period of service up to the date of valuation; and
- *new entrant contribution rates*, which represent the contribution, expressed as a percentage of pensionable remuneration, which would be required to finance the existing pension terms over the period of employment of typical new entrants to the different parts of the public service.

The various measures are reported in the actuarial review as outlined below.

6.2.2 The methodology and most important assumptions used in the actuarial review are detailed in this Section. In carrying out the review, the consultants commented that complete data were not always available across all public service sectors, particularly where information was not held centrally (see also Paragraph 4.3.12). As it was not feasible to collect complete and accurate information in all areas, the consultants formulated data models for the purposes of the report, based on population samples where reasonable levels of data existed. They also made appropriate assumptions in other cases where data items were lacking.

6.2.3 The Commission is satisfied that the projections provide a reasonable indication of the expected development of gross benefit expenditure and contribution income into the future. It should be noted that the projections are sensitive to the assumptions made, which may not be borne out in practice. The most important feature of the projections, therefore, is their overall trend rather than their absolute value in any given year. In summary, although approximations have been made in some areas, we believe the data models used are sufficiently reliable for the purposes of the projections contained in this Report.

6.2.4 In the review, the public service was divided into eight sectors: civil service, local authorities, education, Garda Síochána, prison service, Defence Forces, health, and non-commercial state-sponsored bodies. It was assumed that total numbers of active employees in the public service would remain constant.

Cashflow projections

6.2.5 In estimating gross benefit expenditure and contribution income of the various public service schemes into the future, a number of financial and demographic assumptions were made. Using these assumptions, the probabilities of the various events arising in the future leading to payment of benefits in accordance with the provisions of the particular pension scheme together with the amount of such benefits were calculated.

Accrued liabilities

6.2.6 In establishing the present value of the accrued liability in respect of public service pension schemes, the generally accepted principle that pension benefits should accrue over the period of employment giving rise to these benefits was used. So, for example, the liability in respect of pensions currently in payment (i.e. the present value of all such future pension payments and contingent spouses' and children's benefits) is a fully accrued liability. This is consistent with the funding principle operating in pre-funded schemes that a member's retirement benefits should be fully secured by the time he or she retires. For members currently in employment, the accrued liability was calculated by reference to the service that they had completed to the date at which the valuation took place, in this case January 1997.

6.2.7 The accrued liability value calculated included, amongst other things, an allowance for projected future salary increases over the period to commencement of the benefits.

New entrant contribution rates

6.2.8 Contribution rates were calculated, expressed as the percentage of annual pensionable remuneration (i.e. annual basic salaries plus pensionable allowances, where applicable), that would be required to finance the existing pension terms over the period of employment of typical new entrants to the various public service groups.

6.2.9 These rates could be considered as the typical cost to the State of the various existing pension terms based on the financial and demographic assumptions outlined below. The rates do not necessarily represent the value to specific individuals of the relevant scheme, which depends amongst other things on when they join, what their salary progression is throughout their career, and when they draw benefit.

6.2.10 For the sake of simplicity and comparability, these costs have been expressed in terms of a percentage of annual basic salary plus pensionable allowances, where applicable. The fact that certain benefits are based on total salary and other benefits are based on salary less various offsets in respect of State Social Insurance benefits means that the cost in respect of future new entrants will vary as the relationship between Social Insurance benefits and salaries varies.

Financial assumptions

Price inflation

6.2.11 To avoid having to make an explicit assumption regarding future price inflation, the gross benefit expenditure and contribution projections were prepared in constant (1997) price terms. This meant that any trends emerging in the projections excluded the impact of future price inflation. Thus, if gross benefit expenditure were projected to increase from £10 million currently to £15 million in five years' time, this would not mean that actual expenditure would be £15 million in five years' time — to arrive at the actual figure, an estimate of price inflation for the next five years would have to be added.

Growth in GNP

6.2.12 To be consistent with the 1997 *Actuarial Review of Social Welfare Pensions* undertaken on behalf of the Department of Social, Community and Family Affairs, the following assumptions were used regarding future real growth in GNP:

Table 6.1 Assumptions regarding future real growth in GNP

Period	Excess of growth in GNP over rate of price inflation
1997—2006 inclusive	5% per annum
2007—2016 inclusive	3% per annum
2017—2047 inclusive	2% per annum

The GNP for 1996 was taken as £37 billion (€47 billion).[47]

[47] The most recent estimate for GNP in 1996 is £40.5 billion (€51.4 billion) .It might be noted that real GNP growth in the three-year period 1997—99 was higher than the rate assumed, averaging 8.3% per annum, and that recent estimates project real GNP growth in 2000 of 8.25% (Department of Finance, *Economic Review and Outlook*, 2000). In addition, the longer term assumptions for real GNP growth made by the Department of Finance in the "Report of the Long-Term Issues Group" (forthcoming) are slightly higher than those given in Table 6.1: 2001-2011, 4.3% p.a.; 2011-2021, 3% p.a.; 2021-2036, 2.3% p.a.; 2036-2056, 1.2% p.a. In the medium- to long-term, the effect on the pension cost projections of the differences in initial GNP figure, and in the assumed real rates of growth in GNP, would not be significant.

General salary increases

6.2.13 Based on experience of pay increases in a number of public service grades over the last 15 year and 30 year periods, and views on an appropriate assumption for the future, a future rate of general salary growth of 1.5% per annum in excess of price inflation was assumed. Separate allowance was made for the impact of salary scales and promotional increases.

Salary/promotional scales

6.2.14 The impact of progression along existing salary scales and promotion from one grade to another was estimated by analysing average salaries at each age in the various public service groups and drawing up smoothed salary scales.

Pension increases

6.2.15 Future pension increases were assumed to be at the same rate as general salary increases.

Increases in Social Welfare pensions

6.2.16 Having regard to recent trends, it was assumed that State Social Insurance pensions would grow in the long-term at a rate of 1.0% per annum in excess of price inflation.[48]

Discount rate

6.2.17 This is necessary for the calculation of new entrant rates and to quantify the accrued pension liabilities of the State. For funded pension schemes, the discount rate is the expected future rate of investment return that will be achieved on the pension schemes' assets. For the purposes of providing estimates that would be reasonably consistent with the costings of pension fund liabilities in the private sector, it was assumed that the discount rate would be 4% in excess of price inflation. The effect of a more conservative discount rate of 3.5% in excess of price inflation is shown in the sensitivity analysis below.

Demographic assumptions

Mortality

6.2.18 Standard tables of mortality published by the Institute of Actuaries and the Faculty of Actuaries were used; these tables are used in the valuation of private sector pension schemes.[49] By way of illustration, the life expectancies at age 65 using these tables are 16.5 years for a male, and 20.3 years for a female.

Wthdrawals, ill health retirements

6.2.19 Appropriate tables of withdrawals and ill health retirements were drawn up based on details of employee turnover and ill health retirements in various sectors of the public service.

Age retirements

6.2.20 Assumptions on age retirement patterns were based on the range of ages at which members can retire, information on age retirement patterns in the recent past, where available, and discussions with administrators of the various public service schemes.

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[48] In the four-year period 1997-2000, increases in State Social Insurance pensions were higher than the rate assumed, averaging 3.7% per annum in excess of price inflation. The recommendations of the National Pensions Policy Initiative regarding future rates of increase in Social Welfare pensions, and Government commitments regarding future increases in the period to 2002, are outlined in Paragraphs 16.3.24-16.3.26.

[49] There are no public service mortality tables available.

Other demographic assumptions

6.2.21 Appropriate assumptions were also made in relation to proportions married, the age difference between males and females, childrens' pensions, and numbers of new entrants to each public service group.

6.3 Current (pay-as-you-go) cost of public service pensions

6.3.1 In 1997, the total cost of pensions in the public service was estimated at £636 million (€807 million) made up of pensions, £509 million (€646 million), and gratuities, lump sums, etc., £127 million (€161 million). Total membership of public service pension schemes was estimated at around 203,000 public servants, with an annual payroll of just over £4 billion (€5 billion). There were around 77,200 pensioners in receipt of pension. A detailed breakdown of the 1997 estimate is given in Table 6.2.

Table 6.2 Summary of public service pension scheme numbers, salary costs, pensioner numbers, and annual pension costs (1997)

Sector	Estimated total no. of members	Estimated total annual salary Ir£ (m)	Estimated total no. of pensioners	Estimated total annual pension cost*	
				Ir£ (m)	*Euro (m)*
Civil Service	29,058	513	13,903	87	*110*
Local Authorities	23,993	373	16,017	59	*75*
Education	56,149	1,376	15,022	147	*186*
Garda Síochána	10,746	264	5,492	58	*74*
Prison Officers	2,476	56	252	2	*3*
Defence Forces	13,098	203	11,129	57	*72*
Health Service	59,779	1,141	13,367	85	*108*
NCSS Bodies	7,920	161	2,000	14	*18*
Total	**203,219**	**4,087**	**77,182**	**509**	***646***

* Excluding the cost of gratuities and lump sums.

6.3.2 It should be noted that the total number of active members shown is less than the total number of employees in the public service since not all employees are eligible for pension benefits.[50] Also, the figure for pensionable pay is less than the gross public service pay bill because the latter includes elements of remuneration which are not pensionable.

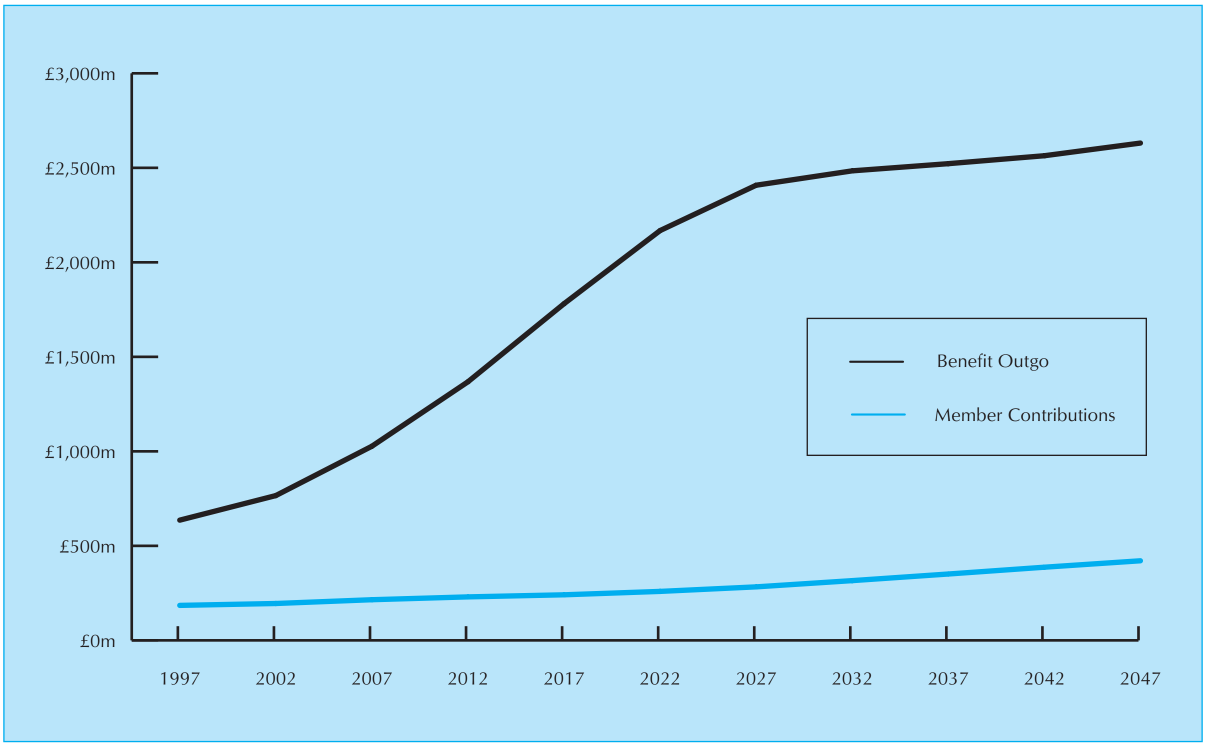
6.4 Development of future cashflows

6.4.1 The methodologies and actuarial assumptions outlined above were adopted for the purposes of estimating the gross benefit expenditure and contribution income of the various public service schemes into the future. The cash flow projections made on this basis are expressed in constant (1997) price terms.

6.4.2 The graph in Table 6.3 sets out the projected development of cashflows for the public service as a whole.

[50] The Department of Finance estimate of public service numbers as at 1 January 1997 was 219,000 ("Analysis of Exchequer Pay and Pensions Bill, 1995-2000", p. 11). This figure includes part-time employees who have been aggregated as wholetime equivalents (for example two part-time employees working half time are deemed to be equivalent to one full-time employee).

Table 6.3 Projected development of cashflows for public service pensions — 1997 to 2047



6.4.3 A more detailed summary of the expenditure projections is contained in the following tables. These are presented in 15 year intervals; projections in five year intervals are contained at Appendix 6.1. Table 6.4 gives gross benefit expenditure projections for the period under review.

Table 6.4 Gross benefit expenditure*

Sector	1997		2012		2027		2042	
	£Ir (m)	*Euro (m)*	£Ir (m)	*Euro (m)*	£Ir (m)	*Euro (m)*	£Ir (m)	*Euro (m)*
Civil Service	96	*122*	164	*209*	378	*480*	369	*469*
Local Authorities	80	*102*	112	*142*	170	*216*	186	*236*
Education	198	*251*	509	*646*	811	*1,030*	820	*1,041*
Garda Síochána	71	*90*	159	*202*	238	*302*	269	*342*
Prison Officers	3	*4*	19	*24*	44	*56*	48	*61*
Defence Forces	65	*82*	119	*151*	165	*210*	193	*245*
Health Service	103	*131*	227	*288*	518	*658*	589	*748*
NCSS Bodies	20	*25*	59	*75*	84	*106*	90	*114*
Total	**636**	***807***	**1,368**	***1,737***	**2,408**	***3,058***	**2,564**	***3,256***

* Including the cost of gratuities and lump sums.

Table 6.5 presents projections of contribution income for the period under review.

Table 6.5 Contribution income

Sector	1997		2012		2027		2042	
	£Ir (m)	*Euro (m)*	£Ir (m)	*Euro (m)*	£Ir (m)	*Euro (m)*	£Ir (m)	*Euro (m)*
Civil Service	7	*9*	14	*18*	29	*37*	52	*66*
Local Authorities	18	*23*	22	*28*	25	*32*	32	*40*
Education	73	*93*	90	*114*	106	*134*	144	*183*
Garda Síochána	9	*11*	13	*16*	21	*27*	28	*36*
Prison Officers	1	*1*	2	*3*	5	*6*	6	*8*
Defence Forces	3	*4*	5	*6*	7	*9*	9	*11*
Health Service	64	*81*	75	*95*	79	*100*	98	*124*
NCSS Bodies	10	*13*	10	*13*	12	*15*	17	*22*
Total	**185**	***235***	**231**	***293***	**284**	***360***	**386**	***490***

6.4.4 Based on the methodology and assumptions set out above, the existing level of gross benefit expenditure for the overall public service is projected, in constant (1997) price terms, to more than double over the next 15 years (i.e. by 2012) and to almost quadruple over the next 30 years (i.e. by 2027).

6.4.5 Thereafter, for the following 20 years, gross benefit expenditure is projected to display limited growth in constant (1997) price terms. This reduction in the rate of growth can be partially attributed to the effects of integration with the State Social Insurance pension for new entrants after 5 April 1995.

6.4.6 The pattern of growth in gross benefit expenditure differs from sector to sector within the overall public service, as shown in Appendix 6.2. In particular, the greater the ratio of active members to existing pensioners, the greater will be the rate of growth for that sector. For example, gross benefit expenditure in the *health service* is set to rise significantly for this reason. In constant (1997) price terms, pension costs are expected to more than double in 15 years' time and to be a multiple of 5 times current levels in 30 years' time. Likewise, in the *education* area, gross benefit expenditure, in constant (1997) price terms, is expected to increase to approximately 2.6 times current levels over the next 15 years, and to more than 4 times current levels in 30 years' time. In the case of the *civil service,* the benefit costs are set to increase, in constant (1997) price terms, to approximately 1.7 times current levels over the next 15 years, and to reach a level of approximately 3.9 times current levels in 30 years' time.

6.4.7 Contributions overall are expected to increase steadily over the next 50 years. In sectors which are already contributory for all benefits (not just spouses' and children's benefits), the growth in member contributions in the early years is diluted by the fact that members who contribute on full salaries will be replaced by new entrants who contribute on integrated salaries for some of their benefits. In sectors which have changed from non-contributory to contributory for post April 1995 new entrants, the total amount of member contributions will increase sharply in the early years. However, salaries for these new entrants have been adjusted to reflect the fact that they will have to pay higher contributions for pension benefits and these salary adjustments will themselves be pensionable (see Paragraph 3.3.57). Hence, the change from non-contributory to contributory status has resulted in some additional cost to the State (in Section 6.8 we discuss the impact upon the State finances as a whole of the change in PRSI status for public servants).

6.4.8 As member contributions will increase at a slower rate than gross benefit expenditure, net benefit expenditure (i.e. the difference between benefit payments and contribution income) is projected to increase at a higher rate than the rate of increase in gross benefit expenditure.

6.5 Present value of accrued liabilities

6.5.1 Based on the methodology and assumptions outlined above, the value in 1997 of the State's accrued liabilities in respect of public service pension schemes was approximately £20 billion (€25.4 billion).[51] The assets of the small number of public service pension funds (held by some universities and non-commercial state-sponsored bodies) amounting to approximately £1 billion (€1.3 billion) should be deducted to arrive at an estimate of the unfunded accrued liabilities of the State.

6.5.2 In Table 6.6, the present value of the accrued liabilities has been broken down between active members and current and preserved pensioners, by sector.

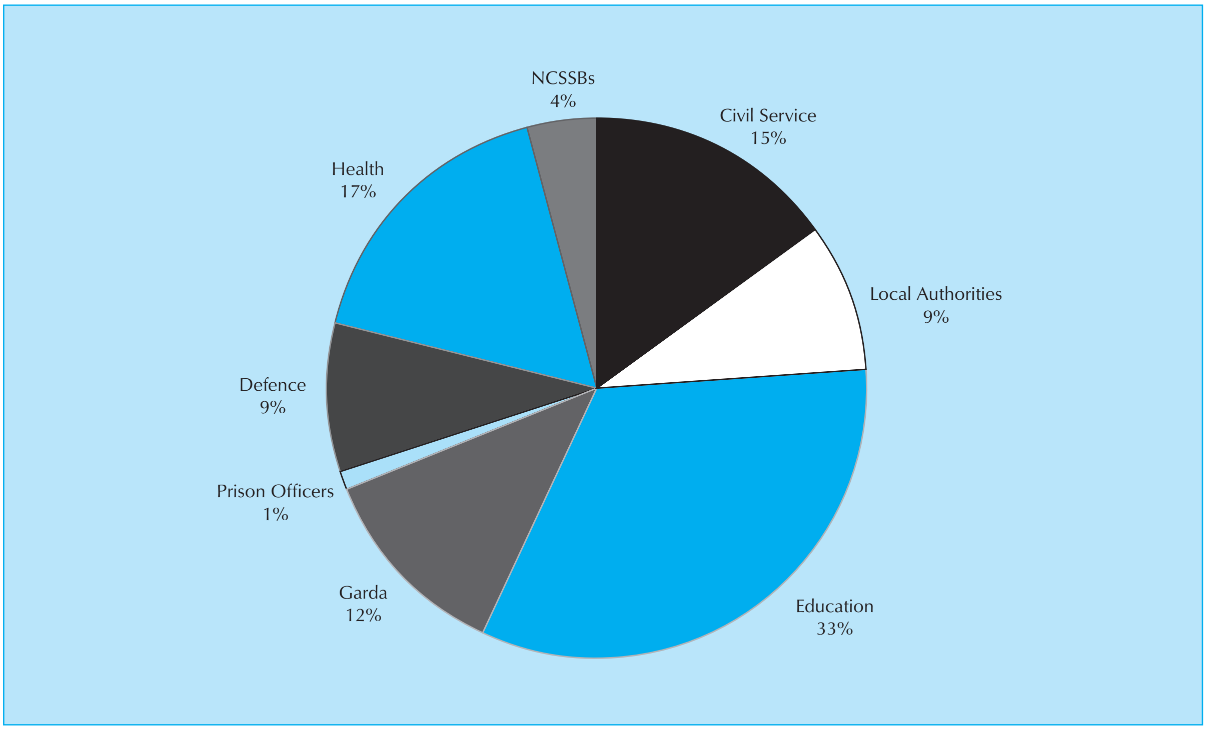
Table 6.6: Present value of accrued liabilities (1997)

Sector	Value of accrued liabilities for active members	Value of accrued liabilities for pensioners and preserved pensioners	Total accrued liability values	
	Ir£ (m)	Ir£ (m)	Ir£ (m)	*Euro (m)*
Civil Service	1,747	1,205	2,952	*3,748*
Local Authorities	1,029	738	1,767	*2,244*
Education	4,696	2,118	6,814	*8,652*
Garda Síochána	1,427	894	2,321	*2,947*
Prison Officers	210	34	244	*310*
Defence Forces	966	848	1,814	*2,303*
Health Service	2,314	1,043	3,357	*4,262*
NCSS Bodies	586	176	762	*968*
Total	**12,975**	**7,056**	**20,031**	***25,434***

The distribution of the value of the accrued liabilities within the public service is illustrated in Table 6.7.

[51] If assets were set aside in a pension fund to meet this liability, a market value adjustment would be made in order to ensure consistency in the way assets and liabilities were valued. Depending on the state of the markets at the time of the fund's establishment, this could mean that the fund assets would have to be somewhat higher than the value of the accrued liabilities.

Table 6.7 Distribution of the value of accrued liabilities within the public service



6.5.3 In addition to the above, the State also has a liability in respect of certain pension costs of Eircom[52] (formerly Telecom Éireann) and a number of commercial state companies, including Coillte Teoranta and the Irish Aviation Authority. The liability relates to pension payments to pensioners and former civil servants arising from service given prior to the establishment of these companies.

6.6 New entrant rates

6.6.1 New entrant rates were calculated for various categories of employment within the eight sectors, based on the methodology outlined at Section 6.2. The rates include the cost of all benefits, i.e. pensions, gratuities, and spouses' and children's benefits, and are inclusive of member contributions. They allow for the fact that new entrants' benefits are integrated with the State Social Insurance pension. For consistency across all sectors, the rates have been expressed as a percentage of the employee's gross salary plus pensionable allowances, ignoring any deduction in respect of the State Social Insurance pension that applies in determining amounts of member contributions.

6.6.2 The new entrant rates for a range of public service grades are given in Table 6.8. As the table shows, new entrant rates vary considerably between sectors, ranging as a percentage of salary plus pensionable allowances from 8% (in the case of male non-established employees in the civil service and local authorities) to 30% (in the case of commissioned officers in the Defence Forces). The new entrant rate applicable to a male or female established civil servant commencing at age 22 at a starting salary of £10,000 per annum would, based on the financial and demographic assumptions made, amount to approximately 16% of salary plus pensionable allowances.

[52] In July 1999, the Minister for Finance announced that part of the proceeds of the privatisation of Telecom Éireann would be used to buy-out the liability in respect of pre-1984 service of Telecom and An Post pensioners and serving staff. An amount of £450 million (€570 million) was subsequently paid to An Post. A final settlement was not agreed with Eircom. It was decided instead to establish a trust into which the Exchequer would pay £800 million (€1,020 million), and that in the event of the trust having insufficient funds to meet the liability in respect of pre-1984 service, the State would meet any residual liability.

Table 6.8 New entrant rates for a range of public service grades (full PRSI class)*

	Category of employment	Assumed starting salary (1997)	Starting age	Male new entrant rate (%)	Female new entrant rate (%)
1	**Civil service**				
	Established	£10,000	22	16	16
	Non-Established	£10,000	25	8	9
	Industrial	£11,000	32	8	9
2	**Local authorities**				
	Officers (without professional added years)	£10,000	22	14	14
	Officers (with professional added years)	£20,000	30	18	18
	Non-established employees	£10,000	25	8	9
	Employees in fire service	£18,000	25	24	23
3	**Education**				
	Primary teachers	£16,500	22	17	16
	Secondary teachers	£17,000	24	16	15
	VECs/RTCs/DIT	£17,000	24	16	15
	Universities	£20,000	30	22	22
4	**Garda Síochána**				
	Garda Síochána	£12,500	22	25	24
5	**Prison Officers**				
	Prison Officer	£16,000	25	21	21
6	**Defence Forces**				
	Commissioned officers	£14,000	20	30	30
	Enlisted personnel	£9,000	18	20	20
7	**Health**				
	Mangement/administration	£10,000	22	14	14
	Consultants	£35,000	35	21	20
	Nurses (general)	£15,000	25	12	11
	Nurses (psychiatric)	£15,000	28	17	16
	Paramedics	£18,000	25	14	13
	Non-officers	£12,000	25	10	10
8	**Non-commercial state-sponsored bodies**				
	Established officer	£10,000	22	16	16

* The new entrant rates include the cost of all benefits, i.e. pensions, gratuities and spouses' and children's benefits, and are inclusive of member contributions.

6.6.3 The rates quoted are for new entrants paying full PRSI to whom integration applies. By way of illustration, the new entrant rate applicable to a male or female new entrant to the civil service (using the same age and salary assumption as above) would amount to approximately 20% of salary plus pensionable allowances if the member's benefits were not integrated with the Social Insurance system.

6.6.4 The degree of variation in the new entrant rates between groups reflects a number of factors:

- the benefit terms and conditions applying to each group. For example, those with earlier retirement ages such as members of the Defence Forces or Prison Officers will have higher relative contribution rates than those on standard terms;

- the promotional salary scale assumed for each group. For example, groups that can expect significant promotional or grade increases during their career will have higher new entrant rates than those for whom more modest increments can be expected;
- the assumed salary level at entry. As benefits are integrated with the State Social Insurance pension, but the new entrant rates are based on un-integrated salaries, the effect is that those on lower salaries at entry have relatively lower new entrant rates;
- the assumed average age at entry. The earlier the age at entry, the longer the period over which costs can be spread, resulting in a lower average contribution rate;
- differences in other actuarial assumptions applying to the various groups, e.g. different rates of withdrawal among different groups (higher among nurses than among civil servants) and different life expectancies (women higher than men).

6.6.5 A further calculation of new entrant rates was carried out to establish the additional cost of benefit scales which offer more favourable pension terms compared with the civil service, i.e. Firefighters/Psychiatric Nurses, primary/secondary teachers, Garda Síochána, Prison Officers.[53] To do this, it was necessary to take the case of an established civil servant, entering at age 22 on a salary of £10,000 per annum, and to apply the same financial and demographic assumptions for a civil servant as in the previous calculations above, except that retirement is assumed to take place at the earliest permitted age under each benefit scale.

6.6.6 On the basis of this methodology, the *additional* cost of each benefit scale compared with the civil service benefit scale was as follows:

• Firefighters/Psychiatric Nurses	48%
• primary/secondary teachers	15%
• Garda Síochána	92%
• Prison Officers	82%

6.6.7 The additional cost of the pension terms of each group may be exaggerated because of the assumption that all civil servants would retire at the earliest available opportunity given more favourable pension and retirement terms. However, the figures do provide some indication of the relative cost of the different benefit scales that currently exist in the public service.

6.7 Sensitivity to variations in financial assumptions

6.7.1 Because of the importance of the financial assumptions in the actuarial review, it was necessary to consider the impact on the results of changes to some of the key assumptions. Accordingly, sensitivity analysis was carried out in relation to variations in general salary increases (and hence pension increases), Social Insurance pension increases and the discount rate used.

Change in general salary increase and Social Insurance pension increases

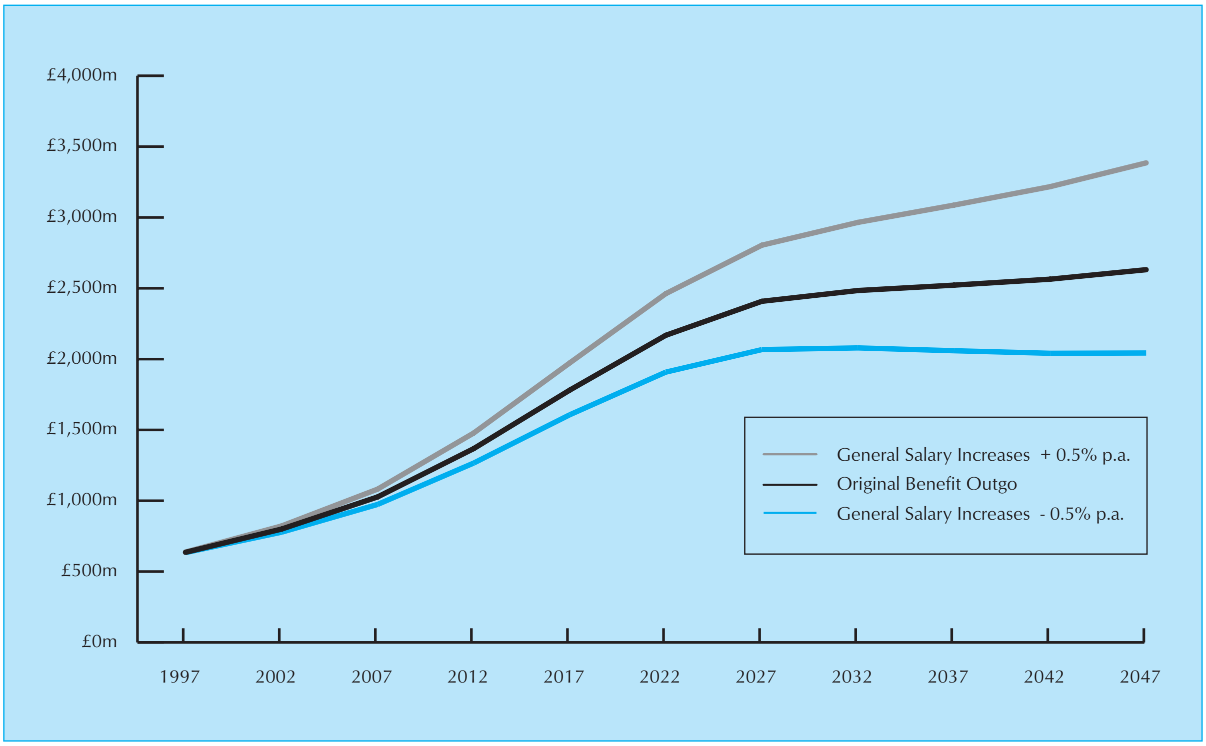
6.7.2 It was decided to examine the impact on projected benefit payments if $\frac{1}{2}$% per annum were added to, or subtracted from, the assumptions regarding the rates of future general salary increase and State Social Insurance pension increases.

[53] The Defence Forces were excluded from this exercise on the grounds that their pension terms and conditions are significantly different from those of other groups.

6.7.3 Adding $\frac{1}{2}$% per annum would lead to revised assumptions that general salary increases would be 2% per annum in excess of price inflation and State Social Insurance pension increases would be 1.5% per annum in excess of price inflation. Subtracting $\frac{1}{2}$% per annum would lead to revised assumptions that general salary increases would be 1% per annum in excess of price inflation and Social Insurance pension increases would be 0.5% per annum in excess of price inflation.

6.7.4 The graph at Table 6.9 outlines the revised benefit payments both before and after these changes.

Table 6.9 Impact of change in assumptions



6.7.5 The total gross benefit expenditure in constant (1997) price terms in 15 years' time would amount to £1.48 billion (€1.88 billion) using the higher rates or £1.27 billion (€1.61 billion) using the lower rates. These figures compare to £1.37 billion (€1.74 billion) on the original basis, representing an increase of 8% or a decrease of 7%, respectively.

6.7.6 The corresponding figures in 30 years' time are £2.8 billion (€3.56 billion) or £2.07 billion (€2.63 billion) versus £2.41 billion (€3.06 billion) on the original basis, representing an increase of 16% or a decrease of 14%, respectively.

Change in discount rate

6.7.7 A change in discount rates would affect the value placed on the accrued liabilities. If the discount rate were changed from 4% per annum to $3\frac{1}{2}$% per annum in excess of price inflation, the revised value of the accrued liabilities would be approximately £21.9 billion (€27.8 billion), which is 9.5% greater than the value determined using a real discount rate of 4% (£20 billion, or €25.4 billion).

6.7.8 The new entrant rates would also be affected by a change in the discount rate. As an example of orders of magnitude, the rate for a male or female established civil servant would increase from 16% to 18.5% of salary plus pensionable allowances if the discount rate were reduced by $\frac{1}{2}$% per annum to $3\frac{1}{2}$% per annum.

6.8 Impact on costs of extension of full PRSI to all public servants

6.8.1 In time, there will be a reduction in the cost of public service occupational pension schemes arising from the implementation of integration on foot of the Government's decision to extend full insurability to all public servants recruited on or after 6 April 1995. As explained in Paragraph 3.3.58, the occupational pension payable under an integrated scheme is lower because it is based on *net* pensionable remuneration (i.e. gross remuneration less the Social Welfare offset). The full impact of this will occur in around 40 years' time, i.e. from around 2035 on, as the majority of post-1995 new entrants reach retirement age.

6.8.2 Public servants paying full PRSI will be entitled to receive Social Insurance pensions in addition to the occupational pension. As the cost of Social Insurance pensions will fall primarily upon the State, the Commission decided to examine whether the long run effect of the change in PRSI status would be to increase or reduce overall pension costs (i.e. combining occupational and Social Insurance pension benefits). This involved consideration of how the combination of changes on introduction of full PRSI status affected the actuarial cost of overall pension benefits to new entrants to the public service.

6.8.3 We summarise the results of our examination in Appendix 6.3. We show that the effect of the change varies by public service group. For a civil servant, the effect of extending full PRSI to new entrants is neutral: the total value of the benefits before the change (i.e. the new entrant rate) is equal to the total value of the benefits after the change.

6.8.4 There is some variation in the results for other sectors of the public service, ranging from a net benefit of 0.2% of career salary in the case of a nurse, to a net loss of 0.7% for a primary teacher, and 1.7% for a Garda.

6.8.5 There are a number of qualifications to these findings as set out in the Appendix.

6.9 Reasons for the increase in public service pension costs

6.9.1 In this Section, we analyse the factors behind the increase in pension costs in the period covered by the actuarial review. Our focus here is upon the cashflow projections reported at Section 6.4.

6.9.2 The first and most important contributing factor is the increase in **public service numbers** which occurred during the 1970s and into the early 1980s. Public service employment levels increased by approximately 35% over the period 1970 to 1983.[54] Recruitment was particularly strong in the period 1977 to 1981. Most public servants who commenced employment in that period will be due to retire from around 2017 onwards, which is when annual pension costs will begin to reach their highest levels. Variation in numbers of public servants recruited has the single greatest impact upon future pension costs.

6.9.3 The impact of the higher recruitment varies from sector to sector, and can be seen in the age profiles of serving employees (see tables in Appendix 6.4). In the public service as a whole, there are large numbers in the younger age cohorts (Table 1). The increased numbers in those age bands is most clear for the civil service (Table 2), and to a lesser degree in the health service (Table 8) and in the education sector (Table 4).

[54] Humphreys, P.C., *Public Service Employment: An Examination of Strategies in Ireland and Other European Countries*, IPA (1983), p. 90.

6.9.4 It should be noted that public service numbers have once again been increasing, although not as rapidly as in the period 1977 to 1981. Over the period 1995 to 2000, there has been an increase of 20,000 in total public service employment.[55] As the actuarial review assumed no change in public service numbers, new recruitment will cause an increase in pension costs in excess of current projections close to the time horizon of the period examined by the Commission.[56]

6.9.5 **Improvements in benefit terms and in pension scheme coverage** is a second factor in the growth in pension costs. The historical development of public service pension terms is outlined in Chapter 3. Changes in terms over the past 30 years which will have most impact on cost include the phased introduction of pension increases in line with pay (from 1969 onwards), the introduction and extension of spouses' and children's pension schemes (from 1968 onwards), and preservation of pension benefits (with effect from 1973). The additional costs arising from the voluntary early retirement schemes of 1987/88 — in the form of added years for pension benefits — are also relevant.

6.9.6 More recent sectoral improvements in benefit terms, e.g. reckoning of past service by secondary teachers at beneficial contribution rates, pensionability of unsocial hours payments in the Gardá Síochána Pension Scheme, will have an impact on costs over the longer run. Apart from improvements in benefit terms, extensions in pension scheme coverage, for example, in relation to temporary and part-time employees, will also add to future costs.

6.9.7 A third factor is the **increase in public service pay** levels relative to price inflation. This impacts on the pension calculation of those retiring in the future as well as the rate of increase of pensions in payment. The actuarial review assumes a future rate of annual general salary growth of 1.5% in excess of price inflation (separate allowances are made for the impact of salary scales and promotional increases). The actual annual rate of increase could in fact be higher: for example, over the period March 1988 to September 1998, public sector earnings increased by an average of 5% per annum,[57] compared with average annual price inflation of 2.6%, giving a differential of 2.4% per annum.

6.9.8 A fourth factor in the growth in pension costs is the **impact of increased life expectancy**. As outlined in Paragraph 7.4.4, it is projected that there will be major improvements in life expectancy in the decades ahead. Projections by the Central Statistics Office indicate an increase of 2.1 years and 2.9 years in the life expectancy of men and women, respectively, at age 65 over the period 1996 to 2026, and these projections may prove conservative. Improved life expectancy will result in an increase in the period over which pensions are paid and so will contribute to increased pension costs.

6.9.9 A number of other factors are also relevant:

- with the ending of the *marriage bar*, there will be a much **greater number of female employees** remaining in service until retirement age than heretofore. As indicated in the actuarial assumptions, females have longer life expectancy than males. While fewer spouses will qualify for spouses' pensions in respect of female public servants compared

[55] Department of Finance, "Analysis of Exchequer Pay and Pensions Bill, 1995–2000" (June 2000), Table XI.
[56] In the short-term, recruitment will reduce costs because additional employee contributions will be paid into pension schemes; however, the long-term position will be an increase in the net cost of public service pensions.
[57] Based on CSO Public Sector Average Earnings Index — see Paragraph 16.5.3.

with male public servants, the overall effect of the increase in the number of females on pension will be an increase in costs;

- the **structure of the public service** has been changing so that there are fewer employees in non-established positions and greater numbers of established public servants. As pension benefits are generally more costly for the latter compared with the former (see new entrant rates in Table 6.8), this change will in time result in increased pension costs;
- as indicated in Section 7.4, there has been a reduction in the **actual age at retirement** in the public service and, it would appear, an increase in numbers retiring early on grounds of ill health; lower retirement ages will mean that pensions have to be paid over a longer period.

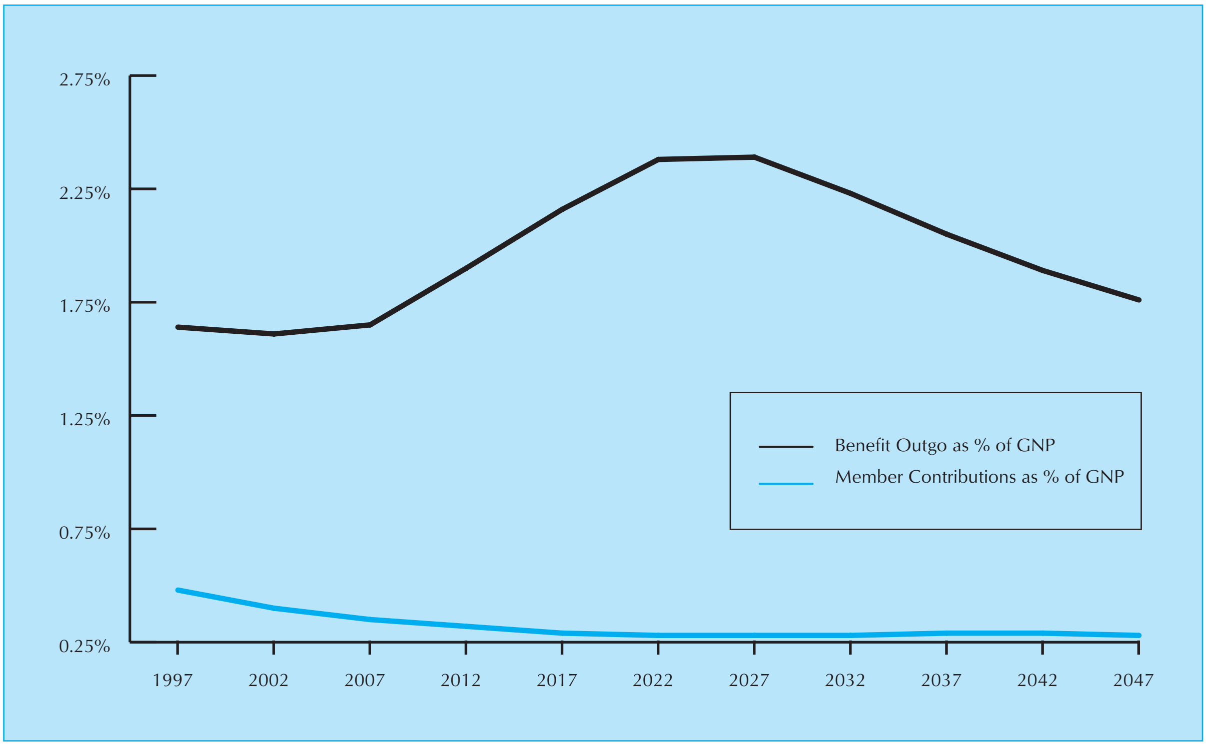
6.10 Affording public service pensions

Estimate of pension costs relative to other measures

6.10.1 Projections of future pension costs relative to other key economic and budgetary variables – such as GNP, public service pay, and tax rates – might not be particularly meaningful since such aggregates would, in any event, be expected to vary in real terms over time in line with the evolution of the economy. Nevertheless, such an approach makes some attempt to place the rise in pension costs into context and to convey a better understanding of the impact which it will have upon the Exchequer.

6.10.2 Table 6.10 takes the projected contribution income and gross benefit expenditure from the actuarial review and expresses them as a percentage of future GNP.

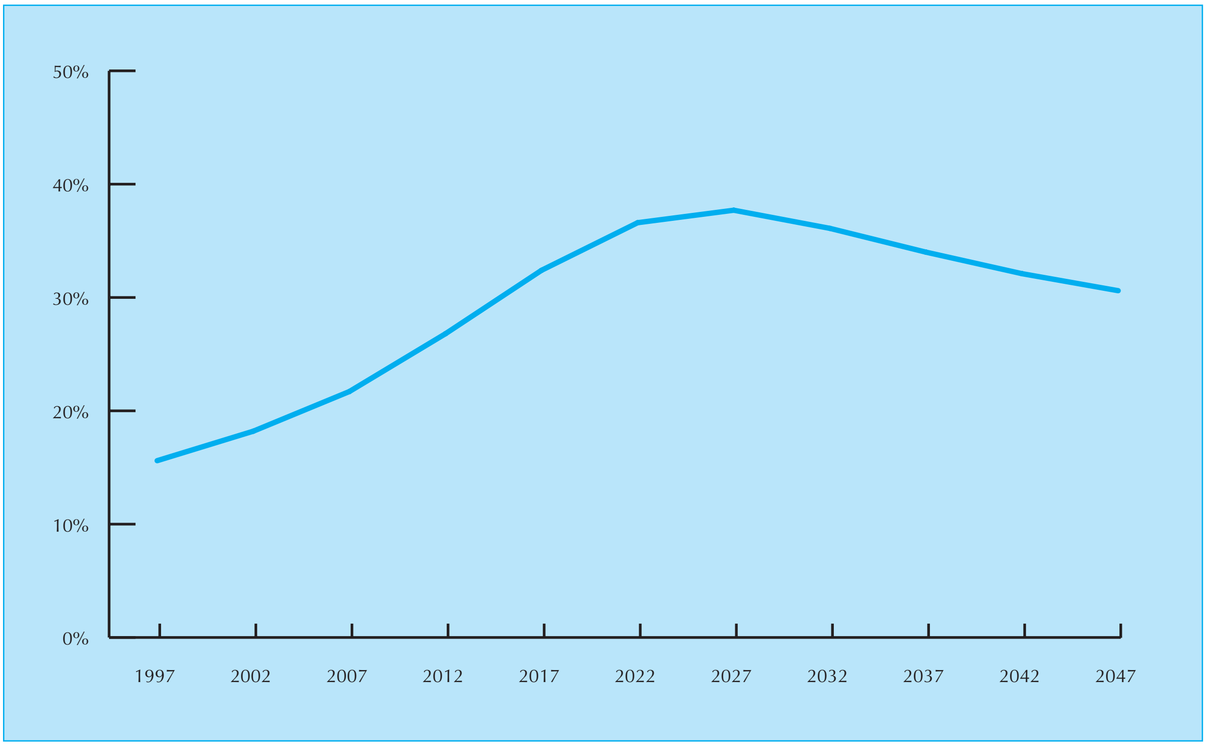
Table 6.10 Future projected benefit expenditure and member contributions as a percentage of GNP



Based on the growth in GNP assumptions used for the purpose of the 1997 *Actuarial Review of Social Welfare Pensions* (see Paragraph 6.2.12), gross benefit expenditure can be expected to remain relatively static as a proportion of GNP for the 10 years to 2007 and then to increase steadily from 1.6% to 2.4% of GNP in approximately 30 years' time. Thereafter, it is projected to return gradually to a level of approximately 1.8% of GNP by the end of the period under review. Member contributions are projected to decrease from approximately 0.5% of GNP to 0.3% of GNP over the period under review.

6.10.3 A second means of assessing the scale of the increase in pension costs is to consider them as a percentage of public service pay over time. This approach makes particularly clear the impact which rising pensioner numbers will have upon the growth in future pension costs. In 1997, gross benefit expenditure represented about 16% of total pensionable pay (which was estimated at £4 billion, i.e. €5 billion). As Table 6.11 illustrates, the expenditure graph rises steadily until gross benefit expenditure reaches a figure of about 38% of pensionable pay in 2027, before falling somewhat to around 30% of pensionable pay in 2047. It is important to note that the projections assume constant public service numbers. Pension costs will represent a smaller percentage of the pay bill over time compared with the projections if public service employment is growing.

Table 6.11 Pension costs as a percentage of pensionable pay



6.10.4 A further means of assessing the scale of future pension costs in current terms is to examine the cost to the Exchequer of a 0.8 per cent of GNP increase in the public service pensions bill from 1.6% of GNP to 2.4% of GNP. According to the Department of Finance, if this increase were to be incurred now, there would be a significant additional charge on the Exchequer which would, if financed through taxation, require an increase of 2p on the standard rate of tax *and* 3p on the top rate of tax.[58]

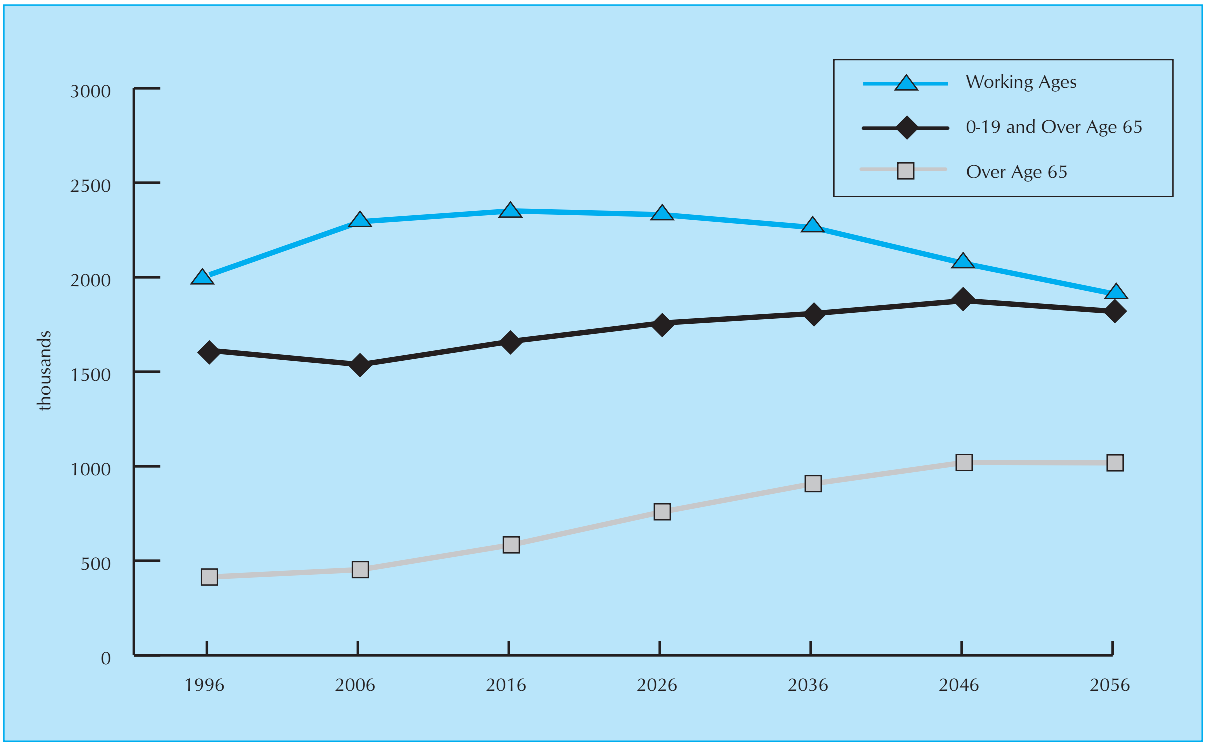
Coping with long-term pension costs

6.10.5 The Commission believes that the growth in public service pension costs should not be considered in isolation. The ability of the State to cope with other long-term demographic trends, including higher Social Welfare and health service costs, must also be considered.

[58] Department of Finance letter of 22 April 1998 responding to the Commission's request for its analysis of the economic implications of the future development of expenditure on public service pensions.

6.10.6 According to demographic projections made in 1997, the number of people in Ireland aged over 65 is expected to increase significantly over the coming decades. Table 6.12 shows in graph form that numbers in that age bracket will rise from 414,000 in 1996 to over 750,000 by the year 2026 and to 1 million by 2046.[59] At the same time, the number of people of working age will rise from 2 million in 1996 to 2.3 million in 2016 and, thereafter, will reduce slowly to 1.9 million in 2056. The table also indicates, however, that the overall dependency level (i.e. the combination of those aged 0-19 and those over 65) will rise more slowly than the old age dependency level, from 1.6 million in 1996 to just over 1.8 million in 2056.

Table 6.12 Projection of future population



Source: Actuarial Review of Social Welfare Pensions, 1997

6.10.7 The increase in the old age dependency level is expected to occur at a time of reducing long-term rates of economic growth, resulting from the eventual fall in the working age population.

6.10.8 It is difficult to gauge the ability of the State in future decades to meet the additional costs attributable to increased public service and Social Welfare pensions and of higher expenditure on health care. Projected economic growth over the next thirty years should help to finance the increased costs. Based on certain assumptions, the Department of Finance estimated in December 1998 that an Exchequer Surplus would be maintained for about 30 years after which time a deficit would emerge which would increase to 2.3% of GNP by 2050.[60] While long-term economic forecasting is an inexact science, these figures would seem to indicate that the necessary revenue will exist into the future to meet ongoing pension and health-care expenditures.

6.10.9 However, the pressures of long-term ageing will come to bear at a time when the dynamics of the demographic structure start to operate in such a way as to significantly reduce Ireland's growth potential. There is a real prospect that the country would be faced with a declining labour force, one that would be asked to shoulder an ever greater dependency level as the century progresses.

[59] The population projections in Table 6.12 are broadly in line with those contained in the more recent *CSO Population and Labour Force Projections 2001-2031* (July 1999).

[60] Department of Finance, "Report of the Long-Term Issues Group" (1998).

6.10.10 The Budget Strategy for Ageing Group of the Department of Finance has attempted to estimate the extra cost which ageing will impose on the Exchequer over 1999 expenditure levels. The Report of the Group concludes that over the next decade *ageing* will require a rise in Exchequer non-capital supply services outlays by 1% of GNP. Ageing costs will rise most rapidly over the following two decades, exceeding 5% of GNP by 2030. By 2056, according to the Group, maintaining Social Welfare and public service pensions in line with earnings for the increased numbers of elderly, and providing them with standard health services, is expected to cost the Exchequer 7% of GNP more than in 1999.

6.10.11 The tight fiscal constraints to which Ireland will be subject in the future are of particular importance in appraising the effect of higher pension and health-care costs. The economic policy environment will be one in which fiscal policy will assume a more important role in macroeconomic policy management. In the medium- and longer-term, apart from dealing with the consequences of demographic ageing, there will be numerous (and conflicting) demands on public resources, such as the need for continuing high investment in infrastructure to facilitate future growth, and the requirement for continuing high levels of investment in manpower development.

6.10.12 The Commission considers that the highest priority for the State is to be afforded the requirement of fiscal flexibility, i.e. ensuring that there is sufficient room for manoeuvre in the conduct of fiscal policy in line with the provisions of the *Stability and Growth Pact*. We would regard the Government's decision to allocate resources to pre-fund part of the long-term cost of public service and Social Welfare pensions as contributing to that objective.

6.11 Conclusions

6.11.1 The Commission devoted considerable time and effort to obtaining these projections on future public service pension costs, particularly from a data gathering perspective. The Commission believes that they provide a reasonable indication of the expected development of gross benefit expenditure and contribution income into the future.

6.11.2 The Commission is satisfied that the assumptions made for the actuarial review are reasonable; the main financial assumptions have been subjected to sensitivity analysis. However, it must be acknowledged that some of the assumptions may not be borne out in practice. In reality, we do not, and cannot, know for sure how the pensions bill will evolve in the future.

6.11.3 But the probability of any significant downsizing of the pensions bill compared with the projections, and hence the likelihood of any significant reduction in the State's liability, due to changed economic or demographic parameters, is small; consequently, concern over the size of the bill is justifiable, particularly when considered in the light of demands for early retirement from a number of public service groups.

6.11.4 In the private sector, such pension liabilities would be supported by an asset portfolio appropriately invested. It is arguable that there is not the same requirement to pre-fund in the public service, as the liabilities of the pension schemes are secured by the Government and its ability to tax. However, this has to be qualified by the fact that at the end of 1997, public service pension liabilities (£20 billion, or €25.4 billion) were equivalent to just under two-thirds of the National Debt (£31 billion, or €39.4 billion), and therefore represent for the State a very substantial additional liability.

6.11.5 The Commission believes that the results of the actuarial review should be used to plan the management of the long-term growth of pension costs, to bring transparency into the incurring of pension liabilities, and to ensure that possible changes to benefit terms do not result in any escalation of costs over current projections. We address these later in this Report.

APPENDIX 6.1

Summary of cashflow amounts in constant (1997) price terms

The following table summarises gross benefit expenditure in 5 year intervals from 1997.

Year	1997	2002	2007	2012	2017	2022	2027	2032	2037	2042	2047
Civil Service	96	109	128	164	230	320	378	398	393	369	346
Local Authorities	80	83	95	112	138	159	170	175	181	186	191
Education	198	267	367	509	655	766	811	807	800	820	858
Garda	71	95	120	159	196	223	238	239	255	269	289
Prison Officers	3	5	10	19	30	39	44	45	46	48	52
Defence	65	79	96	119	139	155	165	172	179	193	207
Health	103	132	167	227	322	426	518	566	588	589	587
NCSS Bodies	20	30	44	59	71	80	84	82	80	90	101
Total Outgo (Ir£m)	**636**	**800**	**1,027**	**1,368**	**1,781**	**2,168**	**2,408**	**2,484**	**2,522**	**2,564**	**2,631**
Total Outgo (Euro)	***807***	***1,016***	***1,304***	***1,737***	***2,261***	***2,753***	***3,058***	***3,154***	***3,202***	***3,256***	***3,341***

The following table summarises contribution income in 5 year intervals from 1997.

Year	1997	2002	2007	2012	2017	2022	2027	2032	2037	2042	2047
Civil Service	7	8	11	14	17	22	29	37	45	52	59
Local Authorities	18	19	20	22	22	23	25	27	29	32	35
Education	73	80	86	90	93	98	106	118	131	144	155
Garda	9	10	11	13	15	18	21	24	26	28	30
Prison Officers	1	1	1	2	3	4	5	5	6	6	7
Defence	3	4	4	5	5	6	7	8	9	9	10
Health	64	67	71	75	76	77	79	83	90	98	107
NCSS Bodies	10	10	10	10	10	11	12	14	16	17	18
Total Income (Ir£m)	**185**	**199**	**214**	**231**	**241**	**259**	**284**	**316**	**352**	**386**	**421**
Total Income (Euro)	***235***	***253***	***272***	***293***	***306***	***329***	***360***	***401***	***447***	***490***	***535***

APPENDIX 6.2

Summary of percentage increases in cashflow amounts in constant (1997) price terms

Appendix 6.1 sets out the projected gross benefit expenditure on public service pensions over the next 50 years. The following table converts the figures into percentage increases over the 1997 level.

Year	1997 %	2002 %	2007 %	2012 %	2017 %	2022 %	2027 %	2032 %	2037 %	2042 %	2047 %
Civil Service	0	14	33	71	140	233	294	315	309	284	260
Local Authorities	0	4	19	40	73	99	113	119	126	133	139
Education	0	35	85	157	231	287	310	308	304	314	333
Garda	0	34	69	124	176	214	235	237	259	279	307
Prison Officers	0	67	233	533	900	1200	1367	1400	1433	1500	1633
Defence	0	22	48	83	114	138	154	165	175	197	218
Health	0	28	62	120	213	314	403	450	471	472	470
NCSS Bodies	0	50	120	195	255	300	320	310	300	350	405
Total Outgo	**0**	**26**	**61**	**115**	**180**	**241**	**279**	**291**	**297**	**303**	**314**

Appendix 6.1 sets out the projected contribution income over the next 50 years. The following table converts the figures into percentage increases over the 1997 level.

Year	1997 %	2002 %	2007 %	2012 %	2017 %	2022 %	2027 %	2032 %	2037 %	2042 %	2047 %
Civil Service	0	14	57	100	143	214	314	429	543	643	743
Local Authorities	0	6	11	22	22	28	39	50	61	78	94
Education	0	10	18	23	27	34	45	62	79	97	112
Garda	0	11	22	44	67	100	133	167	189	211	233
Prison Officers	0	38	75	138	238	350	463	538	613	675	725
Defence	0	13	32	52	71	97	123	152	177	200	223
Health	0	5	11	17	19	21	23	30	40	53	67
NCSS Bodies	0	2	2	1	3	10	22	40	61	73	80
Total Outgo	**0**	**8**	**16**	**25**	**31**	**40**	**53**	**71**	**90**	**109**	**128**

APPENDIX 6.3

Comparison of the value of pension terms of public servants in full and modified PRSI class (in 1998)

1. The Commission analysed the impact on the overall value of pension entitlements arising from the April 1995 change in PRSI status for new entrants to the public service. We also assessed the effect of the April 1995 change on the overall pension costs of the State (including the additional cost to the Social Insurance system). We obtained actuarial advice in carrying out this exercise.[61] We report our findings below. *The Social Insurance contribution rates, thresholds, and benefit levels used are those applying as at October 1998.*

2. The changes to pension terms, and uprating of salary scales in certain cases, following introduction of full PRSI for all public servants, are set out in Paragraph 3.3.57 of the Report.

3. For areas of the public service where the main pension scheme was already contributory, the positive factors following the change, insofar as the individual is concerned, are:

(i) if the post-April 1995 new entrant is entitled to additions to the State Social Insurance pension in respect of qualified adult and child dependants (£2,803 per annum and £790 per annum, respectively), he or she will be better off compared with the pre-April 1995 new entrant;

(ii) if the post-April 1995 new entrant has less than 40 years' service and qualifies for maximum State Social Insurance pension, he or she will also be better off;

(iii) there is an entitlement to a range of non-pension Social Welfare benefits, e.g. death grant, treatment benefit, certain free schemes.

4. The negative factors from the point of view of the individual are:

(i) the post-April 1995 new entrant must pay full PRSI — which is actually lower than the modified rate by 0.9% for annual earnings between £1,040 and £4,160, but higher by 3.6% for annual earnings between £4,160 and £22,300;

(ii) the pre-April 1995 entrant will have his or her full pension increased in line with salary, while the post-April 1995 entrant will receive rates of increase on the State Social Insurance pension element of his or her total pension which, historically, has been lower than the rate of pay increase;

(iii) for the post-April 1995 entrant, a deduction of once the rate of Old Age (Contributory) Pension (OACP) is made when calculating spouses' and children's pensions. For the pre-April 1995 entrant, survivors' contributory pensions are already payable and no deduction is made when calculating the occupational benefits;

(iv) both the pre- and post-April 1995 entrant could leave at a future date and build up sufficient PRSI contributions with other employers to be eligible for a Social Insurance

[61] Commission on Public Service Pensions, "Supplementary Actuarial Information" (October 1998), Report prepared by IPT Actuarial Services Ltd.

pension. However, the post-April 1995 entrant will have the deferred public service pension reduced to allow for integration.

5. In areas of the public service where a contributory pension scheme was introduced following the introduction of full PRSI, the new entrant had two further beneficial effects:

(i) the increase of 1/19th to the individual's salary (lower for members of the Garda Síochána) was greater than the increase in the member contribution required;

(ii) additional pension scheme benefits will be derived from the increased salary.

6. Table 1 sets out the impact on the overall benefit package of a typical new entrant before and after the 1995 change. In the comparison, a value has been placed on the full range of benefits provided. In the case of the public servant in modified PRSI class, the full cost falls onto the occupational pension scheme alone. For the public servant paying full PRSI, the cost of the pensions package falls onto the occupational pension scheme as well as onto the Social Insurance Fund. The table also takes account of the member's pension contributions, as well as the additional PRSI contribution being made by the post-April 1995 new entrant.

7. When comparing the benefit packages of new entrants before and after the changes, it is important to ensure that the position is examined consistently, i.e. either gross or net of tax. Examining the position net of tax would be complicated by the fact that it would require assumptions to be made about the development of the taxation system into the distant future. Consequently, only the gross position has been considered.

8. While individuals will get tax relief on any additional pension contributions they pay, they do not get tax relief on their additional PRSI contributions. It could be argued therefore that some adjustment should be made to the value placed on additional PRSI contributions in the table below. However, such an adjustment would vary according to each individual's tax circumstances, which are dependent on salary progression, marital status, etc. Such an adjustment has not been incorporated, but account should be taken of this when considering the results of this exercise.

9. Taking the example of the civil servant, the table shows that for the pre-April 1995 new entrant the value of the occupational pension, net of member contributions, is 17.8% of career salary. For the post-April 1995 new entrant, taking account of occupational pension, Social Insurance pension benefits, the extra 1/19th of salary, and netting off member contributions and additional PRSI contributions, the table shows that the net value of his or her benefits is also 17.8% of career salary. Thus, there is no gain or loss following the change.

Table 1: Impact of integration on new entrant rates: benefit/cost as percentage of remuneration

	Civil servant (%)	Primary teacher (%)	Nurse (%)	Garda (%)
Before April 1995 change				
(1) Occupational benefits	19.2	19.6	15.7	27.3
(2) Member contributions	–1.4	–6.5	–6.5	–3.2
Net value of occupational benefits	17.8	13.1	9.2	24.1
After April 1995 change				
(1) Occupational benefits	16.4	16.4	11.5	24.5
(2) Contributory old age and invalidity pensions	3.9	3.6	5.5	3.2
(3) Extra 1/19th salary (lower for Gardaí)	5.0	0.0	0.0	2.5
(4) Member contributions	–5.1	–5.3	–5.0	–5.4
(5) Additional PRSI contributions	–2.4	–2.3	–2.6	–2.4
Net value of occupational benefits and additional Social Welfare pensions	17.8	12.4	9.4	22.4
Gain to individual	+0.0	–0.7	+0.2	–1.7

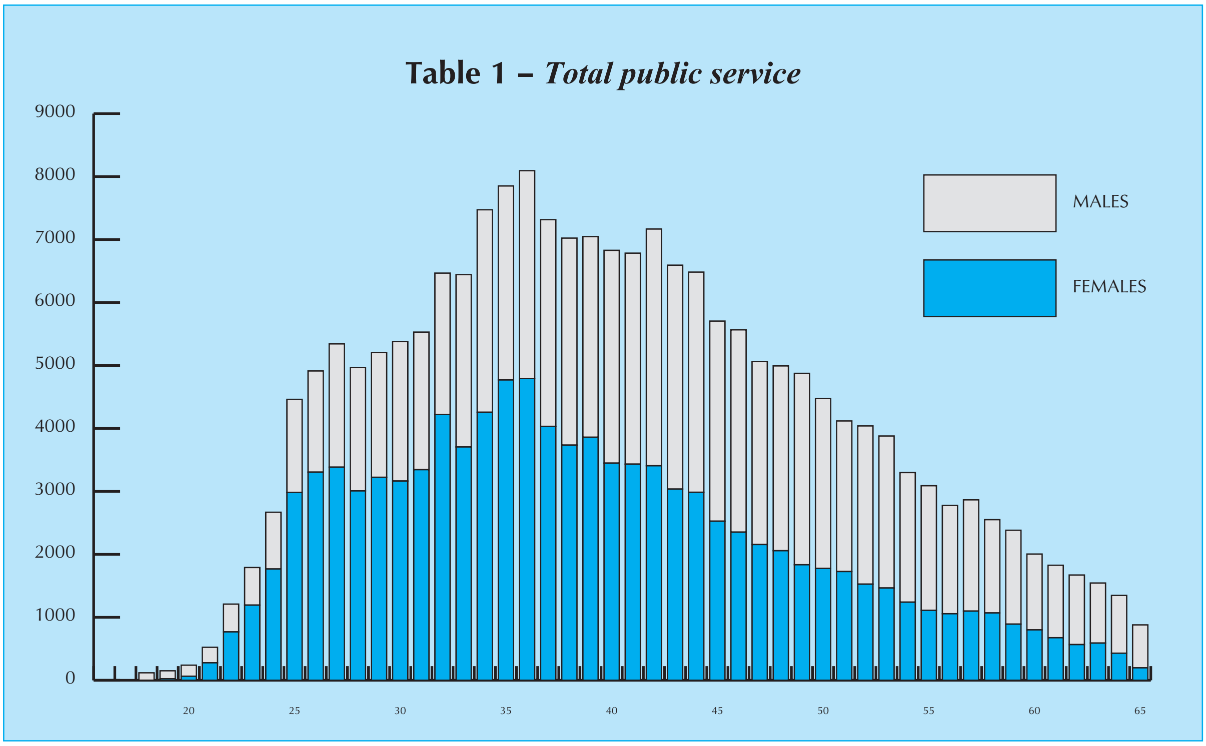
10. The comparable gain/loss figures for teachers, nurses and Gardaí are –0.7%, +0.2%, and –1.7%, respectively. In the case of the Garda Síochána, it seems clear that post-April 1995 new entrants will be at a disadvantage compared with pre-April 1995 new entrants. For example, a post-April 1995 Garda who retires and takes up insurable employment will not be entitled to payment of supplementary pension (which might be equivalent to the amount of OACP); the pre-April 1995 entrant, on the other hand, who takes up employment subsequent to retirement will continue to receive his or her full occupational pension.

11. The figures set out above were subject to some sensitivity analysis. For example, if the rate of increase of Social Insurance pension is more closely in line with earnings increases, i.e. 1.5% ahead of price inflation, rather than 1.0% as is assumed, the gain to the post-April 1995 civil service new entrant changes from 0.0% to 0.3%. Also, if a lower rate of withdrawals is assumed from the civil service into the private sector, the gain to the individual could rise by a further 0.2%.

12. It is difficult to draw absolute conclusions about the impact of integration from the results above. It must be noted, for example, that a number of non-pension Social Welfare entitlements, to which post-April 1995 entrants are entitled, are not valued in the analysis. Also, the fact that individuals do not get tax relief on their additional PRSI contributions has not been taken into account. Finally, the basis for increase in Social Insurance pensions is a matter for some debate (see Paragraphs 16.3.24-16.3.26 of the Report). All of these factors impact on the assessment that can be made.

APPENDIX 6.4

Membership profile of the total public service sector by current age (1997)



Membership profile of each public service sector by current age (1997)

Table 2 – *Civil Service*

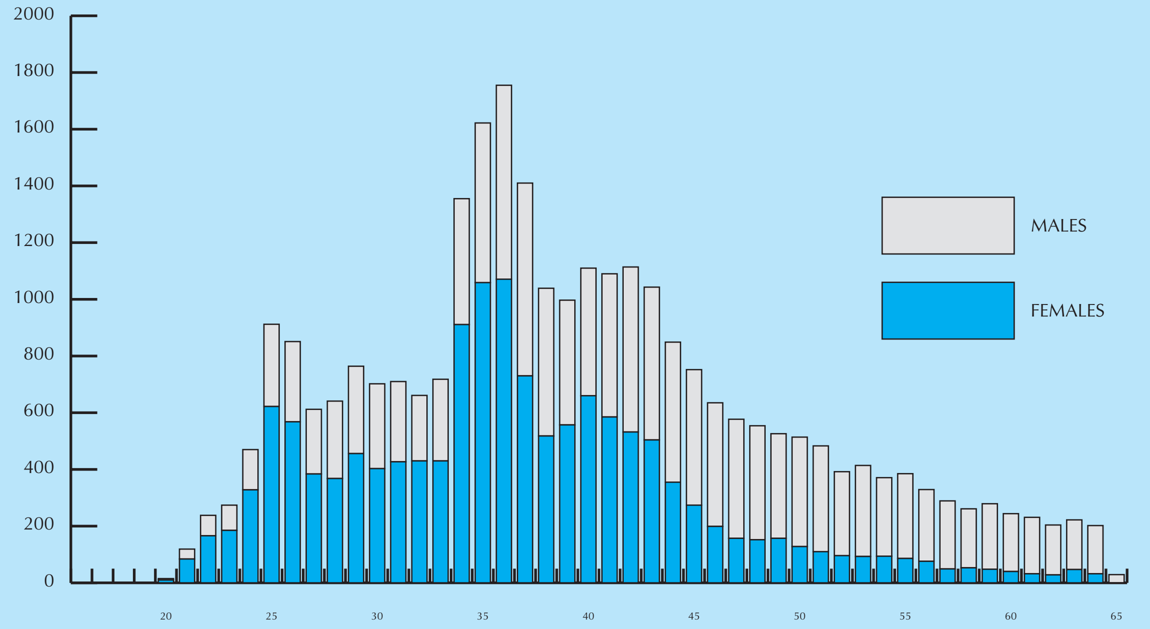


Table 3 – *Local Authorities*

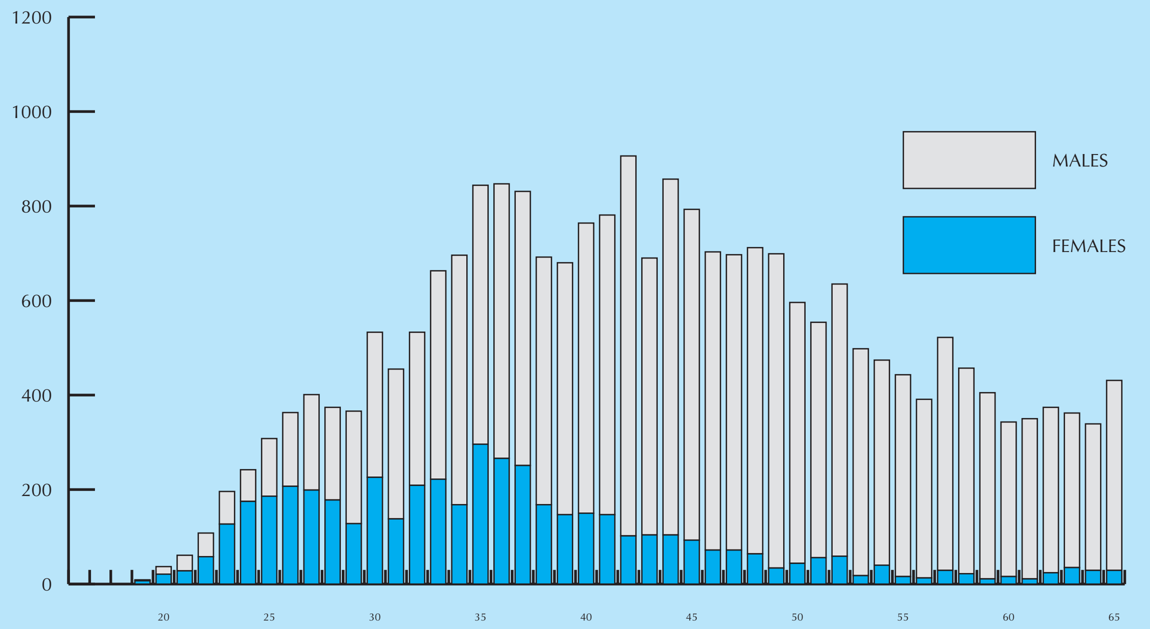


Table 4 – *Education*

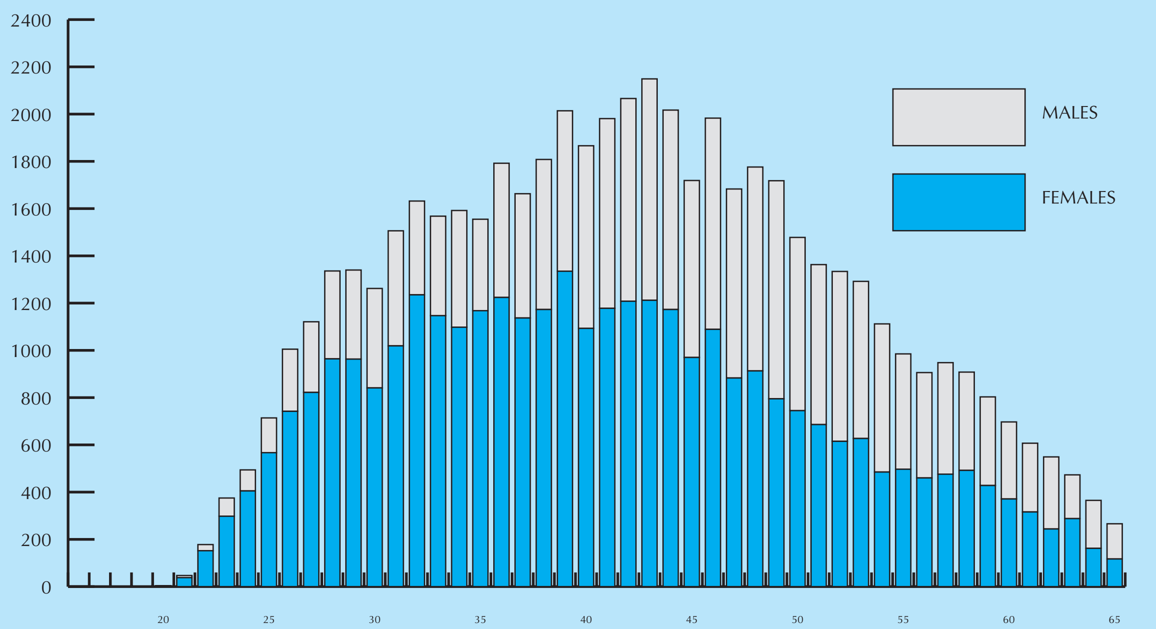


Table 5 – *Garda Síochána*

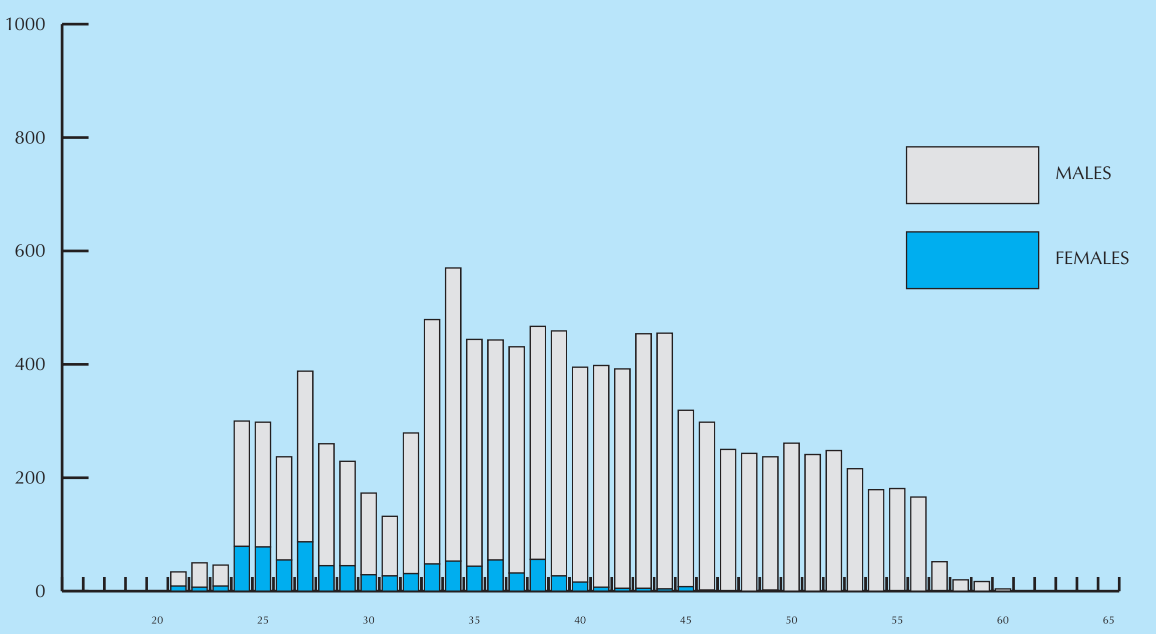


Table 6 - Prison Officers

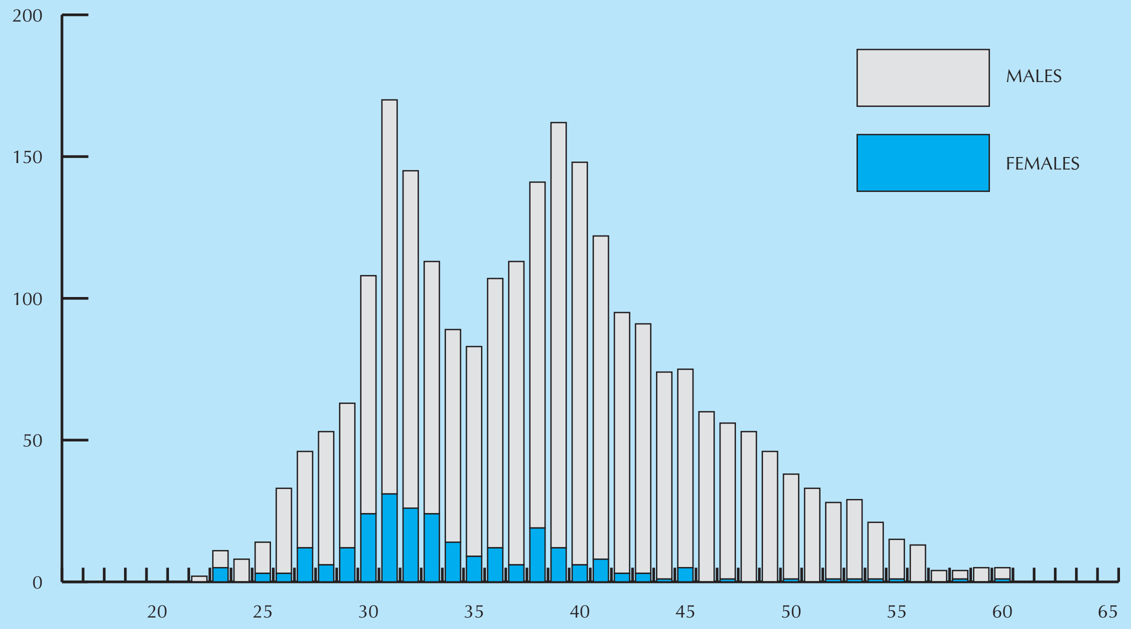
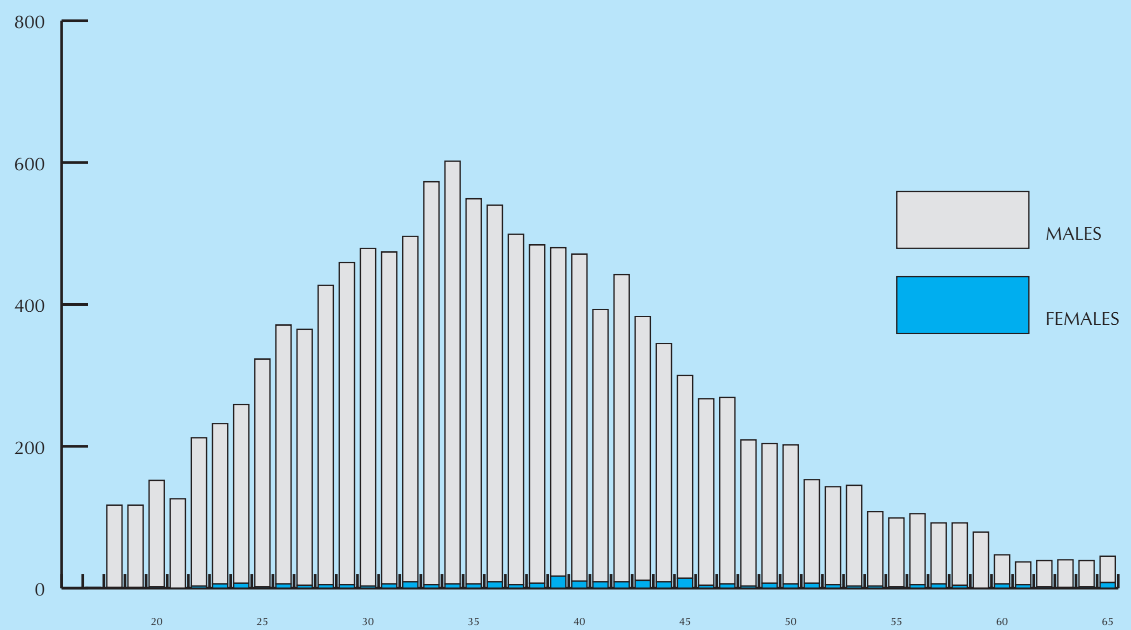


Table 7 – *Defence Forces*



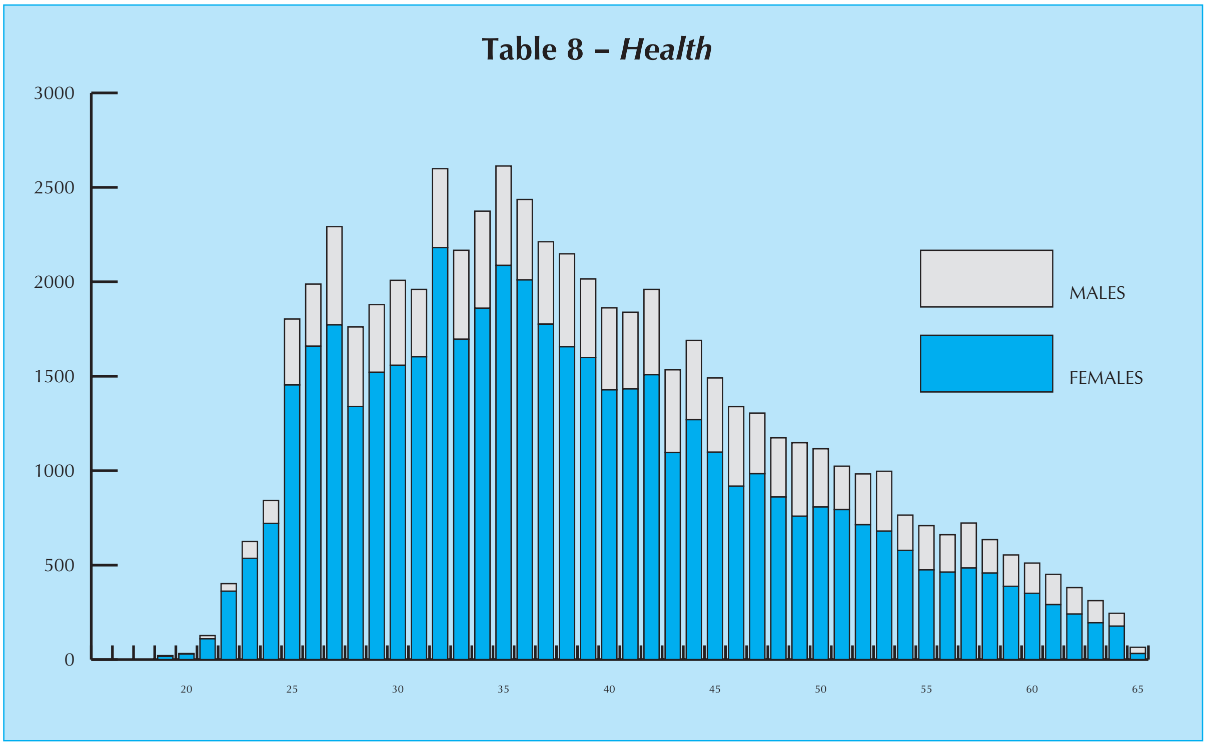


Table 8 – *Health*
3000
2500
2000
1500
1000
500
0
20
25
30
35
40
45
50
55
60
65
MALES
FEMALES

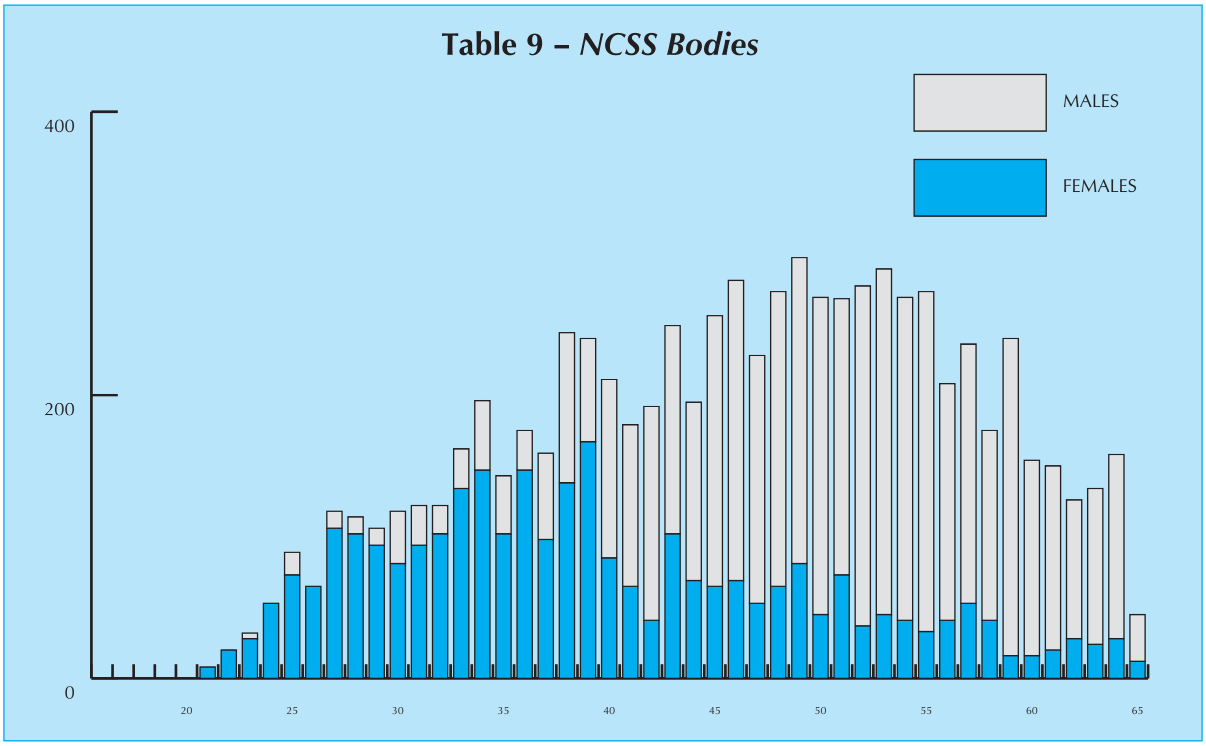


Table 9 – *NCSS Bodies*
400
200
0
20
25
30
35
40
45
50
55
60
65
MALES
FEMALES

Table 10 – *All Teachers*

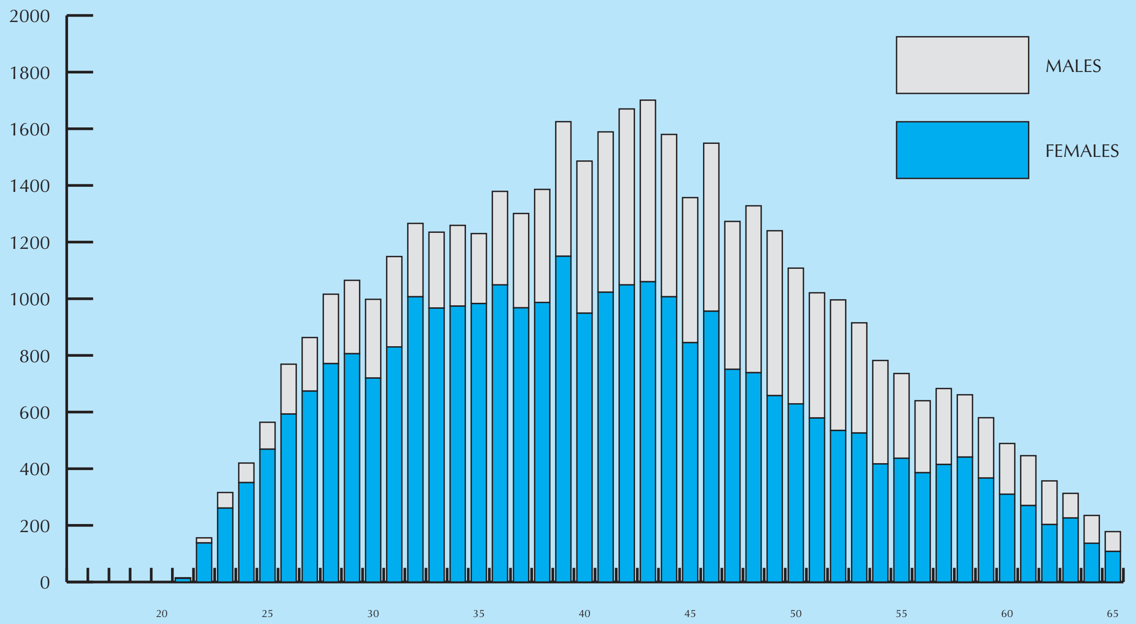


Table 11 – *Nurses*

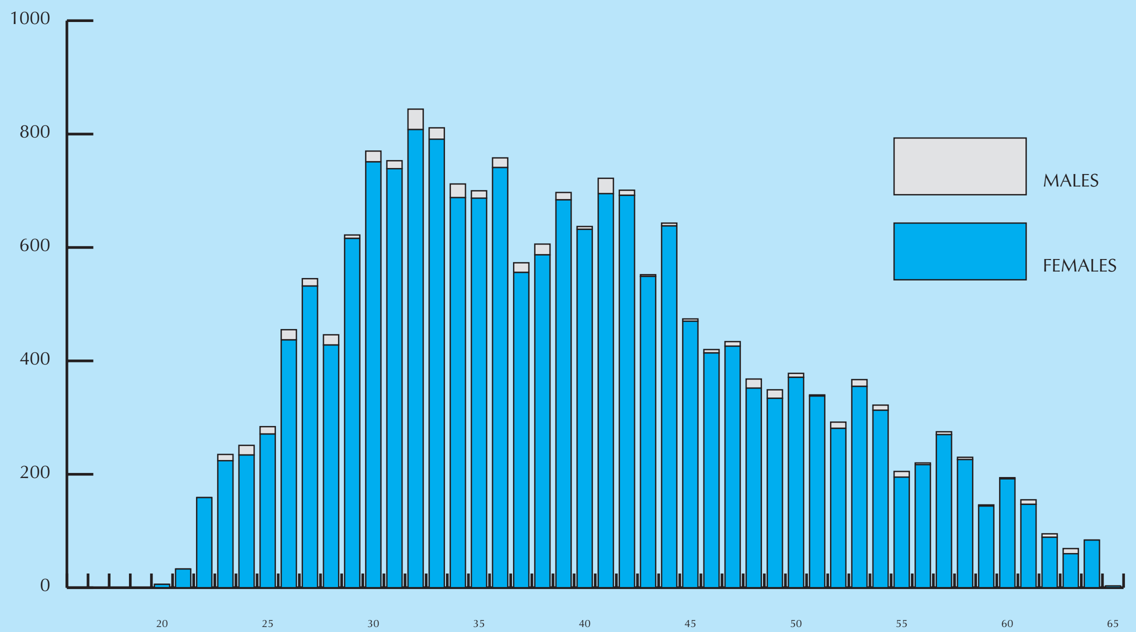
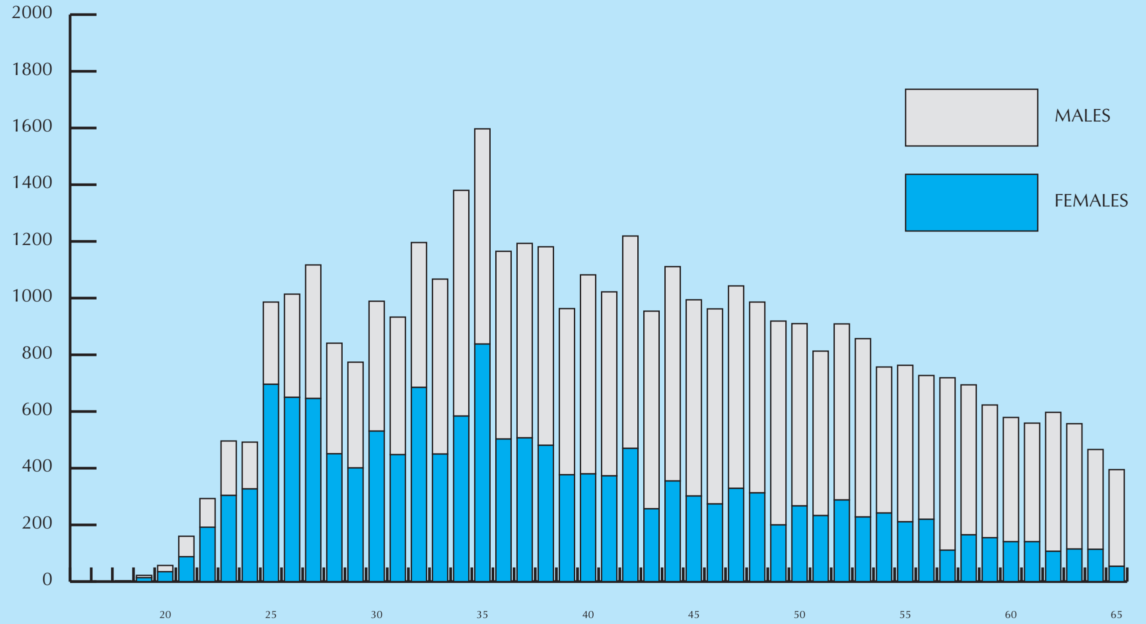


Table 12 – *Pre-95 Co-ordinated*



CHAPTER 7

Changes in Operational Requirements, Working Environment, and Conditions of Employment of Public Servants

7.1 Introduction

7.1.1 As we have shown in Chapter 3, the basic principles of public service pension arrangements were laid down in the nineteenth century. Pension terms were designed to accommodate the generally accepted view of public service employment at that time. Employment was *for life*, commenced usually well before age 20, and the employee worked within the one area of the service until retirement at about age 60. At this stage, the employee was considered unable to continue working because of old age or infirmity, and a reduced maintenance-type payment, or pension, was made by the employer.

7.1.2 In assessing the continued appropriateness of pension terms in today's environment, the Commission believes that account must be taken of changes in the operational requirements, working environment, and conditions of employment of public servants. The process of modernising the public service must also be considered. If the public service is to undergo a process of significant change in the future, corresponding reform of pension arrangements may be necessary. Pension structures interact closely with the labour market and vice versa. To some extent, pension schemes can reinforce loyalty to a particular career path. Also, the career path and its strains and competitive stresses help determine attitudes to certain aspects of pension schemes (early retirement, for example). The Commission considers that pension terms should not be a barrier to change and that they should be capable of adapting to the developing work situation.

7.1.3 Changes in the wider social and economic environment will impact upon the public service and must also be considered when reviewing the conditions of employment of public servants. The relevant factors include improvements in life expectancy, greater flexibility in the work environment, and the consequences of what might be called the quickening pace of life generally.

7.1.4 In this Chapter, the Commission analyses the changes in the working environment and conditions of employment of public servants, as well as the changes in the operational requirements of the public service. We do this under four general headings. It will be clear in a work such as this that it is not possible to examine each area of the public service in detail. However, particular examples and references are made where it is considered helpful to do so. The headings considered are:

- age of entry;
- changing composition of workforce;
- trends in retirement;
- management of performance: implementation of public service change.

7.2 Age of entry

7.2.1 The average age of entry into the public service has been increasing. By way of example, Table 7.1 shows the age of entry to the civil service in recent years.

Table 7.1: Age of entry to the civil service, 1990-97[62]

Year	Under Age 25		Over Age 25		Total		Over Age 30	
	No.	%	No.	%	No.	%	No.	%
1990	634	83	132	17	766	100	94	12
1991	695	82	149	18	844	100	105	12
1992	378	56	303	44	681	100	184	27
1993	212	52	196	48	408	100	131	32
1994	359	51	350	49	709	100	201	28
1995	614	61	400	39	1,014	100	176	17
1996	205	50	205	50	410	100	101	25
1997	213	43	278	57	491	100	147	30

7.2.2 The table shows that in the early 1990s, around 18% of all new entrants to the civil service were aged 25 and over; in later years, the proportion of new entrants in this age category had increased to around 40-50%. The proportion of new entrants over age 30 had also increased significantly in that period. While equivalent details are not readily available for other parts of the public service, indications are that similar trends towards later ages of entry have been experienced.

7.2.3 The later age of entry is due to a combination of factors:

- phased withdrawal of age limits for entry to the public service (the maximum age of entry to the civil service was increased to age 50 in 1991, and to age 65 in 1995).[63] Many newly appointed female civil servants have worked previously in the civil service, having left on marriage grounds;
- educational attainment — greater numbers are joining the workforce from college or university, rather than direct from school;[64]
- work/travel prior to entry — many new entrants have worked elsewhere, whether in the private sector or in employment abroad, prior to taking up public service appointments. Some may have prior pension entitlements in respect of earlier employments.

7.2.4 It is difficult to draw absolute conclusions on the age of entry for the public service generally based on the civil service data presented, as the wide variation in annual recruitment may have had a distorting effect on the outcome. There is no doubt, however, that the average age of entry is rising and will almost certainly continue to do so in the future, due to factors such as those listed.

[62] For established civil servants still in employment as at 1 January 1998.

[63] Clerical Assistants (CAs) made up the majority of new recruits each year. In 1990, around 37% of CAs entering the service in that year were under age 20, while around 4% were over 25; in 1997, however, only about 4% of all new entrant CAs were under age 20, while 41%, approximately, were over age 25.

[64] This may be reflected in the increase in the age of entry for Executive Officers (EOs); in 1990, for instance, approximately 44% of EO new entrants were under age 20, while about 15% were over age 25; in 1997, only about 2% of EOs were under age 20 on entry, while around 48% were over age 25.

7.2.5 In the past, new entrants to many areas of the public service might have expected to be able to accrue maximum pensionable service by retirement age. Special terms were granted to certain groups which had lower retirement ages for operational reasons in order to allow them the same opportunities to earn maximum pension. Other specialist or professional groups were allowed notional added years on the basis that their occupations required pre-entry educational or training qualifications which meant that they entered service at later ages. The fact that the average age of entry is increasing across all public service grades has, in our view, major implications for these special provisions.

7.3 Changing composition of workforce

7.3.1 Since the ending of the *marriage bar* in mid-1973, greater numbers of female employees have decided to remain in, or to rejoin, the public service. Changes in the form of public service employment offered (e.g. atypical employment), and new work-sharing and career break options introduced for those in service, may be seen partly as a response to this development.

7.3.2 *Delivering Better Government* noted that recruitment to the public service was, in the main, restricted to full-time, career-length established service, whereas the exigencies of the current working environment demanded that a more flexible range of options, such as recruitment on a temporary or part-time basis, be available to management. Under the Strategic Management Initiative (see Section 7.5 below), considerable importance is attached to securing greater flexibility in the use of atypical recruitment, such as recruitment on a temporary or part-time basis.[65]

Atypical employment

7.3.3 The development of atypical employment — part-time and temporary working — has enabled many public servants, particularly women, to combine working with family commitments. The introduction of term time (see Paragraph 7.3.12) is also relevant. New developments are ongoing, for example, the proposal in nursing to establish a grade of permanent part-time nurse, and the replacement of job-sharing with a more flexible system of work-sharing in the civil service (see Paragraph 7.3.11). It might be noted that under the *Programme for Prosperity and Fairness*, the Government and the Social Partners have agreed that a National Framework for Family-Friendly Policies should be established to support family-friendly policies at the level of the enterprise.

7.3.4 Types of part-time employment in the public service include the following:

- cleaners in government departments and offices;
- part-time second level teachers;
- substitute national teachers;
- temporary nurses;
- traffic wardens;
- home helps with Health Boards;
- personnel employed during the peak season in the Passport Office;
- exam supervisors.

[65] Government of Ireland, *Delivering Better Government: A Programme of Change for the Irish Civil Service*, Second Report to Government of the Co-ordinating Group of Secretaries (1996), p. 40.

7.3.5 Factors such as hours worked per week, duration of employment, seasonality, subsequent employment in permanent positions, etc. vary considerably for part-time posts in different parts of the public service.

7.3.6 There may be as many as 42,000 individuals working part-time in the public service. However, there are difficulties (e.g. seasonal variation, precise definition of part-time employment) in estimating the numbers of personnel involved. We discuss the incidence of part-time employment in the public service at Appendix 7.1.

7.3.7 It is important to acknowledge that part-time workers have for some time constituted a significant part of total public service employment. For example, figures produced in 1983 indicated that the number of part-time workers had remained reasonably constant between 1970 (21,300) and 1983 (22,900), although falling slightly as a percentage of total public service employment.[66]

Job-sharing and career break schemes

7.3.8 Job-sharing and career breaks — introduced in the 1980s — have quickly been recognised as effective facilities to allow employees combine working with family and other commitments. The level of take-up has been high across many areas of the public service, particularly amongst female employees.

7.3.9 In the civil service, there are approximately 2,900 job-sharers (July 1999), of whom 97% are female. A survey in 1996 estimated that in the public service as a whole there were around 8,000 job-sharers, the vast majority of whom were female.[67] Almost certainly, this number has increased over the last number of years.

7.3.10 Almost all job-sharing appears to be on the basis of either split week arrangements or week on/week off. In the past, job-sharing has applied generally to groups in modified PRSI class; part-time working has not normally been available to these groups, with the exception of teaching. On the other hand, part-time working has applied in relation to groups in full PRSI class.

7.3.11 Proposals are currently being finalised to expand the scope of job-sharing in the civil service by introducing a wider range of attendance patterns (thus changing it from a *job-sharing* to a *work-sharing* scheme). The objectives of the scheme are to facilitate employees who wish to combine work and personal responsibilities or choices, to offer an opportunity to employees near to retirement to ease their transition from full-time work to retirement, and to generate additional employment opportunities where possible.

7.3.12 Term time was first introduced into the civil service in 1998. It is designed to provide new flexibility in working arrangements. The scheme provides for the release of staff with young families or dependent relatives for 10-13 weeks in the summer months. Such periods of leave are unpaid and do not reckon for pension purposes.

7.3.13 Career breaks are available in most areas of the public service. There are no public service wide statistics available on take-up rates. In the civil service, there were 1,136 people on career break in 1998, of whom 78% were female.

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[66] Humphreys, P.C., *Public Service Employment, An Examination of Strategies in Ireland and Other European Countries* (IPA, 1983), pp. 88, 89.

[67] Fynes, B., Morrissey, T., Roche, W.K., Whelan, B.J. and Williams, J., *Flexible Working Lives: The Changing Nature of Working Time Arrangements in Ireland* (Oak Tree Press, 1996).

7.3.14 A greater emphasis on the pensionability of part-time working and other forms of atypical employment, as well as increased usage of provisions allowing individual employees to take breaks from full-time employment, have major implications for public service pension arrangements. In addition, pension schemes need to be sufficiently adaptable to cater for further developments which may be expected to occur in the future.

7.4 Trends in retirement

7.4.1 The normal retirement age for most public servants is age 60-65 (teachers have the option to retire from age 55 with 35 years' service). For public servants who have special pension terms for operational reasons,[68] the normal retirement age is generally age 55 to 60, although some groups have the option to retire from age 50 on achieving maximum service.

7.4.2 For some groups, the *actual* average age of retirement may be lower than the minimum age of retirement when account is taken of early retirement on ill health grounds and any other early retirement facility that may be available.

7.4.3 Generally, the normal retirement age for public servants was set during the 1800s and early 1900s. Since then, there have been significant improvements in life expectancy. We consider the improvement in life expectancy below and then analyse trends in retirement both in the wider economy and in the public service in particular.

7.4.4 Since the mid-1800s, there has been a major increase in life expectancy in Ireland, though not as pronounced as in other Western countries. In 1845, life expectancy for a person aged 65 was 10.9 years for a male and 11.5 years for a female.[69] Recent projections carried out by the Central Statistics Office of changes in life expectancy are given in Table 7.2.

Table 7.2: Projected changes in life expectancy of men and women at age 65[70]

Year	Men (years)	Women (years)
1996	13.5	17.3
2006	14.2	18.3
2016	14.9	19.4
2026	15.6	20.2

7.4.5 In the long-term mortality assumptions used for the actuarial projections of public service pension costs (see Paragraph 6.2.18), life expectancies at age 65 were assumed to be 16.5 years for a male and 20.3 years for a female.

7.4.6 Ireland is significantly behind other major economies in terms of life expectancy and the international experience is that life expectancy at older ages can increase quite rapidly with increasing living standards. Given the experience that for many years actual improvements in life expectancy have generally proved to be a lot greater than anticipated, it seems likely that these projected increases in life expectancy will prove conservative.[71]

[68] Garda Síochána, Prison Officers, fire service personnel, and health service personnel registered under the Mental Treatment Act, 1945 (principally Psychiatric Nurses). Defence Force personnel also have special pension terms. Based on 1997 figures, public servants with special terms make up approximately 31,000 out of the total of 203,000 pensionable public servants, i.e. 15%.

[69] Registrar General, *Life Table and Mean Life Table*, 1845.

[70] Reported in The Pensions Board, *Securing Retirement Income* (1998), p. 96.

[71] The Pensions Board, *Securing Retirement Income* (1998), pp. 95-96.

7.4.7 Increasingly, the newer cohorts of aged people have better health and better educational resources than before. In addition, it has been argued that the process of ageing is not necessarily associated with a loss of functional capacity and productivity.[72]

7.4.8 Notwithstanding the improvements in life expectancy, the employment situation in all industrialised countries over the past 30 years has been characterised by an increasingly early exit from the labour market at end of career.[73] In Ireland, there has been a major fall in numbers (particularly males) in employment above age 50.[74] The contributing factors behind this fall include:

- the declining importance of agriculture. Traditionally, owner-occupier farmers have remained active on their farms later than would be the case for employees working in other sectors of the economy;[75]
- a trend towards earlier retirement, some of which has been driven by companies restructuring in circumstances where strong investment returns on pension funds provided the means to pay higher benefits than would be payable on purely voluntary early retirement;
- an increasing interest in early retirement among people generally.

7.4.9 To some degree, these developments reflected the consensus which existed in many countries amongst the State, enterprises, trade unions, and the community. For the State, early retirement schemes were seen in the 1970s and 1980s as a means of reducing youth unemployment, at its height in those decades. For enterprises, early retirement had a two-fold advantage — productivity could be enhanced through modernising the process of production and the firm restructured without the cost and the embarrassment of rising redundancies. For trade unions, it was a coveted prize in the long struggle to lower the retirement age and so leave workers, who often started their working life young and frequently in strenuous jobs, some years of respite in good health. However, from the 1980s on, there have been signs that the consensus is not as solid as it has been, particularly in relation to the intolerable pressures being placed on pension systems.[76]

7.4.10 Studies indicate that the perception of retirement among individuals has been changing.[77] Increasingly, retirement has ceased to be considered a residue and has progressively become a period of life in its own right, a new stage and a fresh departure that can be prepared for and planned. For the individual, the factors leading to the decision to retire early represent a mixture of *pull* and *push* factors:

- recognition with increasing age that life expectancy is shrinking and that one more year at work means one year less to do those things that he or she has always wanted to do but has not been able to because of the demands of employment;

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[72] Kohli, M., Rein, M., Guillemard, A., van Gunsteren, H., ed., *Time for Retirement: Comparative Studies of Early Exit from the Labour Force* (Cambridge University Press, 1991), p. 42. Also: Delsen, L., Reday-Mulvey, G., ed., *Gradual Retirement in the OECD Countries: Macro and Micro Issues and Policies* (Dartmouth, 1996).

[73] OECD, *Maintaining Prosperity in an Ageing Society* (1998).

[74] CSO, Labour Force Survey, 1997, and National Pensions Board (1993), p. 82.

[75] Fahey, T., Fitzpatrick, J, *Welfare Implications of Demographic Trends* (Oak Tree Press, 1997), p. 70.

[76] Delsen, L., Reday-Mulvey, G., ed., *Gradual Retirement in the OECD Countries: Macro and Micro Issues and Policies* (Dartmouth, 1996). Also, Walker, A., *Combating Age Barriers in Employment*, European Research Report (European Foundation for the Improvement of Living and Working Conditions, Dublin 1997), p. 22.

[77] Delsen, L., Reday-Mulvey, G., ed., *Gradual Retirement in the OECD Countries: Macro and Micro Issues and Policies* (Dartmouth, 1996), p. 8.

- desire for greater personal independence and freedom to choose when, how much, and how to be occupied;
- development of a strong hobby or interest which has become more important than work;
- development of part-time, alternative work which could be more remunerative if more time were available;
- dislike of the present job and wish to withdraw from it;
- a long-term ambition to be independent as soon as income allows.[78]

This changing perception of retirement may have contributed to the greater interest in early retirement which exists amongst a number of public service groups.

Trends in retirement age in the public service

7.4.11 Table 7.3 outlines 1997 data in relation to 3,273 retirements amongst the major public service groups, covering approximately 186,000 serving employees. Assuming the same ratio of retirements to serving staff holds, then for the approximately 17,000 pensionable public servants for whom the relevant data were not readily available (mainly, third level education and non-commercial state-sponsored bodies), an additional 300 retirements can be added, giving a total of about 3,600 retirements in 1997.

Table 7.3: Retirement statistics for major public service groups (1997)

Group	Ill health retirements	Age retirements	Total retirements
Established civil servants	37	215	252
Non-established civil servants	54	125	179
National teachers (i)	67	453	520
Secondary teachers (i)	44	150	194
Garda Síochána	13	258	271
Prison Officers	7	13	20
Army officers (1995) (ii)	0	35	35
Enlisted personnel (1995) (ii)	27	137	164
Local authority officers (includes VECs)	39	256	295
Local authority employees (includes VECs)	127	268	395
Health Board officers (includes nurses)	108	423	531
Health Board non-officers	142	153	295
Voluntary hospitals officers	15	38	53
Voluntary hospitals non-officers	13	15	28
Nominated health agencies	16	25	41
Total	**709**	**2,564**	**3,273**

Source: Government Departments.

Notes:

(i) Total retirement numbers for national and secondary teachers exclude those retiring under the three strands of the limited early retirement initiative.

(ii) A voluntary early retirement scheme operated in the Defence Forces for the period 1996-98. Therefore, 1995 is considered more typical of a standard year for the purposes of this table.

[78] Mallier, A.T., and Shafto, T.A.C., *The Economics of Flexible Retirement* (Academic Press, 1992), p. 82.

7.4.12 We discuss retirement trends amongst a number of public service groups in Appendix 7.2. In Appendix 7.3 we set out past experience as regards age of retirement, service at retirement, and take-up of early retirement options where the relevant information is available. It must be qualified, however, that past experience may be an unreliable indicator of future trends.

7.4.13 Retirement behaviour is not a cohesive and consistent phenomenon across any group of employees or in the public service as a whole. As discussed above, the retirement decision is in each case a personal choice which reflects a wide range of factors. However, based on the available data, we would draw the following conclusions as regards public service retirement trends and experience over the past number of years:

- it would appear that across all groups there was a slight fall in both the average age of retirement and in the average period of pensionable service held at retirement;
- on average, the age of retirement and the period of pensionable service held at retirement was lower for women than for men;
- many public servants who were in a position to do so remained in service until the maximum retirement age or until they had sufficient pensionable service to qualify for maximum pension entitlements;
- over the period, there was an increase in the numbers retiring at the earliest permitted age (or before maximum retirement age), perhaps with less than maximum pensionable service;
- many Gardaí remained in employment when the retirement age was increased from 57 to age 60 for the period November 1989 to December 1992. This suggests the possibility that if the maximum retirement age were increased, many would decide to remain in service for longer. However, there is no evidence available on the impact of an increase in the standard maximum retirement age of 65;
- there was a large degree of variation between groups as regards pensionable service at retirement — many civil servants had maximum service of 40 years, but other public service groups, such as nurses and non-established employees, had lower levels of service;
- those retiring from groups with special *fast accrual* terms (e.g. Garda Síochána, Prison Officers) had a much higher possibility of having maximum pensionable service compared with groups with standard terms;
- there were generally higher numbers of retirements on grounds of ill health amongst non-established public servants compared with established public servants.

7.4.14 There is little research information available on employee attitudes to early retirement in the public service. A report published in 1996[79] contained results of an employee survey carried out in 1994 amongst private and public sector employees under a number of headings, including intentions in relation to early retirement. The public sector sample comprised most public sector bodies and organisations, but excluded a number of important groups (such as civil servants and teachers). The survey results showed that employees in age brackets between 26 and 55 had the highest probabilities of considering early retirement at some future date while the percentage expressing an interest in this option fell significantly for those aged 56 and over. The report noted that the latter might no longer perceive early retirement as being *early* while the former might not

[79] Fynes, B., Morrissey, T., Roche, W.K., Whelan, B.J. and Williams, J., *Flexible Working Lives: The Changing Nature of Working Time Arrangements in Ireland* (Oak Tree Press, 1996), Chapter 6.

have considered in full the financial and other realities of what early retirement could involve. The report also found that while interest in early retirement did not vary significantly between the public and private sectors, a greater number of older public servants expressed interest in early retirement.

7.4.15 The 1994 survey also covered the post-retirement intentions of those who stated that they would be interested in taking up an early retirement option at some date in the future. Only 14% of private sector and 27% of public sector workers said that they would never wish to work again after early retirement. Approximately 53% of both public and private sector employees said that they would like to take up part-time employment, while 32% of private and 18% of public sector employees said that they would consider the option of self-employment after early retirement. The report commented that the net effect of early retirement could be a shift of a section of the labour-force from one form of employment status to another.

7.4.16 Retirement trends have implications both for the design of working arrangements for staff and for pension provision. For example, if public servants are retiring from full-time employment earlier than before, perhaps taking up part-time or contract employment elsewhere after retiring, this may imply that there is a demand to remain working for longer within the public service, but on a commitment of less than full-time. Also, the data show that public servants are retiring with lower levels of pensionable service, on average, than before. Thus, there may be a demand to allow individuals extra pension flexibility to contribute to meet part or all of the gap between actual and maximum benefits on retirement. In conclusion, it is clear that there is no one retirement *solution* — a range of options are needed to cater for different personal choices and circumstances.

7.5 Management of performance: implementation of public service change

7.5.1 A structured approach to managing public service change has come in the form of the Strategic Management Initiative which was introduced in 1994. The modernisation of the public service has implications for occupational pensions, not just in relation to pension terms, but also in relation to the management of pension schemes and of pension costs, both at global and local level. A note on the implementation of change in the public service, with particular reference to atypical employment, employment structures, etc. is contained in Appendix 7.4.

7.5.2 The Government's report, *Delivering Better Government* (May 1996), set out a framework for change embracing a series of independent initiatives which, collectively, are aimed at improving civil and public services. Key areas identified as requiring radical change included:

- human resource management, where there is a need to update practices and systems to ensure a more proactive, strategic approach to the management and development of staff at all levels;
- devolving authority and accountability, so that there is a strong focus, at every level, on achieving results and improving performance;
- financial management, with a view to putting in place comprehensive and effective systems that ensure value for money in every area of public expenditure.

7.5.3 Every significant aspect of human resource management is to be looked at under the Strategic Management Initiative, including recruitment, training and development, performance management including rewards and sanctions, probation, promotion, multiple grade structures, gender-related issues, and terms of employment. It is intended that greater flexibility in human resource management practices will allow the public service to respond more efficiently and effectively to changing needs and demands.

7.5.4 As noted in Paragraph 7.3.2, *Delivering Better Government* stated that while recruitment in the past was generally confined to full-time career-length established service, there was need for the public service to avail of a more flexible range of options — including temporary and part-time work — to meet the exigencies of today's working environment.

7.5.5 One of the features of recent National Programmes has been a marked change in the approach to pay determination in the public service. There has been a move away from the traditional approach of special pay increases based largely on pay comparability and relativities towards local bargaining increases linked to increased productivity, change and the delivery of the public service modernisation programme.

7.5.6 The *Programme for Competitiveness and Work (PCW)* provided for the negotiation of local bargaining increases in one of two ways: what became known as *restructuring* claims under Option A or a straightforward percentage increase under Option B (the vast bulk of settlements were concluded under Option A). There was a requirement in both cases to take account of the need for efficiency, flexibility and change, and the contributions to be made by employees to such a change.

7.5.7 *Partnership 2000* provided for a locally negotiated increase of 2%, payment of which was conditional on the achievement of verified progress to a satisfactory level on implementation of the public service modernisation programme set out in Chapter 10 of the Programme. Unlike the *PCW*, where the flexibility and change measures were negotiated with individual grades, progress on the action modernisation plans was assessed at sectoral and organisational levels.

7.5.8 The *Programme for Prosperity and Fairness* does not include a local bargaining provision. However, the parties commit themselves to full and ongoing co-operation with change, continued adaptation and flexibility and the delivery of the modernisation programme in the public service as set out in Section 1.4 of the Programme. It has been agreed that the payment of the final phase increase of 4%, from a date not earlier than 1 October 2002, is conditional on specific performance indicators being established in each sector by 1 April 2001, and these sectoral targets being achieved by 1 April 2002, with progress in this regard being assessed at organisational level by 1 October 2002.

7.5.9 It is not clear how the overall approach to public service pay determination is likely to evolve over the medium to longer term. The *Programme for Prosperity and Fairness*, which accepts the need to find an appropriate way of benchmarking public service pay to the market, acknowledges that the traditional approach to pay reviews has given rise to serious difficulties in the past and provides for an alternative approach which is to be grounded in a coherent and broadly-based comparison with jobs and pay rates across the economy. In particular, it provides for the establishment of a Public Service Benchmarking Body to examine public service pay and jobs and to make recommendations thereon (the formal establishment of the Benchmarking Body was announced on 19 July 2000). Two aspects of the new approach may be of particular relevance in terms of their possible implications for public service pension schemes, viz:

(i) the stated intention that the Benchmarking Body will take account of the way reward systems are structured in the private sector; and

(ii) the acceptance that issues such as new forms of work organisation embracing innovative work practices, multi-grade and cross-stream teams, and flexibility in grading, including broad-banding, complemented by imaginative reward and recognition systems including an examination of gainsharing are likely to arise from the Benchmarking exercise.

7.6 Conclusions

7.6.1 It is difficult for the Commission to draw clear conclusions on the extent of change which has occurred in the operational requirements, working environment, and conditions of employment of public servants. It is not possible to examine in any detail the specific developments affecting every public service occupation. The changes which have occurred, or which may be expected to occur in the future, in relation to, for example, the form of employment of public servants and their remuneration package, will have fundamental implications for the pension structure and pension terms to be applied. Accordingly, the Commission has endeavoured in this Chapter to analyse these changes for the purposes of determining how radical a change in pension arrangements might be necessary.

7.6.2 The main trends identified by the Commission are summarised below:

- increasing age of entry and trends towards shorter service and greater mobility, on average, in public service employment compared with the past;
- greater usage of atypical, particularly part-time employment (the future position will depend on the level of take-up of available provisions across the public service);
- a stronger focus on ensuring pensionability of atypical employment;
- more frequent breaks in service for many public servants, including periods spent in part-time working, on career breaks, etc.;
- greater interest in retiring earlier than the norm, in some cases with the aim of taking up other forms of working, e.g. part-time working;
- increasing emphasis on delivery of service and management of performance within all areas of the public service;
- modifications in the pay determination system, which has changed in various ways over the last few years and will change further, within the terms of the *Programme for Prosperity and Fairness*.

We consider further the implications of these developments for public service pension arrangements in Chapter 12 of the Report.

7.6.3 A number of responses to increasing longevity and improvements in health and educational resources have been implemented in several OECD countries. These include encouraging working beyond retirement age, more flexible working arrangements at older ages, replacement of the fixed point of retirement with gradual/phased retirement, ensuring availability of job opportunities for older workers and that they are equipped with the necessary skills and competence to take them. In relation to pay-as-you-go public old-age pension systems (state social security systems as well as public service occupational pension schemes), reforms have usually implied changes to several of the basic parameters determining pension benefits, including:

- lengthening the contribution periods required for full pension;
- increase in the standard age of entitlement to public pensions;
- greater flexibility in the age at which benefits can be accessed with actuarial adjustment;
- increase in contribution rates.[80]

[80] OECD, *Maintaining Prosperity in an Ageing Society* (1998), p. 189.

APPENDIX 7.1

Part-time employment in the public service

1. There is no precise definition of what constitutes a part-time employee; many public service bodies appear to consider part-timers to be those working a minimum number of hours a week (around eight hours) for a minimum number of weeks (around 13 weeks). Most bodies appear to make a distinction between employees working a substantial number of hours and paid weekly and those working occasionally and possibly paid a stipend rather than a weekly wage. The definition of a part-time employee is taken here as any employee working less than the standard hours for his or her category of employment.

2. Some part-time staff are permanent, e.g. branch librarians in local authorities (not pensionable); others are temporary. Some part-time employees may have full-time pensionable posts in the private or public sector while also working part-time in the public service, e.g. some part-time VEC teachers. Some persons may have more than one part-time post. Some part-time employees may move to full-time employment at some stage.

3. Based on a review of the available information, it appears that there may be as many as 42,000 part-time public servants, including 12,500 home-helps employed in the health service[81] (in addition, there are perhaps 8,000 job-sharers). This number is subject to seasonal variation. We have attempted to list the main part-time groups below, giving a breakdown by sex where available. For some part-time groups, the majority of employees are male (e.g. non-officers and retained Firefighters in the local authorities); for others, the majority are female (e.g. nursing and support staff in the health service; School Wardens employed by local authorities).

4. It should be emphasised that many part-time employees (e.g. in teaching and nursing) may take up permanent employment in due course; there are arrangements to make prior part-time service pensionable in such circumstances.

Breakdown of part-time employment in the public service

5. ***Health:*** There are 19,700 part-time employees, approximately, broken down as follows: 7,200 mainly concentrated in nursing or support services (about 87% are female) and 12,500 home helps (almost all of whom are female).

6. ***Education:*** There are 14,700 part-time employees, approximately, in the education area, broken down as follows:

(i) Primary sector:

- 800 substitute teachers, employed on a day-to-day basis;

(ii) Secondary sector:

- 900 eligible part-time teachers (employed at least 11 hours per week, i.e. half wholetime hours; on average, they work 16 hours per week and are employed for at least a year);
- 600 part-time hourly-paid teachers (on average, they work a quarter-week, i.e. 6 hours);

[81] While home helps have traditionally been considered as self-employed, we understand that as a result of recent developments, they will in future be considered as employees.

- 2,000 substitute teachers (employed day-to-day; on average, they are employed for one-quarter of the year);
- Part-time cleaners/support staff in schools;

(iii) Third level sector (Higher Education Authority universities and colleges):

- 1,060 academic staff and 990 non-academic staff;

(iv) VECs/Institutes of Technology:

- approximately 6,000 part-time officers employed principally in a part-time teaching/lecturing capacity, of whom 55% are female;
- approximately 2,350 employees, of whom 63% are female.

7. ***Local authorities:*** There are 4,400 part-time employees, approximately, broken down as follows: 2,000 retained Firefighters, 900 Burial Ground Workers and 320 Caretakers (mainly male employees); 650 School Wardens, 230 Cleaners, and 210 Branch Librarians (mainly females employees).

8. ***Garda Síochána:*** There are, approximately, 740 part-timers employed in areas related to the work of the Garda Síochána, broken down as follows: 100 Traffic Wardens, 80 part-time Cleaners/Service Attendants and 560 part-time Cleaners working less than eight hours per week.

9. ***Non-commercial state-sponsored bodies:*** 700 part-time employees, approximately, are employed by the non-commercial state-sponsored bodies.

10. ***Civil service:*** There are 1,600 employees, approximately, broken down as follows: 70 clerical employees in the Passport Office, 300 Caretakers, 300 Water Readers, 250 Guides, 50-100 General Operatives in the Department of Arts, Heritage, Gaeltacht and the Islands/Office of Public Works, 540 temporary Veterinary Inspectors (fee paid) in the Department of Agriculture, Food and Rural Development.

11. The numbers of part-time employees may well be understated because of the lack of clear definition of part-time working and incomplete data.

APPENDIX 7.2

Retirement trends in the public service

1. For the purpose of our analysis, we refer to the tables of retirement statistics presented in Appendix 7.3.

Civil service

2. Table 1 indicates that the average age of retirement for established civil servants has fallen slightly over the period 1980 to 1997. In 1980, the average age for those retiring was 62.7; in 1997, it was 61.6. The average age of all established civil servants retiring in the period 1980-97 was 60.1 (62.1, if the VER scheme is excluded), and was different for men and women: ages 61 and 57.7, respectively. The difference in retirement age for male and female civil servants is explained to a large degree by the greater proportion of women who retire on ill health grounds as compared with men. Table 1 also shows that there has been a decline in the average level of service at retirement from 36.2 years in 1980 to 32.6 years in 1992, stabilising since then at slightly below that level.

3. Table 2 shows retirements categorised by length of service and age at retirement. It is difficult to identify clear trends in these categories in the period reviewed. For example, the numbers choosing to retire at age 60 or between ages 60 and 64 accounted for 30%-50% of annual retirements in the period 1985-91, excluding 1989 when, as a result of the VER scheme, the figure fell to 18%. However, the number of retirements in this category fell to 23% in 1992, before rising steadily (with the exception of 1996) to 38% in 1997.

4. The VER scheme (see Paragraph 3.3.17 of the Report) had a significant impact on retirement patterns in 1988 and 1989 as many civil servants availed of the opportunity to retire before the minimum retirement age of 60. Approximately 1,250 civil servants retired under the scheme; this represented 4.2% of all serving civil servants on 1 January 1988. The VER scheme affected retirement patterns in the subsequent years and probably explains why there was a general fall in the percentage of civil servants retiring voluntarily in the age 60 to 64 category from 1992 on as compared with the 1985-87 period.

5. The percentage of civil servants retiring at maximum age (age 65) fluctuated over the period scrutinised from a low of 8% of retirements in 1988 to a high of 56% in 1992. No coherent pattern emerges other than the fact that, on average, civil servants retiring at age 65 account for a slightly higher percentage of total annual retirements in the latter part of the period as compared with the earlier part.

6. It is not possible to isolate ill health early retirements for the earlier part of the period surveyed because of the inclusion of the VER scheme in the numbers. However, for the period 1994-97 (when the VER scheme is no longer a factor), the number of ill health early retirements ranges from 12% to 19% of total annual retirements.

Prison service

7. During the period 1994-98, there was a total of 71 retirements from the prison service (see Table 3). Of these, 20% retired at the maximum retirement age of 60, 28% retired between the ages of 55 and 59, 15% retired between the ages of 50 and 54, and 37% retired early on ill health grounds. The vast majority of Prison Officers (83%) retiring on age grounds had full pension entitlements, benefiting from the fast accrual nature of their pension arrangements.

Teachers[82]

8. The percentage of national and secondary teachers retiring at maximum age (age 65) declined steadily throughout the period 1985-97 (see Tables 4 and 5). Such retirements as a percentage of total retirements fell from 46% in the case of national teachers, and 49% in the case of secondary teachers, in 1985 to 15% and 19%, respectively, in 1997.

9. The early retirement facility for national teachers (retirement from age 55, provided the teacher has a minimum of 35 years' service) accounted for around 5% of retirements in 1985. This increased to between 18% and 26% of retirements in the period 1990-97. The *55:35* facility was introduced for secondary teachers in 1997 and trends in take-up have not yet been identified.

10. Voluntary age retirements between ages 60 and 64 varied between 24% and 45% of total retirements for both national and secondary teachers over the full period (exceptionally, much lower in 1988 as a result of the VER scheme).

11. The number of national and secondary teachers retiring early on ill health grounds during this period as a percentage of total retirements was 16% and 20%, respectively.

12. A new limited early retirement scheme was introduced as part of the *PCW* restructuring agreement reached between the Department of Education and Science and the teachers' unions. It took effect for national teachers in 1996 and for second level teachers in early 1997 (full details are set out in Appendix 3.4). Take-up under the initiative has been much lower than the overall quota of 400 such retirements per year. A more detailed picture of the take-up rate is contained in Paragraphs 15.3.9-15.3.10.

Garda Síochána

13. As regards the Garda Síochána (see Tables 6 and 7), it is difficult to pick out any discernible trend in retirements during the period 1986 to 1997. The position is complicated by the Government decision to retain until age 60 members of the Force who reached age 57 between 19 November 1989 and 31 December 1992 as a means of temporarily increasing Garda numbers. However, it can be said that the proportion of retirements at maximum retirement age, whether age 57 or age 60, was higher in the period 1994-97 compared with the earlier years of the survey (averaging over 50% as against a figure of less than 40%). On the other hand, throughout the period, many members availed of the opportunity to retire before age 57 on achieving 30 years' service.

14. It is noteworthy that over the period 1989-92 many members availed of the option to remain in service until age 60, eventually retiring in 1993 and 1994. Retirements at age 60 represented 26% and 24%, respectively, of total retirements in those years.

15. The average age of retirement for the overall group over the review period was 55.4. The percentage of members who retired early on ill health grounds was 4%. It should be noted that members of the Garda Síochána, who have fast accrual pension terms (30 years' actual service gives 40 years' pensionable service), almost always have maximum service at retirement.

[82] The data relate to national and secondary teachers. Vocational teachers, who were covered by the Local Government Superannuation Scheme during the period in question, are not included.

Health service (nurses)

16. Contrary to the position with the groups discussed above, data on retirements from the health service are held in a decentralised way and so our comments must be qualified on the basis of limited data availability.

17. Data on retirements from four Health Boards (covered by the Local Government Superannuation Scheme) for the period 1995-97, summarised in the table below, indicate that of 217 General Nurses who retired on age grounds, 20% retired at age 60, 44% between ages 61 and 64, and 36% at age 65. Of the 55 Psychiatric Nurses who retired from the Eastern Health Board during the same period, 28 (51%) were aged between 55 and 59, 3 (5%) were aged 60, 14 (26%) aged 61-64, and 10 (18%) aged 65.

Age at Retirement: 1995-97	55-59	60	61-64	65
	%	%	%	%
General Nurse	–	20	44	36
Psychiatric Nurse	51	5	26	18

A survey of retirements in a number of Health Boards and voluntary hospitals for the period 1995-97 showed that, on average, 37% of all nursing retirements were on early retirement ill health grounds. The figures varied considerably by Health Board/voluntary hospital, ranging from 25% to 64% of total retirements.

18. Based on Eastern Health Board retirements in 1995-97, it appears that most Psychiatric Nurses who have fast accrual terms have maximum service at retirement (73% of all retirements). General Nurses, on the other hand, rarely have maximum service at retirement. For example, based on a sample of 752 retired nurses (the 217 General Nurse retirements considered above, and 535 nurses who had retired under the Voluntary Hospitals Superannuation Scheme), only 8% had 40 years' service while 64% had less than 30 years' service.

Non-established employees (civil service, local authorities, health service)

19. Data available in relation to non-established civil servants and employees in local authorities and the health service indicate that, in general, these groups have less service at retirement than their established or officer equivalents (see also Appendix 11.4 of the Report). The average level of service on retirement for a sample of recent non-established retirements was 21 years. Only 24% of this group had more than 30 years' service. Over the period 1992-95, approximately one-third of all retirements were on ill health grounds.

20. Data on a total of 180 retirements among employees in Dublin Corporation between 1993 and 1996 show that the average service at retirement was 28 years. Just over 60% of employees had more than 30 years' service. Ill health early retirements for the period 1994-96 represented 37% of overall retirements.

21. Information from the Voluntary Hospitals Superannuation Scheme in relation to 477 non-officer pensioners indicates that 87% of this group had less than 30 years' service at retirement, with 64% having less than 20 years. Ill health retirement levels would appear to be particularly high among health service employees with an average figure of 56% of all retirements among a selection of Health Boards and voluntary hospitals for the period 1995-97. The figures ranged from 38% to 67% of all retirements in the bodies surveyed.

APPENDIX 7.3

Table 1: Civil service retirement statistics: established civil servants, excluding Prison Officers

	1980	1985	1990	1992	1994	1995	1996	1997	Overall Total 1980-97
	Years	Years	Years	Years	Years	Years	Years	Years	Years
Service at retirement (i)									
Female	33.6	34.3	32.8	29.8	30.1	32.7	31.1	31.5	32.9
Male	38.1	37.3	33.9	33.7	32.8	32.6	32.9	32.5	34.9
Overall	**36.2**	**36.5**	**33.6**	**32.6**	**32.1**	**32.6**	**32.4**	**32.3**	**34.3**
Age at retirement (ii)									
Female	61.3	60.3	61.4	58.4	57.1	59	57.8	60.7	57.7
Male	63.7	63.3	61.6	61.9	61.7	62.4	62.1	61.8	61
Overall	**62.7**	**62.6**	**61.6**	**60.9**	**60.5**	**61.5**	**61.1**	**61.6**	**60.1 (iii)**

Notes:

(i) Average pensionable service includes added years awarded on retirement on ill health grounds or under the voluntary early retirement (VER) scheme. It excludes any accrued service in excess of 40 years (if such service were included, the average figures would be higher).

(ii) The average age at retirement figures include those who retired on ill health and those who retired under the VER scheme (1,250 civil servants during 1987-88). Most of the persons in these categories retired before age 60.

(iii) Average age at retirement for the period 1980-97 (60.1) is lower than the average age in each of the specimen years shown. The low overall average arises from the effect of the low average age (54.6) among civil servants who availed of the VER scheme in 1988-89.

Table 2: Further civil service retirement statistics: established civil servants, excluding Prison Officers

Category of Retirement (i)	1980		1985-87 (Average)		1990		1992		1994		1995		1996		1997		Total 1980-97	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Aged 60: 40 years' service	2	1	9	3	4	2	1	1	4	2	1	1	7	3	7	3	140	3
Aged 60: < 40 years' service	0	0	9	3	10	6	5	3	8	4	8	4	3	1	17	7	144	3
Aged 60-64: 40 years' service	44	23	86	32	34	20	24	15	40	18	33	16	32	14	47	19	988	21
Aged 60-64: < 40 years' service	13	7	19	7	9	5	6	4	10	5	23	11	16	7	22	9	301	6
Aged 65: 40 years' service (ii)	35	19	66	25	41	24	42	26	46	21	39	19	44	19	45	18	876	18
Aged 65: < 40 years' service	14	7	38	14	42	25	49	30	62	28	69	34	80	35	67	26	784	17
Ill health & VER: 40 years' service	1	1	7	3	4	2	2	1	5	2	3	1	8	3	8	3	308	7
Ill health & VER: < 40 years' service	7	4	15	6	21	12	26	16	38	17	23	11	34	15	29	11	823	17
Retirement after age 65 (iii)	36	19	12	5	6	3	5	3	5	2	4	2	7	3	9	4	258	5
No date of birth available	36	19	4	2	1	1	2	1	2	1	3	1	0	0	1	0	144	3
Total	**188**	**100**	**265**	**100**	**172**	**100**	**162**	**100**	**220**	**100**	**206**	**100**	**231**	**100**	**252**	**100**	**4,766**	**100**

Notes:

(i) These figures are based on the details of pensioners who retired over the period 1980-97 and who continued to be in receipt of pension in 1997.
(ii) Maximum retirement age is 65.
(iii) Although maximum retirement age is 65, some staff may be kept on for a short period after age 65 in special circumstances.

Table 3: Prison Officer retirement statistics

Category of retirement	1994	1995	1996	1997	1998	Total 1994-98	% breakdown
	Nos.	Nos.	Nos.	Nos.	Nos.	Nos.	%
Aged 60: 40 years' service (i)	2	3	2	1	1	9	13
Aged 60: < 40 years' service	0	0	2	3	0	5	7
Aged 55-59: 40 years' service (ii)	0	3	5	5	4	17	24
Aged 55-59: < 40 years' service	1	0	0	0	2	3	4
Aged 50-54: 40 years' service (iii)	1	1	2	4	3	11	15
Ill health	3	5	4	7	7	26	37
Total	**7**	**12**	**15**	**20**	**17**	**71**	**100**

Notes:

(i) Prison Officers must retire by age 60. Every year of service accrued over 20 years is doubled for pension purposes; therefore, 30 years' actual service is equal to 40 years' pensionable service.

(ii) Minimum retirement age is 55 except where (iii) below applies.

(iii) Prison Officers with 30 years' actual service in the prison system may retire with full pension entitlement from age 50.

Table 4: National Teacher retirement statistics

Category of retirement	1985		1987		1988		1990		1992		1994		1995		1996		1997		Total 1984-97	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Compulsory: Age 65	109	46	95	37	98	16	54	19	44	17	54	14	69	16	54	13	90	15	1,074	22
Voluntary: 60-64	75	32	88	34	67	11	69	25	71	27	161	43	194	45	160	38	239	40	1,567	32
Voluntary: 55-59	11	4	27	11	31	5	66	24	67	26	90	24	79	18	95	22	124	21	850	17
Ill health	40	17	43	17	47	7	80	29	61	24	60	16	72	17	67	16	67	11	801	16
Preserved	2	1	4	1	12	2	9	3	15	6	13	3	18	4	13	3	25	4	144	3
VER (i)	–	–	–	–	374	59	–	–	–	–	–	–	–	–	–	–	–	–	374	8
Strand 1(ii)	–	–	–	–	–	–	–	–	–	–	–	–	–	–	7	2	21	3	28	1
Strand 2	–	–	–	–	–	–	–	–	–	–	–	–	–	–	17	4	24	4	41	1
Strand 3	–	–	–	–	–	–	–	–	–	–	–	–	–	–	7	2	11	2	18	0
Total	**237**	**100**	**257**	**100**	**629**	**100**	**278**	**100**	**258**	**100**	**378**	**100**	**432**	**100**	**420**	**100**	**601**	**100**	**4,897**	**100**

Notes:

(i) 374 national teachers availed of the VER scheme in 1988.

(ii) A new limited early retirement initiative comprising of three strands was introduced in 1996 under the *PCW* Agreement (see Section 3.6 of the Report).

Table 5: Second level teacher (excluding VEC) retirement statistics

Category of retirement	1985		1987		1988		1990		1992		1994		1995		1996		1997		Total 1984-97	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Compulsory: Age 65	65	49	55	45	64	18	53	36	44	31	45	24	41	21	48	23	52	19	727	29
Voluntary: Age 60-64	38	29	30	24	58	17	54	36	39	28	79	41	78	40	79	38	88	32	777	31
Voluntary: Age 55-59 (i)	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	10	3	10	1
Ill health	20	15	28	23	30	9	32	21	45	32	45	24	47	24	53	26	44	16	508	20
Preserved	9	7	10	8	19	5	11	7	13	9	21	11	29	15	26	13	18	7	219	9
VER (ii)	–	–	–	–	177	51	–	–	–	–	–	–	–	–	–	–	–	–	183	7
Strand 1 (iii)	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	13	5	13	1
Strand 2	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	32	12	32	1
Strand 3	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	17	6	17	1
Total	**132**	**100**	**123**	**100**	**348**	**100**	**150**	**100**	**141**	**100**	**190**	**100**	**195**	**100**	**206**	**100**	**274**	**100**	**2,486**	**100**

Notes:

(i) The option of retiring from age 55 where a secondary teacher has 35 years' pensionable service was introduced in 1996.

(ii) 177 teachers availed of the VER scheme in 1988.

(iii) A new limited early retirement initiative comprising of three strands was introduced in 1997 under the *PCW* Agreement (see Section 3.6 of the Report).

Table 6: Garda Síochána retirement statistics (Gardaí and Sergeants)

Category of Retirement (i)	1986		1988		1990		1991		1992		1994		1995		1996		1997		Total 1986-97	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Under age 50 (ii)	6	4	12	6	7	7	9	7	2	3	13	4	7	2	17	7	13	5	110	4
Age 50-56 (iii)	70	49	122	56	72	77	90	76	54	75	141	38	153	41	111	44	132	49	1,184	47
Age 57 (Max.) (iv)	34	24	40	18	0	0	1	1	1	1	100	27	130	35	124	49	126	46	769	30
Age 57-59	0	0	1	1	0	0	5	4	6	8	27	7	13	3	0	0	0	0	66	3
Age 60	0	0	0	0	0	0	2	2	9	13	90	24	70	19	0	0	0	0	258	10
Age 60-62 (v)	8	6	18	8	3	3	0	0	0	0	0	0	0	0	0	0	0	0	47	2
Age 63 (Max.)	24	17	25	11	12	13	12	10	0	0	0	0	0	0	0	0	0	0	113	4
Total	**142**	**100**	**218**	**100**	**94**	**100**	**119**	**100**	**72**	**100**	**371**	**100**	**373**	**100**	**252**	**100**	**271**	**100**	**2,547**	**100**

Notes:

(i) These figures are based on the details of pensioners who retired over the period 1986-97 and who continued to be in receipt of pension in 1997.
(ii) It is assumed that almost all of these retirements were on ill health grounds.
(iii) The normal retirement age for Gardaí and for Sergeants is 57. However, retirement is permitted from age 50 where the member has accrued 30 years' actual service in the Force (service in excess of 20 years is doubled for pension purposes; therefore, 30 years' actual service is equal to 40 years' pensionable service).
(iv) A government decision enabled members of the Force who reached age 57 between 19 November 1989 and 31 December 1992 to stay in service until age 60.
(v) Until 1952, new entrants were conditioned to a maximum retirement age of 63. Thus, retirements over age 60 continued up until 1991.

Table 7: Further Garda Síochána retirement statistics (Gardaí and Sergeants)

	1986	1988	1990	1991	1992	1994	1995	1996	1997	Average 1986-97
Average Service (i) (ii) (years)	39.1	39.6	39.1	38.3	39.6	39.6	39.7	39.4	39.7	39.5
% retiring before age 57	53.5	61.5	84	83.2	77.8	41.5	42.9	50.8	53.5	50.8
Average age at retirement	**55.7**	**55.5**	**53.4**	**52.8**	**54.6**	**56.2**	**56.1**	**54.3**	**54.5**	**55.4**

Notes:

(i) Over the period 1986-97, only 6% of Gardaí/Sergeants had less than 40 years' pensionable service at retirement.
(ii) When determining average service, service in excess of 40 years is excluded.

APPENDIX 7.4

Implementation of change in the public service

1. *Civil service*

1.1 Consistent with the implementation of the Strategic Management Initiative, the various restructuring agreements negotiated with the civil service unions under the *Programme for Competitiveness and Work (PCW)* included provision for enhanced grade flexibility in the performance of duties, certain commitments in relation to atypical recruitment (temporary, part-time and contract staff), contracting out of work, varying hours of attendance, redeployment of surplus staff and the development and operation of procedures to deal with underperformance. Specifically,

- the most recent Executive Officer, Administrative Officer and Clerical Officer competitions (the recruitment levels for the general service grades) included provision for the formation of panels for temporary and part-time employees at each of these levels;
- as regards temporary full-time and part-time employment, the civil service currently engages about 300 temporary employees each year to meet short-term needs due, for example, to seasonal or temporary peaks in workloads, staff absences, etc. In the future, temporary requirements among Clerical Officer, Executive Officer and Administrative Officer grades may be met in the first instance from the new atypical panels. With changes to the job-sharing and career break schemes and the introduction of term time, there will be resulting staffing gaps which will be filled with temporary part-time employees. It is not yet clear what level of take-up might be involved in the revised schemes and the consequences for temporary part-time employment;
- in the context of recruitment of greater numbers of atypical civil servants, consideration is being given to the possibility of abolishing the distinction between established and non-established civil servants.

1.2 The Department of Finance has advised that, despite the fact that atypical employment is likely to be a growing category, the most common form of employment in the civil service is likely to remain *long-term* and *wholetime* for the foreseeable future.

2. *Local authorities*

2.1 A series of measures are being implemented with the aim of bringing about local government renewal through implementation of the Strategic Management Initiative. This follows the Department of the Environment document, *Better Local Government: A Programme for Change* (December 1996). The new approach to human resource management is based on local authorities having the freedom to manage their human resources within budget and to deliver more effective services to the public. Some features of the change agenda are as follows:

- a considerable proportion of the control apparatus applying in the human resources area is being dismantled. Further devolution of human resource decisions to local authorities is to take place, subject to a number of guiding principles;
- it is accepted that the present grading arrangements can give rise to rigidities and hierarchical methods of working and that the distinction between the *officer* and *servant* streams is an anachronism which should be addressed in consultation with staff interests;

- as in the civil service, the *PCW* agreements in the local authority service provide for atypical employment. However, temporary employment has been a feature of the local authority service for many years — part-time employment is also a feature;
- it is estimated that the likely incidence of part-time employment (excluding job-sharers) over the next five years will average about 1,600 posts per year. There are also 2,000 part-time retained Firefighters who, on retirement, receive a gratuity. These figures are derived from annual staffing returns on hands and exclude the effect that the proposed introduction of atypical work-sharing arrangements throughout the public service would have on employment in the local authority service;
- job-sharers as a percentage of full-time employees in local authorities is low (1.3%) compared to the Health Boards (7.9%) and the civil service (7.5%). On the basis of these figures, it might be assumed that the evolution of atypical employment is likely to have much less of an effect in the local authority area than in the other areas mentioned.

2.2 The Department of the Environment and Local Government has advised that the bulk of local authority officers and non-officers are permanent full-time employees and that this is unlikely to change over the next five years.

3. *Education*

3.1 The strategy set out in the White Paper, *Charting Our Education Future* (1995), followed by *Implementing the Agenda for Change* (1996), recognised the problems of control, management and monitoring within a highly centralised system. A clear strategic vision for education policy has been formulated linking resources and budgetary accountability with educational demands and quality of services.

3.2 Developments at a macro or national level have been accompanied by changes at the level of the school and by extension in the working environment of individual teachers.

3.3 The concept of partnership is now a central one in education. At the level of policy formulation this has involved continued and active engagement with management groups, unions, and parental interests. The concept, however, extends significantly beyond policy and into the very real world of day-to-day activity at school level where national parents' groups are now very much a central part of the educational landscape and also at the level of the individual school where parental involvement at board of management level is very much the norm.

3.4 Changes in Irish society have impacted particularly upon the world of teaching. It is generally acknowledged that teachers in the classroom face a more stressful environment as they attempt to deal with the problems arising from broken marriages, unemployment, increasing numbers of single parent families, undermotivated pupils and greater pressure for results.

3.5 At the same time, there have been some improvements in the pupil/teacher ratio over the past number of years. Enrolments at second level are expected to drop significantly over the next ten years, while at primary level, enrolments have been falling steadily in recent years and this trend is expected to continue in the years ahead.

3.6 The *PCW* Agreement reached with the teachers' unions focused to a considerable extent on pensions issues, including improved pension arrangements in relation to part-time teachers, early retirement schemes, and purchase of non-pensionable service (these are outlined in Section 3.6).

The Agreement also included measures designed to secure the integrity of the school year and to implement the school management proposals contained in the education White Paper.

3.7 There have always been temporary and part-time teachers at both primary and second level.

4. *Health*

4.1 In the health area, the health strategy statement, *Shaping a Healthier Future*, has redefined the core role of the Department of Health and Children in promoting more effective health and social services: this involves the better targeting of resources towards preventative measures, changing the focus from treatment of illness towards lifestyle improvements and community-based supports and emphasising equity, quality of service, and accountability to users of the services.

4.2 Insofar as a trend for employment in the health service can be discerned, it would be towards less temporary employment and more part-time employment (including permanent part-time employment). In addition, there are indications that there will be pressure to make the job-sharing scheme more flexible in the health area, along similar lines to the changes envisaged for the civil service.

4.3 Given the highly labour-intensive nature of the health service, the Department of Health and Children has advised that there is a case for reviewing traditional work patterns and practices with a view to introducing the flexibility necessary in order to facilitate the deployment of staff in response to service requirements.

4.4 In the particular case of nursing, the *Report of the Commission on Nursing* (1998) has stressed the need for greater flexibility in hours worked, given that it is a predominantly female profession. It has recommended that the Health Service Employers Agency and the nursing unions develop an agreed framework for the provision of permanent part-time contracts of employment for nurses and midwives. The Report supports the view that the level of temporary employment in the service should be kept to the minimum level consistent with operational requirements. It recommends that opportunities for increased use of care assistants and other non-nursing personnel in the performance of non-nursing tasks be examined.

5. *Garda Síochána*

5.1 The *Report of the Steering Group on the Efficiency and Effectiveness of the Garda Síochána* (1997) emphasised the importance of clarifying the core roles and functions of the Garda Síochána and the need to target resources in a more strategic manner. The report places major importance on delivering the policing service, performance management (at individual and organisational level), and control and accountability. The report recommends an accelerated move towards civilianisation of the more routine clerical and administrative functions, thus releasing more Gardaí for operational duties.

6. *Defence Forces*

6.1 Change in the Defence Forces has been underway since 1993, through the report of the Efficiency Audit Group (1994), the *Review of the Defence Forces 1995* (1995), and the *Defence Forces Review Implementation Plan – Phase I* (1996). A White Paper on Defence has recently been published by the Department of Defence.

6.2 It might be noted that the earlier report of the (*Gleeson*) *Commission on Remuneration and Conditions in the Defence Forces* (1990) recommended that a fundamental revision of the

Defence Forces Pension Schemes should be undertaken and highlighted various aspects of the existing arrangements requiring detailed examination in that context. That Commission concluded that the existing arrangements could not be justified on a manpower basis and that fundamental change was required to ensure that the pensions schemes met manpower policy requirements in a cost effective way as well as being fair to different groups of Defence Forces personnel.

6.3 The review of the Defence Forces identified the high age profile of military personnel at all levels as a key issue. Within the required programme of reform, it recommended the development of a manpower policy with the emphasis on lowering the age profile and involving the adoption of a voluntary early retirement (VER) scheme along with continuous recruitment. Such a scheme was implemented over the period 1996-98.

7. *Non-commercial state-sponsored bodies (NCSSBs)*

7.1 There are a wide range of separate bodies under this heading. FÁS and Teagasc, two of the largest NCSSBs, were taken as representative of these.

7.2 Since 1990, FÁS has negotiated a programme for change with its staff which aims to realise major productivity improvements throughout the organisation. FÁS has advised that atypical employment will grow in the medium term, principally with a growth in the numbers of part-time and temporary employees.

7.3 Teagasc has also have experienced a major increase in temporary employment, which is expected to continue. There has been a rapid increase in numbers of staff job-sharing.

PART III

Occupational Pensions: Private Sector and Abroad

CHAPTER 8

Occupational Pensions in the Private Sector

8.1 Introduction

8.1.1 In Part III of the Report, we review occupational pension arrangements in the private sector in Ireland and in the public service in other countries and compare them with public service pensions in Ireland. We discuss recent developments in occupational pensions, where relevant, and identify trends for the future. We highlight particular aspects of pensions practice for further consideration in the context of our recommendations.

8.1.2 Public service pensions have in the past acted as a catalyst in the development of occupational pension arrangements in the private sector. In many countries, the State was the first to make provision for its employees to cater for their old age or infirmity. The idea of occupational pensions spread to other sectors and was encouraged by governments through the creation of favourable conditions for the financing of pensions, above all, by favourable tax treatment. In many ways, public service schemes as they developed were taken by the private sector as models of what good occupational pension schemes might provide. Given this shared history, it is useful to examine how occupational pension provision now compares as between the public service and the private sector.

8.1.3 In this Chapter, the Commission sets out, firstly, to establish what pension terms apply in occupational pension schemes in the private sector and to compare them with pension terms in the public service. Secondly, we identify trends in occupational pension provision in the private sector, most obviously, the increasing use of defined contribution pension schemes. Finally, we reach certain conclusions which will help shape our analysis of the strengths and weaknesses of public service occupational pension schemes. In our examination, we have endeavoured to identify pension solutions and practice which might be of particular interest for the public service.

8.1.4 In summary, the Commission's conclusions on a comparison of pension terms in the public service with large Irish private sector schemes are as follows:

(i) pension scheme coverage for permanent employees is considerably higher in the public service than in the private sector;

(ii) in the public service, the earliest age of retirement is age 60 for the vast majority of employees (the latest is age 65). In the private sector, the normal retirement age is 65 for over three-quarters of the schemes of large firms, but almost all allow members to retire earlier, usually with their benefits being subject to some form of actuarial reduction;

(iii) in the public service, AVC schemes, if available, are generally set up at the behest of individual unions. In the private sector, almost all large firms make provision for AVCs;

(iv) most pension schemes for large firms in the private sector are defined benefit, as are public service pension schemes. However, there is an increasing trend towards defined contribution schemes for new entrants to private sector companies, particularly in the case of newly created schemes, but also, to a lesser degree, in the case of already existing schemes;

(v) most private sector defined benefit schemes operate a 60ths accrual rate with provision for commutation (i.e. conversion of a portion of pension into tax-free lump sum), while public service schemes have separate 80ths-based accrual rates for pension and lump sum. When allowing for the more favourable pensions increase policy of public service schemes (see point (vi)), the value of a public service pension is normally greater than that of a private sector pension;

(vi) pension increases in the public service are based on increases in the pay of serving staff, while increases in the private sector are often discretionary or in some cases no increases are given. Where increases are given in the private sector, they are usually based on changes in the Consumer Price Index, subject to a cap of between 3% and 5% per annum.

8.1.5 Public service pension schemes have been adapted to changing circumstances over a long period of years to encourage public servants to remain in the public service for the whole of their working lives. They do this by offering more favourable pension terms than are generally available in the private sector. This ensures that the average public servant has a higher probability of being covered, of receiving better benefits, and of such benefits maintaining their purchasing power.

8.1.6 However, moving beyond a static comparison of terms, it is clear that private sector pension schemes have had to adapt more to the changing social and economic environment and to developments in the labour market. Furthermore, private sector schemes, supported by better communication and administrative systems, offer a wider range of flexibility and retirement choice (generally at full cost to the member) than are available in the public service.

8.2 Comparison of public service and private sector pension schemes

8.2.1 In early 1997, the Commission contracted the ESRI to carry out a study of the similarities in and the differences between public service and private sector pension arrangements. The aim of the study was to compare the standard public service pension arrangements (represented by the Civil Service Pension Scheme) with pension arrangements in large companies in the private sector, i.e. those with 500 or more employees. For the purposes of the comparison, it was considered that larger companies would be of greater value as comparators than smaller companies, and that the civil service was a reasonable proxy for the public service generally.

8.2.2 Much of the comparative analysis reported below is taken from the ESRI study,[83] with supplementary information drawn from a number of other sources. As regards public service schemes, we have added details on pension terms of other public service groups where these are materially different to civil service terms.

8.2.3 In its report, the ESRI relied on the database created for the earlier ESRI 1995 survey of occupational pension schemes in Ireland, which was carried out for the Department of Social

[83] Hughes, G., "A Comparison of Pension Arrangements in the Civil Service and Large Private Sector Firms" (ESRI, January 1998).

Welfare and The Pensions Board.[84] That survey included 145 private firms and commercial state companies in Ireland employing 500 or more people. The response rate was almost 57%. The large firms that participated in the survey included 12 commercial state companies, and these were excluded from the analysis carried out for the Commission. The ESRI advised that the remaining 70 firms included in the analysis were representative of all large firms in the private sector. Of the schemes operated by these firms, 90% were defined benefit and the remaining 10% were defined contribution.

8.2.4 The comparative analysis on pension terms in the private sector and the public service (represented by the Civil Service Pension Scheme) is carried out below under the following headings:

- pension scheme coverage;
- admission criteria;
- eligibility of atypical workers;
- membership of pension scheme (voluntary v. compulsory);
- normal retirement age;
- defined benefit and defined contribution schemes;
- calculation of pensionable pay and contribution arrangements;
- calculation of pension benefits;
- annual accrual rate;
- integration with State Social Insurance system;
- dependants' benefits;
- early retirement due to ill health;
- early retirement other than on grounds of ill health;
- early leavers;
- pension increases;
- additional voluntary contributions (AVCs);
- professional, technical and specialist added years;
- financing arrangements.

8.3 Pension scheme coverage

8.3.1 Over 144,000 persons are employed in the sample of large firms and 27,000 persons are employed in the civil service. There are important differences between large private firms and the civil service in the kind of employment offered. In the civil service, the number of male and female employees is broadly equivalent and very nearly 100% of all employees are in full-time permanent employment. In the large firms included in the sample, male employees outnumber female employees by almost two-to-one. Of the male employees, 94% are in full-time employment, whether permanent or temporary, while the remaining 6% are in part-time employment. Of the female employees, 71% are in full-time employment while the remaining 29% are in part-time employment.

[84] Hughes, G. and Whelan, B.J., *Occupational and Personal Pension Coverage 1995*, ESRI (1996).

8.3.2 These differences in employment type have a major influence on the proportions of employees covered by occupational pension schemes in the private sector and the civil service. The coverage rate for all employees in the civil service is almost 100%. In large private sector firms, according to the ESRI's study for the Commission, the coverage rate for all employees is 56%.[85]

8.3.3 In the civil service, full-time permanent employees are covered by the pension scheme, but the very small number of employees in part-time permanent employment are not.[86] In large private sector firms, the coverage rate is 69% for full-time permanent employees, 57% for full-time temporary employees, 9% for part-time permanent employees, and 1% for part-time temporary employees.

8.3.4 While membership of the civil service scheme is automatic for civil servants, most occupational pension schemes operated by large private sector firms require fulfilment of minimum age or minimum length of service conditions for eligibility for membership of the scheme. In addition, membership of the civil service scheme is open to all civil servants except those who are part-time, whereas membership of private sector schemes is restricted to certain kinds of employees. Only eight of the large private sector firms in the sample operated schemes that were open to all employees. The great majority of firms, 60 out of the 70, had schemes that were open to some, but not all employees. The remaining two firms did not have an occupational pension scheme for any of their employees.

8.4 Admission criteria

8.4.1 The civil service scheme does not operate minimum entry ages (although service prior to age 16 does not reckon for pension purposes), while 78% of the schemes in the private sector sample have such a condition. Over 40% of large firms have a minimum age of entry for pension benefits of between 18 and 20 and nearly 45% of firms require that the employee must be aged 25 or more before being admitted to the scheme.

8.4.2 The civil service scheme has a minimum service requirement of five years to qualify for pension benefits. For large firms in the private sector, the most prevalent length of service condition to qualify for pension benefits is one year, though a significant number require from three to five years' service. In such a situation, it should be noted that the five years required to qualify a civil servant for benefit is included in total service for pension purposes, whereas in the private sector, pensionable service is normally counted only from the day the employee joins the scheme. In the civil service scheme, as with most private sector schemes, there is no minimum service requirement to qualify for death-in-service benefits.

8.5 Eligibility of atypical workers

8.5.1 Almost 28% of the schemes run by large employers in the private sector are open to all part-time employees. The civil service scheme covers job-sharers. In the private sector, only a minority of schemes cover part-time employees who are job-sharing or who work a specified

[85] It is worth noting that the 1995 ESRI Survey found (p. 51) that 79% of employees in large firms (employing 500 persons or more) were covered by occupational pension schemes. However, these figures include the responses of a number of commercial state companies.

[86] In Paragraph 3.3.61, we note that while no formal pension terms are in place for part-time established civil servants in full PRSI class, the Department of Finance has laid down conditions for the pensionability of such employees.

number of hours. Almost a quarter of the schemes operated by large firms cover permanent part-time employees.[87]

8.5.2 With effect from 1996, the Local Government Superannuation Scheme has admitted part-time non-officer grades to the scheme on an optional basis (see Paragraph 3.4.8). In addition, under the teachers' *PCW* restructuring agreement, teachers who are deemed to be in quasi-permanent employment, i.e. timetabled for a specific number of hours per week, are entitled to scheme membership. Full integration of benefits and contributions applies (see Section 3.6).

8.5.3 The ESRI Report, *Occupational and Personal Pension Coverage* (1995), which surveys a much wider range of occupational pension schemes than those covered in the report for the Commission, indicates that occupational pension coverage is very low for part-time temporary and permanent employees. For part-time permanent employees, the coverage rate is less than 12% and there are no significant differences in the overall rate for men and women — although there are some sectoral differences. Part-time temporary employees fare even worse, as there is no sector in which coverage is offered. The report comments that it would seem that the nature of these jobs is such that there are few advantages to employers in offering to provide an occupational pension scheme.[88]

8.5.4 The Irish Association of Pension Funds[89] (IAPF) 1998 survey of pension benefits provides some information on the number of private sector schemes which give access to part-time and other atypical workers.[90] Based on the survey response, the breakdown of those employers who include non-permanent employees in their workforce is as follows:

Table 8.1 1998 IAPF survey — atypical employment

Workforce includes	% of respondents employing non-permanent workers
Part-time employees	65%
Temporary employees	72%
Short-term contract employees	61%

Companies which employ such employees stated that their scheme covers the following benefits:

Table 8.2 1998 IAPF survey — benefits covered for atypical employees

Benefits	Part-time (%)	Temporary (%)	Short-term contract (%)
Death benefits only	5	16	14
All benefits	74	3	5
Excluded from scheme	21	81	81

[87] The difference in coverage rates for permanent part-time employees as between this Paragraph and Paragraph 8.3.3 is explained by the fact that the former refers to *coverage of employees* while the latter refers to *pension scheme coverage*.
[88] Hughes, G. and Whelan, B.J., *Occupational and Personal Pension Coverage 1995*, ESRI (1996), p. 49.
[89] The IAPF represents over 370 corporate members including the largest occupational pension schemes in the country. The annual IAPF benefits survey covers member plans only and as such is not necessarily representative of all private sector pension plans.
[90] *IAPF Benefits Survey*, 1998 (1999), p. 4.

8.5.5 The 1997 EU Directive on part-time employment and the 1999 Directive on fixed-term work may result in an increase in coverage of atypical employees in private sector schemes in the future (see Paragraphs 12.4.2-12.4.3). It is also relevant that under the *Programme for Prosperity and Fairness*, employers and unions have committed themselves to promoting the introduction of occupational schemes for those employees without access to such schemes, subject to the costs involved not undermining competitiveness and employment in enterprises.

8.6 Membership of pension scheme (voluntary v. compulsory)

8.6.1 Membership of schemes run by large firms is compulsory for three-quarters of the schemes and it is compulsory for the civil service scheme. In contrast, according to the 1995 ESRI study, compulsory scheme membership applies to just under half of the schemes run by small companies (i.e. those employing fewer than 100 persons).

8.7 Normal retirement age

8.7.1 The maximum retirement age in the civil service is 65, although established civil servants have the option to retire on or after age 60, with no actuarial reduction.[91] Under the Pensions Act, 1990, the normal pensionable age is defined as the earliest retirement age at which a scheme member is entitled to receive benefit under the rules of the scheme, disregarding ill health provisions. Using this definition, the normal retirement age for established civil servants and for most public servants would be considered to be age 60. In large firms in the private sector, the normal retirement age is 65 for over three-quarters of all schemes, 60 for 15% of schemes, and 62-63 for around 10% of schemes.

8.7.2 The wider IAPF benefits survey, which includes public sector funded schemes, found that 81% of schemes had a normal retirement age of 65 (down from a figure of 86% in 1991).[92] The survey notes that while these statistics are based on all schemes, there is evidence of a lower normal retirement age amongst defined contribution schemes. Amongst the defined contribution respondents, 65% had a normal retirement age of 65 while the balance had a normal retirement age of between 60 and 63.

8.7.3 A third, more narrowly based survey, found that the most common normal retirement age for senior executives in the private sector continues to be 65.[93] Proportionately more companies have a retirement age of 65 than previously. The survey states that while this seems surprising, it is explained by the number of plans being established with flat benefit structures for all members and also the move towards defined contribution schemes, where the higher retirement age gives executives more time to enhance the value of their retirement account. Of the 19 defined contribution schemes surveyed, only one had a retirement age other than age 65.

8.7.4 As outlined in Chapter 3, a number of public service schemes have lower retirement ages than those applying in the civil service. For example, a Garda may retire from age 50, provided he or she has at least 30 years' service, and must retire by age 57. Prison Officers, fire brigade personnel, health service personnel registered under the Mental Treatment Act, 1945, and Defence Force personnel also have lower normal retirement ages than the norm. In approving

[91] It should be noted that the average actual age of retirement may be lower than the minimum age of retirement, after allowing for early retirement on ill health grounds.
[92] *IAPF Benefits Survey,* 1998 (1999), p. 8.
[93] Irish Pensions Trust, *Executive Benefits Survey*, 1997.

pension schemes for tax purposes, the Revenue Commissioners allow lower retirement ages for certain occupational groups, such as pilots and money brokers/dealers.

8.7.5 The normal retirement age under a pension scheme may bear little relation to the actual average age of retirement. For example, many employees in the private sector avail of early retirement, either in the context of company restructurings or by personal choice. Payment of pension benefits in such situations is often subject to actuarial reduction (see Section 7.4 and Section 8.15).

8.8 Defined benefit and defined contribution schemes

8.8.1 The civil service provides defined benefit schemes for both established and non-established staff. Almost 90% of schemes operated by large firms in the private sector are defined benefit, while the remaining 10% are defined contribution. We discuss trends in relation to defined contribution schemes in the private sector at Section 8.21.

8.9 Calculation of pensionable pay and contribution arrangements

8.9.1 The civil service scheme and almost all of the schemes operated by large firms take basic pay into account in reckoning pensionable pay. The civil service scheme takes shift premium and service pay into account, while only a minority of large firms do so. Bonuses, commissions, and other elements of pay are taken into account by a minority of large firms' schemes. These elements do not form part of civil service remuneration.

8.9.2 As indicated in Paragraph 11.9.4, the majority of public servants in modified PRSI class are in schemes where an explicit pension contribution rate of $6\frac{1}{2}$% of remuneration applies. The civil service scheme has traditionally been non-contributory (with the exception of the spouses' and children's pension scheme, which has a contribution of $1\frac{1}{2}$% of remuneration). However, for pay determination purposes, it has been accepted in a number of arbitration findings that an implicit contribution is made through salary being set at a lower level to take account of the benefits payable under the pension scheme (we examine this matter in Section 11.9). New appointees to public service grades affected by the 1995 PRSI changes pay a contribution of $6\frac{1}{2}$% ($3\frac{1}{2}$% of net remuneration and 3% of full remuneration) in respect of their occupational benefits.

8.9.3 Almost one-third of schemes in large firms do not require a direct member contribution. The remaining two-thirds require either all or some members to contribute. There are 59 schemes in which members make a contribution towards their pension; except for one scheme (in which the contribution is a fixed sum), the contribution payable is a percentage of pensionable pay. The rate of employee contribution is less than 3% of pensionable pay in about one-fifth of schemes in which a contribution is required, between 3 and 4.9% in a further quarter of schemes, between 5 and 5.9% for a third of schemes, and 6% or more for the final one-fifth of schemes.

8.9.4 Consistent with the ESRI findings, the IAPF Benefits Survey, 1998 found that member contributions are required in 64% of defined benefit plans and 66% of defined contribution plans. The survey comments that the typical contribution is 5% of pensionable salary for defined benefit schemes. Member contribution levels tend to be marginally lower for defined contribution schemes, though the survey notes that this must be considered in the context of the definition of pensionable salary.

8.10 Calculation of pension benefit

8.10.1 In the civil service scheme, pension benefit is calculated on the basis of pensionable pay on the final day of service, except in the case of promotion or change of grade in the three years preceding retirement, where an average of pensionable pay in the final three years of service is used. Almost three-quarters of schemes in large firms base their pension benefits on final pensionable pay. Over a quarter of schemes use average pensionable pay or some other method. Where averaging is used, it is usually based on the last three years of pensionable pay.

8.11 Annual accrual rate

8.11.1 The accrual rate is the rate (percentage of final pay) at which pension benefits are *earned* during service.[94] The accrual rates used by the civil service scheme and by about 5% of schemes in large firms are 1/80th for pension and 3/80ths for lump sum. These accrual rates provide for a pension equal to half of final salary and a lump sum equal to one-and-a-half times final salary after 40 years' service. Over three-quarters of the schemes provided by large firms use an accrual rate of 1/60th per year of service, which gives a pension equal to two-thirds of final salary after 40 years' service (part of which may be commuted to a lump sum of up to one-and-a-half times final salary). A small number of schemes in large firms use an accrual rate of between 1/30th and 1/50th, while the remainder use an accrual rate of 1/100th or some other fraction.

8.11.2 The IAPF Benefits Survey, 1998 reinforces these findings, indicating that 87% of plans surveyed had an accrual rate of 1/60th, while only 10% had a better rate and 3% a lesser rate.[95]

8.11.3 The majority of private sector schemes apply a commutation rate which enables pension to be converted into lump sum on a 1:9 basis (1:9.8 for female employees). As shown in Table 11.1, this gives the same outcome as the civil service eightieths accrual rate for pension and lump sum. However, the value of public service pension benefits is more favourable than the value of private sector benefits where 1:9 commutation applies, because of their more favourable pensions increase arrangements. The comparison is less clearcut for the small number of private sector schemes which adopt commutation factors that are more favourable, from the member's perspective, than 1:9. However, we show in Appendix 11.1 that even for such schemes, the cumulative value of the public service benefits will normally exceed that of the private sector benefits.

8.11.4 In the 1995 ESRI survey, over half of the schemes apply the same accrual rates to part-time employees who are members. The remaining firms were asked what accrual rates they apply to part-time employees but the number who replied to this question was too small to provide reliable information.[96]

8.12 Integration with State Social Insurance system

8.12.1 The civil service scheme and two-thirds of the large private sector schemes surveyed are integrated with the State Social Insurance system.[97] Established civil servants recruited on or after 6 April 1995 pay the full rate of PRSI and are subject to integration with Social Insurance benefits

[94] Accrual rates apply in defined benefit plans only.
[95] *IAPF Benefits Survey*, 1998 (1999), p. 9.
[96] Hughes, G. and Whelan, B.J., *Occupational and Personal Pension Coverage, 1995,* ESRI (1996), p. 81.
[97] The private sector schemes surveyed include a small number of defined contribution schemes, which are unlikely to be integrated – but see Paragraph 8.12.5.

(as are all other recruits to the public service from this date). Those recruited before that date pay the modified rate of PRSI and so have no entitlement to Social Insurance old age pension benefits. All non-established civil servants pay the full rate of PRSI and are subject to integration with Social Insurance benefits.

8.12.2 Public service schemes and 90% of the two-thirds of schemes in large firms which apply integration achieve that objective by adjusting the level of pensionable pay on which benefits and contributions are based through deducting a multiple of the basic Social Insurance Old Age (Contributory) Pension (OACP). In the public service scheme a multiple of twice the rate of OACP is used, while in large firms a multiple of $1\frac{1}{2}$ times OACP is used. The two multiples give essentially the same result when one allows for the different accrual rate of 60ths in the private sector and 80ths in the public service (see Paragraph 11.5.8).

8.12.3 The 1995 ESRI Survey found that nearly 60% of members of small schemes and 65% of members of large schemes are in integrated schemes.[98] The report comments that the percentages are based on all schemes, including both defined benefit and defined contribution schemes, and that the latter were unlikely to be integrated (although integration might be reflected in the contribution rates — see Paragraph 8.12.5). In addition, the figures include members of public sector schemes, many of whom pay modified PRSI and so have no entitlement to Social Insurance benefits. Considering the ESRI figures, the report on the National Pensions Policy Initiative, *Securing Retirement Income,* concluded that the vast majority of members of defined benefit schemes in the private sector have their benefits integrated with the Social Welfare scheme.[99]

8.12.4 The IAPF Benefits Survey, 1998 indicates that 71% of schemes integrate their benefits with the State Social Insurance pension.[100] It comments that most defined benefit schemes are integrated, and 69% of defined contribution schemes ignore the State Social Insurance pension. While the proportion of schemes not integrating has been increasing slowly, the report adds that this in part reflects the increasing number of defined contribution schemes.

8.12.5 On the question of the relationship between defined contribution schemes and the Social Insurance system, *Securing Retirement Income* notes that although defined contribution schemes are generally not directly integrated with Social Welfare pensions, in practice the rate of contribution being paid under such schemes will usually have regard to the fact that members will have an entitlement to a Social Welfare pension.

8.12.6 Of the firms which responded to the question about integration arrangements for *part-time employees*, almost 75% integrate their pension benefits with the Social Insurance system, 10% do not, and 15% said that their scheme did not cover part-time employees. Virtually all of the schemes that do integrate pension benefits for part-time employees use the same multiple of OACP as is used for full-time employees.

8.12.7 Where a scheme integrates the pensions of part-time staff with the Social Insurance system there are two main methods for achieving the integration when calculating pension benefits (see Paragraph 11.7.5). Over 80% of these schemes use a method in which pensionable

[98] Hughes, G. and Whelan, B.J., *Occupational and Personal Pension Coverage, 1995,* ESRI (1996) p. 66.
[99] The Pensions Board*, Securing Retirement Income* (1998), p. 55.
[100] *IAPF Benefits Survey*, 1998 (1999), p. 9.

remuneration is taken as the equivalent full-time salary and pensionable service is actual service (i.e. two years working half-time is taken as one full year's pensionable service). The remainder use the second method in which pensionable remuneration is the actual salary earned and pensionable service in any one year is counted as a full year for pension purposes regardless of hours worked (i.e. a year of half-time work is taken as one year's pensionable service). This latter approach is the one followed in the public service in the limited number of cases where part-time service is pensionable.

8.12.8 The 1995 ESRI survey found that only one-eighth of the 5,700 schemes which have integration arrangements for their full time employees integrate the pensions paid to part-time staff with the Social Insurance system, one-tenth do not integrate them, and over four-fifths do not provide any pension coverage for part-time employees.[101]

8.12.9 Information on integration arrangements was limited, and the ESRI stated that the figures should be treated with caution. However, they estimated that less than 100 small firms integrate the pensions of part-time employees by using the first method (i.e. using pensionable remuneration as the equivalent of full-time salary and pensionable service as actual service) whereas this method is used by around 200 large firms. About 100 small schemes use the second method of integration whereby pensionable pay is the actual salary earned and pensionable service in any one year is counted as a full year for pension purposes. This method appears to be used by less than 100 large schemes.[102]

8.13 Dependants' benefits

Death-in-service benefits

8.13.1 In the civil service, the multiple of salary paid as a lump sum in the case of death-in-service varies between 1 and $1\frac{1}{2}$ times salary depending on length of service. The spouse's pension entitlement is 50% of the pension the member would have received had he or she served until age 65.

8.13.2 The ESRI analysis of death-in-service benefits for the Commission is based on replies received in respect of 83 schemes of large firms. The survey found that all schemes provide a death gratuity — 67 of them pay a multiple of between 2 and 4 times salary — to married and single members. In 60% of schemes, a spouse's pension is payable on death-in-service. No details are given on the percentage of pension actually paid. While not specifically asked in the ESRI survey, it is likely that a number of the firms not paying a spouse's pension make provision for payment of a larger death-in-service gratuity.

8.13.3 The IAPF Benefits Survey, 1998 indicates that a death-in-service gratuity of 2 to 4 times salary is generally payable in the private sector. The typical spouse's pension is 50% of the pension which would have been payable to the member had he or she served until normal retirement age. The following is a breakdown from the IAPF survey of the level of spouse's pension payable on death-in-service.[103]

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[101] Hughes, G. and Whelan, B.J., *Occupational and Personal Pension Coverage, 1995,* ESRI (1996) p. 69.
[102] Hughes, G. and Whelan, B.J., *Occupational and Personal Pension Coverage, 1995,* ESRI (1996) pp. 70-71.
[103] *IAPF Benefits Survey*, 1998 (1999), p. 11.

Table 8.3 1998 IAPF survey — spouse's pension on death-in-service

Proportion of member's pension	Percentage of schemes (%)
50% of prospective pension	67
Greater than 50%	12
No spouse's pension	16
Percentage of salary	5

8.13.4 The principal difference between a spouse's pension payable in the civil service and the private sector is that in the case of the latter the pension is generally calculated on a higher base level, i.e. two-thirds of pensionable salary compared with one-half of pensionable salary in the civil service (for maximum service).

Benefits on death after retirement

8.13.5 In the civil service, a spouse's pension of 50% of the rate of member's pension is payable, but, as noted above, it is determined by reference to a lower percentage of pensionable salary when compared with the private sector.

8.13.6 The ESRI report for the Commission and the IAPF Benefits Survey indicate that over 90% of the schemes examined pay a spouse's pension in circumstances where the member dies after retirement. The IAPF survey reports that 78% of such schemes provide a spouse's pension of 50% of member's pension, while 15% pay an amount greater than 50%.[104]

8.13.7 Only 40% of the large firms surveyed provide a pension for the member's dependent children on death-in-service or death after retirement. The corresponding figure in the IAPF survey is only available for death-in-service benefits and indicates that pensions for dependent children are provided for in 63% of schemes. These figures compare unfavourably with the civil service, where children's pensions are payable in almost all cases.

8.13.8 Most private sector schemes guarantee payment of the retirement pension for a period up to five years after retirement. If the former member should die during this period, the balance of pension due is generally paid to the deceased's estate. This provision does not generally apply in the public service.

Dependants' pensions — main points

8.13.9 In conclusion, while there is great variation in private sector practice, the main points of difference between the private sector and the public service as regards dependants' benefits are:

- the death gratuity in the private sector is generally larger than that payable in the public service;
- in many cases, private sector schemes pay a spouse's pension which in percentage terms is higher than that payable in the public service;
- all public service schemes include spouses' and children's benefits; this is not necessarily the case in the private sector;
- spouses' pensions in the private sector are increased on the same basis as other private sector pensions, which is less favourable than the public service policy of increases in line with pay (see Section 8.17);

[104] *IAPF Benefits Survey*, 1998 (1999), p. 12.

- in the private sector, it is not unusual for a smaller spouse's pension to be paid on death-in-service or death after retirement if the age differential between the member and his or her spouse is greater than 10 years. No such provision applies in the public service;
- many private sector pension schemes allow discretion (where the rules permit) as to whom the pension should be paid, i.e. a spouse or common-law spouse. Public service schemes restrict payment to the legal spouse only;
- in some private sector schemes, the spouse's pension is paid for life, even if the person remarries. However, in the public service, the spouse's pension normally ceases on remarriage or cohabitation.

8.14 Early retirement due to ill health

8.14.1 The civil service scheme and almost all schemes in large firms provide benefits if a member retires early due to ill health. In the civil service, pension is based on service accrued to date plus some fraction (usually a maximum of six and two-thirds years) of prospective service to age 65. A quarter of the schemes of large firms calculate the benefit by including all prospective service to normal retirement age. Of the balance, 15% provide a pension based on actual service accrued to date of retirement, with no actuarial reduction in respect of early payment of benefit, while 33% provide a pension based on actual service to date of retirement, with actuarial reduction. The remaining 27% of schemes refund the value of the fund in a defined contribution scheme, pay an amount based on a percentage of salary, or pay an amount determined by permanent health insurance plans.

8.14.2 In the civil service scheme, the employee must be incapable of doing his or her normal job in order to qualify for an ill health pension. The same approach applies in the majority of schemes in large firms which provide ill health cover (many firms operate permanent health insurance or income continuance plans instead), although a significant number apply more stringent tests, requiring that the member be incapable of doing any job before qualifying for ill health retirement.

8.14.3 The civil service scheme and one-third of schemes in large firms require the member to have completed a minimum period of service before becoming eligible for an ill health pension. The remaining two-thirds of large private sector schemes do not have a minimum service condition. In the civil service scheme, the minimum period of service required is five years. Of the schemes in large firms which have a minimum service requirement, over two-fifths require five years' service, one-fifth require between eight and ten years' service, and almost two-fifths have less stringent requirements with service of one to two years being sufficient to qualify.

8.14.4 Employers may make provision for retirement on grounds of ill health through permanent health insurance or income continuance plans. Over half of the large employers surveyed provide such plans. The civil service does not make separate provision as retirement on grounds of ill health is catered for within the pension scheme.

8.14.5 The IAPF Benefits Survey, 1998 found that 94% of participating companies provide disability or ill health retirement benefits, with 67% providing benefit increases automatically during payment.[105]

[105] *IAPF Benefits Survey*, 1998 (1999), p.16.

8.14.6 The IPT Executive Benefits Survey, 1997 indicated that insured disability benefits were provided by 90% of the companies surveyed. These benefits are payable after a deferred period which, in 89% of cases, is 26 weeks. Disability benefit formulae are generally expressed as a percentage of salary. The level of insured disability benefit is typically two-thirds and three-quarters of salary with a deduction of once the rate of State disability benefit. The majority of disability benefits are increased when in course of payment, with 5% per annum being the most common rate of increase.

8.15 Early retirement other than on grounds of ill health

8.15.1 Established and non-established civil servants are required to retire at age 65, but the former may retire with immediate pension at any age after age 60 if they have at least five years' service (see Section 8.7). There is no provision to retire before age 65 for the latter group. Almost all schemes operated by large firms allow members to retire earlier than normal pensionable age, but usually with some form of actuarial reduction. The minimum age at which a member can take early retirement is 50 for 86% of schemes, 55 for 7% of schemes, and 60 for 4% of schemes. There is no minimum service requirement to qualify for early retirement in 47% of schemes, while 38% require one to five years' service, and 15% require service greater than five years.

8.15.2 There is some variation in the basis for payment of early retirement pensions by large firms, most of which apply some form of actuarial reduction. Almost 30% of schemes pay the pension entitlement accrued up to the date of early retirement reduced by 4% per annum, or some other factor more favourable to the member, to take account of the longer period over which the pension is to be paid. Nearly 37% of schemes pay the benefit on a similar basis, but use a less generous reduction factor. Only 8% pay the pension accrued to date without actuarial reduction. About 5% of schemes pay a benefit which depends on the length of service, and nearly 10% of schemes (which are defined contribution) return the value of the accumulated fund. About 10% of schemes use some other method. Although respondents were not asked about the circumstances in which the pension accrued to date would be paid without actuarial reduction, it is likely that private sector firms would only adopt this basis of payment in cases of redundancy or inability to work satisfactorily.

8.15.3 The IAPF Benefits Survey, 1998 indicates that 21% of participating firms provide members with early retirement benefits on a *no discount basis* (or other enhanced basis) as a member entitlement, while 24% provide early retirement benefits on a no discount or other enhanced basis by discretion.[106]

8.16 Early leavers

8.16.1 Where a member opts not to transfer his or her pension rights to another pension scheme on leaving employment, the Pensions Act, 1990 requires the scheme to adopt a specified or more favourable formula in relation to the uprating of benefit to preserve the early leaver's right to a deferred pension. The civil service scheme operates a more favourable formula than that specified in the Pensions Act through uprating the benefit in line with increases in the salary of the grade occupied by the member before leaving service, while 91% of the schemes of large firms operate the Pensions Act formula.

[106] *IAPF Benefits Survey*, 1998 (1999), p. 15.

8.16.2 In the event of death of the early leaver before the age at which the pension becomes payable, the civil service scheme pays a pro rata pension to his or her spouse and surviving children. Only a small minority of schemes in large firms pay a pension where the early leaver dies before retirement age. The favoured course of action for almost 80% of schemes in large firms is to pay the actuarial value of the preserved benefit.

8.16.3 In relation to preservation of benefits, the Pensions Act does not cover service given before passage of the Act.[107] The civil service scheme and most schemes in large firms preserve early leavers' benefits earned before 1991 on a voluntary basis. Over a third of schemes in large firms, revaluing on a voluntary basis, operate the Pensions Act formula, while 57% do not provide for any revaluation in relation to pre-1991 service. As noted in Paragraph 8.16.1, the civil service scheme revalues all preserved benefits in line with pay.

8.16.4 An alternative to preservation is the payment of transfer values in respect of pensionable service earned in the first employment. In the civil service scheme, the public service transfer network allows employees to transfer their pension entitlements within the public service. Prior to 1996, a person entering the civil service from the private sector could use a transfer value from the private sector scheme to secure some service credit under the civil service scheme. However, as a result of an amending legislative provision to the Pensions Act, 1990,[108] it is no longer possible to pay a transfer value into an unfunded scheme. It is expected that a further legislative amendment to address this prohibition on payment of transfer values to unfunded schemes will be made shortly.

8.16.5 Almost all the schemes of large firms accept transfer values in respect of service before the passage of the Pensions Act. The benefits that may be granted in respect of transfer values comprise additional pensionable service in 47% of schemes, a defined contribution or other benefit in 39% of schemes, and a fixed pension — which may be indexed in line with the Consumer Price Index or grade increases — in the remaining 14% of schemes.

8.17 Pension increases

8.17.1 The civil service scheme provides increases in pension in line with changes in the pay of serving staff. In large schemes in the private sector, the basis for increasing pensions, according to the ESRI survey for the Commission, is as indicated in Table 8.4.

Table 8.4 Basis on which increases are made to pensions in payment

Type of Increase	% breakdown
Guaranteed increases, with or without review	39
Discretionary increases, with or without review	33
No increases	20
No pensioners or other basis*	8

* increases are granted on some other basis than those mentioned above.

[107] The Pensions Board Report, *Securing Retirement Income*, recommends for those leaving service after 1 January 2001 that preservation of benefits for pre-1991 service should be introduced by 1 January 2001, revaluation by 1 January 2006, and that funding standards in respect of these must be fully met by 1 January 2011. This recommendation was accepted by the Government, and it is expected that appropriate legislative amendments will be introduced shortly.

[108] The original Section 34(3)(a) of the Pensions Act, 1990 was substituted by the wording in Section 12(c) of the Pensions (Amendment) Act, 1996.

8.17.2 Over 45% of schemes in large firms that provide guaranteed increases in benefits have a rate of increase specified as a percentage of pension. Another 45% match the increase in the Consumer Price Index either to the actual or a maximum figure, and the remaining schemes grant increases on some other basis. Almost all of the schemes that provide a guaranteed percentage increase apply a maximum rate of 3% or 4% per annum. Schemes that match the Consumer Price Index up to a maximum figure generally stipulate that the maximum increase they will pay is 4% or 5% per annum.

8.17.3 The IAPF Benefits Survey, 1998 indicates that 85% of participating schemes provide pension increases, although over half of these are on a discretionary basis. The average increase over the previous 12 months, for schemes where an increase was provided, was 2.7%. This was a little higher than price inflation, reflecting fixed increases for some schemes at 3% or 5% per annum and salary parity for a smaller number of schemes (the IAPF include the schemes of a number of commercial state companies amongst its membership).[109]

8.17.4 The position detailed above reflects generally the defined benefit scheme experience. In a defined contribution scheme, the member will have a choice at retirement as to what type of annuity he or she wishes to purchase. A decision to opt for an escalating annuity (which provides for regular pension increases, e.g. fixed increase of 3% per annum) would mean a lower initial pension as compared with a flat-rate annuity.

8.18 Additional voluntary contributions

8.18.1 In the private sector, if scheme rules allow, members who would not otherwise qualify for full pension may have a facility to make additional voluntary contributions (AVCs) to provide for additional benefits either within the scheme or in a separate scheme. In the civil service, there is provision to purchase notional years of service within the scheme and there are a number of separate union-sponsored AVC schemes. In the private sector, almost all schemes in large firms make provision for payment of AVCs. Nearly 55% of AVC schemes are separate from the main pension scheme. Virtually all of these are defined contribution schemes. We give further details of practice in the private sector and the public service in relation to AVCs in Chapter 12.

8.18.2 The IAPF Benefits Survey, 1998 indicates that 96% of companies surveyed provide an AVC facility to enhance benefits. The vast majority of these schemes (86%) are defined contribution in nature, with only 14% being defined benefit.[110]

8.19 Professional, technical and specialist added years

8.19.1 Under a scheme applying to established civil servants recruited through the Civil Service Commission, notional added years of service are given to professional, technical, and specialist civil servants where the required minimum qualifications and/or experience for the job would have precluded appointment before 25 years of age. This enhancement of benefits is provided without cost to civil servants in relevant professional posts.

8.19.2 Similar notional added years arrangements are found in the local authority, health service and university sectors. In many cases, the arrangements are wider than those applied in the civil service (see Section 22.3).

[109] *IAPF Benefits Survey*, 1998 (1999), p. 13.
[110] *IAPF Benefits Survey*, 1998 (1999), p. 18.

8.19.3 While not directly equivalent, it is likely that arrangements which aim to enhance the level of pension entitlement apply in a number of *top hat* private sector schemes (e.g. better pension accrual rates).

8.20 Financing arrangements

8.20.1 The civil service scheme is financed on a pay-as-you-go basis out of current government revenues. The schemes of large firms are pre-funded, in accordance with the requirements of the Pensions Act.

8.20.2 The civil service scheme is statutory and is administered by various government departments under the aegis of the Department of Finance. Private sector schemes, on the other hand, are generally run by trustees who operate independently of the employer.

8.20.3 Death-in-service benefits offered by the pension schemes of large firms are covered by a contract with an insurance company in 54% of schemes, paid out of the fund without insurance in 33% of schemes, and partly self-insured, partly covered by insurance in 12% of schemes.

8.21 Trends in private sector arrangements.

8.21.1 The Commission has presented above a detailed comparison of benefit terms in public service and private sector occupational pension schemes. In this Section, we review the trends which are evident in private sector pension provision. The trends considered are:

- move to defined contribution;
- fall in occupational pension coverage;
- use of AVCs;
- claims for improvements in pension schemes;
- new tax provisions for pensions of self-employed (and for AVCs).

8.21.2 The principal trend in private sector occupational pension provision over the last 10 years has been a gradual but steady move away from traditional defined benefit schemes towards **defined contribution schemes**. This is particularly noticeable amongst smaller companies and companies in the financial sector, and is reflected in the most recent (1998) IAPF Benefits Survey. In 1991 and 1994, according to the survey, around 94% of all occupational plans were defined benefit. However, by 1998, the proportion of defined benefit plans had fallen to 84%, with 16% defined contribution plans. The IAPF comments that there has been a marked increase in the proportion of defined contribution schemes, but that while many of the more recently established schemes are defined contribution, there is little evidence of schemes switching from existing arrangements. The IAPF acknowledges, however, that some companies with defined benefit main schemes have established defined contribution schemes for atypical employees or for new employees.[111]

8.21.3 The increasing incidence of defined contribution schemes is also apparent in the Pensions Board's scheme registration figures. At the end of 1999, there were considerably more people in defined benefit schemes, as compared with defined contribution schemes, although membership of the latter was growing much more rapidly (see Table 8.5). It should be noted that almost all of

[111] *IAPF Benefits Survey*, 1998 (1999), p. 3.

the growth was in smaller defined contribution schemes, i.e. those with a membership of less than 50 members.

Table 8.5 Pension scheme membership, 1993—99 (excluding unfunded public service schemes)

Year	Defined benefit (DB) subject to the funding standard	Defined contribution (DC)	Total (DB+DC)	DC as % of Total
1993	205,386	33,984	239,370	14.2
1994	203,305	39,902	243,207	16.4
1995	203,002	41,757	244,759	17.1
1996	208,310	46,304	254,614	18.2
1997	212,057	53,788	265,845	20.2
1998	207,227	68,579	275,806	24.9
1999	214,306	84,386	298,692	28.3

Source: The Pensions Board (one member schemes are excluded from the figures).

8.21.4 In the public sector, defined contribution schemes have been introduced by a few of the commercial state companies either for newly appointed fixed-term contract employees or for newly created business units. Some of the universities operate defined contribution schemes for personnel employed on a contract basis (see Paragraph 3.6.30).

8.21.5 A second identifiable trend in the private sector is the **fall in the numbers covered for occupational pensions as a proportion of the workforce**. ESRI surveys indicate that the level of pension coverage has fallen from 54.4% in 1985 to 52% in 1995.[112] It appears that this decline has occurred in private and commercial public sector schemes as the coverage rate in the non-commercial public service remained static over the period in question. It is likely that a change in the types of jobs available may account for some of the decline. In this respect, the more recent ESRI report indicates that between 1988 and 1995 the number of regular full-time jobs in the economy increased by 8% while the number of part-time jobs and the number of occasional jobs increased by 80% and 76%, respectively.

8.21.6 As part of its strategy to promote retirement saving, the Pensions Board has recommended in the National Pensions Policy Initiative that a new type of pension product, the Personal Retirement Savings Account (PRSA) be introduced.[113] A PRSA is an investment account which would be owned by an individual and would comprise units in investment funds held with, and managed by, an approved PRSA provider and which could be transferred from one provider arrangement to another. The proceeds from PRSAs would be available, as with any defined contribution type arrangement, to provide benefits on death or retirement. PRSAs would be designed to meet the needs of a flexible labour market without undermining the aspects of current provision which are considered valuable and sound (for example, company defined benefit schemes). The Pensions Board believes that because of the expected simplicity of PRSAs, they are likely to supplant some existing defined contribution and additional voluntary contribution arrangements, but would not result in an inferior quality of pensions product. It is expected that a new Pensions Bill to provide a legislative framework for the early introduction of PRSAs will be published in late 2000/early 2001.

[112] Keogh, G. and Whelan, B., *National Survey of Occupational Pension Schemes,* ESRI (1985); Hughes, G. and Whelan, B.J., *Occupational and Personal Pension Coverage, 1995,* ESRI (1996).

[113] The Pensions Board, *Securing Retirement Income* (1995), p. 127.

8.21.7 A third trend in private sector schemes has been the increasing use of **AVC schemes**. Company sponsored AVC schemes have become an integral part of pension provision (see Section 12.14); these schemes are designed in such a way as to offer employees a competitively priced means of enhancing their own pension situation, as compared with the use of free-standing arrangements.

8.21.8 Fourthly, it would appear that over the past few years there has been an increasing number of **claims for improvements in company pension schemes** in the private sector, for example, in relation to integration with the State Social Insurance system.[114] This may be because such claims provide significant scope for unions to seek to improve members' remuneration without going outside the terms of national agreements. The willingness of companies to agree pension improvements may be linked at least in part to the healthy financial state of pension funds at present and to possible moves to introduce potentially less expensive defined contribution schemes for new entrants (see above).

8.21.9 Finally, **significant legislative changes to tax provisions relating to pensions for the self employed and proprietary directors** were introduced in the Finance Act, 1999. These changes covered two areas:

(i) the old rule which required pensioners in these categories to take out an annuity has been abolished. Under the new rules, it is now possible, subject to certain conditions, to choose between purchasing an annuity or placing the accumulated fund in an *Approved Retirement Fund* (ARF) or having the accumulated fund paid over to the individual, subject to certain requirements;

(ii) the Act has increased significantly the tax deductible amounts which can be set aside each year to fund retirement benefits. The amounts contributed can now be up to 30% of taxable income, depending on age and occupation.

8.21.10 Under the Finance Act, 2000, the first of these legislative changes will now apply to benefits arising from AVC schemes. The normal Revenue limits applying to the making of additional voluntary contributions, such as the limit of 15% of remuneration for tax relief, will continue to apply (see also Paragraph 12.12.1).

8.22 Conclusions

8.22.1 Public service pension arrangements compare favourably with those available in the private sector. Our conclusions on the comparison of pension terms are summarised in Paragraph 8.1.4.

8.22.2 An important difference between the respective arrangements appears to be the much greater awareness in the private sector about the cost of occupational pensions. This may be due primarily to the requirement to pre-fund. A consequence of this is a more controlled approach to areas such as early retirement, where cost neutrality is the perspective generally adopted, and pension increases, where, if the scheme provides for increases in the first place (20% of schemes do not), they are usually based on changes in the Consumer Price Index, subject to a cap of between 3% and 5% per annum.

[114] See *Industrial Relations News*, 9 September 1999, pp. 2-3; 13 May 1999, p. 6; 22 April 1999, pp. 3-4, 12-13.

8.22.3 By comparison with the public service, private sector pension schemes appear to make greater efforts to communicate benefit entitlements, to offer members a range of pensions and retirement choice, and to provide flexible AVC arrangements enabling members to fund in advance towards their own retirement decisions.

8.22.4 The most significant long-term trend in the private sector is the move towards defined contribution schemes. The principle reason for this is that such schemes enable companies to maintain a tighter control on costs, as contribution levels are known (normally a percentage of income) and, most importantly, fixed. To a very large degree, the risk is passed onto the employees and the company has no responsibility for the level of pension benefits payable, which is largely dependent on how successfully the funds have been invested and on annuity rates at retirement. This is in contrast to defined benefit schemes, which provide a guaranteed level of benefit. With defined benefit, the employer cannot know the exact extent of the full pensions liability until payment of pension has actually ceased. There is evidence, too, that companies pay less into defined contribution schemes than is necessary, on average, to maintain defined benefit schemes (see Paragraph 14.4.9). Thus, a move to a defined contribution scheme (where a defined benefit scheme was already in existence) will most likely entail a reduction in company pension costs and a reduction in the level of benefits.

8.22.5 A further factor in the growth of defined contribution schemes is their popularity with employees, particularly young mobile employees. In the new, increasingly flexible work environment, defined contribution schemes are seen as more portable and easier to understand than defined benefit schemes. The unprecedented growth in stock markets, over the past decade in particular, impacts directly on the balance on the individual's pension account and must also be a relevant consideration.

8.22.6 We examine the private sector approach to AVCs in more detail in Chapter 12. We discuss defined contribution pension schemes further in Chapter 14 and examine the arguments for and against introducing this form of pension scheme design in a public service context.

CHAPTER 9

Public Service Occupational Pension Arrangements in Other Countries

9.1 Introduction

9.1.1 In our Interim Report, the Commission carried out a preliminary review of current public service pension arrangements and developments in other countries in Europe. In this Chapter, we present a more detailed analysis of the public service occupational pension arrangements of a number of countries which we considered particularly relevant — namely, the UK, Germany, Sweden and the Netherlands.[115] We also carry out a more widely-based comparative analysis under a range of headings — retirement age and early retirement, integration with the state social security system, level of benefits, employee contributions, pensions for part-time employees, pension increases, and financing and administrative arrangements. Finally, we identify trends in changes to pension arrangements implemented in the recent past.

9.1.2 For the purposes of the comparative analysis, it is important to acknowledge that pension arrangements in any range of countries will reflect the comparative economic, social and political conditions in those countries. Pensions for public servants may be linked with the national social security system, or, if independent of it, may reflect social security provisions and conditions, for example, in relation to retirement age. In addition, pensions form part of public service conditions of employment and represent agreements reached between public service unions and employers in each country. For these reasons it is difficult in a widely-based review such as this to make direct comparisons between pension and retirement arrangements in Ireland and those in other countries. However, certain features and trends can be identified that provide a helpful backdrop against which to evaluate public service pension arrangements in Ireland, and which point the way to possible improvements.

9.1.3 The Commission visited each of the four countries selected, in most cases meeting representatives of relevant government departments, negotiating agencies, and public service unions.[116] Each of the countries selected had its own particular value from the perspective of our examination. The experience of the *United Kingdom* was useful because of similarities in pension arrangements arising from the shared history of the respective public services, and the ease in making direct comparisons with schemes in this country. *Germany* was interesting because of its plans to address the increasing costs of public service schemes which will arise over the next 25 years due to heavy recruitment in the 1970s. *Sweden* represented a radically different approach to public service pension provision. Its State Pension Scheme — which provides the larger part of the total pension for retired public servants — has been restructured and is now defined contribution in nature. The expectation of possible cost difficulties in the future was the main

[115] The information on public service pension arrangements contained in this Chapter is based on the position as it existed in each country at the time of the Commission's visits (i.e. over the period 1997-99). Subsequent changes in pension arrangements may not be reflected in this Chapter.

[116] We are very grateful for the invaluable assistance received from all of the parties met by the Commission. (Our detailed acknowledgements are presented at the start of this Report.)

stimulus for change. In the *Netherlands*, the public service pension scheme is pre-funded and has been since the 1920s. In recent years, the fund has been privatised and now operates in a similar way to private sector funds. The social partnership model which applies in the Netherlands makes the experience there of particular relevance.

9.1.4 In addition to these countries, we report briefly on pension arrangements for federal government employees in the *USA*, and for teachers covered by the Massachusetts Teachers' Retirement System.

9.1.5 A shared concern which we identified amongst the relevant parties — employers, unions and government — in each of the countries visited was the need to secure the long-term financing and integrity of public service pension schemes in the context of coping with the implications of demographic ageing generally. A second concern was to ensure that pension terms were capable of being modified and adapted to meet changing operational requirements and to address increasing demands by individual public servants for greater control over their own retirement decisions.

9.2 United Kingdom

9.2.1 For historical reasons, the basic provisions of many public service schemes in the UK are similar to those in this country. The state social security systems — insofar as pensions are concerned — are also quite similar, apart from the fact that the basic state pension is comparatively higher in Ireland, and that the UK have an additional State Earnings Related Pension Scheme (SERPS). The civil service pension scheme is typical of a UK public service scheme. Service of forty years is required to qualify for maximum pension. Pension accrues at the rate of 1/80th of pensionable remuneration for each year of reckonable service up to a maximum of 40/80ths, i.e. one-half of pensionable remuneration.[117] Lump sum accrues at the rate of 3/80ths of pensionable remuneration for each year of pensionable service up to a maximum of 120/80ths, i.e. $1\frac{1}{2}$ times pensionable remuneration. The scheme is non-contributory for retirement benefits (other public service schemes are contributory, e.g. the local government scheme), although there is a member contribution of $1\frac{1}{2}$% of salary for spouses' and children's benefits.[118]

9.2.2 The civil service scheme, like most other public service schemes in the UK, is financed on a pay-as-you-go basis — the exception is the local government scheme which is funded. Unlike the position in Ireland, there are systems in place to record the accruing cost of pensions for serving staff and to monitor the medium- to long-term cost of pensions. The costing of pension schemes and of changes to pension benefits is carried out by the Government Actuary's Department, which has been in existence since 1919. From 1995 on, departments and agencies have been required to pay for pensions through employer contributions known as accruing superannuation liability charges (ASLCs). ASLCs are calculated on a salary-banded basis and are based on the principle of charging for pension costs as they are accrued by members of the scheme, rather than when expenditure on benefits is incurred. The remuneration package of civil servants, therefore, includes not only pay but also the pension cost carried by the employer. The ASLC mechanism helps make this pension cost clear to employers and employees.

[117] It is possible to build up in excess of 40 years' pensionable service on working beyond normal retirement age (which is subject to local management approval), up to a maximum of 45 years' pensionable service.

[118] In mid-2000, the principles of a new defined benefit scheme for civil servants were agreed by the Cabinet Office, trade unions and employers. The scheme, which is scheduled to be introduced in 2002, will offer more favourable benefits at the expense of higher contributions from members. New entrants are to be offered the choice of joining the improved defined benefit scheme or a new defined contribution scheme (the details of which have not yet been agreed).

9.2.3 The actuarial approach to costing unfunded schemes is taken further in the Teachers' Superannuation Scheme (and the National Health Service Superannuation Scheme) which operates a *notional fund* arrangement, involving *notional* investments in Government and other securities (including equities), primarily as a means of determining appropriate rates of employer contributions. Once every five years, the Government Actuary's Department carries out a valuation of each notional fund. A modification of the employer contribution may be made to allow for any difference between the value of the assets and the value placed on the accrued liabilities at the date of the valuation. The contributions determined in this way recognise the timing difference between receipt of contributions and the payment of benefits and therefore allow for investment income even though assets are not being set aside specifically for the liability.

9.2.4 The policy has been for public service schemes to be unfunded, although the local authorities are an exception. There is a single uniform Local Government Pension Scheme, the finances of which are operated through a large number of separate funds.

9.2.5 Notional funding and the use of ASLCs are seen as a means of introducing some of the disciplines of funding without the need to provide for actual funding. One example is found in the area of premature retirement: arrangements have been introduced to ensure that while normal accruing pension costs are charged to the employer through the contribution rate, the additional costs arising from the decision to retire an employee early (e.g. for efficiency or restructuring reasons) must be met by the employer through an up-front payment of the full capital cost involved.

9.2.6 A benefit of this arrangement is that it ensures that there is an appreciation of the real cost of early retirement. An organisation is less likely to introduce a costly early retirement package if the full cost has to be borne from within its own resources. Accordingly, it provides the necessary discipline to allow local management to implement early retirement policy. Despite this, there is concern about the extent and scale of premature retirement, particularly in relation to teachers and local authority staff. However, government authorities appear to be of the view that a more centralised approach would undermine the *value for money* philosophy central to public service management structures and would also operate against the concept of a liberalised employment market. Certain changes to pension charges for early retirement have been made to address the shortcomings in existing arrangements.

9.2.7 In the civil service, normal retirement age is 60.[119] However, there are a number of provisions for early retirement below age 60, as follows:

- **approved early retirement**: where either a department with surplus staff seeks volunteers who have five or more years' service or an individual over 55 with 25 or more years' service seeks early retirement and management agrees this would contribute to overall efficiency, immediate payment of accrued pension benefits can be made with no actuarial reduction;
- **flexible early retirement**: management can invite individuals to leave early on grounds of limited deployment options or limited efficiency or to assist with restructuring. No compulsion is involved. Employees with more than five years' service are entitled to

[119] In a recently published Cabinet Office Report, *Winning the Generation Game – Improving the Opportunities for people aged 50-65 in Work and Community Activity* (April 2000), it is recommended that each Government Department should look at the case for allowing its civil servants to retire at age 65. The Report also recommends raising the minimum age at which an immediate tax-approved occupational pension is payable from 50 to 55 between 2010 and 2020.

immediate payment of benefits with service enhanced by up to 6 and 2/3rd years. There is no compensation payment (see compulsory early retirement below);

- **compulsory early retirement**: applies to compulsory retirements (apart from inefficiency) and all redundancy, whether compulsory or voluntary. An employee with five or more years' service is entitled to immediate payment of benefits with service enhanced by up to 6 and 2/3rd years, plus up to six months' pay as compensation payment;
- **actuarially-reduced retirement**: staff aged 50 and over who ask to retire receive immediate payment of actuarially reduced benefits to allow for the longer time these are likely to be paid.

9.2.8 A civil service AVC scheme was introduced in 1989. The scheme is contracted out and is currently provided by two life assurance companies. The AVC arrangements are reviewed annually by the Government Actuary's Department to ensure they are performing up to expectation. The negotiation of special AVC terms for all civil servants has resulted in lower charges than if contributions were made to free-standing AVC schemes.

9.2.9 There are other significant differences in public service pension arrangements in the UK compared with this country. For example, pensions are increased in line with the Retail Price Index rather than in line with salary changes. We summarise the main points of difference in Appendix 9.1.

9.2.10 The above analysis focuses mainly on standard public service pension terms which apply to groups such as civil servants, local authority employees and teachers. However, the most significant changes in pension terms in recent years have taken place in a number of the special group schemes, as outlined below:

- **Prison Officers and Mental Health Officers** (including psychiatric nurses) recruited since 1987 and 1995, respectively, have standard public service pension arrangements, i.e. they serve until age 60, and must accrue 40 years' service to qualify for maximum pension. *Fast accrual* terms (i.e. the entitlement to retire from age 55 with maximum pension after 30 years' service) apply to officers employed before these dates;
- **General Nurses** recruited since 1995 have standard public service pension terms. Nurses employed before this date may retire from age 55 once they have a minimum of 35 years' service (nurses require 40 years' service to qualify for maximum pension);
- **Police and Fire Service** employees have fast accrual pension terms. Both schemes are currently under review with consideration being given to increasing from 30 to 35 years the period of service required for maximum pension.

A more detailed comparison of the pension terms of the above groups and their equivalents in this country is contained in Appendix 9.2.

9.2.11 A source of concern within the public service generally is the increasing number of early retirements on grounds of ill health. This problem is particularly pronounced in the Police and Fire Services. A consultation document published as part of the current review of these schemes comments that the proportion of police officers retiring early on medical grounds is unacceptably high and is not justified by the specific additional risks faced by police officers. Currently, ill health retirements averaged across all police forces account for about 45% of retirements, significantly above the levels achieved by some individual forces.[120] The *spread* between police forces ranges

[120] Home Office, *Police Pensions Review — A Consultation Document*, The Stationery Office (1998).

from a low of 17% to a high of 70%. The consultation document suggests that there is no correlation between the size and nature of a force and the number of medical retirements. It adds that these variations raise serious questions about the quality of management and medical decisions in forces which are out of line with the best performers.

9.2.12 Similar concerns have been expressed about ill health retirements in the Fire Service scheme. Statistics for the three years to 1996-97 indicate that 72% of all retirements were on medical grounds with considerable variations in the level of ill health retirements between individual brigades.

9.2.13 Public service pension administrators, including those of the civil service, local authority and teachers' schemes, have suggested that a tighter and more focused management of ill health, particularly stress related illnesses, with a greater emphasis on the role of occupational health services, is the key to keeping numbers of ill health early retirements at a low level.

9.2.14 Public servants in the UK are entitled to receive the basic state social security pension, but unlike the case in Ireland their occupational pensions are not subject to integration. The public service schemes are contracted out of SERPS (this is possible once the benefits provided by the occupational scheme are on a par with or better than SERPS), and so a reduced rate of social security contribution is payable.

9.3 Germany

9.3.1 The German public service comprises two types of employee: civil servants and public employees. The former make up one-third of the public service and appear to be equivalent to established civil servants in this country. They are covered by a special law, and in effect have permanent status. The latter group do not have the same security of tenure as civil servants and appear to be broadly equivalent to non-established civil servants in Ireland.

9.3.2 The difference in the employment status of the two groups is reflected in their pension arrangements. Civil servants are catered for in a stand-alone pension scheme and, accordingly, have no state social security pension entitlements. Public employees, on the other hand, are covered by the social security system, and have a supplementary pension scheme which is subject to collective bargaining. The distinction is broadly equivalent to that which has existed in Ireland between public servants in modified and full class PRSI.

9.3.3 Civil servants are provided for on the basis of the extended earnings principle, i.e. they are employed for life, and are paid a pension when they reach old age or otherwise become unfit for work. Thus, the pension is not paid in return for contributions made by the individual or calculated on the basis of those contributions. From a legal perspective, the pension is regarded as a form of *maintenance*. A civil servant must have five years' service to qualify for pension, otherwise the years worked count towards the state social security pension. The scheme is non-contributory, except that account is taken of the pension benefit payable when salary levels are being set. It is financed on a pay-as-you-go basis.

9.3.4 Retirement age is 65, although it is possible in certain circumstances to remain in employment until age 68. Police officers must retire at age 60. The earliest age at which a civil servant can retire is age 63 (until recently, it was age 62); however, a reduction in pension of 3.6% is applied for each year of retirement before age 65 (maximum reduction 7.2%). Retirement pension accrues at the rate of 1.875% of pensionable salary for each year of service up to a maximum of 75% after 40 years. No retirement lump sum is payable. A minimum pension provision of 35% of pensionable salary applies due to the fact that civil servants are not covered by the state social security system.

9.3.5 Pensions in payment are increased by reference to the pay of serving civil servants. Pay increases tend to be lower in the public service compared with the private sector. A recent reform has introduced a performance related element to salary structures. Only a maximum of 10% to 15% of staff will benefit from it; however, it will have no impact on pensions in payment. The only benefits which pensioners have received from productivity/restructuring increases in the past arose from what were known as *adjustment bonuses*. These have now been abolished. As a result, there is no longer a direct link between the current salary of each post and the pension received by the former post-holder.

9.3.6 In order to be eligible for ill health retirement, a minimum of five years' service is required, unless disability is due to work-related factors. Pensionable service is based on actual years of service plus two-thirds of potential service to age 60. Due to the particularly high level of ill health retirements amongst teachers, a new regulation was introduced in 1997 which requires that other employment options be explored (e.g. administrative positions) before early retirement can be offered. In addition, the added years provision has been reduced to make the pension terms on ill health retirement less attractive.

9.3.7 On death-in-service, a gratuity equal to one year's salary is payable. There is no minimum service requirement for payment of survivor's pension. Such a pension is 60% of the actual retirement pension or the retirement pension the civil servant would have received had he or she retired on ill health grounds on the day of death. Children's pensions are also payable, though the total amount of survivor's pension and children's pensions cannot exceed the retirement pension to which the deceased would have been entitled.

9.3.8 A Pensions Report issued by the Government in 1996 expressed concern about the medium- to long-term costs of the civil service scheme.[121] It noted that when ill health retirements are taken into account, civil servants in Germany retire, on average, at about age 59 and thus six years before reaching the statutory age limit. The changes to ill health retirement provision and increase in minimum age for early retirement from 62 to 63 (as described above) are aimed at increasing the age of retirement in the future. Apart from retirement age, the major factor in the projected growth in pension costs is rising pensioner numbers. According to the Pensions Report, the number of pensioners will rise sharply from about 2010, due to heavy recruitment in the 1970s. The peak will be reached around 2023 when there will be approximately 1.29 million pensioners. (The public service demographics in Germany are not very different from those in Ireland, as outlined in Chapter 6.)

9.3.9 In an effort to meet the expected peak in future pension costs, the German Government decided to establish a *buffer fund* or special statutory pension reserve, commencing in 1999. Under this reserve-concept, the pay and pensions of civil servants will not be fully adjusted in line with the collective wage agreement for public employees for a period of time so that civil servants and pensioners will make an appropriate contribution towards coping with the problems of providing for old-age pensions in the public service. In practice, pay and pensions will lag behind annual wage agreements by 0.2% for 15 years, thus permanently reducing them by 2.9%. At the end of this time, it is expected that the reserve, including the interest accrued, will amount to

[121] Bundesministerium des Innern, "Data and Final Report on Pensions 1993-2008, with a review up to 2040" (Bonn, October 1996).

more than 60 billion marks. It is intended that the fund will be used at a later stage to contain pension expenditure so that the overall economy is not over-stretched during peak pension cost periods.

9.3.10 As noted above, the pension arrangements of public employees are provided for under the social security system and supplementary occupational pension scheme. A minimum period of five years is necessary to qualify for membership of the pension scheme. The statutory retirement age is 65, or 63 after 35 years' service. The early retirement provisions for civil servants also apply (see Paragraph 9.3.4). The compulsory top-up scheme is a form of supplementary pension which enables payment of pension equivalent to that of a comparable civil servant. It is calculated by reference to overall pension, i.e. the difference between the pension payable to an equivalent civil servant and the pension payable under the state scheme. This is known as gross integration.

9.3.11 Different integration arrangements apply to private sector employees in Germany. The typical arrangement is a *step rate* formula, where an employee accrues social security and occupational entitlements concurrently below a certain income ceiling. The average social security retirement pension after a full career is currently 40-45% of final earnings. While there is no uniformity in the level of supplementary benefit provision, a typical plan might provide for each year of service 0.3-0.5% of final earnings up to the social security contribution ceiling, plus 1.2-1.5% of final earnings in excess of the social security ceiling. This type of plan is becoming less popular in recent times as increases in social security ceilings have tended to lag behind rises in pay. The prudent employer may prefer a freestanding complementary plan. In recent years, some plans have revised the pension formula to reduce the accrual rate and take no account of the social security retirement pension. This protects the employer against a possible future reduction in the social security pension. After a full career, plans typically amount to 10-20% of final earnings up to the social security ceiling and 40-60% above the ceiling.

9.4 Sweden

9.4.1 Civil servants in Sweden are covered by the statutory State Pension Scheme, which covers the entire population. A radical reform to the scheme was due to come into effect in 2000. Special occupational pension schemes for civil servants and other public sector employees are supplementary to the State Scheme, which provides the substantial part of total pension.

9.4.2 The principal reason for the restructuring of the State Pension Scheme is that low economic growth in recent years, combined with the constant rise in pension amounts, has exacerbated the long-term cost position of the existing scheme. Without change, it was estimated that the scheme would have encountered serious problems from about 2010 on.

9.4.3 The characteristics of the revised State Scheme are as follows:

- it will remain the primary source of pension entitlement (i.e. the supplementary occupational scheme will continue to provide a top-up only);
- it will operate as a defined contribution scheme — $18\frac{1}{2}$% of all annual pensionable earnings from 16 years of age will be paid into the system as contributions. Pensionable earnings include incomes from employment and business activities, as well as sickness benefits, parental benefit and other social security benefits. Periods spent taking care of children will also be covered. Earnings up to a certain ceiling will carry pension rights;

- from 2000, half of the $18\frac{1}{2}$% contribution will be paid by the employer, the other half by the employee;
- the major part of the contribution (16%) will be used to finance pension payments in the same year, i.e. it will operate on a pay-as-you-go basis, distributing incomes from the economically active to the retired generation;
- an account of the contributions made by each person to the pay-as you-go system will be maintained. The balance of the account, which will not be backed by any capital asset but rather by a claim on present and future contributors to the pay-as-you-go system, will be adjusted each year according to changes in an index. The index will reflect average income growth in the economy;
- the remaining portion of the contribution ($2\frac{1}{2}$%) will be saved and will earn interest in a premium reserve account. An individual will be able to choose an investment manager for this part of his or her account;
- on retirement, the individual will receive the balance in the premium reserve account, i.e. the capital (contributions) and the yield accrued on the capital. As the reformed pay-as-you-go scheme and the premium reserve scheme are defined contribution schemes, the pension benefit will be related directly to the contributions paid;
- the pension entitlement in the year of retirement will be calculated using a specific divisor. This divisor will be the same for everybody in an age group but may vary between age groups. The divisor will be derived from the expected number of years that pension will be paid, and based on an assumption of what economic growth will be;
- as from the second year, the pension will be increased by the economic adjustment index, which will take into account both price increases and the growth of real wages. The effect of this arrangement is that the pensioner will not receive full growth compensation for price inflation at lower rates of growth than the norm. If growth is higher, the pensioner will not only receive compensation for price inflation but also a share of some of the growth in real wages enjoyed by the economically active;
- the balance in each individual's premium reserve account will determine the size of the pre-funded pension, which will also be calculated on the basis of actuarial principles;
- old age pensions may be drawn down from the month in which the insured person turns age 61 at the earliest. The later the pension is drawn, the greater the annual pension, as it will be paid out over a lesser period of time. Pensioners will also be able to stop drawing pensions temporarily if, for example, they return to gainful employment for a period. These wages will also be added to life earnings which will increase the size of the pension when it resumes. In other words, there is no general retirement age in the new system;
- a guaranteed minimum pension will be paid to those who do not qualify for pension or who only qualify for a small entitlement. This pension will increase in line with prices rather than average income in the economy.

9.4.4 As already noted, the major element in the pension payable to public service pensioners comes from the State Pension Scheme. The main provisions of the supplementary civil service scheme, which dates from 1991, are set out below. It is expected that this scheme will be reformed to bring it into line with the revised State Scheme.

- Scheme membership is compulsory for all civil servants and other employees in the public service, except for military personnel and employees in the local government sector, who are subject to other supplementary pension schemes;
- the major part of the supplementary scheme is benefit defined and is designed to supplement the old State Pension Scheme. Accordingly, it is intended to change the scheme in the next few years to fit in with the new structures (it is expected that the career earnings principle will be adopted);
- retirement age for the purposes of the scheme is 65. It is possible to retire, with the consent of the employer, after the age of 65. In the case of early retirement, available from age 60 at the earliest, a reduced old age pension is payable;
- the defined benefit pension is calculated on final salary, i.e. the average pensionable salary received during the five years preceding the year of retirement. Old age pension is earned at the rate of 0.33% of final salary for each year of pensionable service from the age of 28, up to a maximum of 30 years' service. Therefore, the full pension level is 10% with the State pension expected to provide 55% to 60% of salary up to the earnings salary ceiling. On salary levels above this ceiling, an accrual rate of 2.17% per year is applied, providing a pension entitlement of 65% after 30 years' service for this portion of income;
- a small element of the supplementary scheme is defined contribution in nature. The employer pays 1.7% of salary into a personal pension fund held on behalf of the individual employee, and he or she has the option of supplementing this with further contributions;
- the supplementary pension scheme is administered by an agency known as The National Government Employee Salaries and Pensions Board (SPV).

9.5 The Netherlands

9.5.1 The public service pension scheme in the Netherlands covers all government employees, except for military personnel. It also includes personnel employed in the education sector, as well as employees of private legal bodies performing tasks of public interest which are subsidised by public institutions.

9.5.2 The scheme is funded through the Algemeen Burgerlijk Pensionenfonds (ABP) pension fund, which is the largest pension fund in the Netherlands, with 1,000,000 active employees, 600,000 dormant members and 600,000 pensioners. With over £100 billion in invested capital, it is one of the largest occupational pension funds in the world. It was privatised with effect from 1 January 1996 (see below).

9.5.3 The pension scheme for public servants is based on an agreement reached between government employers and public service unions. This agreement is called the *Pension Regulation*. It is negotiated centrally, unlike most other pay and labour conditions which are determined at a sectoral level. Employers are keen that pension negotiations should in future be devolved to sectoral level in order to reduce relativities and to make the scheme more flexible. However, the unions would appear to oppose such a development on the grounds that it would lead to greater costs, segmentation of the single ABP fund resulting in poorer returns, and that it would weaken their negotiating position.

9.5.4 Civil servants are entitled to a basic state social security flat-rate pension. This is based on the minimum wage and calculated in proportion to the years between ages 15 and 65 that a person has been resident in the country. For single people, the old age pension is 70% of the minimum wage. Contributions are paid towards the scheme by those in employment. The scheme also provides survivors' and disability pensions.

9.5.5 The occupational pension scheme is described as a supplementary pension and is integrated with the state social security pension through the deduction of the basic state pension from final salary for the purpose of pension calculation. Given the flat rate state pension and the practice of integration in this form, the pension structure in the Netherlands is not very dissimilar to that applying to public servants in full PRSI class in Ireland.

9.5.6 The main provisions of the supplementary scheme are as follows:

- it is defined benefit in nature and membership is compulsory. There is no minimum service provision, and normal retirement age is 65. Pension can be drawn on grounds of incapacity at any age;
- pension accrues at the rate of 1.75% of pensionable salary for every year of service, giving a pension of 70% of pensionable salary after 40 years (there is no maximum). Pensionable salary is defined as salary as at 1 January of the year prior to the year of discharge;
- a retirement lump sum is *not* payable in addition to pension;
- pensions are increased in line with a public service pay index. The index averages pay increases across the public service so as to arrive at one percentage figure for pensions increase purposes;
- the contribution rate is calculated annually and on an actuarial basis. Employees contribute one-quarter of the overall contribution with the balance being paid by the employer;
- early retirement arrangements were changed in 1997. Up until then, more generous *pre-pension* provisions applied between the ages of 61 and 65. These were considered expensive, and so were replaced by a flexible retirement system, which is partly pre-funded, with the balance being met on a pay-as-you-go basis;
- a transitional arrangement applies to serving staff aged 35 or over which provides them with a pre-pension entitlement between ages 61 and 65 based on a guaranteed minimum number of years;
- provision is made for groups such as police officers and fire brigade personnel to retire earlier than the norm. Such groups are required to work to age 60, as compared with an average of age 55-60 in Ireland;
- a survivor's pensions (paid to legal spouse or partner) is paid at the rate of 5/7ths of the deceased member's pension. Where the member dies in service, actual service plus potential service to age 62 is reckoned;
- the service of part-time employees reckons in the same way as that of full-time employees, except that pensions are multiplied by the part-time factor, e.g. if a person has only worked for 50% of the time, then his or her pension entitlement will be divided by two;
- any member with an annual pension entitlement less than a certain minimum amount is required to accept a lump sum instead of a pension.

9.5.7 The funded arrangements for public service pensions enables the operation of a transfer value system. Such a facility is important, as there is frequent movement between the public and private sectors.

9.5.8 The number of people receiving disablement pensions is quite high in the ABP scheme — 91,000 as compared with 270,000 drawing old age pension. However, many recipients continue to work, and draw a part pension. This is because the disablement need not be full: the degree of incapacity determines the level of pension payable, e.g. a person who is 15% disabled can qualify for a pension entitlement.

9.5.9 As regards the history of ABP, the Pensions Act, 1922 led to the first funded pension scheme being established for the Municipalities. The pension scheme and the fund have been administered by ABP from the outset. Pension funds at this time were almost entirely invested in government bonds. The scheme was stand-alone until 1963 when the State Pension Scheme was introduced. Integrated pension arrangements date from this time. An Act of Parliament liberalised ABP's investment policy to a limited degree, giving it more freedom to invest in equities. In addition, the unions were permitted to play a more active role in negotiating the terms of the pension scheme than heretofore.

9.5.10 During the 1980s, the Government lowered incrementally the annual pension contribution it paid to ABP from 16.5% to 8.8% of pay. This allowed an actuarial deficit to build up, and led to calls for ABP to be privatised and treated like all other pension funds in the Netherlands. A Government Commission reported in 1992, *inter alia*, on the position of ABP and on the financing problem. On the first issue, the Commission recommended privatisation; this was subsequently implemented in 1996. It was felt that the second issue could be dealt with by virtue of coverage of the privatised ABP fund under the Pension and Saving Funds Act which applies to private sector pension funds. This legislation does not permit pension funds to have actuarial deficits and requires that benefits must be cut if assets would not otherwise be sufficient to meet the pension liabilities. It was argued that this would exclude the possibility of any future depletion of the ABP fund's resources by the Government.

9.5.11 A further consequence of privatisation was that any remaining Government restriction on ABP as regards investment policy had to be eliminated. Generally, funded schemes in the Netherlands have a lesser percentage of their assets invested in equities (approximately 40%) compared with a typical fund in this country (approximately 60%). ABP acknowledges that its own investment portfolio still includes fewer equities than those of other funds in the Netherlands (approximately 25% at the end of 1997), and intends to expand the equity level up to a maximum of 40%.[122]

9.5.12 In summary, it would appear that the move to convert ABP into a private sector type fund was done for the following reasons:

- greater security — treating the fund like a private sector fund removed the danger of depletion by government;
- higher returns — privatisation enabled greater discretion in investment policy;
- ultimately, higher returns would feed into lower pension costs.

[122] Algemeen Burgerlijk Pensionenfonds (ABP), *Annual Report 1997*, p. 18.

9.5.13 At the present time, the board of ABP has a chairperson and six representatives of the employers and six representatives of the employees. The company has a staff of 3,700. According to its 1997 Annual Report, ABP's objectives are:

- a differentiated flexible and coherent range of tailor-made products, based on the requirements of the social partners;
- exemplary service, easy accessibility;
- a high investment return translated into stable, low pension contributions;
- low and transparent operating costs as a result of highly effective and efficient people and information technology and economies of scale.[123]

9.5.14 Apart from its role in managing the pension fund, ABP is also the administrator of the pension scheme. It adopts an active approach, emphasising to scheme members their own responsibilities in providing for their retirement, and communicating the options available to them. Annual statements are issued to all members updating them on their accrued entitlements and projected benefits at retirement, and advising them of options to improve their benefits. Computerisation is an integral part of these arrangements. There is a strong focus on ease of contact for members and for employers participating in the scheme, e.g. a call centre and an Internet site have been established, both of which are regularly used.

9.5.15 Public service employers and union representatives whom the Commission met emphasised the importance of flexibility in pension arrangements. For example, it is intended in the near future to provide scheme members with an option of exchanging a survivor's pension entitlement for a higher retirement pension. However, the major constraint in negotiations to which both parties referred was the potential effect of any change upon the pension fund. Ultimately, it is this factor which determines the feasibility of any modifications to the scheme. Comments by a union representative on the ABP Board reflect the collective approach to the pension scheme and costs:

> *Pensions are a global problem. Large pay rises put them under pressure. We have a final-pay system. In the Netherlands, thanks to our capital funding system, we have a raft which will continue to float even if the rest have sunk. But, if you base yourself on an index-linked pension, and that is something we all want, we too are just as insecure. I am here as a member of the Board of Governors with the duty to realise an objective. That is that every member must be able to rely on a good pension.*[124]

9.6 United States

9.6.1 There are a large range of retirement plans for public service employees in the United States at federal, state, and local level. The Commission obtained information on the plans for federal employees together with the plan applying to teachers in the Commonwealth of Massachusetts. We review both plans below.

Civil Service Retirement System/Federal Employees Retirement System

9.6.2 The Federal Employees Retirement System (FERS) and the Civil Service Retirement System (CSRS) are the two largest retirement programmes for federal civilian employees. Together, they cover about 2.8 million employees (1995). FERS, which applies to post-1983 new entrants, consists of three parts — state social security, a defined benefit plan, and a defined contribution plan

[123] ABP, *Annual Report 1997*, p. 25.
[124] Jan Anneveld, *ABP Annual Report 1997*, p. 10.

(known as the Thrift Savings Plan). The CSRS, which applies to employees recruited prior to 1983, is a stand-alone defined benefit plan. Employees in CSRS are not covered by social security through their federal employment.

9.6.3 FERS was implemented in 1987. The primary impetus for the new programme was the social security amendments of 1983, which required all federal employees hired after December 1983 to be covered by social security. This change was primarily intended to help solve the short run financing difficulties of social security.[125] The structure of FERS was determined after study of private sector retirement plans. Employees covered by CSRS were given the option of switching to FERS but only 2.8% did so.

9.6.4 CSRS provides employees with the option to retire with unreduced benefits at age 55 with 30 years of service, at age 60 with 20 years of service, and at age 62 with five years of service. Pension is based on the highest three years of service earnings, and accrues at the rate of 1.5% for the first five years, 1.75% for the next ten years, and 2% after ten years up to a maximum of 80% of average salary. CSRS is contributory — the contribution rate is 7% of salary.

9.6.5 In FERS, the minimum optional retirement age has been increased from the CSRS' age 55 to age 57 for FERS employees born after 1969. FERS continues the objective of encouraging employees to spend their working careers in federal service. It provides employees with the option to retire with unreduced benefits at their minimum retirement age with 30 years' service, at age 60 with 20 years' service, and at age 62 with five years' service. There is an option to retire with reduced benefits with ten years' service. FERS employees who retire at age 62 or older and who have completed at least 20 years' service are allowed to receive retirement benefits calculated on a formula which gives a higher benefit (some 10% more than on retirement before age 62).

9.6.6 Pension on the defined benefit element of FERS is based on the highest three year average of service earnings and accrues at the rate of 1% per annum, or 1.1% at age 62 with 20 or more years' service, to a maximum of 40-44% after 40 years' service. The employee contribution to the defined benefit plan is 0.8% of salary.

9.6.7 The CSRS provides pension increases in line with prices. However, in order to reduce government expenditure, changes were made so as to reduce or delay the cost of living adjustment (COLA). Over the period 1984-95, COLAs were equivalent to 80% only of the Consumer Price Index increase. FERS provides substantially reduced COLAs compared with CSRS. Pensioners do not receive pension increases until age 62 — an incentive to postpone retirement until that age. Also, for price inflation rates of 3% or more, the COLA equals the increase in the Consumer Price Index less 1%.

9.6.8 Under the defined contribution element of FERS, the Thrift Savings Plan, the Government automatically contributes an amount equal to 1% of salary for each employee. In addition, employees may contribute up to 10% of their salaries and receive government-matching contributions on the first 5%. CSRS employees may also contribute up to 5% to the Thrift Savings Plan, but the Government does not make matching contributions for them. The benefits available from the Thrift Savings Plan supplement the defined benefit pension.

[125] Turner, J.A. and Rajnes, D.M., "Reform of Pensions for Federal Government Employees in the United States" (August 1997), paper presented at the European Network for Research on Supplementary Pensions Conference on Public Service Pensions Policy Issues, Dublin, Ireland, September 26 1997, p. 5.

9.6.9 The Thrift Savings Plan is administered by an independent government agency. It operates similarly to *401(k)* defined contribution plans offered by many private corporations and which have been very popular with employees. Since its foundation, the plan has quickly become one of the biggest pension funds in the US. Individual employees have the option to invest their account in any of three investment funds and can transfer any portion of their balance among the three funds.

9.6.10 Federal retirement plans are funded but, unlike private pension funds, their assets are largely invested in special issue non-marketable Treasury securities available only to the retirement funds. At present, the plans have accumulated a sizeable unfunded liability. The combination of reduced defined benefits payable under FERS compared with CSRS and the introduction of the funded Thrift Savings Plan will over the long-term have the effect of reducing the Government's unfunded pension liabilities in respect of its federal employees.

9.6.11 In conclusion, the reform of the US civil service pension scheme following the state social security changes resulted in a retirement system which on average represented a reduction in benefits on the existing system and was more comparable with private sector plans. It raised the retirement age and partially privatised the pension system by introducing the Thrift Savings Plan. Finally, it improved portability for federal employees, facilitating mobility into and out of the civil service.

Massachusetts Teachers' Retirement System

9.6.12 The Massachusetts Teachers' Retirement System (MTRS) is administered by the Massachusetts Teachers' Retirement Board (MTRB). The Board is chaired by the Commissioner of Education and has four other members, two elected by active and retired members, one appointed by the Board, and one — who must be a retired teacher — appointed by the Governor. It covers teachers and administrators and has about 70,000 active members and 30,000 retired members.

9.6.13 Massachusetts is one of the few US states to decide not to have its state employees covered under the social security system. Accordingly, the question of integration of occupational benefits with the state system does not arise. Under the MTRS, a member may retire and receive immediate pension with 20 years' service, regardless of age, or from age 55 with 10 years' service. As outlined below, the pension accrual rate is lower the earlier the age of retirement; in addition, the value of the early retirement pension over time will be affected by the limited pensions increase arrangements.

9.6.14 Three benefit options are available on retirement: retirement pension with no survivor benefit; retirement pension plus lump sum payment to survivor of any balance remaining on the *annuity savings account* (see below); or retirement pension plus pension to survivor. The retirement pension under the second and third options is 3-5%, and 20-30%, respectively, lower than the retirement pension in the first. Benefits are based on service and the member's highest salary average for three consecutive years. The accrual rate for retirement pension varies with age at retirement, e.g. 1.5% at age 55, 2% at age 60, and 2.5% at age 65, subject to a maximum pension of 80% of final average salary.

9.6.15 A member contribution rate applies, with the rate depending on date of becoming a member, ranging from 5% of salary (membership before 1 January 1975) to 9% (membership from 1 July 1996). In addition, members commencing after 1 January 1979 are subject to an additional 2% contribution on any salary over $30,000 per annum.

9.6.16 Member contributions are forwarded to the MTRB which maintains an annuity savings account on behalf of each individual. The account consists of member contributions plus interest earned, which is credited at a rate equal to an average passbook savings return. The actual contributions are invested for the MTRS in a fund managed by the Pension Reserve Investment Management Board (which also manages the fund of the Massachusetts State Employees Retirement System). The interest credited to the individual annuity savings accounts does not reflect the fund's investment return. The fund's excess investment return is transferred to the system's reserve fund, used to ensure the future stability of the system.

9.6.17 The annuity savings accounts are not like individual retirement or defined contribution accounts. They will only be accessed if the member retires, dies, or becomes an inactive member. As shown above, the calculation of retirement benefit is unrelated to the balance on the account. On leaving active service before age 55, having less than 20 years, a member will be entitled to a refund of the account balance, including the interest credited to the account (which is less than 100% of the interest in certain circumstances). A statement of account is sent annually to all active and inactive members.

9.6.18 Pension increases are done on *ad hoc* basis, i.e. they are subject to an annual vote of the Massachusetts General Court. The first $12,000 (only) of a pensioner's annual allowance is subject to a cost of living adjustment related to a change of at least 3% in the Consumer Price Index. The MTRB have commented that as a result of the limited pensions increase policy, a significant number of retirees' purchasing power has been greatly reduced by price inflation.

9.6.19 Like many public retirement systems, the MTRS was traditionally financed on a pay-as-you-go basis. In 1976, however, the Funding Advisory Committee recommended a move to a system of actuarial funding. This system involved a phase-in over a number of years to an actuarial funding basis which provided for amortising unfunded actuarial liabilities over a 40-year period. The mandate of the Pension Reserves Investment Management Board is to accumulate assets through investment earnings and other revenue sources in order to reduce the Commonwealth's significant unfunded pension liability.

9.7 Comparative analysis of public service pension arrangements abroad

9.7.1 Having carried out a detailed examination of the public service pension arrangements of a number of countries, we now compare the occupational pension arrangements for public servants in a wide range of European countries. We consider the following headings:

- retirement age;
- early retirement provisions;
- integration with the state social security system;
- level of benefits and system of calculation;
- employee contributions;
- pension arrangements for part-time employees;
- provision for pension increases;
- financing arrangements;

- management, administration and communication.[126]

9.7.2 Our general approach is to examine pension provision for civil servants. In many countries, as in Ireland, specific categories of public servants have special pension arrangements which are different to the norm (e.g. military, police); in certain instances, we provide details of these special terms.

9.7.3 By way of qualification, we should acknowledge that pension terms can be complex and that it is not possible to capture accurately the full set of applicable terms and conditions within the summary tables used below.

Retirement age

9.7.4 The position regarding minimum, normal, and maximum retirement ages varies between the countries considered (see Table 9.1). The *normal retirement age* is taken as the earliest age at which a public servant can retire based on actual service, with no actuarial reduction in benefits. The *minimum retirement age* is used where a public servant can retire earlier than the normal retirement age, either subject to a certain minimum service requirement, or subject to actuarial reduction. The *maximum retirement age* is taken as the latest age to which a public servant is entitled to remain in employment.

9.7.5 It is difficult to draw absolute conclusions based on the information presented. However, the table shows that seven countries apply a normal retirement age higher than age 60 (one has age 62, five have age 65, and one has age 67). Two countries apply a normal retirement age of 65 but allow retirement from an earlier age subject to a minimum period of service (age 57 with 35 years' service in one; age 60 with 30 years' service in the other). Six countries apply a normal retirement age of age 60, which is in line with the minimum age of retirement in Ireland (in one case, retirement from age 57 is allowed, provided 40 years' service has been completed).

9.7.6 The evidence suggests that with a number of countries moving to increase the age of retirement, the normal retirement age for public servants in Ireland (age 60) may now be considered amongst the lower of those applying to public servants in Europe. Of course, in comparing pension terms it is necessary too to consider other factors such as pension accrual rate, scale of maximum pension, pensions increase policy, etc.

9.7.7 Generally, minimum service conditions apply. There are no age restrictions for early retirement due to ill health, but different minimum service requirements apply in many countries.

9.7.8 Most countries apply lower retirement ages for certain categories of public servants, such as policemen, firemen, etc. Further details are set out in Appendix 9.3.

9.7.9 Changes have been made to the age of retirement in a number of countries. The trend of these reforms has been to increase retirement ages (we discuss recent and current modifications to pension schemes in Section 9.8).

[126] The main sources used in the comparative study of pension schemes were: (i) European Commission DG IX, ''Comparative Study for the European Commission of Pension Schemes and Allowances Systems for Civil Servants in the Member States, and Staff of selected International Organisations'', report prepared by KPMG European Business Centre (Contract No. 97/14/IX.C.1, December 1998); (ii) ''Pension Schemes for Civil Servants'', document prepared by the European Institute of Public Administration for the Directors General Meeting in Seville, 2-3 November 1995; and (iii) Neyens, P., and Koob, E., *Pension Schemes in the European Public Sector* (European Institute of Public Administration, 1992).

Table 9.1 Retirement ages and voluntary early retirement provisions in the public service schemes of a range of European countries

Country	Retirement age			Actuarial reduction in pension where retirement takes place before a certain age within the minimum and maximum range	Additional pension credit for working beyond normal retirement age
	Minimum•	Normal	Maximum		
Austria	51*	60	65	2.5% for each year prior to 60	No
Belgium	–	60	65	–	–
Denmark	60*	67	70	0.5% to 3% for each year prior to age 67	yes – up to maximum pension
Finland#	60*	65	–	0.5% for each month prior to 65	–
France	–	60-65	–	–	–
Germany#	63*	65	68	3.6% for each year prior to 65	yes – up to maximum pension
Greece#	–	65	67	–	yes – up to maximum pension
Ireland	–	60	65	–	–
Italy#	57 (or 35 years' service)	65 (m) 60 (f)	70	–	yes – up to maximum pension
Luxembourg	57 (or 40 years' service)	60	65	–	No
Netherlands#	55*	62	65	–	–
Portugal	–	60	70	–	yes – up to maximum pension
Spain	60 (or 30 years' service)	65	70	–	yes – up to maximum pension
Sweden	60*	65	–	0.4% for each month prior to 65	pension increased by 0.4% for each month of late retirement.
Switzerland	60*	65	–	benefits reduced on retirement before age 62 or after that age with less than 40 years' service	–
UK	50*	60	65◊	5% and 2.5% for pension and lump sum, respectively, for each year prior to 60	yes – up to maximum pension

• Excluding early retirement on ill health grounds or early retirement in cases of redundancy, specific efficiency measures or other short-term measures to induce structural changes.
Countries where the ages of retirement or early retirement terms have recently been amended.
* In each case, actuarial reduction is applied on retirement at the minimum retirement age indicated.
◊ In the UK, the majority of public servants have a standard retirement age of 60.

Early retirement provisions

9.7.10 As detailed in Table 9.1, retirement with immediate payment of pension from a minimum retirement age is permissible in all countries, subject to certain minimum service conditions and in many cases with actuarial reduction. The minimum age for such early retirement is usually 60, although a number allow early retirement from earlier ages, e.g. the Netherlands (age 55), and the UK (age 50). In the table, we are excluding early retirement on ill health grounds or in cases of redundancy, restructuring, or for reasons of efficiency.

9.7.11 As already noted, special groups of employees such as Police Officers, Firefighters, etc. are permitted in many countries to retire earlier than the norm (see Appendix 9.3). For such groups, a full pension entitlement is generally payable after a shorter number of years than applies to general public service groups.

Integration with the state social security system

9.7.12 All countries have some kind of statutory social security pension scheme. Practice varies as to whether or not civil servants are included in such schemes. It is not uncommon for civil servants to have a separate stand-alone occupational pension scheme (e.g. Germany, Massachusetts teachers' scheme — see above) with no entitlement to state social security benefits; this is the situation in Ireland for public servants in modified PRSI class recruited before 6 April 1995. Where civil servants have an entitlement to a state social security pension as well as a supplementary occupational pension (e.g. the Netherlands, Sweden and Ireland), integration is applied to maintain total overall provision at the intended or target level; however, this does not happen in all cases (e.g. the UK — see Paragraph 9.2.14). Obviously, integration is an issue for private sector occupational pension schemes as much as for occupational pension schemes for public servants. The information available across all countries would appear to suggest that the greater the level of the general state social security pension, the greater is the likelihood of some form of integration being applied under occupational pension schemes.

9.7.13 There are a number of different approaches to achieving integration. In one approach, the occupational pension is calculated as a *gross* amount from which the state social security pension is deducted. If the occupational pension is reduced due to insufficient length of service, the state social security pension is reduced correspondingly. This is the arrangement which operates for public employees in Germany (see Paragraph 9.3.10). In another approach, the occupational pension is calculated as a *net* amount, i.e. an amount in respect of state social security pension is deducted from final salary before the calculation is carried out. This is the arrangement which applies in this country and in the Netherlands (see Paragraph 9.5.5). In Sweden, a *step-up* model applies: the social security pension provides the major portion of pension entitlements up to an earnings ceiling limit, and a supplementary occupational pension provides the balance (see Paragraph 9.4.4). It is also the favoured practice in the private sector in Germany. In such a situation, earnings above the ceiling limit are provided by the occupational pension alone.

9.7.14 A recent report for the European Commission stated that the impact of state social security plans and how they are accounted for does not appear to affect the pensions issue and the total value of pensions provided in a significant way — except in the case of Italy where the non integrated scheme pension is payable on top of the social security pension, without reduction or offset.[127]

Level of benefits and system of calculation

9.7.15 In most countries, the pension calculation involves integral linear progression (i.e. a fraction of pensionable pay is accrued for each year of pensionable service), which is also the system applying

[127] European Commission DG IX, "Comparative Study for the European Commission of Pension Schemes and Allowances Systems for Civil Servants in the Member States, and Staff of selected International Organisations", report prepared by KPMG European Business Centre (Contract No. 97/14/IX.C.1, December 1998), p. 12.

in Ireland. In other countries, the system involves the combination of a constant or a basic sum (for service up to a certain level), and integral linear progression (for service above that level).

9.7.16 The salary used to determine pension benefits varies. Most countries use the salary applicable on retirement or salary averaged over a certain period prior to retirement. In Denmark and Spain, a level of pensionable salary, which may be somewhat below the actual level of salary of the member, is fixed periodically, either by the Ministry of Finance or by law.

9.7.17 The majority of public servants are covered by defined benefit schemes. However, there are some exceptions – Italy is moving to a defined contribution scheme for new entrants, as is Sweden for its revised state pension scheme. In addition, the pension scheme for public employees (but not state appointed civil servants) in Denmark is contribution defined.

9.7.18 In a number of countries, certain groups of employees such as those in the fire service, police service, etc. have earlier retirement ages than the norm (see Appendix 9.3). It would appear that in many of these cases, either enhanced pension terms are applied, as in the UK, or pension can be drawn from an earlier age without actuarial reduction being applied.

9.7.19 The maximum pension entitlements as a percentage of pensionable salary for a range of European countries, the accrual rates used, and the length of service required to qualify for maximum pensions are set out in Table 9.2.

9.7.20 The maximum survivor's pension as a percentage of the deceased member's retirement pension varies from 50% in most countries to 80% (Denmark).

Table 9.2 Maximum service required to qualify for maximum pension; annual accrual rate; and maximum pension benefits

Country	Maximum service reckoned (years)	Accrual rate per year of service (as % of remuneration)	Maximum pension as % of remuneration
Austria	40	(i)	80% of final salary
Belgium	45	1/60th (1.667%)	75% of pensionable salary
Denmark	37	(ii)	57% (approx.) of pensionable salary
Finland*	40	1.5% to age 60 and 2.5% thereafter	60% of pensionable salary
France	37.5	2%	75% of pensionable salary
Germany	40	1.875%	75% of pensionable salary
Greece*	35	1.714%(iii)	60% (approx.) of pensionable salary
Italy*	40	(iv)	80% of pensionable salary (iv)
Luxembourg	40	(v)	83% of pensionable salary
Netherlands	40	1.75% of pensionable salary (less social security pension)	70% of pensionable salary (less social security pension)
Portugal*	40 (vi)	2%	80% of pensionable salary
Spain	35	(vii)	100% of uniform basic salary (vii)
Sweden	30 (viii)	–	70% of pensionable salary approx.
Switzerland	40	(ix)	65% of pensionable salary approx.
United Kingdom	40 (x)	1/80th	66% of pensionable salary (x)

* In these countries, accrual rates have been adjusted for new entrant public servants over the past number of years. The new terms are less beneficial than those they replaced.

Notes:

(i) The pension benefit is based on pensionable basic salary (pbs) which is 80% of the last salary received. The calculation basis is 50% of pbs for 15 years of service plus 2% of pbs for each additional year up to a maximum of 40 years. The maximum pension is equivalent to 80% of considered remuneration.

(ii) The pension benefit is based on pensionable salary, which is an individual basic salary lower than the salary actually paid. The calculation basis is 1.75% of pensionable salary for service between one and 16 years; 1.5% of pensionable salary for service between 17 and 32 years; and 1% of pensionable salary for service between 33 and 37 years.

(iii) This is the calculation basis introduced for new recruits from 1 January 1993.

(iv) A new scheme has been introduced for public servants recruited after 1 January 1996. Pension benefit is determined by the amount of contributions paid during membership. The amount is re-evaluated according to rises in the cost of living index and is multiplied by a specific coefficient which is fixed every ten years and depends on the retirement age, the estimated life expectancy and economic growth. The figure for maximum pension of 80% of pensionable salary represents the old scheme maximum benefit.

(v) The calculation basis is 20/60ths of pensionable salary with a length of service of ten years and a further 1/60th of pensionable salary for each additional year subject to a maximum of 40 years of service.

(vi) For those recruited before 1993, maximum service is 36 years and the annual accrual rate is 1/36th of pensionable salary up to 36 years. Therefore, the maximum pension entitlement is 100% for these members.

(vii) Pensionable salary is basic remuneration which is fixed annually by the law on general State budgets. The pension is the product of pensionable salary and a specific coefficient according to the number of years of service. The maximum pension is fixed by law on an annual basis. The maximum pension is equivalent, on average, to 95.4% of final salary.

(viii) The Swedish system comprises two pillars. The first pillar is a defined contribution system, and the pension reflects the pensionable income earned by a person throughout his or her working life. The maximum pension paid under this pillar is approximately 55% to 60% of pensionable salary. The second pillar pension is based on the average pensionable salary in the five years preceding the year of retirement. 30 years of service is required to achieve maximum pension under this pillar, which amounts to approximately 10% of pensionable salary.

(ix) Combination of state social security and occupational pension.

(x) In the UK system, benefits consist of retirement lump sum and pension; this is generally accepted as being equivalent to a replacement income of 66% of pensionable pay. No other country (apart from Ireland) pays a lump sum in addition to pension. It is possible for a person to qualify for maximum pension benefits of 73% of pensionable salary (i.e. between pension and lump sum) if he or she has 45 years' service at age 65. Normal retirement age is age 60.

Employee contributions

9.7.21 In Austria, Belgium, Finland, France, Greece, Italy, Portugal, Spain, Sweden, Switzerland and the UK, members pay a specific percentage of salary as a contribution towards the scheme. Other than the UK, where a contribution of 1.5% is paid towards dependants' pensions only, the rate of contribution varies from 4% (the Netherlands) to 10.75% (Austria). The rate in most countries is in the 7% to 10% range.

9.7.22 Implicit or notional contributions through either a lowering of salary levels, a levy on the pension, or recoupment of part of the employer's contribution apply or are deemed to apply in Germany, Luxembourg, United Kingdom, the Netherlands and Ireland.

Pension arrangements for part-time employees

9.7.23 Membership of public service schemes is open to part-time employees in all the countries considered. Many countries do not have any minimum hours requirement for this purpose. Where such a requirement exists, it either takes the form of a specified number of hours per week or a specified percentage of equivalent full-time hours.

9.7.24 Part-time service generally counts proportionately to full-time service, with the pension benefit being calculated by reference to the full-time pay equivalent. Pro rata integration applies in the Netherlands, where the level of part-time employment (about one-third of total public service numbers) is much higher than in Ireland. We discuss pro rata and full integration of benefits for part-time workers in Section 11.7.

Provision for pension increases

9.7.25 All countries pay increases to pensions in course of payment, although the method of increase varies. The information available shows that increases by reference to a combination of developments in the cost of living index and salary increases in the public sector apply in a number of countries. Other countries apply increases in line with salaries of serving staff, e.g. the Netherlands applies an index based on pay increases averaged for all public servants. The remainder apply increases in line with a cost of living index. Table 9.3 summarises the position.

Table 9.3 Pension increases in the public service schemes of a range of European countries

Country	Pensions increased by reference to
Austria	Salaries of serving staff (i)
Belgium	Cost of living/salaries of serving staff
Denmark	Cost of living/salaries of serving staff
Finland	Cost of living/salaries of serving staff (ii)
France	Salaries of serving staff
Germany	Salaries of serving staff
Greece	Cost of living/salaries of serving staff
Italy	Cost of living
Luxembourg	Cost of living/salaries of serving staff
Netherlands	Salaries of serving staff
Portugal	Salaries of serving staff
Spain	Cost of living
Sweden	Cost of living
Switzerland	Cost of living (state pension increases are in line with salaries)
United Kingdom	Cost of living

Notes:

(i) From 2000, civil service pensions will be increased at the same rate as pensions provided under the general system, i.e. the net income of pensioners should rise in line with the net income of insured workers.

(ii) For those under age 65, the ratio is 50/50 of both; for those over age 65, the ratio is 20% of salary and 80% of the Retail Price Index.

9.7.26 We give further information on pensions increase arrangements in a number of countries in Appendix 9.4.

Financing arrangements

9.7.27 In most countries, the public service pension provision is budgeted each year with benefits met on a pay-as-you-go basis. Pensions are fully funded in the Netherlands (although some benefits are met on a pay-as-you-go basis), and a fund has been established in Italy as part of a move towards a defined contribution scheme. In the UK, the Local Government Superannuation Scheme is fully funded, as is the defined contribution scheme for public employees in Denmark.

In Finland, Portugal, and Sweden, partially funded systems are in operation. A buffer fund is being established in Germany to meet the peak in costs in about 20 to 25 years time.

9.7.28 Many public pension plans in the United States are funded.

Management, administration and communication

9.7.29 The management, administration, and communication of pensions is an important part of public service pension provision. In Appendix 9.5, we outline briefly the pension administration arrangements of a number of countries. Among the countries visited by the Commission, specialised pension bodies carry out the administration of public service pensions in Sweden (KPA) and the Netherlands (ABP), while scheme administration is done on a sectoral basis in the UK (e.g. NHS pension scheme; teachers' pension scheme).

9.7.30 Where specialised administrative structures are in existence, often the boards or trustees of the relevant pensions bodies bring together representatives of employers, unions, and pensioners (e.g. ABP, Massachusetts Teachers Retirement Board). These boards/trustees often take on the role as providers of impartial advice to employers and unions in relation to pension claims and the cost of pensions.

9.7.31 Compared with Ireland, other countries would appear to make greater efforts to communicate scheme terms and personal benefit entitlements and options to individual public servants. For example, this is seen by ABP as one of its primary responsibilities (see Paragraph 9.5.14).

9.7.32 An objective, independent process of appeal is a feature of pensions administration in a number of countries (e.g. the UK).

9.8 Recent and current modifications

9.8.1 An important consideration emerging from the Commission's review of pension arrangements abroad is the extent of scheme modifications which have been or are taking place. These modifications are usually aimed at making long-term pension costs more affordable (often in tandem with reforms to state social security systems), providing advance funding to meet future pension costs, and allowing individual employees flexibility to gear at least part of the pensions package to their own personal circumstances. In some countries, scheme changes reflect reforms in public service structures and management, while in others, the introduction of defined contribution arrangements reflects the trend in pension provision in the private sector. We give a brief review below on the major changes in public service pension provision in a number of countries.

9.8.2 In the **United Kingdom**, the special terms of Prison Officers, Mental Health Officers and nurses have been brought into line with standard scheme provisions. Consideration is also being given to revising the terms of police officers and fire officers to bring them closer to the norm. A new civil service pension scheme has been agreed which will offer more favourable benefits at the expense of higher contributions from members. New entrants are to be offered the choice of joining the improved scheme or a new defined contribution scheme. A recent government report has recommended that departments consider allowing their civil servants to retire at 65, rather than at the normal retirement age of 60. The report also recommends raising the minimum age at which an immediate tax-approved occupational pension is payable from age 50 to age 55 between 2010 and 2020.

9.8.3 In **Germany**, concern has been expressed at the level of early retirement and the medium- to long-term costs of the civil service scheme. Consequently, the minimum retirement age has been increased, and a buffer fund is being put in place to help with the peak in pension costs in 20 to 25 years' time.

9.8.4 In **Sweden,** the state scheme has been radically revamped due to the costly nature of the existing arrangements and a defined contribution scheme has been put in place. It is expected that the supplementary occupational scheme will also be adapted shortly to fit in with this new model.

9.8.5 In **the Netherlands**, early retirement arrangements were remodelled and made more cost effective in 1997. The ABP public service pension fund was privatised with the aim, partly, of ensuring better returns through a more open investment mandate, thereby making long-term pension costs more affordable.

9.8.6 In the **United States**, the defined benefit retirement plan for federal employees was cut back for new entrants, and a defined contribution plan introduced to make up the difference. This move had the effect of privatising part of public service pension provision. In many cases, the value of the benefits under the new hybrid scheme will be lower than under the original defined benefit plan.

9.8.7 In **Austria**, from 2000 on, pensions in payment will be increased at the same rate as under the general system, rather than in line with civil service pay increases. This is likely to result in lower rates of pensions increase. From 2020, earnings for pension purposes will be based on the best 216 monthly salaries. It is considered that this will reduce the monetary value of emerging pensions.

9.8.8 In **Finland,** retirement age has been increased to 65, and the pension formula has been weakened for new entrants resulting in longer service being required to earn maximum benefits.

9.8.9 In **Italy**, the retirement age is being gradually increased. A defined contribution scheme is being phased in that will eventually replace the defined benefit retirement provision.

9.9 Conclusions

9.9.1 In a widely based review such as this it is difficult to draw firm conclusions. Each country has its own distinctive historical, social and economic characteristics. These help to determine the relative importance of the public service within the economy, the processes for determining pay and conditions for public servants, and the state social security system, all of which combined impact upon the public service pension system in each country.

9.9.2 Notwithstanding these difficulties, we would draw the following conclusions from our comparison of pension terms across public service pension schemes abroad:

- with a number of countries moving to increase the age of retirement, the normal retirement age for public servants in Ireland may now be considered amongst the lower of those applying to public servants in Europe;
- most countries operate defined benefit pension schemes for their public servants, although a small number have been moving to a defined contribution or hybrid pension

scheme design either for certain categories of public servants or for new entrants generally;

- maximum pension benefits, expressed as a percentage of pensionable remuneration, would seem, on average, to be higher in many European countries, but this must be qualified on the basis that the figure for pensionable remuneration used in those countries (based on an average of the final three years' pay, for example) may be lower than that used in public service schemes in Ireland;
- retirement with immediate payment of pension from a minimum retirement age is permissible for public servants in most countries (but not in Ireland), usually subject to actuarial reduction;
- it is normal practice to apply special retirement and pension terms to certain groups facing particular operational requirements, e.g. police, fire service;
- most public service schemes are separate and distinct from the state social security system, with members having no entitlements under the latter. Integration applies in most countries where public servants are covered by the state social security system;
- pensions are generally increased by reference to the Consumer Price Index or by a combination of cost of living and adjustments in line with salaries for serving staff. Ireland applies increases by reference to pay only, which appears to be a more favourable system compared with many other countries. A much less favourable system of pension increases applies in public service retirement plans in the US;
- with some notable exceptions, most countries finance public service pensions on a pay-as-you-go basis;
- compared with Ireland, it would appear that many countries devote greater resources to the administration of pensions and to the communication to members of benefit details and retirement options.

9.9.3 Apart from noting the general trend of modifications to public service pension arrangements abroad, we also identified a number of additional points of interest which were of value in our deliberations:

- use of system of accrual accounting to ensure transparency in pension costs (the UK; pension funding achieves the same result in the Netherlands);
- greater use of occupational health services as part of efforts to address increasing numbers of ill health early retirements, including those on stress-related grounds (the UK, Germany);
- introduction of arrangements to give employees control over part of their pensions package, e.g. defined contribution element of supplementary scheme in Sweden, THRIFT plan for federal employees in the US, and employer-supported AVC plans in the UK;
- proposal to establish buffer fund to help meet the long-term cost of public service plans in parts of the public service (Germany). In some countries, part funding has effectively been introduced through funded defined contribution elements in the pensions package (Sweden, US);
- use of different systems of integration between occupational and state pensions — e.g. different pension accrual rates for different earning levels (Germany);

- use of pay index to arrive at a single average rate of increase in public service earnings for pensions increase purposes (the Netherlands);
- management of pension schemes in a partnership approach involving public service employers, unions, and pensioners (the Netherlands, Germany).

9.9.4 The trends and points of interest identified in this Chapter will be considered as appropriate in the Commission's later deliberations on public service pensions in Ireland.

APPENDIX 9.1

Comparison of public service terms in the United Kingdom and Ireland

United Kingdom	Ireland
Maximum retirement age is 60, although in limited circumstances a person may be retained to age 65.	Retirement age is between 60-65.
Early retirement is available from age 50 on an actuarially reduced basis.	No such provision available.
Pensions are increased in line with cost of living index (RPI).	Pensions are increased in line with salary increases.
Part-time staff are entitled to join pension schemes regardless of hours worked.	Until relatively recently, part-time staff have not generally been allowed to join schemes.
In case of death-in-service, a gratuity of twice pensionable pay is payable, irrespective of service.	The gratuity payable on death-in-service is equal to between 1 and $1\frac{1}{2}$ times pay depending on service.
A five year pension guarantee applies in death after retirement situation.	No such provision available.
No minimum service requirement for benefits.	Five years' service is required to qualify for retirement benefits.
The individual can opt out of scheme membership at any time (must opt for another pension arrangement).	Scheme membership is compulsory; there is no provision to opt out.
The spouse's pension on death-in-service is one-half of what the member would have received if he or she had retired on ill health grounds on the day of death.	The spouse's pension on death-in-service is one-half of what the member would have received had he or she served to age 65, subject to a maximum of 40 years.
Scheme benefits are not integrated with the state social security system.	Integration with the state social security system applies.
Pensionable pay is basic pay and allowances calculated on the best 12 months in the final three years of service.	Final pay is used in all cases except where a person has been promoted in the final three years of service, in which case an average is used.

APPENDIX 9.2

Comparison of special pension terms for public servants in the United Kingdom and Ireland

United Kingdom	Ireland
Police The maximum pension entitlement is 2/3rds of final pay up to a quarter of which can be commuted in exchange for a lump sum (60ths scheme). Fast accrual terms apply, i.e. maximum pension is payable after 30 years, with every year of service after 20 years counting as double. Retirement may take place after 30 years' service (regardless of age), from age 50 with at least 25 years' service, or from age 55 with less than 25 years' service. Compulsory retirement age for Constables and Sergeants is age 55.	**Garda Síochána** The Garda Síochána scheme is similar to the UK police scheme, even though a pension and lump sum (80ths accrual rate) is payable instead of a 2/3rds pension, with commutation. Members of the Garda Síochána may retire from age 50 (not at an earlier age) if they have completed 30 years' service. A higher maximum retirement age of 57 applies up to the rank of Inspector.
Prison Officers Prison Officers recruited since 1987 have similar pension terms to civil servants, i.e. an 80ths scheme and a requirement that they serve for 40 years to qualify for full pension. Prior to this date fast accrual terms applied.	**Prison Officers** Prison Officers have fast accrual terms, i.e. doubling of years for service in excess of 20 years. In addition, they have the option to retire from age 50 once they have 30 years' actual service. Maximum retirement age is 60.
Mental Health Officers Mental Health Officers in service prior to 1995 have fast accrual terms and the right to retire from age 55. New recruits since that date have standard public service pension terms, and have a retirement age of 60.	**Psychiatric Services** Psychiatric Nurses and other grades registered under the Mental Treatment Act, 1945 have fast accrual terms (doubling of years in excess of 20) and the option to retire from age 55. They have a maximum retirement age of 65.
Nurses The standard retirement age of 60 applies to nurses. However, nurses in service prior to 1995 have the option to retire from age 55, with benefits based on accrued service (fast accrual terms do not apply). This option was removed as part of an NHS package implemented in 1995.	**Nurses** Nurses have standard public service terms and can retire between age 60 and 65.
Fire Service The Fire Service scheme is similar to the Police Officer scheme described above, except that the earliest retirement age is 50.	**Fire Service** Pension terms are similar to those of the Garda Síochána and Prison Officers, except that retirement age is generally 55 for Firefighters and between 55 and 65 for officers.
Teachers Teachers have broadly similar pension terms to civil servants.	**Teachers** Teachers have standard public service terms, except for a provision which enables them to retire from age 55 provided they have 35 or more years' service.

APPENDIX 9.3

Retirement ages of certain categories of public servants in other European countries

Country	Police	Fire Service	Nurses	Teachers	Prison Officers
France	55-60	55-60	55-60/60-65 (i)	55-60	55-60
Portugal	56-62	50-60	—	—	—
Germany	60	60	—	65	60
Belgium	60-65	60-65	—	—	—
Denmark	60-63	60	60-65 (ii)	—	63
Finland	58 (iii)	—	—	60	—
Netherlands	—	65 (iv)	60	—	—
Austria	—	—	60-65	—	—
Sweden	—	55/60 (v)	63-65	—	—
UK	48-55	50-55	60	60	60
Ireland	50-57	55	60-65	55-65	50-60

Notes:

(i) The employment category in which a nurse works determines retirement age: if employed in class A (sedentary), a nurse can only retire from age 60, whereas if employed in class B (active), a nurse can retire from age 55.

(ii) A nurse can start drawing a pension from age 60; however, it is actuarially reduced. Full pension is payable from age 65.

(iii) Normal pensionable age for the police is age 63-66. However, they can choose a special occupational retirement age of 58.

(iv) Early retirement can be taken from age 60, but is subject to actuarial reduction.

(v) The flexible pension system allows Firefighters to leave at age 55 and officers at 60. They are then entitled to receive the flexible pension, to which is added a supplement which brings them up to around 80% of their former salary. The supplement is paid by the employer. At age 65, after this transitional period, Firefighters receive their normal retirement pension.

APPENDIX 9.4

Pension increases for public servants in a number of European countries

United Kingdom

1. Pensions are increased annually under the Pensions Increase Act, 1971 (as amended), in line with increases in the Retail Price Index. This is the same rate of increase as is applied to state social security benefits. Public service schemes which are not directly covered by the 1971 Act, e.g. those for the Armed Forces, apply a corresponding increase.

2. Pension increases are paid to pensioners aged 55 or over under all schemes (including the police scheme, under which it may be possible to retire from age 48 on); pension increases are not paid until the pensioner reaches age 55, with the following exceptions:

- where retirement was on grounds of ill health or permanent incapacity;
- where the pensioner is a widow or widower;
- pension is in respect of a child.

3. The pensions increase is paid in April of each year based on the rise in retail prices in the 12 month period up to the end of September of the previous year. For pensioners under age 55 (including those who retired under voluntary early retirement schemes), whose pensions will not generally be increased until they reach that age, when increases commence, the pension will get all the increases made since payment commenced.

4. Before 1971, there was no automatic right for civil service pensioners to receive pension increases after retirement. After a marked fall in the value of money causing hardship to pensioners, the Government sought the authority of Parliament to pay increases to alleviate this hardship. This *ad hoc* approach was criticised as causing uncertainty and delay, and the 1971 legislation introduced automatic increases in line with changes in the RPI.

5. There has never been a link between civil service pensions and earnings as a basis of revaluing pensions (*social security* pensions, rather than civil service pensions, were linked to the greater of increases in average earnings or prices between 1975 and 1979).

Germany

6. The adjustment of benefits for civil service pensioners is related to the pay of serving officers, which falls to be adjusted by law according to overall economic development. Pay increases for civil servants are the result of collective bargaining, and are generally lower than pay increases in the private sector. Pay is not always increased annually — in recent years, the collective bargaining has covered periods of 15/16 months. The rates of pay increases are passed on to pensions in payment, usually after a delay of a few months. A recent pay increase consisted of a flat payment of 300 DM to all civil servants. The same amount was paid to pensioners.

7. General *adjustment bonuses* in addition to the general pay increase negotiated through collective bargaining were paid on a number of occasions during the early 1990s. These payments were passed on to pensioners. The amounts involved will not attract any increases arising from future increases in pay. The practice of paying adjustment bonuses has now ceased. Following recent pension reforms, if any new bonus were to be paid, those who retired after 1 July 1997 would not be eligible to receive it in their pensions.

8. New performance related bonuses and premia have recently been introduced into the civil service. These take the form of faster progression along incremental scales. Pensioners will not be in a position to benefit from these.

9. It might be noted that Germany adjusts its state social security pensions in July of each year (usually) in line with the change in the net national average wage in that year compared with the previous year.

The Netherlands

10. Pension is based on final salary, less an amount in respect of General Old Age Pension. Following retirement, the figure for final salary is indexed in such a way that it will follow the income of serving civil servants. This is done on the basis of a public service pay index, which at the time of each update results in a single rate of increase to be applied to all public service pensions.

Sweden

11. Pension is composed of four elements: the state social security pension (which aims to provide about 60% of retiring income), comprising a career based pay-as-you-go element and a funded element, and a supplementary pension (providing about 10% of retiring income), comprising a final salary pay-as-you-go element and a funded element. The social security pay-as-you-go element is uprated according to an index reflecting both prices and real growth in the economy, while the supplementary pension is inflation protected by a Consumer Price Index which is uprated on a legislative basis annually.

Austria

12. Pension levels for civil servants are currently linked to salaries by means of an automatic incremental system. This means that a salary increase automatically results in an increase in pension payments and dependants' pensions. According to recent reforms to civil service pensions aimed at replacing the final salary system with a career based approach in line with other pension systems in Austria, the automatic incremental system will be replaced by the prevailing adjustment factor used in the statutory Social Insurance system. This rate takes into account the general economic development, increasing contributions collected from employees, price inflation and the constantly increasing life expectancy. The new adjustment system is scheduled to come into effect in 2000.

APPENDIX 9.5

Management and administration of public service pensions in countries with centralised arrangements

We summarise below the management and administrative practice of a number of countries in relation to public service pensions, focusing particularly on organisational structures.

- **The Netherlands:** Algemeen Burgerlijk Pensionenfonds (ABP), now privatised, administers the pension scheme for all public servants in the Netherlands. The schemes are fully funded. Changes to the pension arrangements are negotiated between employers and employees at a central level. While ABP is not active in these negotiations, it offers advice, particularly in relation to costs. ABP has full management responsibility for the schemes under its control and its administration systems (records, payments, etc.) are fully computerised.

- **Portugal:** Caixa Geral de Aposentacoes (CGA) administers the pension scheme for civil servants, local government employees and teachers in Portugal. Changes to the pension scheme are negotiated between government and unions and CGA offers advice in this regard to the Government. CGA manages the scheme centrally and holds all computerised records necessary for the management and administration of the scheme.

- **Belgium:** The Administration des Pensions (AP) Division of the Ministere des Finances is responsible for the pension arrangements which apply to civil servants, local government employees, teachers, police and army personnel in Belgium. Changes to the pension scheme follow negotiations between government and unions and AP advises the Minister for Finance in this regard. All records are computerised and AP calculates all pension awards. A different branch of the Finance Ministry (Treasury Administration) is responsible for payments.

- **France:** Caisse des Depots et des Consignations (CDC) is responsible for the pensions arrangements of local government staff and some health sector staff in France. (There is a separate pension scheme for civil servants which is the responsibility of the Minister for Finance.) Changes to the scheme are provided for by decree of the Minister for Finance with no previous consultation or negotiation with unions. The scheme is managed centrally by CDC and a governing board, which includes union representation, oversees its operations. CDC has a central database of pensioners and they pay all pensions within their area of responsibility. Records relating to serving staff are held by the employers and information for members is channelled through the employers by CDC.

- **Italy:** Instituto Nazionale di Previdenza per i Dipendenti dell' Amministrazione Pubblica (INPDAP) is responsible for the pensions of civil servants and local government employees in Italy. The pension arrangements are managed and administered centrally and they have a computerised database of members' and pensioners' records.

PART IV

Analysis and Assessment of Public Service Pension Arrangements

CHAPTER 10

Evolving Cost of Public Service Pensions

10.1 Introduction

10.1.1 In Part IV of the Report, we present an analysis of existing public service pension arrangements under a range of headings: the evolving cost of public service pensions, the adequacy and fairness of current pension arrangements, the consequences for pension schemes of changing operational requirements, work environment, and conditions of employment of public servants, and the need for flexibility in pension terms.

10.1.2 Chapter 6 outlined the future cost scenario for public service pension schemes, identified the factors behind the expected growth in costs and considered the implications which these costs will have for future generations of taxpayers. In this Chapter, we consider possible responses to the evolving pension costs, and discuss the impact on costs of some key changes in pension arrangements which have been examined by the Commission.

10.1.3 The Commission's terms of reference lay down a number of criteria for our examination of public service pensions. The first is to have regard to the present and future costs arising under the pension schemes financed by the Exchequer. This must, of course, be balanced against the other criteria listed. As discussed in Chapter 1, we have interpreted our main objective as securing the viability and stability of public service pension arrangements over the long-term. This objective underpins our analysis and assessment of long-term pension costs.

10.2 Summary of actuarial review

10.2.1 The main findings of the projections in Chapter 6 on future public service pensions expenditures and contributions are summarised below:

- in constant (1997) price terms, the existing level of gross benefit expenditure is expected to more than double over the next 15 years (i.e. by 2012), and to almost quadruple over the next 30 years (i.e. by 2027); the cost projections are summarised in Table 10.1:

Table 10.1 Expenditure projections for public service schemes

Year	Pensions expenditure	
	Ir£ (million)	*Euro€ (million)*
1997	636	*807*
2012	1,368	*1,737*
2027	2,408	*3,058*
2042	2,564	*3,256*

- for the 20 years after 2027, benefit expenditure is projected to display limited growth, with the reduction in the rate of growth partially attributable to the effects of integration with the State Social Insurance pension for post-April 1995 entrants (taking into account the increased cost of Social Insurance pensions, the *overall* impact on the Exchequer of extending full PRSI to public servants is expected to be broadly neutral — see Section 6.8);
- as member contributions will increase at a slower rate than gross benefit expenditure, net benefit expenditure (i.e. the difference between benefit payments and contribution income) is projected to increase at a higher rate than the rate of increase in gross benefit expenditure over the period to 2047;
- the main factors in the expected growth in public service pension costs include the increase in public service numbers which occurred during the 1970s and early 1980s, improvements in benefit terms and in pension scheme coverage, increases in public service pay relative to price inflation and the impact of increased life expectancy;
- expressed as a percentage of GNP,[128] gross benefit expenditure is projected to remain relatively static for the 10 years to 2007, and then to increase steadily from 1.6% to 2.4% of GNP in around 30 years' time. Thereafter, benefit expenditure will return gradually to a level of approximately 1.8% of GNP by the middle of the century;
- expressed as a percentage of pensionable pay, gross benefit expenditure is projected to grow from 16% of pay to around 38% of pay in 2027, before falling somewhat to 30% of pay in 2047;
- it has been estimated that if the additional pension costs in the year 2027 were to be incurred in 1998 and financed through taxation, it would require an increase of 2p on the standard rate of tax and 3p on the top rate of tax.

10.2.2 Based on the methodology and assumptions used in the actuarial review, the value in 1997 of the State's accrued liabilities in respect of public service pension schemes was estimated at approximately £20 billion (€25.4 billion).

10.2.3 The review found that new entrant rates (the contribution rates which would be required to fully fund the pension benefits of a new employee over the period of employment) vary considerably between sectors and groups within the public service, ranging from 8% to 30% of pensionable pay. The degree of variation in the rates reflected the benefit terms and conditions applying to each group (e.g. earlier retirement ages result in higher new entrant rates), the promotional salary scale assumed (the rates are higher where significant salary increments and/or career progression can be expected), assumed average age at entry, etc. It was calculated that benefit scales for groups with special pension terms cost up to twice as much as the standard civil service benefit scale.

10.2.4 Based on the actuarial review, we conclude that concern over the size of the pensions bill is justifiable, particularly when considered in the light of claims for further cost increasing improvements in pension terms (e.g. early retirement) from a number of public service groups.

10.3 Possible responses to evolving pension costs

10.3.1 Since the Commission takes the view that the accrued benefit entitlements of serving public servants and of pensioners should be protected, this limits the scope for bringing about an

[128] Paragraph 6.2.12 sets out the Commission's assumptions regarding future GNP growth rates.

outright reduction in future pension costs. Thus, the main burden of adjustment must be related to new entrants and to future entitlements of existing employees.

10.3.2 The claims for benefit improvements which have been made by public servants (for example, in relation to early retirement) would, if conceded, result in a further increase in costs over existing projections. In addition, the rise in pension costs is influenced by external developments such as judgements of the European Court of Justice in relation to pensions for part-time employees.

10.3.3 A fundamental equation of pensions financing is that *Benefits equal Costs*. Thus, a reduction in costs can only be achieved at the expense of an equivalent diminution of benefits. Conversely, it is not possible to improve benefits without an exactly corresponding increase in costs. The equation can sometimes be obscured by timing differences; an increase in benefits today (with little or no immediate cost) can involve large cost increases in the future.

10.3.4 The future cost profile of public service pensions involves steady growth over the next 15 years, with a substantial *peak* occurring in the years from around 2017 onwards. It would be difficult to countenance measures which would add to costs during that peak period. Ideally, efforts should be made to reduce the peak in costs.

10.3.5 Given the above considerations, the appropriate response, in the Commission's view, is:

(i) to find ways of smoothing the expected peak in costs, including the use of pension funding;

(ii) to limit any recommended scheme improvements to cost neutral changes, or to cost increasing changes considered absolutely necessary for operational reasons or on grounds of equity and fairness, with a view to preventing as far as possible any net enlargement of the rise in the pensions bill;

(iii) to estimate the impact on long-term costs of all major suggested changes in pension terms;

(iv) to permit as much individual flexibility as possible, consistent with the overall framework of the pensions system, to allow employees to provide for benefit improvements by means of personal contributions (the new flexibility to be facilitated through better communication systems);

(v) where a disimprovement in benefit terms is considered necessary, to confine the change to new entrants only, while having due regard to intergenerational equity.

10.3.6 In order to determine what scope is available for changes of this nature, it is necessary to examine in detail the cost implications of some of the possible improvements and disimprovements in pension terms, as well as the effect of pension funding. We will present a detailed analysis of the issues involved later in the Report; the purpose of the current exercise is to consider the potential long-term cost implications of items such as early retirement, integration, pensions increase policy and funding.

10.3.7 The Commission favours the introduction of a more transparent system of accounting for pension costs within government financial procedures. Such a system would assist in the effective management of the future evolution of public service pension costs. The Commission's recommendations in this regard are presented in Chapter 24.

10.4 Cost implications of improvements in pension terms

10.4.1 The main issues identified by the Commission (see Paragraph 2.1.1) which involve possible improvements to pension terms are:

(i) early retirement;

(ii) integration between occupational pensions and the State Social Insurance system;

(iii) pensions and atypical employment;

(iv) dependants' benefits.

In this Section, we examine the cost implications of (i) and (ii), both of which would have major implications for public service pension costs. We cost items (iii) and (iv) together with a number of other possible changes to pension terms in the appropriate Chapters in Part VI of the Report.

Early retirement

10.4.2 Generally the effect of early retirement without the application of a *cost neutral* actuarial reduction factor is to increase pension costs. The reasons for this are that the lump sum has to be paid earlier, and pension payments begin earlier and have, on average, to be paid for a longer period. While it is true that a pensioner may receive only half, or less, of annual salary in pension, and that the replacement cost of new personnel may initially be below this figure, in the long-term, the cost additions outweigh any cost savings.

10.4.3 The fact that individuals retiring early would have lower service and consequently lower pension entitlements than if they had remained to normal retirement age would have limited bearing on the overall cost situation. At any rate, depending on the terms of the early retirement programme, notional added years of service are often included for the calculation of pension benefits (see, for example, Paragraph 3.3.38 regarding the public service voluntary early retirement scheme of 1987-88).

10.4.4 At a broad policy level, early retirement programmes were often proposed as a means of opening up employment opportunities and so helping to combat unemployment. Governments were disposed to accept this approach in times of relatively low pension costs and of high youth unemployment. However, in recent years, this argument has been rejected by many international organisations (see Paragraphs 7.4.9 and 7.6.3), mainly on grounds of the severe pressures which early retirement places on public pension systems.

10.4.5 Another justification for early retirement schemes is that sometimes older staff may not need to be replaced. Their productivity in the job may have declined. This could arise because of skill obsolescence or because of demoralisation factors. Clearly, estimates of the cost of early retirement must take account of the productivity of the retiring employee (and, where relevant, of the replacement employee) as well as the standard financial variables.

10.4.6 The cost of early retirement from a macroeconomic viewpoint could be different from the cost of early retirement from the perspective of the national finances. From the former viewpoint, the cost is the output foregone of the retiree. Even if the retiree were producing very little while at work, withdrawal from the workplace means that this output is lost to society. There is also a redistributive cost – the retiree has to be provided for from the output produced by those actively engaged in the workforce. To the extent that the retiree moves to other forms of employment (see Paragraph 7.4.15) the net effect of early retirement is to shift a section of the labour force from one employment status to another. The social cost of early retirement declines. Herein lies the economic rationale for encouraging various types of employment following formal retirement. From the narrower perspective of the State finances, such offsetting gains are of limited relevance. Early retirement remains an expensive and unnecessary subsidy for greater labour market mobility. Broadly the same goal could be achieved at less cost through employers making available more flexible working arrangements for employees approaching the end of their career.

10.4.7 From the perspective of the national finances, the precise costs of early retirement can be difficult to measure. For example, it might be unclear what numbers would avail of an early retirement programme. Much would depend on the terms offered, the state of the economy at the time, the availability of other employment opportunities, etc. For pension schemes, early retirement would most likely involve the following costs:

- payment of pension benefits over a longer period of time;
- granting of added years of notional service;
- foregoing of the employee's pension contributions over the period to normal retirement age.

10.4.8 The Commission has decided that the best measure of early retirement for public service schemes is to quantify the additional capital cost of the early retirement terms for a cross section of the population of public servants that might be expected to avail of them. In the following costings — done for a sample of public service grades: established civil servants, teachers, and general nurses — the capital cost is expressed as a multiple of salary of the individual concerned at the time when the early retirement option is being considered. This facilitates ready comparison with the employer's payroll costs in respect of that individual at the time. The extra cost of the early retirement in each case is calculated as the difference between the actuarial value of the immediate lump sum and pension benefits (payable at the earlier retirement age) and the actuarial value of existing accrued benefits payable from the earliest age at which retirement is normally permitted.[129] In this regard, the earliest normal retirement age for established civil servants and general nurses is taken as age 60 and for teachers, age 55 (assuming 35 years' service).

10.4.9 By way of example, the immediate pension benefit payable to a 55 year-old civil servant with 30 years' service, assuming the grant of five added years of pensionable service (option (ii) in Paragraph 10.4.10), is 35/80ths of salary. At the time of early retirement, the civil servant's accrued normal pension entitlement is considered to be 30/80ths of salary payable from age 60. When valuing this accrued benefit, an allowance is made in the calculations for future salary progression. It is the difference between the values of these two benefits (and associated benefits such as the retirement gratuity and spouses' and children's pensions) that is being assessed.

10.4.10 For the purposes of the costing, two different sets of early retirement terms have been assumed: early retirement from age 50 or over based on accrued pensionable service to date with no actuarial reduction and with

(i) no added years of pensionable service;

(ii) up to five added years.

[129] Other approaches could have been adopted, depending on what is considered to be the value of the individual's benefits in the absence of the early retirement options. For example, we could have represented this value by reference to the individual's preserved entitlements on leaving service, being his or her strict entitlements at that time. This would be the correct approach if the individual had left service in the absence of an early retirement option. We have rejected this approach on the grounds that the individual would perhaps be unlikely to leave service of his or her own accord in the absence of some favourable initiative.

10.4.11 Based on the methodology outlined, Table 10.2 gives an indication of the capital cost of early retirement, expressed as a multiple of final salary, for a typical individual in the three sample groups. The cost for a range of different retirement ages and completed years of service are presented.

Table 10.2 Capital cost of early retirement expressed as a multiple of salary for a number of public service groups[130]

Group	Age of early retirement	Past Service	(i) No added years	(ii) Up to 5 added years
	(years)	(years)	Capital cost (as multiple of salary)	
Civil servant	50	25	2.73	4.35
	55	30	1.71	3.21
Teacher	50	25	2.53	4.15
	55	30	1.6	3.09
Nurse	50	25	2.66	4.29
	55	30	1.69	3.18

10.4.12 Taking the example of a civil servant retiring under option (i) at age 50 with 25 years' service, the cost of early retirement with no added years of service is estimated at 2.73 times salary. This figure represents the difference between the capitalised value of the pension benefits payable on early retirement (calculated at 8.13 times salary) and the capitalised value of the pension benefits payable at age 60, based on accrued service at age 50 (5.4 times salary). Thus, for a civil servant with a basic salary of £28,738,[131] the early retirement cost, in capital terms, would amount to just over £78,000. This sum represents the additional cost to the pension scheme of payment of pension benefits (based on accrued service) earlier than the normal age of retirement.

10.4.13 If, instead, the individual had taken early retirement under option (ii) and five added years had been granted, the early retirement of the civil servant in the above example would have cost 4.35 times salary, a capital cost of about £125,000.

10.4.14 Obviously, the cost of early retirement will be lower the later the age of retirement. Also, the cost at any age will be lower for individuals having levels of past service lower than those indicated.

10.4.15 It is worth noting that early retirement on grounds of ill health imposes pension costs of a similar scale. For example, the cost of early retirement for a typical civil servant who is retired on grounds of ill health at age 50 having 25 years' service is 3.55 times salary. As before, this sum represents the additional cost to the pension scheme of payment of pension benefits earlier than the normal age of retirement.

10.4.16 Groups with special pension terms — e.g. Garda Síochána, Prison Officers — have benefit scales which in effect provide for early retirement from age 50 or 55 with enhanced pension terms, although they are generally subject to a lower maximum retirement age than the norm. We detail the additional cost which these scales impose compared with the standard civil service

[130] Costings are taken from Commission on Public Service Pensions, "Further Actuarial Review of Impact of Changes to Pension Scheme Terms" (October 1999), Report prepared by Mercer Ltd.
[131] Maximum point of civil service Higher Executive Officer higher scale on 1 April 2000.

type benefit scale in Paragraphs 6.6.5-6.6.7. We show, for example, that the cost of the Garda benefit scale if applied to an established civil servant would almost double the new entrant rate of 16%.

10.4.17 As already noted, the Commission considers that estimating the cost of early retirement is best done using the capital cost approach. However, we also carried out a costing to show the effect on future cashflows of implementing an early retirement facility for groups having standard pension terms (including teachers, who may retire from age 55 having 35 years' service). We assumed that up to five added years would be granted,[132] and that the scheme would be open to all personnel. Certain assumptions about age retirement patterns were necessary for the purposes of the costing.

10.4.18 On the basis of these assumptions, it was calculated that annual benefit expenditure on public service pensions following implementation of the new facility would increase in constant (1997) price terms by £46 million in 2002 (6% of projected expenditure in that year), rising to £79 million in 2017 (4% of projected expenditure), and £153 million in 2047 (6% of projected expenditure). These results can be compared with the cashflow projections reported in Chapter 6 and summarised at Paragraph 10.2.1. It was estimated that a facility of this nature would add approximately £760 million to the State's accrued liability in respect of public service pensions.[133]

10.4.19 These figures show that early retirement can give rise to substantial additional pension costs. The Commission accepts that there are situations and cases in which early retirement is the appropriate option. However, given the objective of minimising the growth in future pension costs, it is clear that early retirement should be implemented with circumspection. The Commission's views and recommendations on early retirement are presented in Chapter 15.

Integration between occupational pensions and the State Social Insurance system

10.4.20 We describe the practice of integration in Chapter 3. Integration is applied to both contributions and benefits. In the case of the latter, a deduction of twice the single person's rate of Old Age (Contributory) Pension (OACP), currently £10,019 per annum, is deducted from gross pensionable remuneration and pension is calculated using the net figure. Integration applies to all public servants appointed on or after 6 April 1995, as well as to public servants in areas where full PRSI applied prior to that date. Thus, in time, integration will apply in respect of all public service pension schemes.

10.4.21 If integration were to be removed it would have a major effect on the long-term cost of public service pensions. If the change were applied to all serving public servants, the increase in annual benefit expenditure in constant (1997) price terms, while low initially, would rise to £112 million in 2027 (5% of projected expenditure in that year), and reach £427 million by 2047 (16% of projected expenditure).

10.4.22 The effect of the change would be to add over £500 million to the State's accrued liability, primarily in respect of groups which were already in full PRSI class prior to the change of

[132] The amount of added years would be equal to the individual's potential service between date of early retirement and his or her 60th birthday — subject to an overall maximum of 40 years.
[133] Commission on Public Service Pensions, "Actuarial Review of Impact of Changes to Pension Scheme Terms" (December 1997), Report prepared by IPT Actuarial Services Ltd.

6 April 1995.[134] The removal of integration would result in an increase in the new entrant rate for an established civil servant from 16.3% to 20.4% of salary plus pensionable allowances.[135]

10.4.23 The Commission discusses integration in Sections 11.5 and 11.6 of the Report. We present our recommendations on this matter in Chapter 17.

10.5 Impact on future cashflows of disimprovements in pension terms

10.5.1 When considering possible disimprovements in pension terms it is essential to have regard to the entitlements of serving staff which have been earned through past service. Often, the general pensions approach is to make changes which will affect pension entitlements to be earned over future service (but not past service) of serving staff and/or or the pension entitlements of new entrants. Of course, whichever approach is adopted will have implications for how quickly the change will impact upon future pension costs.

10.5.2 We examine the cost implications of possible disimprovements in pension terms as follows:

- raising the age of retirement;
- a change in pensions increase policy;
- an increase in the rate of employee contribution.

Raising the age of retirement

10.5.3 Several countries have raised or are in the process of raising the age of retirement in order to curb rising pension costs (see Section 9.8 for a summary of recent changes in public service pensions terms in a number of countries).

10.5.4 Later retirement age implies a longer period in work and a shorter period in retirement. Thus, an increase in retirement age, while almost certainly resulting in an increase in pensionable pay, should at the same time lead to a reduction in the average period over which a pension would be paid. The overall effect on pension schemes should, therefore, be to reduce pension costs.

10.5.5 The Commission examined the effect on public service pension costs of increasing retirement age by five years. Such a change would generally mean minimum-maximum retirement ages of 65-70 for those with standard terms and 60-65 for those with special terms.

10.5.6 Making certain assumptions about age retirement patterns following the change, we estimated that the impact on public service pension costs, in constant (1997) price terms, would be as follows:

- if applied to all public servants (i.e. serving staff and new entrants), the change would result in savings in annual gross benefit expenditure of £50 million in 2002 (6% of projected expenditure in that year) rising to £120 million by 2017 (7% of projected expenditure). The level of savings would fall over the following 20 years, before rising again, reaching £201 million in 2047 (8% of projected expenditure);

[134] Commission on Public Service Pensions, "Actuarial Review of Impact of Changes to Pension Scheme Terms" (December 1997), Report prepared by IPT Actuarial Services Ltd.

[135] Commission on Public Service Pensions, "Actuarial Review of Public Service Pensions" (November 1997), Report prepared by IPT Actuarial Services Ltd.

- if applied to new entrants only, there would be no effect on annual gross benefit expenditure in the period to 2022, but savings would commence from around 2027 onwards, rising to around £100 million per annum in the period 2037-47 (4% of projected expenditure).

10.5.7 The increase in retirement age (if applied to serving staff) would bring about a reduction in the State's accrued liability for public service pensions of about £1 billion (5% of total liabilities). Similarly, there would be a reduction in new entrant rates for the public service groups affected, e.g. the new entrant rate for an established civil servant would be 13.9% compared with the existing rate of 16.3%.[136]

10.5.8 Some slight downward revision of these estimates could be required to the extent that a longer period in work would entitle some public servants to accrue service in excess of forty years. Also the assumption of *content productivity* might be questioned — can five further years be added without detriment to the quality and quantity of work undertaken by the affected employees? The Commission's recommendations on retirement age are set out in Chapter 15.

Change in pensions increase policy

10.5.9 Public service pensions are increased in line with the pay of serving public servants. Historically, pay has tended to increase faster than price inflation, as measured by changes in the Consumer Price Index (CPI). For example, over the period March 1988 to September 1998, the cumulative percentage change in the CSO public sector earnings index was 66%, compared with a cumulative change of 31% in the CPI over the same period. Over the past 15 year and 30 year periods, increases in public service pay rates mostly fell within the range of 1% to 2% per annum in excess of price inflation; in the Commission's actuarial review, a future rate of general salary growth of 1.5% in excess of price inflation was assumed (see Paragraph 6.2.13).

10.5.10 Thus, changing pensions increase policy from salary-related increases to increases in line with the CPI would cause a reduction in the future cost of pension increases. The Commission calculated that the effect of the change on future pension gross expenditure, in constant (1997) cost terms, would be as follows:

- if applied to new entrants and to the future service of serving public servants, the new pensions increase policy would save £36 million in 2017 (2% of projected expenditure in that year), £128 million in 2027 (5% of projected expenditure), and £327 million in 2047 (12% of projected expenditure);
- if applied to all pensioners, preserved pensioners, serving public servants and new entrants, there would be savings of £45 million in annual benefit expenditure in 2002 (6% of projected expenditure), rising to £196 million in 2017 (11% of projected expenditure), £342 million in 2027 (14% of projected expenditure), and £453 million in 2047 (17% of projected expenditure).

10.5.11 If the change to pension increases were to be applied to all public servants with immediate effect, there would be a reduction in the State's accrued liabilities of just over £2.6 billion (13% of total liabilities). New entrant rates would also be affected. For example, the new

[136] Commission on Public Service Pensions, "Actuarial Review of Impact of Changes to Pension Scheme Terms" (December 1997), Report prepared by IPT Actuarial Services Ltd.

entrant rate for an established civil servant would be reduced from 16.3% to 14.4% if the new pensions increase policy were implemented.[137]

10.5.12 Chapter 16 presents the Commission's deliberations and recommendations on future pensions increase policy.

Increase in rate of employee contributions

10.5.13 There would be a saving in the cost of pensions to the State if serving public servants were required to pay an increased rate of pension contribution. An increase in contributions of 1% (of pensionable pay) would bring about a saving, in constant (1997) price terms, of £38 million in 2002 (5% of projected expenditure in that year), rising to £58 million (2% of projected expenditure) in 2047.[138] The saving to the State resulting from the additional contribution would fall as a percentage of annual pensions expenditure in the period under review.

10.6 Funding

10.6.1 Advance funding represents a means of smoothing long-term pension costs. Monies could be invested in a fund over a period of years when expenditure on pensions was relatively low. The fund would be available to meet part of the cost of pensions in future years — say, from around 2017 onwards — and thus limit the sums which would be required from taxation to meet the cost of pensions in those years. This would not represent full funding along the lines of pension funding in the private sector. Instead, the purpose of this *partial fund* would be to help manage the expected future profile of pension costs, particularly during the period of the expected peak in pension costs in the years 2017-2032.

10.6.2 A fund of this nature could be established in two ways, or by a combination thereof: by deposit of a large initial amount (say by proceeds of privatisation), or by an annual Exchequer contribution. If the latter approach were followed, contributions would be in addition to annual pay-as-you-go benefit expenditures. Any outflows from the fund would reduce the Exchequer's pensions bill. The net impact of the fund on the Exchequer's position in any year would, therefore, be the difference between the contributions paid to the fund and the amount of benefit payments, if any, met by the fund. In general, in the early years of a new public service pension fund, the impact on the public finances would be negative, as the contributions needed would be greater than the outflows from the fund; at some future year, a break-even point would be reached, and thereafter, the annual outgo from the fund would exceed contributions. The level of payments to beneficiaries would not, of course, be affected by the existence of the fund.

10.6.3 The experience of annual budget surpluses in recent years, with the expectation of their continuation for some time into the future, has given added impetus to the debate on pension funding. Another factor has been the exceptionally favourable returns on equity investment during the past decade. As outlined in Section 5.3, the Government decided in July 1999 to allocate resources for the pre-funding of Social Welfare and public service pensions broadly along the lines outlined above, and has recently published a Bill to give legislative effect to that decision.

10.6.4 Funding for the purposes of smoothing the future cost profile of public service pensions will not cause a reduction in those costs. The funding mechanism merely represents

[137] *ibid.*

[138] Commission on Public Service Pensions, "Further Actuarial review of Impact of Changes to Pension Scheme Terms" (October 1999), Report prepared by Mercer Ltd.

a means of bringing forward those costs to a time when they are more affordable. The Commission has expressed concern about the long-term cost of public service pensions under the current pay-as-you-go system. The establishment of a pension fund will not of itself lessen that concern, although the fund could have the effect of obviating the need to take some more drastic action at a later stage.

10.6.5 It is sometimes argued that pension funding makes pension benefits more affordable. The reasoning behind this argument is that the investment return on the monies lodged to the fund is greater than the return which the Government would have obtained on its alternative use of those monies. Another argument is that funding increases total real investment within the economy, which means that when the pensions come to be paid, the economy is more productive than it otherwise would have been.

10.6.6 Both of these arguments have been vigorously contested. Instead of setting up a fund, the Government could use the money to invest directly in infrastructural projects, or return the money to the private sector and allow individuals make the choice of how to invest or most productively spend it. It is not obvious that the returns on an investment fund would necessarily be higher over the long run than the returns on either of the above. Also, we must beware of extrapolating too much from the exceptionally high returns yielded from stock market investments in the US and Europe during the past decade. Perhaps the strongest argument in favour of funding relates to the dangers of over-investment by the State, or worst, wasteful consumption, given its present financial strength.

10.6.7 There is no simple direct link between an increase in the flow of money into funded pension schemes and increased capital formation. The factors that determine the level of capital formation are many and disparate. Even the evidence that is most favourable to the view that funding pensions leads to additional capital formation, suggests that it is a blunt and inefficient instrument to that end. The conclusion is that funding pensions schemes does not necessarily create additional resources that will significantly ease the cost of future pensions.[139] It is our view that a hard-headed approach to the current enthusiasm for funding is well justified.

10.6.8 The strongest points in favour of funding relate to:

- the desirability of smoothing the pensions bill, ensuring greater stability in pension costs, and hence contributing to stability in future taxation/spending patterns;
- the improvement in transparency and cost discipline which funding would bring;
- the need to diversify state expenditure at a time when the economy is at or near full employment and revenues are buoyant; and
- the need to minimise the risk resulting from a too heavy reliance on pay-as-you-go as the basis for financing future pension costs.

10.6.9 The ground rules for setting objectives and determining the management of a pension fund are of course important factors to consider. They are examined as part of our detailed considerations and recommendations in relation to funding public service pensions, as set out in Chapter 23.

[139] Daykin, C., Davis, B., "The Role of the State in Pension Provision", paper presented to the Institute of Actuaries, 23 March 1998; Daykin, C., *Funding the Future? Problems in Pension Reform*, Politea, 1998.

10.7 Conclusions

10.7.1 The evolving cost of public service pensions is a matter of serious concern. It will occur at a time when the effects of demographic ageing generally will begin to impact upon the cost of Social Welfare and health care provision. Against this cost backdrop, it is essential to evaluate carefully any further commitments that would add to the growth in future pension costs. This Chapter has detailed the cost implications of a number of possible changes in pension arrangements.

10.7.2 The pension scheme is an important component in public service remuneration. As such, it has a considerable impact upon the competitiveness of the economy as a whole. In many countries and in the private sector, in the face of changing demographic and competitive pressures, pension schemes have been reformed with the aim of containing long-term costs. Pension schemes in the public service in Ireland are not immune to these pressures.

10.7.3 Funding has been suggested as a means of addressing the evolution of pension costs over the long-term. As has been shown, funding, of itself, will not reduce the cost of pension terms. The means of financing pension schemes is separate to consideration of the cost of the schemes. However, funding could play a valuable role in smoothing the cost profile and thereby stabilising the fiscal and tax environment in future years.

10.7.4 The Commission's aim is to bring together an integrated set of recommendations which address the issues raised, giving due regard to the cost implications of each. Taking on board the role of funding in managing the development of pension costs, the integrated package of measures will, in our view, be consistent with the objective of securing the viability and security of pension schemes while at the same time addressing the reasonable concerns of employees and of pensioners.

CHAPTER 11

Assessment of Adequacy and Fairness of Public Service Pension Schemes

11.1 Introduction

11.1.1 The Commission has identified the major issues to be addressed in our review of public service pensions. We have described in detail the current occupational pension arrangements applying in the public service, and have considered the changes occurring in the operational requirements, working environment, and conditions of employment of public servants. We have examined current occupational pension arrangements and trends for employees in the private sector and public services abroad. In addition, we have presented a comprehensive projection of the future cost profile of public service pensions, discussing in particular the scale and impact of the expected growth in pension costs.

11.1.2 At this point, the Commission is now in a position to make an assessment of public service pension schemes in relation to the issues to be addressed. Accordingly, in this Chapter we present a fuller outline of each of the issues and present an initial discussion of the adequacy and fairness of public service pension terms. We focus our discussion on the issues raised in submissions and otherwise identified by the Commission. These are — in the main — set out in Chapter 2:

- access to schemes;
- retirement age and early retirement;
- accrual rates and retirement income objective;
- integration of occupational pension with State Social Insurance benefits;
- integration and low levels of occupational pension;
- integration in the case of part-time public servants;
- pensions increase policy;
- contributions by public servants towards the cost of pension benefits;
- dependants' benefits.

Flexibility in pension terms, also identified by the Commission as a major pensions issue, is dealt with separately in Chapter 12.

11.1.3 For the purposes of our analysis, the meaning of the terms adequacy and fairness is as set out hereunder.

11.1.4 *Adequacy* refers to the coverage of occupational pension schemes, the level of benefits provided, and the conditions of entitlement to benefits in relation to the public service as a whole and to certain groups in particular. It is measured by reference to the Commission's assessment of the operational requirements of the service, the needs of public servants and pensioners, and pension provision for broadly comparable employments in the private sector and in the public service abroad.

11.1.5 *Fairness* refers to the actual application of pension terms and conditions of entitlement under the public service pensions framework and how their application compares as between different parts of the public service.

11.2 Access to schemes

11.2.1 In general, the public service has a good record of access to occupational pension schemes for its employees. Pension schemes are available in all areas, particularly for full-time permanent public servants, and there is no qualification period to be served before employees become eligible for membership.

11.2.2 However, pension coverage for public servants in atypical forms of employment appears to be problematic. In the past, temporary and part-time public servants were excluded from membership of schemes, although there were arrangements to make temporary and part-time service pensionable on subsequent appointment to full-time permanent positions. More recently, however, policy as regards the former has been changed to allow immediate access to pension schemes where contracts are potentially renewable.

11.2.3 For part-time employees, the question of access is closely linked to the pension terms to be applied (see Section 11.7). Again, there have been recent developments, particularly at EU level. But, for the moment, many part-time public servants are not included in public service schemes. Exclusion from pension schemes means not only the non-accrual of pension entitlements during service, but also lack of coverage for death-in-service and ill health benefits (although compassionate gratuities may be payable — see Paragraph 3.3.63).

11.2.4 In the case of certain groups, e.g. those providing services to the State on a fee paid or contract for service basis, pensions coverage is complicated by the question of whether or not these groups should be considered as public service employees at all. We examine this matter in Section 22.8 of the Report.

11.3 Retirement age and early retirement

11.3.1 Many submissions to the Commission sought the introduction of early retirement facilities and/or the extension of lower retirement ages and enhanced pension terms which are available to certain groups for operational reasons. As regards the latter, submissions argued that it was unfair and inequitable that certain groups enjoyed enhanced terms while others engaged in work of a similar nature did not.

11.3.2 In Section 8.7, we show that normal retirement age in most public service schemes in Ireland is generally lower than normal retirement ages in pension schemes in the private sector (i.e. retirement between ages 60 and 65, as compared with a single normal retirement age of 65). As indicated in Section 9.7, higher pension ages apply in a number of public service schemes in other countries. It should be acknowledged, however, that in both the private sector and the public service abroad, the actual average age of retirement, after factoring in early retirements on grounds of ill health, organisational restructurings, etc., can be much lower than the formal age of retirement.

11.3.3 In Paragraph 7.4.7, we note the argument that the process of ageing should not necessarily be associated with a loss of functional capacity and productivity. There is a growing acknowledgement internationally that there are no medical or scientific criteria which would suggest that people should retire in their 60s, and that people have the capacity to work as well as learn and enjoy leisure for a much longer period of time. This, combined with concern about increasing pension costs, has led many countries to raise State retirement ages and to examine flexible work-retirement transition arrangements.

11.3.4 The Commission considers that the establishment of a reasonable and fair retirement age is difficult and that there are no generally accepted principles about how it should be done.[140] There are many conflicting interests at stake. The fact that there is such diversity of employment within the public service — with a range of different operational requirements — means that it is not possible to apply a uniform approach to retirement age. Employees and employers have different perspectives based on their own needs and experience and these can change significantly over time. For example, existing retirement ages were generally established at a time when both life expectancy and the work environment were very different to what they are today. Accordingly, some employers would argue that special terms are no longer appropriate in certain areas due to changes in the nature of a profession, while some employees would contend that their work environment has so significantly altered over time that special terms should be extended to other groups.

11.3.5 In addition to these conflicting interests, the situation is complicated by the fact that working life is undergoing a process of rapid change and this applies also to the special needs of certain professional categories.

11.3.6 Having examined these factors, we make a series of recommendations in Chapter 15 on the normal retirement age for public servants, voluntary early retirement, and the special retirement provisions applicable to certain groups for operational reasons. We also address a number of related matters, including flexibility in working arrangements and phased retirement.

11.4 Accrual rates and retirement income objective

11.4.1 In addition to benefits on death-in-service, public service pension schemes provide for retirement benefits (pension and lump sum) and spouses' and children's benefits. Retirement benefits are earned or *accrue* for each year of service at a rate of 1/80th of pensionable remuneration for pension and 3/80ths of pensionable remuneration for lump sum.[141] Spouses' and children's benefits are usually related to retirement pension.

11.4.2 Retirement benefits are maximised after 40 years' pensionable service (actual service may be in excess of 40 years). The benefits for a public servant retiring after 40 years' pensionable service comprise a pension of 50% of pensionable remuneration and a lump sum of 150% of pensionable remuneration.

11.4.3 By comparison, a typical private sector scheme will generally provide retirement benefits of 1/60th of final (i.e. pensionable) remuneration per year of service, equal to two-thirds of final

[140] See, for example, Ekebrand, S., "Pension Systems for Civil Servants" in OECD *Civil Service Pension Schemes* Sigma Papers: No 10 (Paris, 1997), pp. 28-29.

[141] A small number of public service schemes (e.g. in some of the universities) have a 60ths accrual rate, as applies in many private sector schemes. In addition, some employees covered by the Local Government Superannuation Scheme availed of the option to retain 60ths accrual when the 80ths scheme was introduced during the 1970s (see Paragraph 3.4.5).

remuneration after 40 years' service, of which the individual is entitled to convert (or commute) a portion to provide a tax-free lump sum of up to 150% of final remuneration (see Section 8.11).

11.4.4 It has generally been accepted that maximum public service benefits are equivalent to the private sector pension target of two-thirds of final remuneration. The Superannuation Act, 1909 introduced death benefits and the retirement lump sum under the Civil Service Pension Scheme (see Paragraph 3.3.2). It did this on a cost-neutral basis by reducing the amount of annual pension in order to provide both a pension and a sum of money. The existing 60ths accrual rate was replaced with an accrual rate of 1/80th for pension and 1/30th (changed in 1973 to 3/80ths) for lump sum. The assumption underpinning the change was that by foregoing an amount of annual pension equal to the difference between 50% and 66% of pensionable remuneration, i.e. one-quarter of pension, this would *buy* a once-off lump sum of one-and-a-half times pensionable remuneration, on the basis that each £1 of pension would have the same value as a lump sum of £9.[142]

11.4.5 In Table 11.1 we give an example to illustrate how a private sector (60ths) scheme allowing commutation of benefits at a rate of £1 pension equals £9 lump sum provides the same pension and lump sum as a public service scheme.[143]

11.4.6 As the example indicates, the pension benefits which public service schemes provide at point of retirement are on a par with those of the vast majority of private sector defined benefit (60ths) schemes, which adopt a 1:9 commutation rate for lump sum. Because pension increase arrangements are more favourable in public service schemes compared with private sector schemes, it follows that the cumulative value of public service benefits will normally exceed the cumulative value of the private sector benefits.

Table 11.1: Comparison of public service and private sector pension scheme (with commutation on a 1:9 basis) for a person retiring with 40 years' service on a final salary of £24,000[144]

Public service benefits

Pension:	£12,000 per annum (40/80ths)
Lump Sum:	£36,000 (120/80ths)

Private sector benefits, assuming 1/60th accrual rate, and commutation on 1:9 basis

Original Pension: 40/60ths x £24,000 = £16,000 per annum

Commutation of $\frac{1}{4}$ pension on 1:9 basis provides:

Lump Sum: 9 x £4,000 = £36,000
(i.e. foregoing £4,000 per annum of pension allows the person to *buy* a once-off lump sum of £36,000)

After commutation, pension is £12,000 per annum

11.4.7 A small number of private sector schemes provide for commutation on a basis other than 1:9. In Appendix 11.1, we carry out a detailed comparison between the value of the benefits provided under one such scheme with the value of the benefits provided by a typical public service scheme. Our findings show that for the small number of private sector schemes which

[142] A pension of 1/6th of final earnings, if valued on 1:9 terms, is worth 9 × 1/6th = 1.5 times final earnings.

[143] In the private sector, most schemes allow commutation of benefits at a rate of £1 pension equals to £9 lump sum for male employees at age 65, i.e. a commutation rate of 9.0. Generally, the commutation rate for female employees at age 65 is 9.8.

[144] The comparison would also hold true if both schemes were integrated with Social Insurance benefits. With the current OACP rate of £96 per week, occupational pension would be £6,991 per annum under the public service scheme and £10,991 per annum, before commutation, under the private sector scheme (assuming a Social Welfare offset of $1\frac{1}{2}$ times OACP). The difference of £4,000 per annum is the amount of pension foregone under the private sector scheme to provide a lump sum of £36,000.

adopt more favourable commutation rates than 1:9, resulting in a more favourable outcome in terms of pension and lump sum at point of retirement, the differences in pension increase arrangements mean that over time the cumulative value of the public service benefits will normally outstrip that of the private sector benefits.

11.4.8 In Table 9.2, we set out the maximum pension benefits for public servants in a range of European countries. We show that the quantum of benefits varies between 57% and 83% of pensionable salary[145] (in many cases, after 40 years' service, and at retirement ages not very different to those in Ireland). Just over half of the countries surveyed pay maximum pension of between 70% and 80% of pensionable salary. While public service pension benefits in Ireland might appear to be low in comparison, it must be remembered that the Irish system of increases in line with pay is favourable compared to other countries, and that in public service pension schemes in Ireland the percentage is calculated (in most cases) on final pay, rather than on a lower level of pensionable pay as is the case in many countries.

11.4.9 In a discussion of the retirement income objective of public service schemes, particular regard must be had to the position of public servants in full PRSI class whose occupational benefits are subject to integration with the State Social Insurance pension. While integration aims to ensure that the total of occupational pension plus Social Insurance pension is equivalent to the pension received by a public servant in modified PRSI class, the level of occupational pension received can be low where net pensionable remuneration (i.e. pensionable remuneration less twice the rate of Old Age (Contributory) Pension) is relatively low. Many low-paid and part-time public servants come into this category. We discuss integration and low pay, and pensions for part-time public servants, separately below.

11.4.10 The Commission believes that the retirement income objective of public service pensions, i.e. retirement pension of 50% of final earnings and lump sum of 150% of final earnings after 40 years' service, is both reasonable and affordable. We consider that this pension target is on a par with best practice in private sector schemes and with public service schemes abroad.

11.4.11 In the case of public servants having less than maximum service (including those who leave service prior to retirement age), there are arrangements in place to ensure that adequate pension rights are earned in respect of the actual period of public service employment. In the next Chapter, we report on facilities enabling public servants to make contributions towards bridging the gap in their pensionable service; our recommendations in this regard are set out in Chapter 19.

11.5 Integration of occupational pension with State Social Insurance benefits

11.5.1 Public servants in full PRSI class are subject to the integration of benefits and contributions with the State Social Insurance system. Prior to the change of PRSI status for new entrants in April 1995, integration applied generally to non-established and industrial civil servants, non-officer grades in the education and local authority sectors, non-officer grades in Health Boards and voluntary hospitals and all grades in nominated health agencies and certain state-sponsored bodies, as well as civilian employees of the Permanent Defence Forces, a total of about 39,000

[145] Excluding Spain, where pension is 100% of uniform basic salary. Maximum pension is equivalent, on average, to 95.4% of final salary (see note (vii) to Table 9.2).

employees. A limited form of integration applied also to enlisted personnel in the Permanent Defence Forces (see Paragraphs 3.7.20-3.7.21).

11.5.2 The majority of pensionable public servants now in service (around 150,000 employees) are in modified PRSI class, have no entitlement to Social Insurance pensions, and so are not subject to integration. However, since April 1995, on foot of a government decision, *all* new entrants to the public service are in full PRSI class and are subject to integration. Obviously, the proportion of modified PRSI class public servants will fall over time as the number of post-April 1995 new entrants increases. The rationale for the Government's decision is set out at Appendix 11.2. In summary, the Government's view was that, notwithstanding the historical background to their treatment under the Social Insurance system, the continued differentiation between modified class public servants and the remainder of the public sector workforce and the generality of private sector employees was no longer sustainable.

11.5.3 Integration applies in both the private sector and the public service (where it is sometimes known as *coordination*). An integrated scheme is one that takes into account the Old Age (Contributory) Pension (OACP), or other similar contributory benefits, in designing the overall benefit promise being made by the pension scheme.[146] It looks upon the OACP as part of the total pension package promised to employees on retirement. It acknowledges the substantial PRSI contributions being made by employers and employees which in turn entitle members to substantial Social Insurance benefits. Integration is a means of taking into account the benefits payable under the Social Insurance system to calculate:

- the amount of occupational pension required, so that the combined pension from both sources is at the level being aimed for in designing the scheme; and
- the level of contributions payable by the employee towards the cost of his or her occupational pension.

11.5.4 The actual methods of integration used to achieve these aims can vary from scheme to scheme. The most common method is by *salary offset*. This means that the employer will regard the Social Insurance benefit as taking care of pension rights in relation to a particular part of salary. Since this part of the member's salary is being *pensioned* by the Social Insurance pension, it is deducted from the person's actual pay to arrive at a figure for *pensionable salary*. The occupational pension scheme provides the pension based on the *pensionable salary* figure. The two parts added together (i.e. the occupational pension and the Social Insurance pension) then give the intended pension rate, based on the full salary.

11.5.5 The most common benefit promise in private sector occupational pension schemes is a maximum pension of 40/60ths (two-thirds) of pensionable salary at normal pensionable age (with commutation to provide tax-free lump sum). If the overall target benefit, including Social Insurance pension, is to be a maximum of 40/60ths of salary, the Social Insurance *offset* figure will be 1.5 times the Social Insurance pension. The operation of integration in a private sector 60ths scheme is shown in the example in Table 11.2. It is assumed that final earnings are £20,000 and pensionable service is 40 years.

11.5.6 In the example, the pension scheme recognises that the Social Insurance system is providing a pension of £5,009 per annum (i.e. equal to 40/60ths of the first £7,514 of annual

[146] The Pensions Board, *A Brief Guide to Integration* (January 2000).

salary). The employer's pension scheme, therefore, needs to provide the benefit based on salary in excess of that amount.

Table 11.2: Example of integration in private sector scheme for an individual with a salary of £20,000 p.a. and 40 years' service

Calculation of occupational pension			
Annual OACP	£96 p.w. x 52.18	=	£5,009 p.a.
Social Welfare offset ($1\frac{1}{2}$ times OACP)	£5,009 p.a. x 1.5	=	£7,514 p.a.
Pensionable salary	£20,000 – £7,514	=	£12,486 p.a.
Occupational pension	£12,486 p.a. x 40/60	=	£8,324 p.a.
Total pension benefit			
Annual OACP	£5,009 p.a.		
Occupational pension benefits	£8,324 p.a.		
Total pension benefits	£13,333 p.a. (66% of retiring salary)		

11.5.7 It is important to note that integration applies to contributions as well as benefits. In practice, the Social Welfare offset is deducted from remuneration before the pension contribution is calculated. This has the effect of making the contribution lower than it would otherwise have been, and reflects the fact that the individual makes a separate contribution (through PRSI) towards his or her Social Insurance pension.

11.5.8 In Section 8.12, we show that integration is applied in about two-thirds of private sector schemes. In general, the only point of difference in the practice of integration between public service and private sector defined benefit schemes is that the former apply a higher Social Insurance offset, reflecting the fact that, as discussed in Section 11.4, they have a 1/80th accrual rate for pension and 3/80ths for lump sum while private sector schemes have a pension benefit accrual rate of 1/60th, with commutation. Thus, the offset of one-and-a-half times OACP usually applied in the private sector scheme becomes twice OACP in the public service scheme; while the two offsets are technically different, they give essentially the same result.[147] The operation of integration in public service schemes is included in the description of pension terms in Chapter 3, and is summarised in Appendix 11.3.

11.5.9 Under public service arrangements, a temporary pension known as a supplementary or bridging pension may be payable for any period in which the pensioner is not employed and due to causes outside his or her own control fails to qualify for a Social Insurance benefit or qualifies for benefit but at a rate less than the maximum rate of OACP. A supplementary pension of this nature would not appear to be common practice in the private sector.

11.5.10 As noted in Paragraph 8.12.5, while defined contribution schemes in the private sector are not directly integrated with Social Insurance pensions, in practice, the rate of contribution paid will usually have regard to the fact that members will have an entitlement to Social Insurance pensions.

[147] The Pensions Board has shown that for annual earnings of £15,600 and a total of 40 years' service, a private sector (integrated) 60ths scheme will give a retirement pension of £6,084 p.a. which with commutation will give a lump sum of £23,400 and pension of £3,484 p.a. (assuming pension is reduced by 1/9th for lump sum), the same values as will be produced by a public service (integrated) 80ths scheme (*Securing Retirement Income*, p. 179).

11.5.11 Integration is an accepted practice internationally, although different forms of integration are used, for example, the use of different occupational pension accrual rates for different levels of earnings (see Paragraphs 9.7.12-9.7.14).

11.5.12 The Minister for Social, Community and Family Affairs has commented on integration as follows:

> *By using integration employers contribute towards an earnings related pension which might otherwise not be possible to provide for employees. This is a sensible arrangement, and one which I understand is the practice in other countries, since both employers and employees are also contributing to their Social Welfare pension through the PRSI system.*[148]

11.5.13 We examine the cost implications of integration within public service pension arrangements in Section 10.4. The figures indicate that the removal of integration would result in an increase in the new entrant rate for an established civil servant from 16.3% to 20.4% of pay and that, over time, it would bring about an increase of 16% in projected annual expenditure on public service pension schemes.

11.5.14 The Commission considers that occupational pensions should take account of entitlements to Social Insurance benefits. Integration ensures that the overall pension bears a reasonable relationship to retiring salary and that the cost of the occupational pension, which is additional to the cost of the Social Insurance pension, is affordable to both employees and employers. Integration is standard practice in the majority of private sector schemes since virtually all private sector employees are now covered for full PRSI, and also features in various forms in public service pension schemes in many other countries.

11.5.15 It is worth noting that the higher the pre-retirement salary, the less significant is the effect of deducting the Social Welfare offset.[149] This is relevant when considering the pension position of those who retire while in receipt of relatively low levels of pay and of part-time employees (see Sections 11.6-11.7).

11.5.16 Our impression is that the rationale and operation of integration is poorly understood and inadequately communicated in the public service. Thus, serving employees may only find out about the deduction of the Social Welfare offset from their pensionable remuneration at the time of retirement. We believe that the recently published Pensions Board booklet, *A Brief Guide to Integration* (January 2000), will help address this situation.

11.6 Integration and low levels of occupational pension

11.6.1 In certain circumstances, the effect of integration (with its flat rate deduction) can be to produce a very low or zero rate of occupational pension. In the public service, the relatively low levels of pay and career progression applicable to many groups who have traditionally been subject to integration (see Paragraph 11.5.1) contribute to this effect. Several groups have met the Commission and have forcefully communicated their members' dissatisfaction with this outcome.

11.6.2 The example in Table 11.3 shows the effect of integration for two public servants retiring on different levels of pensionable remuneration, £250 per week and £500 per week. Two different levels of service at retirement are assumed: 40 years and 25 years. The rate of OACP is taken as £96 per week (May 2000).

[148] Speech at the launch of The Pensions Board's Trustee Handbook, January 1998.
[149] Finucane, K., & Buggy, B., *Irish Pensions Law and Practice,* Oak Tree Press (1996), pp. 48-50.

Table 11.3: Calculation of occupational pension at different levels of pensionable remuneration and pensionable service

Level of service	Pension calculation	% of pensionable remuneration
	Pensionable remuneration — £250 per week	
40 years	£250 – (2×£96) = £58 × 40/80 = £29 per week	12%
25 years	£250 – (2×£96) = £58 × 25/80 = £18 per week	7%
	Pensionable remuneration — £500 per week	
40 years	£500 – (2×£96) = £308 × 40/80 = £154 per week	31%
25 years	£500 – (2×£96) = £308 × 25/80 = £96 per week	19%

11.6.3 Table 11.4 sets out the level of pension contributions paid by both public servants. The contribution rate is $3\frac{1}{2}$% of net remuneration (i.e. remuneration less twice the rate of OACP) towards pension, and $1\frac{1}{2}$% of remuneration towards lump sum. The table indicates that the level of contribution is related to the size of the prospective occupational pension payable. Accordingly, relative to remuneration, the higher paid public servant pays a significantly larger weekly pension contribution (disregarding the lump sum contribution) than the lower paid public servant.

Table 11.4: Occupational pension contribution (per week)

Remuneration	Pension contribution*	% of remuneration
£250 per week	£2.03 per week	0.8%
£500 per week	£10.78 per week	2.2%

* Excluding contribution in respect of lump sum and spouses' and children's benefits.

11.6.4 Table 11.5 shows total pension when Social Insurance pension is added to the occupational pension. For both employees, the combination of occupational pension and OACP equals 50% of pensionable remuneration after 40 years' service.

Table 11.5: Combined occupational pension and OACP at different levels of pensionable remuneration and pensionable service

Pensionable remuneration	£250 per week		£500 per week	
Length of service	40 years	25 years	40 years	25 years
Occupational pension	£29 per week	£18 per week	£154 per week	£96 per week
OACP	£96 per week	£96 per week	£96 per week	£96 per week
Occupational pension plus OACP	£125 per week	£114 per week	£250 per week	£192 per week
% of pensionable remuneration	50%	46%	50%	38%

11.6.5 As Table 11.5 indicates, of the maximum pension of 50% of pensionable remuneration, the proportion made up by the OACP is much higher for the lower paid compared with the higher paid individual. This reflects the flat rate nature of the Social Insurance pension entitlement.

11.6.6 Where service is 25 years, the lower paid public servant receives a total pension which expressed as a percentage of pensionable remuneration is *higher* than that received by the higher paid public servant, 46% as against 38%. In this situation, the Social Insurance pension[150] makes up the bulk of the former's total pension. The occupational pension received by the lower paid public servant, £18 per week, represents 7% of pensionable remuneration, while the occupational pension received by the higher paid public servant, £96 per week, represents 19% of pensionable remuneration.

11.6.7 Integration of benefits takes place at the time occupational pension comes into payment. Subsequent adjustments to pensions in payment are made only in respect of increases in salary. This is administratively convenient, but it can result in total pension (i.e. occupational pension plus OACP) as a percentage of the current salary of the grade rising or falling depending on how the rate of OACP changes in comparison with salary increases. For a person still in employment, significant increases in the rate of OACP relative to salary in the years leading up to retirement might result in the level of occupational pension being lower than would have been expected. It is possible for individuals retiring within a few years of each other on the same salaries and with the same level of service to have quite different overall pension levels. To counteract this, the rate of occupational pension could be adjusted in response to changes in the OACP to maintain an appropriate equilibrium throughout retirement. However, this would result in a decrease in occupational pension where the OACP was increasing at a faster rate than salary. This approach has never been adopted in the public service, nor in most private sector schemes, due to the generally accepted view that occupational pensions in payment should not be reduced as a consequence of increases in the OACP. The Social Welfare Act, 1999 has recognised this and has made such practice illegal.

11.6.8 In Appendix 11.4 we detail the actual rates of occupational pension being paid to three of the public service groups affected by integration prior to the April 1995 change: non-established civil servants, non-officers in the Local Government Superannuation Scheme (LGSS), and non-officers in the Voluntary Hospitals Superannuation Scheme (VHSS). Some of the findings, based on 1997 data, are summarised below:

Non-established civil servants

- a total of 4,399 main scheme pensioners (i.e. not including pensioners in receipt of spouses' and children's pensions) were each being paid an average occupational pension of £1,345 per annum (£25.78 per week), broken down into 3,713 male pensioners, with an average pension of £1,458 per annum, and 686 female pensioners, with an average pension of £726 per annum;
- of the male pensioners, 77% were in receipt of an annual pension of less than £2,000, 39% an annual pension of £1,000 (£19.16 per week) or less, and 14% an annual pension of £500 (£9.58 per week) or less. Of the female pensioners, 83% were in receipt of a pension of less than £1,000 per annum, and 50% an annual pension of £500 or less;
- on the basis of a sample of recent retirements, the average level of service at retirement was 21 years.

Non-officers covered by the Local Government Superannuation Scheme

- the average amount of main scheme pension in payment to 12,309 local authority, health service, etc. pensioners was £2,967 per annum (i.e. £56.86 per week);
- based on a sample of retirements, average service at retirement was 28 years;

[150] Excluding any additional amount which may be payable in respect of qualifying adult or child dependants.

- pension amounts under the LGSS are higher than for non-established civil servants because under the scheme, integration applies only to service after 1977, and service at retirement is higher.

Non-officers covered by the Voluntary Hospitals Superannuation Scheme

- data on the VHSS indicated that the average amount of annual pension was £1,133 (£21.71 per week), and that 64% of pensioners had 20 years' service or less at retirement.

11.6.9 The figures show that the average amount of occupational pension amongst these groups is low, and that quite a number of pensioners are in receipt of very low rates of weekly pension. However, the Social Welfare pension must also be taken into account.

11.6.10 It must be recognised, however, that a number of factors — not just the operation of integration — contribute to the lower rates of occupational pension experienced by these groups compared with most other public servants. These include lower average levels of service and generally lower levels of pay at retirement. Both of these factors are related to matters other than pensions, and while some attempt can be made to mitigate the effects of low pay, lower levels of service are more of a recruitment issue and thus outside the Commission's remit.

11.6.11 In *Securing Retirement Income*, the Pensions Board noted that the issue of integration had been raised in the submission process of the National Pensions Policy Initiative. The Board considered a number of possible options to minimise the negative impact of integration on pensioners, with particular reference to lower paid employees, including:

- setting a minimum level of pension by reference to members' contributions (120% of members' contributions, with interest at the rate normally applying to refunds of contributions on leaving service);
- providing a minimum level of pension accrual for defined benefit schemes;
- the use of a pro rata Social Welfare offset for lower-paid part-time employees, particularly if they do not qualify for full Social Welfare pension but also to improve their pension position generally (see Section 11.7).[151]

11.6.12 The Commission acknowledges that in the case of employees whose pay does not rise significantly with long service or seniority the smaller levels of occupational pension may appear to be unsatisfactory both in absolute terms and in relation to contributions made. Compared with such employees, those who have progressed significantly through the ranks receive a pension that is better relative to individual pension contributions made. However, as discussed in Chapter 14, this is an integral feature of final salary defined benefit schemes; it is suited to the requirements of public service employment in that it rewards and encourages upward career progression.

11.6.13 In addition, while perhaps not widely appreciated, the value for money for the individual of the Social Insurance system (i.e. the present value of expected pension benefits compared with the present value of expected employee contributions) is much higher for those on low pay than for those on high pay.[152]

[151] The Pensions Board, *Securing Retirement Income* (1998), p. 181.

[152] Department of Social, Community and Family Affairs, *Actuarial Review of Social Welfare Pensions*, Report by Irish Pensions Trust Ltd. (1997), p. 29.

11.6.14 It is not clear how the value for money of the combined pensions package (occupational plus Social Welfare pension) compares between the public servant who experiences favourable career progression and the public servant whose pay is low and remains static throughout his or her career.

11.6.15 In Chapter 17, we examine the question of whether or not an adjustment should be made to integration to address the pension position of those retiring on relatively low levels of pay and we make specific recommendations in this regard.

11.7 Integration in the case of part-time public servants

11.7.1 We discuss part-time employment and job-sharing arrangements in the public service in Chapter 7. There may be as many as 42,000 part-time public servants and perhaps around 8,000 job-sharers. As noted in Section 11.2, many part-time public servants are not covered by public service pension schemes. In recent years, there has been a strong move — coming from the EU and with support from public service unions — to extend pension schemes to part-time employees. In addition, public service employers are seeking greater flexibility in atypical employment arrangements.

11.7.2 At present, most part-time public servants are found in areas where full PRSI applied prior to the 1995 change. Thus, when considering the extension of pension terms to part-time employees, the question of integration and low levels of occupational pension arises.

11.7.3 A further issue is the comparative pensions treatment of job-sharers and part-time public servants. A different approach to the former has been adopted because:

- unlike part-time public servants, most job-sharers are in modified class PRSI; and
- it is an assumption of the job-sharing scheme that public servants availing of it will job-share for a period of time before returning to full-time employment.

11.7.4 However, with the extension of full PRSI to all new entrants to the public service and the proposed introduction of work-sharing (see Paragraph 7.3.11), the difference in pension calculation for job-sharers and part-time public servants becomes difficult to sustain. In addition, there is the question of equity of treatment between both groups. Equality as defined under EU law also arises — the competing arguments are summarised at Paragraph 11.7.17 and discussed in detail in Chapter 18.

11.7.5 There are two means of calculating pensions for public servants working other than on a full-time basis:

(i) to use actual remuneration at retirement and *notional service*, i.e. the period of time in which the individual has worked part-time (this is the basis currently applying to part-time public servants); or

(ii) to use *notional remuneration*, i.e. full-time remuneration for the position, and actual service based on the conversion of the individual's part-time service into its full-time equivalent (this is the basis currently applying to job-sharers in the public service).

We illustrate the effect of each below.

11.7.6 Where there is no Social Insurance pension and no integration, both approaches give the same outcome. For someone working 50% of normal hours, retiring after 40 years on weekly pay of £200, the calculation is:

(i) £200 × 40/80 = £100

(ii) £400 × 20/80 = £100

11.7.7 However, when integration is applied, the two formulas give different outcomes. Approach (i) is full integration, while approach (ii) is pro rata integration. The difference between the two systems may be seen in the following example for two employees — A and B — who are engaged in comparable work, A full-time, B part-time. The first treatment, illustrated in Table 11.6, is **full integration**.

11.7.8 Under full integration, with the addition of OACP, both A and B receive a total pension which is half of final earnings — meeting the retirement income objective of public service pension arrangements where there is maximum service of 40 years. The part-time employee, B, receives total pension benefits which relate to that of the full-time employee, A, engaged in comparable work, proportionate to the hours worked.

11.7.9 It will be seen that if B had worked full-time and was in receipt of £200 per week at retirement (i.e. the pay rate per hour worked was halved), his or her pension would be calculated in the same way and would give the same outcome — an occupational pension of £4 per week which when added to OACP of £96 would give a weekly pension of £100, half of final earnings. This is an argument made in favour of full integration for part-time employees — that it is consistent with the pensions treatment of full-time employees.

Table 11.6: Comparison of pension entitlements of full-time employee and part-time employee under full integration

	A — Full-time	B — Part-time
Weekly hours	39 hours p.w.	$19\frac{1}{2}$ hours p.w.
Years worked	40 years	40 years
Pensionable service	40 years	40 years
Pensionable remuneration	£400 p.w.	£200 p.w.
Net pensionable remuneration	£400 – (OACP (£96) × 2) = £400 – £192 = £208	£200 – (OACP (£96) × 2) = £200 – £192 = £8
Pension calculation	£208 × 40/80 = £104 p.w.	£8 × 40/80 = £4 p.w.
Lump sum[153]	£31,308	£15,654
OACP	£96 p.w.	£96 p.w.
Total pension (incl. OACP)	**£200 p.w.**	**£100 p.w.**

11.7.10 The aim of integration is to ensure that a certain percentage of pensionable remuneration is paid through the combination of Social Insurance and occupational pension. However, as shown in Section 11.6, where pay is low, as it is for employee B, the proportion of total pension represented by the Social Insurance pension is much higher.

[153] Pensionable remuneration × 52.18 weeks × 120/80.

11.7.11 Turning to **pro rata integration**, which is illustrated in Table 11.7, the calculation of benefits for B will change (A's position is unchanged). B's pensionable service is no longer 40 years, as above, but 40 years multiplied by hours worked as a percentage of full-time hours, i.e. $40 \times \frac{1}{2} = 20$ years. B's pensionable remuneration is actual remuneration uprated to the full-time equivalent, i.e. £400 per week.

11.7.12 With pro rata integration, the occupational pension for the part-time employee relates to that of the full-time employee proportionate to the hours worked. In the example, just as the part-time employee works one-half of the weekly complement of 39 hours, he or she receives one-half of the occupational pension.

Table 11.7: Comparison of pension entitlements of full-time employee and part-time employee under pro rata integration

	A — Full-time	B — Part-time
Pensionable service	40 years	20 years
Net pensionable remuneration	£400 – £192 = £208	£400 – £192 = £208
Pension calculation	£208 × 40/80 = £104 p.w.	£208 × 20/80 = £52 p.w.
Lump sum	£31,308	£15,654
OACP	£96 p.w.	£96 p.w.
Total pension (incl. OACP)	**£200 p.w.**	**£148 p.w.**

11.7.13 However, when OACP is included, the part-time employee receives a total pension under pro rata integration which is proportionately higher, as a percentage of final earnings, than that of the full-time employee. For B, total pension of £148 represents 74% of final earnings. Apart from the fact that the total pension is in excess of the 50% promised by public service pension arrangements for an individual having 40 years' service, it is also higher than the pension of a full-time employee having a lower hourly pay who retires on the same rate of weekly pay and with the same service. As shown above, this employee qualifies for a total pension of £100, 50% of final earnings.

11.7.14 Pro rata integration can also be achieved by adjusting the OACP offset in the proportion that total hours worked bear to full-time hours, with each year of pensionable service counting as one year's service. In the above example, net pensionable remuneration would be £200 — £96 = £104, and pensionable service would be 40 years. Both approaches to pro rata integration give the same result where hours worked have remained constant through service.

11.7.15 In conclusion, under existing public service integration arrangements *(full integration)*, the total pension — combining occupational pension plus Social Insurance benefit — for a part-time employee compares with the total pension of a full-time colleague engaged in comparable work and in receipt of the same (hourly) pay, pro rata to the hours worked, assuming both have worked for the same number of years.[154] In effect, this means that the rate of occupational pension (excluding Social Insurance benefit) is proportionately lower for the part-time employee compared with the full-time employee to compensate for the fact that the same flat rate amount of Social Insurance entitlement is payable to both.

[154] Note that the part-timer's total pension will be proportionally greater where pensionable remuneration is less than twice the rate of OACP.

11.7.16 Under an alternative approach *(pro rata integration)*, the comparison between the full-time and part-time employee is done not on total pension but on occupational pension only. This means that the rate of occupational pension for the part-time employee compares with that of the full-time employee pro rata to the hours worked. Under this approach, occupational pension is higher when compared with existing arrangements.

11.7.17 We discuss the basic arguments in relation to both forms of integration in Chapter 18. They are summarised below:

Full integration

(i) it results in the part-time employee receiving a combined Social Insurance and occupational pension which is consistent with the aim to provide retirement income of 50% of final earnings for a person with 40 years' service;

(ii) it is the system which applies to employees generally. To adopt a different approach would be to favour part-time employees over all others, particularly those on low pay.

Pro rata integration

(i) it appears to meet the equality requirement under Community law, as currently interpreted by the European Court of Justice, to provide the part-time employee with hour for hour the same pay (defined to include occupational pension) as a full-time employee engaged in comparable work;

(ii) as all new entrants are paying full PRSI, and in light of the drawing together of part-time working with the job-sharing scheme, it will be increasingly difficult to justify a situation where part-time employees, who are generally on lower levels of pay, will be entitled to a less favourable system of integration than that applying to job-sharers;

(iii) it is more capable of dealing with the position of public servants having more than one part-time job given that only one Social Insurance pension is payable.

11.7.18 In the private sector, of the small number of schemes that include part-time employees as members, the majority use the pro rata approach (see Paragraph 8.12.7). In the Netherlands, which operates a flat rate Social Insurance structure similar to that applying in Ireland, the public service scheme integrates its occupational pension using an arrangement similar to pro rata.

11.7.19 The Commission considers that part-time public servants should in principle be given access to occupational pension schemes. We have demonstrated the different outcomes and difficulties that arise under different models of integration with Social Insurance benefits. We recognise that many part-time public servants find existing arrangements to be inequitable. The Commission examines this issue further and makes definitive recommendations in Chapter 18 of the Report.

11.8 Pensions increase policy

11.8.1 In the public service, pensions are increased in line with the pay of serving public servants (a system known as *pay parity*). The operation of pay parity is described in detail at Appendix 3.2, while a note on the history of pension increases is contained in Appendix 16.1. As has been shown in Chapters 8 and 9, this system is more favourable to pensioners than that applying in the private sector, where schemes provide limited increases in line with price inflation (some schemes do not grant pension increases), and more favourable than the systems applying in a number of public service pension schemes in Europe.

11.8.2 Pay parity is costly. The effect of changing pensions increase policy from salary-related increases to increases in line with the Consumer Price Index is set out in Section 10.5. It is shown that over the long-term, such a change could bring about a saving of up to 17% in annual pensions expenditure, and would reduce the State's accrued pension liabilities by just over £2.6 billion.

11.8.3 The application of pensions increase policy became a matter of some dispute between the Government, the public service unions and public service pensioner representatives during 1996 and 1997 as a result of restructuring agreements made under the *Programme for Competitiveness and Work (PCW)*. Existing pensions increase policy caters for general and special pay increases, but it makes no specific provision for the more flexible restructuring type agreements.

11.8.4 Over the period 1994 to 1998, different public service groups reached agreements under clause 2(iii) of Annex 1 to the *PCW* pay agreement (see Paragraph 7.5.6). There was great variation in the nature of the agreements reached, some of which focused on pensions and retirement matters, others on the introduction of long service increments and restructuring of grades and/or pay scales, and others on increases to the basic pay scale.

11.8.5 The Department of Finance decided to await the outcome of all restructuring negotiations before deciding on the application of pensions increase policy to the public service as a whole. The Department argued that the *PCW* agreements did not fit comfortably with the traditional pensions increase policy.

11.8.6 The Department also pointed out that the various agreements differed widely in their structure and, as a result, if traditional parity applied, the impact on public service pensioner groups would vary significantly.

11.8.7 Pensioner associations and the Public Services Committee of the ICTU sought retention of pay parity but with some provision for groups who would not benefit as a consequence. The agreed position of the Public Services Committee of Congress was parity with a floor of 3%.

11.8.8 The arguments on behalf of the pensioners focused on the role played by retired public servants in developing the public services at a time of hardship and poor economic conditions, the commitments made by successive governments dating back to 1969, the view of pensions as compensation for lower levels of public service pay compared with the private sector, the productivity and flexibility given by former public servants, and the fact that public servants had contributed towards their pensions and the value of pay parity (this last point is considered in Section 11.9).[155]

11.8.9 The Government's joint programme, *An Action Programme for the Millennium* (1997), stated that key priorities would include *"protection of Public Service pensions"*.

11.8.10 On 4 November 1997, the Minister for Finance announced the Government decision that public servants who retired before the commencement of restructuring deals under the *PCW*

[155] Many of these arguments were developed in a two-day Dáil debate on a Labour Party motion to re-establish pay parity on 21-22 October 1997.

should benefit from those deals on a pay parity basis subject to a minimum adjustment of 3% in their pension (or 2% in the case of those pensioners who had already received an advance payment of 1%). The Minister stated that this was a one-off measure and that the policy in relation to any future restructuring deals would be determined in the light of the recommendations in the Final Report of the Commission on Public Service Pensions.

11.8.11 In the context of pay parity, the principal question in our view is whether it is appropriate to give the benefit to pensioners of restructuring agreements in which serving employees commit themselves to productivity improvements, savings and increased flexibility in the future.

11.8.12 The present policy of increasing pensions in line with changes in the pay scales of serving employees has created many *practical and administrative difficulties*, which were exacerbated as a result of the *PCW* restructuring agreements. These include:

- how to continue the pensions link with specified grades where posts are regraded over time, sections and work programmes are discontinued, and entire grades disappear;
- the greater number of pensioner pay scales to be maintained following the introduction under the *PCW* of higher and lower scales for certain grades (e.g. for the Executive Officer grade in the civil service, there will now be at least four scales applying to different pensioners from that grade);
- the number of occasions on which pensions have to be increased (exacerbated by delays in finalising local bargaining agreements, resulting in a wide range of pension increases having to be processed at the one time);
- confusion among pensioners leading to a higher level of correspondence and greater number of calls from individual pensioners;
- the need to examine pensioner files manually particularly after *PCW* restructuring deals. It is necessary to determine in each case exactly what pensions increase should apply;
- dealing with extending or shortening of pay scales.

11.8.13 In the civil service alone, 15,000 individual pensioner files — some of which related to retirements in the 1950s and 1960s, or even earlier — had to be examined manually by the Department of Finance. In most cases, it was necessary to consult with other departments in an inherently time-consuming process.

11.8.14 From the pensioners' perspective, a number of issues have arisen which have caused difficulties. These include:

- the non-application to pensioners of certain long service increments in the case of groups for whom these were a feature of the pay agreement;
- the requirement that to qualify for certain long service increments, a person had to have three years on the maximum point of the scale. This is a variation of the first issue. Many pensioners argued that this was an unfair condition to place upon those who had retired, as anybody with insufficient service could not hope to benefit;
- the effect on pensions in payment of decisions to make new allowances pensionable. In a number of cases in the past, it was decided to amend pension terms for certain groups by making certain allowances pensionable and to apply the revised terms in respect of personnel who retired or died *after* the effective date of the decision. Pensions in

payment prior to the effective date were not affected. Pensioners have sought consequential increases in pension on the basis that these allowances were applicable to all or many who served in the groups concerned and thus formed a central part of remuneration (see Appendix 11.5).

11.8.15 In considering these issues, the Commission has had regard to the need to protect the real incomes of pensioners, to preserve equity, and to ensure that the system is affordable, viable and secure over the long-term.

11.8.16 The Commission notes that under the *Programme for Prosperity and Fairness* there is no specific provision for restructuring agreements; instead it is stated that the third phase increase of 4% will be paid not earlier than 1 October 2002 and will be dependent on specific performance indicators having being established by 1 April 2001, and these sectoral targets having been achieved by 1 April 2002, with progress in this regard having being assessed at organisational level by 1 October 2002.[156]

11.8.17 The Commission's recommendations on pensions increase policy are set out in Chapter 16.

11.9 Contributions by public servants towards the cost of pension benefits

11.9.1 In assessing public service pension arrangements, it is necessary to take into account the contributions — whether implicit or explicit — being made by individual public servants towards the cost of their pension benefits, including the role of pensions within the salary determination process.

11.9.2 Most occupational pension schemes in the private sector are contributory (though, as noted in Section 8.9, about one-third of schemes are not). Of these, about 60% apply a member contribution rate of between 3% and 6% of pay.

11.9.3 As shown in Paragraph 9.7.21, the rate of contribution by public servants in 11 European countries varies between 4% and 10.75% of pay; the rate in most countries is in the range 7% to 10% of pay. Implicit or notional contributions apply or are deemed to apply in the other countries surveyed.

11.9.4 The majority of public service occupational pension schemes in Ireland (covering about three-quarters of all pensionable public servants) are contributory, although this fact does not appear to be widely recognised outside the public service. We have shown in Chapter 3 that a main scheme contribution of 5% of remuneration applies to a number of groups, including teachers, and local authority and health service personnel. The contribution rate for spouses' and children's benefits is $1\frac{1}{2}$% of remuneration. Thus, the combined contribution made by many public servants is $6\frac{1}{2}$% of remuneration.

11.9.5 All new entrants to the public service appointed on or after 6 April 1995 to areas where the lower modified rate of PRSI formerly applied and who now pay the full rate of PRSI, pay an explicit main scheme pension contribution of 5% ($3\frac{1}{2}$% of net remuneration[157] for pension and $1\frac{1}{2}$% of remuneration for lump sum). The operation of integration means that the effective

[156] See (c) in point 4 of Annex II, page 36 of the *Programme for Prosperity and Fairness.*
[157] Net remuneration is remuneration less twice the rate of OACP.

contribution rate is lower than for contributory public servants in modified PRSI class (see Paragraph 11.5.7).

11.9.6 The principal areas of the public service where explicit main pension scheme contributions do not apply (leaving aside the April 1995 changes for new entrants) are the civil service (both established and non-established) and the Permanent Defence Forces. A main scheme contribution rate which is lower than the 5% norm applies in the case of the Garda Síochána (1.75% of remuneration).

11.9.7 As outlined below, the absence of an explicit main pension scheme contribution was taken into account in the past under the traditional approach to pay determination by setting salary rates at a lower level than would otherwise have been the case and thus, in effect, imposing an implicit pension contribution. In addition, a number of arbitration board findings and reports by the Review Body on Higher Remuneration in the Public Sector applied a further deduction, or implicit contribution, in respect of the more favourable pension benefits applicable to public servants relative to their private sector comparators. However, it is not clear to what extent these implicit contributions are still reflected in the pay of civil servants.

11.9.8 The first deduction arose in certain negotiations on pay for established grades in the civil service when comparisons were done with analogous employments in the private sector and elsewhere in the public sector. For those private sector employments having contributory pension schemes a deduction was made in respect of the amount of employee pension contribution. This deduction, which averaged about 5%, was and is seen as an implicit contribution by civil servants towards the cost of their pension. A similar approach was adopted in various reports of the Review Body on Higher Remuneration.

11.9.9 As noted in Paragraph 11.9.5, an explicit 5% contribution rate, in line with that applying in other public service contributory pension schemes, was introduced in April 1995 for new entrants to areas where modified PRSI rates formerly applied. In consequence, salaries and relevant allowances which were subject to periodic pension deductions were uprated by 1/19th.

11.9.10 In addition to this *basic* deduction, certain reports of the Review Body on Higher Remuneration have made a further deduction when setting the salaries of public servants in respect of the more favourable pension arrangements which they hold in comparison with the private sector. Report No. 20 (the second General Review) of 1979 concluded that a deduction of $3\frac{1}{2}$% would be appropriate in the case of those public servants who had civil service type post-retirement pensions increase arrangements.[158] Report No. 30 (the third General Review) of 1987 made a wider comparison of all superannuation costs, and determined that a deduction of 1.5% would be appropriate to take account of the more favourable arrangements applying in the public sector.[159]

11.9.11 Similarly, a 1983 report of the Civil Service Arbitration Board (No. 474) in relation to the pay of executive grades made a deduction of 3% to reflect the more favourable post-retirement increase arrangements in the civil service compared with the private sector. The report noted:

> *Where similar comparability exercises had been carried out in the UK or by the Review Body on Higher Remuneration in the Public Sector, adjustments had been made to reflect the post retirement increase arrangements attaching to Civil Service pension rights when compared with arrangements in employments outside the Civil Service. It was considered that the practice should equally apply in this case and that the appropriate deduction would be 3%.*

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[158] Review Body on Higher Remuneration in the Public Sector, *Report No. 20 to the Minister for Finance* (1979), p. 14.
[159] Review Body on Higher Remuneration in the Public Sector, *Report No. 30 to the Minister for Finance* (1987), p. 72.

11.9.12 In 1988, Report No. 531 of the Arbitration Board continued this deduction for executive grades and stated as follows:

> *These deductions have been heavily criticised by the staff side and it has been urged in relation to the present claim that quasi index linked or other similar pension arrangements are now much more common in the private sector.*
>
> *It is considered that these deductions were fully justified in the light of subsequent events and that in so far as the comparative pension situation may have changed this factor was more than offset by the ever increasing asset value of security of tenure.*

11.9.13 As a result of these arbitration determinations, many other groups have in effect been subject to the same deduction by virtue of the fact that in the past their pay was determined wholly or partly by reference to the pay of civil service executive grades which have been used as *marker* grades for pay purposes.

11.9.14 In relation to civil service clerical grades, a 1988 Arbitration Board Report (No. 536) did not attach very much significance to the difference in pension rights between the public service and the private sector.

11.9.15 A pay claim in respect of the higher civil service grades of Principal and Assistant Principal Officer went to arbitration in 1986 and 1991, but there was no mention of any deduction on foot of comparative pension benefits with the private sector in the arbitrator's findings.

11.9.16 Some public service groups — Gardaí, Prison Officers, Psychiatric Nurses, fire brigade staff — enjoy more favourable pension terms than the generality of public servants (see Chapter 3). In relation to the Garda Síochána, while the *Conroy Commission* (1970) referred in Paragraph 291 to *"superannuation rights"*, there is no evidence that any specific account was taken of this factor in fixing the pay of Gardaí or of any of the other groups.

11.9.17 The most recent report of the Review Body on Higher Remuneration — Report No. 37 of December 1996 (the *Buckley Report*) — which had a significantly different approach to pay determination compared with previous general reviews, made no reference to any such deduction. Because the methodology adopted was based primarily on internal differentials and did not involve a survey of private sector pay rates, the question of a deduction in respect of pension arrangements may not have been relevant.

11.9.18 The most recent pay increase for civil service grades represented by the Public Service Executive Union — which was negotiated under the local bargaining provisions of the *PCW* rather than the traditional comparison with private sector rates — makes no reference to the inclusion of the deduction in respect of post-retirement benefits in the current salary structures. The same applies to the other public service groups whose pay had been linked to or influenced by the pay levels of executive grades in the civil service.

11.9.19 The views of the Department of Finance in relation to the question of whether or not there continues to be an implicit contribution towards a more favourable pension system in the public service compared to the private sector are set out in Appendix 11.6. The Department concludes that it is a matter of some speculation as to whether the former deductions in respect of post-retirement retirement benefits are still reflected in the current pay or salary structures. However, this view is not shared in the submission of the Public Service Executive Union.

11.9.20 This review of developments over the past 20 years highlights the difficulties involved in attempting to establish the extent to which pension terms are reflected in present pay levels in the public service or in drawing a general conclusion on this matter in relation to the public service as a whole. While it is possible to say that up until the *PCW* agreement a deduction for post-retirement benefits was included in the salary structures of executive and related grades, it cannot be said with the same certainty that the deduction continues to apply in what is now a significantly different pay determination environment. It should be noted, however, that the changes which have taken place in pay determination are not necessarily of a permanent nature. Moreover, it can be argued that no matter what pay determination system is applied there will always be a case for relating public service pay to the position of comparable groups in the private sector from time to time. However, this issue is likely to arise again in the context of the benchmarking exercise which is provided for in the *Programme for Prosperity and Fairness*.

11.9.21 The Commission considers that it is appropriate that new entrants to the public service make an explicit contribution towards the cost of their pension — we discuss this further in Chapter 22. While different contribution rates would be appropriate if a strict actuarial approach were being adopted — to take account of the more costly pension benefits applying in one area compared with another — we recognise the complexities, particularly the implications for pay rates, were such a proposal to be pursued.

11.9.22 The Commission's recommendations on pensions increase policy (see Chapter 16) have implications for pension contributions by public servants.

11.10 Dependants' benefits

11.10.1 The spouses' and children's pension schemes are a key component in public service pension arrangements. They provide an important social and financial benefit to the families of deceased members. The benefits of the schemes, taken in conjunction with the gratuity payable on death-in-service, are reasonable when compared with dependants' benefits of public service schemes in other countries and with schemes in the private sector.

11.10.2 A number of issues in relation to the spouses' and children's schemes were raised in the submission process. These include:

- the case of public servants who declined to join the schemes on previous occasions and are now seeking a further option to join; and
- the payment of pensions to non-marital partners.

11.10.3 The spouses' and children's schemes were introduced for male public servants in most parts of the public service between 1969 and 1971 (1977 in the case of the Permanent Defence Forces). Because the schemes were contributory, serving public servants were given the option to join; all new entrants were automatically made members of the schemes. Serving female staff became eligible for scheme membership in 1981 (or later in some instances). In 1984, an option to join revised schemes was made available in most areas of the public service. Because the teachers' unions did not agree the introduction of the revised scheme (except for vocational teachers who were included in the revision of the scheme under the LGSS), a second option has not been made available to national and secondary teachers.

11.10.4 Many public servants and their unions are seeking a new option to join the schemes. Many of those not in the schemes are women. For example, in the local authorities, while only

20% of male employees up to age 60 are outside the relevant scheme, 75% of female employees in the age bracket 34 to 44 (who would have been in service when the first option was offered) are outside the scheme. The majority of male teachers are in the schemes, whereas about 40% of female teachers aged 38 or over are not. The only significant area where male employees opted out of spouses' and children's scheme membership in large numbers is the Permanent Defence Forces: of roughly 13,000 Defence Force personnel provided with the option in 1977, 7,700 declined to avail of it; about 540 of these took up the opportunity of the second offer in 1985.

11.10.5 The case made by those now seeking to join the schemes is that they had experienced a change in personal circumstances since the date of the option and that they had misunderstood the nature of the option or had not fully appreciated its consequences. A number suggest that the new legislation on separation and divorce has affected the position. As regards the particular case of female public servants, some submissions argue that the position of women in society has changed fundamentally since the original options were exercised.

11.10.6 A second issue raised is the confining of eligible beneficiaries to the legal spouse and dependent children only. In Ireland's changing social structure, an increasing number of family units are not based on marriage. Many private sector pension schemes allow payment of dependant's pension to a cohabiting partner in certain circumstances. If the purpose and aim of the spouses' and children's schemes is to provide for the dependants of deceased public servants, it can be asked why pension benefits do not extend to cover non-marital partners.

11.10.7 Both of these issues are addressed in the Commission's recommendations in relation to dependants' benefits in Chapter 20 of the Report.

11.11 Conclusions

11.11.1 In this Chapter, we have examined in a preliminary way the adequacy and fairness of public service pension arrangements in relation to a range of issues identified by the Commission:

- access to schemes;
- retirement age and early retirement;
- accrual rates and retirement income objective;
- integration of occupational pension with State Social Insurance benefits;
- integration and low levels of occupational pension;
- integration in the case of part-time public servants;
- pensions increase policy;
- contributions by public servants towards the cost of pension benefits;
- dependants' benefits.

11.11.2 It is difficult to assess adequacy and fairness in relation to any single pension term and to decide against what yardstick they should be measured. While this difficulty cannot easily be resolved, this Chapter has discussed the arguments and competing views in relation to several important aspects of the pension schemes which have been the subject of submissions to the Commission and to which we have had to give detailed consideration. The analysis will be taken further in Part VI of the Report, in the context of the Report's recommendations.

APPENDIX 11.1

Comparison of pension benefits in public service (80ths) schemes with private sector (60ths) schemes

1. This Appendix presents a comparison between the retirement benefits provided by a private sector scheme with the benefits provided under standard public service terms. The level of retirement benefits in any scheme depends on various factors including the characteristics of the person retiring. The comparison presented below is based on an individual with the following characteristics:

- retirement age: 60
- salary at retirement: £20,000 per annum
- service at retirement: 40 years

2. For the purpose of the comparison, it is assumed that the private sector scheme allows retirement on full pension at age 60 with benefits based on salary at retirement. It is also assumed that benefits are not integrated with the Social Insurance system.

3. Public service benefits on normal retirement provide a pension of 1/80th of pensionable remuneration and a lump sum of 3/80ths of pensionable remuneration for each year of service. Benefits under private sector schemes vary greatly and it is necessary to make a number of assumptions about the terms of the private sector scheme used in the comparison. The approach adopted is to base the comparison on the benefits provided by a "good quality" private sector scheme. Differences between public service and private sector retirement benefits arise, in the main, from differences in accrual rate, in the rate of pensions increases, and in the basis used to commute pension to lump sum. The relevant terms of the private sector scheme used in this comparison are outlined below:

(i) **accrual rate**: it is assumed that retirement benefits are based on an accrual rate of 1/60th of pay for each year of service — most schemes in the private sector use this accrual rate;

(ii) **pension increases**: the best terms available in private sector schemes provide for increases in line with the Consumer Price Index (CPI) up to a certain maximum of, say, 4% or 5% per annum. If the rate of increase in the CPI is above the maximum specified, then pension increases may be below CPI. The comparison presented below is based on an assumed increase of 3% per annum in the CPI and therefore the maximum figure is not relevant to the comparison;

(iii) **commutation factors**: many private sector schemes provide retirement benefits in the form of a pension only; a person with 40 years' service will then be entitled to a pension of 2/3rds pay. However, members are generally allowed to commute pension up to a certain amount; this is a process whereby a certain amount of pension is given up in return for a lump sum payment; the residual pension then depends on the factor used to convert pension to lump sum. Many schemes use a commutation factor for male employees of 9, i.e. £1 of pension is commuted for a lump sum of £9 (for female employees the equivalent commutation factor is generally 9.8). However, some schemes offer better terms and commutation factors may vary with age at retirement, and with the level of increases expected on pensions in payment. Revenue rules apply in relation to both the maximum amount of retirement lump sum and to the maximum reduction in pension in return for a given lump sum. Maximum commutation factors allowed by Revenue are not explicitly stated and Revenue will accept factors calculated by an actuary subject to various conditions. Revenue would allow factors as high as around 15 at age 60 for males (17 for females) and 13 at age 65 for males; however, the best factors actually available for a small number of schemes appears to be around 13 for a male at age 60.

4. It can be reasonably assumed that a person will take the maximum lump sum benefit at retirement, in particular, in a scheme which allows commutation on the basis of a factor of 13:1. In the example used here, the maximum lump sum amounts to 1.5 times pay or £30,000. The pension given up is then £30,000 divided by 13 or £2,308, leaving an initial net pension of £11,025 (£13,333 – £2,308). Public service benefits accrue separately and amount to an initial pension of £10,000 and lump sum of £30,000. In effect both schemes provide the same lump sum benefit and the comparison is then between a public service scheme providing an initial pension of £10,000 per annum which is increased in line with public service pay and a private sector scheme providing an initial pension of £11,025 per annum which is increased in line with CPI.

5. Public service pay increases (and pension increases) have in the past been around 1% to 2% in excess of increases in the CPI; the public service pension can be expected to increase at a faster rate than the private sector pension and to exceed the private sector pension at some stage if the pensioner survives for a sufficient period. Clearly, any pensioner who lives for only a short period will receive greater pension payments under the private sector scheme. To carry out a more detailed comparison the following assumptions are made:

- in line with the assumption used in Chapter 6 of the Report, it is assumed that public service pensions increase at 1.5% in excess of prices;
- it is assumed that prices increase at 3% per annum;
- a male retiring now at age 60 is likely to live, on average, for around 20 years.

6. In comparing the two systems, the only factor that is relevant is the value of the annual pension. Table 1 below compares the projected level of pension payments over a twenty year period for both the public and private sector schemes. The Table shows that the annual pension from the private sector scheme pension is higher for the first six years. Cumulative payments are higher from the private sector scheme for 12 years. Over the life time of an average male pensioner, total payments from the public sector scheme are 6% greater.

7. There are other factors which would need to be taken into account in any full comparison of public service terms and terms provided by the small number of private sector schemes which adopt more favourable commutation rates than 1:9. A number of points are mentioned below:

(i) **female pensioners**: as noted above in Paragraph 3(iii) better commutation terms are generally available to female employees. As a result, annual payments from the private sector scheme in the case of a female would be greater for nine years, and cumulative payments for 16 years. The comparative position for the average female would be similar to that for the average male when allowance is made for the greater life expectancy of a female;

(ii) **public service pension terms are guaranteed**: this relates to both the general Exchequer guarantee and also to the absence of an upper limit to pension increases.

If price inflation in any one year is in excess of a certain percentage, the benefits in the private sector scheme may not be increased in line with CPI;

(iii) **spouses' benefits**: the public service scheme provides a spouse's pension of half the member's. Private sector practice varies, with the *better* schemes providing a benefit of over one-half of the member's pension. The value of a public service spouse's benefit at retirement is about the same value as the private sector provision when allowance is made for the higher increases on public service pensions in payment;

(iv) **retirement at age 65**: for pensioners who retire at age 65 (rather than age 60), annual payments from the private scheme would be greater for the first five years and cumulative payments for eight years;

(v) **private sector**: most private sector schemes guarantee pensions for a period after retirement — usually for five years — with the balance of the pension payable in the form of a lump sum if the pensioner dies within the guaranteed period. This guarantee improves the relative position of the private sector scheme in the case of a pensioner who dies within the relevant period;

(vi) **flexibility of choice of pension or lump sum at retirement**: this flexibility in private sector schemes is of limited value given the tax-free status of retirement lump sums;

(vii) **time value of pension payments**: if account is taken of the timing of the respective pension payments this improves slightly the relative position of the private sector payments.

Table 1: Comparison of pension payments from a public service and a private sector scheme (with commutation on a 1:13 basis)

Age	Annual pension amounts			Cumulative pension payments		
	Private Sector	Public service	Difference	Private sector	Public service	Difference
60	£11,026	£10,000	(£1,026)	£11,026	£10,000	(£1,026)
61	£11,356	£10,450	(£906)	£22,382	£20,450	(£1,932)
62	£11,697	£10,920	(£777)	£34,079	£31,370	(£2,709)
63	£12,048	£11,412	(£636)	£46,127	£42,782	(£3,345)
64	£12,409	£11,925	(£484)	£58,536	£54,707	(£3,829)
65	£12,782	£12,462	(£320)	£71,318	£67,169	(£4,149)
66	£13,165	£13,023	(£142)	£84,483	£80,192	(£4,291)
67	£13,560	£13,609	£49	£98,043	£93,801	(£4,242)
68	£13,967	£14,221	£254	£112,010	£108,022	(£3,988)
69	£14,386	£14,861	£475	£126,396	£122,883	(£3,513)
70	£14,818	£15,530	£712	£141,214	£138,413	(£2,801)
71	£15,262	£16,229	£967	£156,476	£154,642	(£1,834)
72	£15,720	£16,959	£1,239	£172,196	£171,601	(£595)
73	£16,192	£17,722	£1,530	£188,388	£189,323	£935
74	£16,677	£18,519	£1,842	£205,065	£207,842	£2,777
75	£17,178	£19,353	£2,175	£222,243	£227,195	£4,952
76	£17,693	£20,224	£2,531	£239,936	£247,419	£7,483
77	£18,224	£21,134	£2,910	£258,160	£268,553	£10,393
78	£18,770	£22,085	£3,315	£276,930	£290,638	£13,708
79	£19,334	£23,079	£3,745	£296,264	£313,717	£17,453
Total	**£296,264**	**£313,717**	**£17,453**			

APPENDIX 11.2

Government arguments for extending full PRSI to public servants[160]

1. The Government accepted that, historically, there were sound reasons for the exclusion of certain public sector employees from full Social Insurance coverage; however, the Social Insurance code had changed radically since its inception in 1911 and the Government shared the view of the Commission on Social Welfare (1986 Report) that the system of Social Insurance was an expression of social solidarity and citizenship and that the variable treatment of public bodies for Social Insurance purposes was difficult to justify.[161]

2. Initially the Social Insurance code covered two risks only and applied to those with low earnings and having no occupational benefits; now, full Social Insurance covered a greatly expanded range of contingencies and applied to virtually all employees; the Social Insurance regime could now be characterised as a system under which all participants, regardless of their individual circumstances, contributed towards and were eligible for, a range of benefits affording to all a basic level of income protection; the next logical step was extension to modified public servants, thereby providing comprehensive Social Insurance cover for all employees while spreading the cost of such cover as widely as possible by extending the contribution base.

3. Over the years employers had improved the range of benefits provided to employees through the introduction of occupational sick pay and pension schemes for many groups, including public sector groups not previously covered by such schemes; this applied to non-established civil servants and other Class A public sector employees; thus, the original gap between public servants with occupational benefits which protected them against the contingencies offered by Social Insurance and those without any such occupational protection had greatly diminished.

4. The existing Social Insurance cover for public servants had many inconsistencies and anomalies, e.g. commercial state bodies such as ESB and RTÉ employees had modified cover while Aer Lingus and Bord na Mona employees had full cover; officers in the local authorities were in Class D, while employees were in Class A — this type of differentiation perpetuated outdated and class-based distinctions between ''white-collar'' and ''blue-collar'' workers.

5. It was clear that the existing special status for modified public servants was widely perceived as constituting preferential treatment for the employees concerned and no less clear that this perception could not be dispelled so long as these employees remained outside full Social Insurance cover.

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[160] Taken from ''Report of Joint Government/Congress Working Party on the application of full Social Insurance to public servants who, at present, have modified status'' (December 1993).

[161] In the Final Report of the National Pensions Board, a majority of the Board recommended extending Social Insurance cover for invalidity, retirement and old age contributory pensions to new entrants to public sector employments currently insured at the modified rate. In time, they stated this would result in all employees in both the private and the public sector having the same range of pension cover under Social Insurance and contributing on the same basis to the costs involved. They added, however, that no change should occur in the current arrangements for existing public sector employees insured at the modified rate (Final Report of the National Pensions Board, 1993, p. 106).

APPENDIX 11.3

Integration with Social Insurance benefits under public service occupational pension schemes

1. In general, integrated pension terms in the public service are as set out below (based on the arrangements introduced for new entrants in April 1995, with a number of minor adjustments). An example of the calculation of benefits and contributions follows.

Occupational pension

2. Occupational pension is calculated on the basis of net pensionable remuneration, i.e. pensionable remuneration reduced by a Social Welfare offset of twice the rate of OACP payable on the last day of pensionable service to a single person with no adult dependants or qualified children. The offset is based on the period required for maximum occupational pension — 40 years for a pension of 40/80ths of pensionable remuneration. In excluding the portion of pensionable remuneration deemed to be replaced by the OACP, the reciprocal of this fraction is used — 80/40ths or twice the rate of OACP.

3. Total pension consists of occupational pension plus whatever pension or other long-term benefit is payable under the Social Insurance system. Retirement pension under the Social Insurance system is payable from age 65 (where the person has retired) while OACP is payable after age 66 (with or without retirement). Where a person has retired before age 65 under the rules of the scheme, voluntary early retirement, or on ill health grounds, he or she may qualify for unemployment benefit, invalidity pension, or disability benefit under the Social Insurance system.

Supplementary (or bridging) pension

4. The supplementary pension is an addition to the occupational pension and is payable for any period in which the pensioner is not employed and fails to qualify for invalidity pension, unemployment benefit, disability benefit, retirement pension, or OACP due to causes outside his or her own control, or where a Social Insurance benefit/pension is being paid but is less than the maximum rate of OACP due to causes outside his or her own control.

5. The amount of supplementary pension is the difference between:

- the pension which would have been payable had it been calculated by reference to pensionable remuneration rather than to net pensionable remuneration (i.e. without the OACP offset); and
- the actual pension payable under the scheme, together with the personal rate of Social Insurance payment being made (if any).

6. With the extension of full PRSI to all post-April 1995 new entrants, the question of paying supplementary pensions will arise for greater numbers of public servants retiring in age brackets 60-65, and even younger in the case of groups which have special early retirement terms. To qualify for supplementary pension, a public servant should not be in insurable employment and should have made every effort to qualify for the relevant Social Insurance benefit.

Spouses' and children's pensions

7. These have normally been calculated by reference to the actual rate of pension being paid (or which would have been paid) to the member. However, under the April 1995 rules, the OACP offset is reduced from twice to once, giving a higher rate of member's pension for the purposes of the calculation. In return for this improvement, the member contribution towards spouses' and children's benefits is higher: $1\frac{1}{2}$% of remuneration rather than of net remuneration.

Retirement lump sum

8. As no lump sum is paid under the Social Insurance system, no integration adjustment is made to the calculation of retirement lump sum under public service pension schemes.

Contributions

9. The main scheme employee contribution rate of 5% is divided between $3\frac{1}{2}$% for pension and $1\frac{1}{2}$% for lump sum. The lump sum element of the contribution is unaffected by integration. The former is reduced to take account of the contribution the employee is making towards the Social Insurance system through the PRSI rate. This is done by calculating the $3\frac{1}{2}$% contribution on remuneration less the offset of twice the rate of OACP.

10. The contribution for spouses' and children's benefits is, as indicated above, $1\frac{1}{2}$% of remuneration rather than of net remuneration (i.e. no OACP offset is applied).

11. An example is given below of the system of pension benefits which apply in the case of an Executive Officer in the civil service paying full PRSI and entitled to a Social Insurance pension. It is assumed that no pensionable allowances are payable at retirement.

Salary[162]	£25,012 per annum
Service	40 years
OACP (May 2000)	£96 per week
OACP offset (OACP × 2 × 52.18 weeks)	£10,019
Net pensionable remuneration (salary – OACP offset)	£14,993
Pension (net pensionable remuneration × 40/80)	£7,497 per annum
Lump Sum (salary × 120/80)	£37,518

Total pension consists of the occupational pension of £7,497 per annum plus the Social Insurance pension of £5,009 per annum, a total amount of £12,506 per annum. This is exactly half of salary, the amount which would have been paid by the occupational pension scheme alone if the individual had been in modified PRSI class while employed in the civil service and not entitled to a Social Insurance pension.

The individual's occupational scheme **contribution** during service, using the retiring salary figure of £25,012, is $3\frac{1}{2}$% of net remuneration and 3% of remuneration, an annual figure of £1,275 (£24.43 per week).

In the event of the death of the member after retirement, a **spouse's pension** is payable as follows:

Adjustment to net pensionable remuneration:	
Salary – (1 × OACP)	£20,003
Spouse's pension:	
Net pensionable remuneration × 20/80	£5,001 per annum

The spouse will likely qualify for contributory widow's/widower's pension under the Social Insurance system.

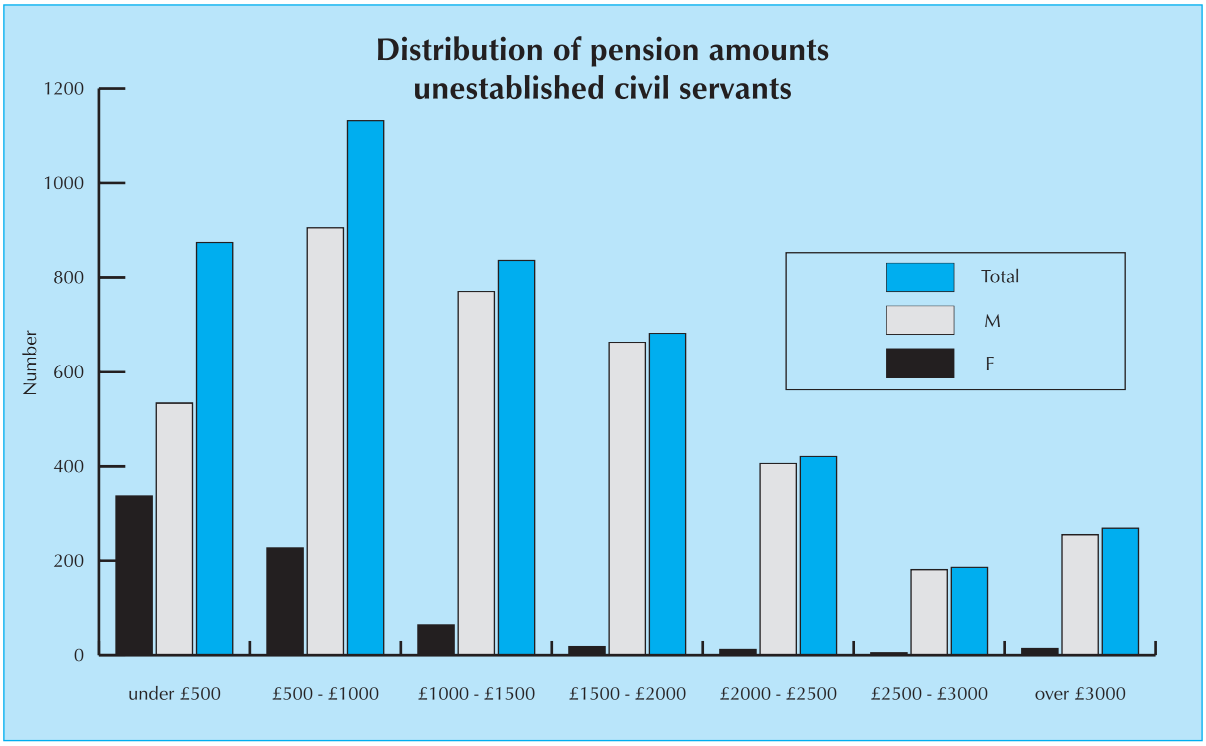
[162] The salary used for the purpose of the above example is the maximum point on the higher scale for Executive Officers recruited after 6 April 1995 as of 1 April 2000.

APPENDIX 11.4

Full PRSI groups: Rates of pensions in payment in 1997

Non-established civil servants

1. The distribution of pension amounts by sex, as at 1997, is shown in the table below.



2. Further analysis of pension records provides the following information:

- a total of 4,399 main scheme pensioners (i.e. not including pensioners in receipt of spouses' and children's pensions) were each being paid an average occupational pension of £1,345 per annum (£25.78 per week), broken down into 3,713 male pensioners, with an average pension of £1,458 per annum, and 686 female pensioners, with an average pension of £726 per annum;
- of the male pensioners, 77% were in receipt of an annual pension of less than £2,000, 39% an annual pension of £1,000 (£19.16 per week) or less, and 14% an annual pension of £500 (£9.58 per week) or less. Of the female pensioners, 83% were in receipt of a pension of less than £1,000 per annum and 50% an annual pension of £500 or less;
- it should be noted that the level of ill health early retirements (in which added years of service are granted) is high among non-established civil servants. Of average retirements of 165 over the period 1992-96, 55 or exactly one-third retired early on ill health grounds;
- there were a total of 1,993 persons in receipt of a spouse's pension, the average amount of which was £737 per annum (£14.12 per week). Of these, 1,500 were in receipt of £1,000 per annum or lower, and 784 were in receipt of £500 per annum or lower;
- pensioners in this category also qualify for Social Insurance payments — the rate of OACP was £78 per week (1997 rate) which when added to the average occupational pension of £25.78 per week gave a total weekly pension payment of £103.78;

- on the basis of a sample of recent retirements, the average level of final service on retirement was 21 years, with an overall breakdown as follows:

Service band	Percentage
less than 10 years	14%
10-20 years	40%
20-30 years	22%
30-40 years	15%
40 years and over	9%

Non-officers covered by the LGSS (which includes local authorities, health service, VECs, etc.)

3. The main findings on the available data for the LGSS in respect of employees *(non-officers)* is based on 1997 data:

- the average amount of main scheme pension in payment to 12,309 pensioners was £2,967 per annum (i.e. £56.86 per week);
- the average amount of spouses' and children's pension was £1,740 per annum (4,374 pensioners);
- with the addition of the OACP, the average weekly pension payment to a main scheme pensioner was £56.86 plus £78 (1997 rate of OACP) or £134.86 per week;
- on the basis of a sample of retirements, average service at retirement was 28 years;
- pension amounts under the LGSS are higher than for non-established civil servants because under the scheme, integration applies only to service after 1977, and service at retirement is higher.

Health Service

4. Apart from the LGSS, which covers the Health Boards, details are also available on non-officer pensioners being paid under the VHSS:

- average pensionable pay was £12,805 per annum;
- distribution of service at retirement was as follows:

Service band	Percentage
less than 10 years	16%
10-20 years	48%
20-30 years	23%
30-40 years	12%
40 years and over	1%

- the average amount of annual pension was £1,133 (£21.71 per week, £99.71, if OACP of £78 per week is included), broken down as follows:

Pension band	Percentage
0-£500	15%
£500-£1,000	41%
£1,000-£1,500	22%
£1,500-£2,000	11%
£2,000-£3,000	8%
Over £3,000	3%

5. The experience of the VHSS is closer to that of the scheme for non-established civil servants than the LGSS — the scheme was introduced for non-officers in 1985 and has always been subject to integration.

APPENDIX 11.5

Allowances which were made pensionable — implications for those already in receipt of pension

Garda Síochána

1. A number of allowances, principally rent allowance which is paid to all members of the Force up to the rank of Superintendent, were made pensionable as a result of arbitration in 1983. A cut-off date of 1 October 1982 was applied — only those who went on pension after that date benefited from the change.

2. In 1994, unsocial hours payments were made pensionable under the Garda restructuring agreement. Those who went on pension prior to 1 January 1993 received no benefit in their pension (it should be noted that the *floor* of 3% from the Government decision of 4 November 1997 — see Paragraph 11.8.10 of the Report — would have given those pensioners some increase arising from the restructuring agreement).

3. It was argued in submissions that the original introduction of unsocial hours payments during the 1970s and the substantial increase in rent allowance in the late 1970s had exacerbated the question of the pensionability of allowances. In 1998, the rate of rent allowance (married rate) was £1,855 per annum, while unsocial hours payments could amount to £5,000 per annum for those currently going on pension. Thus, compared with the pension of a Garda retiring in 1998, the pension of a Garda who had retired prior to January 1993 could be £2,500 per annum lower, while the pension of a Garda who had retired prior to October 1982 could be £3,400 per annum lower.

Permanent Defence Forces

4. Military Service Allowance (MSA) was made pensionable following the *Gleeson Commission* report on the Permanent Defence Forces.[163] A cut-off date of August 1990 was applied by the Department of Defence. MSA applies to all military personnel in the Permanent Defence Forces; it was introduced first for enlisted personnel and junior officers on 1 May 1979, and was extended to senior officers on 1 August 1990. In 1998, it stood at a flat rate of £2,000 per annum for members of all ranks.

5. Pensioner representatives pointed to the finding by the *Gleeson Commission* that MSA was an integral part of military pay, and argued that pensions of pre-August 1990 pensioners should be revised to take account of pensionability of the allowance.

Prison Officers

6. Rent allowance has been a feature of Prison Officer pay and conditions since 1834. It was consolidated into pay in 1961; however, it became an allowance again in 1972. Under the *PCW* agreement for Prison Officers, rent allowance was made pensionable for those serving on or after 1 January 1994. It was also made reckonable for the purpose of calculating lump sum or death gratuity in the case of members who retired or died in service in the period 1 January 1993 to 31 December 1993. In such cases, pension was adjusted to take account of rent allowance with effect from 1 January 1994. Therefore, Prison Officers retiring before 1 January 1993 — even

[163] Government of Ireland, *Report of the Commission on Remuneration and Conditions of Service in the Defence Forces* (July 1990).

though they may have been in receipt of rent allowance at retirement — are not entitled to receive any pension credit for having held this allowance.

7. For most Prison Officers in modified PRSI class going on pension after the effective date for the pensionability of rent allowance (June 1997), a further £1,750 approximately was added to pensionable remuneration. This resulted in an additional £875 a year in pension for those with maximum service at retirement.

Teachers

8. Under the *PCW* agreement for teachers, a number of new allowances were introduced:

(i) an allowance of £1,000 for teachers with 35 years' or more incremental service during the period of the pilot early retirement scheme;

(ii) allowances in respect of a series of qualifications which had not previously been recognised.

It was agreed that the above allowances would be reckonable towards pension entitlements if a teacher held one or either of them at retirement.

9. This arrangement differs from the others in that no teacher had previously held these allowances before they were made pensionable for serving staff. (In all three groups above, the allowances in question had been introduced several years before they were made pensionable.) However, it has been argued that as the new allowances for teachers were, in effect, a form of pay increase, and that a significant number of pensioners would have qualified for the new categories of allowance if they had been in employment, there are strong grounds for passing on the benefits to pensioners as would happen if it were a standard pay increase.

10. The **normal public service policy** is that allowances in the nature of pay held at retirement are pensionable subject to the normal rules on three-year averaging. For Gardaí, it was argued that rent allowance and rostered unsocial hours allowances were essential elements in remuneration of the Force, and similar arguments were made in relation to MSA by Defence Force personnel. Now that these allowances are pensionable, the argument advanced by pensioner groups is that in refusing to pass on the benefit to pensioners, the Government is effectively breaking pay parity. The introduction of new allowances or large increases in existing allowances, perhaps in lieu of increasing pay rates, became a greater feature of remuneration in certain areas of the public service during the 1970s. It was argued that it took some time before focus was placed on the question of pensionability, and because of the delay, those who went on pension in the meantime lost out.

11. The Commission's examination of this issue is set out at Section 22.6.

APPENDIX 11.6

Department of Finance view on the implicit member contribution towards the cost of pension benefits and role in pay determination process

1. In its letter of 25 November 1997, the Department of Finance confirmed to the Commission the approach in the past where pay of public servants with non-contributory pension benefits was being determined by reference to the pay of comparable groups in the private or public sectors which had contributory schemes. The general deduction made as a result was 5%.

2. Noting that some Reports of the Review Body on Higher Remuneration in the Public Sector and of the Civil Service Arbitration Board had made an additional deduction in respect of the more favourable pension arrangements of public servants compared with the private sector (particularly, in relation to earnings-related pension increases), the Department also pointed to a number of arbitration reports where little reference had been made to comparative pension benefits with the private sector. It noted that the most recent Review Body report, the *Buckley Report* (December 1996), had adopted an approach to pay determination which was so significantly different to previous practice that the issue of a deduction in respect of pension arrangements became irrelevant.

3. The Department commented that the most recent pay agreement for civil service grades represented by the Public Service Executive Union (under the local bargaining provisions of the *PCW*, rather than the traditional comparison with private sector rates) meant that it was a matter of some speculation as to whether the former deduction in respect of post-retirement benefits was still reflected in the current pay or salary structures. This point, it was argued, could even more forcibly be made in respect of the numerous other pay groups, e.g. nurses and teachers whose pay in the pre-*PCW* period was related to, or influenced in some way by, developments for PSEU grades and who under the *PCW* secured entirely different settlements fitted to their particular circumstances.

4. The Department added that pay determination within the public service could not be regarded as a single homogenous system nor could it be assumed that pay could be determined in some clear-cut mechanistic manner which incorporated different adjustments and refinements and then produced a single correct rate of salary for a given grade. Salary rates were determined in a wide variety of ways and there had been a significant change in recent years in what might be termed the traditional approach to pay determination. In the final analysis, the Department suggested, it came down to such matters as compromise, an evaluation by a third party of a variety of arguments and counter arguments and the likelihood of acceptability by the parties.

CHAPTER 12

The Changing Public Service and Flexibility in Pension Terms

12.1 Introduction

12.1.1 We discuss in Chapter 7 the process of change and modernisation which the public service is undergoing in relation to operational requirements, and the working environment and conditions of employment of public servants. These have important implications for public service pension arrangements.

12.1.2 Side by side with the changing public service, there has been an increasing demand for greater flexibility in pensions, particularly in relation to retirement age, treatment of part-time work, and the scope for individual public servants to contribute towards their own pensions package. This development is clear from the submissions received by the Commission and reviewed in Chapter 2.

12.1.3 In many respects, change in the public service and the demand for greater pension flexibility represent the two sides of the same coin. For example, a natural consequence of the trend towards a later age of entry is an increase in the numbers of public servants with short service who may wish to improve their pension benefits. Similarly, employers recruiting atypical employees, as well as the employees themselves, require pension terms that are appropriate to this form of employment.

12.1.4 In the first half of this Chapter, we examine how adequately existing pension terms are addressing the main points of change in the public service. We consider the following points identified in Chapter 7:

- increasing age of entry, trend towards shorter service, and more mobile work force;
- growth of atypical employment;
- ensuring pensionability of atypical employment;
- more frequent breaks in service;
- employee interest in retiring earlier than the norm;
- emphasis on delivery of service and management of performance;
- changes in pay determination.

In the second half of the Chapter, we examine the degree of flexibility in pension terms currently available, particularly, the schemes for the purchase of notional service and additional voluntary contribution (AVC) arrangements. Here we reach certain conclusions on the requirements to be met by pension flexibility provisions — these are taken up later in Chapter 19.

12.2 Increasing age of entry, trend towards shorter service, and more mobile work force

12.2.1 The fact that the average age of entry to the public service has been increasing affects an assumption of public service pension arrangements: that in normal circumstances the individual should be capable of earning a *full pension* (based on 40 years' service) by virtue of his or her public service. In this regard, the public service is drawing closer to the situation in the private sector. As a consequence of later ages of entry and because of wider pensions coverage in the private sector, increasing numbers of public servants will find that they have pension rights derived from earlier employments. Thus, it will not be uncommon for public servants at retirement age to qualify for one or more *preserved* or *deferred* pensions[164] from previous employers (including pensionable employments abroad).

12.2.2 Arising from increased mobility and widespread pensions coverage, there is a demand for facilities enabling the transfer of service into public service schemes from the private sector and from the public service abroad. This is partly due to the preference amongst many employees to carry a single pension entitlement between employments, with the final pension scheme being charged with payment of full career benefits. However, there may be cost considerations involved, particularly in the case of defined benefit pension schemes. Preservation (under which pension earned is *frozen* in each employment worked), even though it may appear cumbersome, may often be the more realistic option to cater for career mobility under defined benefit pension schemes. We discuss this matter further in Section 22.4.

12.2.3 Defined contribution schemes have a more straightforward approach. On leaving service, the individual's defined contribution account can be left in place, earning investment return until normal retirement age, at which point it will be converted into pension benefits in the normal way. Alternatively, the account balance may be paid immediately into another pension scheme or other approved vehicle as a transfer amount.

12.2.4 Because they are seen as more responsive and suitable to the needs of a mobile work force, many employees as well as employers favour the use of defined contribution schemes rather than the standard defined benefit model, particularly in areas where short-term contracts and mobility is a feature of the employment. In Chapter 14, we discuss the relative advantages and disadvantages of defined contribution and defined benefit scheme structures for the public service.

12.2.5 With the increasing age of entry, and depending on whether or not they are carrying pension rights from previous employments, large numbers of public servants will find that their potential service at retirement will provide them with a pension package that is less than they require or desire. Thus, there will be a strong demand for cost-efficient and flexible contribution arrangements to secure improved pension benefits, whether through schemes for purchase of notional service or AVCs. As shown below, many public servants are now contributing towards AVC schemes as a means of enhancing their pensions.

12.2.6 Apart from groups with standard pension terms, the developments discussed above have implications for groups which have *fast accrual* pension terms (e.g. Gardaí, Prison Officers). Part of the justification for these terms is that they allow the groups concerned to accrue pension benefits on a par with those which have standard pension terms, despite being required to retire

[164] The concept of preserved benefits (often known as deferred benefits in private sector schemes) is explained in Paragraph 3.3.44.

at an earlier age. If, in fact, the average level of service at retirement is falling for groups with standard terms, the continuing justification for this special treatment becomes less clear.

12.2.7 Similar considerations apply to specialist and professional groups which receive notional added years of service in respect of pre-entry educational or training qualifications, at a time when many of those now entering general public service grades have themselves prior qualifications or training.

12.3 Growth of atypical employment

12.3.1 Atypical, particularly part-time, employment has always been a significant component of public service employment. It is not clear at the present time that numbers of atypical employees are increasing. However, initiatives have been introduced in parts of the public service which, if taken up to any great extent, could lead to a significant expansion in such employment. In addition, new work options such as work-sharing and term time, will, if they prove popular, lead to an increase in the number of personnel who work in atypical forms of employment for at least part of their career.

12.3.2 The increased incidence of atypical employment will lead to pressure to ensure that pension terms are appropriate to such forms of employment. Were employment in the public service to change to a model of temporary or contract appointments, this would have major implications for pension scheme design. The new situation might be one in which individuals served for only short periods in the public service, with a very high degree of mobility between the public service and the private sector. A defined contribution pension scheme structure might be more appropriate in such circumstances. In addition, such an approach might better address the requirements of part-time employees.

12.4 Ensuring pensionability of atypical employment

12.4.1 As noted in Section 11.7, there is a strong move — coming from the EU and with support from public service unions — to ensure that atypical forms of employment are covered by pension schemes. Permanent part-time workers represent an important and growing category of workers generally with low levels of pension coverage.[165]

12.4.2 An EU Directive for equal treatment of part-time workers was adopted in December 1997. While the Directive does not specifically name pensions (it only refers to conditions of employment), it has been agreed in the context of the *Programme for Prosperity and Fairness* that the definition of remuneration in the Directive will include occupational pensions.[166] The necessary legislation will shortly be introduced by the Department of Enterprise and Employment. The Directive states that in respect of conditions of employment, part-time workers shall not be treated in a less favourable manner than comparable full-time workers solely because they work part-time unless different treatment is justified on objective grounds.

12.4.3 An EU Directive on fixed-term work (contract for service employment) was adopted in June 1999. As with the part-time Directive, it provides that fixed-term workers shall not be treated in a less favourable manner than comparable permanent workers solely because they have a fixed-term contract, unless different treatment is justified on objective grounds. Legislation to implement the Directive is to be enacted by July 2001.

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[165] The Pensions Board, *Securing Retirement Income* (1998), p. 154.
[166] Government of Ireland, *Programme for Prosperity and Fairness* (2000), Paragraph 6, p. 18.

12.4.4 In line with the situation in private sector schemes, the vast majority of part-time public servants are not included in pension schemes. As discussed in Section 11.7, the operation of integration is an issue of contention in relation to part-time public servants in full class PRSI.

12.4.5 Many public servants who have worked part-time for a period before being appointed to full-time pensionable positions are required to pay contributions in order to reckon the past part-time service for pension purposes (in some schemes, there is no requirement to reckon past service). Because the contribution rates in such circumstances are the same as the periodic employee contributions for current service, they are obviously much lower than the contribution rates charged under the schemes for purchase of notional service.

12.4.6 At present, public servants leaving employment with less than five years' service have no pension entitlements and are refunded any pension contributions which they have made. Thus, they obtain no benefit from the employer's element of their pension. Obviously, this would be a particular problem for contract employees who work for only a short period in the public service. However, there are proposals which have been accepted by Government to reduce the maximum period of reckonable service required to qualify for preserved benefits from five to two years.[167]

12.5 More frequent breaks in service

12.5.1 The introduction of career breaks and job-sharing from the mid-1980s has meant that many public servants now take breaks from full-time public service whether for family reasons, to travel abroad, or to study. The proposed replacement of job-sharing with the more flexible work-sharing facility will most likely bring about an increase in the numbers availing of the scheme. Greater use of temporary, contract, and seasonal working will also contribute to the growing number of pensionable public servants for whom breaks of service will be a regular occurrence.

12.5.2 At present, public servants have the option to *buy* service while on career break (see Paragraph 12.10.5 below). Alternatively, they can opt to make a lump sum purchase of service within six months of return from career break. The normal rules governing the purchase scheme apply — the individual can purchase service only if he or she is not in a position to accrue 40 years' service by age 65.

12.5.3 Public servants who avail of job-sharing also have the option to purchase service, subject to the rules of the purchase scheme. They must be over age 50 when job-sharing commences. Alternatively, they must have completed five years' continuous job-sharing, in which case they can project forward their future work pattern and purchase service based on the expected shortfall in making up 40 years' service. If they return to full-time work sooner than they expected they may be entitled to a refund of contributions.

12.5.4 We discuss the advantages and disadvantages of the purchase scheme as a means of making up shortfalls in service in Section 12.11.

12.6 Employee interest in retiring earlier than the norm

12.6.1 In Chapter 7, we review retirement experience across the public service over the past number of years. The evidence indicates that there has been a slight fall in both the average age of retirement and in the average period of pensionable service at retirement. While many public

[167] The Pensions Board, *Securing Retirement Income* (1998), p. 168.

servants remain in service until the maximum age of retirement and/or until they have accrued maximum pensionable service, there has been an increase in numbers retiring from the minimum age of retirement, sometimes with less than maximum service.

12.6.2 The majority of schemes do not provide the option for individual public servants to retire earlier than normal retirement age at full cost to themselves (i.e. *actuarially reduced early retirement*). This is a common feature of private sector pension schemes (see Section 8.15). The minimum age at which early retirement is offered on this basis is age 50 in the majority of schemes.

12.6.3 While many public servants would find actuarially reduced early retirement unattractive because of the reduction in income involved, we believe that the introduction of such an option in public service arrangements would bring much needed flexibility into scheme terms at no cost to the employer. It could be combined with new arrangements to allow the individual to contribute in advance towards the cost of early retirement.

12.6.4 As already noted, while the purchase of service schemes allow individuals to purchase additional service, they do this only by reference to the maximum age of retirement.[168] Thus, it would not be open to a public servant (having standard pension terms) who would have 40 years' service by age 65, to purchase service with the aim of retiring on maximum benefits within the age range 60-64.

12.6.5 Where a person has the potential to achieve maximum service at normal retirement age, funding for additional retirement pension and lump sum (for example, through an AVC scheme) is not permissible under Revenue rules. Thus, it is not possible to fund directly for early retirement in such a situation. However, it would be permissible to fund for other benefits, such as additional spouse's benefits or pension on non-pensionable earnings, in accordance with the Revenue rules. If the individual decided to take early retirement in due course, the balance on the AVC account would be available to supplement his or her own occupational pension benefits.

12.6.6 At present, public service pension schemes operate a fairly rigid approach to retirement and the calculation of pension benefits. As final salary schemes, the pension calculation focuses generally upon salary at the point of retirement and allowances averaged over the previous three years of service. While this has the advantage of encouraging public servants to seek promotion and career progression throughout their career, it also has the disadvantage of penalising those who might wish to reduce their work commitments in the lead up to retirement. In addition, the system makes it difficult for public service employers to redeploy individuals from areas which involve the payment of pensionable allowances to areas which do not because of the adverse effect on the individual's pension entitlements.

12.6.7 As pointed out in Paragraph 7.6.3, many countries have been seeking to encourage working beyond retirement age, to introduce more flexible working arrangements at older ages, and to replace the fixed point of retirement with gradual or phased retirement. The Commission is of the view that similar types of arrangements should be considered for the public service in Ireland.

[168] National and secondary teachers are an exception to this rule as they have an option to purchase service by reference to age 60 or 65 — see Paragraph 12.10.8.

12.6.8 For example, a more flexible approach to retirement might encourage public servants who would otherwise retire early to remain in public service employment for longer. Such an approach might cover the following:

- working at a lower level of responsibility (e.g. reverting to a lower grade);
- downscaling numbers of unsocial hours worked;
- part-time working.

12.6.9 The aim of any possible change to pension terms would be to ensure that the individual's pension would not be governed by the final salary and allowances in payment at the actual point of retirement. One means of achieving this would be to allow the individual to preserve benefits based on the higher salary/allowance point as at the date of changing his or her work pattern, with separate accrual of benefits based on the lower salary/allowance point in respect of the period served in the new work pattern. We understand that an adjustment of this nature has been made to pension terms in certain cases in the past.

12.6.10 With the increase in life expectancy and improvements in health and living conditions at older ages, some public servants may wish to remain in service longer than the maximum age of retirement. This option is not generally available in most parts of the public service; where such a facility is offered, it is a condition that no further pension entitlements are accrued beyond age 65. Another means of retaining public servants in employment after normal retirement age is the offer of fixed term contracts after the individuals concerned have formally retired.

12.7 Emphasis on delivery of service and management of performance

12.7.1 The process of public service reform under the Strategic Management Initiative is one of devolving authority and accountability in order to bring about better management of performance and improved delivery of service.

12.7.2 As well as comprising a major part of government expenditure, staff represent one of the primary resources of the public service. Better quality human resource management is a key element in the modernisation of the public service. Human resource management extends to a range of management decision-making which include a pensions dimension, e.g. designing the overall remuneration package, the management of redundancy and organisational restructuring. Pension schemes are also an important component in staff costs.

12.7.3 In the private sector, managers regularly use pension schemes as part of the effective deployment of staff resources, for example, in relation to:

- early retirement — to address situations in which staff numbers are surplus to requirements, in case of restructuring, or where improvements in efficiency might be realised;
- recruitment — offer of additional pension entitlements as part of the remuneration package for new employees;
- changing overall remuneration package of serving employees — for example, replacing non-pensionable overtime payments with pensionable shift allowance.

Because their pensions are externally funded, private sector companies normally calculate the capital cost of decisions having pension implications (see Paragraph 10.4.8) and, in many cases, pay this cost in advance to the pension scheme trustees.

12.7.4 Similar flexibility in the use of pension schemes at local level is not readily available to public service managers. Matters such as those listed above (including situations where an individual employee might be involved) are normally dealt with centrally, and usually require the approval or sanction of the relevant Government Department and/or the Department of Finance. This difference in approach between the public service and the private sector has to do, largely, with the approach adopted in the control of pension costs.

12.7.5 This in turn stems mainly from differences in how pension scheme costs are financed and accounted for. As shown in Chapter 5, the existing cash accounting approach to recording pension costs within government financial systems tends to conceal the long-term cost implications of current decisions. To compensate for this deficiency, the aim of departments and particularly the Department of Finance is to maintain a disciplined centralised control of pension costs. Sometimes this necessarily comes at the expense of local management flexibility. Also, as discussed in Section 5.2 and elsewhere, it is arguable just how effective the control of pension costs can be in a system where there is little transparency in the incurring of those costs.

12.7.6 It might be suggested that the lack of effective management and deployment of pension schemes at local level imposes a *"cost"* upon public service organisations. For example, because of the need to obtain central sanction and extra budget resources from the Department of Finance, managers may be unwilling to consider early retirement in cases where it might be the appropriate option. In addition, accounting structures may be such that any cash savings realised from an early retirement programme may not impact upon the organisation's own budget. These factors may result in the foregoing of possible efficiency gains and delays in implementing necessary organisational restructurings.

12.7.7 As an alternative to existing arrangements, the effective application of an accrual accounting treatment of pension costs would enable public service organisations to replicate some of the advantages of occupational pension schemes available to private sector companies. A change of this nature would be consistent with the need to bring greater transparency into the State's pension costs and support the process of devolving authority and accountability as close as possible to the point of delivery of public services, while still maintaining an overall control of spending. We consider this matter further in Chapter 24.

12.8 Changes in pay determination

12.8.1 It is unclear to what extent pay determination in the public service will be changed to a system in which performance-related pay becomes a major component. The evidence appears to suggest that the vast majority of public servants will, in the medium-term at least, continue to experience salary and career progression in broadly the same way as at present.

12.8.2 The existing final salary structure of public service pension schemes would have difficulties in dealing with a situation in which pay varied substantially during an individual's career. It would seem that a defined contribution approach would be better suited to such an environment.

12.8.3 In the private sector, once-off performance bonuses are not normally treated as pensionable. A similar treatment applies under public service schemes in respect of the small number of cases in which bonuses are paid.

12.8.4 As with non-pensionable overtime payments, it is open to individuals to contribute to AVC scheme in respect of bonus payments.

12.8.5 Under pay parity, pensions are increased in line with changes to salaries and pensionable allowances of those currently in service. Pay parity does not cover the impact of grade restructurings, payments resulting from changes in work responsibilities, and the effect of promotions and regradings included in pay agreements. It would appear that, compared with the past, these factors may become more regular occurrences. This would call into question the appropriateness of pay parity as a means of relating public service pension increases to earnings improvements amongst serving public servants.

12.9 Flexibility in pension terms

12.9.1 Having considered in the first half of this Chapter how adequately existing pension terms are addressing the main points of change in the public service, we now consider the degree of flexibility in pension terms currently available, particularly the schemes for the purchase of notional service and additional voluntary contributions (AVCs). Under these arrangements — which were the subject of a study carried out by consultants on behalf of the Commission[169] — public servants have the option to make additional contributions in return for better pension benefits.

12.9.2 Before examining these arrangements in detail, it should be noted that existing public service pension arrangements include several other types of flexibility which can be availed of by the individual. For example, public servants with standard pension terms have the option to retire before age 65 once they have reached age 60 and have at least five years' service. Also, there is a facility to allocate part of retirement pension to provide a separate pension for nominated beneficiaries.

12.9.3 Several forms of scheme choice and flexibility are available through the payment of additional pension contributions:

- improvement in pension benefits where service is less than maximum pensionable service of 40 years;
- measures to provide pension on allowances that are not pensionable under the scheme;
- measures to enable public servants to reduce the effects of integration;
- age of retirement: public servants may wish to boost pension benefits in case of retiring early.

12.9.4 Given the nature of these options, we consider it reasonable for each individual, not the pension scheme, to meet the costs involved.

12.9.5 In considering the question of individual pensions choice, it is necessary to have regard to the benefit limits laid down by the Revenue Commissioners for the purposes of approved tax exemption for pension schemes and contributions. These limits will often determine what benefit a member can choose to contribute towards and/or limit the amount of additional contribution which he or she can make.

[169] Commission on Public Service Pensions, "Review of Additional Voluntary Contribution and Purchase of Notional Service Arrangements", Report prepared by Mercer Ltd (May 1999).

12.9.6 For example, the option to pay contributions to secure additional pension and lump sum at retirement is restricted by the Revenue requirement that total pension benefits should not exceed two-thirds of final remuneration at normal retirement age.[170] Similarly, the Revenue limits in relation to spouse's pension and death gratuity are 4/9ths of remuneration and four times remuneration, respectively, while maximum public service benefits are one-quarter of remuneration for spouse's pension and one-and-a-half times remuneration for death gratuity. Apart from limits of this nature, tax relief on employee contributions is available only for contributions not exceeding 15% of annual remuneration. We summarise the more important Revenue limits at Appendix 12.1.

12.9.7 Our approach is to examine ways of providing maximum pension scheme flexibility for public servants, subject to considerations of:

- the value for money relative to contributions made;
- administrative requirements and costs imposed upon the State;
- maintenance of legal and regulatory oversight by the State.

12.9.8 As a first step, we consider the relative merits and demerits of the schemes for purchase of notional service and AVC schemes by reference to these requirements. We examine AVC practice in the private sector and consider briefly the implications of the development of Personal Retirement Savings Accounts (PRSAs). Finally, we reach a number of conclusions on existing arrangements. We take these up in Chapter 19 in our recommendations on a new approach to pensions flexibility for public servants.

12.10 Purchase of notional service

12.10.1 The first scheme for the purchase of notional service was introduced for established civil servants in 1979. Similar schemes have since been introduced for other public service groups. Subject to certain conditions, the schemes enable public servants to purchase notional service in respect of the shortfall which they would otherwise have in making up the maximum (40 years') service by retirement age. Appropriate actuarial tables are available to cater for the different purchase options available. The civil service scheme was revised in 1990, pushing out the age by reference to which service could be purchased from the minimum retirement age of 60 to the maximum retirement age of 65. The scheme has been designed in such a way as to make it self-financing, although we identify below some issues on this point. We list the purchase tables (i.e. the contribution rates charged to public servants) and discuss the actuarial basis of the scheme in Appendix 12.2. In Appendix 12.3, we detail the comments of the Commission's consultants on the pricing basis of the scheme.

12.10.2 To be eligible to participate in the civil service notional purchase scheme, applicants must have less than 40 years' potential service at age 65. A number of further conditions apply. The amount of service purchased may be affected as a consequence of the public servant having received, or having an entitlement to, retained benefits from a previous pension scheme.

12.10.3 Service can be purchased in one of two ways: by periodic deduction from salary or by lump sum payment. In the case of the latter, the option to purchase must be exercised within

[170] For the purposes of the Revenue limits, it is taken that the maximum public service retirement benefits of one-half of final remuneration for pension and one-a-half times final remuneration for lump sum is equivalent to two-thirds of final remuneration (see also Section 11.4).

two years of an employee's appointment, or within two years of maximum retirement age.[171] In circumstances where an employee has been on a period of special leave without pay or on career break, he or she can exercise a lump sum purchase option within 6 months of return to purchase a period of service which may not exceed the duration of the period of special leave or career break.

12.10.4 Purchase scheme contribution rates are calculated by reference to age. There are separate rates for:

- men and women (because of their different life expectancies);
- members and non-members of the spouses' and children's pension scheme;
- employees with different retirement ages (e.g. age 60 for Prison Officers; age 55 for Firefighters);
- staff appointed before and after 6 April 1995.

It should be noted that separate purchase tables are available to teachers to allow purchase of service by reference to either age 65 or age 60 (see Paragraph 12.10.8).

12.10.5 Alternative arrangements are available for career breaks. An individual can opt to pay a quarterly contribution for the duration of his or her absence on career break. The relevant rates for public servants appointed before 6 April 1995 are $18\frac{1}{6}\%$ for members of the spouses' and children's scheme, and $15\frac{1}{6}\%$ for non-members. These rates apply at all ages and to both males and females. The standard purchase rates for members of spouses' and children's schemes are lower at all ages up to age 56. To date, take up of this facility appears to be low.

12.10.6 Under the purchase scheme, the benefits in respect of each year purchased are in accordance with normal pension benefits, i.e.

- pension at maximum retirement age: 1/80th of pensionable remuneration or net pensionable remuneration as appropriate;
- lump sum at maximum retirement age: 3/80ths of pensionable remuneration;
- death-in-service gratuity: the service purchased at the date of death reckons in full for death gratuity;
- spouses benefit: for members of the spouses' and children's scheme, the service purchased at the date of death reckons in full for spouses' and children's pension. On death after normal retirement the spouse's pension is half the member's pension, i.e. the years purchased are generally fully reflected in the spouse's pension. For members who make a lump sum contribution, the years purchased are generally fully reflected in the spouse's pension on death pre- or post-retirement;
- in circumstances where a public servant qualifies for pension benefits before maximum retiring age (other than a death benefit or a benefit under the spouses' and children's scheme) the portions of his or her benefits which are attributable to purchased service are subject to actuarial reduction to take account of early payment of those benefits; and

[171] The restrictions on lump sum purchase are designed to prevent the possibility of an individual electing to purchase service in advance of an expected promotion, and so receiving a benefit from the scheme that was disproportionate to the amount of the contribution paid.

- the addition to pension arising from the purchase of notional service will attract pension increases in the same way as pension based on actual service.

12.10.7 In 1990, it was found that the contribution rates specified in the civil service purchase scheme were below what was required to meet the full actuarial cost of the scheme. The civil service unions were informed of this and accepted the necessity for increased contribution rates. A new scheme was offered which, in addition to the new contribution rates, contained a number of changes in conditions. The unions agreed to the revised scheme but opted for payment of purchase contributions up to age 65 rather than the age 60 limit which previously applied. While there was actuarial equivalence between the age 60 and 65 arrangements, the rates under the latter arrangement were lower, reflecting the longer contribution payment period involved and the assumption of retirement at the age of 65.

12.10.8 The revised purchase scheme and contribution arrangements were subsequently extended to staff in the local authorities, the health service and other public service groups. It was agreed with the teachers' unions that the revised purchase scheme for national and secondary teachers would be on the lines of that agreed in the civil service with the option of age 60 or age 65 contribution arrangements (or a combination of both).

12.10.9 As discussed in Appendix 12.2, the actuarial assumptions underpinning the purchase tables pose certain difficulties from the point of view both of the State and of the individual. We summarise some of these difficulties briefly below.

12.10.10 In general, the lower the rate of investment return assumed in the purchase tables, the greater the contribution rate. In the current tables, a real rate of return of 2.5% per annum is assumed,[172] which is similar to that used in the valuation of large funded pension schemes. However, purchase scheme contributions are not actually invested, and there is no obvious way of measuring what return is received by the State. It might be suggested that the assumption of favourable investment return, which helps to underpin the *competitive* pricing basis of the scheme (see the consultant's comments on the pricing basis of the scheme in Appendix 12.3) from the point of view of employees, in fact, exposes the State to additional costs.

12.10.11 A second assumption, the rate of salary progression, has a major impact on contribution rates. The single set of purchase tables for established civil servants, teachers, health service and local authority officers is based on salary progression of 1% per annum to maximum retirement age. In fact, an analysis of average pay progression across groups reveals significant variation from the 1% assumption. In addition, pay progression can vary greatly between individual public servants within any group. The effect which the salary progression assumption can have on the rates is shown in the following example:

> At age 30, the lump sum cost of one year's service based on a 2.5% per annum salary progression is 20.6% of pay as compared to 12.5% if a 1% per annum progression is assumed; on a salary of £20,000, the difference in the lump sum contribution would amount to £1,620.

12.10.12 Any person purchasing service whose rate of salary progression is greater than 1% per annum over the whole of his or her career will do better from the scheme than has been anticipated by the tables. The converse is true of public servants whose rate of salary progression

[172] In this context, the real rate of return is the annual return in excess of annual salary increases.

is less than 1% per annum. This suggests that the scheme, as presently constructed, offers better value to some groups as compared with others.

12.10.13 Another feature of the purchase scheme is that it offers better value to public servants whose salaries increase rapidly in the latter stages of their career (as they are paying a higher rate of contribution for a lesser period of time) than to those who have the same final salary but have had a more gradual increase in salary over their careers. However, it would not be possible to devise a meaningful set of tables which would allow a defined benefit purchase scheme to differentiate between individuals on the basis of assumed career paths.

12.10.14 Take-up of purchase of notional service schemes would appear to be low compared with take-up of AVCs. It would seem that approximately 400 primary teachers and 1,500 secondary teachers are availing of the purchase scheme, while 4,000 primary and 4,000 secondary teachers are availing of AVC schemes. Approximately 1,400 non-officers are contributing to the SIPTU AVC plan. Fewer than 300 civil servants are contributing under the purchase scheme, although the numbers eligible to participate in the scheme are low. The low take-up of the purchase scheme compared with AVCs may be partly due to the relative lack of promotion of the scheme compared with the more actively promoted AVC schemes and to the use of AVCs to maximise retirement lump sum thereby maximising tax relief.

12.10.15 We consider below the relative advantages and disadvantages of the purchase scheme for the individual and for the State.

12.11 Advantages and disadvantages of purchase scheme

12.11.1 The scheme for purchase of notional service is an important feature of public service pension arrangements. It enables the State to facilitate employees who would otherwise have less than maximum pension entitlements at retirement to acquire and pay for additional years of pensionable service without itself incurring any additional cost.

Advantages of purchase scheme

12.11.2 The primary attractions of the purchase scheme for the **individual public servant** may include:

(i) *Certainty and simplicity:* the scheme gives absolute certainty and clarity about the benefits being purchased. For example, a public servant who will have three years less than maximum service at age 65 can elect to purchase those years at full actuarial cost. The amount of the benefits will be related to remuneration at retirement and pension will be increased subsequent to retirement in line with public service pension increases generally;

(ii) *Guaranteed contribution rates:* the contribution rate being paid is fixed as a percentage of remuneration. There will be no adjustment even if the rate turns out to be lower than that required to meet the full cost of the years being purchased (if, for example, through promotion and increments, salary progression outstrips the assumption made for the purposes of the tables);

(iii) *No administration charge:* the State, not the individual, bears the administrative burden of operating the purchase scheme;

(iv) *Tax relief:* the individual receives tax relief at his or her marginal rate on the contributions made under the scheme;

(v) *Competitive rates:* depending on the individual's circumstances, and having regard to the certainty of the benefits purchased, the contribution rates may be seen as very attractive compared with those which would be required to secure a broadly similar (but more risky) level of benefits under an AVC scheme.

12.11.3 For the **State**, the benefits of the purchase scheme may be listed as follows:

(i) *Meets a staff need:* subject to certain conditions, the scheme allows individuals who wish to do so to enhance their overall pension package by means of contributions at competitive rates. The existence of the scheme has been an important component in the State's response to staff claims for the grant of *free* notional added years of service;

(ii) *Self-financing:* on the basis of the actuarial assumptions underlying the tables, the liability in respect of additional benefits secured under the scheme is matched by additional contributions from public servants. Thus, provided the assumptions are reasonable, a key objective of the State is satisfied. As detailed in Appendix 12.3, the Commission's actuarial advice indicates that the current pricing basis is broadly similar to that employed by private sector pension schemes when providing additional service credits in return for transfer payments from other employments/AVCs, etc.;

(iii) *Ease of communication:* while its rules may appear complex, the communication of the purchase scheme is straightforward as it provides benefits in exactly the same way as the pension scheme generally (i.e. based on final remuneration and years of service). This contrasts with the position relating to AVCs which must be communicated as individual cash balances to be converted into pension and lump sum at retirement.

Disadvantages of purchase scheme

12.11.4 For the **individual**, the disadvantages of the purchase scheme may include:

(i) *Inflexibility:* the main drawback of the scheme is its inflexibility in relation to:

- Retirement age — in most cases, service may only be purchased by reference to a service *shortfall* at age 65 (and age 60 in the case of national and secondary teachers), which means that those entering earlier than age 25 cannot opt to purchase, and that there is a limit on purchase which might be more restrictive than the Revenue limits;
- Benefits — under the scheme, benefits secured must follow main scheme design, i.e. retirement pension, lump sum, spouses' and children's benefits. Thus it would not cater for contributions towards a particular benefit (e.g. retirement pension or lump sum only), or where the public service benefits left a shortfall on Revenue limits (e.g. death gratuity);
- Income — unlike AVCs, the scheme does not allow an individual to contribute towards additional pension benefits in respect of items of non-pensionable earnings/integration, etc. It does not allow for the additional flexibility available to AVCs under the Finance Act, 2000 (see Paragraph 12.12.1);

- Contributions — there are significant restrictions on lump sum contributions and administrative problems in dealing with adjustment to periodic contributions.

(ii) *Cost:* notwithstanding the relative attraction of the benefits provided by the purchase scheme, there may be a perception amongst certain individuals that the rates charged are expensive;

(iii) *Pricing anomalies:* currently, some of the purchase of notional service tables attempt to incorporate an allowance for expected career and salary progression. Although valid from a global actuarial perspective, this can lead to pricing anomalies between different public service groups, for example, those who benefit from a series of promotions versus those experiencing flatter salary progression and individuals who experience a different *shape* of promotional increment.

12.11.5 For the **State**, the disadvantages of the purchase scheme could be listed as follows:

(i) *Underwriting risk:* under the purchase arrangements, the State underwrites substantial risk in relation to the purchaser, for example, as regards future salary and career progression, life expectancy, and the rate of pension increases paid in retirement. This may create certain difficulties for the State when it comes to actively promoting the purchase schemes;

(ii) *Cost:* while the scheme is designed to be cost neutral, the assumption of investment returns on employee contributions in line with pension fund returns may result in a cost to the State. In addition, the obligation to pay the benefits purchased will serve to increase even further the State's pay-as-you-go expenditure on public service pensions;

(iii) *Ensuring fairness of cost structure:* it is extremely difficult to put in place purchase tables which would be considered fair and would deliver value for money for the large number of different public service groups and for individuals experiencing different career and salary progression, while at the same time ensuring that the purchase scheme was self-financing;

(iv) *Administrative burden:* the State bears the administrative burden of operating the purchase of notional service arrangements. The system is complicated by the existence of a multiplicity of tables (for different public service groups) and also by difficulties associated with updating the tables following actuarial review. In addition, there are major problems in devising tables for staff in full PRSI class, in particular for lower paid staff.

12.12 Additional voluntary contributions

12.12.1 An AVC scheme is an arrangement which allows employees to make additional pension contributions to a trust which passes them for investment to an external financial institution. AVCs are used to improve the members' benefits over and above those provided by the pension scheme rules but within the limits laid down by the Revenue Commissioners. AVCs may be used where there would be a shortfall of service at retirement or where ultimate pension benefits would fall short of the Revenue limits. Amounts paid into an AVC scheme are invested on behalf of the individual public servant. At retirement, the cumulative fund is used to secure additional benefits, subject to the Revenue limits. Under the Finance Act, 2000, the new arrangements in relation to

Approved Retirement Funds and Approved Minimum Retirement Funds which were introduced in 1999 for the self-employed and directors of family companies have been extended to AVCs.[173] As a result of the change, AVC members now have much greater flexibility in the use of AVCs either at retirement or thereafter.

12.12.2 In the private sector, the payment of additional voluntary contributions may be included as a facility in the main pension scheme; alternatively, AVCs may be established separately to the main scheme under irrevocable trust. Whichever approach is adopted, AVCs must be aggregated with other member contributions so that the maximum total on which tax relief can be obtained is limited to 15% of remuneration. In addition, payment of AVCs must be monitored to ensure that overall prospective benefit limits are not exceeded. It should be noted that the Finance Act changes referred to in the previous paragraph do not affect the Revenue limits regarding contributions to AVCs.

12.12.3 In the civil service, AVC schemes were first approved by the Department of the Public Service in a letter to Personnel Officers dated 19 February 1987. They have since been extended to many other parts of the public service. Their introduction, which was agreed with the public service unions, was intended to provide employees with alternative, more flexible, arrangements to the purchase scheme for obtaining additional pension benefits by means of payments to an outside agency.

12.12.4 From the outset, union-centred AVC schemes have operated within the public service. The policy of the Department of Finance is that there should only be one AVC scheme per union. This is to help minimise administrative costs to the State in relation to the handling of payroll deductions for staff. The schemes are administered by trustees (almost invariably, trustee firms closely associated with the broker who promotes the arrangement or the institution who manages the investment) nominated by agreement with the relevant union under an approved trust deed. The Department of Finance or other relevant employer (e.g. the Department of Education and Science in the case of teachers, and individual local authorities, Health Boards, etc. in the case of personnel covered by the Local Government Superannuation Scheme) co-sign the trust deed as the *primary employer*.

12.12.5 There may be 40 or more different AVC schemes currently in operation throughout the public service. The larger schemes accommodate AVC savings in respect of teachers (primary and secondary) and nurses. As at the beginning of 1999, these larger schemes had membership of around 12,000, with an annualised contribution of £18 million. Total assets of the teachers' schemes amounted to around £50 million. Of 900 employees from amongst the approximately 1,400 members of the SIPTU AVC plan in the local authority sector, it was found that 260 were contributing 3-4% of salary, 300 were contributing 4-5% of salary, and 340 were contributing more than 5% (September 1998).

12.12.6 For public servants, the objectives of opting to pay AVCs may include one or more of the following (subject to the Revenue limits):

[173] For the groups affected (and in the case of AVCs) there is no longer an absolute requirement to purchase an annuity at retirement. Two new options are available. Up to 25% of the fund may be taken as tax-free cash, subject to the Revenue limits applying to occupational pension benefits generally. After providing for a minimum pension (£10,000 per annum) or preserving some of the fund (£50,000) they can take the rest of it in taxed cash, or they can invest it in an Approved Retirement Fund (ARF), an investment vehicle specifically designed for investing pension fund monies after retirement. There are no limits on the amount that can be withdrawn from the ARF (subject to any restrictions imposed by the investment manager). Income tax is payable on any capital withdrawn from the ARF; however, investment return is taxed within the ARF.

- obtaining better pension benefits at retirement (where pensionable service is less than 40 years), including better benefits where retirement takes place earlier than maximum retirement age;
- increasing the death-in-service gratuity from 1.5 times to up to 4 times final remuneration;
- increasing spouses' and children's entitlements (e.g. to make up the difference between maximum public service spouse's pension of one-quarter of deceased member's remuneration to the Revenue limit of 4/9ths of final remuneration);
- facilitating contributions towards additional benefits on earnings which are not pensionable under the main scheme, e.g. overtime;
- bridging the gap between an integrated and non-integrated pension for public servants in full class PRSI (i.e. to make up the Social Welfare offset);
- maximising the retirement lump sum entitlement where it falls short of the maximum entitlement of 1.5 times final remuneration.

12.12.7 Some AVC schemes (for example, some civil service plans) are used exclusively to enhance the level of death-in-service benefits. In contrast, it would appear that many teachers and nurses avail of AVCs with the aim of supplementing their pension entitlements on retirement earlier than age 65.

12.12.8 The Revenue limits are an important factor as regards the benefits which can be funded under an AVC. As noted above, public servants may contribute towards additional retirement benefits (pension and lump sum) where they would have less than 40 years' service at age 60. In Chapter 7, we show that many civil servants are in a position to have maximum benefits by age 60 (see Table 2 in Appendix 7.3); thus, they would not be eligible to contribute to AVCs on this basis. Other groups having lower levels of service at age 60, such as health service personnel and teachers, would be entitled to make AVCs for improved retirement benefits. Contributions for retirement before age 60 are possible in the case of those teachers who would be in a position to retire having 35 years' service between the ages of 55 and 60.

12.12.9 Where it is being used to provide extra pension rather than increasing death cover, an AVC scheme is really a variation on a defined contribution scheme. The main difference is that the scheme is an adjunct to main pension benefits rather that being the primary source of benefits. It shares all the characteristics of the defined contribution scheme insofar as an employee (occasionally an employer as well) contributes a generally predetermined rate to a fund over a period of time with the level of benefits being determined by:

- investment returns during the member's working lifetime up to the moment of retirement;
- the amount and timing of contributions paid in;
- market annuity rates for the purchase of pension at retirement (see below);
- charges levied and transaction costs incurred by the various brokers and investment firms involved.

We discuss the characteristics of defined contribution schemes in Section 14.4.

12.12.10 The choice available to trustees for investment in AVCs is extensive. It could include conservative cash deposits, with-profit plans, managed funds and specialised sector funds, although in practice the choice extended to individual members may be quite restricted.

12.12.11 An important factor which the AVC contributor must consider is the age at which he or she intends to retire. For a public servant planning to retire at, say, age 63 and paying AVCs accordingly, a decision to retire instead at age 60 would have a marked effect on the size of the annuity which he or she could draw. This is due to the smaller amount of money being invested than originally planned and the longer period over which the annuity would have to be paid (a reduction also applies under the purchase of notional service scheme where retirement takes place earlier than age 65 — see Paragraph 12.10.6). Compared with the purchase scheme, it is easier for the individual to change his or her contribution rate during service, for example, according to changed personal circumstances and the investment performance of the AVC fund.

12.12.12 Another important factor is the investment strategy to be followed. In the case of a managed or sector type investment, the date of retirement may happen to coincide with a downturn in the investment markets; this could result — because of a high equity exposure — in a significant loss of value to the AVC fund. Employees such as public servants generally have a long lead into retirement age and so exposure to the more high risk equity markets should be capable of being reduced by switching to fixed interest or cash funds.

12.12.13 At retirement, to the extent that it is not used to increase retirement lump sum, or has not been drawn down in accordance with the new Finance Act options (see Paragraph 12.12.1), the AVC fund must be used to purchase an annuity. There are different types of annuity which include:

- a level annuity;
- a guaranteed annuity (guaranteed on death of member for 5/10 years);
- an escalating annuity;
- a joint life annuity which provides a spouse's pension.

With an escalating annuity, pension increases may be at a specified level (e.g. 3% per annum) or partially linked to CPI.

12.12.14 The amount of the annuity depends on the mortality and interest rates assumed by the insurance company. Annuity rates are closely linked to long-term interest rates and these rates have varied greatly in the past; for a given sum, the annuities available in 1985 were about twice current annuity amounts. In recent times — a period with relatively stable interest rates — annuity rates have fallen significantly. Over time it is likely that they will continue to fall gradually as improvements in life expectancy are incorporated into the rates. On the other hand, while a fall in annuity rates is primarily associated with falling interest rates, one has to take account also of the tendency of asset values to increase in such an economic environment.[174]

12.12.15 In the public service, the trust deed for each AVC scheme makes clear that the employer's role is primarily a facilitatory one; the employer's administrative functions include providing the AVC trustees with information on individual entitlements (to ensure that the Revenue limits are not breached) and the deduction and passing on of contributions to the relevant financial institution. Whilst not having any formal legal association with the AVC

[174] See The Pensions Board, *Securing Retirement Income* (1998), p. 165.

arrangements, the *sponsoring* trade unions play a key role in relation to the selection and appointment of the commercial organisations responsible for the promotion, administration and investment of these arrangements.

12.12.16 It must be borne in mind, however, that under trust law and Revenue practice, every AVC scheme has to have a principal employer as a party to the trust deeds. In this role, the State has the power to appoint and remove trustees, to amend scheme rules in conjunction with the trustees, and to initiate the windup of the scheme. Thus, it is not possible under the existing environment for the State to absent itself from any direct involvement in the establishment and oversight of AVC arrangements. We note this below as one of the disadvantages to the State of the continuation of existing AVC arrangements.

12.13 Advantages and disadvantages of public service AVC schemes

12.13.1 Like the purchase of notional service scheme, AVCs allow flexibility to public servants who wish to contribute towards improvements in their pension benefits at no additional cost to the State. AVC schemes are now an accepted part of occupational pension arrangements in many employments, including the public service.

Advantages of AVCs

12.13.2 For the **scheme member**, AVCs may be seen as offering the following advantages:

(i) *Flexibility:* compared with the purchase scheme, AVCs are flexible in relation to:

- Retirement age – an individual can make contributions with the aim of retiring earlier than age 65;
- Benefits – it is possible to fund for any or all of the full range of pension benefits. These include funding for the shortfall in public service benefits as compared with the Revenue limits;
- Income – contributions may be made in order to secure benefits on non-pensionable elements of remuneration or to offset the effect of integration;
- Contributions – it is possible to vary rates of periodic contributions and to make lump sum contributions, depending on the individual's financial circumstances and retirement objectives, subject always to the Revenue limits;
- Use – the balance on the AVC account can also be drawn down in accordance with the options available under the Finance Act, 2000.

(ii) *Providing for early retirement:* in certain circumstances, it is possible to contribute under an AVC scheme with the aim of providing a supplement to pension in the event of early retirement;

(iii) *Tax relief:* as with the purchase scheme, additional voluntary contributions qualify for tax relief at the marginal rate;

(iv) *Participation in stock market:* scheme members may have a positive reaction to participating in the stock market, particularly at a time of rising share values;

(v) *Information and advice:* although there are exceptions, it would appear that external providers deliver comprehensive information/advice to scheme members. The fruits of this promotional activity are evidenced by the high take-up levels amongst certain public service groups.

12.13.3 For the **State**, the advantages of AVCs may be seen as including:

(i) *Absence of risk:* with AVCs, the State has zero exposure in relation to the substantial risks which it underwrites in the purchase scheme;

(ii) *Administrative burden:* AVC administration is carried out by external providers. Thus, other than the requirement to make payroll deductions in respect of a potentially large number of different schemes, the State has no administrative responsibilities;

(iii) *Funding:* some might see the provision of benefits from a fund held by a source independent of the State, rather than by the State itself on a pay-as-you-go basis, as an advantage of AVCs. In addition, with AVCs, the State would not be taking on potential additional costs through the provision of purchase rates on a competitive basis.

Disadvantages of AVCs

12.13.4 For the **individual public servant**, the disadvantages of AVCs may include:

(i) *Absence of certainty:* the amount of benefit will be determined largely by economic factors outside the control of the individual member — particularly, investment return during service and annuity rates at retirement. This lack of certainty is a fundamental point of difference with the purchase of notional service scheme. Furthermore, options such as pension indexation in line with public service pay increases are not available in the annuity market;

(ii) *Administration charges:* the cost of running the AVC scheme is met by deduction from employee contributions. Thus, other things being equal, this represents a disadvantage to members relative to the purchase of notional service approach — where the State carries administration costs. AVC administration charges can be high — we outline the consultant's examination of charge structures of public service AVC schemes in Appendix 12.4 (we address this matter further in Paragraph 12.14.2);

(iii) *Multitude of AVC schemes:* there may be more than 40 different AVC schemes in operation throughout the public service. Each appoints its own administrator, trustee, investment manager, etc. The fragmentation of the current arrangements may be seen as a disadvantage to both members and the State. Furthermore, the current approach does not capture any benefit from the *bulk buying power* opportunity which must be available.

(iv) *Trustee arrangements:* questions might be asked as to whether it is desirable or in the best interest of the members that in many cases the trustees of the AVC arrangements are closely related to the organisations who have a direct financial interest in the operation of the schemes. Occasions may arise where the best interests of the members may be in conflict to some degree with the commercial interests of the organisations with which the trustees are associated.

12.13.5 The disadvantages of AVCs for the **State** may be listed as follows:

(i) *Multitude of AVC Schemes:* as noted above, the State has to provide for a large number of different AVC schemes across all parts of the public service;

(ii) *State's role in relation to AVC schemes:* it is necessary for the State to carry out a number of formal responsibilities which go with its position as *primary employer* for the purposes of AVC trust deeds, i.e. in relation to the establishment and oversight of the AVC arrangements, including arrangements for the appointment and removal of trustees, *policing* of the Revenue limits in relation to the aggregate of AVC and main scheme benefits, etc.;

(iii) *Existence of two avenues for member flexibility:* the existence of purchase of notional service schemes alongside AVC schemes raises the question of ensuring that objective information on the relative advantages and disadvantages of both options is made available to individual public servants, who are then free to choose having regard to their own personal circumstances.

12.14 AVC arrangements of large private sector employers

12.14.1 In assessing public service AVC arrangements, we considered it useful to compare them with practice in the private sector. A brief survey of pension schemes amongst a small selection of larger companies covering a range of different industries indicated that:[175]

- most schemes provide an AVC facility on a defined contribution basis; additional death cover is not normally provided for as existing arrangements under the main pension scheme are usually regarded as adequate;
- because private sector schemes usually have 60ths accrual with an option to commute in favour of a lump sum (see Section 11.4), AVCs are usually taken in lump sum format, within Revenue limits, to avoid surrendering any of the main scheme pension (this is obviously different from a public service model where the basic entitlement comprises both a pension and a separate gratuity — thus limiting the scope to use AVCs exclusively for the purpose of maximising the tax-free lump sum);
- under defined contribution arrangements, it is usual to offer a full suite of investment options (i.e. varying from high equity to cash);
- where pensions are purchased from AVCs, it is usual to use open market annuity rates. However, four out of the ten schemes surveyed provide pensions from the main defined benefit fund priced mainly on the basis of long-term financial assumptions. Currently, such assumptions would tend to be more favourable than market annuity rates (this is not very different to the public service arrangement allowing the purchase of notional service by lump sum within two years of retirement);
- where administration charges are levied on members (four out of ten schemes), the typical costs are:

  flat fee: £25 per annum
  the flat fee or policy fee is an annual charge made on the AVC account.

  charge on contributions: 2% to 2.5%
  the charge on contributions or *handling fee* is a percentage deducted from the employee's gross contributions in respect of administrative costs including collection of the AVC contribution;

[175] In their report for the Commission (see Paragraph 12.9.1), the consultants examined practice in ten of their larger clients covering a range of different industries.

- investment management charges reflect *wholesale* rates available to large pension plans; typically these are in the order:

  bid/offer spread: 0% to 3%
  the employee contribution (less the charge on contributions) is used by the AVC scheme trustees to buy units in a unit linked investment fund managed by a life office or investment bank. The bid/offer spread is the differential between the price at which the institution sells units to the trustees and the price at which it buys these back. Thus, at encashment, the value of the individual's AVC investment account will be reduced;

  fund charge: 0.5% to 0.75% per annum
  this is the charge levied on units by the life office or investment bank for managing the investment fund;

- most schemes provide extensive promotional information and advice (e.g. projections of benefit, investment information, etc.) to their members; invariably (nine out of the ten schemes surveyed), the employer meets the cost of such services;

- just one scheme provides for an employer contribution to match the member's AVC contribution.

12.14.2 The **key differences** between existing public service AVC options and typical private sector practices are:

- as indicated in Appendix 12.4, overall charges levied on public service AVC schemes would appear to be higher than those charged in AVC schemes of typical private sector firms (the fact that the State does not meet any of the administration/promotion costs may be a factor in this — see Paragraph 19.3.16);

- charges are borne exclusively by scheme members whereas typical private sector practice is for employers to bear a significant proportion of the cost of operating the AVC facility (of course, in the context of the public service, the State meets the administrative costs of the purchase of notional service scheme);

- private sector AVC plans comprise a single legal entity, sponsored by the employer, and usually with a separate trustee board. Within this structure there may be several fund options (possibly from different institutions), but the key point is that the employer/trustees retain responsibility for the administration of the plan, appointment of external providers, etc.

12.15 Implications of Personal Retirement Savings Accounts

12.15.1 In Paragraph 8.21.6 we outline the Pensions Board's proposals in the National Pensions Policy Initiative in relation to the proposed new pensions vehicle, the Personal Retirement Savings Account (PRSA). A PRSA is to be an investment account owned by the individual and managed by an approved PRSA provider. It will be fully portable from one provider to another. While individual in nature, PRSAs could be grouped as an umbrella scheme or other group arrangement for administrative purposes.

12.15.2 If the Pensions Board proposals are put in place, every employer will be required to either have available an AVC scheme or to provide a payroll deduction facility to at least one PRSA provider to facilitate individuals who wish to make AVCs (currently, there is no obligation on any employer to offer an AVC facility).

12.15.3 We would suggest that the imminent introduction of PRSAs, against the backdrop of the large number of separate AVC schemes that already exist in the public service, could lead to problems in terms of further fragmentation of AVC-type provision.

12.15.4 Experience in the UK has shown that free-standing AVC schemes have consistently provided far poorer value to employees than employer sponsored AVC arrangements. A similar situation would be expected to hold true in an Irish context where either AVCs provided under a group trust or a group PRSA arrangement should be capable of delivering better value than under individually arranged PRSA policies.

12.15.5 The Minister for Social, Community and Family Affairs has committed himself to publishing by late 2000/early 2001 a Pensions Bill which will provide a framework for the introduction of PRSAs.

12.16 Conclusions

12.16.1 In the first half of this Chapter, we discussed how changes in the nature of public service employment affect the continuing validity of the basic principles and assumptions underlying existing public service pension schemes. The modernisation of the public service must be considered in this context. If the public service is to undergo a process of significant change in the future, corresponding reform of pension arrangements may be necessary.

12.16.2 The main trends of change which the Commission has identified in the public service, and which we considers relevant in our review of public service occupational pension arrangements, are:

- increasing age of entry, trend towards shorter service, and a more mobile work force;
- growth of atypical employment;
- ensuring pensionability of atypical employment;
- more frequent breaks in service;
- employee interest in retiring earlier than the norm;
- emphasis on delivery of service and management of performance;
- changes in pay determination.

12.16.3 Based on our analysis and the information and views made available to us, we have concluded that while there may be development in the existing model of public service employment by virtue of changes which might be expected in pay determination systems, greater variety in future work patterns, and increased mobility between the public and private sector, the majority of public servants will continue to be employed under the traditional framework in the medium- to long-term.

12.16.4 Pension terms must not be a barrier to change and should be capable of adapting to the developing work situation. It is important to determine whether a process of gradual reform rather than a more radical overhaul of the pensions system is necessary. We address this further in Part V of the Report, which deals with alternative pension scheme structures, and in our recommendations in Part VI.

12.16.5 In the second half of the Chapter, we examined the purchase of notional service and AVC schemes, each of which provide opportunities for individual public servants to *top up* their pension benefits, within the limits laid down by the Revenue Commissioners. The two sets of arrangements work in very different ways: under the purchase scheme, the public servant agrees to buy a specified number of added years of notional service, thereby increasing the total period of pensionable service for the calculation of pension benefits under the occupational pension scheme; under the AVC arrangement, the public servant makes contributions for investment in an individual fund which, at retirement, is used to provide additional benefits.

12.16.6 The relative advantages and disadvantages for the individual public servant of the purchase of notional service scheme and AVC schemes may be summarised as follows:

- the purchase scheme gives absolute certainty and clarity about the level of benefits being purchased. Benefits are risk-free and pension is increased in line with public service pay. Under AVC schemes, benefits are determined by external factors over which the individual has little or no control, such as investment return, annuity rates at retirement, and AVC charges;
- AVCs are significantly more flexible than the purchase scheme in terms of contributions, benefits to be funded (allowing for purchase of tax-free lump sum, amongst other things), age of retirement, etc. Even more flexibility is available to AVCs following the Finance Act, 2000 changes. Most importantly, AVCs can be used in certain circumstances to finance part of the cost of early retirement. It is difficult to envisage how the purchase arrangements could be amended so as to provide the same degree of flexibility;
- the assumptions underpinning the purchase scheme involve significant cross-subsidisations — public servants with relatively favourable career and salary progression will do better than the average, while those with relatively *flat* career profiles will do worse than the average. AVC benefits, on the other hand, are directly related to the amounts contributed by each individual;
- AVC funds not taken as lump sum or drawn down in accordance with the Finance Act changes must be used to purchase a pension annuity. In recent times, annuity rates have fallen significantly;
- there are no administrative charges included in the purchase table rates, while AVC scheme members are liable to meet scheme charges.

12.16.7 It is clear that personal requirements and circumstances are key factors in determining whether a person opts for the purchase of notional service scheme or the AVC approach. However, on the basis of data on actual take-up, AVCs schemes must be considered to be the more attractive option for a significant majority of public servants, notwithstanding the substantial benefits offered by the purchase option. The level of take-up of AVCs is a reflection, perhaps, of the increasing average age of new entrants, greater numbers of serving public servants in the 35-50 age bracket, the perceived flexibility of AVCs compared with the purchase scheme, and active promotion by external product providers.

12.16.8 For the State, the relative strengths and weaknesses of the purchase scheme and AVCs may be summarised as follows:

- with AVCs, the State bears no responsibility for the benefits provided. Thus, contrary to the position with the purchase scheme, these benefits do not serve to increase the State's pay-as-you-go costs for pension provision. In addition, with AVCs, the State is not required to underwrite risks in relation to future salary progression, life expectancy, and future rates of pension increases;

- the State has been able to point to the security and certainty of the purchase scheme as a particularly attractive feature of public service conditions of employment. However, the positive response to the scheme is diminished by its perceived disadvantages — particularly in relation to member flexibility — in comparison with AVC schemes;
- there would appear to be major difficulties in adapting the purchase tables to the changing requirements of the workforce — to cater for the increasing age of entry across a wide variety of public service groups, the impact of full PRSI for post-April 1995 new entrants, etc.

12.16.9 Apart from reviewing the features and relative strengths and weaknesses of the purchase scheme and AVCs, we have identified in this Chapter a number of issues to be considered in relation to current arrangements:

- as reported by the consultants (see Appendix 12.4), overall charges levied on public service AVC schemes examined would appear to be higher than those charged in AVC schemes of typical private sector firms. In addition, the multiplicity of arrangements in the public service reduce considerably the possibilities available from *bulk buying power*;
- in the public service, AVC charges are borne exclusively by the scheme members, whereas in the private sector employers often bear a significant proportion of the costs;
- as noted in Section 4.3, the State makes little effort to communicate benefit entitlements and pension options to its staff. To some degree, external AVC providers provide this service through their scheme booklets and ongoing advice and presentations to individual public servants;
- it is necessary to ensure that the State is in a position to carry out the formal responsibilities which go with its position as *primary employer* for the purposes of AVC trust deeds;
- with the advent of PRSAs, there would be concern that in the absence of action to address the matter, the already fragmented nature of AVC provision in the public service would be made even more complicated.

12.16.10 As indicated by the developments discussed in the first half of the Chapter, the increasing age of entry, more frequent breaks in service, and interest in early retirement, there is likely to be a growing demand in the future for a well designed, cost-effective, and flexible facility which would allow public servants to contribute towards improved pensions and a package more suited to their individual circumstances. For the State, the requirements of any such facility are cost, administrative convenience and the minimisation of any possible exposure under the legal and regulatory framework applying to the facility.

12.16.11 Having examined in detail the existing arrangements of the purchase scheme and AVCs, the Commission proposes in Chapter 19 new arrangements for pension scheme flexibility which we consider would be better capable of delivering on the requirements of individual public servants and of the State.

APPENDIX 12.1

Maximum benefits approvable by the Revenue Commissioners (*Revenue rules*)[176]

A brief note on the maximum benefits normally approvable by the Revenue Commissioners is given below.

1. Eligibility: Employees, whether full-time, part-time, permanent or temporary, can be included in a pension scheme. The defining characteristic of an employee is that he or she is taxed under Schedule E (the part of the tax code which covers workers who pay their tax under PAYE).

2. Normal retirement age: Any time between ages 60 to 70. Revenue may be prepared to accept a normal retirement age outside the above range for exceptional occupations.

3. Retirement pension at normal retirement age: A pension of two-thirds of final remuneration can be provided at normal retirement age for a member who has completed ten or more years' service with that employer.[177] If the member has less than ten years' service, the following scale applies:

Years of service completed by retirement age	1–5	6	7	8	9
Maximum pension as a fraction of final remuneration	$\frac{1}{60}$ per year	$\frac{8}{60}$	$\frac{16}{60}$	$\frac{24}{60}$	$\frac{32}{60}$

If a lump sum is paid at retirement, the maximum approvable pension is reduced by the pension equivalent of that lump sum.

4. The maximum member's pension calculated in accordance with the above is inclusive of the following:

- pension equivalent of any lump sum benefit at normal retirement age which is in addition to the member's pension;
- any pension derived from voluntary contributions paid by the member;
- deferred or current pensions from previous employment;
- retirement annuities in respect of any period of self-employed or non-pensionable employment, with certain exceptions;
- pension equivalent of refunds of contributions from membership of a previous scheme.

5. Tax free lump sum at normal retirement age: A basic cash amount of 3/80ths of final remuneration for each year of service can be provided. The maximum 120/80ths or $1\frac{1}{2}$ times final remuneration may be provided for any member with at least 20 years' service with that employer at normal retirement age. As in the case of a member's pension, the maximum lump sum may

[176] The main document outlining Revenue practice is the *Revenue Pensions Manual* issued by the Retirement Benefits District of the Revenue Commissioners.

[177] It is generally accepted that maximum public service benefits (pension and lump sum of one-half, and $1\frac{1}{2}$ times, final remuneration, respectively) is broadly equivalent to a pension of two-thirds of final remuneration, with commutation (see Section 11.4 of the Report).

have to be reduced in certain cases, e.g. where a member has a deferred lump sum from a previous employment. Where service is 8 years or less, a strict basis of 3/80ths of pay per year of service applies. For more than 8 years, a sliding scale goes from 3/80ths per year for 9 years, to 120/80ths for 20 years.

6. **Final remuneration**: Comprises total pay of an employee in respect of employment except where pay includes fluctuating elements such as bonus or commission. The latter must be averaged over the preceding three years. Final remuneration on which maximum approvable benefits can be based is generally one of the following:

(a) salary in any one of the last five years before retirement, plus fluctuating emoluments suitably averaged, or

(b) the member's total pay averaged over three consecutive years ending no earlier than ten years prior to retirement date.

7. **Lump sum benefits on death-in-service**: The maximum benefit is 4 times final remuneration at the date of death, plus the return of the member's contributions to the scheme with interest. Any lump sum provided in excess of this level must be used to purchase pension for dependants or other beneficiaries.

8. **Spouses' pensions (death-in-service or death after retirement)**: A maximum spouse's or dependant's pension of 2/3rds of the member's maximum approvable pension can be provided, inclusive of any retained benefits. Additional dependants' pensions can be provided to bring the total benefit to a level equal to the member's own maximum pension expectation. Children's pensions, where provided, must cease when the child is no longer dependent. The same limits apply on death-in-service and death in retirement.

9. Payment of the member's pension can be guaranteed to continue after the death of the member up to a maximum of ten years after retirement. Where the guaranteed period does not exceed 5 years, the outstanding instalments at death may be paid in a tax-free lump sum. No other lump sum may be provided on death after retirement.

10. **Benefits on leaving service**: In a contributory scheme, a member can elect to take a refund of contributions on withdrawal, subject to the preservation provisions of the Pensions Act. This refund is subject to a tax liability of 25% which may be deducted, if the rules permit, from the amount payable to the member. Where a refund of contributions is not possible, elected deferred benefits may be provided.

11. **Pension increases**: In general, the maximum increase which may be given on a pension after retirement is the increase in the Consumer Price Index or other similar agreed index (e.g. in line with salary increases) as applied to the maximum pension the member could have received. An exception to this is that increases of 3% per annum compound may be promised and paid, regardless of the level of price inflation.

12. **Early retirement**: The minimum age at which early retirement benefits can be paid to a member in normal health is 50 years. Any departure from this has to be considered on its own merits by the Revenue Commissioners. In the event of retirement due to ill health, there is no age limit and an employee retiring on ill health may be given benefits up to the maximum which he or she could have been given at normal retirement age. On early retirement other than on ill

health grounds, maximum pension and lump sum would usually be equal to those which could have been provided had the member continued in service until normal retirement age, based on final remuneration at date of retirement multiplied by N/NS where N is service to date of retirement and NS is service up to normal retirement age.

13. **Retirement after normal retirement age**: If a member remains in service after normal retirement age and total service at that date is, or exceeds, 40 years, additional benefits may be provided in respect of the service completed after normal retirement age, subject to an overall maximum of 45/60ths. Lump sums can be similarly increased. Alternatively, regardless of service completed, there can be an actuarial increase in the benefits to take account of the deferment of payment. As a further alternative, benefits could be provided based on any actual salary increases of the member to the date of retirement, or age 70 if earlier.

14. **Employee contribution**: Voluntary contributions are permitted on condition that they do not result in the maximum benefit which the Revenue would approve, based on the salary and service of the member, being exceeded. Employees may contribute up to a maximum of 15% of gross pay, provided that the total member contributions do not exceed 5/6ths of the total costs of all benefits being provided. The 15% limit includes voluntary as well as compulsory contributions.

APPENDIX 12.2

Actuarial basis for contribution rates for purchase of notional service

Basis for purchase tables

1. The principle underlying the calculation of the purchase table contribution rates is that the purchaser pays the full cost of the benefits bought. This means that the value of the contributions – either lump sum or periodic – should equal the value of the benefits. Given that the amount of benefits will not be known for many years until after the death of the purchaser (and his or her spouse), and given that the *investment return* on the accumulated contributions will never be known, the tables can only be drawn up on the basis of assumptions. In deriving a table, assumptions need to be made about the following:

(i) future rate of general pay increase;

(ii) future rate of investment return (notional) on contributions paid;

(iii) future mortality rates;

(iv) future salary increases due to promotion/increments;

(v) proportions married and age difference between spouses;

(vi) future rates of increase in the Social Insurance Old Age (Contributory) Pension (this is relevant in the case of public servants in full PRSI class who are subject to integration).

2. Different rates apply to different ages and by sex; separate tables are needed for groups with different maximum retirement ages, e.g. Prison Officers (60), Firefighters (55); and for groups with different PRSI status (e.g. established and non-established civil servants). The current contribution rates – periodic and lump sum – applying to established civil servants, teachers, staff in the health service and local authorities (and others) are given in Schedules I and II below.

3. For public servants in modified class PRSI, the contribution rate for a particular age and sex is levied on full remuneration; for public servants in full class PRSI, separate rates are levied on net remuneration[178] and on full remuneration; the value of the net remuneration contributions should, on average, equal the cost of the pension and the value of the full remuneration contributions should equal the cost of the gratuity.

Future salary increases and future investment returns

4. The assumptions regarding the future rate of general salary increases and the rate of investment are merged into a single assumption relating to the difference between investment return and salary increases, i.e. a real rate of return. There is no need to make an assumption as to either the absolute level of future salary increases or to the absolute level of investment returns. Purchase scheme contributions are not actually invested and there is no obvious way of measuring what return is achieved on the contributions paid to date since these contributions are not held separately from other Exchequer income. The approach adopted is to base the real rate of return on the rate likely to be achieved by large funded schemes which are otherwise similar to public service schemes. For recent tables, a real rate of 2.5% has been used;[179] this rate is at the upper end of the rates used in the valuation of funded schemes. In general, the lower the rate of return assumed, the greater the contribution rate.

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[178] Net remuneration is remuneration less twice the rate of OACP.
[179] This rate is the same as that assumed in the actuarial review of public service pensions (see Section 6.2).

Incremental/promotional scales

5. The rate of career salary progression varies greatly between public service groups and between individual public servants. At present, tables for non-established civil servants make no allowance for salary progression while the single set of tables for established civil servants, teachers, health service and local authority officers are based on a 1% per annum salary progression to maximum retirement age (MRA). Tables for Gardaí are also based on a 1% per annum salary progression.

An increase of 1% per annum from age 25 to 65 increases actual pay by about 50%. An analysis of current average pay by age for specimen public service groups, used for the purposes of the actuarial valuation of public service pension schemes detailed in Chapter 6, showed the following average annual pay progression from age 25 to age 65:

- non-established civil servants 0.3%
- established civil servants 2.4%
- nurses 0.7%
- teachers 1.6%
- Gardaí (age 27 to age 57) 1.0%

The rate of salary progression assumed has a significant impact on the contribution rate, as illustrated in the examples in Table 1. At age 30, the lump sum cost of one year's service based on a 2.5% per annum salary progression is 20.6% of pay as compared to 12.5% if a 1% per annum progression is assumed; on a salary of £20,000 the difference in the lump sum contribution would amount to £1,620.

Table 1: Theoretical contribution rates for a male public servant at age 30 for different rates of salary progression to age 65

Salary progression (per annum) %	Periodic %	Lump sum %
0	0.39	8.9
1	0.48*	12.5*
$2\frac{1}{2}$	0.62	20.6

* These rates are taken from Schedules I and II below.

In practice, few public servants would experience a level rate of salary progression from date of purchase of service to MRA. In general, the sooner the maximum salary (in real terms) is reached, the lower the theoretical periodic contribution that is required. The current periodic rate of 0.48% per annum at age 30 is based on a level annual increase of 1% from 30 to 65; if the same final salary were achieved over 10 years rather than over 35 years, the periodic contribution should be lower, at 0.42% per annum.

The value of the benefits purchased depends on actual salary at retirement but not otherwise on the pattern of career increases; if the contributions were being invested in a fund, then the amount of this fund at MRA would depend on the actual progression to final salary. A person entering at age 30 on a salary of £10,000 and retiring at age 65 on £25,000 will receive the same pension irrespective of how quickly he or she reached the salary of £25,000; however, if the person reached final pay level at age 45, the accumulated contributions (in an AVC fund) at age 65 would be 30% greater than would be the case if his or her pay increases were spread evenly between ages 30 and 65.

Mortality rates

6. Mortality rates may vary between public service groups; the practice to date has been to use the same mortality table for all groups; the current table is one of a number of different tables that are used in the valuation of funded schemes.

Current purchase tables

7. At present in the public service there are three main sets of purchase tables:

(i) table based on 1% salary progression;

(ii) table for public servants in areas where full PRSI already applied prior to the April 1995 change (no allowance for salary progression);

(iii) table for post-April 1995 entrants to areas where modified PRSI formerly applied.

The first table has been used for groups which receive increases from increments or promotion — established civil servants, local authority officers, teachers (who have two sets — based on retirement at age 60 and at age 65), and nurses and other health service officers. The second table is used for groups with low career increases — non-established civil servants and non-officers in the local authorities and health service. A separate table for the Garda Síochána is based on a 1% per annum progression to age 57. There may be other tables in use, for example, among non-commercial state-sponsored bodies.

It might be noted that the 1% per annum figure reflects, in broad terms, the average rate of increase at the present time over the ages 25 to 65 for teachers, established civil servants, local authority and health service officers.

Current set of assumptions

8. In summary, the main assumptions used in devising the most recent set of tables for established civil servants, teachers, and officers in the local authorities and health service are as follows:

- real rate of return: 2.5% in excess of annual salary increases;
- salary progression: 1% of net pay at all ages to age 65;
- spouses: 90% married up to age 55 and three years difference between spouses;
- mortality: standard tables of mortality published by the Institute of Actuaries and the Faculty of Actuaries.

Purchasers of service

9. Those opting to purchase service are likely to be a select group in terms of their likely career paths and mortality; for example, a person close to retirement and in poor health is unlikely to purchase service; if a lump sum purchase option were available at all times then members might be inclined to purchase service as they approached a possible promotion (the rules of the purchase scheme effectively exclude this possibility at present).

In theory, the assumptions underlying the purchase table for a group should take into account the likely profile of those who will buy service and not the average profile of the group. However, this would not be a practical proposition.

Schedule I

Purchase scheme — periodic contributions (for public servants in modified class PRSI with a maximum retiring age of 65)[180]

1. The table below shows the rate of periodic contribution for each year of service purchased which will be levied on salary payable between the date of the public servant's next birthday and the date on which he or she attains maximum retirement age.

2. Where purchased service is not an exact number of completed years, the contribution will be calculated by applying the appropriate fraction to the contribution rate in question.

Age next birthday at exercise of option	Non-Members of the Spouses' and Children's Pension Scheme		Members of the Spouses' and Children's Pension Scheme	
	Male	*Female*	*Male*	*Female*
20	0.25	0.32	0.34	0.35
21	0.26	0.33	0.35	0.36
22	0.27	0.34	0.37	0.37
23	0.28	0.35	0.38	0.38
24	0.29	0.36	0.39	0.39
25	0.3	0.37	0.4	0.4
26	0.31	0.39	0.41	0.42
27	0.32	0.4	0.43	0.43
28	0.33	0.41	0.44	0.45
29	0.34	0.43	0.46	0.46
30	0.35	0.44	0.48	0.48
31	0.37	0.46	0.49	0.5
32	0.38	0.48	0.51	0.52
33	0.4	0.5	0.53	0.54
34	0.41	0.52	0.56	0.56
35	0.43	0.54	0.58	0.59
36	0.45	0.57	0.6	0.61
37	0.47	0.59	0.63	0.64
38	0.49	0.62	0.66	0.67
39	0.52	0.65	0.69	0.7
40	0.54	0.68	0.72	0.73
41	0.57	0.71	0.76	0.77
42	0.6	0.75	0.8	0.81
43	0.64	0.79	0.84	0.85
44	0.67	0.84	0.89	0.9
45	0.71	0.89	0.94	0.95
46	0.76	0.94	1	1.01
47	0.81	1	1.07	1.07
48	0.87	1.07	1.14	1.15
49	0.93	1.15	1.22	1.23
50	1	1.24	1.31	1.32
51	1.09	1.34	1.41	1.43
52	1.19	1.46	1.54	1.55
53	1.3	1.59	1.68	1.7
54	1.44	1.75	1.84	1.87
55	1.6	1.95	2.04	2.07
56	1.8	2.19	2.28	2.32
57	2.06	2.49	2.59	2.64
58	2.38	2.87	2.98	3.04
59	2.82	3.39	3.5	3.58
60	3.43	4.11	4.22	4.33
61	4.36	5.19	5.32	5.47
62	5.9	7	7.14	7.36
63	8.99	10.63	10.79	11.15

[180] The tables in Schedules I and II are those applying at March 2000.

Schedule II

Purchase scheme — lump-sum contributions (for public servants in modified class PRSI with a maximum retiring age of 65)

1. For a public servant who opts to purchase service by a lump sum contribution, the following table shows the rates of contribution for each year of notional service being purchased which will be levied on salary payable at the date the option is exercised.

2. Where purchased service is not an exact number of completed years, the contribution will be calculated by applying the appropriate fraction to the contribution rate in question.

Age next birthday at exercise of option	Non-Members of the Spouses' and Children's Pension Scheme		Members of the Spouses' and Children's Pension Scheme	
	Male	*Female*	*Male*	*Female*
20	7.96	10.15	10.9	11.05
21	8.08	10.3	11.03	11.21
22	8.21	10.46	11.18	11.37
23	8.33	10.61	11.32	11.53
24	8.46	10.77	11.47	11.7
25	8.59	10.94	11.63	11.88
26	8.72	11.1	11.78	12.04
27	8.85	11.27	11.95	12.22
28	8.99	11.44	12.11	12.4
29	9.13	11.61	12.28	12.58
30	9.27	11.78	12.46	12.76
31	9.4	11.96	12.63	12.95
32	9.55	12.14	12.81	13.14
33	9.69	12.32	12.99	13.33
34	9.84	12.51	13.18	13.53
35	9.99	12.7	13.37	13.73
36	10.15	12.89	13.55	13.93
37	10.3	13.09	13.75	14.13
38	10.46	13.29	13.94	14.34
39	10.62	13.49	14.14	14.55
40	10.79	13.7	14.34	14.76
41	10.96	13.91	14.54	14.98
42	11.13	14.13	14.75	15.2
43	11.31	14.35	14.95	15.42
44	11.49	14.57	15.17	15.65
45	11.68	14.8	15.38	15.89
46	11.87	15.04	15.6	16.12
47	12.07	15.28	15.84	16.37
48	12.27	15.52	16.04	16.61
49	12.49	15.77	16.27	16.87
50	12.71	16.04	16.51	17.12
51	12.94	16.31	16.74	17.39
52	13.18	16.58	16.99	17.65
53	13.43	16.87	17.24	17.95
54	13.7	17.16	17.5	18.24
55	13.99	17.46	17.77	18.54
56	14.3	17.78	18.05	18.85
57	14.63	18.11	18.35	19.18
58	14.98	18.45	18.66	19.51
59	15.36	18.81	19	19.86
60	15.76	19.19	19.35	20.22
61	16.2	19.58	19.73	20.61
62	16.67	20	20.14	21.02
63	17.17	20.44	20.58	21.45
64	17.72	20.91	21.06	21.9
65	18.36	21.53	21.46	22.58

APPENDIX 12.3

Comments by pension consultants on pricing basis of scheme for purchase of notional service[181]

1. In our view the current pricing basis is broadly similar to that employed by private sector pension schemes when providing additional service credits in return for transfer payments from other employments/AVCs etc. In particular the typical interest rate ''differential'' between the assumed rate of investment return and the allowance for salary inflation tends to be in the order of 2% to 3%. Thus, particularly when considered in the context of a separate allowance being made for career progression the rate of $2\frac{1}{2}$% incorporated within the current NS [notional purchase] tables is very much in line with common practice amongst private sector schemes. The logic behind the assumptions used for funded private sector schemes is that it is reasonable to expect the return on an equity oriented investment portfolio to outstrip general salary increases by a margin of around 2% to 3%. The same logic is not directly applicable to an un-funded public sector arrangement. However, there are strong grounds for adopting the private sector model because:—

(a) it represents a competitive pricing basis for members, and

(b) it would be justifiable if the Exchequer chose to fund the purchase of NS arrangement and thus represents the ''opportunity cost'' of using such monies for other purposes.

2. We understand that the mortality table underlying the NS tables is PA(90) with a two year age reduction. In recent years Irish actuaries have tended to favour the more recent PMA(80) mortality assumptions which, on average, are about 4% more expensive than the older PA(90) table with a two year age reduction. Thus one might conclude that the current mortality pricing, when considered in isolation, is a bit on the weak side.

3. The purchase tables do not contain any explicit allowance for administration expenses and these are, therefore, borne by the Exchequer. Furthermore, pricing anomalies may exist between different groups and between individuals who experience varying salary progression. It is an inevitable feature of any purchase of notional service system that such cross-subsidisation will occur.

[181] Taken from Commission on Public Service Pensions, ''Review of Additional Voluntary Contribution and Purchase of Notional Service Arrangements'' (May 1999), Report prepared by Mercer Ltd.

APPENDIX 12.4

Consultants' examination of charge structures of public service AVC schemes[182]

1. The main providers to the existing arrangements consist of organisations providing administration services, investment services, scheme promotion and distribution and individual financial advice. In practice there are a range of charging structures in operation. From the literature provided to scheme members it is not possible in all cases to deduce the complete charging structure. However it has been possible to do so in respect of three cases which include some of the largest public service AVC arrangements.

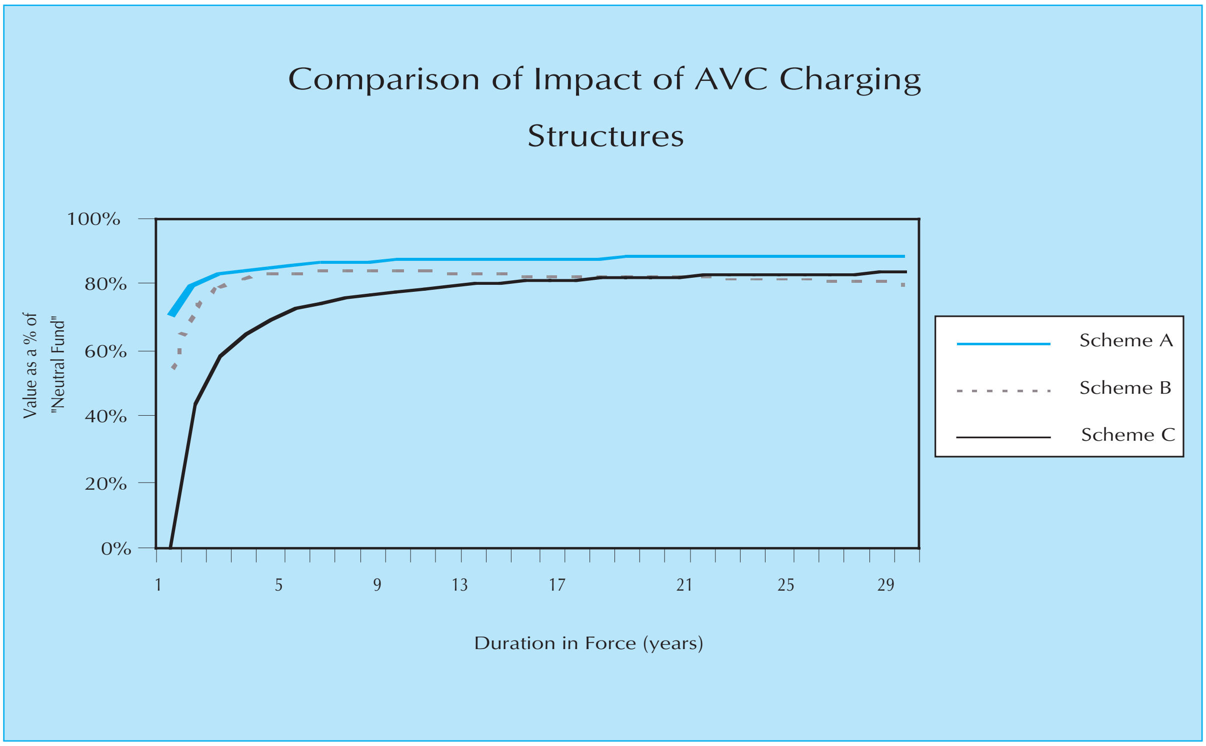
2. In respect of these schemes which we will refer to as Scheme A, Scheme B and Scheme C, the following are the main charges which are applied in practice :—

Charge Type	Scheme A (%)	Scheme B (%)	Scheme C (%)
Year 1 Allocation	77	100	0
Year 2 Onwards Allocation	97	100	97.5
Bid/Offer Spread	5	5	5
Annual Fund Management Charge	0.75	1.75 reducing to 1.25 after 15 years	0.75
Annual Policy Fee	£24	Nil	£30
Set Up Charge	n/a	£480	n/a

3. It is difficult to directly compare these charges given the variation in structures adopted. Furthermore it is not possible to gauge as to whether higher charges relate to the provision of higher quality and/or additional services to the scheme members.

4. To facilitate a relative comparison, we have carried out a projection as to how the accumulated value of AVCs would develop over time under the different charging structures on the assumption that each company achieved an equal investment return. For the purpose of this projection, we have taken a member aged 30 contributing £100 per month. We have projected the accumulated fund amount arising from a neutral cost structure (i.e. assuming no charges apply other than a 0.75% per annum charge in respect of investment management). We have then projected the accumulated fund values under Schemes A, B and C and expressed each as a percentage of the neutral cost fund amount. In this way we can gauge approximately the proportion of the overall contributions which go towards the various charges. The results of our projections are set out in the following graph:

[182] Taken from Commission on Public Service Pensions, "Review of Additional Voluntary Contribution and Purchase of Notional Service Arrangements" (May 1999), Report prepared by Mercer Ltd.



5. It is clear from the above that a significant level of charges are being levied on members of the public service AVC arrangements. These appear to range from approximately 12% of the overall fund up to almost 20% depending on the duration and scheme looked at. In respect of those schemes for which the charging structure is not explicitly available from the member literature we can only surmise that they must be of at least similar levels of magnitude.

6. It should be noted that the above percentage figures for charges cannot be taken as absolutes which apply in all circumstances. Instead they apply specifically to the assumed fund input and duration assumptions assumed earlier. The percentage level of charges would generally rise with lower fund input amounts and conversely be lower for higher input amounts. Duration is also a key variable.

7. The assumed level of investment return has a less significant impact on the level of charges. It should be made clear that higher charges do not give rise to any expectation of a better investment return.

8. Most larger private employers meet part of the costs of promoting and running their AVC arrangements. In the one case included in our survey where the employer does not contribute to the costs, the total administration charge (equal to 7.5% on a basis comparable to the above projections) is significantly lower than the equivalent rates to the public service scheme.

9. There is no particular reason why charges should be higher in public service AVC schemes than those of AVC schemes established by private sector employers. If anything, due to simple economies of scale, public sector AVC scheme member charges should be lower than their private sector equivalents.

10. A less direct comparison may be made with the recently launched IBEC Umbrella Pension Arrangement. The IBEC Umbrella Arrangement is a series of employer sponsored pension trusts established under the one umbrella. Each trust will have its own plan design, deed and rules and trustees. The umbrella arrangement provides for full administration, investment and consultancy services as well as the production of promotional material.

11. The total charges under the IBEC Umbrella Scheme amount to 8% of all contributions plus a fund management charge of 1% per annum. The only other charge is a Pensions Board registration fee of £5 per annum per member.

12. The IBEC Umbrella arrangement is significantly more complex and difficult to administer than an employer sponsored AVC arrangement. Projections of the IBEC charging structure on the same basis as used above for public service AVC arrangements show the IBEC charging structure to be equivalent to the best of the public service AVC schemes. This comparison makes no allowance for the additional complexity and diseconomies of scale inherent in the IBEC arrangement. Relative to the IBEC Umbrella Arrangement, the public service AVC arrangements are expensive in terms of the magnitude of charges levied.

13. There are potentially significant economies of scale to be obtained in terms of charges under the public service AVC arrangements. If the IBEC scheme charge level could be considered as the absolute maximum appropriate level, a target to aim for could be the low charge rates pertaining to the AVC arrangements operated by the UK Civil Service Pension Scheme. Under these arrangements the total charges appear to be of the region of $2\frac{1}{2}\%$ of money input plus a fund management charge of only 0.5% per annum plus a relatively small per transaction fee.

14. The economies of scale that can be realistically obtained in the UK are considerably greater than those which may apply in Ireland. Nevertheless it proves that there is considerable scope to obtain a significant reduction in fee charging levels applied to current AVC arrangements through obtaining benefits of scale economies and through placing appropriate pressure on the service providers.

PART V

Criteria for a Public Service Pensions Framework and Pension Scheme Design

CHAPTER 13

Criteria for a Public Service Pensions Framework

13.1 Introduction

13.1.1 Part IV of the Report presents an assessment and analysis of public service pension schemes, exploring the various issues which are to be addressed by the Commission. In Part V, we identify the shared objectives for public service pensions and develop a set of principles or criteria which a new public service pensions framework should be capable of meeting. We then examine alternative pension structures in order to determine whether a move to a radically different pension structure is necessary or whether instead it is preferable to reform the existing defined benefit structure so as to address the issues identified.

13.1.2 This Chapter deals with the identification of the shared objectives of, and the criteria for, public service pension schemes. In undertaking this task, we take account of the individual views and preferences of different *stakeholder* groups. The stakeholders include employees, government/employers, pensioners and the taxpayer. Other groups, too, have an interest in public service pensions, such as the pensions industry and business interests, and some of these have made submissions to the Commission. In our analysis, two broad categories of stakeholder have been given particular attention: *employees and pensioners* (including unions and employees, pensioner representative groups and individual pensioners) and *employers* (incorporating the Government and public service employers).

13.1.3 We begin by focusing on the separate concerns of employees/pensioners on the one hand, and government/employers on the other, as identified on the basis of submissions and views expressed (the points raised in submissions are reviewed in Chapter 2). We then endeavour to identify common points between both sets of concerns. Finally, we present our own assessment of the criteria to be met by the new public service pensions framework.

13.2 Concerns of employees and pensioners

13.2.1 Employee and pensioner submissions — which had common threads although with a different emphasis — indicated a widespread concern that public service pension schemes should be **viable and secure** over the long-term. The Commission detected a certain unease about the financial underpinning of public service pensions and about the long-term viability of the existing pensions system.

13.2.2 As regards pension terms, running through many submissions was a desire for greater pension **choice and flexibility**. Existing terms were seen by many as rigid and incapable of adapting to meet changing personal circumstances. It was suggested that employees generally wanted more scope to make their own decisions about how to increase their pension benefits, how to pay for the choice to retire early, and how to structure their benefits to meet their retirement needs.

13.2.3 The submissions confirmed that many employees were interested in having an **option to retire early**. Reference was made to a rapidly changing work environment, where the pace of both work and life was quickening, with the result that the experience of stress and burnout among public servants was more prevalent than heretofore. Some elements of pension schemes were seen as contributing to the pressures placed upon employees who were close to retirement — for example, the drive to work unsocial hours in order to boost final pensionable earnings, and the inability of the system to cater for those who wished to **adjust their work pattern** prior to retirement by working at a lower grade level or reducing their working time commitment.

13.2.4 Submissions referred to what were seen as **inequities in the pension treatment** of different groups — for example, it was claimed that one particular group might have lower retirement ages and more favourable terms compared with another, but that the more favourable treatment was not based on objective factors, such as differences in operational requirements. It was claimed also that treatment for the purposes of professional or specialist *added years* (the addition of years of notional service where the individual has particular professional expertise or qualifications) was also inequitable as between different public service groups.

13.2.5 The question of **equal treatment between men and women** arose in relation to a number of issues. Submissions pointed out, for example, that many female public servants worked part-time and so could expect very low or zero rates of occupational pension at retirement. A number of submissions noted that women who took up public service employment having previously resigned as a result of the *marriage bar* were required to repay their marriage gratuities with interest — which could amount to large sums of money — if they wished to have the first period of service reckoned for pension purposes. In certain areas of the public service, the question of options to join spouses' and children's contributory pension schemes affected female public servants particularly (see below).

13.2.6 For a variety of reasons, large numbers of public servants had opted not to join **spouses' and children's contributory pension schemes** when membership was first extended to them, or at a subsequent date. Submissions from several groups and individuals sought a further option to join, on the basis of a change in personal circumstances and/or misunderstanding of the significance of the original decision. Some referred to ongoing legislative and social developments, such as the introduction of judicial separation and divorce, and the changing position of women in society.

13.2.7 Other submissions expressed concern about the low rates of occupational pension emerging for public servants in full PRSI class whose pensions were subject to **integration** with the State Social Insurance system and who retired on relatively low levels of pay. Concern was expressed also at the pension treatment of **part-time employees** who because of the operation of integration could expect to receive a very low or zero rate of occupational pension. Payment of some form of minimum occupational pension was sought in a number of submissions.

13.2.8 The exclusion from the **definition of pensionable remuneration** of certain non-pensionable allowances, such as overtime, was raised in a number of submissions. On a related point, submissions from pensioner representatives argued that where particular allowances had been made pensionable from a specific date, the consequent increase in pension should have applied not only to those who retired on or after that date, but also to those who had retired before that date.

13.2.9 Many submissions, particularly those received from pensioners, referred to **pensions increase policy**. They expressed concern that the existing system of pay parity might be under threat, particularly in the context of the new restructuring type agreements, for example, those made under the *Programme for Competitiveness and Work*. They argued that public servants had contributed towards the cost of earnings-related pension increases and that these represented an entitlement.

13.3 Concerns of Government and public service employers

13.3.1 The importance of managing the **evolving cost of pensions** was a key focus of departmental/employer submissions. An important objective for employers was to prevent any further escalation in what was seen as an already difficult cost outlook.

13.3.2 Emphasis was placed on the rise in pension costs expected to occur around the period 2015-25. At that time, submissions noted, demographic ageing generally would be placing greater demands upon Exchequer resources through increased expenditure on the health service and on Social Welfare pensions. They argued that the long-term **cost implications of improvements in benefit terms** needed to be carefully evaluated. In their view, changes to pension terms should be broadly cost neutral and ideally be designed so as to bring about a reduction in pension costs. They argued that claims for benefit improvements in relation to early retirement and minimum pensions should be assessed in this context.

13.3.3 The possibility of setting aside finances now with the aim of helping to meet the expected peak in costs — i.e. some form of **advance funding** — was suggested as worthy of consideration.

13.3.4 The lack of **transparency in pension costs** under the pay-as-you-go system was a particular concern for employers. Given the time-lag that usually occurred between the incurring of costs and actually meeting those costs, they suggested the long-term cost implications of decisions on pension scheme coverage, recruitment of new employees and early retirement tended to be overlooked.

13.3.5 Some submissions argued that with increasing life expectancy at older ages and improvements in health and living conditions, there was a case for increasing **retirement ages**, given that these had been fixed in the nineteenth century.

13.3.6 On the other hand, some employers argued that, for operational reasons relating to a number of specific groups, existing retirement ages which were lower than the standard retirement age (and linked to enhanced pension terms) should be retained in present circumstances. However, they expressed concern about the potential knock-on effects of these **special terms** on other groups. They suggested that it was essential to ensure on an ongoing basis that special terms were linked to current operational requirements, such as the need to maintain a comparatively low age profile in the occupations in question. They argued that where there was a substantial change in operational requirements over time, this should be reflected in the adapting of the special terms; in some situations it might be necessary to remove the special terms. They suggested that rationalisation along these lines would ensure greater internal equity within the public service pensions framework and bring greater concordance between public and private sector pension terms.

13.3.7 Submissions stressed the need to ensure the continued appropriateness of existing public service pension terms in the light of current employment conditions and operational requirements and the changes which might be expected for the future. While the public service norm, at least in the short to medium term, was likely to remain close to the traditional model of employment for life, **pension systems had to adapt to change** taking place in public service employment, including later ages of entry, greater incidence of atypical employment, and the possibility of greater employee mobility. It was suggested that a move in pay determination away from a relativities approach towards more performance-related remuneration had also to be taken into account. Employers asked whether the pensions system was sufficiently adaptable to meet all of these developments, or whether it should instead be fundamentally redesigned.

13.3.8 Employer submissions suggested that as a result of these changes the new environment should be one where there was a more **active role for the employee** in providing for his or her own pension.

13.3.9 Some employers pointed to **particular rigidities in the existing system**. While these were not always pensions issues, there was often a pensions dimension. For example, in some parts of the public service recruitment of part-time employees was problematic, and job-sharing — i.e. the splitting of one job between two individuals — was the only available option. Different pension calculations applied in respect of employees who were job-sharing and those in part-time employment. Employers argued that in order to provide services more efficiently and effectively, they needed to have much **greater employment flexibility** as regards work pattern, the number of hours worked, duration of employment, retirement, etc., and that pension systems should facilitate rather than hinder the introduction of such flexibility.

13.3.10 It was suggested also that some public service pension terms were **overly expensive in comparison with those in the private sector**. Particular reference was made to the public service practice of increasing pensions in line with increases in pay, compared with best practice in the private sector of increasing pensions in line with price inflation. Submissions from pension industry representatives advocated introduction of the latter approach for public service schemes. Employers asked whether **pay parity** was an appropriate method for protecting pensions during retirement, particularly in a context where pay increases might have been granted to particular groups of employees on foot of changes in their duties and responsibilities and given that the emphasis on linking pay increases to changes in the nature and responsibilities of jobs was likely to be accentuated in the future.

13.3.11 The application of **professional added years** was also raised. It was suggested that the continued need for this facility should be reappraised in the light of changes occurring in the labour market and in private sector pensions coverage since it was originally introduced.

13.4 Shared goals

13.4.1 On the face of it, the different concerns of scheme members and pensioners and public service employers are difficult to reconcile. However, the Commission has identified points of overlap between the two sets of submissions, as set out below.

13.4.2 Both parties accept the view that the State as an employer should offer **good pension schemes** to its employees, and that the schemes should be **credible, secure and stable**. Employers wish to ensure that their employees are protected adequately against the contingencies of death or ill health and can anticipate a reasonable standard of living in retirement. For their part, employees need to be confident that they and their dependants will be financially secure in the event of death or ill health and will have a reasonable source of income in retirement.

13.4.3 Both agree that pension terms should be applied to all public servants under a **consistent set of principles**. Differences in treatment between public service groups should be based, insofar as possible, on objective, verifiable, operational criteria, and these should be subject to regular review and updating.

13.4.4 The need for pension terms to be **adaptable and flexible** is accepted by employers and employees. Increasingly, public service employers are adopting new approaches to employing personnel in order to deliver on the standards of service and quality expected under the Strategic Management Initiative and the requirements of public service reform. Equally, many employees, particularly female employees, find that atypical forms of work, e.g. part-time or temporary working, meet their needs through the additional personal flexibility they offer. Accordingly, there is an acceptance that pension schemes should raise no unnecessary barriers to the introduction of change desired by both employers and employees and, in particular, that they should be capable of catering for atypical forms of employment.

13.4.5 For employees, the desire for flexibility extends to **choice** within the pension system itself — for example, in relation to early retirement, dependants' benefits, and improving pension benefits generally. For their part, employers would be willing to facilitate the offer of additional pension flexibility, provided that there was no additional cost to the pension scheme, that the administrative costs were reasonable, and that the new facilities did not become a barrier to mobility either within the public service or between the public service and the private sector.

13.4.6 Employers and employees have a shared interest in ensuring that pension schemes do **not result in a distortion of preferred work choices**. Employees might wish — for reasons of choice but also of health — to adjust their work towards less operationally demanding duties or to work reduced hours in the lead-up to retirement, without unduly affecting their pension rights. This could suit management too. However, the present pension system, with its focus on final earnings, has the effect of encouraging public servants to work longer and/or more unsocial hours towards the end of their careers in order to boost pension benefits. This may be in the interest of neither the employee nor of the service concerned.

13.4.7 Both employers and employees require that pension terms are **applied transparently and fairly**. There is a shared interest in having a pension system that is **efficiently administered**, with changes in pension arrangements effected without undue disruption and confusion. Scheme provisions, including benefit entitlements and options which may of their nature be quite complex, should be **actively communicated** in as simple and straightforward a manner as possible, and unnecessary complexity in pension schemes should be eliminated.

13.4.8 Both parties accept that pensions should be **financed in a balanced way between employers and employees**. Both would wish to minimise the risk that the benefits promised might not be delivered due to the cost reaching a level which became unaffordable to the taxpayer. They would be willing to consider some form of advance funding — through the investment of employee and employer contributions in an independently controlled fund — on the basis that this would help promote the robustness and long-term viability of benefit promises.

13.4.9 In conclusion, employers, employees, and pensioners have a common interest in **securing the long-term viability and stability of public service pension schemes**. Equally, they wish to have in place pension arrangements that are affordable, fair, flexible and transparent, and that can be justified to the wider public who must ultimately finance them.

13.5 Criteria for a public service pensions framework

13.5.1 A Commission must take note of and carefully consider the views of interested parties, but without being bound by them and without permitting them to preclude other options. Our analysis of the issues suggests that public service pensions should be assessed on their ability to meet the following requirements:

- adequacy and comprehensiveness;
- viability;
- flexibility;
- fairness;
- cost.

We discuss each briefly below.

Adequacy and comprehensiveness

13.5.2 The State, as a good employer, should offer comprehensive and adequate pension schemes to its employees, taking account of pension terms and arrangements available in the private sector and in public sectors in other countries at a similar stage of economic development.

Viability

13.5.3 Benefits promised should be affordable to the taxpayer and reasonable in relation to the country's capacity to pay.

Flexibility

13.5.4 Pension structures should be capable of dealing with the position of the low paid, part-time employees, contract workers, and those with variable earnings. They should also be capable, insofar as possible, of offering choice to public servants in relation to their pensions package and retirement decisions.

Fairness

13.5.5 Fairness in pension terms means that differences in treatment between groups should be based on clear objective criteria, and that pension terms are seen to be applied transparently and correctly in all cases.

Cost

13.5.6 The long-term development of pension costs should be known and prepared for in advance. The consequences for pension costs of decisions in relation to recruitment, early retirement, improvements in benefit terms, etc. should be clearly costed and made transparent.

13.6 Conclusions

13.6.1 This Chapter has outlined the concerns of employees, pensioners, and employers as set out in submissions received. On the basis of these, the Commission has developed a listing of shared objectives for public service pensions and a set of criteria which should be met by any new public service pensions framework. These objectives and requirements will be used in our assessment of alternative pension scheme structures in Chapter 14. In addition, they will be used to guide our recommendations in Part VI of the Report.

CHAPTER 14

Alternative Pension Scheme Structures

14.1 Introduction

14.1.1 The analysis of earlier Chapters has dealt with the issues raised in relation to the existing public service pensions structure. However, an important consideration is whether in the light of the analysis a completely new pensions model for the public service should be proposed as an alternative to reforming the existing structure. This is particularly important given the long-term outlook which we have adopted in our deliberations.

14.1.2 In this Chapter we outline a number of different pension structures and consider how they might be applied in a public service context. We evaluate the advantages and disadvantages of each structure in light of the criteria for a public service pensions framework identified in the previous Chapter.

14.1.3 As a first step, we review the strengths and weaknesses of the existing defined benefit pension structure of public service pension schemes.

14.2 Existing public service defined benefit pension structure

14.2.1 Pension terms are an integral part of the remuneration package of public servants. Together with security of tenure, the occupational pension is a particularly attractive feature of public service employment and represents an important component in the recruitment and retention of employees.

14.2.2 The current design of public service schemes is consistent with the traditional attitude of public service employers towards their employees. According to this view, the public servant is expected to remain in service for a long period of time and the employer, accordingly, should accept far-reaching responsibility to provide for him or her. This view is consistent with the idea of pensions as a form of extended (albeit reduced) earnings.

14.2.3 The main arguments in favour of retaining the existing defined benefit scheme structure of public service pension schemes are as follows:

(i) **maintenance of living standards:** since the pension level is related to the employee's earnings immediately prior to retirement, it guarantees (with sufficient service) a standard of living related to the one enjoyed at the end of his or her career. In addition, the fact that pension increases are paid in line with earnings increases helps maintain the standard of living of the pensioner by reference to the position of serving public servants;

(ii) **incentive to earn promotion:** the final salary principle favours public servants whose careers offer a high salary during the final phase of their employment. Their pensions are higher in relation to their career earnings than for those whose salary does not change very much throughout their career. While this could be considered a disadvantage, it has the benefit of making the connection between performance, as measured by earnings, and pensions very clear and thus directly encouraging individual performance and career progression;

(iii) **lower employee turnover:** the current pension structure, which places a premium on the achievement of the highest possible level of pensionable earnings, encourages employees to remain in public service employment throughout their working life;

(iv) **security:** the risk associated with the pension promise rests with the employer rather than with the employee — this obviously suits the employee. The employer will usually make good any shortfall arising in the financing of the scheme, while members' contributions remain unchanged (in the public service pay-as-you-go approach, there is no direct connection between the rate of employee's contribution and the ultimate cost of the scheme);

(v) **equitable, fair, and attractive pension terms:** virtually all public servants are covered by occupational pension schemes, and pension terms are considered to be attractive by reference to the private sector (see Chapter 8). In addition, in applying one common set of pension terms, the aim is to ensure consistency, equity, and fairness across the whole public service;

(vi) **mobility:** pension schemes support the free movement of employees across different parts of the public service. Mobility with the private sector and abroad can be catered for through preservation and purchase provisions;

(vii) **adaptability:** the pension structure has shown itself to be reasonably adaptable to the needs of public service employees. Examples of change include the introduction of spouses' and children's schemes, preservation of service, purchase of notional service, AVCs, etc.

14.2.4 The nature of public service employment is changing. While appointment on a permanent full-time basis will remain the primary model of employment, at least for the foreseeable future, an increasing number of public servants are likely to be employed in a temporary and/or part-time capacity. Against that backdrop, it can be argued that the employer's responsibility as regards occupational pension should now be different to that proposed in Paragraph 14.2.2, and that this should be reflected in a radically different pensions structure.

14.2.5 The main arguments which may be made against continuing the existing defined benefit scheme structures for public service pensions include:

(i) **pensions seen as deferred not extended earnings:** it is now generally accepted that pensions represent deferred earnings, i.e. a portion of the remuneration package that is set aside or saved in order to provide for the individual's old age. If that is the case, it would be more appropriate that pension be correlated with earnings all through service rather than with earnings at retirement. An employee's work contribution earlier in his or her career should have the same value when it comes to calculating his or her pension as final salary;

(ii) **salary progression:** the final salary principle favours those whose careers offer a high salary during the final phase of their career. This approach raises questions as to the fairness of the system. It also raises cost issues for the employer who, in effect, must raise the pension in the case of the employee who has enjoyed more favourable career progression;

(iii) **manipulation of final earnings:** there is a risk that the final salary principle may encourage manipulation of an employee's earnings for the purpose of achieving an excessively high pension. Conversely, the principle makes it problematic to reduce work commitments prior to retirement, even if both the employer and the employee might consider this desirable — this applies equally to pensionable allowances;

(iv) **uncertainty of cost:** in a defined benefit structure, the final cost cannot be predicted. As shown in Chapter 6, detailed actuarial calculations, based on uncertain assumptions, are necessary to ascertain the long-term cost. Employees do not need to worry about the financing, since it is the employer who bears the risk of the costs being higher than estimated;

(v) **resistance to change:** defined benefit final salary schemes can by their nature create resistance to change. Since a certain proportion of the pension has always been earned at any given time, it is difficult to change the promise in a way that is both reasonable and fair. Changes for the worse, however reasonable and necessary they may be, may perhaps with some justification be described as a breach of promise (it would be easier to change a defined benefit scheme based on career earnings, as the change could clearly be applied to future earnings only);

(vi) **obstacle to mobility:** it is sometimes argued that defined benefit final salary schemes are an obstacle to labour mobility (but not within the public service where a transfer network applies) — this is the obverse of the argument that the schemes encourage employees to remain in the public service for their full working career.

14.3 Alternative pension structures

14.3.1 Of the wide range of possible pension structures available, we considered the following:

- **defined contribution** — under this structure, the employer and usually the employee make a pre-determined contribution, expressed as a percentage of salary, into an account held on behalf of the employee. The contributions, less charges levied on them, are invested up to retirement and the pension at retirement is whatever the employee's fund at that point can buy (up to one-and-a-half times salary can be taken as a tax-free lump sum). Thus, the pension is determined directly by the contributions made, the investment return on those contributions, and annuity rates at retirement. It is open to employees to make additional employee contributions to secure additional benefits. As noted in Chapter 8, newly established occupational pension schemes in the private sector are generally defined contribution, while in some companies, membership of existing defined benefit schemes is closed, with new entrants being enrolled in defined contribution schemes;
- **hybrid scheme design** — a hybrid design can take one of many forms. In the example which we consider below, the *core* of the scheme is a defined benefit component, which provides pension in respect of basic pensionable salary, and the remainder is a defined contribution component in the form of a retirement savings account. The account can be used to provide retirement lump sum, to cover pension on pensionable allowances, or to provide for pension increases;
- **career average earnings** — under this structure, benefits are calculated not by reference to salary at the point of retirement, death, or leaving service, but on the average salary earned over an employee's career. In other words, subject to adjustment by reference to an appropriate index up to the point of retirement (e.g. prices or pay), the salary level

at recruitment would be taken into account just as would the retiring salary in the calculation of retirement pension.

14.3.2 In considering potential scheme designs,[183] the Commission decided that any new scheme should be expected:

- to deliver a broadly similar level of benefits as is provided under existing pension schemes;
- to introduce appropriate flexibility in relation to changes which have or may take place in the future in the nature and conditions of public service employment; and
- to provide a means of addressing the need to manage and contain the growth of the long-term cost of public service pensions and potentially to mitigate the peak in pension costs anticipated between 2015 and 2025.

14.4 Defined contribution

14.4.1 Public service pension schemes could, in principle, be operated on a defined contribution model, though a transfer to such a system would be considered a radical change in the Irish context. The essential features of this model are:

- contributions are made to individual defined contribution funds by employers and employees;
- pension is determined primarily by fund performance and pension annuity rates at retirement;
- management of pension funds is carried out by a dedicated organisation; and
- there are varying degrees of individual discretion in determining the pension fund portfolio.

14.4.2 The most fundamental difference between a defined benefit and a defined contribution scheme is the certainty of the former's benefits compared with the latter's exposure to market investment returns, good and bad. Because future investment returns are not predictable and potentially may be highly volatile, the eventual outcomes for individuals may vary significantly from those projected. Control over the management of the pension fund by individual employees can vary. In some cases, the individual cedes all day-to-day management to a fund manager. In other models the individual can exercise choice between different types of funds and can switch resources between them.

14.4.3 In a defined contribution scheme, each individual has his or her own separate investment account which must be used to provide benefits for him- or her-self. There are no cross subsidies between individual members, as in defined benefit schemes, depending on the timing and contingency on which various benefits arise.

14.4.4 One of the most significant variables affecting the benefit outcome under a defined contribution scheme is the investment return achieved. This is reflected in the fact that at the end of a typical career of 30-40 years, as much as two-thirds of the member's final retirement account could be made up of accumulated investment returns with just one-third made up of total

[183] In our deliberations, we had regard to the following report: Commission on Public Service Pensions, "Review of Alternative Structures" (July 1998), Report prepared by Mercer Ltd.

contributions paid. Management of investment risks, therefore, and who bears the investment risk, are issues of major importance. A key point to emphasise is that a switch from defined benefit to defined contribution pension provision involves the transfer of investment risks from the employer to the member. Among the risks transferred are:

- **market risk**: members will generally appreciate the risk to their retirement benefits on retiring immediately following a stock market crash such as *Black Monday* when world stock markets fell by 22% in October 1987;
- **timing risk:** the volatility of stock markets means that what falls quickly has also a habit of making a sharp (and usually unexpected) recovery. The performance of the Irish stock market during 1975 (+86%), 1983 (+85%) and more recently, 1993 (+58%) testifies to this. Perhaps the greatest risk is being out of the market during these recovery periods. The performance of the US equity markets over the 25 years (or 300 months) ended 1994 illustrate this point with the average return over this period being 11% per annum. If the best 10 months are excluded (i.e. just 3% of the period) the return is reduced to 6% per annum — the return falls to 3% per annum if the 20 best performing months are excluded;
- **price inflation risk:** investing retirement savings in a vehicle with similar characteristics to a post office savings account has an intuitive appeal to conservative investors. However, studies show that over time cash deposits generally grow at a rate which just about keeps pace with price inflation (and probably falls short of real wage growth). Conversely, the long-term performance of international stock markets has been around 5-6% per annum in excess of corresponding price increases;
- **manager risk:** the particular investment manager chosen may significantly under-perform relative to his peers. In extreme circumstances, such as a manager trading fraudulently, the assets may be at risk.

14.4.5 In a defined contribution scheme, the risk/reward profile of investment options available to the individual is important. The appropriate risk/reward profile will vary over an individual's career. Very young employees may be able to tolerate a high degree of risk in pursuit of higher expected returns. Older employees would normally shift to a lower risk combination of fixed interest and cash type investments in order to stabilise their expected benefits in the years immediately prior to retirement. A range of investment options is normally available to members of a defined contribution plan.

14.4.6 Where the proceeds of a defined contribution scheme are taken other than as a lump sum, the issue of converting the accumulated fund into another form of benefit arises. A competitive market exists for providing certain types of conventional pension income streams through the purchase of annuities with life insurance companies. Annuities are sold on the basis of prevailing long-term interest rate conditions (i.e. when interest rates are low, annuities are relatively expensive but become cheaper in a high interest rate environment), the life expectancy of the annuitant and to a lesser extent the level of expenses being charged by the insurer. As long-term interest rates are currently at historically low levels, annuity rates are less attractive than in the past.

14.4.7 The impact on annuities of a change in interest rates was illustrated in 1993 when the latter fell from 9.6% (1 January) to 6.8% (31 December). During this twelve month period, the price of buying a pension increased by one-third. In such a situation, it is not possible to defer the purchase of an annuity until rates improve or to provide retirement income by some other means.

Consequently, in addition to the investment risks outlined above, individuals in a defined contribution scheme are also exposed to an **annuity pricing risk** at retirement.

14.4.8 Our discussion of investment and annuity risk clearly highlights that the **information needs** are very different for employees under a defined contribution compared with a defined benefit scheme. Employees will need to understand how much net income they are likely to need in today's terms and at what age they expect (or would like) to retire. They should also be aware of the inherent risks of a defined contribution scheme in delivering on these expectations. Thus,

- having identified a desired retirement age and income, the member needs to know what level of funding, given sensible assumptions about price inflation and investment returns, should be made;
- although every scheme will have a different choice of investment funds available, ranging from a fund chosen by the trustees to allowing members make their own selection from funds available from the provider, members need to understand which funds are appropriate given their age and attitude to risk, and to direct their contributions appropriately;
- because of the extensive range of annuities on offer, the importance of determining how to apply the retirement fund should be understood. Account needs to be taken of a range of factors including financial, marital, medical, and lifestyle.

14.4.9 It is often argued that the move from defined benefit to defined contribution schemes is driven by the wish of employers to reduce contribution rates. The Pensions Board report, *Securing Retirement Income,* indicates that, typically, total contribution rates in defined benefit schemes equate to about 11-12% of salary, with the employee meeting about a third of the cost. By contrast, in defined contribution schemes, average contribution levels run at 9-10% of salary divided evenly between employer and employee.[184] Commenting on a similar disparity in UK defined benefit and defined contribution scheme contribution rates, *Occupational Pensions* magazine commented:

> *A higher funding rate does not necessarily lead to higher benefits, and there are a number of reasons why the difference may be overstated, but nonetheless it is clear that, on average, members of final-salary schemes can expect to be better off in retirement than members of money-purchase schemes.*[185]

Of course, assuming contribution rates are sufficient, there is no reason why a defined contribution scheme could not produce equivalent pension benefits as a defined benefit scheme (particularly where the individual has joined the scheme at a young age).

14.4.10 The main **arguments which can be made in favour of adopting a defined contribution scheme** structure for the public service are as follows:

(i) defined contribution would allow greater flexibility to public servants to tailor their retirement package to their own circumstances. For instance, an individual could decide to increase his or her level of contributions or pay a lump sum into the fund, subject to Revenue rules, to meet changing needs. This would address the demand for scheme flexibility which we discuss in Chapter 12;

(ii) a defined contribution scheme would deal with variable earnings, pensions for part-time employees, temporary contract work, etc. This would be a particularly important

[184] The Pensions Board, *Securing Retirement Income* (May 1998), p. 49.
[185] *Occupational Pensions*, "Focus: NAPF Survey", May 1997, p. 4.

advantage if such features were to become an integral part of public service employment in the future;

(iii) it would enable public servants to make contributions towards additional benefits at retirement on the basis of earnings which would not be pensionable under existing arrangements, e.g. overtime;

(iv) it would be better equipped to deal with the case of individuals who would like to reduce their working time commitment prior to retirement;

(v) it would give individuals the potential to benefit from the upside of the investment market by providing them with a range of funds in which to invest their money;

(vi) as discussed in Section 12.2, defined contribution scheme benefits are perceived to be more portable than defined benefit scheme benefits, and in an increasingly mobile work environment this would be seen as a major attraction;

(vii) a defined contribution scheme would be a more equitable arrangement for the public service than existing schemes, as it would reflect more accurately income earned during the course of each person's whole career, not just salary at retirement (which favours those having favourable promotion progression). In addition, defined contribution schemes tend to deliver a relatively higher benefit to those who experience a lower level of salary progression over their career;

(viii) a defined contribution scheme would provide a clearer picture of year by year costs thereby making budgeting easier for employers — as shown in Chapters 5 and 6, this is a major weakness in existing arrangements;

(ix) transparency of defined contribution schemes and their closeness to other everyday financial transactions would mean that communication with scheme members should be relatively straightforward.

14.4.11 The **arguments which might be made against a defined contribution pension structure** for the public service include:

(i) employees rather than employers would be required to bear the investment and annuity risks associated with defined contribution schemes. As discussed above, these risks can be substantial;

(ii) for any individual, the amount of future benefits would be difficult to quantify. On a broader level, there would be a concern that the contributions made would not be sufficient to provide the same level of benefits as under the existing structure;

(iii) in many cases, particularly for those retiring early and who experience high salary progression, benefits would not be comparable with existing arrangements. The final salary principle of the defined benefit scheme acts as a greater incentive to earn promotion than a defined contribution scheme;

(iv) a period of sustained high price inflation could reduce significantly the real value of the pension after retirement;

(v) the costs of administering a defined contribution scheme would be high;

(vi) the issue of an Exchequer *bail-out* could arise if a defined contribution plan under-delivered on expectations. A possible example of this would be a major fall in stockmarket values leading to a much reduced fund and consequently a lower pension entitlement.

14.4.12 The transition from a defined benefit to a defined contribution system could be very costly. During the period of transition, the State would have to bear a dual burden of paying pensions and of contributing to the defined contribution fund for existing and new employees.

14.5 Hybrid scheme

14.5.1 The Commission also considered the development of a pension scheme design based on a hybrid defined benefit/defined contribution approach, and obtained advice from pension consultants in this regard.[186]

14.5.2 The specific hybrid scheme examined had at its core a defined benefit component (defined benefit plan). This would provide pension benefits in respect of basic salary for full-time permanent employees on the basis that a defined benefit approach would be inherently best suited as a mechanism for pensioning stable income in a typical employment situation.

14.5.3 The defined contribution component of the hybrid scheme (defined contribution plan) would take the form of a retirement savings account. The accumulated value of this account could be used to top up core benefits and to fund non-core benefits, such as, for example, the retirement lump sum. It might also be the sole means of providing benefits in respect of:

- pensionable allowances for those in full time employment; and
- all earnings for those in atypical employment.

14.5.4 In line with our requirements as set out in Paragraph 14.3.2, the hybrid scheme model developed below was intended to be cost neutral (as measured in relation to new entrant rates).

Structure of hybrid scheme — established civil servant new entrant

14.5.5 A logical starting point in designing the defined benefit plan was the existing public service benefit structure. However, this had to be reduced to a core level so that meaningful *savings* were released which could be redirected to the defined contribution plan.

14.5.6 The **defined benefit plan** would be as follows:

- pension of 1/80th of basic salary (excluding pensionable allowances) less twice the Social Insurance Old Age (Contributory) Pension for each year of service;
- no supplementary occupational pension to cover the period between retirement age and age 65 when Social Insurance pension becomes payable;
- pensions would be increased in line with price inflation (instead of public service pay);
- a small number of other modifications to existing terms would apply (e.g. improved death gratuity).

14.5.7 The **defined contribution plan** would involve the following:

- the *savings* achieved through the net reduction in the value of benefits under the defined benefit plan would reduce the new entrant rate of 16% for an established civil servant (see Paragraph 6.6.2) by about 5% of basic salary. This saving would be redirected to the defined contribution plan. The contribution rate in respect of shift pay and other pensionable allowances would be about 16% (the total new entrant contribution rate)

[186] Commission on Public Service Pensions, "Review of Alternative Structures" (July 1998), Report prepared by Mercer Ltd.

of those earnings. Similarly, this rate would also be applied in respect of all earnings for those in atypical employments. The contributions paid to the defined contribution component would be invested and accumulated on a retirement savings account basis;

- the accumulated value of the defined contribution plan would be available at retirement to secure benefits additional to those provided under the defined benefit plan. In the first place it would be likely that, subject to Revenue limits, most or all of the defined contribution fund would be taken in the form of a tax-free lump sum benefit (no retirement gratuity would be provided under the defined benefit plan). Other possible uses of the defined contribution fund would include:
  - replacement of the supplementary pension;
  - use as a financing vehicle for increasing core pension entitlements;
  - provision of a higher level of pension increases, perhaps up to pay parity; and
  - purchasing additional death-in-service and ill health cover;
- the defined contribution plan could also be seen as providing an efficient mechanism for replacing and rationalising the many public service additional voluntary contribution schemes (see Chapter 12). It would also bring a greater element of comparability with private sector arrangements and provide a vehicle for accepting transfer values from mid-career entrants;
- it was assumed that the existing level of employee contributions for all categories would remain at present levels, and that part of the employee contribution would be diverted for inclusion in the contribution to the defined contribution plan.

Hybrid scheme modelling — benefit values and amounts

14.5.8 The key part of the development of the hybrid scheme was to project the likely outcome for individual employees relative to the status quo. To provide a meaningful comparison with the existing system it was necessary to model the overall present value of benefits emerging. This made a like-for-like comparison of different benefit structures and types possible.

14.5.9 For the purposes of placing a value on the various pension benefits, the actuarial assumptions underlying the actuarial review of public service pensions were adopted (see Section 6.2). However, in order to illustrate the potential variation in the benefit outcome under the defined contribution plan component, the modelling included the effect of investment returns being either 1% per annum higher or lower than the expected long-term rate assumed in the core projections.

14.5.10 The modelling exercise was carried out in respect of a 22 year old established civil servant new entrant. It indicated that the capital value of total benefits provided under the hybrid scheme, on best estimate basis, equated with the status quo at almost exactly age 64. At ages below this point, the hybrid scheme produced a less favourable benefit outcome. This arose principally because under the status quo there is an inherent pooling of experience so, in effect, extra *costs* which arise in respect of early retirees are offset by corresponding *savings* from those who choose to retire at or near the normal retirement age of 65. The potential for this type of cross-subsidisation is more limited under the hybrid scheme.

14.5.11 This effect was compounded by the introduction of some minor improvements into the defined benefit plan and higher leaving service benefits which would inevitably arise under the defined contribution plan. The effect of these factors was to defer crossover point by just over a year.

14.5.12 The effect on the modelling exercise of annual investment returns being 1% higher improved the position of the hybrid scheme *vis-à-vis* the status quo by pushing forward the age at which the value of total benefits in both schemes equated to between 61 and 62 (on best estimate basis), with the hybrid scheme being better thereafter. However, where annual investment returns were 1% lower, the value of total benefits was always less than those available under the status quo.

14.5.13 Under current legislation, the Revenue Commissioners set a maximum limit on the pension lump sum that may be taken by an individual based on age, service and final remuneration. In all circumstances, this limit would be equal to or greater than the corresponding status quo gratuity amount and it is assumed that members would wish to avail of this.

14.5.14 The balance, if any, of the defined contribution fund would have to be converted into some form of pension income subject to Revenue limits (see Appendix 12.1). It might be used to:

- augment the member's core pension up to Revenue limits;
- augment the spouse's pension;
- provide a supplementary pension where retirement is before age 65;
- provide for pension increases up to a pay parity level.

This would give retiring employees considerable flexibility. On the other hand, it should be remembered that individuals retiring before the *crossover point* (see Paragraph 14.5.10) could not expect to be able to *buy back* fully the status quo level of benefits.

Catering for individual circumstances under the hybrid plan

14.5.15 The above projections were done for a *typical* new entrant. The following considers the cases of older new entrants and public servants with different career progressions to the norm.

14.5.16 The hybrid scheme would tend to under-deliver for older new entrants because the 5% contribution rate, although appropriate to a 22 year old new entrant, would not be sufficient. A scale of contribution which increases as an employee gets older was investigated as a means of resolving this difficulty. However, for a scale related to attained age to be effective it would have to be very steep indeed with very low percentage contributions at the younger ages. The Commission considered that this would not be practical.

14.5.17 For the gap for late entrants to be closed, it would be necessary to adopt a contribution structure which depended on the age at which the employee joined the public service. For instance, at age 35, an 8.5% contribution rate would be required if a similar outcome to the typical entrant aged 22 were to be achieved in terms of total benefits.

Career/salary progression

14.5.18 The replacement income level at retirement under the defined contribution plan would be substantially affected by an individual's salary progression over his or her career. Under the cost neutral model assumed, a salary scale is incorporated which anticipates the new entrant on a scale of £10,000 receiving civil service type promotional increases over his or her career.

14.5.19 Should an individual's pattern of promotional increases exceed the scale assumed, relative benefits would be lower. Conversely, benefits would be higher should an individual experience a flatter career path. Table 14.1 compares the value of hybrid scheme benefits to the value of the status quo benefits for a 22 year old new entrant receiving, respectively, 50%, 100% and 150% of the assumed pattern of promotional salary increases.

Table 14.1: Value of hybrid scheme benefits as a percentage of status quo

Retirement age	Percentage of promotional salary scale		
	50%	100%	150%
63	99	96	94
64	104	99	96
65	110	103	99

14.5.20 The above table highlights the tendency for the defined contribution plan to deliver a relatively higher benefit to those who experience a lower level of salary progression over their career. The true extent to which the defined contribution plan favours those with relatively lower promotional salary progression, however, is partly masked by the interaction of integration of State Social Insurance benefits with the assumptions underlying the projections.

14.5.21 Because of its defined contribution component, the hybrid scheme would share many of the advantages and disadvantages of a fully defined contribution scheme (see above). Specifically, the **arguments in favour of implementing a hybrid scheme** for the public service might include:

(i) the significant defined benefit element within the scheme means that it would provide considerably more security than a purely defined contribution scheme;

(ii) the hybrid scheme would offer the strengths of defined contribution — in relation to pension flexibility, equity of outcome, participation in investment markets, etc. — but with much less risk to the individual public servant;

(iii) it would be sufficiently adaptable to deal with a variety of different employment patterns (e.g. part-time employment) and remuneration types (including variable pay);

(iv) the introduction of a funded defined contribution component would have the effect of part-funding public service pensions (similar to the introduction of the Thrift Savings Plan for US federal employees — see Paragraph 9.6.9);

(v) by giving public servants direct ownership and an ongoing interest in part of their pensions package, the hybrid scheme would help to reinforce in a transparent way both the cost and value of public service pensions.

14.5.22 The **arguments which might be made against introducing a hybrid scheme pensions structure** for the public service include the following:

(i) compared with the status quo, the hybrid scheme would not deliver comparable retirement benefits for public servants who retire early. Should investment returns be less than those assumed in the modelling outlined above, then the hybrid scheme would fare even more poorly than the status quo;

(ii) the scheme would be subject to the downside of investment markets;

(iii) to cater for variation in age of entry and career progression, it would be necessary to have different contribution rates under the defined contribution element. However, in reality, a hybrid scheme structure would be incapable of delivering the same benefits as the existing structure in respect of all public servants;

(iv) the administration of the defined contribution component of the scheme and its communication to members would be very complex;

(v) there could be an exposure to mis-selling claims or an Exchequer *bail-out* if the defined contribution component under-delivered on expectations;

(vi) there would be concern from an equality perspective of applying the defined contribution component only to part-time public servants while both the defined benefit and defined contribution components would be applied to all other public servants.

14.6 Career average earnings

14.6.1 Under the existing defined benefit structure, benefits are calculated by reference to salary at the point of retirement, death, or leaving service. Thus, the present practice is fundamentally different from a career average system whereby the benefit calculation would depend on the average salary earned over an employee's career. In other words, subject to adjustment by reference to an appropriate index up to the point of retirement, the salary level at recruitment would have as much influence on the calculation of retirement pension as would the retiring salary.

Structure of career average earnings scheme

14.6.2 A career average structure would have a benefit framework similar to the existing system, but with some modifications. For the purposes of determining the career average scheme salary (and integrated salary) consideration would have to be given to the following alternative methods of revaluing each year's salary from the year in which it was earned up to retirement (or earlier death or leaving service):

- in line with price inflation; or
- in line with public service pay.

14.6.3 In applying either of the above revaluation methods, the following points are relevant:

- even if pay indexation were adopted, career average scheme salaries would invariably be lower than final salaries because existing arrangements envisage an increasing pattern of pensionable remuneration due to promotional increments, particularly for established civil servants;
- if revaluation were by reference to price inflation, career average scheme salaries would be much lower again as it is assumed that price inflation is 1.5% per annum less than general salary increases.

14.6.4 New entrant rates for the proposed career average scheme approach were calculated and compared with the new entrant rates of the existing scheme, based on the actuarial valuation. As outlined in the preceding paragraph, two alternative revaluation approaches were considered — in line with price inflation and in line with public service pay. Under the latter approach it was assumed that pensions in payment would also be subject to pay parity indexation.

14.6.5 On this basis, the male new entrant rates were deduced as follows:

Table 14.2: Male new entrant rates under a career averaging scheme

	Established civil servant (%)	Local authority non-officer (%)
Existing new entrant rate	16.3	8.5
Career average new entrant rate: uprating in line with:		
(a) CPI inflation (b) Public service wage inflation	9.7 11.7	6.5 8.0

14.6.6 As would be expected, the career average scheme results in far lower benefits than under the current structure, with a consequent impact on the new entrant rates.

14.6.7 Cost neutrality could be achieved in a number of ways including:

- an uplift in accrual rate;
- the inclusion of (currently) non-pensioned income;
- a reduction in employee contributions.

14.6.8 In brief, the **arguments in favour of a career average scheme** include:

(i) this type of scheme would allow variable pay to be included in pension in a more suitable way than under a defined benefit scheme;

(ii) it would avoid the problem created by career progression.

14.6.9 **Arguments against a career average scheme** include:

(i) it would be unfavourable to those who experience rapid salary progression relative to existing terms, and this might be a disincentive to performance and achievement;

(ii) the administration and communication of the scheme would be very complex;

(iii) further complexities would be required to achieve broad cost neutrality, especially for transfers from existing staff, new entrants, etc.

14.7 Discussion of existing and alternative structures

14.7.1 In our view, the basic requirements of any new pension scheme structure for the public service are that it provide: (i) a broadly similar level of benefits as under the existing structure, (ii) appropriate flexibility, and (iii) a means of managing and containing the growth of the long-term cost of public service pensions. In addition, the pension scheme should meet the criteria which we identified in Chapter 13 in relation to adequacy, viability, flexibility, fairness, and cost.

14.7.2 The pension scheme structure currently applying in the public service, **defined benefit** (final salary), is the most appropriate structure for employment on a permanent basis where salary is not subject to wide variation through service and increases steadily over the course of the person's career.

14.7.3 While public service pension schemes have shown themselves capable of adapting to meet changing circumstances, it might be argued that the extent of reforms in the nature of public service employment and remuneration currently being implemented and which can be expected in the future will go beyond the ability of the present system to accommodate them. We have shown in Chapter 7 that changes are occurring in relation to age of entry, breaks in service, levels of atypical employment and the management of performance. Variability in earnings is also a growing feature – and may grow further with the possible introduction of performance-related pay. In addition, a much greater level of interest is being expressed by individual public servants in relation to retirement and pension benefits. There is a demand for much greater choice and flexibility in relation to such issues as early retirement, pensions for partners, etc.

14.7.4 For the employer, the defined benefit model financed on a pay-as-you-go basis offers little transparency in pension costs, although this difficulty could be addressed through the introduction of accrual accounting for pension costs.

14.7.5 The need for improved pension scheme flexibility could be met through a move to a **defined contribution structure**. This would be in line with the trend in the private sector. From the employee's point of view, defined contribution schemes are perceived as flexible and portable – two important features of today's labour market. They are particularly suited to the situation of mobile employees. To avoid any diminution of pension outcome, it would be necessary to ensure that employer contribution rates were kept at a level sufficient to guarantee benefits comparable to the existing scheme.

14.7.6 In a public service context, a major difficulty arises in relation to comparability of benefits and the question of risk. In a defined contribution scheme, the level of benefits would depend crucially, not just on age of entry, the degree of salary progression, and contribution rates, but also on investment return and annuity rates at retirement. Thus, two people retiring on the same final salary having the same total service, could have very different pensions under a defined contribution scheme. Under existing arrangements, they would both receive the same rate of pension.

14.7.7 The administration and communication costs associated with a defined contribution scheme would be substantial. These would occur all during service, as public servants would seek to maximise their investment position at lowest risk consistent with their personal situation. A second set of communication issues would arise at point of retirement, as the individual would have to choose what type of annuity to purchase (flat, with guaranteed increases, with spouses' pension, etc.) and to find the best available rates.

14.7.8 One of the main advantages of a defined contribution scheme would be its flexibility. A second is that it would make pension costs more transparent: the practical effect of introducing a funded defined contribution scheme for the public service would be to move to full funding.

14.7.9 The **hybrid scheme** offers a third way between a fully defined benefit and a fully defined contribution solution. The bulk of the pension benefit would continue to be provided on a defined benefit basis, which might be considered consistent with the needs of the public service employment model as it currently stands. The balance would be provided on a defined contribution basis, offering a degree of member choice in relation to a component of the benefit. The defined contribution element would allow for additional member contributions to cover non-pensionable earnings and to help finance part of the cost of retiring early.

14.7.10 For the employer, the introduction of a defined contribution element and reducing pay-as-you-go defined benefit pensions accordingly, would help to partially fund pension provision.

14.7.11 However, many of the disadvantages of a full defined contribution scheme would apply. For example, different investment returns, annuity rates and salary and career progression would give rise to major variations in benefits. Different contribution rates would also be required for different public service groups to ensure that benefits were broadly consistent with present arrangements and to cater for late entrants. Furthermore, there would be major communication and administrative complexities.

14.7.12 An important requirement of any new structure relates to its impact on the expected peak in future pension costs. Under the hybrid structure, the funding requirement of the defined contribution element for new entrants would result in an increase in expenditure over the next 30 to 40 years. There would be little likelihood of current employees transferring to the new structure thereby accelerating cashflows (in effect bringing forward some of the peak in costs). Thus, in overall terms, the hybrid structure would exacerbate the peak in expenditure.

14.7.13 A further pension structure considered above is **(defined benefit) career average earnings**. A defined contribution system — leaving aside the use of individual accounts, etc. — is a form of career averaging, as contributions paid are related to income at the time. This system would be more equitable than the existing final salary system.

14.7.14 A career average earnings defined benefit arrangement would represent a diminution in pension terms which, ultimately, would lead to a reduction in pension expenditure.

14.8 Conclusions

14.8.1 The existing model of public service employment involves permanent employment and steady salary and career progression through service. There may be developments in the model by virtue of changes which might be expected in pay determination systems in the public service in the future. In addition, there may be greater variety in future work patterns and greater mobility between the public and private sector. Nonetheless, as we have stated at Paragraph 12.16.3, the Commission believes that the majority of public servants will continue to be employed under the traditional framework in the medium- to long-term.

14.8.2 Pension scheme structure should form an integrated component within the overall employment model. Hence, we consider that it is appropriate to recommend retention of the existing pensions structure, but subject to a range of reforms which would make it better capable of adapting to changing circumstances and of delivering the flexibilities required by public servants. Also, as discussed in Chapters 4 and 5, we believe that reforms are necessary to ensure greater openness and transparency in public service pensions, both in terms of the management of pension costs, and in the communication of benefit terms and choices to employees.

14.8.3 In our view, the particular issues which should be considered in the context of a new public service pensions framework include:

- **greater flexibility in working arrangements** — it is clear that there is a strong demand on behalf of employers, for operational reasons, and employees, for reasons of individual choice and preference, for the introduction of more flexible forms of working, whether part-time (with varying levels of hours), work-sharing, temporary and seasonal working, or fixed term contract. The pension scheme should be capable of adapting to these requirements, rather than being seen as an obstacle to change;

- **performance pay** — it is not clear at this stage to what degree performance pay may be introduced, but some recent agreements reached with public service unions allow temporary payments in recognition of exceptional performance. The implementation of any significant scheme of performance-related pay might have implications for the existing pension structure, which focuses almost exclusively on the final remuneration earned by the individual at retirement;
- **breaks in service** — with full implementation of work-sharing, career breaks, and term time, greater numbers of employees will find that they will not be in a position to achieve 40 years' service to qualify for maximum pension;
- **reducing work commitments prior to retirement** — as noted above, the defined benefit final salary system is resistant to the situation of those who would like to reduce their work commitments coming up to retirement, whether by reducing the working of unsocial hours, reverting to a lower grade, or deciding to work part-time;
- **demand for flexibility in pension arrangements and the age of retirement** — many public servants are seeking greater choice and flexibility in relation to the age at which they would like to retire, possibilities for improving their pension, and adaptation of the pension package to suit their particular lifestyle.

14.8.4 Possible modifications to address some of the deficiencies of the existing defined benefit structure which we have identified might include the following:

- amendment of pension calculation in the case of low-paid and part-time employees;
- introduction of facilities to cater for the case of individuals who wish to reduce their working time commitment prior to retirement;
- provision of greater flexibility to public servants to allow them contribute towards early retirement, enhancement of pension benefits, etc.;
- introduction of early retirement provisions to allow individuals to retire earlier than normal retirement age at full cost to themselves, or, in certain limited cases, with enhanced pension provision;
- improved communication of benefit entitlements and options to public servants;
- greater transparency in the communication of the cost of public service pensions and the value to the individual public servant.

The reforms recommended by the Commission are set out in Part VI of the Report.

14.8.5 In the particular case of small or temporary organisations, where it might be deemed appropriate, the Commission considers that there should be an option to consider the introduction of funded defined contribution type schemes on a basis that was mutually acceptable to the organisations concerned and to the relevant public service unions. We address this matter further in Paragraph 22.9.46.

14.8.6 Pension structures should not be fixed, but should be capable of change. If changes in the employment framework for the public service turn out to be radically different from those anticipated, or should cost and other pressures faced by pension schemes increase dramatically, then it may be found necessary at some future date to replace the defined benefit structure with a more flexible and transparent defined contribution (or hybrid) pension scheme. The Commission believes that the analysis has been carried out to implement such a scheme alteration were it to be considered necessary.

PART VI

Commission Recommendations

CHAPTER 15

Retirement Age and Early Retirement

15.1 Introduction

15.1.1 We conclude in Part V of the Report that it is appropriate to recommend retention of the existing public service pensions structure, subject to a number of reforms. In Part VI, we present our recommendations in relation to public service pension terms, the funding of pensions, accounting for pension costs and pensions management and administration systems. We set out our deliberations and recommendations on retirement age and early retirement in this Chapter.

15.1.2 We were required by our terms of reference to have particular regard to claims for early retirement. It is clear that there has been an increasing demand for early retirement facilities across the public service and amongst certain groups in particular. For many, a desire for early retirement has merged over time with claims for enhanced pension terms which apply to a number of groups for operational reasons. In some cases, early retirement is sought as an option within the pension scheme, one that might not actually be taken up. We reached the view in our Interim Report that it was not immediately clear that the demand for early retirement (i.e. with no actuarial reduction of pension to cater for the longer period over which it will be paid) was sustainable on grounds of cost, operational requirements, practice in the private sector, increased longevity, and trends in public service retirement arrangements abroad.

15.1.3 The purpose of this Chapter is to examine and make recommendations on the normal retirement age for public servants, voluntary early retirement, and the special retirement provisions applicable to certain groups for operational reasons. We also address a number of related matters, including flexibility in working arrangements and phased retirement.

15.1.4 The determination of what is a reasonable and fair retirement age is a complex and difficult task. There are many conflicting interests at stake. The diversity of employment within the public service — with a range of different operational requirements — means that it is not possible to apply a uniform approach to retirement age. Employees and employers have different perspectives based on their own needs and experience and these can change significantly over time. For example, existing retirement ages were generally established at a time when both life expectancy and the work environment were very different to what they are today. Accordingly, some employers would argue that special terms are no longer appropriate in certain areas due to changes in the nature of a profession, while some employees would contend that their work environment has altered so significantly over time that special terms should be extended to other groups.

15.1.5 In addition to these conflicting interests, the situation is complicated by the fact that working life is undergoing a process of rapid change; this applies to the public service as a whole (as, indeed, to the workforce generally) as well as to the special needs of certain groups.

15.2 Existing retirement and early retirement arrangements

15.2.1 Most public servants are eligible to retire from the age of 60 onwards, provided they have a minimum of five years' service; the latest age of retirement is age 65.[187] Maximum pension benefits are payable based on 40 years' pensionable service. In the case of the civil service, the minimum retirement age and the 40 year requirement for maximum pension date from the 1859 Superannuation Act.

15.2.2 In Chapter 3, we set out the lower retirement ages and enhanced pension benefits (*special terms*) which apply to a number of groups for operational reasons. These are summarised below:

Garda Síochána
Based on 1925 regulations, members of the Force may retire at any age after 50 having completed 30 years' service. Service in excess of 20 years is doubled for pension purposes, subject to a maximum pension based on 30 years' actual, i.e. 40 years' pensionable, service. The latest retirement age is age 57 for all ranks up to and including Inspector.[188] In general, members in the rank of Superintendent or higher are subject to a maximum retirement age of 60.

Prison Officers
Under legislation dating from 1919, Prison Officers may retire and receive immediate pension from age 55 onwards provided they have a minimum of five years' service. They have the option to retire with full pension from age 50 onwards once they have completed 30 years' service (this provision dates from 1983). Maximum retirement age is 60. Fast accrual terms apply, i.e. service in excess of 20 years is doubled, subject to a maximum of 30 years' actual, i.e. 40 years' pensionable, service.

Health service personnel registered under the Mental Treatment Act, 1945
Health service personnel in this category, principally Psychiatric Nurses and some doctors, having at least five years' service, may retire and receive immediate pension from age 55 onwards. Fast accrual terms apply, enabling those with 30 years' service to qualify for maximum pension based on 40 years' pensionable service. Maximum retirement age is 65.

Fire service
Most Firefighters are required to retire at age 55 (although some local authorities apply later retirement ages). They qualify for immediate pension provided they have at least five years' service. As above, doubling of service applies for service in excess of 20 years.

Senior Fire Officers may retire on immediate pension at any age between age 55 and age 65; doubling of service in excess of 20 years applies.

Defence Forces
Enlisted personnel qualify for immediate gratuity after three years' service, for immediate gratuity and pension after 21 years' service (thus retirement is possible from age 39), and for maximum benefits after 31 years' service. Maximum retirement age is 60.

Commissioned officers qualify for immediate gratuity after five years' service and for immediate pension and gratuity after 12 years' service. Qualifying period for maximum benefits varies by rank and service – Captains and Commandants require 23/24 years' service. Maximum retirement age varies from 54 for a Captain to 63 for a Lieutenant General.

Teachers
National school teachers have similar retirement terms to civil servants with the exception that they may retire with immediate pension from age 55 once they have completed 35 years' service. This facility was recently extended to secondary and vocational teachers. Maximum retirement age for all teachers is 65.

[187] Non-established civil servants are an exception to this general rule; they have a retirement age of 65/66, with no option to retire between ages 60 and 65.
[188] Some Gardaí who were in service in 1983 have the facility to retire after age 50, having 25 years' service.

Non-commercial state-sponsored bodies

Special terms apply to certain full-time board members and equivalents under the schemes of a limited number of non-commercial state-sponsored bodies. Maximum benefits are payable after 24 years' service; lump sum is $1\frac{1}{2}$ times pension as distinct from $1\frac{1}{2}$ times salary. In certain cases, pension may be paid prior to age 60, for example where a member is not reappointed (assuming it is not for reasons of misconduct) and he or she has accrued five years' service. Otherwise, pension is paid from between 60 and 65.

15.2.3 Early retirement is available generally in cases of ill health or, in certain limited circumstances, for management reasons. Enhanced pension benefits are usually payable. Special early retirement provisions were recently introduced on a pilot basis in respect of teachers and nurses.

Ill health early retirement

Public servants may be granted early retirement on grounds of ill health if, subject to medical certification, they become incapable of working in the area assigned. In the calculation of benefits, notional service of up to ten (usually six-and-two-thirds) added years are granted to pensionable service. On death after retirement, spouse's pension (if any) is calculated on the basis of potential service to maximum retirement age.

Early retirement for management reasons

In the civil service, the facility to retire individuals on grounds of efficiency and economy or abolition of office terms is available under the Superannuation and Pensions Act, 1963 and the Superannuation Act, 1909. Pension benefits are paid immediately, and up to ten notional added years are included in pensionable service. A special severance payment of up to one-half of salary may be paid. These terms have been used relatively infrequently.

Top level appointments

Secretaries General of government departments appointed through the Top Level Appointments Committee (TLAC), and other top level public service posts such as County and City Managers, who reach the end of their seven year term before age 60 may, with the agreement of the Government, be allowed the option of early retirement with enhanced superannuation benefits. These consist of an award of up to ten added years and a special severance gratuity of six months' salary on the terms specified in Sections 6 and 7 of the Superannuation and Pensions Act, 1963. These terms are subject to special abatement provisions on subsequent appointment, below age 65, to any public sector position following retirement.

Voluntary early retirement schemes

In 1987/88, a voluntary early retirement (VER) scheme was offered in certain areas of the public service as a means of reducing public service numbers. The scheme included a redundancy added years option which offered public servants under age 60 immediate payment of pension and lump sum and up to seven added years. The terms of the scheme continue to be applied in a small number of instances where public servants are deemed surplus to requirements.

VER schemes have been offered from time to time in other parts of the public service, usually in cases of overstaffing, organisational restructuring, or where there was a need to reduce the age profile of the workforce because of specific operational requirements.

Pilot early retirement initiatives in respect of teachers and nurses

A new limited early retirement scheme was agreed as part of the *PCW* restructuring agreement reached between the Department of Education and Science and the teachers' unions in early 1997. The three strands of the scheme — detailed in Appendix 3.4 — are:

- Strand I which covers the situation of teachers who are consistently experiencing professional difficulties;
- Strand II which addresses the position of teachers who wish to retire and whose retirement would facilitate change;
- Strand III which covers posts which are surplus to requirements.

Special retirement terms, involving the granting of added years in certain circumstances and immediate payment of pension with no actuarial reduction, apply. Strands I and II are subject to an overall quota of 150 retirements per year; Strand III is subject to an overall quota of 250 retirements per year.

Under the *PCW* restructuring agreement reached with nurses in early 1997, two new retirement initiatives were agreed. They comprise:

- a pre-retirement initiative, whereby nurses are allowed job-share at age 55 and retire at age 60 with full pension credit for the period of job-sharing; and
- a limited early retirement initiative (facility to retire from age 55, having at least 35 years' service).

Both initiatives are subject to an annual quota — 200 per year under the pre-retirement initiative, and 600 over a three year period under the limited early retirement initiative, with a maximum of 300 in the first year. Further details are given in Appendix 3.3.

15.3 Retirement (including ill health early retirement) trends and statistics

15.3.1 In Chapter 7, we analyse retirements in the public service over the past number of years. We note that retirement behaviour is not a cohesive and consistent phenomenon across any group of employees or across the public service as a whole. Nonetheless, we arrive at the following conclusions on the basis of the data considered:

- it would appear that across all groups there was a slight fall in both the average age of retirement and in the average period of pensionable service held at retirement;
- on average, the age of retirement and the period of pensionable service held at retirement was lower for women than for men;
- many public servants who were in a position to do so remained in service until the maximum retirement age or until they had sufficient pensionable service to qualify for maximum pension entitlements;
- over the period, there was an increase in the numbers retiring at the earliest permitted age (or before maximum retirement age), perhaps with less than maximum pensionable service;
- many Gardaí remained in employment when the retirement age was increased from 57 to age 60 for the period November 1989 to December 1992. This suggests the possibility that if the maximum retirement age were increased, many would decide to remain in service for longer. However, there is no evidence available on the impact of an increase in the standard maximum retirement age of 65;
- there was a large degree of variation between groups as regards pensionable service at retirement — many civil servants had maximum service of 40 years, but other public service groups, such as nurses and non-established employees, had lower levels of service;
- those retiring from groups with special *fast accrual* terms (e.g. Garda Síochána, Prison Officers) had a much higher possibility of having maximum pensionable service compared with groups with standard terms;
- there were generally higher numbers of retirements on grounds of ill health amongst non-established public servants compared with established public servants.

There is no evidence available to the Commission on which to assess the potential impact on retirement behaviour of new measures suggested in submissions and elsewhere, including pre-retirement flexibility such as *bridge jobs* (see Paragraph 15.10.4), job-sharing, and the working of reduced hours, as well as the impact on retirement age of a choice to continue the accrual of pensionable service beyond 40 years.

15.3.2 According to data made available to the Commission, summarised in Table 15.1, the number of early retirements on grounds of ill health appear quite high in some parts of the public service and is a cause of concern.

Table 15.1: Age and ill health retirements from the public service, 1997

Group	Ill health retirements	Age retirements	Total retirements	Ill health as of total retirements (%)
Established civil servants	37	215	252	15
Non-established civil servants	54	125	179	30
National teachers	67	453	520	13
Secondary teachers	44	150	194	23
Garda Síochána	13	258	271	5
Prison Officers	7	13	20	35
Army officers (1995)	0	35	35	0
Enlisted personnel (1995)	27	137	164	16
Local authority officers (includes VECs)	39	256	295	13
Local authority employees (includes VECs)	127	268	395	32
Health Board officers (includes nurses)	108	423	531	20
Health Board non-officers	142	153	295	48
Voluntary hospitals officers	15	38	53	28
Voluntary hospitals non-officers	13	15	28	46
Nominated health agencies	16	25	41	39
Total	**709**	**2,564**	**3,273**	**22**

Note: Table is based on the data presented in Table 7.3.

15.3.3 The table shows that, measured as a percentage of total retirements from each group, the highest number of ill health early retirements are amongst support staff (i.e. non-officers) in the health service, local authority employees, Firefighters,[189] and non-established employees in the civil service. A further survey by the Commission (see Appendix 7.2, Paragraph 21) indicated that amongst non-officers in a selection of Health Boards and voluntary hospitals, approximately 56% of all retirements during the period 1995-97 were early retirements on ill health grounds.

15.3.4 This survey also showed that the percentage of ill health early retirements amongst nurses was quite high — approximately 37% of overall retirements during the period 1995-97. This compared with the equivalent measure (in 1997) for established civil servants, national teachers and secondary teachers of 15%, 13% and 23%, respectively.

15.3.5 It should be noted that while the figures for ill health retirements for Prison Officers and Firefighters appear high, account must be taken of the low overall number of retirements relative to the size of each group.

[189] Dublin Corporation Firefighter retirement statistics for the period 1995-97 indicate that about 40% of all retirements were on ill health grounds.

15.3.6 The figures indicate that there is substantial variation in numbers of ill health early retirements as between different organisations and employers, even within the one sector of the public service. For example, the numbers of ill health early retirements varied between the individual Health Boards and voluntary hospitals surveyed in the range 38%-67% of total retirements in the case of employees, and 25%-64% of total retirements in the case of nurses. There would appear to be little evidence of particular operational or demographic factors contributing to a higher incidence of ill health early retirements in any one Health Board or voluntary hospital compared with another. Where a similar experience of wide variation in numbers of early retirements on medical grounds was found between local authorities in the UK, it was suggested that this more likely reflected different management practice rather than markedly different incidences of ill health and stress within the workplace.[190]

15.3.7 The figures suggest that there may be a relationship between the incidence of ill health retirement and the availability of an early retirement option. For example, primary teachers who have had a long standing option to retire from age 55 if they have 35 years' service, an option only recently extended to secondary (and VEC) teachers, experience a lower rate of ill health retirement compared with secondary teachers (in 1997, 13% compared with 23% of total retirements). This factor may also be relevant in the comparison of ill health retirements between established civil servants, who have the option to retire from age 60, and non-established civil servants who may retire only at age 65/66 (15% compared with 30% of total retirements in 1997). Of course, the fact that the work of the latter group is generally of a manual nature also contributes to the higher incidence of ill health early retirement amongst that group.[191]

15.3.8 The Commission recognises that the ill health retirement statistics presented above are only a *snapshot* of such retirements in just a single year, and that to analyse them as a percentage of total retirements may not be the most appropriate approach. While they are a useful indicator of the actual and comparative levels of ill health retirement in different parts of the public service, they do not, in isolation, enable definite conclusions to be reached on this matter. Other factors which should be taken into account include:

(i) the differences in the nature of the work — for instance, generally speaking, the work of the groups with higher levels of ill health retirement is more physical in nature;

(ii) the age profile and gender breakdown of the workforce — statistics show that a workforce which has a substantial number of older employees and/or female employees will normally have higher rates of ill health retirement than one which is younger and has a greater number of male employees; and

(iii) whether or not an option to retire early under the pension scheme is generally available.

15.3.9 In analysing trends in retirement and early retirement in the public service, it is interesting to consider the experience of the pilot three strand early retirement scheme which has been in operation for teachers over the past number of years. According to data provided by the Department of Education and Science, the number of teachers who availed of the scheme over the period 1997-99 was as follows:

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[190] Response of Steering Committee on Local Government Pensions to report of Audit Commission, *Retiring Nature — Early Retirement in Local Government* (1997).

[191] It is worth noting that non-established civil servants who retire on ill health grounds between ages 60 and 65 may be eligible for the grant of ill health added years (see Paragraph 15.2.3), while established civil servants in that age category do not qualify for added years (given that they already have the option to retire once they reach 60).

Table 15.2: Teachers' early retirements under pilot initiative, 1997-99

Year	Type of school	Applications	Retirements
1997	Primary	91	57
	Secondary	113	89
	Vocational	46	33
	Total	250	179
1998	Primary	66	45
	Secondary	103	80
	Vocational	26	18
	Total	195	143
1999	Primary	71	39
	Secondary	157	109
	Vocational	18	9
	Total	246	157
1997-99	**Overall total**	**691**	**479**

Notes : (i) The breakdown of retirements between the different strands was as follows:

Strand I	159
Strand II	189
Strand III	131

(ii) Not all applications were accepted, so the number of actual retirements is less than the number of applications made.

15.3.10 The number of teachers availing of early retirement each year averaged about 160, much lower than the annual quota of 400 available for such early retirements (see Paragraph 15.2.3).[192] This may suggest that offering the choice of early retirement does not necessarily lead to a rush amongst public servants to retire early. On the other hand, particular conditions applying to the teachers' scheme — including a centralised process of assessment and approval — make it difficult to draw wider conclusions for the public service as a whole.

15.4 Factors considered in review of retirement age and early retirement

15.4.1 In our consideration of retirement age and early retirement in the public service, we had regard to a number of factors, as follows:

- historical basis for present arrangements;
- staff claims in relation to retirement and early retirement;
- desire for retirement flexibility;
- operational considerations;
- macro-economic and labour market considerations;
- improvements in health and life expectancy;
- cost to pension schemes;
- retirement age in the Social Welfare system;

[192] It could be argued that the Strand III figures should be removed from the comparison as they relate to posts considered surplus to requirements. The average of teacher retirements under Strands I and II, i.e. 116 per annum, represents a much higher proportion of the permitted annual quota of 150 retirements per annum for these strands.

- retirement age in the private sector;
- retirement age in the public service abroad.

We discuss each of these below.

15.5 Historical basis for present arrangements

15.5.1 It is often the case that pension terms date from a different era and that little effort is made to ensure that they are updated in line with present day requirements. This is particularly the case in relation to retirement age.

15.5.2 Pension terms for established civil servants date originally from the eighteenth century and were formalised in legislation in the nineteenth century (see Paragraph 3.3.1). The retirement age of 60 and the 40 year eligibility requirement for maximum pension were fixed in legislation in 1859. The essential structure of the pension scheme was also fixed at that time. The minimum retirement age of 60 was based on an 1857 Commission of Enquiry Report which concluded that at this age productivity often begins to decline due to old age or infirmity.

15.5.3 The Superannuation (Prison Officers) Act, 1919 made a special change to the pension terms of Prison Officers — who are civil servants — to substitute age 55 for age 60 as the minimum age of retirement. It also provided for the doubling of service for years served in excess of 20. The 1919 change was made to take account of the demanding nature of employment in the prison service with its tensions and dangers and the obvious necessity to ensure physical and mental fitness and alertness for the proper discharge of prison duties. A further change was made in 1983 on foot of an arbitration decision to enable Prison Officers having at least 30 years' service to retire at any age after age 50.

15.5.4 The pension terms of local authority personnel date from 1865. From the beginning, the terms were generally in line with civil service terms. The special terms of fire service employees were formally provided for by the Local Government Superannuation Act, 1948; however, these terms had been available for a number of years prior to this.

15.5.5 Teachers' pension terms in this country date from 1879. They were revised in 1918 to provide a scheme based closely on that of the civil service. The current national teachers' scheme was drawn up under 1928 legislation. It incorporated the already longstanding provision enabling national teachers to retire from age 55 once they have achieved 35 years' service (the precise date and circumstances of the original introduction of this provision are not clear). The same provision was introduced for secondary and vocational teachers in 1997 under the *PCW* restructuring agreement.

15.5.6 From the outset, pensions for health service personnel — other than those employed by private hospitals — came under the local authority code, and pension terms have remained broadly consistent with the civil service norm. However, special terms are applicable to those who are registered for the purposes of the Mental Treatment Act, 1945. These terms derived from the 1919 change made to Prison Officer terms (which also applied to warders in criminal lunatic asylums) as well as from legislation dating from 1909, and perhaps earlier. The special terms have, historically, been linked to the *"care or charge of patients"*.

15.5.7 The special pension terms applying to the Defence Forces date from the 1930s and perhaps earlier.

15.5.8 Historically, police officers enjoyed better pension terms than civil servants. In 1877, a committee recommended that there should be an entitlement to a pension after twenty-five years' service when a constable *"had practically given all his best years and energies to the force and was, as a rule, no longer thoroughly efficient"*.[193] The *Ross Commission*, 1920 in respect of the RIC and Dublin Metropolitan Police, adopted for Ireland the recommendation of the *Desborough Commission* that all ranks be entitled after 25 years to retire on a pension of half pensionable pay, and after 30 years to retire on a pension of two-thirds of pensionable pay.

15.5.9 As is clear from the above, most of the basic provisions of retirement age and pension terms have been fixed for some time. Apart from the case of health service personnel registered under the Mental Treatment Act (in respect of whom the Department of Health and Children has signalled a future change in pension terms – see Paragraph 4.1 of Appendix 2.2), there has been little evidence of any move to ensure that special terms remain appropriate having regard to changes in operational requirements and conditions of employment since they were first introduced.

15.6 Staff claims in relation to retirement and early retirement

15.6.1 At the time of the Commission's establishment, early retirement was the subject of claims by a number of public service groups, particularly teachers and nurses. The importance of early retirement for staff interests was confirmed in the submissions received from unions and individual employees, and in the presentations made by those whom the Commission met. A number of different early retirement arrangements were proposed (with particular variations in the case of those groups which already had different retirement provisions to those applying generally in the public service), such as the following:

- introduction of *fast accrual* schemes in which all service in excess of 20 years would count as double, coupled with an earlier minimum retirement age. This scheme would be similar to that applying currently to the Garda Síochána, Prison Officers, etc. Early retirement was sought particularly for personnel in shift-based employment, and/or those who considered themselves to be in hazardous or stressful occupations;
- the right to retire before age 60 where an employee had accrued 40 years' service;
- in the case of those with special terms, the facility to retire below age 50 once 30 years' service had been given (another suggestion made was that retirement with full pension entitlement should be available after 25 years' service);
- introduction of a more flexible approach to retirement so that public servants could retire at any age between 55 and 70, with a pension based on actual service to be paid immediately;
- a form of job-sharing for those approaching retirement. For example, a person aged 56 having 38 years' service might be allowed job-share for four years with pro rata service credit, giving 40 years' pensionable service at age 60.

15.6.2 In support of the case for early retirement, submissions argued that the pace of change in certain areas of the public service – particularly with the introduction of new technology – and the increasing demands placed upon the public service means that many employees are finding it more difficult to cope; the converse, however, is that other employees thrive in this more

[193] Rhodes, G., *Public Sector Pensions,* George Allen & Unwin Ltd. (London), 1965, p. 60.

dynamic environment, and find a retirement age of 65 restrictive. Accordingly, it was suggested that a more flexible approach to retirement was necessary.

15.6.3 It was not in the interest of the service, submissions argued, to require public servants who were approaching the end of the traditional working life span to carry out the full range of duties expected. It was necessary to consider the impact of stress and burnout amongst public service employees.

15.6.4 It was pointed out that in some parts of the public service, employees with special terms were working side by side with colleagues with standard terms.

15.7 Desire for retirement flexibility

15.7.1 On the basis of submissions received, it would appear that there is much greater demand than before amongst individual employees for improved retirement choice.

15.7.2 In Chapter 12, we note that there is a high level of take-up of additional voluntary contribution (AVC) schemes amongst nurses and teachers, two groups for whom this information is available. The take-up of AVCs may reinforce the view that there is a strong employee interest in early retirement. However, it also indicates that many public servants are attracted by the option of paying towards the cost of retirement choice.

15.7.3 Unlike the private sector, public service schemes make no provision to enable individuals to retire early at full cost to themselves. In effect, the vast majority of public servants who have standard pension terms have no possibility of retiring earlier than age 60 (other than on grounds of ill health). While the introduction of cost-neutral early retirement might not prove attractive to all public servants, its availability might be welcomed by a significant number.

15.7.4 Based on the evidence of submissions, some public servants might be interested in downscaling their work commitments or working a lesser number of hours in the period prior to retirement (i.e. phased early retirement), provided their pension benefits were not unduly affected as a result. Others who work unsocial hours might prefer to work fewer additional hours prior to retirement, without unduly affecting their pension entitlements.

15.7.5 In addition, the Civil Service Inter-Departmental Committee on Work Sharing requested the Commission to examine the pension implications of a proposal for job-sharing for those over age 55 having a minimum of 30 years' service.[194]

15.7.6 On the other hand, many public servants might not be so keen to reduce their work commitments because of the consequent drop in income or simply because they enjoy their work. The experience in the Garda Síochána when retirement age was increased (see Paragraph 15.3.1) might suggest that some public servants would decide to remain in service for longer if that option were available to them.

15.7.7 These points would suggest that greater work flexibility, more widely available choice, and increased flexibility within the pension system might go a long way to addressing staff needs in this area.

[194] Department of Enterprise and Employment, "Report of Inter-Departmental Committee on Work Sharing in the Public Service" (July 1996), p. 58.

15.8 Operational considerationsî

15.8.1 Public service employers require their employees to be capable of working effectively up until the minimum age of retirement. For public servants who are experiencing serious, medically-related difficulties in their work, early retirement is available on grounds of ill health. If the minimum age of retirement is too high, this will become evident in increasing numbers of ill health retirements, high absenteeism, sick-leave, etc., as well as demands to introduce lower retirement ages.

15.8.2 The high numbers of ill health early retirements indicated in Section 15.3 are a matter of concern. Differences in the incidence of ill health early retirement between the different groups may, as noted in Paragraph 15.3.8, be attributable to the physical nature of the work being undertaken, the age profile and gender breakdown of the workforces in question, and whether or not an option to retire early exists under the pension scheme. However, the wider variation in the incidence of early retirement between different public service organisations raises questions about management practice in this area.

15.8.3 The experience in Ireland and abroad is that stress and burnout are becoming increasingly important factors in the workplace, as well as contributing to higher numbers of medically-related early retirements. Much of the research in the area of occupational health focuses upon the management of stress within the work environment. In the context of the public service, measures such as the introduction and promulgation of occupational health services and a more active approach to redeployment might be considered as a means of addressing the high numbers of ill health early retirement which currently exist in certain areas.

15.9 Macro-economic and labour market considerations

15.9.1 As noted in Section 7.4, the average age of retirement has been falling in many western countries. Similar trends have been experienced in Ireland. In the past, there may have been an underlying consensus to early retirement, involving employers (who preferred younger workers), unions (who saw early retirement as a valuable perk), and governments (who were attempting to combat youth unemployment).

15.9.2 However, in response to the changing demographic balance in Europe and the growing realisation of the long-term costs of such early retirement initiatives, the focus now is shifting to one of improving the individual's lifetime contribution to national production. Ways are being explored of encouraging people to delay rather than bring forward the age of retirement. In some countries the approach has been to increase minimum retirement ages. Another approach has been to encourage moves towards different types of employment (e.g. part-time or contract working, in the same or different occupation) as an alternative to complete withdrawal from the workforce.

15.9.3 In a competitive labour market, public service employers may need to consider measures – such as increasing retirement age, perhaps in conjunction with actuarially enhanced pension entitlements – in order to retain employees having the necessary training, skills and expertise.

15.10 Improvements in health and life expectancy

15.10.1 In Paragraph 7.4.4, we detail the improvements which have occurred in life expectancy since public service pension schemes were introduced in the middle of the nineteenth century.

In 1845, life expectancy for a person aged 65 was 10.9 years for a male and 11.5 years for a female. The actuarial review of public service pensions assumes life expectancy at age 65 of 16.5 years for a male and 20.3 years for a female. This represents an increase of 56% and 77%, respectively. It has been suggested that current projections for increases in life expectancy in Ireland may prove conservative (see Paragraph 7.4.6).

15.10.2 Combined with better health and educational resources, the increase in life expectancy would suggest, at least in theory, that people should be able to work effectively for a longer period of time. However, the trend in Ireland and internationally (although perhaps not uniformly across all countries) has been that increasing life expectancy has resulted in a greater emphasis than before on an improvement in the duration and quality of the period of retirement (i.e. not in formal employment).

15.10.3 The OECD has suggested that the potential gains both to individuals and society of a more active life by older people in society is not being fully realised. That organisation proposes more flexible work-retirement transitions as a means of breaking down the formal division between work and retirement.[195]

15.10.4 One way of achieving this would be to encourage older people to continue working through *bridge jobs*, i.e. part-time or temporary employment that creates a more gradual transition from full-time work to retirement. Research has indicated that in the United States, nearly half of all men and women who had been in full-time employment in middle age moved into such bridge jobs at the end of their working lives.[196] It suggests that there are two very different types of bridge job holders: those who continue to work because they have to, and those who continue working because they want to, even though they could afford to retire.

15.11 Cost to pension schemes

15.11.1 The improvement in life expectancy means that occupational pensions are being paid for a longer period, thus imposing substantial additional costs on pension schemes. Many countries have opted to increase the age of retirement as a means of minimising these costs.

15.11.2 In Paragraphs 10.5.3-10.5.8, we examine the impact of increasing the retirement age for public servants to compensate, at least partly, for the increase in life expectancy. We show that an increase of five years, if applied to all public servants, would result in a reduction of £1 billion in the State's accrued pension liabilities, and would reduce annual expenditure on pensions in the long-term by up to 8%.

15.11.3 Early retirement results in major increases in pension costs. The precise measurement of early retirement costs can be difficult. The additional cost to the State arises from the payment of pension benefits over a longer period of time, the granting of years of notional service (if any), and the foregoing of the employee's pension contribution over the period to normal retirement age. In national terms, the cost of a person retiring from the labour force is the cost of the output they would have produced had they remained in employment. If the person works after retirement, including work of an unpaid voluntary nature, this lessens the cost to society in general.

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[195] OECD, *Maintaining Prosperity in an Ageing Society* (1998), p. 48.

[196] Quinn, J., "The Role of Bridge Jobs in the Retirement Patterns of Older Americans in the 1990s", Working Paper 324 in Salisbury, D., ed., *Retirement Prospects in a Defined Contribution World* (Employee Benefit Research Institute, 1997), pp. 25-39.

15.11.4 There are occasions when early retirement is the appropriate option, for example, in cases of restructuring or downscaling of the workforce, or where the employee considers that he or she is not in a position to contribute effectively and the employer agrees that his or her early retirement would enhance operational efficiency.

15.11.5 We have calculated (see Paragraph 10.4.12) that the capital cost of early retirement for a civil servant, aged 50, having 25 years' service (with no added years), and on a basic salary of £28,738, would be equal to 2.73 times his or her salary, a cost of just over £78,000. This is the difference between the actual capital cost of payment of pension from age 50 (8.13 times salary) and the equivalent capital cost for payment of pension from age 60 based on the same level of accrued service (5.4 times salary). This sum represents the additional cost to the pension scheme of payment of pension benefits (based on accrued service) earlier than the normal age of retirement.

15.11.6 Obviously, early retirement costs are much higher if notional added years of service are granted. In the above case, if five years' notional service were granted, the capital cost of the early retirement would increase to about £125,000.

15.11.7 The fact that public service pensions are financed on a pay-as-you-go basis means that the impact of retirement age and early retirement on pension costs might not be easily recognised. But as the above figures indicate, the cost implications are significant.

15.11.8 The cost of pension terms of groups with special retirement terms — early retirement and enhanced pension terms — for operational reasons is much higher than for groups with standard terms. For example, the new entrant rate for a civil servant is 16%; for a member of the Garda Síochána it is 25% (we discuss new entrant rates in Chapter 6). We have shown that the cost of the Garda benefit scale if applied to an established civil servant would almost double the new entrant rate of 16% (see Paragraph 6.6.6).

15.11.9 While early retirement gives rise to substantial additional pension costs, there are circumstances in which it is the appropriate option. However, it is necessary, in the Commission's view, to ensure that the early retirement decision is made carefully and that it takes into account the additional costs which will arise as a result.

15.12 Retirement age in the Social Welfare system

15.12.1 At present, retirement age for the State (Social Welfare) pension is age 65 for Retirement Pension (payable if the qualifying individual has retired) and age 66 for Old Age (Contributory) Pension (the qualifying individual does not have to have retired).

15.12.2 In *Securing Retirement Income*, the Pensions Board examined the issue of retirement age, taking account of the demographic position and of the improvements in life expectancy. The report noted that Ireland is already significantly behind other major economies in terms of life expectancy and the general international experience is that life expectancy at older ages can increase quite rapidly with increasing living standards. The Board concluded that retirement age in Ireland is not currently out of line with most other countries but that public expectations tend to run in the opposite direction to demographic and economic pressures.[197]

[197] The Pensions Board, *Securing Retirement Income* (1998), pp. 95, 98.

15.12.3 The complexities of the practical issues involved in considering changes to retirement age (even over a long period) meant that the Board did not make any recommendations in this regard in relation to the Social Welfare pension. However, it stated that the issue should be considered regularly in the future and that the regular actuarial reviews of Social Welfare pensions provide a good platform for doing so.

15.12.4 The Department of Social, Community and Family Affairs has recently published a review of the entitlement conditions for Old Age (Contributory) and Retirement Pensions.[198] Phase 2 of the review will include an examination of issues relating to retirement age and will take account of the issues raised by the Pensions Board. The Government has taken no decision on retirement age under the Social Welfare system.

15.13 Retirement age in the private sector

15.13.1 As reported in Section 8.7, the normal retirement age is age 65 in the majority of private sector schemes. Unlike the public service, retirement is not generally available from an earlier age in the private sector, unless subject to actuarial reduction of benefits to cover the longer period of payment.

15.13.2 However, apart from early retirement on grounds of ill health, most private sector schemes allow members to retire early, usually subject to actuarial reduction. In the majority of cases, the minimum age of early retirement is 50.

15.13.3 It would seem that where early retirement takes place in the case of company restructuring or redundancy, the actuarial reduction is normally waived. In some cases, enhancement of benefit may occur.

15.13.4 The Revenue rules applicable to funded pension schemes (see Appendix 12.1) permit a normal retirement age in the range 60-70. They allow a normal retirement age outside this range for exceptional occupations (e.g. airline pilots and money brokers/dealers). The rules permit the provision of early retirement benefits on or after age 50.

15.13.5 As outlined in Section 12.14, many private sector schemes offer AVC options to their employees. Should an individual paying into an AVC avail of early retirement, the balance of funds in his or her account would be available to help offset the reduction in benefits brought about by early retirement (subject to compliance with the Revenue rules).

15.13.6 Funded private sector schemes, unlike unfunded public service schemes, require that arrangements be made in advance to meet the capital cost of early retirement. The company may have to pay the amount involved, either up front or over an agreed period of time. In some cases, early retirement may be financed by means of a surplus on the pension fund.

15.13.7 As discussed in Section 15.9, notwithstanding improvements in life expectancy and the cost which this imposes on both state and private pension schemes, the employment situation in many industrialised countries has been characterised by an increasingly early exit from the labour market at end of career. In Ireland, there has been a major fall in numbers (particularly males) employed above age 50. A contributing factor in this has been the trend towards early retirement,

[198] Department of Social, Community and Family Affairs, *Review of the Qualifying Conditions for the Old Age (Contributory) and Retirement Pensions* (2000).

some of which has been driven by companies restructuring in circumstances where strong pension fund investment returns provided the means to pay higher benefits than would be payable on purely voluntary early retirement grounds.

15.14 Retirement age in the public service abroad

15.14.1 In Section 9.7 and Table 9.1, we present details of retirement age and early retirement arrangements in other European countries. We show that seven countries apply a normal retirement age higher than age 60 (one has age 62, five have age 65, and one has age 67). Two countries apply a normal retirement age of 65 but allow retirement from an earlier age subject to a minimum period of service (age 57 with 35 years' service in one; age 60 with 30 years' service in the other). Six countries apply a normal retirement age of age 60, which is in line with the minimum age of retirement in Ireland (in one case, retirement from age 57 is allowed, provided 40 years' service has been completed).

15.14.2 The evidence suggests that with a number of countries moving to increase the age of retirement, the normal retirement age for public servants in Ireland (age 60) may now be considered amongst the lower of those applying to public servants in Europe. Of course, in comparing pension terms it is also necessary to consider other factors such as pension accrual rate, scale of maximum pension, pensions increase policy, etc.

15.14.3 Most countries allow public servants to retire from an age earlier than normal retiring age (in their fifties in some cases). Usually, an actuarial reduction of benefits is applied. In Ireland, early retirement before age 60 is not permitted (other than on grounds of ill health).

15.14.4 Six of the 15 countries examined allow public servants to remain in employment and earn pension rights beyond age 65. In some cases there is an actuarial enhancement to pension because of payment over a shorter period of time.

15.14.5 We also found that it is normal practice to apply special retirement and pension terms to certain groups facing particular operational requirements, e.g. police, fire service. Usually, a full pension entitlement is payable after a shorter number of years than applies to general public service groups. In the UK, which historically had similar arrangements to those in Ireland, special terms have been removed for new entrants to the prison service and for Mental Health Officers (see Paragraph 9.2.10).

15.14.6 In the countries visited by the Commission, we noted a widespread concern about rising pension costs. This was partly due to the average age of retirement being lower than the normal retirement age as a result of early retirement on grounds of restructuring and high numbers of ill health early retirement. As regards the latter, particular attention was being devoted in some countries to creating alternatives to early retirement, including redeployment, retraining, phased retirement, etc. In some countries, greater resources were being devoted to the use of occupational health services.

15.14.7 As a further response to cost concerns, arrangements have been introduced in the UK to charge employers for the full cost to the pension scheme of early retirements on efficiency or restructuring grounds.

15.14.8 Based on our review, it would appear that the trend of reform in retirement arrangements is to increase the age of retirement or the period of service required to qualify for maximum pension and to limit the cost of early retirement provisions to the State. At the same time, changes have been made in some countries to enable public servants to retire early or to take phased retirement (usually at some cost to themselves).

15.14.9 To conclude, public service pension arrangements in other countries reflect the general economic and social conditions of those countries which, of course, differ from country to country. Changes have been introduced in response to the need to cut government expenditure and/or improve national competitiveness. These might not be directly relevant to the situation in Ireland.

15.15 Conclusions and recommendations

15.15.1 The evolving cost of public service pensions is a matter of serious concern. Accordingly, we believe that it is essential to evaluate carefully any possible changes in relation to retirement arrangements which could add to the growth in future pension costs.

15.15.2 At the same time, general perceptions of retirement — within the public service and wider — have been changing. Retirement no longer implies an end to the individual's income earning and productive capacity, and many retirees seek to find alternative employment, including part-time and consultancy working. In addition, many retirees continue to contribute productively by means of voluntary, community or other unpaid work.

15.15.3 In our view, the decision to leave formal employment is one of the most important decisions which an employee will make; accordingly, we consider that appropriate supports should be made available to underpin that process.

15.15.4 The Commission considers that employees should be provided with regular and comprehensive information on their entitlements and the retirement options available to them. Structured programmes of retirement planning and counselling should be initiated so as to raise the issue with individuals well ahead of their retirement and to provide information on the options open to them.

15.15.5 The Commission notes that the increase in life expectancy is placing ever greater cost pressures on pension schemes. International reports suggest that in the face of demographic ageing across all western countries, there is need to increase the period of productive contribution to the workforce of those at older ages. The Commission agrees with this aim. One means of achieving progress in this regard is the introduction of greater flexibility in working arrangements as well as in relation to retirement, including phased retirement.

15.15.6 The Commission considers that a more flexible approach to working and retirement would encourage public servants who would otherwise retire early to remain in public service employment for longer. New flexibilities might include, for example, working at a lower level of responsibility, part-time working, the facilitation of reduced working of unsocial hours prior to retirement, and the re-employment of retired personnel having required skills and expertise.

15.15.7 In our view, the proposal of the Civil Service Inter-Departmental Committee on Work Sharing to expand the scope of the job-sharing scheme to a wider range of attendance patterns (to be known as work-sharing) addresses much of the above. The new scheme is currently being finalised and will, presumably, be extended to other parts of the public service. Our recommendations below, if implemented, would dovetail with this more flexible approach to working, particularly in the lead-in to retirement.

15.15.8 We recommend that changes be made to pension terms to enable public servants who wish to do so to work at a lower level of responsibility prior to retirement without unduly affecting their pension rights. Individuals should be allowed to freeze benefits based on the salary/allowance point immediately prior to changing work pattern, and to separately accrue benefits based on the lower salary/allowance point for the period served in the new work pattern.

15.15.9 We recommend in Paragraph 22.9.14 a change in the pensionability rule for variable allowances so that averaging would cover the best three years' allowances in the last ten, rather than the allowances received in the final three years of service. This change would address the position of employees who might prefer to work fewer unsocial hours close to retirement without unduly affecting their pension rights. Apart from facilitating public servants who wish to have greater flexibility prior to retirement, this change would also meet some of the concerns of management in this regard.

15.15.10 Depending on developments in the labour market, it is possible that the public service may in the future find that it has to take steps to encourage suitably qualified and experienced personnel to remain for longer in public service employment. This could be approached in a number of different ways including:

- the offer of enhanced pension benefits to serving public servants, as applies in certain public service schemes abroad. For example, subject to compliance with Revenue limits, the pension enhancements might comprise the granting of further pensionable credit for service in excess of 40 years up to a maximum of 45 years' service, and/or actuarial enhancement for payment of benefits later than retirement age;
- the retention of personnel beyond maximum retirement age, with the accrual of further pension rights to be limited by the maximum limit on pensionable service, either 40 or 45 years, as appropriate; or
- the re-employment of personnel with the required expertise/skills on a contract basis after retirement, while at the same time relaxing the abatement of pension rules to ensure the necessary financial incentive existed for such an arrangement to operate successfully.

15.15.11 Changes of this nature would offer possible advantages in terms of bringing about an increase in the average age of retirement, thereby reducing future pension costs. However, we note that a number of non-pension-related issues are involved, such as the potential impact on promotion opportunities, and the question of how each of these options would be integrated into the performance management systems to be introduced as part of the Strategic Management Initiative. We believe that the third option listed would be the most appropriate means of targeting areas of the public service in which there were particular shortages of experienced and skilled personnel. It would, in our view, provide the most balanced approach by ensuring that the needs of the public service were met without unduly affecting the normal employment turnover patterns essential for the maintenance of a motivated workforce.

15.15.12 Accordingly, we recommend that, in a context of ongoing labour shortages, some relaxation of the abatement of pension rules should be made in order to facilitate the re-employment of public servants with required expertise/skills on a contract basis after retirement.

Three members of the Commission expressed reservations regarding the approach adopted in relation to this issue — see Paragraph 8 of "Reservation by Senator Joe O'Toole, Rosheen Callender and Dan Murphy".

15.15.13 Improved retirement choice for public servants could be achieved by allowing individuals the opportunity to make personal contributions towards the cost of retiring early. This would ensure that the choice to retire early would not impose further increases in future pension costs.

15.15.14 We recommend the introduction of *cost neutral early retirement*. This would allow public servants aged 50 and over[199] to retire with immediate payment of benefits, subject to actuarial reduction to cater for the longer period over which the benefits would be paid.

Three members of the Commission expressed reservations regarding the failure to recommend an early retirement option, without actuarial reduction, for public servants who have completed 40 years' service — see Paragraph 10 of "Reservation by Senator Joe O'Toole, Rosheen Callender and Dan Murphy".

15.15.15 As recommended in Chapter 19, public servants would have recourse to the Scheme for Public Employees' Additional Retirement Savings (SPEARS) as a well designed, cost-effective, and adaptable facility providing for genuine retirement choice. SPEARS would enable public servants to help offset part of the reduction in scheme benefits resulting from a decision to opt for cost neutral early retirement.

15.15.16 As discussed in Sections 15.10 and 15.11, there have been substantial improvements in life expectancy since public service pension schemes were introduced in the middle of the nineteenth century, and current projections are that it will continue to improve further in the years ahead.

15.15.17 Reflecting this change, we recommend that the age of retirement for new entrants with standard pension terms should be changed from age 60-65 to a single retirement age of 65,[200] with consequential changes in the retirement ages for groups which have special retirement terms for operational reasons (see Paragraph 15.15.33).

Three members of the Commission expressed reservations in relation to the above recommendation — see Paragraph 7 of "Reservation by Senator Joe O'Toole, Rosheen Callender and Dan Murphy".

15.15.18 Early retirement (other than on an actuarially reduced basis) gives rise to substantial additional pension costs. Given the objective of minimising the growth in future pension costs, it is clear that early retirement should be implemented with circumspection. However, there are situations and cases in which early retirement may be the appropriate management option.

[199] Aged 55 and over in the case of new entrants, in accordance with the Commission's recommendation at Paragraph 15.15.17.
[200] As a consequence of this recommendation, the age at which benefits could be claimed in the case of new entrants who resign prior to normal retirement age and who have preserved pension entitlements under public service schemes (including groups which have special retirement terms for operational reasons), should be increased from age 60 to age 65.

15.15.19 The Commission recommends that early retirement provisions should be made available — at an individual/group level — to cater for organisational restructurings, reductions in staff numbers, and as part of new performance management systems to be introduced in the public service. The existence of these provisions and the conditions applying to them should be clearly stated in pension scheme documentation provided to public servants. In view of the cost of early retirement, we recommend that it should be used only where other reasonable avenues — such as retraining and redeployment, flexible working, etc. — have been considered.

15.15.20 However, we consider that there is need for further provision, particularly in light of the arguments presented in submissions and in our meetings with interested parties.

15.15.21 Accordingly, we recommend the introduction of an additional early retirement facility, called *Approved Early Retirement*. Early retirement under this facility would be available in respect of public servants aged 55 or over[201] with 20 or more years' service who consider that they are unable to make a fully satisfactory contribution and where management accept that their early retirement would improve the general level of efficiency and effectiveness of the service in question. It would be initiated either by management or the individual public servant, and would be subject to agreement by both parties. Pension benefits under Approved Early Retirement would consist of the immediate payment of pension and retirement lump sum with no actuarial reduction.

15.15.22 In the light of the significant cost which early retirement imposes, the Commission recommends that an annual quota of Approved Early Retirements be set and that all applications across the public service be assessed at a central level. We suggest below (see Paragraph 24.5.3) that alternative arrangements should be examined which would involve departments or organisations meeting the additional capital cost of early retirement from within their own resources.

15.15.23 We recommend that a review of the Approved Early Retirement facility should be carried out in five years' time, having regard to its efficacy in addressing the needs of management and staff, the level of take-up, and the development and implementation of new systems to monitor performance in the public service, including early retirement provisions (see Paragraph 15.15.19).

15.15.24 As part of their respective restructuring agreements reached under the *Programme for Competitiveness and Work*, a number of limited retirement and early retirement initiatives were agreed for teachers and nurses. These initiatives were to operate on a pilot basis, subject to annual quotas, and would be reviewed in the light of our Final Report.

15.15.25 The Commission recommends that the limited retirement initiatives for teachers and nurses should be continued for a further five years, and that they be included in the review referred to at Paragraph 15.15.23.

15.15.26 The Commission considers that the high incidence of early retirement on grounds of ill health in certain parts of the public service is a matter of concern — in terms of the effect on pension costs, the impact upon the individuals affected, and the consequences of the loss of experienced and qualified employees from the public services in question.

[201] Aged 60 or over in the case of new entrants.

15.15.27 Accordingly, we recommend that a review should be carried out of procedures followed in processing ill health early retirements across the public service, with the aim of developing a consistent approach and to identify best practice.

15.15.28 We acknowledge the work of occupational health units in helping individual public servants to address difficulties which they are experiencing in their work, particularly the debilitating effects of adverse stress and burnout.

15.15.29 A range of additional actions should be taken to address factors which have potentially negative effects on the health and performance of individuals. These include identifying and addressing the most prevalent causes of adverse stress where they occur in various public service occupations (e.g. under-resourcing, excessive work loads), developing and extending occupational health services to address health and welfare issues, and the effective use of redeployment, accompanied by retraining.

15.15.30 The Commission accepts that it is necessary for operational reasons for certain public service groups to be subject to lower retirement ages than the norm, and as a consequence to have enhanced pension terms.

15.15.31 For the application of special terms to be justified, it should be possible to demonstrate that it is an absolute prerequisite that all employees in the group are required, as the central feature of their employment, to maintain throughout their period of service a consistently high work capacity, defined in terms of physical capability, alertness, and speed of response so as to be able to respond quickly and effectively to an operational emergency, and that the application of lower retirement ages is a reasonable means of maintaining a high work capacity.

15.15.32 In assessing the position of public service groups in light of this requirement, the Commission considered operational requirements and environmental conditions, the historical basis and development of current arrangements, and practice in the private sector and in comparable employments in the public service of other countries.

15.15.33 Based on the information available to the Commission,[202] and taking into account our recommendation to raise retirement ages for new entrants to the public service generally (see Paragraph 15.15.17), our specific recommendations on the application of special terms for operational reasons are as follows:

(i) new entrants to those parts of the psychiatric services where special terms currently apply should in future have standard pension terms; there should be no change in the special terms (i.e. doubling of service on serving in excess of 20 years, and retirement on reaching age 55) of personnel currently employed in the psychiatric services;

(ii) new entrants to the Garda Síochána should be subject to a minimum retirement age of 55 and should be retained beyond that age, to a maximum retirement age of 60, subject to meeting certain minimum standards of health and fitness on an annual basis; there should be no change in the special terms as they are applied to members of the Garda Síochána currently in service;

[202] The Commission examined the position of groups which have special terms and those seeking their extension in light of the criteria listed in Paragraph 15.15.32. The Commission also considered the views expressed by the relevant departments and employees/unions, submissions, the available retirement data, reports prepared on the different groups and services, and other available research information and studies.

(iii) in the case of the prison service, the optional facility to retire between ages 50 and 55 on achieving 30 years' service should not apply to new entrants; the new Prisons Board should examine whether, in light of developments in operational requirements in the prison service, special terms in their entirety (i.e. retirement between ages 55 and 60, and doubling of service on serving in excess of 20 years) should be removed; there should be no change in the special terms as they are currently applied to personnel now in employment;

(iv) in the case of the fire service:

(a) new entrant Firefighters should continue to be subject to a retirement age of 55, with service in excess of 20 years doubled for pension purposes;

(b) new entrant officers, who have the option to remain in employment until age 65, should have standard pension terms;

(c) new entrant Firefighters who are subsequently promoted to non-operational positions should have standard pension terms, but should receive a higher pensions credit for the period served as Firefighters (this is known as *uniform accrual*);[203]

(d) there should be no change in special terms as they are currently applied to all serving personnel;

(v) new entrant teachers should have standard pension terms; the provision whereby teachers may retire between age 55 and age 60 (on achieving 35 years' service) should continue for all serving teachers (the limited retirement initiative for teachers is addressed in Paragraph 15.15.25);

(vi) new entrants to the Defence Forces should have special pension terms more in line with the special terms which apply to certain other public service groups, consistent with current personnel policy (see Chapter 21);

(vii) having regard to the available information, and in light of the range of other recommendations made in relation to retirement age and early retirement, the Commission does not recommend the extension of special pension terms to any other public service group.

Three members of the Commission expressed reservations in relation to the above recommendation — see Paragraph 9 of ''Reservation by Senator Joe O'Toole, Rosheen Callender, and Dan Murphy''.

15.15.34 The purpose of the Commission's recommendations in relation to retirement age and early retirement — which we believe are essential to ensure internal equity and fairness in pension arrangements for the future — is to arrive at a situation where increased flexibility in pension and working arrangements is available to all public service groups, and where departure from standard pension terms occurs only where it is considered absolutely necessary for operational reasons. The recommendations in relation to special pension terms focus upon the retirement terms of new entrants; thus, the entitlements of serving staff members would not be affected in any way.

[203] For groups with special terms involving the doubling of service after 20 years' service, a full pension based on 40 years' service is payable after 30 years' actual service. *Uniform accrual* ensures that where a public servant is subject to special terms of this nature and transfers to a public service scheme where standard terms apply, his or her service in the original scheme is multiplied by the fraction 4/3. Thus, for example, 15 years' service in the special scheme is credited as 20 years' service in the standard scheme.

CHAPTER 16

Pensions Increase Policy

16.1 Introduction

16.1.1 The maintenance of the value of pensions over time is an important element in the terms of a pensions scheme. Pension increases in the public service are currently determined on the basis of *pay parity*, that is, in line with the pay of the grade in which the former public servant once served. This has proven an advantageous arrangement for the pensioner, mainly because pay has increased at a consistently higher rate than price inflation. Consequently, it has also proven a costly arrangement for the State. In addition, new forms of pay increase in the public service — which reward restructuring, improved productivity, and modernisation — have raised questions about the manner of implementation of pay parity.

16.1.2 In this Chapter, the Commission summarises the issues which have arisen in relation to pensions increase policy and discusses the factors which would be involved in any change to the present arrangement. Following consideration of a range of options, the Commission recommends continuation of pension increases in line with public service earnings, subject to an additional explicit contribution by public servants towards the cost involved. In a change from the existing form of pay parity, we recommend that a single index of public service earnings be used in the future, with pension increases based on changes in the index to be paid automatically on a twice-yearly basis.

16.2 Existing system of pension increases

16.2.1 Under pay parity, public service pensions are increased in line with, and with effect from, the same operative date as any relevant pay increases — both general and special — applicable to serving staff. In general, the increases are effected on an administrative basis initially, and are later given statutory effect by means of regulations made under Section 29(2) of the Pensions (Increase) Act, 1964. We present a full description of existing arrangements in Appendix 3.2.

16.2.2 General pay increases are those contained in national pay agreements such as the *Programme for Prosperity and Fairness* or previous similar agreements concluded between the social partners. Special pay increases are those which are pertinent to specific grades or posts.

16.2.3 We outline the history of pensions increase policy for public service schemes in Appendix 16.1. Prior to 1969, pensions in payment were increased from time to time on an informal basis. In the 1969 Budget, the Minister for Finance announced his decision in principle to adopt pay parity and to move towards it over a number of years. In the 1984 Budget, full parity (i.e. revision of pensions from the same date as the relevant pay increases) was introduced for general pay increases. In the 1986 Budget, full parity was introduced for grade and special pay increases.

16.2.4 We discuss pensions increase policy in Section 11.8. We note that pension increases represent a significant component in the cost of pensions. Obviously, the more favourable the pensions increase policy the greater the cost. Apart from cost, the issues which arise in relation to existing pension increase arrangements include:

- **pay parity in the context of a changing approach to pay determination**: in an environment in which pay determination systems increasingly reward change and modernisation, and where there is wide variation in the rates of pay increases granted to different groups, the tracking of salary of the grades from which pensioners have retired may be seen as less appropriate;
- **administrative difficulties**: many practical difficulties have arisen in the implementation of pay parity, for example, the problem of continuing links with specific grades that have over time been amalgamated with other grades or regraded, dealing with lengthening or shortening of pay scales, and verifying service requirements for payment of pension on the introduction of long service increments. These problems have been exacerbated by the complexity of many of the restructuring agreements made under the *Programme for Competitiveness and Work (PCW)*; for example, in the civil service alone, 15,000 individual pensions files — some of which relate to retirements in the 1950s and 1960s, or even earlier — had to be examined manually in an inherently time consuming operation;
- **effect on pensions in payment of decisions to make new allowances pensionable**: in a number of cases in the past (see Appendix 11.5), it was decided to amend pension terms for certain groups by making certain allowances pensionable, and to apply the revised terms in respect of personnel who retired or died *after* the effective date of the decision; pensions in payment *prior* to the effective date were not affected; pensioners have sought consequential increases in pension on the basis that these allowances were applicable to all or many who served in the groups concerned, and thus formed a central part of remuneration (the Commission considers this issue in Section 22.6).

16.3 Relevant factors in the consideration of pensions increase policy

16.3.1 The Commission accepts that some regular adjustment of pensions is desirable. First, to maintain living standards, upward adjustment to take account of price inflation is necessary. Second, account should be taken of progression of pay generally in order to maintain *relative* living standards. Public sector schemes in other countries regularly raise pensions in line with price inflation. Pay parity is less common as a basis for adjustment. We believe that a change in pensions increase policy is necessary in order to address the issues outlined above. In formulating our recommendations, we had regard to a range of factors:

- commitment to increase pensions;
- Government statements on pension increases;
- employee contributions and pension increases;
- pay parity and restructuring agreements;
- administrative considerations;
- cost;
- pension increases in the private sector;
- pension increases in the public service abroad.

Commitment to increase pensions

16.3.2 An important question to be considered is the nature of the State's commitment to increase pensions. The Pensions (Increase) Act, 1964, which is the legislative basis for all public service pension increases, does not state how often or in what form pension increases should be made. Thus, it is formally the case that pension increases are at the discretion of the Minister for Finance.

16.3.3 However, pensioner representatives, unions, and many Deputies who spoke in a Dáil debate on this issue in October 1997[204] claim that there is an expectation amongst pensioners and serving public servants that pensions will be increased in line with increases in pay from the effective date of those increases.

16.3.4 Notwithstanding the formal position under the 1964 Act, it is clear that any change which might be recommended in future pensions increase policy must take account of the reasonable expectations of three different parties — pensioners, serving employees, and new entrants. These expectations are influenced by the need for some adjustment to take account of price inflation at minimum, and some link with pay to avoid relative deprivation. Also, government statements in relation to pensions increase policy, and the argument that public servants contribute towards the cost of pension increases need to be considered (see following paragraphs).

Government statements on pension increases

16.3.5 Pay parity was introduced in a long line of Budget statements dating back to 1969 (as detailed in Appendix 16.1). More recent statements appear to reinforce the commitment to pay parity. For example, in *An Action Programme for the Millennium* (1997), the Government listed as a key priority the *"protection of public service pensions"*. Also, in its statement of 4 November 1997 regarding increases to pensions arising out of the *PCW* restructuring agreements (see Paragraph 11.8.10), the Government made clear that pay parity was to continue:

> *The refinement of traditional parity announced today* [parity with a "floor" of 3%] *meets the particular complexities of the PCW restructuring deals and is a one-off measure to address these particular circumstances.*

16.3.6 However, the statement added that policy in relation to any future restructuring deals would be determined in the light of the recommendations of our Final Report.

Employee contributions and pension increases

16.3.7 Many pensioners and serving employees claim that they have been or are contributing to the cost of the pension benefits they enjoy, particularly the cost of pension increases in line with pay. This *notional contribution* — the extent to which public service pay is reduced to take account of the favourable pension increase arrangements which apply — is examined in Section 11.9 which reviews developments over the past 20 years.

16.3.8 In Paragraph 11.9.20, we note the difficulties involved in attempting to establish the extent to which pension terms are reflected in present pay levels in the public service or in drawing a general conclusion on this matter in relation to the public service as a whole. While it is possible to say that up until the *PCW* agreement a deduction for post-retirement benefits was included in the salary structures of executive grades in the civil service and in the pay of related grades in the civil and public service, it cannot be said with the same certainty that the deduction continues to apply in what is now a significantly different pay determination environment. It should be noted, however, that the changes which have taken place in pay determination are not

[204] Dáil debate on motion on Public Service Pensions under Private Members' Business, 21-22 October 1997.

necessarily of a permanent nature. Moreover, it can be argued that no matter what pay determination system is applied, there will always be a case for relating public service pay to the position of comparable groups in the private sector from time to time. However, this issue is likely to arise again in the context of the benchmarking exercise which is provided for in the *Programme for Prosperity and Fairness*.

Pay parity and restructuring agreements

16.3.9 As outlined at Appendix 3.2, the effect of special pay increases is generally passed on to pensioners provided that the increases in question were applied to all employees serving in the grade concerned and that assimilation of serving employees to the revised pay scales was on a *corresponding points* basis. Also, the increase must not have been awarded in consequence of a substantial restructuring or alteration of duties which, in effect, constituted regrading of the posts concerned, and the increase must not have been awarded in respect of increased productivity by serving staff.

16.3.10 Prior to the Government's decision on the *PCW* agreements in November 1997, the Department of Finance had argued that these agreements were different to special pay increases. The Department pointed to the fact that the agreements were negotiated in the context of an overall national pay agreement, and that they emphasised changes in structures, work practices, or other conditions in service. In addition, the agreements called for savings and an improved quality of service to the public, and they sought to take account of the need for efficiency, flexibility and change and the contribution to be made by employees to such change. The Department also pointed to the wide variation in the nature of the agreements reached for different public service groups, leading, the Department argued, to an inequitable pensions outcome if traditional pay parity were to be applied.

16.3.11 In response, pensioner representatives and unions argued that the *PCW* restructuring agreements were no different to special pay increases and for that reason should be passed on to pensioners in accordance with existing policy.

16.3.12 In order to assess the competing viewpoints on *PCW* restructuring agreements as compared with traditional special pay increases, the Commission considered it useful to briefly review two examples of the latter:

> **Report of the *Gleeson Commission* on the Defence Forces (1990)**[205]
> This was the first independent Commission in the history of the State to examine pay and conditions within the Defence Forces. The Commission's conclusions on pay were arrived at on the basis of a detailed analysis of a large volume of data on pay rates, and an examination of the duties, responsibilities and skills of Defence Forces personnel relative to those of employees in other employments. Other factors were also taken into account. The Commission recommended increases in rates of regimental pay and Military Service Allowance ranging from 7.7% for a Captain, 11.4% for a Private 3 Star, 14.9% for a Sergeant Major, and 16.1% for a Lieutenant Colonel.
>
> ***Civil Service Arbitration Board Report No. 531 (1988)***
> This was an arbitration report on a claim by the Civil Service Executive Union for a substantial increase in the pay of the grades of Executive Officer, Higher Executive Officer and Administrative Officer. The arbitrator followed the principles of the UK *Priestly Commission*[206] and recommended increases in pay of 10-11%.

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[205] Government of Ireland, *Report of the Commission on Remuneration and Conditions of Service in the Defence Forces* (1990), pp. 2-3.

[206] The Royal Commission on the Civil Service (the *Priestly Commission*) of 1953-55 recommended that the primary principle of civil service pay should be *"fair comparison with the current remuneration of outside staffs employed on broadly comparable work, taking account of differences in other conditions of service"* (Scott Report, 1981, p. 15).

In accordance with existing pensions increase policy, both sets of special pay increases were passed on to pensioners.

16.3.13 Although there was always a need to distinguish between these two types of pension increases for pay parity purposes, the difficulties in this regard were highlighted by the very explicit linkages between pay and change which were established in the *PCW*, the significant variations in the structure of the *PCW* local bargaining agreements and the associated flexibility and productivity elements.

16.3.14 The question of pay parity and restructuring was recently clarified in a judgement of the Circuit Court in which a claim for an increase in pension arising out of a restructuring of the system for paying hospital consultants was refused. In the judgement, the Court found that pensionable remuneration was calculated by reference to the salary of the employee as of the date of cesser of his employment, and "*that there is nothing to say or to suggest or to imply that pension is based on the salary of the Successor*".[207] Thus, it would appear that pension increases on the basis of increases in the pay and allowances of serving staff are far from automatic and it is quite possible that any one restructuring agreement — depending on its terms — might fall outside existing pensions increase policy.

16.3.15 It is clear that there was substantial variation in pension increases resulting from the application of pay parity under the *PCW* restructuring agreements. In the case of some groups, the relevant agreement focused on non-pay conditions of service such as promotions or early retirement, while in others substantial *straight* pay increases were awarded. Under strict pay parity, pensioners in the former group would receive no increase while pensioners in the latter would benefit from the relevant pay increase.

16.3.16 The Commission notes that the Government's decision of November 1997 did not simply *restore* parity in accordance with a particular view of how pay parity operates; the *"refinement on traditional parity"*[208] which involved the provision of a minimum increase of 3% can be seen instead as an improvement in parity. The Commission is satisfied that in the absence of any change in pensions increase policy, the kinds of pressures which arose in relation to the restructuring agreements will recur. These will be particularly difficult if, as expected, future pay determination is to focus on rewarding performance, productivity, and the delivery of change in a more flexible way.

16.3.17 It is worth noting that the *Programme for Prosperity and Fairness* does not provide for the making of restructuring agreements in the form provided under the *PCW*. However, an element of the pay increases it contains is to be linked to the achievement of specific performance indicators in relation to ongoing modernisation of the public service. There is provision also for benchmarking, i.e. a broadly based comparison with jobs and pay rates across the economy.

[207] The Circuit Court, County of the City of Dublin, *Sean Baker v. The Southern Health Board, the Minister for Health, Ireland and the Attorney General*, Record No. 5417197, (24/3/99), paragraph 19.
[208] Government press statement of 4 November 1997.

Administrative considerations

16.3.18 The present policy of increasing pensions in line with changes in the pay scales of serving employees has created many practical difficulties which have been exacerbated by the impact of the *PCW* restructuring agreements.

16.3.19 There were two types of delay in the case of the restructuring agreements: the period between the date of the agreements (some dating from 1994/95) and November 1997 when the Government made its decision on pension increases, and the period required following the Government decision to calculate and process the increases and arrears due for each public service group. The lack of clarity initially about the pensions treatment of the agreements generated much concern and unease amongst pensioners about the future of pension increases generally. In addition, the delays which occurred between the date of the Government decision and the payment of increases, as well as arguments about the implementation of the decisions, created further difficulties.

16.3.20 The Commission considers that pensions increase policy should be clear and easy to understand. Pension increases should be calculated and implemented promptly. Given the experience of the past number of years and the possibility of further changes in pay determination in the future, it is questionable whether existing policy is capable of meeting those objectives.

Cost

16.3.21 In Section 10.5, we outline the cost impact for public service pension schemes if pay parity were to be replaced with pension increases in line with price inflation. For example, we calculated that applying the change to all pensioners and serving staff would result in the State's actuarial liability for public service pensions falling by just over £2.6 billion (i.e. 13%). However, it should be noted that this reduction in costs would be achieved at the cost to pensioners of a major diminution in the future value of their accrued pension entitlements.

16.3.22 The case has been made to the Commission that in view of the particular benefit that earnings-related pension increases represents, public servants should be expected to make an explicit contribution towards the cost involved. We address this matter in our recommendations below.

16.3.23 At this point, it is useful to consider policy in relation to Social Welfare pension increases on the basis that:

- Social Welfare pension increases, like public service pension increases, are determined formally at the discretion of the Government; and
- through the operation of integration, a portion of the pension package for many public service pensioners is provided by the Social Welfare pension.

16.3.24 According to the Department of Social, Community and Family Affairs, over the past five, ten and 20 years, there has in practice been effective indexation of Social Welfare pensions to earnings, albeit that these increases have been on an *ad-hoc* basis.

16.3.25 Significantly, the Pensions Board has expressed the view that:

> *it would be desirable to aim, over the medium-term, to increase Social Welfare pensions, in real terms, in line with growth in earnings in the economy, as has effectively happened over the past 20 year period.*[209]

16.3.26 This recommendation has been noted by the Government. In its review of *An Action Programme for the Millennium* (November 1999), the Government has stated that it will advance the goal of bringing the Old Age (Contributory) Pension to £100 per week and extend the £100 commitment to all Social Welfare old age pensions by 2002. It also stated that over the lifetime of the Government, all Social Welfare payments would be increased in line with average earnings. These commitments were endorsed in the *Programme for Prosperity and Fairness.*

Pension increases in the private sector

16.3.27 Under Revenue rules, funded pension schemes may provide for increases in pensions to counteract the effects of price inflation. Discretionary increases may be made to maximum pensions up to the level of increases in the Consumer Price Index (CPI) or another similar agreed index. Guaranteed increases may be made by using either of the following formulae:

(i) fixed increases of not more than 3% per annum compound (regardless of CPI levels); or

(ii) increases linked to CPI or another similar agreed index.

A formula providing for the greater of (i) and (ii) is not acceptable.

16.3.28 Augmentation of existing pensions to put the recipients on a par with current holders of the same employment will normally be approved.

16.3.29 In Section 8.17, we set out private sector practice in relation to pension increases. In large schemes in the private sector, the basis for increasing pensions, according to the ESRI report for the Commission, is as indicated in Table 16.1.

Table 16.1: Basis on which increases are made to pensions in payment

Type of Increase	% breakdown
Guaranteed increases, with or without review	39
Discretionary increases, with or without review	33
No increases	20
No pensioners or other basis*	8

* increases are granted on some other basis than those mentioned above.

16.3.30 Over 45% of schemes in large firms that provide guaranteed increases in benefits have a rate of increase specified as a percentage of pension. Another 45% match the increase in the CPI either to the actual or a maximum figure and the remaining schemes grant increases on some other basis. Almost all of the schemes that provide a guaranteed percentage increase apply a maximum figure of 3% or 4% per annum. Schemes that match the CPI up to a maximum figure generally stipulate that the maximum increase they will pay is 4% or 5% per annum.

[209] The Pensions Board, *Securing Retirement Income* (1998), p. 107. The representative of the Minister for Finance on the Pensions Board stated in the Report (p. 116) that he was unable to support any rate of pension increase which was explicitly linked to earnings.

16.3.31 In relation to defined contribution pension schemes, it is worth noting that the individual must decide when purchasing an annuity at retirement whether or not to include a guaranteed pension increase provision. Obviously, the initial value of the pension will be lower if guaranteed annual pension increases are included.

16.3.32 As indicated by the above, pensions increase policy is significantly more favourable in public service schemes compared with private sector schemes.

Pension increases in the public service abroad

16.3.33 We describe in Paragraph 9.7.25 the basis on which public service pensions are increased in other countries. From the information available it would appear that five countries among those surveyed — Austria, France, Germany, the Netherlands and Portugal — increase pensions in line with the rate of salary increase. Five countries make reference to both cost of living and rate of salary increase. In the remaining five countries, pension adjustments are linked to developments in the cost of living index only. Much more restrictive arrangements apply in US pension plans.

16.3.34 On balance, based on the pension systems reviewed, it would appear that Ireland operates a pensions increase policy that is amongst the more favourable of those considered. Of course, pension increases are only one aspect of pension scheme terms and it can be difficult to reach proper conclusions on a comparison of this pension term alone. For example, maximum pension would appear to be more favourable in many other European countries.

16.4 Possible alternative pension increase arrangements

16.4.1 Having considered the growing problems attached to the operation of pay parity, the Commission decided to examine a number of alternative pension increase arrangements, namely:

- in line with CPI;
- in line with general earnings (average industrial earnings);
- in line with a newly developed public service earnings index (we consider this option in Section 16.5).

16.4.2 Before considering the alternatives, we review the arguments for and against the existing system.

Pay parity

In favour of existing system of pay parity

(i) it would maintain the standard of living of pensioners by reference to those currently retiring from the grade in which they served;

(ii) pay parity is relatively easy to understand and appears to be fair and transparent;

(iii) pay parity is the expectation of public servants and pensioners, on the basis of formal government commitments given over a number of years;

(iv) pay parity applies in the pension schemes for public servants in a number of other European states.

Against existing system of pay parity

(i) there are growing difficulties in deciding how to deal with pay agreements where they involve elements of reward for performance. The maintenance of a direct connection *in all cases* between pension and individual grade pay rates across the public service may in fact become unworkable;

(ii) pay parity has led to perceptions of unfairness and to outcomes which would be seen as anomalous — e.g. allowances made pensionable, but not passed on to pensioners;

(iii) pay parity is administratively very difficult and will probably become more so;

(iv) pay parity does not apply in the pension schemes for public servants in a number of other European states.

16.4.3 The main considerations relating to the alternative pension increase systems are as follows:

Consumer Price Index

In favour of Consumer Price Index

(i) periodical adjustment of pensions in line with changes in CPI would meet the objective of preserving the real value (purchasing power) of the pension over time;

(ii) this is the system applying to the public service in several other EU states and to private sector pension schemes in Ireland (for those schemes which pay pension increases — 20% do not — a maximum annual limit of 3-5% applies);

(iii) it would be automatic, regular and simple to administer;

(iv) it would be an objective and transparent system of pension increases: all pensioners would receive the same percentage increase in their pensions.

Against Consumer Price Index

(i) the *relative* standard of living of pensioners (compared with serving employees) would fall over time;

(ii) Social Welfare pensions in Ireland have, effectively, been increased in line with earnings in the past number of years. If earnings-related increases in Social Welfare pensions are continued, it would be unreasonable to apply a less favourable pension increase system to public service pensioners;

(iii) it would fail to meet the expectations of pensioners and serving public servants.

General earnings (average industrial earnings)

In favour of general earnings

Under this approach, the Central Statistics Office (CSO) index of Average Industrial Earnings would be taken as an appropriate measure of changes in earnings over time:

(i) pension adjustments in line with earnings would maintain the relative amount of the pension constant over time. Increases in pensions would be the same, on average, as the increases received by employees generally;

(ii) increases in line with general earnings is the system applying in the public service pension schemes of a number of other European countries;

(iii) as with CPI-related increases, the system would be simple to administer and would be objective and transparent.

Against general earnings

(i) there would be no logical reason why public service pensions should be linked to an index which does not include public service earnings;

(ii) industrial employment accounts for less than 30% of total employment and excludes the services sector which accounts for over 60% and which more closely represents public service activities;

(iii) it would fail to meet the expectations of pensioners and serving public servants.

16.5 Public Service Earnings Index

16.5.1 In view of the deficiencies of both the Consumer Price Index and the general earnings index, the Commission explored the possibility of establishing a new index — the Public Service Earnings Index. Such an index has been constructed in the Netherlands (see Paragraph 9.5.6) where it is used to determine the rate of pension increases. The Public Service Earnings Index would aim to capture changes in pay across the whole public service. By matching pension increases to developments in this index, pensioners would benefit from the earnings growth of the public service as a whole.

16.5.2 Ideally, the Public Service Earnings Index would measure the average pay increase given to serving staff where the increases to be taken into account were those which would be applied to pensioners under the current system of pay parity. At present, there is no measure of this rate of increase. The CSO publish, on a quarterly basis, details of public sector average weekly earnings together with a public sector earnings index which is designed to measure the trend in average weekly earnings in the public sector. This index has a number of characteristics which may make it unsuitable, in theory, as a basis for calculating the appropriate rate of increase for pension purposes. However, based on an examination of the changes in the index since it was first compiled in 1988, it appears that the current index could act as a reliable indicator of average changes in public service pay. The application of this index system should lead to increases in pensions which, *on average*, would be broadly the same as the increases which would take place under the current system. We set out in Appendix 16.2 a detailed note on the development of a public service earnings index on the basis of the existing CSO index.

16.5.3 Appendix 16.2 also gives details of the values of the current index for the ten year period from its start in March 1988 to September 1998. From this historical series it is possible to examine the increases that would have been paid to all pensioners if the index system had been in place. Over this period, the index increased by 66%, or 5% per annum; the corresponding increase in the CPI was 31%, or 2.6% per annum. Over the same period, total pay increases awarded under general pay rounds amounted to 32%. Special pay increases, combined with the impact, both positive and negative, of other factors such as increments, promotions, recruitment and retirement, made up the balance.

16.5.4 In developing the Public Service Earnings Index as a basis for increasing public service pensions, the following modifications to the current CSO public sector average earnings index would be necessary:

(i) inclusion of the health sector; we understand that the CSO have been considering this matter, and that it should be possible to publish an index which includes this sector;

(ii) exclusion of the commercial state companies;

(iii) exclusion of the effect of the wide variation in total overtime payments which can be experienced in the case of the Garda Síochána and Prison Officers (see Paragraph 7 of Appendix 16.2). Overtime amongst other groups would appear to be more stable over time;

(iv) calculation of an *arrears* percentage; this would be based on the average amount of arrears paid to serving public servants in a period.

16.5.5 This additional Public Service Earnings Index figure might be published by the CSO on a twice-yearly basis. The Commission understands that the first three of the above modifications could be completed within a reasonable period, assuming that there were no further problems in obtaining reliable data from the health sector. Additional information would need to be provided by all respondents to enable an *arrears* percentage to be calculated. With the commitment of the relevant public service bodies, the relevant information should also be available within a reasonable period.

16.5.6 In summary, the Public Service Earnings Index considered by the Commission would have the following features:

- the index would be prepared by the CSO on a six-monthly basis. It would be issued around three months after the period covered, and would be applied automatically to all pensions in payment, with arrears to be paid as appropriate;
- a single rate of increase would be applied twice-yearly to all pensions, based on the change in earnings averaged for the public service as a whole over the previous six-monthly period (thus all *general*, *special* and *restructuring* increases would be comprehended within the new system);
- the index would be based on the existing CSO public sector earnings index, modified as appropriate, in line with the discussion at Appendix 16.2. Consultations would take place with public service unions and pensioner representatives prior to introduction of the index;
- unions and pensioner representatives, along with government/public service employers, would have an opportunity on a five-yearly basis, to assess the practical implications of the application of the index and of any specific problems arising therefrom;
- pensions would be increased automatically under the new system. This would be provided for in new legislation sponsored by the Minister for Finance;
- the index would not result in any change in *average* rates of pension increase nor in the overall cost of pension increases to the State. While, obviously, some groups would gain and some lose by the change at different times, depending on the development of pay for different groups of serving staff at different times, it would be expected that, over time, the effect would be broadly neutral.

16.5.7 The arguments for and against the Public Service Earnings Index are listed below:

In favour of the Public Service Earnings Index

(i) it would aim to provide the same total amount of pension increases as before, but calculated in a more simple and transparent manner;

(ii) it would help deal with the problems associated with restructuring type agreements – in particular, by removing ambiguities inherent in the existing system. In addition, it would capture the effect of a shift from the system of general and special pay increases to one involving greater elements of performance pay, restructuring of grades, etc.;

(iii) the earnings index would be automatic and objective. There would be no need to negotiate on the application of pension increases in the future (the formula could be revisited from time to time, as agreed);

(iv) it would be broadly consistent with the preferred approach of the National Pensions Policy Initiative in linking Social Welfare pension increases to increases in average earnings;

(v) compared to the existing system, this form of pay parity would be administratively more convenient.

Against the Public Service Earnings Index

(i) the setting up and monitoring of the index would require additional resources;

(ii) over the short run, from the perspective of public servants and of pensioners, there would be both *winners* and *losers* compared with the existing system of pay parity;

(iii) it could happen that a person retiring might receive a different pension to that currently held by someone who retired on the same grade point and having the same pensionable service (if the earnings index gave a higher rate of increase than the pay increase for the grade in question).

16.6 Conclusions and recommendations

16.6.1 The Commission considers that pension increases in line with changes in the Consumer Price Index (CPI) would represent the minimum provision required for the maintenance of the standard of living of public service pensioners. We also believe that some link to broader pay increases remains highly desirable. In most schemes, the formal position is that the grant of increases in pension is at the discretion of the Minister for Finance. The Commission acknowledges the possibility that in the absence of any change now to secure pension increase arrangements into the future, pressures might arise, perhaps in a time of straitened financial circumstances, to move to a system of CPI-related pension increases.

16.6.2 The Commission notes the arguments made on behalf of many pensioners and employees that pay parity represents a benefit to which they have contributed and that public servants have consistently placed a greater importance and value upon good pension benefits than have employees in the private sector. We would suggest that with the changing nature of pay determination in the public service, and in the absence of any change to pensions increase policy, the practical difficulties, disputes, and delays in finalising pension increases which have arisen in the past will continue.

16.6.3 In an environment in which pay determination systems increasingly reflect commitment to public service change and modernisation, the tracking of salary of the grades from which pensioners have retired may be seen as less appropriate for pension increase purposes.

16.6.4 For these reasons, the Commission considers that an alternative system of increasing pensions, based on an average of pay increases in the public service as a whole, would be more appropriate to this changing environment, and that in light of the substantial benefit which pay-related pension increases represents, should be made subject to an additional contribution by public servants towards the cost involved.

16.6.5 Accordingly, the Commission recommends that a CSO Public Service Earnings Index should be developed (along the lines set out in Paragraph 16.5.6) for calculation twice-yearly of a single rate of pay-related increase to be paid to all public service pensioners. The implementation of the index should involve consultation with public service employers, unions and pensioner representatives. In view of the value to public servants of a guaranteed system of pay-related pension increases, the Commission recommends that all serving public servants should make an additional explicit 1% contribution of remuneration or net remuneration, as appropriate, towards the cost of pay-related pension increases. We also recommend that the State should explicitly guarantee the new system of pension increases by means of legislation and through the establishment of a Public Service Pension Fund to meet the full cost of pension increases.

Three members of the Commission expressed reservations in relation to the additional 1% employee pension contribution recommended above — see Paragraph 11 of ''Reservation by Senator Joe O'Toole, Rosheen Callender and Dan Murphy''.

16.6.6 The Commission believes that the new system of pay-related increases, supported by an employee contribution and a pension fund, would represent an affordable, administratively straightforward and equitable pension increase system. Given the uncertainty which characterises existing arrangements, the new system should strengthen confidence as to the continuation of pay-related pension increases into the future.

16.6.7 A new explicit contribution of 1% of remuneration to be made by all serving public servants is a necessary part of our recommendation, having regard to the value to public servants of a guaranteed pay-related pension increase system secured by legislation and a pension fund. The introduction of the contribution would serve to justify what have to date been more favourable pension increase arrangements applying to public servants compared with all other pension recipients in the economy, and would represent an explicit commitment by serving public servants towards the establishment of the new system.

16.6.8 As discussed in Chapter 23, we recommend that the 1% contribution towards the cost of pension increases, when it is introduced, should be lodged to the Public Service Pension Fund. The Public Service Earnings Index should be developed with a view to its implementation after the completion of the current *Programme for Prosperity and Fairness*.

APPENDIX 16.1

History of pension increases in the public service[210]

Early history

1. The First World War was followed by a period of rising prices and falling money values. The 1920 cost of living figure was 130% above the 1914 figure. Facing demands for improvements in the pensions of those who retired before the post-war codes came into place, the British Government implemented the Pensions (Increase) Act of 1920 which granted increases to those who could show satisfactorily that their means, including pension, were less than £150 a year, if unmarried, or £200 a year if married. The assessment of means included annual value of house property, interest, gifts, etc. Charges on income included interest or mortgage, loan debts, etc. Increases granted were scaled depending on level of means: thus, an increase of 50% applied where means were £50 or under, 40% for means exceeding £50 and under £130, and 30% for means exceeding £130 and under £200. The 1924 Pensions (Increase) Act raised the rate of percentage increases to 70% for annual means under £25 and made a few other changes to the increases already granted.

2. The essential principle underlying the British approach was that whereas normally the pensions of former public servants were not adjusted to meet changes in circumstances after retirement, in exceptional circumstances of severe deterioration in the value of money, it was justifiable to give some help to those pensioners in serious need of help — that is, to those living on small incomes.[211] A similar approach was adopted by the new Irish administration. Pensions (Increase) Acts were passed in 1950 (the first time public service pensions were increased in Ireland), 1956, 1959, 1960 and 1964.

3. The 1950 Act, for example, granted a range of pension increases depending on the amount of annual pension received, ranging from 30% (for those on high pensions) up to 50% (for those on lower pensions). Pensions above £450 a year were excluded from the Act. To qualify, the pension had to be awarded for service ending not later than 31 October 1946.

"Campaign" for pay parity

4. Following the Second World War, the most important issue which successive Irish governments had to deal with in connection with civil service pensions was whether they should be protected against the effects of price inflation. In the late 1940s and during the 1950s different governments argued that they had no obligation to provide for formal indexation of civil service pensions and that the most that could be expected was that the position of those who had retired would be reviewed informally from time to time as circumstances dictated.

5. The Pensions (Increase) Act, 1964 covered increases granted in the 1962 and 1963 Budgets. The 1962 increases brought all pensioners who retired before the pay revision of 1 November 1955 up to the level of their equivalent colleagues who retired with the benefit of that revision. These pensions, after revision to the 1955 level, were increased by a further 6% as were pensions awarded between 1 November 1955 and 15 December 1959 (or equivalent date). Flat rate pensions were increased by 20%. The 1963 increases brought all pensioners who retired before 15 December 1959 (i.e. the date of the 7th round for civil servants) or corresponding date, up to

[210] Material in this Appendix is drawn from Hughes, G., *The Irish Civil Service Pension Scheme*, ESRI (1988), pp. 8-18 and Appendix 1.
[211] Government of Ireland, *Report of the Committee on Post Retirement Adjustments in Public Service Pensions* (1965), p. 24.

the level of their colleagues who retired immediately after those dates. Flat-rate pensions were increased by a further 5%.

6. Section 29 of the 1964 Act also provided for future indexation of pensions by means of Statutory Instrument instead of an Act of the Oireachtas.

7. Informal adjustments in pension entitlements to compensate for increases in the cost of living were thought to be unfair by civil servants and opposition parties in the Dáil, and the Minister for Finance eventually agreed in September 1964 to appoint a Committee on Post-Retirement Adjustments in Public Service Pensions with the following terms of reference:

> *To examine the principles involved in making post-retirement adjustments in public service pensions, with particular reference to (1) the cost and manner of financing these adjustments (2) the consequence of such adjustments in relation to other superannuation schemes (including those outside the public service) and to social welfare benefits, and to make recommendations.*

8. In its report of March 1965,[212] the Committee considered the pensions increase policy of Irish and British business concerns as well as practice in the public service in other countries. They concluded that arrangements had been made in a number of other states for regular reviews of pensions and for granting increases in pensions to offset falls in purchasing power. A small number of companies in Ireland had similar arrangements. Thus, there were ample precedents for regular review of pensions and for providing appropriate pension increases. Two methods were available: cost of living or full parity with current pensions. The Committee concluded that parity was not acceptable, principally on grounds of cost:

> *We do not agree that as compared with other classes in the community public service pensioners should be granted preferential treatment of this kind and at such a cost. Most pension schemes are designed to provide a pension based upon retiring pay or average pay over a certain number of years of service. Under such schemes no liability is undertaken for a pension other than that calculated on pensionable service rendered and actual pay received. There is, therefore, no financial justification for regular adjustment of pension by reference to pay increases given to serving staff after the pensioner has retired.*[213]

9. The Committee recommended that pensions be increased to an extent sufficient to offset increases in the CPI that had occurred from the dates of the general rounds of pay increases to which pensions were currently related, to the date of the most recent general pay increase. They argued that this would have the effect of maintaining the purchasing power of pensions and of protecting pensioners from the effects of increases in living costs. It would meet in a reasonable way the problem of post-retirement adjustments in public service pensions and discharge equitably any obligation the State had to its former servants.[214]

10. Recognising the pressure on state-sponsored companies and private sector companies to implement similar pension increase arrangements, the Committee suggested that it would be appropriate for the additional liability arising to be met by increasing the existing pension contributions from employers and employees. The Committee added that pension increases to offset cost of living increases represented such a valuable improvement in the pension terms of public servants that the payment of some premium or contribution for the improvement appeared to be justified (a minority of the Committee disagreed). As contributions were not generally payable across the whole public service, they recommended that in return for pension increases

[212] Government of Ireland, *Report of the Committee on Post-Retirement Adjustments in Public Service Pensions*, 1965.
[213] *ibid.,* p. 18.
[214] *ibid.,* p. 19.

future pension awards be based on pay averaged over the last three years of service rather than on pay at retirement.[215]

Commitments made in Budget speeches

11. The campaign for pay parity continued and the Committee's recommendations were overtaken by subsequent developments. In the *1969 Budget*, the Minister for Finance stated that certain increases to public service pensions had been made but noted that those longest retired had the most immediate needs because of the lower pay rates to which their pensions were related. However, full parity with pensions of those currently retiring, as sought by pensioner representatives, would be quite expensive. The Minister stated that while he could not give full effect to parity at that time, he had decided to adopt it in principle and to move towards it over a number of years. As a start, the pensions of those who retired before the general pay revision of 1 February 1964 would be brought up to the level of those who retired with the benefit of that revision.

12. In the *1972 Budget*, the Minister stated that it had not been possible because of cost to implement fully the principle of parity which was accepted by Government in 1969. Since then, three increases had been granted, bringing pensions up to a level based on June 1969 pay rates. The Minister said:

> *it gives me particular pleasure to announce that I am granting parity to public service pensioners by bringing their pensions up to levels related to pay as on 1 January 1972, the date of the most recent general revision of public service pay.*

The overall average of the pension increase was around 28%.

13. The *1973 Budget* continued parity, with pensions being revised by reference to 1 July rates of pay with effect from 1 October. The *1974 Budget* eliminated the time lag. Thus, revised pensions would be paid as from 1 July each year by reference to the rates of pay in force on that date. The annual increases were implemented by means of Pensions (Increase) Regulations as provided for under Section 29 of the Pensions (Increase) Act, 1964.

14. In the *1984 Budget*, the Minister noted that there had been pressure for many years for full parity, i.e. pensions to be revised with effect from the **same date** as the pay increase. As an exceptional measure the previous year, in the context of negotiations on the first phase of the Public Service Pay Agreement, it had been agreed that that increase would apply with effect from 1 September 1983 to pensions in payment on that date (rather than 1 July 1984 as would otherwise have been the case). The Budget announced that in the case of general pay increases such as the second phase of the Public Service Pay Agreement, full parity would be implemented from 1 February 1984 onward. So far as grade or special increases were concerned, parity would be dealt with in the context of negotiations for the next pay round and the new arrangements would be implemented in 1985. It was stated that negotiators would, of course, have to take these commitments into account in costing future pay claims.

15. The *1986 Budget* noted that certain superannuation matters — including parity on grade and special increases — had arisen during the recent pay negotiations. It announced the Government's decision that, in the context of the phasing arrangements set out in the package agreed with the unions, full pension parity in relation to special increases would be introduced with effect from 1 July 1986.

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[215] *ibid.*, p. 22.

APPENDIX 16.2

Public Service Earnings Index

1. This note discusses the issues arising in developing the Public Service Earnings Index (see Section 16.5) which the Commission recommends should be used as a basis for increasing public service pensions in line with increases of earnings of all public servants.

New index or major modifications to current index?

2. The steps involved in compiling a new index or in making *fundamental* changes to the current CSO public sector earnings index would be similar to those involved in compiling the current index. The main tasks involved would be as follows:

- identifying the data to be collected;
- selecting the public service groups to be used as the basis for the calculations;
- collecting the data;
- checking the data;
- writing the computer programs; and
- testing the procedures.

3. Experience in the many years spent in developing the public sector earnings index has highlighted the difficulties involved in carrying out the above tasks. These difficulties include problems with the diversity of computer systems in the public sector, the number of grades, non-respondents and problems in checking data. A clear commitment to the index would be needed to ensure the full co-operation of the various public sector groups in providing reliable data, and substantial resources would also need to be made available to enable the extensive work involved to be carried out. Even with this commitment it could take years to develop a new index. Accordingly, we examined instead how a public service earnings index could be developed by making a number of *minor* modifications to the existing CSO public sector earnings index.

Current index

4. The following paragraphs discuss a number of the features of the current index which might cause difficulties in an ideal pension increase structure. We propose some modifications to the current index which should enable the CSO to produce an additional index figure which would be more suitable for pensions purposes. It might be noted that the discussion below concentrates on problems with the current index. For each problem, it is important to consider the significance or otherwise in practice of the problem being discussed.

Sources of data

5. Data are collected on aggregate earnings and on employment in a variety of formats; these formats include computer printouts, special forms and electronic media; details on individual members are not collected. Given the aggregate nature of the data, the CSO are limited in the modifications they can make to the current index. To make some desirable modifications would require the development of a new system.

Coverage of the current index

6. At present, the CSO index covers all of the public sector (including the commercial state companies) with the exception of the health sector. For the purposes of the Public Service Earnings Index, however, it would be necessary to amend the existing index by integrating the health sector while excluding the commercial state companies. As aggregate earnings figures are collected from all the major public service groups and from a representative sample of other public service groups, we envisage that the CSO should be in a position in due course to devise an index to address these points.

Earnings included in the current index

7. Earnings included in the current index represent the gross amount payable to employees and include all the usual payments with the exception of *back-pay*. Changes in the amount of overtime would therefore be reflected in the index level. The CSO could produce an index which excluded the overtime paid to Prison Officers and to Gardaí. It is not possible using the data collected at present to exclude overtime for other groups. However, the level of overtime to other public service groups is low and relatively stable and an index which excludes overtime payments to the Gardaí and to Prison Officers should be sufficient in this regard. The inclusion of other forms of non-pensionable pay should not be a significant factor.

Methodology

8. The current index is based on a weighted average of increases in pay for each public service category. It covers all increases in pay, including general pay increases, special pay increases and increases to individuals arising from promotion or from incremental scale progression. The Public Service Earnings Index should in theory only include those increases which would have been paid to pensioners under the current pay parity system. The present CSO index system cannot exclude particular forms of pay increases. However, given the continuation of existing staffing structures, we consider that it would not be unreasonable to pay pensioners the total average increase in pay in the public service.

Delays in publishing the index

9. At present, the CSO index is published about six months after the quarter to which it refers. For example, the index for September 1998 was published in April 1999. Given the large amount of data that has to be collected and processed, a time-lag will always occur. We expect that it should be possible to reduce the period required to produce the index to around three months. If a modified index is to form the basis for increasing pensions, it should be possible to encourage public service bodies to return data more speedily.

Persons covered by the index

10. All categories of staff are covered by the current index. It might be argued that the Public Service Earnings Index should be based on the pay of pensionable staff only. At present, the total earnings of non-pensionable staff is only a tiny proportion of the overall public service pensionable pay bill and in future there are likely to be very few non-pensionable public servants in the public service. (Most non-pensionable public servants are part-timers and many of these will become pensionable within a short period.)

Changes in the index arising from recruitment, withdrawals, increments and promotions

11. Ideally, the pensions index should not be affected by patterns of recruitment or withdrawals, nor by promotions or increments. There are three possible problems with the current CSO index under this heading:

- significant recruitment of staff can depress the value of the index;
- significant retirements will tend to inflate the index if promotions follow a retirement and if those retiring are not replaced by new recruits;
- the current index reflects fully pay increases arising from increments and promotions.

12. It is not possible to make any adjustment to the current index to improve matters. If the number of persons on each point of each scale remain fixed from year to year then none of the above three characteristics would affect the index. However, the public service at present is not in this state but it is impossible to measure the effect which of any one of these characteristics have had on the index to date. Based on an examination of the changes in the index to date, it appears that the **cumulative** effect of the above has not had a significant effect on the **overall** index. It appears likely that for the overall public service the three characteristics listed above will impact only to a minor extent on the index. If there were to be a fundamental change in staffing structures, however, some special adjustment might have to be considered.

13. A separate problem relates to seasonal changes in the number of staff in certain public service bodies, e.g. changes in the number of part-time staff in the education sector. There would be some difficulty in obtaining the information needed to eliminate this problem. However, such seasonal changes are unlikely to have a significant effect on the overall index level.

Timing of pay increases

14. Pay increases are reflected in the current index only when they are paid. This leads to two possible issues if pensions are to be increased in line with an index:

(i) effective date of pension increases; a public service earnings index figure which is published in December and which relates to a six month period to September will be based on increases which, on average, take place in June/July; each increase could be backdated to the mid-point of the relevant index period;

(ii) pay increases to serving staff which include some back-pay; the current index does not include earnings representing backdating of pay increases; for example, if a pay increase is actually paid on 1 July but backdated, then this increase will be reflected in the September quarter index and none of the previous index figures will be adjusted.

15. Public service pay agreements — in particular, special pay increases — often include a substantial amount of back pay. A rough estimate is that, on average, back pay amounting to 1.5% of pay was paid to serving staff during each six month period in the years 1996 to 1998; this would represent an annual payment of around £250 to an average pensioner. If no provision was included for the payment of back pay, then any delays in concluding future pay agreements would discriminate unfairly against pensioners. It would appear to be essential that in developing the Public Service Earnings Index, an allowance for back pay should be included as part of the system. At present, the CSO do not collect information on arrears paid to public servants, and it would be necessary for this information to be collected in the future.

16. For each index period, two figures would be produced:

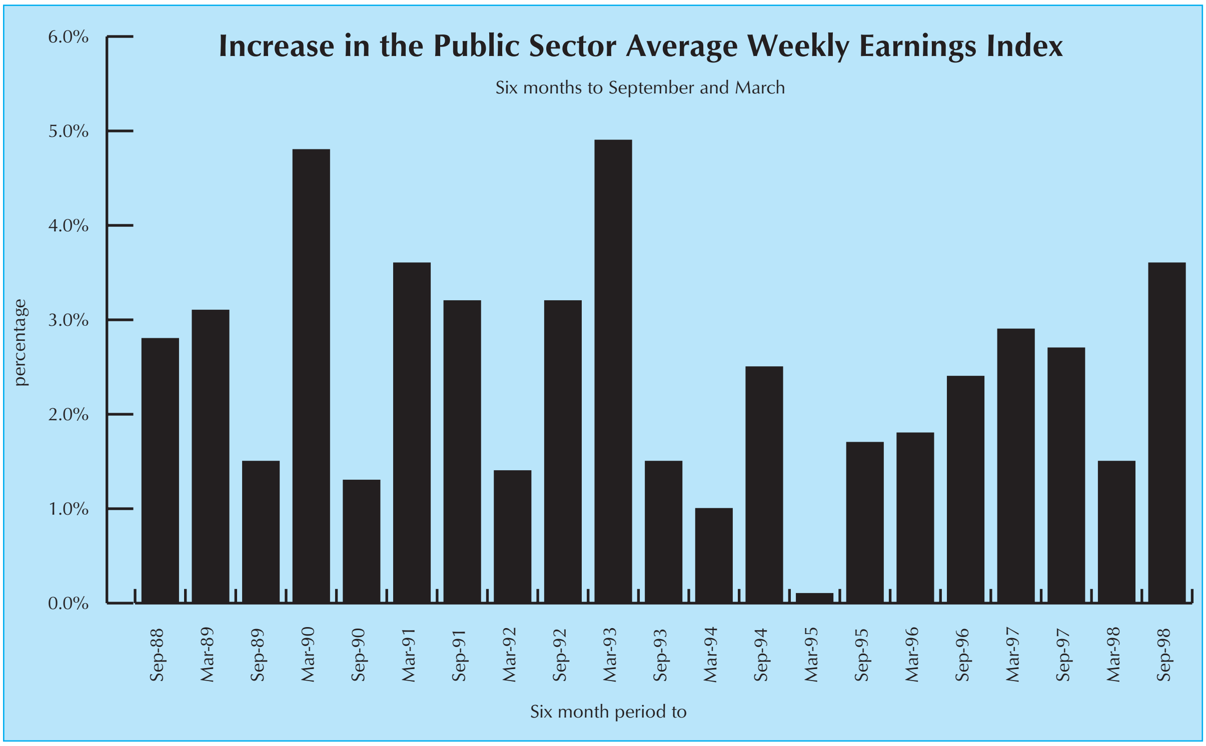
(i) an index which would be used as the basis of increasing each pension;

(ii) an *arrears* percentage which would be converted into a lump sum payment (back pay) to each pensioner.

Frequency of calculating the Public Service Earnings Index

17. The current index is published quarterly in March, June, September and December of each year. We envisage that the new Public Service Earnings Index would be published on a twice-yearly basis.

18. In the period 1988-98, the overall index fell in seven of the 42 quarterly periods; each fall is likely to have been due to significant recruitment or retirements during the period in question. However, the index did not fall over any six month period. The graph below shows changes in the index over the six month period to March and September of each year. It would probably be reasonable to include a guarantee that if the Public Service Earnings Index fell in any period, pensions would remain unchanged until the index rose above its previous highest level.



19. At present, the public sector average earnings index comprises twenty-one individual indices published each quarter with each based on changes in a particular sector of the public sector. The new system would only require one extra index. This new index, the Public Service Earnings Index, would cover the overall public service. We would envisage that no new indices for individual sectors would be published.

Cost

20. The new index system would provide pay parity in line with the average pay increase to serving staff. In theory, the average index increase could be slightly different to increases arising under the current pay parity system. The reason for the possible difference is that the composition of pensioners in terms of grade/point of scale at retirement is different to the composition of serving staff. However, the increases awarded and the total cost involved should be broadly the same under both systems.

CHAPTER 17

Integration with State Social Insurance Benefits and Low Levels of Occupational Pension

17.1 Introduction

17.1.1 Integration is a central feature of public service pension schemes and of the majority of defined benefit schemes in the private sector. It is also the practice in many other countries. Integration is the arrangement whereby, in the case of public servants who are fully covered for Pay-Related Social Insurance (PRSI), the Social Welfare pension is merged (or coordinated, or integrated) with the occupational pension to provide a combined pension which is both reasonable, by reference to pensionable pay and the period in employment, and affordable to both employees and employers. In effect, integration avoids *double pensioning* that tranche of income which is already *pensioned* by the employer's and employee's PRSI contributions. The Commission accepts that integration is a fundamental component in the public service pensions framework and is strongly of the view that it should be continued.

17.1.2 However, as shown in Section 11.6, integration can have a substantial impact on the occupational pensions of public servants who retire on relatively low levels of pay. In this Chapter, the Commission considers the question of integration with State Social Insurance benefits and low levels of occupational pension. We review the arguments for and against adjusting aspects of the integration formula and consider a number of possible approaches. Finally, we recommend an adjustment to the manner in which integration is implemented which would have the effect of improving the rates of occupational pension for the groups affected.

17.1.3 We deal with integration in the case of part-time public servants separately in Chapter 18.

17.2 Background

17.2.1 The way in which integration operates in public service schemes ensures that for a public servant with 40 years' service, the combination of Social Insurance and occupational pension equals 50% of pensionable remuneration. This objective is achieved by deducting twice the single rate of Old Age (Contributory) Pension (OACP) from pensionable remuneration before calculating the occupational pension entitlement. Table 17.1 shows the effect of this for two public servants, A and B, each paying full PRSI, each with 40 years' service, but retiring on different levels of pensionable remuneration — £250 per week and £500 per week, respectively. The figure used for the OACP is the rate applying from May 2000, i.e. £96 per week.

Table 17.1: Calculation of occupational pension

Pensionable remuneration	Calculation of occupational pension	Occupational pension	Total pension including OACP
£250 p.w. (A)	£250 – (2 × 96) = £58 × $^{40}/_{80}$	£29 p.w.	£125 p.w. (£29 + £96)
£500 p.w. (B)	£500 – (2 × 96) = £308 × $^{40}/_{80}$	£154 p.w.	£250 p.w. (£154 + £96)

17.2.2 From the above Table it can be seen that although the *total* pension of both A and B is 50% of their pensionable remuneration, A's occupational pension forms a far lower proportion of the total than B's (23% compared with 62%). This is illustrated further in Table 17.2.

17.2.3 The occupational pension makes up a significantly greater portion of the overall pension for the higher paid compared with the lower paid public servant, no matter what level of service has been accrued. Table 17.2 shows an example of this for the two public servants discussed earlier, assuming service at retirement of 40 years, and 25 years, respectively.

Table 17.2: Combined occupational pension and OACP at different levels of pensionable remuneration and pensionable service

Pensionable remuneration	(A) £250 per week		(B) £500 per week	
Length of service	40 years	25 years	40 years	25 years
Occupational pension	£29 p.w.	£18 p.w.	£154 p.w.	£96 p.w.
% of pensionable remuneration	12%	7%	31%	19%
Occupational pension plus OACP	£125 p.w.	£114 p.w.	£250 p.w.	£192 p.w.
% of pensionable remuneration	50%	46%	50%	38%

17.2.4 It should be noted that the individuals in the above examples also receive a significant lump sum payment at retirement which is not subject to integration. The retirement lump sum is a valuable component of public service pension scheme benefits and so should be considered when examining the question of integration in a public service context.

17.2.5 Integration also affects employee pension contributions. For groups in schemes which are contributory for main pension benefits, employee pension contributions are deducted from pay at the rate of $3\frac{1}{2}$% of net remuneration (i.e. remuneration less twice the rate of OACP) towards pension and $1\frac{1}{2}$% of remuneration towards lump sum. Table 17.3 sets out the level of pension contributions paid by both public servants in the above examples (the contribution towards retirement lump sum is not shown). The level of pension contribution is related to the size of the prospective occupational pension payable: thus, B (who earns £500 per week) pays a significantly higher weekly pension contribution, proportionally, than A (who earns £250 per week). This point is not always recognised.

Table 17.3: Occupational pension contribution (per week)

Remuneration	Pension contribution*	% of remuneration
(A) £250 p.w.	£2.03 p.w.	0.8%
(B) £500 p.w.	£10.78 p.w	2.2%

* Excluding contribution in respect of lump sum and spouses' and children's benefits.

17.2.6 While the aim of integration is to ensure that the combination of Social Insurance and occupational pension for a public servant in full PRSI class equals 50% of pensionable remuneration (after 40 years' service), the same outcome as for a public servant in modified PRSI class, it should be noted that the total pension benefit is more favourable for the public servant paying full PRSI class in a number of circumstances:

(i) where earnings at retirement are below twice the rate of OACP;[216]

(ii) where service is less than 40 years (if individual (A) from Table 17.2 had been in modified PRSI class, his or her occupational pension would have been 25/80ths of £250 after 25 years' service, i.e. £78 per week compared with total pension of £114 per week in the example);

(iii) where the individual is in receipt of a dependant's addition on top of the Social Insurance benefit for which he or she qualifies.[217]

17.2.7 Integration applies only to public servants who are in full PRSI class and are thereby entitled to receive Social Insurance benefits.[218] At present, most of these (around 39,000 public servants) are non-established civil servants or are employed in non-officer grades in the health, education and local authority sectors. The issue of integration and low pay is of particular relevance to this group — both to pensioners and to serving staff. However, in future, the proportion of public servants in full PRSI class and therefore subject to integration will increase (eventually to 100%) on foot of the Government decision to apply full PRSI to *all* new entrants taking up employment in the public service on or after 6 April 1995.

17.3 Arguments against adjustment of integration for employees in receipt of relatively low levels of pay

17.3.1 The Commission considered various arguments against making any adjustment to the way integration operates, or introducing a minimum occupational pension, so as to improve the occupational pensions of public servants retiring on relatively low levels of pay. These arguments include:

(i) the purpose of introducing a minimum occupational pension would be to improve the income of public servants retiring on relatively low rates of pay. However, this can be seen as primarily the role of the Social Welfare system, rather than of occupational pension schemes;

(ii) low occupational pensions are the result of low pay (and, in many cases, short service), not pension structures *per se*. It is unreasonable to argue that pension systems should be expected to compensate for the wider issues of low pay, short service and incomes adequacy;

(iii) payment of a minimum pension would be contrary to a central objective of public service pension schemes, namely, to provide a total pension of one-half of retiring pay for a person retiring with 40 years' service (a retirement lump sum is also payable). If the purpose is to relate pensions to retiring pay, as distinct from some measure of adequacy, a minimum pension could cause *overpensioning*, in the sense that benefits

[216] This point was noted by the Pensions Board in *Securing Retirement Income* (1998), p. 179.

[217] The *Actuarial Review of Social Welfare Pensions* (1997) found that the proportion of pensioners qualifying for adult dependants' additions to Retirement Pension/OACP and Invalidity Pension in 1996 was 27% and 31%, respectively, and that this proportion was expected to fall steadily in time, to around 13% and 25%, respectively, by 2056 (p. 53).

[218] Enlisted personnel in the Defence Forces who are fully insured for almost all benefits under the Social Welfare Acts are also subject to a partial form of integration (see Paragraphs 3.7.20-3.7.21).

paid to retired employees could form a high proportion of retiring pay — even higher, in some cases — than the take-home pay of those at work;

(iv) the relative position of public servants paying full PRSI and the majority of public servants who still pay modified rates of PRSI must be borne in mind. Integration ensures that the aggregate benefits payable to both groups is broadly similar (as we show in Paragraph 17.2.6, the pensions of the full PRSI group are more favourable in certain circumstances). A change to the integration formula or the provision of a minimum pension would improve the position of the full PRSI group relative to the modified group, and this, too, would be seen as unfair (especially as between individuals on similar pay rates);

(v) any adjustment to pension arrangements aimed at improving future occupational pensions would also have to be applied to those currently in receipt of pension. Depending on the nature of the change made, the additional cost involved could be significant;

(vi) there appear to be very few examples from the private sector of payment of a minimum pension or the adjustment of integration to favour those retiring on relatively low levels of pay. An independent consultancy report for the Health Service Employers' Agency in December 1996[219] concluded that pension arrangements for the public service groups affected by integration were *''significantly more valuable''* than those available in the private sector. Therefore, pension improvements for public servants — even those in receipt of relatively low levels of pay at retirement — could be seen as further widening the existing difference in standards and quality of pensions coverage.

17.4 Arguments in favour of adjustment to integration

17.4.1 The Commission also considered various arguments in favour of changing the operation of integration to the benefit of public servants retiring on relatively low levels of pay, including the following:

(i) the pensioners who see themselves as adversely affected by integration are in receipt of average rates of occupational pension which are quite low (see Appendix 11.4). While the Social Insurance pension must be added to give the total pensions picture, most of those affected consider that a Social Insurance pension is an entitlement on foot of their PRSI contributions, and that it should not affect their occupational pensions position to such a significant extent. Moreover, increases in the OACP are seen by this group as worsening rather than improving their occupational pension and hence their rewards for work;

(ii) the *value for money* of occupational pension benefits received, relative to the employee contribution made, is much greater for those who have favourable career progression and who retire on a high level of pay compared with those who have a low salary and little career progression (see Paragraph 14.2.3 (ii)). In addition, in the case of a contributory scheme, contributions may have been paid on the basis of a higher level of remuneration than actually applies at the point of retirement;

[219] Report to the Health Service Employers' Agency, ''Investigation of Non-Officers Pension Arrangements'' (December 1996) prepared by Mercer Ltd.

(iii) while the Pensions Board report on the National Pensions Policy Initiative stopped short of making definitive recommendations on integration (other than in relation to better information and the introduction of a contributions test),[220] it considered a number of possible options for improving the occupational pension benefits of lower-paid workers by minimising the negative impact of integration on their pensions — e.g. by providing a minimum pension or by setting a floor on pensionable earnings — and it suggested that these options might be negotiated between management and unions;[221]

(iv) As regards the comparison of the relative position of public servants paying full PRSI with those paying modified PRSI, it should be noted that:

- the comparison is not altogether valid as it suggests that, in general, those paying modified PRSI will retire on the same salary point and with the same service as those paying full PRSI. In fact, the generality of modified PRSI groups enjoy better career and salary progression compared with most of the existing full PRSI groups;
- in certain respects, the position of public servants in full PRSI class is already different from that of public servants in modified PRSI class. For example, where service is less than 40 years, the former will receive a greater overall pension than the latter (with the same service and final pay);
- the comparison with public servants paying modified PRSI will become irrelevant in the long run as this group reduces in size over time;

(v) public servants in receipt of relatively low levels of earnings, who can least afford it, may feel unable to pay into AVCs or the purchase scheme to enhance their pension benefits;

(vi) most other countries have either a higher level of State pension or a State supplementary pension system (such as SERPS in the UK) which specifically seeks to improve the pension position of those who retire on relatively low levels of pay. Ireland is not in that position, so it would seem reasonable that the question of using the occupational system to improve the pensions of those in receipt of relatively low levels of pay should arise.

17.5 Modification to integration to address the pensions position of public servants who retire on relatively low levels of pay

17.5.1 The Commission examined a number of possible modifications to integration which would have the effect of improving the occupational pensions position of public servants retiring on relatively low levels of pay.

Modifications considered

17.5.2 As already indicated, the Commission is supportive of integration as a cost-effective way of providing reasonable, income-related pensions for the majority of public servants. An across-the-board removal of integration would result in a major increase in pension for all public servants in full PRSI class, and would be seen as resulting in *overpensioning* in many cases. As stated in

[220] The Pensions Board, *Securing Retirement Income* (May 1998), p. 182. The report recommended that contributory defined benefit schemes should be required to provide minimum benefit levels whose value equated to 120% of the member's ordinary personal contributions, with interest thereon.

[221] The Pensions Board, *Securing Retirement Income* (May 1998), pp. 176-177, p. 181.

Paragraph 11.4.10, the Commission believes that the retirement income objective of public service pensions, i.e. pension of 50% of final earnings and lump sum of one-and-a-half times final earnings after 40 years' service, is both reasonable and affordable. To go beyond this objective would cause a major escalation in future pension costs well in excess of existing projections.[222]

17.5.3 An alternative to the removal of integration would be to modify it by reducing the level of the Social Welfare offset from twice to, say, one-and-a-half times, or once, the rate of OACP. The Commission cannot support such an approach for the reasons set out in Paragraph 17.5.2. It is our view that any adjustment to integration should be targeted at the group where the greatest need lies, i.e. to address the pension position of public servants retiring on relatively low levels of pay, rather than to increase the pensions of *all* public servants in full PRSI class, which this particular modification would do.

17.5.4 The Commission also rejected the idea of a flat-rate approach which was unrelated to the occupational pension formula. This might involve a minimum pension which would be payable to all, irrespective of length of service, or a minimum pension payable by reference to length of service. The Commission considered that neither approach would have any inherent logic or coherence, and could also lead to difficulties at the *cut-off* points.

17.5.5 We examined a number of other proposals including the list of suggestions set out in the report of the National Pensions Policy Initiative (see Paragraph 17.4.1 (iii)). Most of these involved changes to the pension calculation formula. Another suggestion was to leave the formula unchanged but to focus on increasing pensionable remuneration by the inclusion of non-pensionable allowances such as overtime. However, we believe that there are a number of reasons why this option would not be fair or feasible, including the fact that overtime is usually worked on a casual basis and is not necessarily carried out by the employees concerned on an equal basis. Making it pensionable would obviously create an incentive to work additional overtime prior to retirement in order to boost pension, and this may not always be equitable and/or desirable (we discuss this matter at Paragraphs 22.9.8-22.9.15). There are similar difficulties with including other elements of pay that are not already pensionable in the calculation of pension benefits.

Criteria to be met by adjustment to integration

17.5.6 The Commission therefore looked to other possible forms of modification to integration and, in considering the range of available options to improve the pensions position of those retiring on relatively low levels of pay, we developed the following criteria to guide our approach:

(i) the adjustment should focus on relatively low levels of final pay, rather than low levels of service. Thus, the trigger for any modifying mechanism would be the level of pensionable remuneration at retirement;

(ii) public servants retiring on levels of pensionable remuneration above the *cut-off* figure should be unaffected by the change. Therefore, no extra cost would arise in respect of the majority of public servants and the additional expenditure would be directed entirely to those retiring on relatively low levels of pay;

[222] We set out the full cost implications of removing integration in Paragraphs 10.4.20-10.4.22 above: if the change were applied to all serving public servants, annual expenditure on pensions would, in due course, be up to 16% higher than it would otherwise have been.

(iii) the adjustment should be done within the overall structure of public service pension benefits. Therefore, provided an individual qualified for it, the scale of the adjustment would vary with service, in the same way as pension benefits generally;

(iv) there should be no complications arising out of equality provisions, particularly in relation to part-time employees; in other words, the formula should operate on a pro rata basis according to hours worked (see Chapter 18);

(v) the adjustment should be automatic and capable of indexation over time.

17.5.7 Having regard to these criteria, the Commission developed a new form of integration which would have the effect of changing the pension calculation formula for all public servants in such a way as to ensure that an increase in the actual rate of occupational pension would occur only for public servants retiring on levels of pensionable remuneration below a certain cut-off point. We outline this alternative approach to integration below.

Amended calculation of occupational pension

17.5.8 Under current arrangements, public servants whose benefits are integrated receive a retirement pension based on an accrual rate of 1/80th of net pensionable remuneration, i.e. pensionable remuneration less twice the rate of OACP. (They also receive a retirement lump sum.) In the case of contributory main schemes, the contribution rate during service consists of $3\frac{1}{2}$% of net remuneration for pension and $1\frac{1}{2}$% of remuneration for lump sum.

17.5.9 Under the *amended pension calculation formula*, an accrual rate of 1/240th would be applied to pensionable remuneration below a limit of three times the rate of OACP, and an accrual rate of 1/80th would be applied to pensionable remuneration in excess of this limit.[223] Based on the weekly OACP rate of £96 (May 2000), this would give a cut-off point of £15,028 per annum. The cut-off point would be increased in line with future changes in the rate of OACP.[224] The lump sum calculation under the new system would remain as at present (i.e. 3/80ths of pensionable remuneration per year of service).

17.5.10 In Table 17.4, we show the effect of the amended formula for two public servants earning £250 and £500 per week, each with 40 years' service at retirement. The first, A, is in receipt of pensionable remuneration which is less than 3 times the rate of the OACP (£288 per week). Thus, the entire occupational pension is calculated by reference to the 240th accrual rate, giving a weekly pension of £42. This compares with an occupational pension of £29 per week under existing arrangements (see Table 17.1). The second public servant, B, whose income is in excess of the threshold of three times the rate of OACP, has occupational pension calculated on the first £288 of weekly pensionable remuneration by reference to the 240th accrual rate, and the balance by reference to the 80th accrual rate. Under this formula, the total occupational pension entitlement of £154 per week is the same as it would be under existing arrangements, as is the case for anyone whose pensionable remuneration is in excess of the cut-off point. We would envisage that pensioners would also be affected by the change in the pension calculation formula.

[223] This method of applying integration would be similar to the *step rate* formula which applies in private sector pension schemes in Germany (see Paragraph 9.3.11).

[224] If, for example, the OACP were £100 per week, the cut-off point would be £300 per week, or £15,654 per annum; if the OACP were £115 per week, the cut-off point would be £345 per week, or £18,002 per annum.

Table 17.4: Amended pension calculation formula

Employee	Pensionable remuneration	Length of service	Pension calculation under amended formula	Total occupational pension
A	£250 p.w.	40 years	£250 × 40/240 = £42	£42 p.w.
B	£500 p.w.	40 years	£288 × 40/240 = £48 **plus** £212 × 40/80 = £106	£154 p.w.

Effects of the modification to integration

17.5.11 In Table 17.5, we show the effect of the modification to integration for public servants retiring on pensionable remuneration of between £9,000 and £15,000 per annum; the figures are based on the May 2000 rate of OACP. The examples are for a public servant with 40 years' service at retirement; the pension for shorter periods of service would be proportionately less.

17.5.12 For example, for a person retiring with 40 years' service, whose pensionable remuneration was £12,000 per annum, the annual occupational pension would increase from £991 to £2,000 per annum; if service at retirement was 20 years, then the corresponding figures would be £495 and £1,000 per annum, respectively.

17.5.13 As the figures show, all individuals whose pensionable earning are less than £15,028 per annum at retirement would gain from the proposal. The lower the level of pensionable remuneration, the greater the gain from the change. At a given level of pensionable remuneration, the percentage increase in pension would be the same at all service levels.

Table 17.5: Effect of the proposed change to pension calculation formula for a range of different amounts of pensionable remuneration

Pensionable remuneration	Occupational pension under existing system	Under proposed new system			
		Occupational Pension	Increase in occupational pension	Total pension, including OACP	Total pension as % of pensionable remuneration
(p.a.)	(p.a.)	(p.a.)	(p.a.)	(p.a.)	(%)
£9,000	£0	£1,500	£1,500	£6,509	72%
£10,000	£0	£1,667	£1,667	£6,676	67%
£11,000	£491	£1,833	£1,342	£6,842	62%
£12,000	£991	£2,000	£1,009	£7,009	58%
£13,000	£1,491	£2,167	£676	£7,176	55%
£14,000	£1,991	£2,333	£342	£7,342	52%
£15,000	£2,491	£2,500	£9	£7,509	50%
£15,028	£2,505	£2,505	£0	£7,514	50%

Note: Assuming a full-time employee with 40 years' service at retirement.

Numbers affected by the change

17.5.14 As indicated above, this proposal would result in improved occupational pension in the case of those with pensionable remuneration below the cut-off figure of three times the rate of OACP at the time that pension came to be calculated on retirement or death. In general, the public servants affected would be those who enter the public service on relatively low levels of pay, who receive little or no career increase, and who are not in receipt of large amounts of pensionable allowances at retirement. Almost invariably, they would come from amongst the non-established groups in the civil service and non-officers in the health, education and local authority sectors. These groups were in full PRSI class and subject to integration prior to the Government's decision to extend full PRSI cover to all new entrants to the public service. Salary maxima for a number of relevant grades (1 April 2000) are as follows:

Civil service	
General Operative (Dublin)	£12,653 p.a.
Services Officer	£13,953 p.a.
Health service	
Domestic/Porters (Group 1 of non-nursing scales)	£13,315 p.a.

17.5.15 The total number of serving public servants in these areas was approximately 39,000 in 1997; however, many of these will retire on pay above the cut-off point of three times the rate of OACP. It should also be noted that a critical factor impacting on the numbers who would, in fact, benefit from the change is the rate of increase in the OACP in the future as compared with future rates of pay increases for the grades concerned.

17.5.16 Table 17.6 presents an estimate of the expected distribution of pay at retirement in areas of the public service integrated before 5 April 1995, based on pay rates as at April 2000. According to these figures, it is expected that 57% of those retiring in these areas will be in receipt of pay below £15,028 per annum and would therefore benefit from this new formula. The percentage of current staff on pay below this level is somewhat greater than 57% at present; however, some of these will benefit from career-related increases in pay which will bring them above this threshold.

Table 17.6: Expected distribution of pay at retirement in areas of public service integrated before 5 April 1995

Pay category	Percentage
Under £13,000 per annum	27%
£13,000 per annum to £14,000 per annum	20%
£14,000 per annum to £15,000 per annum	10%
Over £15,000 per annum	43%

If the above pattern of pay distribution changes, and/or the relationship between increases in pay and increases in the rate of OACP changes, then the proportion of public servants who would benefit from the new formula would be different from that indicated.

Cost of proposal

17.5.17 The Commission attempted to quantify the cost of making this adjustment to integration. The cost of applying the change to serving staff would depend on a number of factors such as:

- current pay distribution;
- current rate of OACP;
- service at retirement of the groups affected;
- salary progression including any future changes in pensionable allowances;
- the relationship between future pay increases and future increases in the OACP.

17.5.18 Most of the estimated 203,000 pensionable public servants are on incremental scales where the maximum point is well in excess of £15,028 per annum. As noted above, almost all of those likely to retire on pay below this amount are in areas of the public service where integration applied prior to April 1995. Of the approximately 39,000 employees in these areas, many are already on pay above £15,028 per annum.

17.5.19 The cost of the proposal in relation to serving public servants is critically dependent on the distribution of pay at retirement relative to the rate of OACP. Assuming that pay and OACP increase at the same rate, it is estimated that introducing this change for serving staff would result in a small increase in the pensions bill for a number of years, gradually rising to an overall increase of around £13 million per annum, in constant (1997) price terms, in about 40 years' time.

17.5.20 There are approximately 18,000 pensions in payment which relate to areas in which full PRSI applied prior to April 1995.[225] The Commission has estimated that the cost of extending the proposal to the current group of pensioners is likely to be of the order of £1 million to £2 million in year one, and that the annual cost would fall gradually over time, in constant (1997) price terms.

17.5.21 In summary, the costs associated with the proposed formula, if applied to serving staff and current pensioners, would result in an increase of around £2 million in year one, rising, in constant (1997) price terms, to an annual increase of around £13 million in about 40 years' time if the rate of OACP is fixed relative to pay.[226]

Effect on employee contribution rates

17.5.22 Under existing arrangements, there is an equivalence in the base used in the calculation of pension benefits and the calculation of periodic contributions (i.e. remuneration less twice the rate of OACP).[227] Given the proposed improvement in the method of calculating occupational pension, the Commission considered the question of whether or not a new contribution formula should also be introduced which would have the effect of increasing the level of employee contributions.

17.5.23 One option would be to require additional contributions from public servants who would benefit from the new formula, i.e. those retiring on pensionable remuneration below the limit of three times the rate of OACP. We rejected this option on the basis that it would probably have to be implemented by means of lump sum deduction from retirement benefits. In addition, we considered that it would be inappropriate to make a once-off adjustment to the pension calculation formula which was aimed at improving the pension position of those retiring on relatively low levels of pay while at the same time charging extra contributions for the additional benefit.

17.5.24 A second option would be to increase the contribution rate for all public servants, not just those who would benefit from the new formula. However, given the once-off nature of the adjustment, and in the context of the Commission's recommendations on public service pensions as a whole, we decided not to proceed with a recommendation of this nature.

[225] As noted in Paragraph 3.4.5, pensions payable under the Local Government Superannuation Scheme in respect of non-officers are integrated only in respect of service after May 1977.

[226] If the rate of OACP were to increase more quickly than pay, then the costs associated with this proposal would also increase; for example, if the current rate of OACP were £115 per week instead of £96 per week, then the cost of introducing this proposal would rise to around £40 million per annum, in constant (1997) price terms, in about 40 years' time.

[227] It should be noted that not all groups which were in full PRSI class and subject to integration prior to April 1995 are subject to a main scheme contribution (e.g. non-established civil servants, enlisted personnel in the Defence Forces).

17.5.25 Accordingly, we propose that there should be no change in the existing way of calculating pension contributions for public servants, whether above or below the cut-off point. Thus, everyone in a contributory scheme would continue to pay contributions on an integrated basis.

17.6 Conclusions and recommendations

17.6.1 Integration of occupational pensions with the Social Insurance system ensures that employers and employees can, together, provide an affordable level of occupational pension which, when combined with Social Insurance benefits, will give a total pension that bears a reasonable relationship to final earnings. The Commission accepts that integration is a fundamental component in the public service pensions framework and is strongly of the view that it should be continued. However, the Commission also recognises that for public servants who retire on relatively low levels of pay, integration can give rise to certain difficulties.

17.6.2 As noted in Chapter 14, the current final salary defined benefit pension structure for the public service works particularly to the advantage of those experiencing relatively beneficial career and salary progression. However, the operation of integration means that employees who are in receipt of relatively low levels of pay on retirement can receive a low or zero rate of occupational pension (although they will receive a retirement lump sum). This gives rise to a perception that for them the occupational pension is poor *value for money*, and that their work in the public service is inadequately reflected in their pension, as the total amount of pension may not differ substantially from the Old Age (Contributory) Pension or even the Old Age (Non-Contributory) Pension.

17.6.3 Clearly, the complete abolition of integration (which, in relative terms, would benefit the groups particularly affected by this issue the most) would result in a significant increase in pension benefits, as well as in the cost of public service pension schemes. We could not recommend such an approach. Apart from the impact on future costs, it would represent a radical recasting of the public service pensions framework. In our view, the removal of integration would impact upon the long-term viability of existing schemes, perhaps to the point where future governments might consider replacing them with defined contribution schemes.

17.6.4 The Commission examined the arguments for and against making an adjustment to integration for employees who are in receipt of relatively low levels of pay at retirement. We considered the possibility of adjusting the calculation formula in a targeted way for the benefit of those directly affected (including pensioners in receipt of integrated pensions), in the context of retaining the existing public service defined benefit pension structure.

17.6.5 Having decided that such a change is necessary, the Commission recommends that, in order to enhance the pension position of public servants in full PRSI class and subject to integration and who retire on relatively low levels of pay, the operation of integration in all public service schemes should be amended through the introduction of a new pension calculation formula as follows:

Pension to be calculated using accrual rates of:

1/240th for pensionable remuneration below three times the rate of OACP, and

1/80th for pensionable remuneration in excess of this limit.

17.6.6 This formula would result in an increased occupational pension in the case of those retiring on pensionable remuneration of less than three times the rate of OACP (i.e. £15,028 per annum, based on the May 2000 OACP rate of £96 per week), and an unchanged occupational pension for those retiring on pensionable remuneration above this limit. The Commission considers that such a cut-off level is appropriate in current circumstances having regard to the salary maxima of the various grades for whom the issue of integration and low levels of occupational pension was raised. In our view, the improvement in the pension calculation formula recommended, which is to be financed in full by the State, meets the concerns of public servants retiring on relatively low levels of pay. It would, of course, be open to individual employees to make additional contributions to SPEARS (see Chapter 19) as a means of further improving their pension situation.

17.6.7 The Commission recognises that a case could be made to increase the contribution rate of some or all public servants in order to recover at least part of the cost of the proposed change. However, for the reasons set out in Paragraphs 17.5.22-17.5.25, we have decided against making such a recommendation.

17.6.8 Under the new pension calculation formula, the cut-off point of three times the rate of OACP, currently £15,028 per annum, would be adjusted in line with future changes in the rate of OACP; each change would affect the calculation of pension for new retirements only (i.e. there would be no retrospective adjustment to existing pensions on foot of a change in OACP rates).

17.6.9 In its report, *Securing Retirement Income*, the Pensions Board recommended that the rate of OACP should be increased to 34% of average industrial earnings over a five to ten year period.[228] The Commission is conscious that if this target rate is reached, the salary point which it is recommending as the cut-off point for the calculation of improved rates of occupational pension would be equal to 102% of average industrial earnings. The Commission considers that, even though the adjustment to occupational pension tapers off very steeply as pay rises towards the cut-off point, such a high cut-off point might prove hard to justify. There are questions of principle and indeed of the cost of the proposed adjustment formula that would need to be reviewed at the point of implementation.

17.6.10 The new occupational pension calculation takes account of the Social Insurance pension not by making a deduction from pensionable remuneration as at present, but by applying two different pension accrual rates. The lower (240th) rate would apply to pensionable remuneration of up to three times the rate of OACP, while the standard 80th rate would apply to pensionable remuneration in excess of this limit. In effect, this approach regards the OACP as providing the major part of an individual's pension for pensionable remuneration up to the integration cut-off point while occupational pension provides all of the pension for pensionable remuneration in excess of the cut-off point. Where pensionable remuneration is equal to or in excess of the cut-off, the amount of occupational pension would be exactly the same as under the existing form of integration.

17.6.11 Based on the current rate of OACP of £96 per week, the new approach to integration may be represented as follows:

[228] The Pensions Board, *Securing Retirement Income* (1998), p. 88. The representative of the Minister for Finance stated (p. 116) that he was unable to support this rate (or any rate which was explicitly linked to earnings).

Table 17.7: Breakdown of Social Insurance and occupational pension provision under new pension calculation formula (based on OACP rate of £96 per week)

Portion of pensionable remuneration	Calculation of occupational pension	Social Insurance pension
For pensionable remuneration up to £288 per week, or £15,028 per annum	1/240th of pensionable remuneration per year of service	OACP (£96 p.w.)
	plus	
For pensionable remuneration in excess of £288 per week, or £15,028 per annum	1/80th of pensionable remuneration per year of service	–
Total	**Occupational pension (as above) plus OACP**	

17.6.12 In Paragraph 25.5.6, the Commission recommends that annual benefit statements be issued to public servants outlining their accrued entitlements to date. It can be argued that some of the problems with integration have to do with inadequate communication. Many public servants in full PRSI class do not appear to be aware of the manner in which their total retirement income is calculated. Thus, the focus should be on ensuring that all employees understand that their total pension is made up of two parts — the Social Insurance pension, supplemented by the employer's occupational arrangements. In addition, the current rate of OACP should in all cases be mentioned in the benefit statements. This should, we hope, go some way towards correcting the *information deficit* surrounding the integration issue.

CHAPTER 18

Pensions and Atypical Employment

18.1 Introduction

18.1.1 In Chapter 7 and Appendix 7.1, we set out the current position in relation to atypical employment in the public service and comment on the likely development of such employment in the future. We discuss some of the implications for existing occupational pension arrangements in Chapters 11 and 12.

18.1.2 Atypical working has always been a major part of public service employment. It is not clear that the numbers in atypical employment are set to increase substantially in the future, but new arrangements are currently being introduced which could have a significant impact on the position. In any event, there is now a strong emphasis on ensuring pensionability of all forms of atypical employment, particularly part-time employment.

18.1.3 In this Chapter, the Commission discusses and makes recommendations on access to pension schemes for part-time employees, and the pension terms to be applied to such employees.

18.1.4 The position of other types of atypical employment, principally temporary (sometimes referred to as *fixed term contract*) employment, is also addressed in our recommendations.

18.2 Access to pension schemes for part-time employees

18.2.1 In the past, the State provided pensions for public servants who were permanent and full-time; part-time employees were entitled only to non-statutory gratuities. More recently, there has been a move to extend pensionability to part-time employees in various parts of the public service. This has been driven to a large degree by greater union and staff involvement in this issue, but also by developments in European Community law. A number of cases decided by the European Court of Justice (ECJ) in relation to sex-based discrimination have clarified the position as regards access to pension schemes for part-time employees, most of whom are female.[229]

18.2.2 These cases have concluded that Article 119 of the *Treaty of Rome*, which requires that men and women receive equal pay for equal work, extends to the question of access to occupational pension schemes. The rationale of the ECJ is that if a pay policy consisting of setting a lower hourly rate for part-time work than for full-time work may in certain cases entail discrimination between men and women, the same applies where part-time workers are refused a company pension. As pension benefits are included in the definition of pay under Article 119, it follows that, hour for hour, the total remuneration paid to full-time workers is higher than that paid to part-time workers.

18.2.3 More recently, an EU Council Directive signed in December 1997 implements a framework agreement on part-time work concluded between the social partners in Europe.

[229] For example, *Bilka Kaufhaus GmbH v Weber von Hartz* (case 170/84) [1986] – 2 CMLR 701 and the *Fisscher* case [1995] CMLR 881.

Effectively, this Directive outlaws discrimination on the basis of part-time status (i.e. it will no longer be necessary to prove direct or indirect sex-based discrimination). The Directive provides that, insofar as conditions of employment are concerned, part-time workers shall not be treated in a less favourable manner than comparable full-time workers, solely because they work part-time, unless different treatment is justified on objective grounds. As noted in Paragraph 12.4.2, new legislation to give effect to the Directive in this country will be introduced shortly. For the purpose of the legislation it has been agreed in the *Programme for Prosperity and Fairness* that the definition of remuneration in the Directive will include occupational pensions.

18.2.4 There is likely to be greater usage of part-time employment in the public service in the future (particularly in the health service and the civil service). In Section 7.3 and Appendix 7.4, we detail some of the new provisions and facilities being developed, e.g. in relation to *atypical panels* and work-sharing. Given the greater range of opportunities for part-time working, the need to attract suitably qualified personnel to take up such opportunities, and the current position under Community law, there will be a strong focus in the future on ensuring that part-time employees have access to occupational pension schemes.

18.2.5 In the Department of Finance framework for occupational pensions coverage of part-time civil servants (see Paragraph 3.3.61), the Department applies a cut-off for pensionability of eight hours work per week. This cut-off may be justifiable by reference to Community law on the basis that the very low value of benefits involved would be outweighed by the administrative difficulties and cost involved in arranging pensionability.

18.2.6 The Commission considers that public servants should, in principle, be given access to occupational pension schemes. We acknowledge that for part-time public servants there is a close interlinkage between the question of access to pension schemes and that of the pension terms to be applied (particularly the operation of integration). Rulings of the ECJ in relation to equal pay are relevant in this regard. The question of the pension terms to be applied to part-time staff is discussed below.

18.3 Pension terms to apply to part-time employees

18.3.1 There are two possible approaches to integration for part-time employees (as outlined in Section 11.7). One method is to calculate the part-timer's actual service at retirement (i.e. to add together all the hours, days and years the person has worked) and apply this service to the full time remuneration for the position (less the Social Welfare offset of twice the rate of OACP). This is known as *pro rata integration*. The other method is to take the actual remuneration of the part-timer at retirement (less the Social Welfare offset) but to treat each year in which he or she has worked (regardless of the actual time put in) as a full year of service for pension purposes. This is known as *full integration*. The public service currently applies the latter approach (although the pensions of job-sharers are based on pro rata integration). From the perspective of the employee, full integration gives a less favourable level of occupational pension than pro rata integration.

18.3.2 The different outcomes of the two approaches may be seen in the following example involving two employees — A and B, who are engaged in comparable work, A, full-time, B, part-time. Under existing integration rules, both A and B are subject to an integration offset of twice the rate of OACP, i.e. £192 (based on the May 2000 rate of OACP, £96 per week). Table 18.1 gives an illustration of the pension calculation under **full integration**.

Table 18.1: Comparison of pension entitlements of full-time employee and part-time employee under full integration

	A — Full-time	B — Part-time
Weekly hours	39 hours p.w.	$19\frac{1}{2}$ hours p.w.
Years worked	40 years	40 years
Pensionable service	40 years	40 years
Pensionable remuneration	£400 p.w.	£200 p.w.
Net pensionable remuneration	£400 – (OACP (£96) × 2) = £400 – £192 = £208	£200 – (OACP (£96) × 2) = £200 – £192 = £8
Pension calculation	£208 × 40/80 = £104 p.w.	£8 × 40/80 = £4 p.w.
Lump sum[230]	£31,308	£15,654
OACP	£96 p.w.	£96 p.w.
Total pension (incl. OACP)	**£200 p.w.**	**£100 p.w.**

Note: If the new pension calculation formula recommended in Chapter 17 were applied (occupational pension calculated at 40/240ths for earnings up to three times OACP (£288 per week), and 40/80ths for earnings in excess of that figure), the calculation of occupational pension for A and B would be as follows:

A:	£288 × 40/240	=	£48
	£112 × 40/80	=	£56
	Total		£104 per week (i.e. as above)
B:	£200 × 40/240	=	£33 per week (as compared with £4 per week in the Table)

18.3.3 Under full integration, with the addition of OACP, both A and B receive a total pension which is half of final earnings — meeting the retirement income objective of public service pension arrangements where there is maximum service of 40 years. The part-time employee, B, receives total pension benefits which relate to that of the full-time employee, A, who is engaged in comparable work, proportionate to hours worked.[231]

18.3.4 Turning to **pro rata integration**, as illustrated in Table 18.2, it will be seen that the calculation of benefits for B changes (A's position is unchanged):

Table 18.2: Comparison of pension entitlements of full-time employee and part-time employee under pro rata integration

	A — Full-time	B — Part-time
Pensionable service	40 years	20 years
Net pensionable remuneration	£400 – £192 = £208	£400 – £192 = £208
Pension calculation	£208 × 40/80 = £104 p.w.	£208 × 20/80 = £52 p.w.
Lump sum	£31,308	£15,654
OACP	£96 p.w.	£96 p.w.
Total pension (incl. OACP)	**£200 p.w.**	**£148 p.w.**

Note: If the new pension calculation formula recommended in Chapter 17 were applied, the amount of occupational pension in respect of both A and B would be as above. Unlike the case in the note to Table 18.1, B's final salary under pro rata integration would be taken as the notional salary of £400 per week. Because this figure is in excess of three times the rate of OACP, the new formula would not result in an increased occupational pension compared with the outcome under pro rata integration on the basis of the existing formula.

[230] Pensionable remuneration × 52.18 weeks × 120/80.

[231] Note that the part-timer's total pension will be proportionally greater where pensionable remuneration is less than twice the rate of OACP.

18.3.5 With pro rata integration, the occupational pension for the part-time employee relates to that of the full-time employee proportionate to the hours worked. The part-time employee's pension here is half that of the full-time employee, just as he or she works half of the weekly complement of 39 hours.

18.3.6 However, when OACP is included, the part-time employee receives a total pension under pro rata integration which is proportionately higher, as a percentage of final earnings, than that of the full-time employee. For B, total pension of £148 represents 74% of final earnings. Thus, the total pension is in excess of the 50% promised by public service pension arrangements for a person having 40 years' service. In addition, it is higher than the pension of a full-time employee having a lower hourly pay who retires on the same rate of weekly pay and with the same service. The full-time employee retiring in such circumstances would have the same pension as B (part-time) in the example in Table 18.1 — i.e. a total pension of £100, 50% of final earnings.[232]

18.3.7 The basic arguments which have been made in relation to both forms of integration are:

Full integration

(i) it results in the part-time employee receiving a combined Social Insurance and occupational pension which is consistent with the aim to provide retirement income of 50% of final earnings for a person with 40 years' service;

(ii) it is the system which applies to employees generally. To adopt a different approach would be to favour part-time employees over all others, particularly those on low pay.

Pro rata integration

(i) it appears to meet the equality requirement under Community law, as currently interpreted by the European Court of Justice, to provide the part-time employee with hour for hour the same pay (defined to include occupational pension) as a full-time employee engaged in comparable work;

(ii) as all new entrants are paying full PRSI, and in light of the drawing together of part-time working with the job-sharing scheme, it will be increasingly difficult to justify a situation where part-time employees, who are generally on lower levels of pay, will be entitled to a less favourable system of integration than that applying to job-sharers;

(iii) it is more capable of dealing with the position of public servants having more than one part-time job given that only one Social Insurance pension is payable.

18.3.8 As shown in the note to the full integration example given in Table 18.1, if the new pension formula recommendation in Chapter 17 were applied, the part-time employee, B, would receive an improved weekly occupational pension of £33 per week compared with £4 per week under the existing formula. A's pension would be unchanged as pensionable remuneration in A's case is in excess of the cut-off envisaged in the new formula. It is important to note that the new formula, of itself, would not provide the part-time employee with pro rata benefits either in relation to occupational pension only, or in relation to the total of occupational pension and OACP.

18.3.9 It is important to consider the equality issue arising under EU Community Law. We address this issue below.

[232] The total pension for the full-time employee would comprise an occupational pension of £33 per week plus OACP, i.e. £129 per week, if the new pension calculation formula were applied — see note to Table 18.1.

Equality and pensions for part-time employees

18.3.10 As with the question of access to pension schemes, EU case law in relation to the pension terms of part-time employees revolves around the fact that most part-time employees are female. However, there is uncertainty at present about precisely how Community law views integration in the case of part-time employees.

18.3.11 The essential question is whether an occupational pension scheme can apply a rule (viz full integration) in order to compensate for an unequal outcome for part-time and full-time employees under the State Social Insurance system but which may, according to a certain interpretation of EU law, give rise to a possible discrimination case because it results in a part-time employee receiving a lower rate of occupational pension than a full-time employee. Since 1991, part-time employees in Ireland who earn a minimum of £30 per week have the same flat rate Social Insurance entitlements as full-time employees. This is the justification offered for full integration: the pension scheme's promise is payment of a fixed percentage of final income on retirement. If the Social Insurance system pays the same rate of pension to a part-time as to a full-time employee, irrespective of hours worked, the scheme is justified in paying a lower rate of occupational pension to the part-time employee. In this way the scheme ensures that the pension promise is fulfilled equally for all employees, be they part-time or full-time.

18.3.12 The opposing argument is that in an equal work scenario (disregarding the Social Insurance system), full integration, which results in a lower rate of occupational pension for a part-time employee compared with a full-time employee, constitutes discrimination against part-time employees, the majority of whom are women.

18.3.13 The EU Part-time Directive (soon to be implemented in Irish legislation — see Paragraph 18.2.3) states that part-time workers shall not be treated less favourably than comparable full-time workers solely because they work part-time (unless there are objective grounds for such treatment). The Directive adds that, where appropriate, the principle of *pro rata temporis* shall apply. It is not clear, however, whether in the context of integrated occupational pension schemes, the pro rata comparison should include or exclude Social Insurance benefits.

18.3.14 Perhaps the most useful recent case offering guidance on this particular point is the *Shillcock case*, which was the subject of a determination by the UK Pensions Ombudsman in October 1997, and is now under appeal.[233] The Ombudsman found that it was wrong to exclude an employee from a pension scheme on the grounds that her part-time earnings were lower than the State pension offset. He found also that if the employee had been admitted to the scheme, the operation of the State pension offset would have constituted indirect sex discrimination in contravention of Article 119 of the *Treaty of Rome*. He added that a pro rata approach to integration would have given an outcome which would not be discriminatory.

Integration and part-time pensions — other considerations

18.3.15 Few private sector schemes currently grant access to occupational pension schemes to their part-time employees. Of the small number which grant such access, 80% apply pro rata integration (see Paragraph 8.12.7).

18.3.16 In the Netherlands, which has a flat-rate Social Insurance pension system similar to ours (see Paragraph 9.5.5), it would appear that the pension scheme for public servants applies a pro rata approach to calculating pensions for part-time employees.

[233] Determination by the Pensions Ombudsman in the case of Mrs E.M. Shillcock, 30 October 1997 (FOO317/AJLK).

18.3.17 In *Securing Retirement Income,* the Pensions Board notes that the operation of full integration for part-time employees has been a source of dissatisfaction. However, the Board acknowledges that any special treatment for part-time employees would create other anomalies — application of a pro rata offset would have the effect of giving a part-time employee a higher occupational pension than a full-time employee, where both are on similar earnings and service.[234]

18.3.18 Finally, it is worth considering the administrative practicalities of both approaches. Typically, part-timers' hours of employment vary over their life-time. Under full integration, if the general rule for full-time employees were applied *simpliciter* (i.e. that pension is based on retiring salary or the average of the final three years), part-time employees whose hours of work increased in later years would gain disproportionately while those who chose to reduce their work commitments prior to retirement would lose out. A practical solution might be to base pensionable pay on the average number of weekly hours on a full career basis multiplied by the hourly rate on retirement. Even so, the system might be susceptible to abuse.

18.3.19 Under pro rata integration the focus would be more firmly on hours worked, which feed directly into the calculation of pensionable service. This is currently the approach in the case of employees who are made full-time and pensionable and are allowed to reckon previous part-time service. Obviously, for such an approach to be effective, information systems would need to be put in place to ensure detailed recording of hours worked by each individual public servant.

18.3.20 The administrative advantages of pro rata integration are: actual service in each year can simply be added together to arrive at a figure for total pensionable service; the pro rata system is not open to manipulation to increase pension; and it does not penalise people who switch to part-time working prior to retirement.

18.4 Cost of pro rata integration for part-time employees

18.4.1 The Commission obtained costings on the extension of pensions coverage to part-time employees on the basis of pro rata integration.[235] Certain assumptions were made about the number of part-time public servants in each area of the public service. Where pension schemes were contributory, it was taken that when given access to pension schemes, the outstanding employee pension contributions in respect of past service would have to be paid. It was assumed that this would be done by means of deduction from retirement lump sum or death gratuity.

18.4.2 The cost projections indicated that pensionability of part-time public servants on the basis outlined above would have a minimal effect on annual pensions expenditure in the short-term. Over time, there would be an increase in pension costs, in constant (1997) price terms, of the order of £11 million per annum, net of employee contributions.

18.4.3 The addition to the State's accrued liability as a result of the change would be approximately £32 million (compared with total accrued liabilities, as currently estimated, of £20 billion).

18.4.4 It should be noted that these estimates relate only to part-time employees still in service. The projections and valuations do not include the additional effect if the improvement was extended to part-time public servants who have now left public service employment.

[234] The Pensions Board, *Securing Retirement Income* (1998), p. 177.

[235] Commission on Public Service Pensions, "Further Actuarial Review of Impact of Changes to Pension Scheme Terms" (October 1999), Report prepared by Mercer Ltd.

18.5 Pension terms in the case of temporary or contract employees

18.5.1 Public service occupational pension schemes have been moving towards a policy of allowing immediate access to schemes in the case of all full-time temporary and contract public servants.

18.5.2 This approach, which the Commission endorses, is consistent with the general principles and minimum requirements relating to fixed-term work as set out in the 1999 EU Directive on Fixed-term Work (see Paragraph 12.4.3). The Directive states that innovations in occupational social protection systems are necessary in order to adapt them to current conditions, and in particular to provide for the transferability of rights.

18.5.3 At present, public service schemes do not allow preservation of pension benefits where service at time of leaving is less than five years. Obviously, this could create a difficulty in the case of contracts of employment expected to be of shorter than five years' duration. Other than for death-in-service cover and the refund of employee pension scheme contributions (if any), individuals with contracts of employment of less than five years could not expect to benefit from their scheme membership.

18.5.4 We note that in the National Pensions Policy Initiative, the Pensions Board have recommended that the maximum period of reckonable service required to qualify for preserved benefits should be reduced from five to two years.[236] This recommendation has been accepted by the Government, and we understand that legislation to implement it will be introduced shortly.

18.6 Conclusions and recommendations

18.6.1 The Commission recommends that public servants in temporary and part-time work should be granted access to public service pension schemes, provided that they are in regular or quasi-permanent employment and, in the case of part-time employees, that they work a certain minimum number of hours per week.

18.6.2 In the specific case of part-time employees (where integration and low rates of occupational pension are at issue), the Commission is conscious of developments occurring at the level of European Law, through cases being decided at the European Court of Justice.

18.6.3 Under existing public service integration arrangements (*full integration*), the total pension – combining occupational pension plus Social Insurance benefit – for a part-time employee compares with the total pension of a full-time colleague engaged in comparable work and in receipt of the same (hourly) pay, pro rata to the hours worked, assuming both have worked for the same number of years. In effect, this means that the total pension (occupational plus Social Insurance benefit) of the part-time employee is proportional to the total pension of the full-time employee.[237] However, the rate of occupational pension on its own (excluding Social Insurance benefit) is proportionately lower for the part-time employee compared with the full-time employee.

18.6.4 Under an alternative approach (*pro rata integration*), the comparison between the full-time and part-time employee is done not on total pension but on occupational pension only. This means that the rate of occupational pension for the part-time employee compares with that of

[236] The Pensions Board, *Securing Retirement Income* (1998), p. 168.
[237] Except where pensionable remuneration is less than twice the rate of OACP.

the full-time employee, pro rata to the hours worked. Under this approach, occupational pension is higher when compared with existing arrangements.

18.6.5 The question of deciding whether full or pro rata integration should apply to part-time employees arises, at least in part, because of the flat rate nature of the entitlement to Social Insurance benefits. If, instead, Social Insurance benefits were earnings related, it is likely that occupational pension schemes would not have to address this particular issue.

18.6.6 The Commission gave careful consideration to the question of the pension terms to be applied to part-time employees, in particular, the question of integration. For a number of reasons, including:

- the blurring of the distinction in the public service between job-sharing and part-time working,
- the general implications of the European Commission's Part-time Work Directive and of recent ECJ decisions in relation to direct and indirect sex discrimination, and
- the need to accommodate atypical forms of working for socio-political reasons,

the Commission considers that occupational pensions for part-time public servants should be calculated on the basis of pro rata integration.

18.6.7 Accordingly, the Commission recommends a change in the form in which integration is applied to part-time public servants from full to pro rata integration; this modification in scheme terms would result in improved occupational pensions for such employees (the change in the operation of integration recommended at Paragraph 17.6.5 would impact on the pension calculation of any part-time employees where the amount of notional full-time pensionable remuneration was less than three times the rate of OACP).

18.6.8 The Commission believes that the effect of this recommendation would be to facilitate the pensionability of part-time employment within the existing benefits structure and to achieve a practicable system for treating atypical service.

18.6.9 The Commission recognises that pro rata integration would give a part-time employee a higher hourly pension (combining occupational and Social Insurance pension) compared with a full-time employee in a different occupation retiring on the same salary where both have worked for the same number of years. However, our recommendation of pro rata integration is based generally on the principle of equal pay, i.e. the payment of the same hourly rate of remuneration, *including pension*, for those engaged in the same or similar work within the one area. Thus, the comparator for a part-time employee is a full-time employee engaged in the same or similar work, not a full-time employee who is engaged in different work and receiving a lower hourly rate of pay.

18.6.10 The Commission's recommendations on pension terms to be applied to part-time public servants on full class PRSI are outlined below in full:

(i) the part-time staff must be in regular, quasi-permanent employment (including wholetime temporary, regular temporary, or seasonal working);

(ii) they must be working a minimum of eight hours work per week (i.e. in the case of a standard working week), assuming a cut-off of this nature is justified by reference to Community law on the basis that the very low value of benefits involved would be outweighed by the administrative difficulties and cost involved in arranging pensionability;

(iii) there should be pro rata integration of notional pensionable remuneration (i.e. based on full service) with the State Social Insurance OACP;

(iv) pensionable service should be counted as actual service (e.g. two years' service worked half-time is taken as one year's pensionable service);

(v) employee contributions should be calculated pro rata, i.e. based on actual remuneration, with a pro rata adjustment to the Social Welfare offset based on hours worked.

18.6.11 As regards death-in-service benefits, the Commission considers that the general approach should be to ensure that the benefits of part-time employees are pro rata those of full-time employees. However, there are certain difficulties in deciding how the principle of pro rata should be applied in the context of the calculation of death gratuity and spouses' and children's benefits, particularly the notional added years obtained by projecting forward to normal retirement age. For example, spouses' and children's benefits could be calculated using notional pensionable remuneration and assumed pensionable service to normal retirement age based on continuation of the existing work pattern at time of death. This might seem reasonable in the case of a public servant who was originally appointed on a part-time basis and who had worked the same level of weekly hours up until time of death. However, such an approach might not be thought fair in the case of a public servant who had worked primarily on a full-time basis and had moved to part-time working (perhaps with the intention of resuming full-time working) just before time of death. There are technical issues involved, and regard must be had to the implications of EU equality requirements and to wider policy concerns.

18.6.12 The Commission recommends that discussions should take place between public service unions and employers in order to arrive at a reasonable and equitable approach to the calculation of death gratuity and spouses' and children's benefits for part-time public servants. These discussions should take account of practice in private sector pension schemes and of the existing approach of public service schemes in relation to job-sharing, part-time, and contract public servants, as well as giving appropriate weighting to each individual's pattern(s) of employment.[238] Insofar as possible, the principle of pro rata benefits should apply. In addition, particular regard should be had to the commitments entered into by the Social Partners in relation to the promotion of family friendly policies.

18.6.13 Finally, the Commission recommends that the period of reckonable service required to qualify for preserved benefits under public service schemes should be reduced from five to two years,[239] in line with the recommendation of the Pensions Board in the National Pensions Policy Initiative. We believe this change should apply to serving staff only from a current date.

[238] For instance, a person who has worked for ten years — the last two on a half-time basis — could have his or her death-in-service/spouses' and children's scheme benefits determined in line with the overall level of full-time service accrued at the time of death, i.e. in this case nine years out of a possible ten. Accordingly, the death gratuity would be equivalent to 90% of that payable in respect of a full-time employee, and the potential service to retirement age for the spouses' and children's scheme would be 90% of that of a full-time employee.

[239] In line with current practice for job-sharers, two years of part-time service in this context would be treated as two years at work, not as two years' pensionable service.

CHAPTER 19

Pension Scheme Flexibility

19.1 Introduction

19.1.1 A major component in the new public service pensions framework is the provision of pension scheme flexibility. With the increasing age of entry to the public service, more frequent breaks in service, and widespread interest in early retirement, there is likely to be a growing demand in the future for a well designed, cost-effective, and adaptable facility which would allow public servants to contribute towards improved pensions and a package more suited to their individual circumstances. For the State, the requirements of any such facility are cost, administrative convenience, and the minimisation of any possible exposure under the legal and regulatory framework applying to the facility.

19.1.2 The Commission believes that public servants should have the opportunity to provide for enhanced pension benefits and to plan in relation to the age at which they would like to retire. This Chapter sets out our deliberations and recommendations on this important aspect of our terms of reference, having regard to the requirements of public servants and the State.[240]

19.1.3 There are a number of ongoing developments which make it difficult at this point to be clear on the formal structures which might be implemented in the future, and on the regulatory and taxation environment in which these structures would operate. These developments include the imminent introduction of PRSAs and the new measures to apply to AVCs as a result of the reforms introduced under the Finance Act, 2000. Our recommendations must be qualified accordingly (see Paragraph 1.4.6).

19.2 Review of existing arrangements

19.2.1 In Chapter 12, we discuss the two existing arrangements for providing pension flexibility, the schemes for purchase of notional service and AVCs. They work in very different ways: under the purchase scheme, the public servant agrees to buy a specified number of added years of notional service, thereby increasing the total period of pensionable service for the calculation of occupational pension benefits; under the AVC arrangement, the public servant makes contributions for investment in an individual fund which, at retirement, is used to buy additional pension benefits.

19.2.2 The comparative features of the two arrangements, from the point of view of the individual public servant and of the State, might best be summarised in tabular form.

[240] In formulating our recommendations, the Commission obtained expert advice from pension consultants, Mercer Ltd. (report entitled "Review of Additional Voluntary Contribution and Purchase of Service Arrangements", May 1999).

Table 19.1: Comparative features of purchase scheme and AVCs from the perspective of the individual public servant

Purchase scheme	AVCs
Benefits are guaranteed	Benefits are uncertain — they depend on factors such as investment return and annuity rates at retirement
Rules govern eligibility, contributions, retirement age, etc.; difficult to tailor to personal circumstances	There is flexibility, subject to Revenue rules, re. contributions, benefits being funded, retirement age, obtaining pension on non-pensionable income, funding for additional lump sum
The scheme is not designed to cater for early retirement	AVCs can help finance the cost of early retirement in certain circumstances
There is little necessity to review the purchase option once the initial decision is made	Individual can/should take active role in reviewing AVC balance and deciding investment strategy
No direct administrative charges are levied on the individual	The member is required to meet AVC scheme charges
Some groups/individuals gain at the expense of others in the purchase rates; it is increasingly difficult to arrive at *correct* rates for all	Benefits are related to contributions made by each public servant — no cross-subsidisations are involved
The contribution rates assume pension fund investment return — thus, the pension is less expensive than an annuity in the private sector	Annuities are more costly than public service pensions because of the link to interest rates. Under the Finance Act, 2000, there is greater flexibility as regards drawdown of the fund at retirement
The pension is increased in line with public service pension increases (although this is factored into the contribution rates)	The member must purchase an escalating annuity to obtain pension qualifying for increases — generally, increases are less favourable compared with public service pension increases
It is not possible to fund increased death cover up to Revenue limits	Improved death cover is available, up to the Revenue limits

Table 19.2: Comparative features of purchase scheme and AVCs from the perspective of the State

Purchase scheme	AVCs
Contribution rates are designed to be cost neutral	AVCs are contributions made by the individual — there is no cost to the State
The assumptions made in the tables mean that the State is underwriting significant risk elements	There is no underwriting by the State; benefits are wholly related to value of AVC account
While the assumption of pension fund investment returns means that the rates are competitive, this can be seen as increasing the State's exposure	Not relevant
The State can point to the guarantees of the purchase scheme as an important benefit of public service employment	The State receives little *kudos* from the high take-up of AVCs
Apart from the assumptions in the purchase tables, the State has no continuing explicit exposure in relation to the operation of purchase scheme	The State has certain legal and regulatory responsibilities for the purposes of AVC trust deeds
The State bears the administrative costs of the schemes, including the cost of devising and negotiating changes to the purchase tables	Administrative and promotional costs are borne by the AVC member; the State bears the cost only of deducting and remitting employee contributions
The State does not actively promote the purchase schemes	External providers actively promote AVC schemes and provide comparative analysis with purchase option
The scheme is not funded; thus, contributions received are treated as current revenue, and the benefits purchased, when paid, add to the pay-as-you-go cost of pensions	The State's pay-as-you-go cost of pensions is unaffected by the benefits provided from AVCs

19.3 Review of shortcomings in current AVC arrangements

19.3.1 Prior to 1987, when the first public service AVC schemes were introduced, schemes for purchase of notional service were the only available option for public servants who wished to contribute towards improved pensions. At the time of their introduction, AVCs were seen as an alternative, more flexible vehicle to deliver pension improvements for public servants.

19.3.2 We note that the State is not *obliged* to provide AVC schemes for its employees and that at the present time, it would seem to be involved in public service AVC schemes only to the extent that, as employer, it is required to do so for the purposes of Revenue law and practice. We have reached the view that an AVC-type facility should be considered as an integral part of public service pension arrangements for the following reasons:

- AVCs are a flexible facility enabling public servants to tailor part of their pensions package to their own individual circumstances. Thus, they help to provide genuine retirement choice to individuals, including the facilitating of early retirement. In addition, they represent a transparent measure of the cost and value of pensions. The large take-up of AVCs shows that they are an attractive option for many public servants. With implementation of the new flexibilities under the Finance Act, 2000 (see Paragraph 12.12.1), AVCs may become even more attractive;
- AVCs allow public servants to provide for improvements in certain benefits up to the Revenue limits in a way that is not possible under the purchase scheme (e.g. retirement lump sum, death gratuity, spouses' and children's pensions);
- AVCs are now standard practice in occupational pension arrangements. As noted in Paragraph 8.18.1, almost all private sector schemes make provision for payment of AVCs. A small survey of ten large private sector employers — reported in Section 12.14 — revealed that all ten offered an AVC facility (most on a defined contribution basis);
- with the introduction of Personal Retirement Savings Accounts (PRSAs), it appears that all employers will be required either to make available an AVC scheme or to provide a payroll deduction facility to at least one PRSA provider to facilitate individuals who wish to make additional voluntary contributions (see Section 12.15).

19.3.3 As discussed in Chapter 12, a number of issues arise in relation to the framework under which AVCs currently operate in the public service. We review these below under the following headings:

- number of AVC schemes;
- role of the employer;
- trusteeship;
- AVC charges;
- promotion of AVC schemes.

Number of AVC schemes

19.3.4 From the date of their initial introduction, the State has insisted that there be at most one AVC scheme per public service union. This was done with the aim of minimising administrative costs in the handling of payroll deductions. At the time, there was a concern that public servants would seek separate approval for their own individual AVC schemes. By requiring AVCs to be linked to particular unions, it was hoped to minimise the numbers of AVCs in any one area.

19.3.5 However, with the extension of AVC schemes throughout the public service, there would now appear to be over 40 separate schemes, and this number continues to grow as new schemes are established. Each scheme has its own administrator, trustees, investment managers, etc. They each impose their individual charge structures on their members. Thus, there is no advantage from *bulk buying power*.

19.3.6 In certain parts of the public service, because the relevant union has opted not to negotiate the introduction of an AVC, or because the AVC option available offers death-in-service cover only, it may not be possible at present to use AVCs to improve pension on retirement. Thus, there may be pressure to establish new AVC plans and/or group PRSAs in the future.

19.3.7 In the private sector, by comparison with the fragmented approach in the public service, the AVC scheme generally comprises a single legal entity sponsored by the employer and usually with a separate trustee board; there may be several fund options within the structure (possibly from different institutions), but the key point is that the employer/trustees retain responsibility for the administration of the plan, appointment of external providers, etc.

Role of the employer

19.3.8 Under the heading *"employer's responsibilities"*, the trust deed of a typical public service AVC scheme states that the employer shall cooperate with the trustees, as necessary, in the collection of members' contributions and their payment to the trustees; that the investment and management of the fund, and the grant or the payment of benefits under the plan, shall be the exclusive responsibility of the trustees; and that the employer shall not, under any circumstances, be responsible for the grant or the payment of benefits to, or in respect of, members or for any loss incurred by the fund. Apart from its formal responsibilities under the trust deed, the employer also exercises a role, in conjunction with the trustees of the AVC scheme, in *policing* the Revenue limits in relation to contributions and benefits (we summarise the principal Revenue limits at Appendix 12.1).

19.3.9 For each AVC scheme, it is clear that the trustees bear a major burden of responsibility in relation to the setting up of the scheme, administration, choosing consultants and managers, investment performance, provision of information, and the grant and payment of benefits. While some of this work may be delegated, ultimate responsibility for ensuring that the scheme is run properly lies with the trustees.

19.3.10 However, under the trust deed, the employer has the power to appoint and remove trustees, to amend scheme rules in conjunction with the trustees, and to initiate the windup of the scheme.

19.3.11 In our view, it is necessary to ensure that the State is in a position to carry out the formal responsibilities which go with its position as *primary employer* for the purposes of the AVC trust deeds, i.e. in relation to the establishment and oversight of the AVC arrangements, including appropriate arrangements for the appointment and removal of trustees, overseeing compliance with the Revenue limits, etc.

Trusteeship

19.3.12 At present, the *sponsoring* trade unions, which have no formal legal association with the scheme, play a key role in the selection and appointment of the commercial organisations responsible for the promotion, administration and investment of AVCs.[241] While the power to appoint the trustees formally rests with the State, it appears that, in practice, the selection of the initial trustees is made by the trade unions through their agreeing to the involvement of a particular provider.

19.3.13 The trustees of the existing AVC arrangements are almost invariably trustee firms closely associated with the broker who promotes the arrangement or the institution who manages the investments. Notwithstanding the provisions of the Pensions Act allowing for member representation, the vast majority have no member-appointed trustees.

19.3.14 Questions might be asked as to whether it is desirable or in the best interests of the members that, in many cases, the trustees of the AVC arrangements are closely related to the organisations which have a direct financial interest in the operation of the scheme. Occasions may arise where the best interests of the members may be in conflict to some degree with the commercial interests of the organisations with which the trustees are associated.

AVC charges

19.3.15 Overall charges levied on public service AVC schemes would appear to be higher than those charged in AVC schemes of typical private sector firms (see Appendix 12.4). In addition, existing arrangements preclude the possibility available from bulk buying power across the public service. It might be noted that in the private sector, the employer pays the administration charges of AVCs in a number of cases (see Section 12.14).

19.3.16 The fact that the State as employer does not meet any of the administrative/promotional costs of AVCs may be a factor in the higher charges of public service AVC schemes compared with those of AVC schemes of private sector firms. Another factor which may contribute to the higher charges is the scale of the operation required to promote and market the schemes to large and sometimes geographically dispersed public service groups. The level of take-up of AVC schemes in the public service may be an indicator of the extent of the promotion and direct marketing by AVC providers, the cost of which must be recovered through charges on members. A lower level of direct marketing would be required in the case of private sector firms where the employer pension scheme administrators would assume the main responsibility for promoting the AVC arrangement.

Promotion of AVC schemes

19.3.17 In general, public service AVC schemes would appear to be actively marketed. We believe that this is a factor in their high level of take up relative to take-up under the schemes for purchase of notional service.

19.3.18 As noted in Paragraph 19.3.16, active marketing must be paid for and, under current arrangements, commissions and other expenses associated with active marketing campaigns are in one way or another recouped from the contributions paid by the participating employees.

19.3.19 In nine of the ten schemes surveyed in the private sector (see Section 12.14), the employer, not the member, paid the cost of promotional activity.

[241] For some AVC schemes, for example, those established for employees of non-commercial state-sponsored bodies, it is the public service body itself, not any union or group of unions, which takes the initiative in establishing the scheme.

19.3.20 The Commission considers that an AVC facility can be an attractive feature of employment if it is adequately marketed and presented. The production of marketing and promotional material gives rise to substantial costs. Arguably, the employer gains by having an active approach to publicising AVCs as the employee's perception of the employer is likely to rise as a result. Following this line of thought, it can be argued that the employer should contribute to the cost of marketing an AVC-type arrangement. In the public service context, it should be noted that the employer meets the administrative costs associated with the schemes for purchase of notional service.

19.4 Development of a new public service AVC-type arrangement: the Scheme for Public Employees' Additional Retirement Savings

19.4.1 In order to address the shortcomings identified above, the Commission examined the development of a new public service AVC-type facility, to be called the *Scheme for Public Employees' Additional Retirement Savings (SPEARS)*. SPEARS would be a central plan for the public service as a whole. Initially, we considered the establishment of separate plans for each major area of the public service, but decided instead for reasons of efficiency of delivery and economies of scale in favour of a public service-wide plan. The plan would be open to all public servants, who would be able to carry their individual pension account between different public service employers. Because of its size, SPEARS would most likely offer reduced charges compared with the wide range of smaller AVC plans now in existence.

19.4.2 In terms of legal structure, SPEARS could be established as an AVC scheme, a group PRSA, or other structure. We concluded that no definitive decision could be reached on which structure to adopt until the framework for PRSAs had been put in place. In the event that SPEARS was set up as an AVC scheme under trust deed, we would consider that the independent trustees of the scheme should include representatives of public service unions and employers. If the scheme were set up initially as an AVC, it might be considered desirable to convert it into a group PRSA in due course.

Provision of benefits under SPEARS

19.4.3 We envisage that SPEARS would consist of two separate facilities — an individual savings account and a lump sum death benefit. These facilities would operate in broadly the same way as in existing AVC schemes (with the exception of the additional option to purchase a public service pension which we address in Section 19.6).

19.4.4 When an individual public servant joins SPEARS, a separate **savings account** would be established in his or her name. Periodic contributions made by deduction from salary and/or lump sum contributions would be lodged to the account and invested on behalf of the member. Transfer amounts paid from other pension schemes could also be lodged to the account. At retirement, the balance in the account would be available to *buy* additional pension benefits which would be paid alongside the occupational pension. The additional benefits would consist of extra pension, lump sum, and spouses' and children's benefits (on the death of the member), or a combination of all three. Changes implemented in the Finance Act, 2000 in relation to AVC arrangements would allow greater flexibility in the use of the savings account.

19.4.5 As discussed in Section 12.12, the form in which pension benefits are paid and the level of contributions which the member can make are subject to the limits laid down by the Revenue Commissioners and tax legislation. Briefly, it is possible under Revenue rules to *fund* the following pension benefits:

- additional benefits in respect of items of remuneration which are not pensionable under the occupational scheme (e.g. overtime);
- to obtain maximum permissible benefits at normal retirement age (age 60 for public servants with standard pension terms; age 55 having 35 years' service in the case of teachers);
- to bridge the gap between an integrated and a non-integrated pension for public servants in full class PRSI;
- to provide additional spouses' and children's pensions up to the Revenue limits;
- to maximise the retirement lump sum entitlement where it falls short of the maximum entitlement of $1\frac{1}{2}$ times pensionable remuneration.

19.4.6 Using the savings in the account to finance a temporary early retirement supplement could be a further option, although this might require certain changes to the way in which the Revenue limits operate (see Paragraph 12.12.8).

19.4.7 The purchase of annuities at the point of retirement at market annuity rates can give rise to considerable volatility and variation in the level of pension benefits that may emerge. The level of annuity rates has deteriorated substantially in recent years, in line with the experience of historically low interest rates (see Paragraphs 12.12.14 and Paragraphs 14.4.6-14.4.7). We consider that members of SPEARS should have the facility to apply their retirement savings on the open market to buy the most appropriate annuities available to them and that the full range of annuities should be offered, including guaranteed, unit linked, and with profit. We note that with implementation of the Finance Act, 2000 changes, it is no longer necessary to purchase annuities in certain circumstances (the new arrangements do not affect the current restrictions as regards the basis for making *contributions* to AVC schemes).

19.4.8 In addition to the above, we make a particular recommendation at Section 19.6 on the use of the SPEARS savings account to purchase a defined benefit pension within public service pension schemes.

19.4.9 The second section of SPEARS would be the **lump sum death benefit facility**. This would provide death benefits which would be additional to the balance available under the savings account. This additional life assurance cover would consist of a lump sum cover of $2\frac{1}{2}$ times pensionable remuneration,[242] with a flat rate charging structure (percentage of pensionable remuneration). We believe that a fixed lump sum cover would offer the best possibility of obtaining scale efficiencies for the benefit of the members.

19.4.10 We would suggest that the life assurance element of SPEARS would be offered by tender to appropriate institutions (e.g. life assurance companies). This would result in the obtaining of keen rates, having regard to the fixed level of cover.

SPEARS charging structure

19.4.11 The operation of SPEARS would give rise to various expenses. The key expenses would be related to:

[242] This is the difference between the maximum death gratuity payable under public service schemes of one-and-a-half times pensionable remuneration and the maximum benefit allowable under the Revenue limits of four times pensionable remuneration.

(i) the administration of SPEARS, including record keeping, correspondence with members, collection of contributions, compliance with statutory reporting requirements, etc.;

(ii) costs incurred in the management of the investment funds available;

(iii) costs in relation to the promotion and distribution of SPEARS to new potential members.

19.4.12 Provision of advice to public service employees in relation to their retirement needs is another service which could be made available by providers under SPEARS. However, we believe that the provision of individual advice should be limited to that contained in the scheme promotional materials and other regular correspondence issued to members, such as an annual statement. The provision of any further personal financial advice (other than at outset and retirement) would add substantially to the operational costs without necessarily adding greatly to the overall effectiveness of the scheme.

19.4.13 There is a strong argument, given the particular nature of any AVC-type arrangement, that charges arising under (i) and (ii) of Paragraph 19.4.11 above should be paid by the individuals participating in the scheme. The situation in relation to (iii) is less clear cut. A reasonable case could be made, particularly having regard to practice in the private sector, for the State (as employer) carrying these costs. The case would be strengthened in the context of the phased withdrawal of the schemes for the purchase of notional service (see Paragraph 19.5.6).

19.4.14 The Commission suggests that the permitted charging structure for SPEARS would take the form of a percentage of new contributions and/or a percentage of the funds under management. In practice it is likely that a combination of the two forms of charges would operate.

Investment management

19.4.15 Of the investment options to be offered to employees participating in SPEARS, we would suggest that the following four standard investment mandates should be made available:

- portfolio with a particular emphasis on investment in equities suitable for maximising long-term returns;
- mixed portfolio comprising a high proportion of equities, but also fixed interest stock and other assets;
- fixed interest stock, in order to counterbalance the risk of falling annuity rates;
- short-term cash instruments.

19.4.16 An important facility could be the inclusion of certain lifestyle-type funds which automatically manage the investment exposure of individuals over their lifetime, and also access to certain smoothed capital protection-type products. In our view, these two options should probably be included in the range of funds available notwithstanding the additional overheads of extra choice.

19.4.17 A possible area for expense savings would relate to the buying and selling of units in funds with different bid and offer prices (see Paragraph 12.14.1). This mechanism can give rise to considerable scope for investment managers to obtain significant windfall profits to the extent that they are in a position to match sellers and buyers of units at any transaction date. To counteract this, the Commission would propose that all SPEARS investment funds would have to operate on the basis of a single unit price at which all buying and selling took place at any given date.

Operational management

19.4.18 We assume in what follows that SPEARS would operate as an AVC under a pension trust. As noted above, other approaches are possible, for example, the new PRSA vehicle, when introduced. Depending on the nature of the regulatory framework to be introduced for PRSAs, a different form of operational management to that envisaged might be necessary.

19.4.19 The State (probably in the name of the Department of Finance)[243] would be the sponsoring employer of the SPEARS trust. Among the first duties of the State would be to write the initial rules in consultation with the public service unions. The rules of the trust would provide for trustees, possibly in line with the member representation requirements of the Pensions Act. It is likely also that the rules would provide for the trustees to appoint some form of secretariat to carry out a compliance and monitoring function under their direction.

19.4.20 To avoid unnecessary duplication of structures, the Commission would suggest that the trustees might be the same trustees as, or form a sub-committee of, the trustees for the Public Service Pension Fund (see Chapter 23). In addition, the Public Service Pensions Office recommended in Chapter 25 could act as the independent secretariat to the trustees (see Paragraph 25.4.12).

19.4.21 The key role of the trustees of SPEARS would be to:

- ensure that SPEARS was operated in compliance with all legal requirements and in accordance with the rules;
- formally appoint advisors/contractors with the approval of the State to carry out various functions required for the operation of SPEARS (see below);
- monitor the performance of the duties and tasks they have delegated to any sub-contractors;
- suggest amendments to the operations of SPEARS which may appear necessary over time;
- report to the members of SPEARS and other relevant authorities as appropriate;
- co-operate with the State regarding the promotion of the scheme to public service employees.

19.4.22 Other key clauses which would have to be included in the initial rules would relate to the appointment mechanism for the trustees and the specification of the roles and responsibilities of the various parties in the event of a full or partial wind-up of SPEARS.

19.4.23 The initial rules would clearly set out how SPEARS would be operated in practice. The trustees would have the power to propose subsequent amendments to the scheme. As is the case

[243] We envisage that the Department of Finance would act as *primary employer* in respect of all public servants employed by government departments and by public service bodies coming under the aegis of government departments. In the case of non-commercial state-sponsored bodies which have stand-alone pension schemes, it would be necessary for each body to decide whether they wished to introduce SPEARS for their employees or to continue existing AVC arrangements. The advantages of SPEARS would include more favourable member charges and the enhancement of employee mobility within the public service.

with employer-sponsored AVC schemes in the private sector, the State would retain the right to approve such amendments and to initiate any rule amendments that it considered appropriate which did not adversely affect historic rights of the members.

19.4.24 The State's main ongoing role in relation to the operation of SPEARS would be to monitor the operations of the scheme. The State would be expected to receive periodic reports from the trustees on actions they had taken and on the performance of the various tasks for which they were responsible. The State would have a role in approving formal SPEARS documentation and member communications. The State might also meet some of the cost of the promotion and distribution of SPEARS. As with existing AVC schemes, the State would not be responsible for the grant or the payment of benefits, or for any loss incurred by the fund.

19.4.25 The trustees would be responsible for decisions taken in relation to the investment of the assets of SPEARS. In the private sector, it is common practice for the employer to provide a full indemnity to the trustees for all their actions in relation to the AVC scheme, with the possible exceptions of fraud and fraudulent negligence. In the context of SPEARS, we would suggest that the possibility of the State providing a similar form of indemnity to the trustees should be examined.

Outsourcing suppliers

19.4.26 A key component of the initial rules would be the identification of procedures for the appointment of various sub-contractors to carry out the operating functions of SPEARS, such as administration, investment, promotion and insurance. It would be necessary to specify the service standards that would be required from any provider under each of these headings.

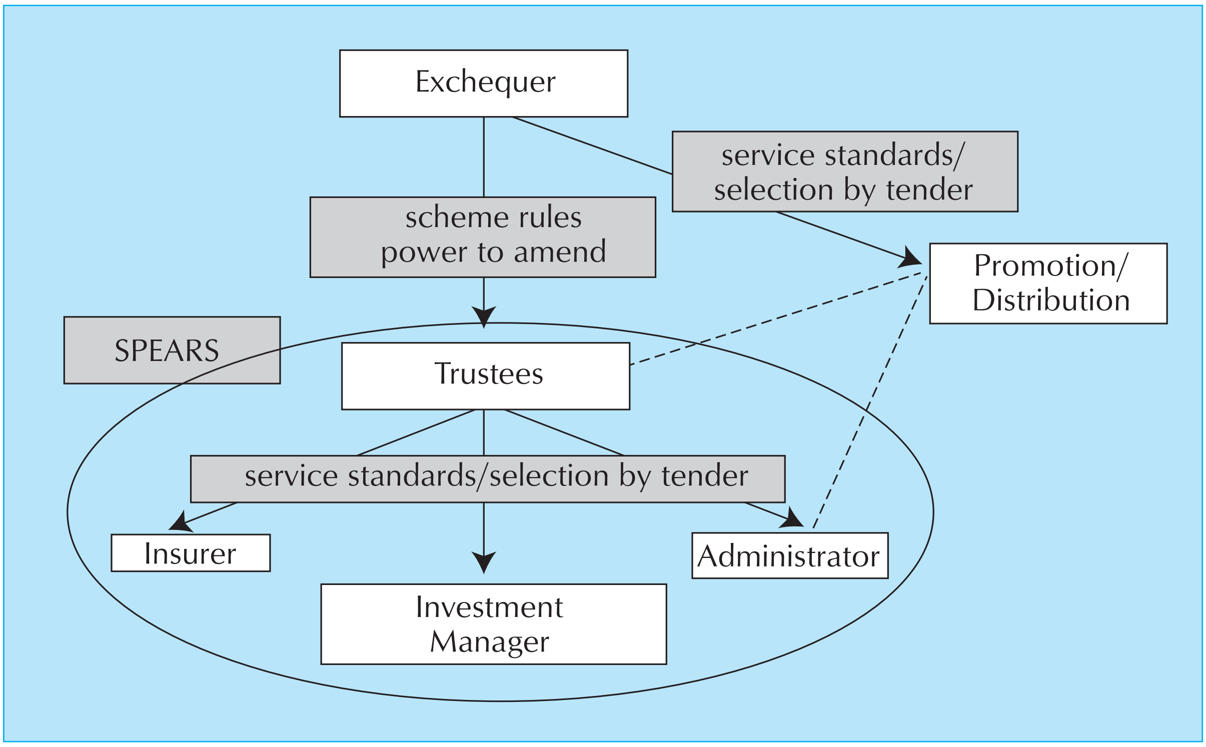
19.4.27 Depending on the best overall cost-benefit package that could be obtained, we would suggest that these services should be contracted out on either a *bundled* or *unbundled* basis (i.e. tender proposals to cover any one or combination of the administration, investment promotion and insurance functions).

19.4.28 The selection of the sub contractor(s) to implement SPEARS would be on the basis of a competitive tendering process. This process could operate at five year intervals or more frequently if deemed necessary.

19.4.29 The actual quantum of the operational expenses would be driven by the best available market terms for the given described service levels. Given the potential size of SPEARS, it is likely that very keen market prices would be available. Significant reductions in member charges from current levels could be expected.

19.4.30 In setting the terms on which the various services would be contracted out, explicit steps should be taken to minimise the potential for providers to obtain hidden charges. Charges from each provider should be fully accounted for and visible in order to ensure that SPEARS would operate in a cost-efficient and value for money manner.

19.4.31 We would envisage that the general arrangement and roles of the key players in the operation of SPEARS would be as represented in the following diagram.



19.4.32 Having identified the shortcomings in existing AVC practice and examined the development of a new AVC-type arrangement for the public service, we now move on to consider the schemes for purchase of notional service.

19.5 Review of shortcomings in schemes for purchase of notional service

19.5.1 We have outlined in Paragraph 12.11.2 the very real advantages to public servants of existing schemes for the purchase of notional service. In assessing the value for money of a pension provided by an AVC (i.e. excluding lump sum) compared with a pension provided under a purchase scheme, much depends on the circumstances of the individual. However, it may be concluded that, provided they meet the eligibility requirements of the purchase scheme, public servants who wish to secure additional pension would in many circumstances be better advised on cost grounds to avail of the purchase scheme rather than AVCs. Also, the purchase schemes have the advantage of offering a *guaranteed* addition to pension benefits, together with a pension which will be increased in line with increases to public service pensions generally. Of course, this comparison leaves out of account the additional flexibility of AVCs and their facility for increasing lump sum benefit, features which might be of particular worth to the individual.

19.5.2 In light of the above, it is clear that the purchase of service arrangement represents a valuable condition of service. (It is open to private sector schemes to provide such an option, but most choose not to do so.) For this reason, the Commission has given careful consideration to the future of the purchase schemes, whether as the continuation of a separate option to AVCs, or as amended to form part of SPEARS as a single vehicle for the delivery of pension scheme flexibility.

19.5.3 The **arguments in favour of retaining a separate facility for the purchase of notional service** in the context of the introduction of SPEARS include:

(i) purchase schemes operate in a relatively straightforward manner and are valued as an attractive feature of public service pension arrangements. The purchase option suits individuals who wish to guarantee an additional pension at retirement which is directly linked to their final remuneration, rather than to external factors such as investment return. The fact that no administration costs are imposed and that pensions are increased in line with general pension increases are also relevant considerations;

(ii) the purchase schemes now in existence are valued by employees. The State benefits from employee appreciation and so would be reluctant to recommend their removal;

(iii) while take-up of purchase schemes appears to be relatively low (see Paragraph 12.10.14), the State (and, possibly, the public service unions) could remedy this by becoming more directly involved in the active marketing of the purchase option. This would help to ensure that more comprehensive information was made available on the relative merits of purchase compared with AVCs;

(iv) while the rules of purchase schemes are seen as overly rigid, they could be amended to make them more flexible. Changes might include: purchase of any one or combination of lump sum, pension, and spouses' and children's pensions, purchase by reference to a range of retirement ages, not just age 65, and allowing for additional lump sum contributions alongside periodic contributions;

(v) difficulties regarding the assumptions underpinning the purchase rates, e.g. in relation to salary progression, could largely be addressed by introducing a wider set of tables for groups having broadly similar circumstances. This would ensure greater equity in the arrangements;

(vi) if the purchase option were not available, public servants would be obliged to avail of AVCs and to purchase annuities in order to enhance their retirement pension. Annuity rates can be subject to considerable volatility and variation and are now at historically low levels. These factors could lead to considerable pressure to retain the purchase option (however, the changes made in the Finance Act, 2000 have changed the position somewhat).

19.5.4 The **arguments against retaining a separate facility for the purchase of notional service** include:

(i) the continuation of two separate and, to a certain extent, competing arrangements for public servants to improve their pension benefits (SPEARS and the purchase schemes) would leave open the problem of ensuring that comprehensive and objective information on the relative advantages and disadvantages of each was being made available. At present, the State makes little effort to communicate the relative merits of the purchase option, whereas private providers market the AVC option in an active way;

(ii) by their design, purchase schemes are subject to fixed conditions and requirements. While changes are possible, it would be virtually impossible to adapt them to provide the same kind of flexibility which AVCs can offer (and which has recently been extended in the Finance Act, 2000 in relation to the drawdown of benefits);

(iii) the assumptions used in drawing up the purchase tables result in significant cross-subsidisations, arising in particular from different rates of career and salary progression for groups and individuals within groups. It would be extremely difficult to provide *fair* contribution rates which would be appropriate for all. In addition, the establishment of separate tables could hinder mobility within the public service;

(iv) with the extension of full PRSI to all public servants, it has become virtually impossible to devise tables capable of catering for lump sum contributions shortly after entry (this is because the figure for net remuneration — on which contributions are based — can be low);

(v) take-up of purchase schemes is relatively low compared with take-up of AVCs. Accordingly, it would seem reasonable to ask the State to promote purchase schemes more actively and to highlight their advantages *vis-à-vis* AVCs. However, to do so would expose the shortcomings outlined above and increase the risks underwritten by the State in the purchase rates in relation to future salary progression, life expectancy, and future rates of pension increase. In addition, it is arguable that the assumption of pension fund investment returns, which helps to underpin the competitiveness of the purchase rates, in fact serves to impose additional costs upon the State, the greater the level of take-up.

19.5.5 In analysing the arguments for and against retaining the purchase schemes, we were particularly conscious that there is an increasing demand amongst many public servants to be able to prepare and plan for their retirement in as flexible, cost-effective and secure a means as possible.

19.5.6 Having regard to the development of SPEARS as an improved AVC-type option for the public service and the difficulties which would be involved in amending purchase of notional service so as to provide the degree of flexibility required by public servants, as well as a fair and equitable pricing basis, we have concluded that a revised purchase arrangement should be introduced, which would allow the use of SPEARS to purchase a public service pension (we address this option in Section 19.6). In this context, we would favour the phasing out of the purchase of notional service schemes. The precise period over which this should be done should be determined by the State, in consultation with the public service unions, based on the level of take-up of the scheme in comparison with the new SPEARS option.

19.6 Use of SPEARS to purchase index-linked public service pensions

19.6.1 Notwithstanding the relatively low level of take-up of the notional purchase schemes, the security which the schemes offer, in particular, the provision of guaranteed index-linked public service pensions which are not dependent on investment returns and annuity rates, means that they are widely considered as an attractive element of public service pension arrangements. Consequently, we believe that it is important that any alternative scheme should take account of this desire for pension security while at the same time providing for enhanced member flexibility.

19.6.2 Accordingly, we propose the introduction of a facility under SPEARS to purchase an amount of public service pension. We note that a similar facility to use an AVC to purchase pension under the main company pension scheme, rather than to purchase an external annuity, is available in a number of private sector companies. The facility to convert some or all of the SPEARS saving account into a cash value public service pension would be exercised at retirement, or could be done at any stage prior to retirement (as a preserved benefit). We illustrate some examples of the use of SPEARS in this way in Section 19.7. As with existing AVC plans, public servants would continue to have the option under SPEARS to purchase an annuity at retirement, or to draw down the balance on their accounts in accordance with the new flexibilities under the Finance Act, 2000 (see Paragraph 19.4.7).

19.6.3 Under the proposed new mechanism, it would also be possible to convert lump sum payments by the individual and transfer payments received from other schemes immediately into an amount of preserved pension, indexed in line with public service pensions generally (see below), and payable at retirement age. This could be done as an alternative to investing these amounts under SPEARS and converting them into pension at retirement. In addition, this mechanism would be capable of providing at retirement for the conversion of some or all of the retirement lump sum into additional pension (see Paragraph 22.9.45).

19.6.4 We would envisage that a public service pension secured in this way, whether at point of retirement or at an earlier stage, would be increased in line with the Public Service Earnings Index which we recommend should be introduced in Chapter 16. The cost of pension increases on this basis would be factored into the purchase price.

Purchase rates for public service pension

19.6.5 The balance of the SPEARS saving account (including any lump sum cash payment, transfer amount, or converted retirement lump sum) would be used to secure a guaranteed level of deferred pension income payable from age 60 using actuarial principles. The key financial assumption would be the difference between the expected level of investment return and the rate of increase in the Public Service Earnings Index. Specifically, an age-related table would be drawn up to facilitate this conversion process.

19.6.6 At a detailed level, it would be necessary to firm up on the precise financial and demographic assumptions to be used for pricing purposes. Given the absence of any linkage to an individual's promotional salary achievement, we believe that a single age-related purchase table should be applied to all public servants. In the interests of simplicity we would recommend that such a purchase table be priced on a single (unisex) basis.

19.6.7 The new purchase table would set out, by age, the rates of conversion of a lump sum cash amount into annual pension, payable from age 60 and increased in line with the Public Service Earnings Index. Retirement earlier than age 60 would result in an actuarial reduction factor being applied; retirement later than age 60 would result in actuarial enhancement. An option to purchase spouses' and children's pensions in case of death after retirement would also be available.

19.6.8 As noted above, conversion into pension could be done before retirement or at point of retirement. In the event of death-in-service following the conversion, the capitalised value of the pension would be calculated using the same purchase tables, and would be available as a lump sum payment.

19.6.9 We envisage that the State would underwrite the pension purchased under this mechanism in much the same way as it provides for payments under the current purchase of notional service schemes.

19.6.10 The key exposures to the State would be to ensure that the long-term financial experience (i.e. the difference between the notional long-term investment return and the increase in the Public Service Earnings Index over the same period) would not be lower than the assumed rate underlying the purchase table and that an appropriate allowance was made for the life expectancy of public service employees. In any event, we would envisage that the purchase table would be subject to regular actuarial reviews and adjusted as necessary over time. Any adjustments could affect all future purchases of pension after the effective date of the pricing adjustment.

19.6.11 To facilitate the introduction of the proposed system it is likely that an amendment to the Pensions Act, 1990 would be necessary, similar to that needed to allow for payment of transfer values to unfunded public service schemes (see Paragraph 8.16.4).

19.7 Examples of purchase of public service pension under SPEARS

19.7.1 A number of examples might help to illustrate how we envisage that the proposed new purchase mechanism under SPEARS would work.

Example 1: Planning for maximum benefits/retirement at age 60

19.7.2 A civil servant in full PRSI class takes up employment at age 23 on an annual salary of £16,000. At age 28, the civil servant decides that he or she would like to be able to retire at age 60 with maximum, or close to maximum, benefits.

19.7.3 We assume that the individual will have steady incremental and career progression until age 45, when he or she reaches the maximum salary point of the grade at which he or she will eventually retire. We also assume that the current maximum salary for this grade is £30,000 per annum, and that this rate will increase in line with general pay increases.

19.7.4 The rate of general pay increase is assumed at 4% per annum. The May 2000 rate of Old Age (Contributory) Pension (OACP) is £96 per week, and is assumed to increase in line with general pay increases. Investment return is assumed to be 7% per annum, in nominal terms. Charges on SPEARS are assumed to comprise an annual charge of 1% of the fund.

19.7.5 At age 60, retirement benefits would in the normal course consist of a pension of 37/80ths of net pensionable remuneration and lump sum of 111/80ths of pensionable remuneration. To secure benefits equivalent to 40 years' service at age 60 (pension of 40/80ths, lump sum of 120/80ths), it is necessary for the civil servant to contribute to SPEARS in order to make up the shortfall.[244]

19.7.6 If the civil servant contributed to SPEARS from age 28 onwards at a rate of *1.5% per annum* of remuneration, then, on the basis of the above assumptions, he or she would have a savings account balance at age 60 of *£74,000*. On the basis of our estimate of the purchase table rates — priced on a single (unisex) basis — this would be sufficient to make good the shortfall in maximum benefits, i.e. to provide lump sum of 9/80ths of pensionable remuneration, a retirement pension equivalent to 3/80ths of net pensionable remuneration, and spouses' and children's pension. The additional pension purchased would be increased in line with the Public Service Earnings Index.

19.7.7 The civil servant would have the option not to *buy* all three elements of public service pension benefits — for example, he or she might wish to purchase additional retirement pension only. Given the same assumptions, this would imply a lower contribution rate to SPEARS. The individual would also have the option, as with existing AVC schemes, to buy an annuity on the open market or to drawdown the SPEARS account in accordance with the recent Finance Act changes.

[244] For the purpose of this example, we assume that the civil servant does not contribute to SPEARS with the intention of bridging the gap between an integrated and a non-integrated pension.

19.7.8 If, during the course of his or her career, the civil servant decided to retire earlier than age 60, the SPEARS account would be available to provide additional pension benefits, subject to the Revenue limits.

19.7.9 Because this is an AVC route to securing additional pension, it would be open to the civil servant at any age to increase or to reduce the rate of contribution, for example, on reconsidering his or her planned age of retirement, or if investment returns to the fund were better or worse than expected. It would also be possible to make lump sum contributions into SPEARS at any stage during service, subject to the Revenue limits.

Example 2: Pension on non-pensionable elements of pay

19.7.10 A public servant in full PRSI class takes up service at age 25, and receives a salary of £12,000 per annum and non-pensionable allowances of £3,000 per annum. He or she plans to retire at age 65, and wishes to contribute so as to maximise pension at that age.

19.7.11 The general assumptions are as set out in the earlier example. We assume that the individual in this example experiences relatively low career and salary progression, and will retire from a grade for which the current salary maximum is £15,000 per annum. This pay figure, and the amount of non-pensionable allowances of £3,000 per annum, are assumed to increase in line with future general pay increases.

19.7.12 Because the employee's occupational pension is subject to integration, he or she has the option to contribute towards the cost of the difference between an integrated and a non-integrated pension. Alternatively, or in addition, the employee may contribute in order to secure pension benefits on the £3,000 non-pensionable income at retirement.

19.7.13 We assume that the employee chooses the latter route only. By contributing to SPEARS at a rate of *2.8% per annum* of remuneration from age 25 to age 65, he or she would have a savings account of *£135,000* which would be sufficient to obtain full pension benefits on the non-pensionable allowances. The additional pension purchased would be increased in line with the Public Service Earnings Index.

19.7.14 There are many assumptions involved in these two examples, the most important of which are the rate of investment return, career and salary progression, and general salary increases. The outcome could be quite different if these assumptions were not realised in practice. For instance, a lower rate of investment return could significantly reduce the size of the savings account available at retirement. In any event, as with AVCs generally, the individual would be well advised to continuously review his or her pension savings decision and to consult regularly with the SPEARS administrators and promoters. Of course, there would be no risk exposure once the public service pension had been purchased.

19.8 Advantages of using SPEARS to purchase public service pension

19.8.1 The key advantages of the proposed mechanism would include the following:

- it would enable public servants to secure guaranteed pensions that qualified for indexation at the same rate as under the main pension scheme (i.e. in line with the Public Service Earnings Index);
- it would be sufficiently flexible to accommodate a range of retirement ages, varying contributions, non-pensionable earnings, etc.;

- it would be a key promotional characteristic relative to other AVC offerings available in the market;
- the single pricing structure would provide for a more simplified administrative process than the existing purchase of notional service regime;
- all pension conversions would be carried out by reference to the Public Service Earnings Index; therefore, equity would be achieved between members because:
  - pricing would be unaffected by expected career and salary progression; and
  - anomalies between contributions paid and benefits received due to varying salary progression of different groups during service would be removed.

19.8.2 The mechanism which we are proposing would be a predictable and stable means of purchasing pensions. It is highly unlikely that the market of its own accord would deliver such a vehicle, particularly as there are no suitable assets which would provide matching to the rate of return of the Public Service Earnings Index. Therefore, we envisage that the State would effectively manage the pricing and benefit payments under the purchase system.

19.8.3 The risk to the State under the proposed mechanism would mirror the position under existing purchase of notional service schemes. In fact, the risk to the State would be lower under SPEARS compared with the purchase schemes because the commitment would be to pay guaranteed amounts of additional pension rising in line with the Public Service Earnings Index, rather than additional pension years, the value of which would depend upon the individual's grade and salary point at retirement.

19.8.4 By rolling the defined contribution and defined benefit options together under SPEARS, they can both be promoted on an equal basis as one approach would not necessarily be competing with the other for funds.

19.8.5 In summary, the option to purchase a public service pension would not be an essential part of a reconstituted public service-wide AVC-type facility. However, if included, the Commission believes that the scheme would provide a far more comprehensive range of pension choice than would be available through a combination of a reconstituted but exclusively defined contribution AVC or group PRSA scheme plus the existing purchase arrangements. Furthermore, as listed above, there would be a number of important advantages to public servants and to the State if this proposal were implemented.

19.9 Implications for existing arrangements

19.9.1 As SPEARS would have significant implications for the continuation of AVC schemes, we believe that careful consideration should be given to those participating in existing arrangements.

19.9.2 There are a number of options in relation to existing AVC arrangements. These range from allowing the existing arrangements to remain in place and having SPEARS as an additional option available, to the State unilaterally forcing the trustees to wind-up and discontinue existing arrangements and transfer investments to alternative vehicles.

19.9.3 In our view, neither of these two approaches would be satisfactory. The main disadvantage of leaving the existing arrangements in place would be the high level of fragmentation and extra administrative burden that would be experienced by the State on an ongoing basis. To the extent that SPEARS would offer better value for money to individual employees, and at least equivalent levels of flexibility as existing arrangements, we do not see why such a wide range of schemes should continue to be facilitated.

19.9.4 As the sponsoring employer, the State has the power under the trust deeds of the existing AVC arrangements to require them to be discontinued and wound up, subject to the giving of a short period of notice to the trustees. Forcing a wind-up of existing AVC schemes could have significant adverse consequences for participating members. Therefore such an approach would equally not be viable.

19.9.5 A possible solution would be the adoption of a partnership approach between the State and the public service unions to ensure that the efficiencies of SPEARS were made available to all employees without undermining the possible continued participation of employees who are currently availing of existing arrangements.

19.9.6 This could best be achieved by closing existing arrangements to new entrants and reviewing each scheme in conjunction with the relevant trade union. The purpose of the review would be to assess whether it was in the best interest of the members to:

- continue contributing to the scheme through to retirement age;
- pay future contributions to SPEARS but to retain accumulated investments within the existing arrangement; or
- transfer both future contributions and existing investments to SPEARS.

Such a review would have to be carried out on a scheme by scheme basis as it would be dependent upon the specific terms and conditions under which each scheme was set up.

19.9.7 It would be important that the public service unions fully supported the implementation of SPEARS. Given that they are identified as sponsors of the existing AVC arrangements (even though they are not a direct party to most of the trust deeds) they have a significant sense of ownership and responsibility in this area. Only by adopting a partnership approach would it be possible to create a harmonious environment in which the significant benefits of SPEARS could be realised.

19.9.8 Existing providers could be invited to participate in the tender process for the provision of services in connection with the operation of SPEARS as their existing experience, systems and distribution mechanisms could be of considerable value to the successful implementation of SPEARS.

19.10 Conclusions and recommendations

19.10.1 The existing arrangements for the provision of pensions flexibility for public servants are the schemes for purchase of notional service and AVCs. Purchase of notional service has the advantages that it is designed to be self-financing and that it provides certainty in relation to the benefits purchased. Its disadvantages are its strict eligibility requirements, inflexibility as regards benefits purchased, and pricing anomalies. AVCs have the advantages of flexibility, external funding, good communication and promotion. Their disadvantages include the uncertainty of benefits, administrative charges, and fragmentation of schemes across the public service. The level of take-up of AVC schemes would appear to be high, particularly when compared with the take-up under the purchase schemes.

19.10.2 In this Chapter, the Commission has developed a new AVC-type arrangement for the public service (SPEARS), which would represent a drawing together of the two existing arrangements in a way which would address some of the shortcomings of both. SPEARS would have a strong *product profile* and would represent a new and valuable benefit to public servants. In the context of our recommendation for the introduction of cost-neutral early retirement from age 50 on (see Paragraph 15.15.14), the scheme would give public servants the option to avail of a well designed, cost-effective, and adaptable facility to provide them with genuine retirement choice.

19.10.3 For the State, the new scheme would meet its requirements in relation to cost, administrative convenience and the minimisation of any possible exposure under the legal and regulatory framework applying to the facility.

19.10.4 Accordingly, the Commission recommends the introduction, in consultation with the public service unions and having regard to the position of existing AVC schemes, of a single AVC-type scheme for the public service as a whole. We recommend that this scheme should be established and operated broadly along the lines envisaged in this Chapter, and called the Scheme for Public Employees' Additional Retirement Savings (SPEARS). SPEARS should include a savings account facility and a lump sum death benefit facility. In addition to providing the options available under existing AVC schemes, SPEARS should incorporate a new purchase arrangement to enable the use of the savings account at, or prior to, retirement to purchase an amount of public service pension, which would be increased in line with public service pensions generally.

19.10.5 We recommend that the structure of SPEARS (AVC, group PRSA, or other) should be decided once the framework for PRSAs has been put in place. However, in the event that the scheme were set up initially as an AVC under trust deed, we recommend that the independent trustees of the scheme should include representatives of public service unions and employers. It might be considered desirable to convert SPEARS into a group PRSA in due course and this matter should be decided by the State at the appropriate time, in consultation with the public service unions.

19.10.6 The Commission recommends that existing schemes for the purchase of notional service should be phased out, the precise period involved to be determined by the State in consultation with the public service unions, based on the level of take-up of the schemes in comparison with the new SPEARS option.

19.10.7 SPEARS should include an option at retirement to use any or all of the retirement lump sum to purchase additional pension.

19.10.8 We recommend that the State should consider meeting part of the administrative cost of SPEARS, in particular, the cost of promoting the scheme, in the context of the phased removal of the schemes for purchase of notional service.

19.10.9 As we have noted in Paragraph 12.12.8, the Revenue limits can have an important impact on the pension benefits which an individual can fund towards, including early retirement. While not formally coming within our terms of reference, the Commission would suggest that consideration should be given to introducing greater flexibility into the operation of these limits. We note that greater simplification in the tax treatment of pensions is recommended in the National Pensions Policy Initiative.[245]

[245] The Pensions Board, *Securing Retirement Income* (1998), p. 147.

CHAPTER 20

Dependants' Benefits

20.1 Introduction

20.1.1 The spouses' and children's contributory pension schemes and death-in-service benefits provided under the main pension schemes are key components in the public service pension system. We consider that the former, in particular, have proved to be one of the more important developments in public service pensions policy over the last 30 years. Through public service spouses' and children's schemes, it has been possible to provide for the surviving family members of public servants when they die after retirement or while in public service employment. As well as meeting an important social need, the schemes have helped ensure a degree of financial security and peace of mind for individual public servants and for their dependants.

20.1.2 The first widows' and orphans' scheme, the civil service scheme, was introduced in 1968. Similar schemes were subsequently introduced throughout the rest of the public service. In due course, with the admission of female public servants from 1981 on, the schemes were changed to spouses' and children's schemes.

20.1.3 In summary, the schemes provide the spouse and children of a contributing member with an entitlement to a pension on the death of the member. Pensions are calculated as a fraction of the deceased member's pension, which is defined as the actual rate of pension in payment to the member at time of death or, in case of death-in-service or death following ill health retirement, of the member's potential pension had he or she served to age 65. The rate of spouse's pension is one-half of the deceased member's pension; the rate of children's pension (where a spouse's pension is in payment) is one-sixth of the deceased member's pension in respect of each child, up to a maximum of three children. Members of the scheme generally pay periodic contributions at a rate of $1\frac{1}{2}$% of remuneration, plus 1% of final remuneration for any period of pensionable service for which periodic contributions were not paid. In 1997, the total number of individuals in receipt of spouses' and children's pensions in the public service as a whole was approximately 19,000 persons, representing almost a quarter of all public service pensioners.

20.1.4 The death gratuity was first introduced into the Civil Service Pension Scheme in 1909. A death gratuity is payable where a public servant dies while in public service employment. It is calculated at a rate of between one and one-and-a-half times pensionable remuneration, depending on service at time of death.[246] The death gratuity is normally payable to the legal personal representative, and is in addition to any benefits payable under the spouses' and children's scheme.

20.1.5 We set out further information on the history, terms and conditions of spouses' and children's pension schemes and of the death gratuity in Chapter 3.

[246] A preserved death gratuity, equal to the amount of preserved lump sum, is payable on the death of former public servants who had an entitlement to preserved benefits (see Paragraph 3.3.44).

20.1.6 The purpose of this Chapter is to consider the continuing need for, and role of, spouses' and children's schemes within the public service pensions framework, and to examine a range of other issues which have arisen in relation to dependants' benefits. We present our deliberations and recommendations below under the following headings:

- role of spouses' and children's pension schemes;
- membership option for spouses' and children's schemes;
- extension of scheme beneficiaries to include non-marital partners;
- other spouses' and children's scheme issues;
- death gratuity;
- nomination of beneficiary for receipt of death gratuity.

20.2 Role of spouses' and children's pension schemes

20.2.1 In the late 1960s and 1970s, when widows' and orphans' schemes were being introduced in the public service, the social and economic environment was one in which the vast majority of married women did not have paid employment and were almost universally dependent on their husbands. The widows of public servants were often financially vulnerable, particularly in old age, as many had no entitlement to a widow's pension under the State Social Insurance system.

20.2.2 Over the intervening period, the financial position of the spouses of public servants has changed quite significantly due to a number of factors. Firstly, an increasing number of women are now joining the labour force. According to the CSO, there have been dramatic gains in the labour force participation rates of married females in the recent past.[247] Notwithstanding these increases, Ireland still lags somewhat behind most countries in the EU in terms of the labour force participation of married females, and the CSO assume that the catching-up process will continue. Apart from their independent source of income while in employment, many married females are members of pension schemes in their own right, and so do not have the same need as before for dependants' pensions deriving from their husbands' pension entitlements. The introduction of PRSAs may have the effect of extending pensions coverage more widely still.

20.2.3 Secondly, there have been major developments in the coverage and eligibility provisions of the Social Welfare system over the past thirty years, with the result that many spouses of public servants might be considered to be already provided with an adequate basic level of income protection.

20.2.4 Thirdly, the extension of spouses' and children's schemes in 1981 (later in some sectors) to cover female public servants also impacted upon the stated rationale behind the original introduction of the schemes in the 1960s and 1970s, which was to provide welfare support to widows who would not have had any independent means of support.

20.2.5 Given these developments, it can be argued that the concept of dependants' pensions has become outdated, and that in the present social and economic environment, married couples should be expected to take individual responsibility for their own pension provision. This would

[247] Central Statistics Office, *Population and Labour Force Projections, 2001-2031* (July 1999), p. 22; according to the CSO, the average annual increase in participation rates for married females aged 25-49 in the period 1986-98 ranged from 3.6% per annum for 25-29 year olds to 6.7% per annum for 35-39 year olds.

be consistent with the trend of reforms in the tax and Social Welfare systems, which place an increasing emphasis on the individualisation of allowances, reliefs and benefits.

20.2.6 On the other hand, the arguments in favour of retaining spouses' and children's schemes, in their present format, as an integral part of the public service pension system are as follows:

- the schemes were introduced to protect those who were financially vulnerable and dependent, particularly in their old age. Notwithstanding the trends discussed above, there will almost certainly be individuals who continue to come into this category in the future;
- spouses' and children's benefits represent an entitlement for which public servants make a contribution of $1\frac{1}{2}$% of remuneration (designed to represent one-half of the cost of the scheme);
- we understand that the definition of *dependency* used by the Revenue Commissioners in relation to occupational pension schemes, in effect, recognises *financial interdependence*, i.e. the Revenue rules allow payment of a dependant's pension in cases where a second income has been relied upon to maintain a certain standard of living prior to the member's death;
- benefits for dependants in defined benefit schemes in the private sector (see Section 8.13) and in public service pension schemes abroad (see Chapter 9) are broadly similar to those provided under public service schemes in Ireland.

20.2.7 Having assessed the trends and arguments set out above, the Commission is of the view that spouses' and children's schemes are an important part of the overall public service pensions framework, one to which public servants and their unions are committed. While social circumstances have changed markedly since the schemes were first introduced — resulting in a different understanding of what a dependants' benefit scheme should offer, i.e. a form of insurance cover to provide for financial interdependency — the Commission does not see any convincing argument for revising the basic structure of the schemes, particularly since they continue to play an important role in protecting those who are financially vulnerable and dependent. In reaching this conclusion, the Commission was particularly conscious of the role played by the public service unions in the original introduction and subsequent development of the schemes, and of the continuing $1\frac{1}{2}$% contribution which is being made by public servants towards the cost of the schemes.

20.2.8 In Paragraph 25.3.8 below, we recommend that, for reasons of administrative efficiency, consideration should be given to drawing up a single public service occupational pension scheme and/or rationalising the large number of separate schemes currently in existence. We recommend that spouses' and children's schemes should be included in that process. Furthermore, we do not see that there is a value in maintaining spouses' and children's schemes separately from main pension schemes.

20.2.9 It could be argued that the absorption of the employee spouses' and children's contribution rate into an overall pension scheme contribution rate would weaken the financial discipline imposed by having separate spouses' and children's schemes jointly financed by public service employers and employees. However, the reality is that spouses' and children's schemes and contribution rates are not subject to periodic valuation and review, separate from main pension schemes. We believe that our recommendations in relation to transparency in pension costs and liabilities generally, as set out in Chapter 24, should help to ensure a disciplined approach in the future in relation to both main scheme and spouses' and children's scheme costs.

20.3 Membership option for spouses' and children's schemes

Background

20.3.1 The *original* widows' and orphans' contributory pension schemes were introduced for male public servants in most parts of the public service between 1968 and 1971. In general, the schemes were extended to include female public servants from 1981 onwards.

20.3.2 At the time of their original introduction and subsequent extension to include female public servants, membership of the schemes was made automatic for new entrants, and optional for those who were then in service. This latter provision was necessary because of the contributory nature of the scheme — periodic contributions were required, along with a lump sum deduction from gratuity or lump sum for pre-membership service — and the fact that the individual circumstances of public servants would determine to what extent, if at all, they would be likely to gain as a result of joining the scheme. This approach was agreed with the public service unions.

20.3.3 The *revised* spouses' and children's contributory pension schemes were introduced to most parts of the public service in 1984 (or shortly afterwards). While the original schemes restrict the classes of beneficiaries to spouses and children of marriages which take place prior to leaving public service employment, the revised schemes cover post-retirement marriages and children born outside of marriage. In order to meet the additional costs of the wider definition of beneficiaries in the revised schemes, the contribution refund arrangements were made more restrictive than in the original schemes.

20.3.4 Following the approach adopted with the original schemes, the revised schemes were applied automatically to new entrants to areas in which they were introduced. An option to join the schemes was made available not only to serving staff (including those who had opted not to join the original scheme), but also to retired public servants and to the surviving spouses of former public servants. Member contributions were calculated in broadly the same way for all groups, i.e. by means of periodic contributions and/or lump sum deduction to ensure that contributions were made in respect of the full period of pensionable service. In the case of surviving spouses and retired public servants who opted to join the schemes but died subsequently before having paid the full amount due, outstanding contributions were recovered by withholding payment of spouses' pensions for a certain period of time (it was calculated that the period of withholding pension would not exceed 18 months and six days).

20.3.5 The revised schemes were not introduced in the particular case of national and secondary teachers (vocational teachers were included in the introduction of the revised scheme under the Local Government Superannuation Scheme). This was because the terms under which the schemes were introduced in the civil service and elsewhere did not prove acceptable to the relevant teachers' unions. Thus, unlike most other public service groups, national and secondary teachers have availed of just one option to join the schemes. Recently, there have been discussions with the teachers' unions about the possibility of introducing the revised schemes for new entrants and of giving a membership option to serving national and secondary teachers who are already members of the original schemes and who did not have an option to join the revised schemes.

20.3.6 It would appear that no actuarial costings were carried out in 1984 or later on the cost impact of introducing the revised spouses' and children's schemes. However, it seems clear that a substantial cost would have arisen as a result of offering scheme membership to retired personnel who had previously opted not to join the original scheme, and as a result of paying spouses' pensions (following a withholding period) to the surviving spouses of deceased public servants who had originally decided not to join. Payment of benefit was virtually guaranteed in all cases, and the amount of contributions received would have represented only a small element of the total cost involved.

20.3.7 For a variety of reasons, a number of serving public servants, both male and female, declined to join the revised and/or original spouses' and children's contributory pension schemes. This was a public service-wide phenomenon. A range of submissions received by the Commission sought a new option to join the schemes. We examine below the arguments for and against allowing a new option to join the schemes, and make a number of recommendations based on our analysis.

20.3.8 In Table 20.1, we set out an estimate of the number of members and non-members of spouses' and children's schemes in the public service in 1997.[248] The figures show that just under 7,700 male public servants and approximately 20,500 female public servants were listed as not being covered by spouses' and children's schemes. Obviously, employees who were most recently offered the option to join, for example, female public servants and non-established public servants, represent the greatest numbers of non-members.

Table 20.1: Members and non-members of spouses' and children's schemes

Sector	Members		Non-members		Total
	Males	Females	Males	Females	
Civil service	13,826	11,523	894	2,815	29,058
Local authorities	16,541	2,355	2,659	2,438	23,993
Education	19,798	23,803	2,441	10,107	56,149
Gardaí	9,878	868	–	–	10,746
Prison Officers	2,224	252	–	–	2,476
Defence*	12,196	263	639	–	13,098
Health	13,070	41,415	689	4,605	59,779
NCSS bodies	4,544	2,442	368	566	7,920
Total	**92,077**	**82,921**	**7,690**	**20,531**	**203,219**

* Most of those in the Defence Forces who opted not to join the spouses' and children's scheme are no longer in public service employment.

20.3.9 The main factors which may have influenced individual public servants in their decision not to join spouses' and children's contributory pension schemes included:

- age at time of option;
- personal circumstances at time of option, e.g. if single or separated (divorce and remarriage was not available);
- reluctance to meet cost of periodic contributions and/or lump sum deduction, particularly if close to retirement and the amount of lump sum deduction was high;
- ignorance of consequences of decision, or failure to consider the possibility of a future change in personal circumstances;
- perception of female employees that they would not need pensions cover for their spouses and dependants.

[248] Commission on Public Service Pensions, "Further Actuarial Review of Impact of Changes to Pension Scheme Terms" (October 1999), Report prepared by Mercer Ltd. Because of incomplete data it was necessary to estimate the level of membership of the spouses' and children's scheme in many cases.

Arguments against new option to join spouses' and children's schemes

20.3.10 There are a number of arguments against providing another option to join the spouses' and children's schemes, principal among which is cost. The schemes are based, generally, on the insurance principle, with the employee contribution of 1.5% of remuneration designed to meet one-half of the cost. This contribution rate is based on the long run costs associated with mandatory membership. A new option, if granted, would almost entirely be availed of in cases where an immediate benefit was payable or where there was high expectation of benefit, as happened in the offer of the 1984 revised schemes. There could, therefore, be substantial costs involved and this would have implications for the contribution rates.

20.3.11 The Commission obtained actuarial advice on the impact of providing a new option to those who had previously declined to join the schemes. It was decided to cost the option on the same basis as the 1984 revised scheme option. Thus, pensioners and surviving spouses would also be included in the option as costed.[249]

20.3.12 The costing was prepared on the basis of the provision of standard benefits, i.e. a spouse's pension of 50% of the member's current or prospective pension, plus children's pensions of up to a further 50% of the member's pension for the three categories of people affected: serving staff, retired members and surviving spouses. It should be noted that it is not possible to forecast the take-up of a new offer to join spouses' and children's schemes with any certainty. The general approach adopted has been to show the extra costs if there were a 100% take-up by those not in the schemes at the moment.

Serving staff

20.3.13 For serving employees, the figures showed that if all those currently outside the scheme decided to accept the new offer, there would be an addition of £103 million to the existing estimate of overall accrued liabilities of £20 billion (as at 1 January 1997).

20.3.14 Table 20.2 summarises the effect on cash flows, both benefit expenditure and contribution income, at 20 yearly intervals from 1997.

Table 20.2: New spouses' and children's offer for serving members

	Benefit expenditure			Contribution income		
	Original projection	Projection if take-up is 100%	Relative difference	Original projection	Projection if take-up is 100%	Relative difference
Year	£m	£m	%	£m	£m	%
1997	122	116	–4.9	185	193	4.3
2017	1,502	1,513	0.7	241	244	1.2
2037	2,465	2,494	1.2	351	351	–

Note: Benefit expenditure represents total pension expenditure for serving staff, not just expenditure under spouses' and children's schemes; in 1997, the figures represented primarily the cost of retirement lump sum and death gratuity, and an element of pensions costs, in respect of those who retired or died in service during that year.

[249] Commission on Public Service Pensions, "Further Actuarial Review of Impact of Changes to Pension Scheme Terms", Report prepared by Mercer Ltd. (October 1999).

20.3.15 From the table, it can be seen that benefit expenditure after the new offer would be lower, reflecting the higher lump sum deductions from gratuity that apply to retirees in those years. Gradually, the extra spouses' and children's benefits would fall to be paid and this would outweigh the gratuity effect.

Pensioners

20.3.16 The impact of a new spouses' and children's scheme offer was examined for three specific pensioner groups: civil service, teachers (national and secondary), and members of the Defence Forces.

20.3.17 It was assumed for the three groups that all pensioners not currently in the schemes would accept the new offer to join. In this scenario, the increase in the State's accrued liabilities (as at 1 January 1997) in respect of retired teachers would be minimal, while there would be an increase of £12 million in the case of retired civil servants, and £23 million in the case of the retired members of the Defence Forces.

20.3.18 The effect of the change on benefit expenditure for all three groups would be relatively low in the case of civil service and teacher pensioners (in 2027, an addition of 3.8% and 3.6%, respectively), and slightly higher in the case of Defence Force pensioners (in 2027, an additional 8.4%). Table 20.3 shows the effect on benefit expenditure at ten yearly intervals from 1997 for all three pensioner groups.

Table 20.3: Projected benefit expenditure for civil service, teacher and Defence Force pensioners

	1997	2007	2017	2027
Original projection for existing retirees (£m)	251	203	127	59
New projection if offer take-up is 100% (£m)	249	204	130	62
Relative difference (%)	–0.8	0.5	2.4	5.1

Dependants of deceased former members

20.3.19 If the approach adopted in 1984 was followed, the option to join the spouses' and children's schemes would be offered to dependants of former public servants who have died and who were never members of the scheme. As information on the number of potential claimants is not available it is not possible to quantify possible liabilities under this heading. They are, however, potentially the most expensive category in terms of cost per individual, since benefits would be paid almost immediately.

Other arguments against a further membership option

20.3.20 Apart from cost, other arguments against allowing a further option to join spouses' and children's schemes are as follows:

- almost all groups in the public service (with the exception of most primary and secondary teachers) have had two options to join the schemes. It is not possible to run pension schemes on a *pick-and-choose* basis;
- a new option to join would mean pressure in the future for yet a further option for those not availing of it;

- a new option would inevitably increase the pressure for an option to leave schemes. This would be relevant particularly in the case of those who are widowed or separated. A major concern about allowing members to leave is that it is possible that a very small number of married members might do so in order to exclude a spouse from benefit for vindictive reasons, with consequent pressure for special treatment of the surviving spouse on the death of the former member.

Arguments in favour of new option to join spouses' and children's schemes

20.3.21 The following points may be made to justify allowing a further option to join spouses' and children's schemes:

- although explanatory material was circulated, the terms and conditions of the schemes, including the irrevocable nature of the option, might not have been fully understood and some of those who opted not to join may have done so without fully appreciating the possible future consequences;
- with the introduction of judicial separation and divorce, personal circumstances may have changed for a number of public servants from the time the original decisions were made (for example, an individual who opted out initially may desire to join the scheme on remarriage);
- social conventions at the time may also have had an influence on why so many female public servants opted not to join the schemes. Many would have held the view that when they got married, they would resign to raise a family, and therefore there was little point in signing up to such a scheme. This position has been changing as greater numbers of women decide to remain in the workforce;
- for certain groups, the proximity of the two options may help explain the large numbers who opted not to join on two successive occasions. Circumstances or views might not have changed significantly in the interval — for example, between 1981 and 1984 in the case of female civil servants; by contrast, the male employees who opted out of the scheme in 1969 had had a long time to reconsider their position between that date and 1984;
- in the specific case of national and secondary teachers, only one option has to date been availed of to join the (original) schemes.

20.3.22 The Commission gave careful consideration to the arguments for and against providing another option to join spouses' and children's schemes. On balance, we have decided not to recommend a further general membership option across the public service as a whole (we address the particular case of teachers separately, in Paragraph 20.3.28). We would be particularly concerned about the major additional costs which a new option would impose, given that it would almost certainly be availed of by those who would either have an immediate entitlement or a high expectation of benefit at a later stage. We would be concerned also that a further option would weaken the integrity of the schemes, leading to pressure for individuals to enter and leave at will. Such a development could undermine fundamentally the financing of the schemes.

20.3.23 We explored the possibility of establishing an appeal mechanism which would enable an examination to be carried out of the circumstances of individuals who are seriously disadvantaged or experience particular hardship as a result of a decision not to join a public service spouses' and children's scheme. However, we decided that it would not be possible to arrive at fair and credible criteria on which to base such an appeal mechanism. For example, it would be difficult to base the decision on factors such as hardship when, as discussed above, it is clear that the concept of *dependency* has changed substantially.

20.3.24 Unlike occupational pension schemes, the Social Welfare system is specifically designed to address the question of hardship where it arises. The vast majority of the spouses of deceased public servants would be entitled to Widow(er)s' Contributory Pensions, Bereavement Grants and, if there are dependent children, Widowed Parents' Grants. The entitlement conditions for such benefits are very flexible and can be based on either spouse's Social Insurance record. If the person does not qualify for a contributory pension, a non-contributory pension is payable, subject to a means test.

20.3.25 The Commission accepts that in a number of cases, perceptions of injustice may have arisen as a result of the exercise of past options not to join public service spouses' and children's pension schemes. For the reasons already discussed, we do not believe that it is possible to consider as a basis of appeal the experiencing of hardship on the part of the individuals affected. However, we consider that a valid appeal mechanism, one which would stand up to legal scrutiny, would involve an examination of the exercise of the option itself.

20.3.26 Accordingly, the Commission recommends that a limited appeals process for spouses' and children's scheme membership options be established to examine individual cases and to allow appeals that meet any one of the following criteria:

(i) where there is no evidence that an option was provided to the individual public servant in the first place;

(ii) where there is medical evidence to indicate that the person making the decision not to join the scheme was of sufficiently unsound mind not to appreciate the consequences of his or her decision;

(iii) where a member of the original scheme declined to join the revised scheme in circumstances where there would have been no reasonably foreseeable adverse financial consequences for the individual (in terms only of his or her scheme contributions) had he or she instead opted to join the revised scheme.

20.3.27 With the exception of VEC teachers who at the time were members of the Local Government Superannuation Scheme (LGSS), the revised scheme has not been introduced for teachers, and so there has been no second option for national and secondary teachers who were in service in 1984 to join a spouses' and children's scheme. We understand that the relevant teachers' unions are now favourably disposed to the introduction of the revised scheme for new entrants, and that an offer has been made by management in this regard.

20.3.28 The Commission considers that an option to join spouses' and children's schemes in the case of teachers (other than VEC teachers covered by the LGSS) should proceed on the basis of the management offer made at the Teachers' Conciliation Council (i.e. an option to join the revised schemes is to be offered to national and secondary teachers in the original schemes).

Three members of the Commission expressed reservations regarding the approach adopted in relation to groups which had not had a second option to join public service spouses' and children's schemes — see Paragraph 12 of "Reservation of Senator Joe O'Toole, Rosheen Callender and Dan Murphy".

20.4 Extension of scheme beneficiaries to include non-marital partners

20.4.1 Under public service spouses' and children's schemes, a spouse's pension may only be paid to the legal spouse of the member. This arrangement reflects the constitutional imperative to protect the family based on marriage. Given that many family units are not based on marriage, and in light of pensions practice in the private sector, the Commission decided to examine the question of payment of spouse's pension to non-marital partners. We looked first at the position under the Constitution, which, unlike the case in the private sector, is particularly relevant for the State as sponsor of occupational pension schemes.

20.4.2 The *Constitutional Review Group*[250] stated that the present emphasis of Article 41 of the Constitution is the protection of the rights of the family as a unit rather than the protection of individuals resulting from a family relationship. This approach, the Group argued, presented significant difficulties if the definition of the family unit were to be extended beyond the family based on marriage, given the uncertainties of defining what constitutes a family at any given time.

20.4.3 The Group recommended that a revised Article 41 should retain the pledge to protect the family based on marriage, but that an amendment should be made so as to make it clear that this pledge should not prevent the Oireachtas from providing protection for the benefit of family units based on a relationship other than marriage.

20.4.4 Revenue rules in relation to occupational pension schemes permit the payment of a survivor's pension to a cohabiting partner on the basis that the person was wholly or substantially dependent financially on the employee or was so dependent at the time of the employee's death. In practice, we understand that the existence of dependency is recognised where two people are sharing a household, as financial *interdependence* is the determining factor, i.e. a second income has been relied upon to maintain a certain standard of living prior to the member's death.

20.4.5 Income tax and capital acquisitions tax rules, on the other hand, distinguish between the situation of a family based on marriage and that of a cohabiting couple. It is worth noting in this regard that the report of an interdepartmental group[251] (1999) stated that the group was sympathetic, in principle, to changes in the tax legislation to address issues raised relating to cohabiting couples. Under the Social Insurance system, a qualified adult addition to Retirement or Old Age (Contributory) Pension may be payable if the pension recipient is married or living with someone as husband and wife; however, a widow's or widower's pension is not payable should one partner die.

20.4.6 In contrast to the position in the public service, a significant number of private sector schemes promise a pension to the spouse or other nominated adult person financially dependent upon the member in the case of death-in-service. Under normal circumstances, where the member is married at the time of death, the dependant's pension is paid to the legal spouse. Where a member is cohabiting and has no legal spouse, the trustees have discretion to pay a pension to the member's partner, providing he or she has been appropriately nominated by the member prior to his or her death and a financial interdependency can be shown to exist. A member who is legally separated and is involved in another relationship can nominate his or her cohabiting partner to receive the dependency pension instead of the legal spouse. Under this scenario, the

[250] Government of Ireland, *Report of the Constitutional Review Group* (May 1996).

[251] Department of Social, Community and Family Affairs, *The Report of the Working Group Examining the Treatment of Married, Cohabiting and One-Parent Families Under the Tax and Social Welfare Codes* (1999).

trustees are not obliged to accede to the member's wish, but nomination will generally form an important part of their adjudication.

20.4.7 Of the foreign pension schemes considered in detail by the Commission (see Chapter 8) only the Netherlands makes provision for the payment of pensions to cohabiting partners. In the UK, there have been claims from public sector unions to widen the definition of dependant to include cohabiting and same-sex partners. In response, employers have suggested that the additional cost to the scheme should be met by an increase in the employee contribution rate.[252]

20.4.8 The Commission is sympathetic to the argument that a spouse's pension should be payable to the surviving partner of a public servant where the two parties were living together as husband and wife prior to the member's death, and where financial interdependency can be shown to have existed. A reform of this nature would enable public service schemes to remain reflective of wider social developments and would bring them into line with practice in most occupational pension schemes in the private sector. However, we are conscious of the constitutional obligations of the State. The legislative nature of public service pension schemes requires that they conform to the provisions of the Constitution. It would be important, therefore, that any change in this area should not cause difficulties in relation to the special protection of the institution of marriage under Article 41 of the Constitution.

20.4.9 Taking these considerations into account, we recommend that the existing provisions of public service spouses' and children's schemes should be modified to allow payment of a survivor's pension to a financially dependent partner in circumstances where there is no legal spouse and where a valid nomination has been made. We would suggest that the system of nomination to be introduced on foot of this recommendation should provide for regular review, preferably as part of the annual issue of the statement of pension entitlements (see Paragraph 25.5.6). We would envisage that the nomination form would seek details on the nature and extent of the financial dependency and that it would state that documentary evidence of financial dependency would be required should the member predecease his or her partner. We consider that the form should also state that a nomination, assuming there was no legal spouse, would not be binding on the scheme administrators, and that a pension would not be paid where there was no valid nomination in place.[253]

Two members of the Commission expressed reservation in relation to the above recommendation – see Paragraph 1 of "Reservation by Joe McGovern and John Cullen".

20.4.10 The approach which we recommend would ensure that:

- the constitutional imperative not to penalise marriage would be respected by continuing to favour the family based on marriage over any other type of arrangement;
- there would be absolute certainty that survivor's entitlements would be payable to the legal spouse where the member was legally married; and
- pension scheme administrators would have discretion to pay a survivor's pension to a partner in circumstances where the member was not married.

[252] The new pension scheme (which provides for a higher contribution rate) to be introduced for civil servants in the UK (see footnote to Paragraph 9.2.1) will provide for payment of dependants' benefits to the spouse or to a financially interdependent partner.

[253] It would follow from this recommendation that where spouses' and children's contributions are owing at retirement or on death-in-service, an arrangement similar to that applicable to married public servants should apply for the collection of any outstanding amounts (i.e. deduction from lump sum or death gratuity – see Paragraphs 20.5.18-20.5.22).

20.4.11 This approach would prohibit payment of survivor's pension to a non-marital cohabiting partner in circumstances where the public servant was married at time of death, but separated. In such a case, the survivor's pension would continue to be payable to the legal spouse. We are of the view that should there be constitutional change in this area, the matter should be considered again by employers and unions.

20.5 Other spouses' and children's scheme issues

Compulsory membership for single people

20.5.1 The compulsory and non-refundable nature of contributions under the revised spouses' and children's schemes has caused a number of single people to make submissions about having to pay towards schemes from which it will not be possible to derive a benefit. This was not perceived as a problem under the original schemes as the terms of those schemes allow public servants who are single at retirement to receive a complete refund of contributions.

20.5.2 The Commission accepts the view that public service spouses' and children's schemes are structured on a group insurance basis and that the member contribution rates take account of the fact that payment of benefits will not arise in respect of all members. We also note that implementation of our recommendation in Paragraph 20.4.9 would ensure that there would be a wider range of scheme beneficiaries than heretofore. For these reasons, we do not recommend any change in the rules providing for automatic membership of spouses' and children's schemes, nor in the refund arrangements for membership contributions.

Amount of spouse's pension

20.5.3 Revenue rules permit the payment of a maximum spouse's pension of two-thirds of the member's maximum approvable entitlement. In a private sector 60ths scheme (before commutation), this would give a maximum entitlement of four-ninths of pensionable salary. In reality, however, most private sector schemes pay a maximum spouse's pension of one-third of pensionable salary. This compares with a maximum spouse's pension of one-quarter of pensionable salary in the public service.

20.5.4 Pension increases (in line with earnings) are more favourable in the public service compared with the private sector (often in line with the Consumer Price Index, subject to an annual limit, where payable). This makes a significant difference over the medium- to long-term, and makes up in most cases for the starting pension differential (see Paragraphs 11.4.6-11.4.7).

20.5.5 It is primarily for this reason that the Commission is satisfied that the level of pension payable under the spouses' and children's schemes is reasonable. We would suggest that individual public servants who wish to enhance the level of survivors' benefits would have the option of using SPEARS (see Chapter 19) to do so.

Cessation of spouse's pension on remarriage or cohabitation

20.5.6 Under existing arrangements, anyone in receipt of a public service spouse's pension who remarries or cohabits with someone as husband and wife will generally lose his or her pension entitlement. While this is a legal requirement under the spouses' and children's schemes, and is subject to an annual certification by the pensioner, it is not actively monitored and depends on pension recipients volunteering the relevant information. Many private sector schemes do not provide for cessation of pension in such circumstances.

20.5.7 On the other hand, payment of Social Insurance Widow's or Widower's Contributory Pension ceases on the remarriage or cohabitation of the recipient. Of course, as more people come into the Social Insurance system over time, greater numbers will be relying on their own, rather than their spouse's PRSI contributions in order to qualify for Social Insurance pension (e.g. Retirement Pension or Old Age (Contributory) Pension), to which no remarriage/cohabitation cut-off provision applies.

20.5.8 The Commission considers that the cessation of pension on remarriage or cohabitation is in keeping with the traditional view of dependants' benefits in which the surviving spouse was always assumed to be female. On remarriage or cohabitation, it was assumed that the new partner would provide for the spouse and her family (if any) and, accordingly, that payment of a spouse's pension would no longer be necessary. However, in Section 20.2 we consider how extension of dependants' benefits to include female public servants, societal change, etc. has meant that this conception of dependants' benefits is no longer valid. The modern view of dependants' benefits is that they are a form of insurance cover to provide for financial interdependency. We believe that continuation of the remarriage/cohabitation condition would be inconsistent with this modern view.

20.5.9 Accordingly, the Commission recommends the removal of the provision which requires a spouse's pension to cease on grounds of remarriage or cohabitation.

Three members of the Commission expressed reservation in relation to the above recommendation – see Paragraph 2 of "Reservation by Joe McGovern and John Cullen." Anne Vaughan supported this reservation.

Additional spouse's pension payable under the Garda Síochána Pensions Orders

20.5.10 Article 15(5) of the Garda Síochána Pensions Order, 1981 provides for the payment of a spouse's pension in addition to the spouses' and children's scheme pension in certain limited circumstances. This feature, which is unique to the Garda pension schemes, occurs where the surviving spouse would have had an entitlement to Social Insurance Widow's/Widower's Contributory Pension by virtue of the ex-member's insurance record or by virtue of his or her own insurance record. Only one entitlement is recognised for the purposes of the Social Insurance pension. However, an Article 15(5) pension, equal to the amount of the Social Insurance pension, may also be awarded by the Department of Justice, Equality and Law Reform.

20.5.11 Thus, under the Garda pension schemes, three pensions may be payable to the spouse of a deceased member: a Social Insurance Widow's/Widower's pension, a spouse's and children's scheme pension, and an Article 15(5) pension. As at May 1999, around one thousand Article 15(5) pensions were in payment, at an annual cost of £4.1 million.

20.5.12 The introduction of the Article 15(5) pension resulted from the fact that the Garda Síochána already had a widows' and children's pension entitlement (known as an *ordinary widows' and children's pension)* before the introduction of the widows' and orphans' contributory scheme (in 1972). At that time, members were not eligible to be insured under the Social Welfare Acts and so, unlike civil servants, were not covered for the purposes of the Social Insurance Widow's pension. However, the ordinary widow's and children's pension payable under the Garda pension scheme meant that, effectively, their overall position as regards spouse's benefits was broadly equivalent to that of civil servants.

20.5.13 It was clear, however, that members of the Force would be admitted to the Social Welfare system at some stage and, consequently, it was agreed that when this occurred, the entitlement to the ordinary widows' and children's pensions under the Garda pension scheme should cease. The relevant agreement with the Garda Associations stated:

> *... at any later time, his widow or children, if they qualify for Social Welfare contributory pensions in respect of such insurance, will not be eligible in addition for ordinary benefits under the Garda Pension Orders.*[254]

20.5.14 The reference in the agreement to "*such insurance*" related to the PRSI contribution record of the member. Thus, it was decided when the agreement was being implemented that if a Social Insurance pension were payable to the spouse of a former member by virtue of his or her own (i.e. the spouse's), rather than the deceased member's, insurance record, the pension payable under the Garda pension scheme, now known as an Article 15(5) pension, should not be affected.

20.5.15 In effect, the Article 15(5) pension has replaced the ordinary widow's pension under the Garda pension scheme, but it applies only where there are two separate insurance records (those of the deceased member and of his or her spouse) which would each be sufficient to convey an entitlement to a Social Insurance Widow's/Widower's Contributory Pension. Where there is only one insurance record, i.e. that of the deceased member, no Article 15(5) pension is payable.

20.5.16 As we have shown, the historical circumstances of the introduction of the Article 15(5) pension under the Garda pension scheme were quite complex. However, the Commission considers that in present circumstances the basic qualifying criterion for these pensions, which is related to dual qualification for survivors' pensions under the Social Insurance system, can apply equally to all other public service groups. In these circumstances, we do not see any justification for continuation of this special arrangement in respect of the Garda Síochána.

20.5.17 Accordingly, the Commission recommends that the Article 15(5) pension payable in certain circumstances under the Garda Síochána Pensions Order, 1981 to spouses of deceased members of the Force should be discontinued in the case of new entrants to the Force.

Payment of contributions for pre-membership service

20.5.18 The payment of spouses' and children's scheme contributions at retirement or in case of death-in-service to cover pre-membership service has been raised in a number of submissions. The purpose of this deduction, which amounts to 1% of pensionable remuneration for each year owing, is to ensure that benefits under the scheme are calculated by reference to all of the member's service; for example, if a member has 40 years' service at retirement, but has only paid periodic contributions for a period of 30 years, then the balance of ten years' contributions must be paid for the purpose of the scheme. The contribution is made by deduction from lump sum, or death gratuity in case of death-in-service, and is significantly reduced by the application of tax relief at the marginal rate. The Commission believes that it is essential that members should pay fully for spouses' and children's scheme benefits and therefore recommends no change in existing arrangements. We note that in due course the question of contributions for pre-membership service will no longer arise.

[254] Report of Working Party on Widows' and Children's Pensions for members of the Garda Síochána, 29 January 1971.

Payment of contributions in respect of added years of notional service

20.5.19 In circumstances where an employee dies in service, potential service to normal retirement age (up to a maximum of 40 years) is credited for the purposes of calculating spouses' and children's benefits. For example, if a civil servant with 20 years' service dies at age 45, his or her spouse will receive a pension which is based on actual service plus an additional 20 years' notional service to age 65. As with pre-membership service (see above), a contribution of 1% of pensionable remuneration must be paid in respect of these notional added years of service. The total amount due (20% of pensionable remuneration in the example given) is deducted from the amount of death gratuity payable.

20.5.20 Similar provisions apply in the case of public servants who retire on grounds of ill health. Because spouse's pension in such cases is calculable on the basis of what the public servant's total service would have been had he or she remained working until age 65, a deduction to cover the contributions due on the notional years which would be granted under this calculation is made at the time the member actually retires. Again, the contribution is charged at a rate of 1% of pensionable remuneration for each year of potential service, and is deducted from retirement lump sum. No such deduction is made where the individual is single at retirement, although this would change in the future if our recommendation at Paragraph 20.4.9 were implemented (see footnote to that Paragraph).

20.5.21 In the private sector, where a single scheme covering main and spouses' and children's benefits is the norm, lump sum deductions of this nature are not generally applicable.

20.5.22 The Commission considers that spouses' and children's benefits in case of death-in-service and death following ill health retirement are relatively advantageous elements in public service pension arrangements, and that public servants should contribute towards the cost involved. Accordingly, we do not recommend any change in these provisions.

Payment of children's pensions where both parents are members of the same pension scheme

20.5.23 At present, where both parents are members of the spouses' and children's scheme in the same public service employment, only one pension is payable where a dependent child is orphaned. The Commission believes that it is difficult to justify this approach since both parents contribute towards the spouses' and children's scheme, and that if they worked in different public service organisations, two children's pensions would be payable.

20.5.24 Accordingly, the Commission recommends that where a dependent child is orphaned and both parents are members of the same spouses' and children's scheme, two children's pensions should be payable. We note that the cost of this change would be minimal.

20.6 Death gratuity

20.6.1 In public service schemes, the gratuity payable on death-in-service is the greater of an employee's pensionable remuneration on the last day of reckonable service, or the gratuity he or she would have received had he or she retired on ill health grounds, subject to a maximum of $1\frac{1}{2}$ times pensionable remuneration.[255]

[255] A minimum death gratuity of £12,000 was introduced for non-officers in the Local Government Superannuation Scheme in 1996. It is indexed in line with pay increases and is paid on a pro rata basis in the case of part-timers.

20.6.2 The typical level of death gratuity in private sector schemes in which a spouse's pension is normally payable is between two and four times earnings (see Paragraph 8.13.2). The maximum payment permitted under Revenue rules is four times earnings. The death-in-service gratuity in the UK civil service pension scheme is two times pensionable pay and is paid irrespective of a person's length of service.

20.6.3 An analysis of a sample of civil service death gratuity payments for the period 1995-97 indicated that the average size of a gratuity as a proportion of income was between 1 and 1.2 times pensionable remuneration. A sizeable deduction was generally made in respect of contributions owing under the spouses' and children's scheme (see above), bringing the actual gratuity payment in many cases below an amount of one times pensionable remuneration.

20.6.4 It can be argued that the nature of the spouses' and children's pension arrangements in the public service, particularly the superior pension increase mechanism, makes the overall death-in-service package more attractive in the long-term when compared with that available in the private sector (see the detailed comparison in Paragraph 8.13.9).

20.6.5 The Commission obtained actuarial costings on the impact of changing the death-in-service gratuity in the public service to two or four times pensionable remuneration. The benefit would no longer be linked to service, nor would there be any deductions from the gratuity in respect of the spouses' and children's scheme. It was estimated that the increase in costs in 1997 for the public service would have been £6 million if the death gratuity had been increased to two times pensionable earnings for existing staff, and £18 million if increased to four times pensionable earnings.[256]

20.6.6 While the Commission accepts that private sector death gratuity arrangements are better than those in the public service, we believe that this is more than balanced out in other areas, such as pension increases. In addition, the availability of cheap, tax effective AVC and life insurance arrangements — widely availed of by public servants — lessens the need to make changes in this area.

20.6.7 However, the Commission does recognise the demand for additional death cover and has proposed that a public service wide scheme should be incorporated within SPEARS (see Paragraph 19.4.9) to enable employees to take out additional cover of two-and-a-half times pensionable remuneration.

20.7 Nomination of beneficiary for receipt of death gratuity

20.7.1 Under most public service pension schemes, the death-in-service gratuity is payable to the legal personal representative and is distributed according to the rules of probate/administration. An alternative approach would be to put in place a nomination format, i.e. a system which would enable a member to nominate the recipient of the death gratuity paid in case of death during service. This approach is used in the private sector and is the basis on which the UK Civil Service Pension Scheme operates. Its primary advantage is that it allows the member to exercise some discretion over a portion of the death-in-service benefits by removing it from the legal estate (which under the Succession Acts must be disposed of in certain guaranteed percentages).

[256] Commission on Public Service Pensions, "Actuarial Review of Impact of Changes to Pension Scheme Terms" (December 1997), Report prepared by IPT Actuarial Services Ltd.

20.7.2 The Commission recommends that an appropriate system for nomination of death gratuity should be introduced into public service pension schemes.[257] It should provide for annual review of the nomination as part of the annual issue of the statement of pension entitlements. Preferably, and subject to legal advice, this change should be introduced by means of primary legislation in order to ensure that due regard is had to the property rights of the spouses of public servants.

20.7.3 This recommendation is in line with the Commission's determination to introduce a greater degree of flexibility into public service pension schemes.

20.8 Conclusions and summary of recommendations

20.8.1 The Commission considers that spouses' and children's pension schemes are a key component in public service pension arrangements. They provide an important social and financial benefit to the families of deceased members. The benefits of the schemes, taken in conjunction with the gratuity payable on death-in-service, are reasonable when compared with dependants' benefits in public service schemes in other countries and with schemes in the private sector.

20.8.2 In summary, the Commission's recommendations in relation to spouses' and children's pension schemes and death gratuities are as follows:

(i) consideration to be given to including public service spouses' and children's schemes in a single public service pension scheme and/or rationalising the large number of schemes currently in existence (Paragraph 20.2.8);

(ii) provision of a limited appeal mechanism to enable the exercise of options not to join spouses' and children's schemes to be examined in individual cases, having regard to certain stated criteria (Paragraph 20.3.26);

(iii) option to join spouses' and children's schemes in the case of national and secondary teachers to proceed on the basis of the management offer made at the Teachers' Conciliation Council (Paragraph 20.3.28);

(iv) amendment of spouses' and children's schemes to allow payment of a survivor's pension to a financially dependent partner in circumstances where there is no legal spouse (Paragraph 20.4.9);

(v) removal of the provision which requires a spouse's pension to cease on remarriage or cohabitation grounds (Paragraph 20.5.9);

(vi) the discontinuance in the case of new entrants to the Garda Síochána of the spouse's pension payable under Article 15(5) of the Garda Síochána Pensions Order, 1981 (Paragraph 20.5.17);

(vii) where a dependent child is orphaned and both parents are members of the same spouses' and children's scheme, two children's pensions to be payable (Paragraph 20.5.24);

(viii) the provision of an appropriate system for nomination of beneficiary for receipt of death gratuity (Paragraph 20.7.2).

[257] We would envisage that the nomination of beneficiary for receipt of death gratuity would operate alongside that for nomination of partner for receipt of dependant's pension where there is no legal spouse (see Paragraph 20.4.9).

CHAPTER 21

Defence Forces Pension Schemes

21.1 Introduction

21.1.1 In Chapter 15, the Commission considered retirement age and early retirement. Amongst other things, we examined and made recommendations on the pension terms of public service groups which have special retirement ages and enhanced pension arrangements due to particular operational requirements. The Defence Forces also come into the category of groups with special terms. However, due to the unique nature of the Defence Forces Pension Schemes, which bear little relationship to other public service pension schemes, we decided that it was appropriate to deal separately with the pension terms of the Defence Forces.

21.1.2 Uniquely amongst the public service groups covered by the Commission's terms of reference, there was already a review of pension terms underway (being conducted by the Department of Defence) during the period of our deliberations. An important starting point in the review has been the 1990 *Report of the Commission on Remuneration and Conditions of Service in the Defence Forces* (the *Gleeson Commission*), which made specific findings on superannuation and related matters. Another major factor in the review is the ongoing development of a new personnel policy as part of the restructuring of the Defence Forces. The high age profile of military personnel at all levels was a key issue to be addressed in the process of reorganisation and reform which has been underway since the mid-1990s. Obviously, the development of a personnel policy capable of delivering a lower age profile has direct implications for pension terms and retirement age in the Defence Forces.

21.1.3 In light of the above, the Commission concluded that our best approach would be to make a series of general recommendations which would be taken into account by the Department of Defence in completing its review of the Defence Forces Pension Schemes. To set a context for these recommendations, we briefly review below the main pension terms of officers and enlisted personnel, consider the cost of pensions for the Defence Forces, detail the analysis made by the *Gleeson Commission*, and outline recent developments in relation to personnel policy.

21.1.4 Some issues which have arisen in relation to occupational pension arrangements in the Defence Forces are common to other public service schemes — for example, spouses' and children's benefits and integration with State Social Insurance benefits. Our comments and recommendations on these are contained elsewhere under the appropriate headings of the Report.

21.2 Existing Defence Force pension terms

21.2.1 In the context of public service pensions generally, the Defence Forces Pension Schemes are unique in many respects. The emphasis is on immediate benefits payable on retirement, whether voluntary or otherwise, and unlike other areas of the public service, there is no provision for the preservation of benefits. Immediate pensions together with gratuities, are payable regardless of age to officers after 12 years' service and to enlisted personnel after 21 years' service; gratuities only are payable after five and three years' service, respectively. There are maximum retirement ages, but retirement at any earlier age is generally available at the discretion of the individual. (In the case of officers, the approval of the Minister for Defence is required.) Unlike other public service schemes, many of the benefits are not directly pay-related; pensions, for example, are not based on final remuneration, but are flat rates based on rank and service. The essential features of the schemes date from the 1930s.

21.2.2 In the case of officers, maximum retirement age varies according to rank and ranges from age 54 for a Captain to age 63 for a Lieutenant General. Maximum pension can be obtained long before maximum retirement age. For example, a Commandant can qualify for maximum pension in his or her early 40s (maximum retirement age is 56). Maximum retirement lump sum of $1\frac{1}{2}$ times pay, plus appropriate addition in respect of Military Service Allowance (MSA), is payable only on retirement within two years of the maximum retirement age. Minimum pension after 12 years' service is about 20% of maximum pay (plus addition for MSA).

21.2.3 Officers who hold specialised qualifications (e.g. doctors, engineers) are paid extra remuneration and can serve up to age 65. They qualify for a percentage addition to the standard rates of pension. Pension in case of ill health retirement is quite different to standard public service terms; for example, where retirement takes place after one but less than ten years' service, an enhanced gratuity — but no pension — is payable. As with other parts of the public service, officers commissioned on or after 6 April 1995 are in full PRSI class, and their benefits and contributions are integrated with the State Social Insurance system.

21.2.4 For enlisted personnel, the current maximum retirement age is 60 years for all ranks. Enlisted personnel are in Class H PRSI and so are fully insured for all Social Insurance benefits, except Occupational Injuries Benefits. As noted above, both pension and lump sum are payable after 21 years' service. Pension consists of a basic flat rate amount, which varies according to rank, plus appropriate addition in respect of MSA. An additional increment is paid for each year of service in excess of 21, up to a maximum of 31 years. Minimum pension is about 36%-39% of maximum pay (plus addition for MSA) depending on rank; maximum pension is about 47%-53% of maximum pay. A special form of integration with the Social Insurance system applies: on qualification for Retirement Pension or Old Age (Contributory) Pension at age 65 or age 66, the additional increment to pension for service in excess of 21 years is withdrawn. Certain forms of extra remuneration are reckonable for pension purposes; an addition of 3% of the standard rate of pension is made in respect of each additional payment. A special pension and gratuity are payable on discharge for medical reasons, where service is between 12 and 21 years.

21.2.5 Members of the Army Nursing Service and the Chaplaincy Service are entitled to gratuity only where service is greater than five and less than 20 years. There is an entitlement to immediate pension, but no gratuity, after 20 years' service (ten years if retirement is on medical grounds). Pension is calculated at a rate of 1/60th of reckonable pay per year of service, an additional 1/60th being granted for each year in excess of 20 years. Thus, maximum pension of 2/3rds of reckonable pay is payable after 30 years' service. There is no minimum retirement age to qualify for pension or gratuity and maximum retirement age for both services is age 65.

21.2.6 We give a more detailed description of the pension terms of commissioned officers, enlisted personnel, and members of the Army Nursing Service and Chaplaincy Service in Section 3.7 above.

21.3 Cost of Defence Forces Pension Schemes

21.3.1 The clearest way of illustrating the cost of the Defence Forces Pension Schemes is to consider the relevant new entrant rates. As discussed in Chapter 6, these rates can be considered as the typical cost to the State of existing pension terms based on certain financial and demographic assumptions. They are expressed as the percentage of annual basic salaries, plus pensionable allowances where applicable, that would be required to finance the existing pension terms over the period of employment of typical new entrants.

21.3.2 The new entrant rates for the Defence Forces, taken from Table 6.8, are set out below (see Section 6.2 for methodology and assumptions used in the actuarial review of public service pension schemes).

Table 21.1: New entrant rates for Defence Forces personnel

Rank	Starting age	New entrant rate
Commissioned officers	20	30%
Enlisted personnel	18	20%

In the case of officers, the rates are for new entrants in full PRSI class, to whom integration applies. For officers commissioned prior to 6 April 1995 who are in modified PRSI class, the new entrant rates are higher than those indicated.

21.3.3 As shown in Table 6.8, the new entrant rates quoted for the Defence Forces indicate that their pension terms are amongst the most costly in the public service. The new entrant rate of 30% for officers is by far the highest, and compares with a rate of 25% for the Garda Síochána (the group with the next most costly pension terms), 16% for the civil service, and 17% for primary teachers.

21.3.4 The most costly element in the Defence Forces scheme is the entitlement to early pension benefits: after 21 years' service for enlisted personnel, and after 12 years' service for commissioned officers. Payment of pensions may commence from as early as age 39 for the former, and from age 32 for the latter. Retirement is largely at the discretion of the individual, subject to the maximum retirement age; accordingly, it is open to the individual to choose when to retire so as to maximise personal benefits.

21.3.5 The tables in Appendix 21.1 set out retirement statistics for the Defence Forces over the period 1989-95.[258] The tables show that a high proportion of enlisted personnel (averaging around 60% over the period 1992-95) who leave the Defence Forces after three years' service qualify for pension as well as gratuity. Equally, a high proportion of officers who leave having a minimum of five years' service are eligible for pension and gratuity at retirement, whether voluntary or on age grounds. Obviously, the greater the number of personnel leaving the Defence Forces who qualify for pension, and the earlier the age at which pension comes into payment, the greater is the cost to the pension scheme.

21.3.6 As part of our actuarial review of pension schemes, the Commission examined the impact on new entrant contribution rates for the Defence Forces if the existing pension terms were

[258] More recent data include the effect of the Defence Forces voluntary early retirement scheme (1996-98), and so have not been included in the Table.

replaced with a public service-type scheme where special terms applied.[259] For the purposes of this exercise it was assumed that existing terms of the Garda Síochána scheme would apply.[260]

21.3.7 There were a number of difficulties associated with this calculation, for example, how to estimate the impact on retirement behaviour of the new scheme and the adjustment of the promotional salary scale assumed for the purpose of the costing.

21.3.8 The results of the exercise indicated that if the promotional salary scale for commissioned officers were in line with that of the Garda Síochána, but making allowance for withdrawals prior to age 50, then the new entrant rate might be in the range 20%-25% of salary.

21.3.9 Allowing for a lower promotional salary scale and a heavier withdrawal assumption, the new entrant rate for enlisted personnel might be in the range 15%-20% of salary.

21.3.10 These are only very broad indications of the cost impact of amending the Defence Forces scheme, but they give some idea of the exceptional cost of existing pension terms.

21.4 Views of the *Gleeson Commission*, 1990[261]

21.4.1 The approach of the *Gleeson Commission*, which examined claims for improvements in pension terms as part of its review of the remuneration and conditions of service of the Defence Forces, was to consider the type of pension arrangements which should ideally apply, taking account of the particular circumstances of the Defence Forces and the practice in other areas of the public service. The *Gleeson Commission* concluded that while there was merit in some of the claims made, there were also aspects of the pension schemes which were very advantageous to Defence Forces personnel and which were relatively costly and, in some cases, difficult to justify in the light of manpower policy requirements and the arrangements elsewhere in the public service. The *Gleeson Commission* suggested that, viewed in isolation, some elements of the schemes appeared less favourable than corresponding provisions in other public service schemes, but that the overall value of benefits provided was considerably in excess of that available under other schemes.

21.4.2 The *Gleeson Commission* made a specific recommendation that the pension schemes should be amended so as to provide for the reckoning of MSA in calculating benefits. It considered that any further changes in the superannuation arrangements should be introduced only in the context of a fundamental revision of the pension schemes.

21.4.3 The *Gleeson Commission* expressed specific views on a number of other points, including the following:

(i) the early availability of immediate pensions was very costly and could encourage personnel, including those with third level qualifications to cut short their military careers to pursue careers in civilian employment. This could prove more lucrative

[259] Commission on Public Service Pensions, "Further Actuarial Review of Impact of Changes to Pension Scheme Terms" (October 1999), Report by Mercer Ltd.

[260] Retirement at age 57 or in the age range 50-57 on completion of 30 years' service; doubling of pensionable service for service in excess of 20 years, subject to a maximum of 40 years' pensionable service; preservation of benefits (to age 60) on leaving service earlier than retirement age.

[261] Government of Ireland, *Report of the Commission on Remuneration and Conditions of Service in the Defence Forces* (July 1990), Chapter 10.

because of the availability under the Defence Forces schemes of an immediate pension and gratuity;

(ii) even allowing for the particular manpower policy requirements of the Defence Forces, a strong case existed for the abolition of the payment of immediate pensions for enlisted personnel under the age of 50 and for officers under the age of 55;

(iii) the absence of any deferred pension benefit for enlisted personnel with less than 21 years' service was out of line with practice in other public service pension schemes. The introduction of preserved benefits for persons with at least five years' service would ensure that individuals who did not qualify for immediate pension on departure would qualify for preserved benefits payable at age 60;

(iv) consideration should be given to the replacement of the largely flat-rate benefits with a system more closely related to pay and service at departure;

(v) the present gratuity arrangements on leaving service were not sufficiently selective and in some respects contradicted manpower policy objectives.

21.4.4 The *Gleeson Commission* argued that the manpower policy requirements of the Defence Forces differed from those of other public service bodies and that these differences should be reflected in the pension arrangements. However, a convincing case in support of the present superannuation arrangements could not be made on a manpower policy basis. On the other hand, the present arrangements meant that some individuals were entitled to very valuable benefits in the form of immediate pensions at a very early stage while others who might have given a reasonable amount of service did not acquire any pension entitlements. The *Gleeson Commission* concluded that fundamental change was necessary to ensure that the Defence Forces Pension Schemes met manpower policy requirements in a cost effective way, as well as being fair to the different groups of personnel.

21.5 Personnel policy

21.5.1 A consultants' review conducted for the Efficiency Audit Group (EAG) in 1994 showed that at all levels in the Defence Forces, the average age of personnel was too high,[262] and identified the following as the critical manpower problems:

- the age profile was too high at all rank levels;
- maximum retirement ages were too high;
- too many personnel were rated Medical Category C (unavailable for the full range of military duties);
- there was overmanning at officer level;
- *stop/go* recruitment was a detrimental factor.

21.5.2 The age profile problem might be considered to be a product of both the stop/go recruitment approach of the past and the fact that too many personnel remained in service beyond the appropriate age/rank profile. For example, the consultants noted that a custom had grown up over the years, facilitated by the Defence Forces Regulations, of allowing personnel to serve until

[262] According to the consultants, the age of private soldiers should ideally lie between 19 and 25 years. At the time of the review, only 10% of private soldiers fell within this age range. Senior non-commissioned officers, depending on rank should be between 33 and 50 years of age; however, only about one-quarter fell within the ideal range for their rank. Similar problems were found among commissioned officers; for example, only 48 out of 650 senior officers fell into the ideal range for their rank.

they reached the age of 60, and contrasted this with the need for lower retirement ages and a higher turnover of personnel.

21.5.3 The *Defence Forces Review Implementation Plan* (1996) provided for a phased plan to address the issues identified by the EAG as part of a longer term reform. An essential part of this process was the implementation of a voluntary early retirement (VER) scheme over the period 1996-98 (1,500 personnel availed of the scheme at a cost of £65 million in retirement benefits). The primary purpose of the scheme was to achieve the required reduction in numbers to meet the new manpower levels and create the scope for recruitment. The recruitment, which occurred simultaneously with the operation of the VER scheme, was considered necessary if the high age profile were to be seriously addressed.

21.5.4 For the longer term, the Implementation Plan also proposed new personnel models for officers and enlisted personnel, aimed at ensuring a continuous turnover of personnel, and the provision of adequate advancement opportunities for career personnel.

21.5.5 For officers, the new policy had the objectives of higher turnover at junior rank level and a lowering of retirement ages by one year, coupled with the capping of service in the more senior ranks. The introduction of short service commissions and graduate entry was also proposed.

21.5.6 According to the Implementation Plan, the proposed personnel model for enlisted personnel is underpinned by the following essential elements:

(i) a major reduction in age profile for all ranks, and particularly private soldiers;

(ii) improved career prospects for personnel deemed suitable for promotion;

(iii) an emphasis on skill development and improved employability for all personnel to enhance their job prospects on leaving the Defence Forces.

21.5.7 The Implementation Plan has resulted in a policy of regular recruitment being put in place – considered a vital part of reducing the age profile. Applicants for enlistment should be aged not less than 17 and not more than 24 (26 for the Naval Service) and are recruited for an initial period of five years, which may be extended to nine and 12 years subject in each case to strict medical, physical and other criteria. It is envisaged that privates who have not been promoted to NCO rank will be compulsorily discharged on completion of 12 years' service and only NCOs will be eligible to continue to serve beyond that (to complete 21 years' service). It is also envisaged that all Junior NCOs (Corporals and Sergeants), will be compulsorily discharged on completion of 21 years' service and only senior NCOs (CQMS and higher) will be eligible to remain in service beyond 21 years (up to 55 years of age at most).

21.6 Conclusions and recommendations

21.6.1 Defence Forces pension arrangements date from the 1930s. We consider that a fundamental revision of these arrangements is necessary for the following reasons:

- it is difficult to justify the substantial variation in treatment which exists under the Defence Forces schemes compared with all other public service pension schemes and having regard to standard provisions of occupational pension schemes generally (e.g. preservation of benefits, pay-related pension calculation);

- while existing pension schemes for the Defence Forces are costly compared with other public service pension schemes, the experience has been that they have not been successful in maintaining a balanced age structure;
- it is necessary to ensure that pension terms complement the new personnel policy for the Defence Forces.

21.6.2 Certain aspects of the Defence Forces Pension Schemes are in conflict with the Commission's overall approach to public service pensions as set out in this Report. The fact that many personnel qualify for an immediate gratuity but not a preserved pension is contrary not just to our views but to national pensions policy as indicated in the Pensions Act, 1990 and in the Pensions Board report on the National Pensions Policy Initiative, *Securing Retirement Income*. The basic objective of a pensions system should be to provide a form of saving for retirement. A payment for early departure which is designed to *buy out* any call on future pension is inconsistent with that objective.

21.6.3 A further concern to the Commission is the immediate payment of pension to those who leave the Forces at a relatively early age and who are fully capable of taking up further employment. While we appreciate that the aim of this policy may originally have been the encouragement of staff turnover at lower ages, this was done in a context where there was a more limited Social Insurance system and a completely different attitude to employment mobility generally. The fact that these pension provisions are not targeted means that in some cases highly qualified personnel are in effect being subsidised to take up employment elsewhere. These factors again point to the need to replace the present system of immediate benefits with one involving preserved benefits. Special provisions could be introduced to deal with particular cases, consistent with specific personnel and operational requirements.

21.6.4 As discussed in Chapter 14, the Commission favours a pension system that allows for the building up of pension entitlements based on service and remuneration at retirement age. The Defence Forces schemes, on the other hand, involve flat rate pensions based on rank and service, and there are non-standard arrangements to cater for allowances and integration with the Social Insurance system.

21.6.5 Elsewhere in the public service, personnel policy involves seeking to retain staff in employment and the various pension schemes contribute to achieving this objective. The Defence Forces, on the other hand, require a policy of regular turnover of personnel, coupled with the retention of career personnel. It would be important that pension scheme design be capable of supporting this personnel policy.

21.6.6 Having regard to the above considerations, the Commission makes the following recommendations in relation to the design of a new pension scheme for new entrants to the Defence Forces:

(i) consistent with our recommendation for the public service schemes generally, the pension scheme should have a defined benefit final salary structure, integrated with the Social Insurance system. Pension and lump sum should be based on pensionable remuneration (integrated as appropriate) and service at retirement;

(ii) maximum retirement ages would be as laid down under the personnel policy and maximum pension would accrue over a period of 30 years. However, the Commission recommends that pension should not be payable earlier than age 50. Preservation of pension benefits should apply in the case of personnel who, having two or more years' service,[263] leave service earlier than age 50;

(iii) on retirement/discharge earlier than age 50 there should be an appropriate severance arrangement in certain circumstances. This should only be made available on a limited and selective basis in the light of specific personnel and operational requirements;

(iv) allowances in the nature of pay should be included in the definition of pensionable remuneration, consistent with policy in other public service pension schemes;

(v) the same general pension provisions should apply to officers and enlisted personnel;

(vi) in line with our recommendations on pension contributions generally (see Section 22.2), the pension contribution should be 3% of remuneration, plus $3\frac{1}{2}$% of net remuneration (this already applies to officers commissioned after 6 April 1995);

(vii) as a separate matter, we consider that the existing provisions in relation to occupational injuries under the Army Pensions Acts should be examined, having regard, particularly, to the many substantial changes which have taken place since their introduction;

(viii) new entrants to the Army Nursing Service and the Chaplaincy Service should have standard public service pension terms and retirement ages.

21.6.7 The Commission recommends that the new pension schemes for new entrants should be drawn up as soon as possible, with appropriate consultation involving the Defence Forces' representative bodies. Furthermore, the Commission recommends that, having regard to the advantageous nature of the existing Defence Forces Pension Schemes considered in the round, no fundamental modifications to the pension terms of serving personnel should be made.

[263] Assuming implementation of our recommendation at Paragraph 18.6.13 to reduce the period required to qualify for preserved benefits from five to two years.

APPENDIX 21.1

Table 1: Defence Force retirements: enlisted personnel (1989-95)

Category of Retirement	1989			1990			1991			1992			1993			1994			1995		
	SNCO	NCO	Pte	SNCO	NCO	Pte	SNCO	NCO	Pte	SNCO	NCO	Pte	SNCO	NCO	Pte	SNCO	NCO	Pte	SNCO	NCO	Pte
3-20 yrs – Gratuity only	9 20%	116 63%	252 90%	5 25%	63 54%	184 90%	0 0%	27 30%	105 73%	0 0%	21 25%	66 63%	0 0%	11 12%	66 53%	0 0%	25 24%	63 54%	2 9%	18 18%	45 42%
21 yrs plus – Pension & Gratuity	35 80%	59 32%	23 8%	15 75%	43 37%	13 6%	25 100%	61 66%	29 20%	19 100%	59 70%	27 26%	26 100%	75 82%	50 40%	25 100%	78 74%	45 38%	21 91%	72 74%	44 41%
12-20 yrs – Ill health	0 0%	8 5%	5 2%	0 0%	11 9%	8 4%	0 0%	4 4%	10 7%	0 0%	4 5%	11 11%	0 0%	5 6%	9 7%	0 0%	2 2%	9 8%	0 0%	8 8%	19 17%
Total	44 100%	183 100%	280 100%	20 100%	117 100%	205 100%	25 100%	92 100%	144 100%	19 100%	84 100%	104 100%	26 100%	91 100%	125 100%	25 100%	105 100%	117 100%	23 100%	98 100%	108 100%

Note: SNCO = Senior Non-Commissioned Officer; NCO = Non-Commissioned Officer; Pte = Private.

Table 2: Enlisted personnel: breakdown between those receiving pension & gratuity and gratuity only

	1989	1990	1991	1992	1993	1994	1995
Pension & Gratuity	130	90	129	120	165	159	164
	26%	26%	49%	58%	68%	64%	72%
Gratuity Only	377	252	132	87	77	88	65
	74%	74%	51%	42%	32%	36%	28%
Total Retirements	507	342	261	207	242	247	229
	100%	100%	100%	100%	100%	100%	100%

Note: Enlisted personnel receiving pension and gratuity comprises those retiring on age grounds with 21 or more years' service and those retiring on ill health grounds with between 12 and 20 years' service.

Table 3: Commissioned officers: age and voluntary retirements by rank

	1989		1990		1991		1992		1993		1994		1995	
Category of Retirement	**Snr Off**	**Jnr Off**	**Snr Off**	**Jnr Off**	**Snr Off**	**Jnr Off**	**Snr Off**	**Jnr Off**	**Snr Off**	**Jnr Off**	**Snr Off**	**Jnr Off**	**Snr Off**	**Jnr Off**
Age Retirement	19	0	10	0	20	0	24	0	21	0	20	1	8	2
	53%	0%	42%	0%	67%	0%	69%	0%	68%	0%	72%	5%	35%	17%
Voluntary Retirement	17	25	14	15	10	6	11	19	10	11	8	20	15	10
	47%	100%	58%	100%	33%	100%	31%	100%	32%	100%	28%	95%	65%	83%
Total	36	25	24	15	30	6	35	19	31	11	28	21	23	12
	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

CHAPTER 22

Other Issues Relating to Pension Terms

22.1 Introduction

22.1.1 In the preceding Chapters, the Commission has considered the major public service pensions issues which come within our remit. However, as part of our comprehensive examination of public service pension arrangements, it is necessary to examine a range of other issues relating to pension terms, some of which have been raised in the submission process. They include:

- employee contributions;
- notional added years;
- portability of pensions/preservation of service;
- pension terms on ill health early retirement;
- pensionability of allowances: consequences for pensioners;
- differences in pension terms between established and non-established type employees;
- pension scheme coverage for certain professional and other groups;
- other issues.

In this Chapter, we present our views and recommendations in relation to each of these issues.

22.2 Employee contributions

22.2.1 In this Section we examine a number of issues having to do with employee contributions towards the cost of pension benefits. These are:

- whether there should be a single rate of employee contribution for the public service as a whole, or different contribution rates for different sectors, reflecting the actual value of the pension benefits applying to each;
- how pension benefits and employee contributions should be treated in certain forms of pay determination in the future;
- the question of introducing explicit main scheme pension contributions, with consequent uplifting of salary scales, in respect of groups for whom there is currently no such contribution.

Single rate of employee contribution

22.2.2 Since 5 April 1995, new entrants to most areas of the public service pay the same rate of pension contribution, as outlined in Table 22.1.

Table 22.1: Employee contribution rates under typical public service scheme

Scheme	Nominal rate	Contribution calculation
Main pension scheme	5%	$3\frac{1}{2}$% of net remuneration[264] (in respect of pension) *plus* $1\frac{1}{2}$% of remuneration (in respect of lump sum)
Spouses' and children's scheme	$1\frac{1}{2}$%	$1\frac{1}{2}$% of remuneration

Thus, the overall nominal rate of contribution between the two schemes is $6\frac{1}{2}$%, calculated as 3% of remuneration and $3\frac{1}{2}$% of net remuneration.[265]

22.2.3 Given the application of a uniform contribution rate, it is clear that the employee contribution does not reflect the variation in the value of the pension package between different public service groups, as indicated in the calculation of new entrant rates (see Table 6.8).

22.2.4 An alternative approach would involve the application of a separate rate of employee contribution for each group relative to the value of the pension package applying to that group. For example, it might be decided that employees should pay one-third of the estimated cost of the pension benefits. This type of approach has been adopted by some public service schemes in other countries.

22.2.5 Assuming that the calculation of appropriate *group-specific* rates of employee contribution would be possible, a case might be made for a consequential adjustment to the pay rates of the groups affected in much the same way as the uplifting of salaries which occurred when the 5% employee contribution was introduced for new entrants in April 1995. To be consistent across all groups, it would be necessary to reduce pay rates in the case of groups having relatively low pension costs.

22.2.6 An advantage of establishing a direct link between employee contributions and pension costs is that the separate rates would help to make clear to employees in each group the value of their pension benefits. In addition, once there was agreement on the apportionment of pension costs between employers and employees, it would be relatively straightforward to adjust the contribution rates to reflect changes in the cost of pension benefits in the future.

22.2.7 On the other hand, the existence of a wide variety of employee contribution rates would be administratively complex, while the introduction of such a system in the first place would be a difficult and time-consuming task. In addition, the question of adjusting pay rates would arise.

22.2.8 A further complication with group-specific contribution rates is that there would be no limit to the extent to which the *"groups"* might tend to splinter. A case could be made, for example, for contribution rates to apply to each grade, rather than to a sector as a whole. Such a system could become quite complicated. Furthermore, there would be a concern that group-specific rates, howsoever defined, would be destabilising from an industrial relations perspective.

[264] Remuneration less twice the rate of Old Age (Contributory) Pension.

[265] The main exceptions are: non-officers in the local authorities and the health service whose contributions are the same as the above, with the exception that the spouses' and children's scheme contribution is $1\frac{1}{2}$% of net remuneration rather than of remuneration; and non-established civil servants, whose total contribution is $1\frac{1}{2}$% of net remuneration for spouses' and children's benefits (there is no contribution for main scheme benefits). Enlisted personnel in the Defence Forces contribute only towards the spouses' and children's scheme — see Paragraph 3.7.7 for details of contribution level.

22.2.9 In Paragraph 24.6.4, we recommend that where future changes are made to pension terms affecting a particular group or groups, increases in employee contribution rates should be made (subject to agreement between management and unions) in order to finance or part-finance the change. It would not be essential to have group-specific rates in order to introduce this type of arrangement.

22.2.10 While there may be a logic to *group-specific* contribution rates, which are the practice in some public service schemes abroad, the Commission considers that, on balance, it would be preferable to continue the application of a standard rate of employee contribution for new entrants across all public service groups.[266]

22.2.11 Over time, as noted in Paragraph 22.2.9, there could be future variation in rates reflecting changes in pension terms negotiated for particular groups.

Employee contribution and pay determination

22.2.12 For pay determination purposes, in a number of arbitration findings in the past, a deduction has been made when setting the pay of certain civil service grades and, by extension, of other public service grades having a direct pay linkage with those grades to reflect the difference in contribution arrangements and the more favourable pension terms applying in the civil service compared with the private sector. This latter deduction would not appear to have applied uniformly in other arbitration findings, nor was it applied to other public service grades. As discussed in Paragraph 11.9.20, it is not possible to say with certainty that such a deduction continues to exist in what has been — through the effect of national pay agreements and restructuring agreements — a significantly different pay determination environment.

22.2.13 However, it is likely that pay determination in the public service will continue to require the carrying out from time to time of some form of comparison with private sector pay. This is recognised in the benchmarking element of the agreement on public service pay contained in the *Programme for Prosperity and Fairness*.

22.2.14 We recommend that to the extent that any future pay determinations for public service grades are carried out by means of a comparison with equivalent positions in the private sector, any adjustment which might be made to reflect the value of public service relative to private sector pension arrangements should take into account the employee contribution being made by the public servants concerned.

22.2.15 There is an argument that any deduction made in the pay determination process in respect of the value of pension benefits should be explicit, i.e. the *correct* pay level should be set and if there is a need for a deduction in respect of pension arrangements this should be made by increasing the explicit contribution.

Introduction of explicit employee contribution

22.2.16 A standard rate of pension contribution has been introduced for new entrants to all parts of the public service (apart from the groups listed in the footnote to Paragraph 22.2.2). However, a significant number of public servants, who took up employment prior to 6 April 1995,

[266] In Section 22.7, we address the question of the differences in pension terms applying to non-established compared with established employees (including employee contributions). As regards the application of standardised contribution rates for enlisted personnel in the Defence Forces, this is included as part of our recommendations on a new Defence Forces Pension Scheme (see Paragraph 21.6.6 (vi)).

do not currently pay an *explicit* main scheme contribution, or pay a contribution of less than 5%. All other public servants make an explicit 5% main scheme contribution, integrated as appropriate.

22.2.17 It was strongly argued in a small number of submissions that an explicit main scheme contribution of 5% should be introduced for these public servants and that salaries and pensionable allowances should be uplifted accordingly. The main groups which would be affected by any change are the pre-April 1995 entrants to the civil service, Defence Forces,[267] and the Garda Síochána. The uplift in the case of the first two groups, to whom no main scheme contribution applies at present, would be 1/19th or 5.26% of salary and pensionable allowances. In the case of the Garda Síochána, to whom a main scheme contribution of 1.75% already applies, the uplift in salary and pensionable allowances would be lower, at 3.42%. The effect of the change, insofar as pensions are concerned, would be to increase the remuneration base for the calculation of pension benefits.

22.2.18 The Commission notes that the debate on contribution rates dates back some considerable time, and has been related to a number of other issues, including consideration of the most appropriate financing basis for different public service schemes. The non-contributory nature of the Civil Service Pension Scheme (disregarding the April 1995 change) dates from the nineteenth century; the scheme was contributory for a time during the first half of that century.[268] The $2\frac{1}{2}$% contribution for the Garda Síochána Pension Scheme (now 1.75%) dates from the mid-1800s when police pension funds were being established throughout the United Kingdom. Prior to the making of the 1934 National Teachers Superannuation Scheme, national teachers paid an explicit contribution, fixed at 4% of salary in 1921, to a pension fund charged with meeting teachers' pension costs. The 1934 scheme was non-contributory, but because the Government had effectively abolished the teachers' pension fund and taken on the liability for future pension costs, teachers' salaries were cut by 9% (the net reduction was 5% as teachers were no longer required to pay the explicit 4% contribution). In 1968, an explicit 5% contribution was introduced for national teachers in the context of a move to a common contributory salary scale for all teachers (secondary teachers had traditionally paid a 5% contribution).

22.2.19 We have estimated that the cost impact of the change sought, if applied to serving public servants as well as to current pensioners, would be to increase annual benefit expenditure, in constant (1997) price terms, by £13 million in 2002 (i.e. 1.6% of projected benefit expenditure in that year), rising to £39 million in 2027 (1.6% of projected benefit expenditure). After 2032, the addition to benefit expenditure would begin to fall and, in the long run, would eventually disappear. It should be noted that these are estimates of the increased cost of pension benefits arising from the higher remuneration base on which pension benefits would be calculated. The additional pension contributions received from employees would go to cover the increased payroll costs. Of course, these pension cost estimates exclude the impact of the increased salary rates on the cost of employer PRSI, overtime and unsocial hours allowance payments.

22.2.20 The addition to the State's accrued liabilities arising from the change would be of the order of £340 million.[269]

[267] Officers commissioned prior to 6 April 1995 would be affected in the first instance. Enlisted personnel (including new entrants) do not currently pay an explicit main scheme contribution. For the Commission's recommendations on a new Defence Forces Pension Scheme, see Chapter 21.

[268] Hughes, G., *The Irish Civil Service Superannuation Scheme* (1988), p. 105.

[269] Commission on Public Service Pensions, "Further Actuarial Review of Impact of Changes to Pension Scheme Terms" (October 1999), Report prepared by Mercer Ltd.

22.2.21 The arguments in favour of introducing an explicit contribution for the groups concerned are:

(i) in equity, the public servants concerned should be entitled to have their pension benefits calculated on a higher remuneration base in the same way as other public servants who are on *contributory pay scales*. The effects of this can be seen where there are employees in different areas of the public service which are agreed to be doing identical work and where it is also agreed that they should have identical pay as a result but one is in a non-contributory scheme and the other is in a contributory scheme. In such a situation, if the former is paid £19,000 a year, then the latter receives £20,000 a year with the first paying no explicit contribution and the second paying a 5% explicit contribution. The result is that both of them have the same income while working (£19,000) but when it comes to superannuation, one has a higher pension than the other, since the gross pay is the base for pension purposes;

(ii) a similar adjustment was made in 1968 when a 5% contribution was introduced for national teachers to bring their pay scales into line with those of secondary teachers. This change — which was made to introduce consistency as between different categories of teachers — strongly supports the need to recognise the same issue of consistency as between the public servants concerned in this issue and other public servants;

(iii) it is a historical accident that the groups concerned do not currently have contributory pension schemes;

(iv) with the introduction of full PRSI and employee contributions for new entrants taking up employment after 6 April 1995, the position will be rectified for the future. This makes it more important to address the position of those public servants who have been left behind following the change and who are a declining group since all new employees from April 1995 in the employments concerned have an explicit contribution.

22.2.22 The arguments against the change are as follows:

(i) as indicated above, the cost of introducing employee contributions for the groups affected would be substantial. In addition, the uplifting of salary scales would give rise to increased overtime payments, employer PRSI contributions, etc.;

(ii) the application of uplifting in return for a contributory scheme would mean that public servants who served on the uplifted scales for as little as one day would benefit from those scales, as would pensioners who never had the uplifted scales. Such an artificial transaction would be difficult to justify having regard, in particular, to the costs involved and to the fact that, despite the cost, it would not contribute to addressing the agreed issues of concern in public service pension arrangements;

(iii) in the past, different public service schemes had different financing and contribution arrangements and, as indicated above, these were subject to change over time. The introduction in April 1995 of contributory scales and explicit main scheme contributions to areas where they did not previously exist was done solely with the aim of ensuring equity of treatment for new entrants to contributory and non-contributory parts of the public service in the context of the introduction of full PRSI and a reduction in occupational pension benefits. The 1968 change to teachers' pension terms was made in order to establish a common pay scale for serving national and secondary teachers. Unlike these two examples, there are no independent factors supporting the argument in favour of contributory scales and explicit pension contribution in this case.

22.2.23 The Commission gave careful consideration to these arguments. We were concerned particularly about the cost implications of the proposed change which, in the context of our projections of the future cost of public service pensions, would be difficult to justify. In addition, we remained unconvinced by the argument that because main scheme contributions applied to modified PRSI class public servants under local authority, health service, and teachers' pension schemes, they should have applied also to modified PRSI class civil servants, Defence Forces personnel, and members of the Garda Síochána, with consequent adjustment in pay rates (and in the rates of pension currently in payment).

22.2.24 In other parts of this Report where we noted differences in pension terms as between two separate groups which could not be justified by reference to operational or other reasons, we recommended that the difference in treatment should be removed for new entrants. Insofar as differences in employee pension contribution arrangements are concerned, this outcome has already been achieved as part of the April 1995 change to introduce full PRSI for all new entrants to the public service. For these reasons, the Commission is unable to recommend the introduction of explicit pension contributions and consequent uplifting of salary for the groups affected.

Three members of the Commission expressed reservations regarding the approach adopted in relation to this matter — see Paragraph 13 of ''Reservation by Senator Joe O'Toole, Rosheen Callender and Dan Murphy''.

22.3 Notional added years

22.3.1 The granting of notional added years of pensionable service to certain public servants in professional, technical, and other grades is a particular feature of public service pension schemes. The notional added years are intended to compensate for the inability of individuals in such positions to qualify by maximum retirement age for a *full pension* based on 40 years' service.

22.3.2 There are two types of added years award, professional added years and *ad hoc* added years.[270] The former normally provides a larger award, and is applied mainly within the local authority, Health Board, and university sectors to designated professional grades and academics, respectively (there is also a civil service scheme, but it is rarely used, having been largely superseded by the later scheme). The *ad hoc* added years schemes apply to both professional and technical staff in the civil service and state-sponsored bodies, and to technical staff (mainly) pensionable under the Local Government Superannuation Scheme (LGSS). They are subject to more stringent criteria than professional added years schemes in relation to qualification and abatement of awards.

22.3.3 The **professional added years** scheme in the local authorities/Health Boards was first introduced in the nineteenth century as an aid to recruitment. The system adopted was to simply designate all professional grades recruited through the Local Appointments Commission with the result that all entrants past and future would automatically benefit. This blanket approach means that it can apply to grades in circumstances where a difficulty in recruitment is not a factor. Qualifying professional posts include engineers, doctors, architects, as well as top management

[270] So termed because they derived from the fact that the terms of the scheme for grant of added years to professional grades in the civil service were widened as a result of an *ad hoc* arbitration in 1985.

grades. The number of added years awarded is one-third of the officer's pensionable service, subject to a maximum of ten years. Such an award cannot bring total pensionable service over the 40 year threshold, and if the individual retires between ages 60 and 65 (except on ill health grounds) the addition must be reduced by the difference between the age of retirement and age 65. No award is allowed where a person leaves service before age 60 (except in case of ill health early retirement).

22.3.4 ***Ad hoc* added years** are awarded to technical and professional public servants in circumstances where the minimum qualifications and experience for a post are such that a person could not have been appointed to it by age 25. Under the original scheme (which still applies in the local authorities, education and health service, etc.), a *gross award* (of up to ten added years) is made if the minimum qualifications and experience required for a post are such that an appointment could not have been made by age 25 (it is assumed that the education/training for the occupation in question commences at age 18). For example, if a particular post requires a qualification which takes three years to obtain, followed by five years' relevant experience, the appointment could not be made by age 26, and the *gross* added years award is eight years. Alternatively, if a minimum entry age in excess of 25 years is specified, added years equal to the difference between the specified entry age and age 25 may be allowed.

22.3.5 Such gross awards are often subject to significant reduction or *abatement* at retirement, for example, to take account of other pension entitlements (including State Social Insurance benefits), or where retirement takes place prior to age 65.

22.3.6 Public servants covered by the LGSS (which is contributory) who qualify for added years under the *ad hoc* scheme are required to pay outstanding contributions on the added years at the time of retirement (this provision does not apply in relation to professional added years).

22.3.7 In the civil service, the *ad hoc* added years scheme has been modified for new entrants recruited on or after 1 April 1997. A more restrictive method of calculating gross awards applies under the new scheme. However, compared with the original scheme, the abatement of awards is much more limited – for example, there is no abatement where retirement takes place between ages 60 and 65.

22.3.8 In our view, the arguments in favour of the schemes of notional added years are as follows:

(i) as an incentive to recruitment. It can be argued that the added years schemes are an important factor in attracting suitably qualified people to various professional positions;

(ii) as a means of retaining staff. Most of the schemes do not award added years where a person resigns before age 60. The revised civil service scheme is an exception to this;

(iii) in many cases, because of stringent educational and qualification requirements, individuals taking up employment in professional and technical positions in the public service have no past pensionable service and so would have little opportunity to qualify for maximum pension entitlements by retirement age.

22.3.9 The arguments against the continuation of these schemes include:

(i) as discussed in Section 7.2, many individuals now entering general grades in the public service have a range of professional and educational qualifications. It is inappropriate to continue a system of added years for certain professional and technical grades in that context;

(ii) a weakness in the added years system is that it takes no account of the needs of the public service at any particular time. For instance, if the economy is sluggish and there is an excess number of professionals in the job market, automatic qualification for added years is an unnecessary and costly enhancement. Such a facility would not generally be available in the private sector for an equivalent position;

(iii) in times of heavy demand for professional employees, it would seem more appropriate that pay — which would be more flexible and responsive to immediate needs — should be the main factor in recruitment policy rather than an added years scheme at retirement;

(iv) pensions coverage within the private sector is now more extensive than when the added years schemes were originally introduced. Many of those entering the public service in a professional capacity may already have accrued pensionable service. This, combined with the availability of purchase of notional service and AVCs, reduces the need for the State to provide additional years for such groups. SPEARS (see Chapter 19) could also play an important role in enabling employees to provide for additional pension;

(v) added years schemes inhibit employment mobility by discouraging people from moving out of the public service. They also inhibit mobility within the public service (for example, those in professional grades would appear to be reluctant to move to the civil service from the local authority sector because of the impact on potential added years awards);

(vi) there are anomalies in the application of added years schemes in different parts of the public service. For example, some universities offer added years to administrative as well as academic staff, while administrative staff are excluded from the civil service *ad hoc* added years scheme. Also, lecturers in third level colleges and institutions are subject to the terms of the *ad hoc* scheme while university lecturers, as well as professional staff covered by the LGSS, are covered by the more favourable professional added years provisions.

22.3.10 The growth of pensions coverage in the private sector coupled with more extensive transfer and preservation arrangements means that many individuals have already accrued pensionable service before they take up public service employment. Moreover, there is more scope for individuals to make additional pension provision for themselves than in the past through the notional service schemes and various AVC arrangements. The introduction of SPEARS would further improve this position. It is also relevant that the added years schemes were introduced for public service groups at a time when the majority of public servants had limited Social Insurance coverage; this is no longer a factor for future entrants, given the extension of full PRSI to all public servants.

22.3.11 The Commission considers that the schemes of notional added years are a crude instrument for the purposes of addressing recruitment difficulties. They are not designed to be responsive to the needs of the relevant areas of the public service at the time of recruitment. We believe that pay (and/or the lodgement of employer contributions to SPEARS) would be a more appropriate and responsive recruitment incentive. In our view, such an approach would allow for more effective targeting of those areas of the public service in which particular recruitment difficulties were being experienced at any given time.

22.3.12 Having weighed the considerations for and against, the Commission is of the view that the schemes of notional added years are no longer appropriate as a component in public service pension arrangements and, accordingly, recommends their abolition for new entrants.[271] In that context, consideration should be given to the offer of other forms of recruitment incentive.

22.4 Portability of pensions/preservation of service

22.4.1 Increased mobility and more widespread pensions coverage in the private sector has led to demands for the introduction of facilities to enable transfer of pensionable service into public service schemes. A similar demand has arisen in relation to pensionable employment in the public service abroad, particularly in Northern Ireland and Great Britain. Several submissions to the Commission sought a facility to transfer service on a year-for-year basis from private sector schemes and from public service schemes abroad. Such an arrangement is available for transfers between public sector schemes, including the small number of private sector schemes covered by the transfer network (see Paragraphs 3.3.45 and 4.3.8).

22.4.2 The main issue in the transfer of pension rights is cost. In the context of private sector schemes, Part III of the Pensions Act, 1990 has established a legal framework for the portability of pensions which enables members (in certain circumstances) to transfer their benefits to the scheme of a new employer. A member's benefits must be converted into a lump sum in order to effect the transfer. In a defined benefit scheme, the transfer payment is the actuarial value of the preserved benefit on the date on which the notification to transfer is received (under the Act, trustees are not obliged to include benefits accrued prior to 1 January 1991).[272] In a defined contribution scheme, the transfer payment is the accumulated value of the *appropriate contributions*, as defined under the Act.

22.4.3 There is no particular reason why public service schemes should not accept transfer payments in respect of pensionable service given in previous employments. In the past, transfer payments have been used to purchase service under the lump sum option of purchase of notional service schemes.[273] If our recommendations in Chapter 19 are implemented, it would be possible to lodge transfer payments to individual SPEARS savings accounts.

22.4.4 The question of transferring service on a year-for-year basis (assuming both schemes are defined benefit final salary schemes, as in the public service) raises major cost issues. These arise because of differences in the relative value of the benefits earned between the two schemes:

- the starting pay of the position in the new employment is generally higher than the final pay of the previous employment;

[271] For the purposes of this recommendation, *new entrant* includes a person who takes up employment having served elsewhere in the public service, but not if he or she had an entitlement to added years in the previous public service position.

[272] We understand that this position is to change shortly as a result of the Government's acceptance of the National Pensions Policy Initiative proposal that for those leaving pensionable employment after 1 January 2001, preservation of benefits for pre-1991 service should be introduced by 1 January 2001, revaluation by 1 January 2006, and that funding standards in respect of these must be fully met by 1 January 2011.

[273] At present, pensions legislation does not allow for the payment of transfer amounts to unfunded pension schemes (which include public service schemes). We understand that a technical amendment is to be proposed shortly to address this issue (see Paragraph 8.16.4).

- salary progression in the new employment will likely be greater than the rate of increase applied to the preserved benefit in the previous employment; and
- when it eventually comes into payment, the Irish public service pension will be increased in line with pay which is more favourable, and hence more costly, than pension increases applied to the pension earned in the previous employment.

22.4.5 The calculation of a transfer amount automatically captures the effect of these cost differences. In general, a transfer amount would purchase a period of service in an Irish public service scheme which would be less, sometimes much less, than the period actually worked in the previous employment.

22.4.6 Thus, while it may be desirable to transfer benefits to the new scheme – benefits are consolidated in one scheme, meaning that the person does not have to enquire about pension benefits in the former workplace – the cost implications have to be taken into account. In certain cases, it might be better not to transfer, but instead to preserve the benefits in the original scheme: preservation ensures that the pension earned in the first employment is safeguarded, to be claimed at normal retirement age, and that its value is increased in line with price inflation (subject to an annual limit).

22.4.7 A transfer scheme of the type operated in the public service, which allows for transfer on a year-for-year basis, involves the taking on of substantial liabilities by the participating organisations. Such an arrangement can only be expected to operate by agreement with the other organisations and on a reciprocal basis. A transfer scheme which did not operate on a reciprocal basis would have the effect of imposing an open-ended and one-sided obligation upon public service employers.

22.4.8 In all the circumstances, the Commission recommends that (apart from the special rules applying to organisations covered by the Public Service Transfer Network) public service schemes should operate the same arrangements as apply to private sector occupational schemes generally in relation to the accepting of transfer payments in respect of previous employments.

22.4.9 The transfer of public sector pension entitlements from other European countries is a more difficult matter to address, however, due to differences in pension arrangements between countries. At present, only Social Insurance entitlements accrued in the EU, or other countries where reciprocal agreements are in place, are reckonable in this country.

24.4.10 However, there appears to be a growing acknowledgement that occupational pension schemes should be able to take full advantage of the opportunities of the Single Market and the Euro. This is the basic premise underlying EU level action in this area and, in this context, the European Commission announced in the 1999 *Financial Services Action Plan* that it will make concrete proposals in the near future revolving around two main planks. The first of these is a proposal for a Directive on the supervision of occupational pension funds and the second is the coordination of national tax rules. This proposed modern framework for occupational pension schemes is an immediate priority for the European Commission and will have the objectives of protecting the rights of members and beneficiaries, helping supplementary pension institutions to perform as well as possible, permitting cross-border affiliation and liberalising the provision of asset management and custodial services for pension funds.

22.4.11 We consider that the transferability of pensionable service cannot be addressed on a unilateral basis and will only be dealt with satisfactorily with the cooperation of the individual EU member states.

22.4.12 However, in view of the increasing numbers entering the public service in Ireland who have served previously in the UK public service, we recommend that the relevant authorities here take up with the relevant authorities in the UK the question of amending the respective transfer schemes so as to enable individuals who have built up pension entitlements in the public service in one jurisdiction to have the benefit of those entitlements transferred to the other jurisdiction and given appropriate credit for the purposes of the pension scheme applicable in the other jurisdiction. We recognise that any such arrangements could only be made where there was an agreement to operate them on a reciprocal basis and that the arrangements would have to reflect the overall parameters of the schemes. (In practice, therefore, it is likely that any such changes would only apply in relation to future transfers and that the service credit would be the actuarial equivalent of the accrued entitlements.)

22.4.13 The option to preserve pension benefits on resignation, having five or more years' service, was introduced into the Civil Service Pension Scheme with an effective date of 1 June 1973. Preservation was subsequently extended to other public service pension schemes. It did not have retrospective effect. Thus, former public servants who resigned prior to the effective date have no entitlement to preserved benefits. A number of submissions raised this matter and asked the Commission to review what they describe as the arbitrary nature of this decision.

22.4.14 The Commission has some sympathy with the views expressed in the submissions received. However, we are of the view that, prior to the introduction of preservation, the foregoing of pension was clearly understood to be an integral part of the decision to leave the public service prior to retirement age. We also consider that it was appropriate to apply a cut-off date (as well as a minimum service threshold) when preservation was being introduced in the mid-1970s. The approach adopted by public service schemes, i.e. to preserve benefits for all service of qualifying individuals, not just service accrued after the effective date, was more favourable than that provided for in the Pensions Act, 1990 (see Section 8.16 and Paragraph 22.4.2). For these reasons, the Commission is unable to recommend a change in the conditions which were applied when preservation of benefits was first introduced into public service schemes.

22.5 Pension terms on ill health early retirement

22.5.1 Several submissions received by the Commission sought an improvement in ill health retirement terms. At present, employees can qualify for a pension on ill health grounds if they have served for a minimum of five years' service and are found to be medically unfit to continue in employment. Up to ten notional added years may be granted, though the normal award is $6\frac{2}{3}$ years. Generally, the award is calculated by reference to the minimum retiring age of 60, rather than the maximum retiring age of 65.

22.5.2 In Paragraph 8.14.1, we report that a quarter of schemes of large firms calculate ill health benefits by including *all* prospective service to normal retirement age; 15% include actual service accrued to date of retirement, with no actuarial reduction for early payment of benefit; 33% provide a pension based on actual service to date of retirement, with actuarial reduction. The remaining 27% of schemes refund the value of the fund in a defined contribution scheme, or pay an amount based on a percentage of salary, or pay an amount determined by permanent health insurance plans.

22.5.3 In Chapter 15, we have expressed concern about the experience of high numbers of early retirements on ill health grounds in certain parts of the public service, and have recommended that a review be carried out on procedures in this area with the aim of developing a consistent practice for the public service as a whole (see Paragraph 15.15.27).

22.5.4 While some private sector schemes provide more favourable terms, the Commission believes that the existing pension terms on ill health retirement in public service schemes are generally reasonable. We would note that the number of years required to qualify for ill health pension would be reduced from five years to two years, in line with our recommendation to reduce the number of years required to qualify for pension benefits (see Paragraph 18.6.13). We would note also that the modification to integration recommended in Chapter 17 would benefit public servants retiring on ill health grounds whose remuneration was less than the cut-off point envisaged in the formula proposed of three times the rate of Old Age (Contributory) Pension.

22.6 Pensionability of allowances: consequences for pensioners

22.6.1 In the past, decisions were made to introduce new (pensionable) allowances in the nature of pay or to make pensionable certain allowances already in payment. Generally, the impact of these decisions for pensions applied from a current date, i.e. in respect of personnel who retired following the effective date of the decision. Pensioner groups, particularly those representing retired members of the Garda Síochána and the Defence Forces and retired teachers sought consequential increases in pension arising from a number of these decisions.[274] Further information on this issue is set out in Appendix 11.5.

22.6.2 The Commission obtained actuarial advice on the impact of making the allowances in question pensionable in the specific case of Garda and Defence Force pensioners for future pension payments only. The advice indicated that this would result in an immediate increase in benefit expenditure of £9 million per annum, based on 1997 costs. Because of the age profile of the groups in question, the level of increase was projected, in constant (1997) price terms, to fall substantially over the following 25 years, and by 2022 would amount to an additional annual cost of £2 million. There would be no additional costs after 2032.

22.6.3 The accrued liabilities of the State would increase by £116 million if this change were implemented for both groups.[275]

22.6.4 It was argued on behalf of the groups affected that these allowances represented an integral part of remuneration and, consequently, that an increase in pension should have been made so as to be consistent with the policy of pay parity.

22.6.5 On the other hand, pensions increase policy laid down by the Department of Finance, and as operated over the past 20 years, states (see Appendix 3.2, Paragraph (ix)) that if emoluments which were not hitherto pensionable become pensionable, or a new pensionable emolument is introduced with effect from a specific date, personnel who retired prior to that date do not benefit from such developments.

[274] This issue might not have arisen had the new system of pension increases based on a Public Service Earnings Index (as recommended in Chapter 16) been in place. This is because under that system, any new allowances in the nature of pay would be included in the figure for remuneration for the group in question. Thus, the new allowance would, as with an increase in pay for any public service group, feed into the calculation of a single rate of pension increase to be applied to all public service pensions.

[275] Commission on Public Service Pensions, "Further Actuarial Review of Impact of Changes to Pension Scheme Terms" (October 1999), Report prepared by Mercer Ltd.

22.6.6 The Commission has shown that the cost of any change in policy on this matter would be substantial. In addition, a change in policy could possibly extend to other pensioner groups with similar claims for pension increases. Accordingly, having assessed the arguments involved, the Commission does not recommend any increase in pension for the groups concerned.

22.7 Differences in pension terms between established and non-established type employees

22.7.1 Different pension terms apply to established and non-established civil servants: the age of retirement is 60-65 for the former (excluding Prison Officers), and age 65/66 for the latter; newly appointed established (but not non-established) civil servants pay an explicit main scheme contribution and are subject to an uprated salary scale; and a different form of integration applies to both groups in respect of contributions and benefits under the spouses' and children's scheme. There are a number of differences too in the pension terms of officer and non-officer grades covered by the LGSS, in relation to minimum death gratuity, membership of scheme for temporary employees, etc.

22.7.2 It would appear that differences in pension terms between established and non-established employees in the public service have arisen because of the significant differences in the nature of each form of employment. Traditionally, established civil servants have been recruited centrally and are permanent and pensionable (see Paragraphs 3.3.22-3.3.23). Non-established civil servants on the other hand are appointed by Ministers and their employment status is deemed to be temporary. In the civil service, non-established employees were only granted pensionability as late as 1970.

22.7.3 The Commission considers that the distinction between established and non-established employees for pension purposes has become anachronistic for the vast majority of public servants: new entrants to both groups are now fully insurable under the Social Insurance Code and atypical employment, which is becoming increasingly prevalent, is removing the basic points of difference between both streams. The Commission's aim is to remove all points of difference in pension terms which cannot be justified by reference to objective operational factors.

22.7.4 Accordingly, the Commission recommends that, in the context of further public service reforms which would have the effect of removing points of difference between established and non-established type employment in the public service, the pension terms for non-established employees (new entrants) should be amended to bring them into line with those of established employees (new entrants).

22.8 Pension scheme coverage for certain professional and other groups

22.8.1 A number of groups provide professional and other services to the State on a basis other than a standard employer-employee relationship. Often, these groups are self-employed and are in a position to engage in business outside of the public service. The State pays these groups for the services provided on the basis of fee, commission, stipend, or other arrangement. A number of groups, including State Solicitors and Coroners, sought pension entitlements in submissions made to the Commission.

22.8.2 In Paragraph 18.6.1, the Commission recommends that those in atypical forms of employment should be granted access to public service pension schemes. As regards the groups referred to above, it is necessary to determine in the first instance whether or not they may be considered to be *public service employees*. To do this, a number of factors should be taken into account, including status under the tax and Social Insurance systems. The position can sometimes be unclear, and may require the making of a formal determination (which can sometimes be subject to appeal).

22.8.3 The Commission considers that groups found to have an employee relationship with the State should, in principle, be given access to public service pension occupational schemes. However, the defined benefit final salary structure of the schemes may cause difficulties in accommodating such groups, having regard to their form of remuneration. In the absence of a change to salary based remuneration, a defined contribution pension structure might be considered more appropriate.

22.8.4 It is, of course, open to groups not considered to be public service employees to assign part of their fee or stipend for payment into their own personal/company pension plan.

22.9 Other issues

Revenue limits

22.9.1 The question of Revenue limits was raised in a number of submissions.[276] While this matter does not formally come within the Commission's terms of reference, we have suggested at Paragraph 19.10.9, in the context of the introduction of SPEARS, and in line with the recommendations of the National Pensions Policy Initiative, that consideration should be given to introducing greater flexibility into the operation of these limits.

Compulsory membership

22.9.2 The compulsory nature of the membership of public service occupational pension schemes was questioned. It was suggested that public servants should be enabled to opt out of occupational schemes and to contribute to personal pension plans, as is permitted under UK public service pension arrangements. The Commission does not favour such a proposal, as we consider the current arrangements to be the most satisfactory way of providing for occupational pension coverage in the public service.

Forfeiture of pension

22.9.3 As a result of a revision of the Civil Service Pension Scheme with effect from 1 January 1994, provision for forfeiture of pension has been removed in case of dismissal or resignation to pre-empt dismissal (except where there is financial loss to the Exchequer — see below).[277] Consequently, dismissal or resignation to pre-empt dismissal will not affect entitlements to preserved lump sum and pension, which are payable, as in normal circumstances, on application from age 60.

22.9.4 Provision has also been made under the civil service scheme to pay preserved pension and lump sums on application to those who were dismissed or resigned to pre-empt dismissal prior to 1 January 1994 (it should be noted that these arrangements do not apply to dismissals or resignations to pre-empt dismissal prior to the introduction of preservation). Such benefits are payable from a person's 60th birthday or 1 January 1994, whichever is the later.

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[276] We summarise the key Revenue limits at Appendix 12.1.

[277] It might be noted that Part III of the Pensions Act, 1990, which deals with preservation of benefits, prohibits forfeiture in respect of preserved benefits. Public sector schemes are excluded from this part of the Pensions Act.

22.9.5 In all cases involving financial loss to the Exchequer, the amount of the loss, plus compound interest, is recouped from the employee concerned or, in the event that the losses are not otherwise repaid, they are recouped from the preserved benefits payable.

22.9.6 The civil service changes to the operation of forfeiture have now been applied to other public service schemes, including the LGSS and the Garda Síochána scheme.

22.9.7 The Commission considers that the exercise of forfeiture in this way is appropriate. In Paragraph 22.9.34, we recommend a reduction in the interest rate to be charged on the recoupment of financial losses to the Exchequer.

Pensionability of variable allowances, including overtime, bonuses, etc.

22.9.8 The general rule under public service pension schemes is that allowances in the nature of pay are pensionable if they are of a permanent nature or are for extra or inconvenient hours of duty, if a regular and recurring feature of the job and a compulsory condition of service, e.g. unsocial hours duties, and shift allowance. *Overtime* is pensionable in certain limited circumstances where it is, in effect, equivalent to an allowance, being regular, rostered, compulsory and substantial, and given in a working context where management have determined that overtime is the most efficient means of dealing with the work involved.

22.9.9 A number of submissions argued that the definition of pensionable allowances should be extended to include overtime generally. The Commission has considered this matter, but believes there are no substantive grounds for recommending a change of this nature. The fact that overtime is usually of a fluctuating nature, i.e. there is no regular and recurring pattern to the overtime worked, means that it does not meet one of the essential characteristics of a pensionable allowance.

22.9.10 In the context of changes in the pay determination system in the public service, which can be expected to change further, within the terms of the *Programme for Prosperity and Fairness*, it is necessary to consider the question of the *pensionability of performance-type payments*, such as merit pay, bonuses, etc. The Commission believes that there is no compelling argument in favour of pensionability of such payments as, in most circumstances, such rewards are of a once-off nature. Even where of a more regular nature, there is unlikely to be any significant pattern to justify making them pensionable.

22.9.11 However, we have commented elsewhere that the pensions system should not be an unnecessary deterrent to change. It is possible that there may be a move at some future date to introduce a system of performance pay as an important element in public service remuneration. Accordingly, we would not rule out absolutely the possibility that certain limited forms of performance pay could be included in pensionable remuneration, in a way that was consistent with normal policy in relation to pensionability of allowances.

22.9.12 The Commission considers that the use of SPEARS (as recommended in Chapter 19) would enable employees, subject to the Revenue limits, to make appropriate provision towards the pensionability of overtime, bonuses (including once-off payments), or other variable non-pensionable allowances received over the course of their careers.

22.9.13 The calculation of pension on variable allowances such as unsocial hours payments was raised in submissions, particularly the focus on the final three years of service under the *three-year* *averaging rule* (see Paragraph 3.3.31). It was suggested that this approach put pressure on employees to work extra unsocial hours close to retirement when they might prefer to work less, and that it disadvantaged employees who became unable to work unsocial hours due to ill health. Employers, too, have suggested that there are sound operational reasons why employees should have the choice not to work operationally demanding duties, or to work reduced hours in the lead up to retirement, without unduly affecting their pension entitlements.

22.9.14 The Commission considers it appropriate to address this issue. We believe that the pension system should not result in a distortion of preferred work choices. Accordingly, we recommend that the reckoning of variable pensionable allowances under the *three-year averaging rule* should, subject to any necessary adjustment or amendment of the Revenue limits, be changed to an average of the variable pensionable allowances received in the best three consecutive years in the ten years preceding retirement, as uprated to the date of retirement, in line with the Public Service Earnings Index (see Chapter 16). Averaging would not apply in this way in cases in which salary on promotion had effectively taken the place of allowances received in the ten years preceding retirement, or where the allowances in question had been incorporated into the pay scale. There would be no change in the averaging rules as applied to salary.

22.9.15 The Commission acknowledges that this recommendation, which will facilitate public servants who wish to have greater flexibility prior to retirement, as well as meeting the concerns of employers, would give rise to some minor additional costs for public service pension schemes.

Scheme reviews

22.9.16 A number of submissions pointed to certain pension terms in public service schemes which might now be considered to be obscure, unnecessary and dated. We did not examine these in any great detail. However, we recommend that, as a general principle, pension terms and provisions which now appear outdated or which add to the complexity of pension schemes without conveying any significant advantage in terms of efficacy, fairness, or cost should be deleted or modified as appropriate.

Pensionable service

22.9.17 The Commission considered the question of making pensionable certain periods of time spent in training, developing new skills, or otherwise acquiring appropriate and relevant experience, whether pre-service or after taking up employment, on an unpaid non-pensionable basis. We do not recommend that such periods should be made pensionable in light of the general principle that, except in certain very limited circumstances, only paid public service employment should be reckoned for pension purposes. It would be open to individuals who had engaged in external training or skills development of this nature to avail of SPEARS (if implemented) to enhance their pension position. Our views on this matter are consistent with our approach in relation to the grant of notional added years for those in professional grades (see Section 22.3).

Age limit for children's pensions

22.9.18 An increase in the upper age limit for the payment of children's pensions under spouses' and children's contributory pension schemes was suggested in a number of submissions. On this matter, we note that the recent civil service scheme increase in the age limit for payment of pensions to children in full-time education from age 21 to age 22 is to be applied across the public service. We do not believe that any further increase is necessary, but consider that the age limit should be kept under review in light of developments in the Social Welfare code.

Equalisation of pension contributions in the Garda Síochána scheme

22.9.19 Some members of the Garda Síochána pay pension contributions at a rate of 2.5% of salary as opposed to the standard rate of 1.75% of salary. This has arisen from the equalisation of retirement options for male and female members in 1983 (see Paragraph 3.8.6). Prior to 1983, female Gardaí were entitled to retire on full pension at age 50, provided they had 25 years' service (they paid contributions at a rate of 2.5% of salary). Male Gardaí could retire on full pension at age 50, provided they had 30 years' service (their contributions were paid at a rate of 1.75% of salary). In 1983, female Gardaí were offered the retirement terms applicable to male Gardaí (including the 1.75% contribution rate), while male Gardaí were offered the terms applicable to female Gardaí (including the 2.5% contribution rate). All new entrants after 1983, male and female, are conditioned to the arrangements applicable to male Gardaí.

22.9.20 Submissions argued that several of those who accepted the 25 year option (subject to the 2.5% contribution rate) misunderstood its purpose, as they have, or will have, 30 years' service by age 50 anyway and are not benefiting from the higher contribution. Others who would not have had 30 years' service by age 50 have decided to continue in employment and will in fact have 30 years' service at retirement. It was argued that members of the Force who are subject to the 2.5% contribution rate should be allowed to pay the lower contribution rate and that a refund of the additional contribution should be made where, it was suggested, no benefit is derived from it.

22.9.21 The Commission considers that the purpose of the additional contribution was made clear at the time when the option was presented, i.e. to provide a facility to retire on or after age 50 after 25 years' rather than 30 years' service. The fact that the facility is or is not taken up is not relevant. Accordingly, we can see no reason why pension contributions should now be equalised.[278]

Social Welfare issues

22.9.22 A number of submissions raised issues which were specifically relevant to Social Welfare policy, such as the non-entitlement of public servants in modified PRSI class to the Old Age (Contributory) Pension,[279] and to certain entitlements such as free electricity, free travel etc., which may be granted to those in receipt of Social Insurance payments. The Commission has made no recommendations on these issues, as they do not come within our terms of reference. However, we note that Budget 2000 extended entitlement to Free Electricity Allowance, Free Telephone Rental Allowance and Free TV Licence to all persons aged over 75 years from October 2000, regardless of their income or household composition. This improvement will therefore benefit those public service pensioners aged over 75 who do not currently qualify for these free schemes due to income and/or household composition rules.

Five year pension guarantee

22.9.23 Payment of retirement pension ceases on the death of the former public servant. Where death occurs shortly after retirement, a balancing gratuity may be payable, usually to the deceased's estate, which is equal to any shortfall between the annual pensionable remuneration (i.e. the minimum death gratuity payable in case of death-in-service) and the total amount of lump

[278] We understand that agreement has been reached between management and the Garda Associations to restore the position of those who were under age 20 at the time of the 1983 option and so would not have been in a position to avail of the additional retirement facility.

[279] Individuals who have paid modified PRSI contributions for a large part of their working life may qualify for a pro rata mixed insurance retirement pension if they satisfy the yearly average condition using a mixture of full rate PRSI contributions and modified rate contributions.

sum and pension paid up to date of death. (Of course, spouses' and children's pensions may also be payable.)

22.9.24 It was suggested in submissions that a *pension guarantee* of five years should apply, i.e. that where a death occurs within five years of retirement, the balance of retirement pension which would have been payable over that period should be paid as a lump sum to the deceased's estate. A guarantee of this nature is included in many private sector schemes (see Paragraph 8.13.8).

22.9.25 In favour of introduction of this provision, it may be argued that public servants contribute towards their pensions, either implicitly or explicitly, and so there should be a reasonable expectation of a benefit deriving from those contributions, even where death occurs shortly after retirement. In addition, the cost of making the change would be minimal.

22.9.26 On the other hand, it can be said that overall public service terms are better, on average, than those provided in the private sector and consequently there is little justification for enhancing public service arrangements in this way.

22.9.27 On balance, the Commission considers that existing public service pension benefits in case of death shortly after retirement are adequate. In Paragraph 8.22.1, we conclude that public service schemes compare favourably with those available in the private sector. Against that backdrop, we consider that it is appropriate to adopt private sector practice on any particular issue only where there is a compelling case to do so on grounds of the inadequacy or inequity of public service practice. We do not think that this applies in this particular instance. Accordingly, we do not recommend the introduction of a five year pension guarantee of the nature discussed above.

Preservation of benefits in the case of groups with special pension terms

22.9.28 Public service groups which are subject to lower retirement ages than the norm and have enhanced pension terms (e.g. Garda Síochána, Prison Officers) are generally entitled to retire on pension during their 50s. However, where an employee resigns before normal retirement age, preserved pension entitlements (i.e. pension accrued up to date of resignation) are payable at age 60 (as in standard public service schemes) rather than from an earlier retirement age.

22.9.29 It was argued in submissions that groups which have special pension terms should be eligible for payment of preserved benefits from age 50 or age 55. The principal argument against such a proposal is that special terms are designed to cater for the demanding and physical nature of the particular work environment of these groups. Having withdrawn from this work environment, it is necessary only to ensure that the employee receives pension at the normal retirement age applicable in the public service, currently age 60.

22.9.30 Having considered this matter, the Commission believes there is no justification for paying preserved pension entitlements in the case of groups with special terms from an age lower than that applicable to public servants generally. Early retirement and enhanced pension terms are a function of the physically demanding nature of the work to which these groups are conditioned. The nature of the work and its demands are no longer relevant considerations where individuals have left service prior to retirement age, other than on grounds of ill health early retirement. Accordingly, we are of the view that uniformity of age in respect of eligibility for preserved pension entitlements should be continued for all public service groups.

Marriage gratuities

22.9.31 The repayment of marriage gratuities was raised in the submission process. Prior to 1974, female public servants were required to resign when they got married. Once they had accrued a minimum of five years' service, they qualified for payment of marriage gratuity (see Paragraph 3.3.35).

22.9.32 If subsequently reappointed, the public servant has the option to refund the marriage gratuity, in which case all prior service is aggregated with subsequent service for pension purposes. Where a person is re-employed in the normal course (e.g. through a competition of the Civil Service Commission) compound interest is charged when calculating the amount of refund due. Even with the addition of compound interest, we would suggest that it is probably in the person's interest to refund the marriage gratuity, in view of the increased pension benefits which that would give. In cases of reinstatement on compassionate grounds, i.e. widowhood or non-support by husband (provisions no longer applicable in the public service), no compound interest is charged.

22.9.33 The main concerns raised about the repayment of marriage gratuities were

- the effect of compound interest (charged in most cases at a rate of 6% per annum) on the amount of refund due;
- perceived inflexibilities in the refund arrangements; and
- the difference in treatment with regards to the charging of compound interest in the case of those reinstated on compassionate grounds and those re-employed in the normal course.

22.9.34 The Commission considers that compound interest should be applied to repayment of marriage gratuities (and in other cases in which repayments are made) in order to reflect the value of the reinstated service. However, we believe that the current rate of 6% per annum is too high. Accordingly, the Commission recommends that compound interest in the case of refund of marriage gratuities, payment of outstanding employee contributions (see below), and recovery of financial losses to the Exchequer (see Paragraph 22.9.5) should be reduced from a rate of 6% per annum to a rate of 4% per annum from a current date, and that the rate should be reviewed as a matter of course.

22.9.35 We recommend the introduction of a provision enabling marriage gratuities to be repaid over a fixed period of time (say, no more than ten years) on the basis of regular deductions from salary, rather than by specific minimum instalments such as one month's gross pay. In such situations, compound interest would continue to be applied to the reducing balance.

22.9.36 As regards the more favourable refund arrangements applicable to public servants reinstated on compassionate grounds compared with those re-employed in the normal course, the Commission does not consider that any change should be made, particularly because reinstatement on compassionate grounds is no longer possible.

Payment of contributions in respect of prior non-pensionable service

22.9.37 Under contributory public service pension schemes, personnel appointed to permanent positions subsequent to earlier service which was non-pensionable are required to pay outstanding contributions in order to make that service pensionable. For those in modified PRSI class, compound interest is applicable at the rate of 6% per annum on the outstanding balance[280] while those employed on a full PRSI basis since 6 April 1995 pay outstanding contributions on a current salary basis.

22.9.38 The Commission believes that, as with the refund of marriage gratuities, it is appropriate that contributions for temporary and part-time service should be uprated either by compound interest or on the basis of current salary to take due account of the pensions value of the service. As above, we recommend a reduction in the compound interest rate from 6% to 4% per annum.

Supplementary pension

22.9.39 The occupational pension of employees in full PRSI class is integrated with the State Social Insurance system. This is done on the assumption that a Social Insurance benefit is, in fact, payable. However, except in cases of ill health early retirement, Social Insurance benefits may not be payable until age 65. Under public service pension arrangements, a supplementary occupational pension may be payable in certain circumstances on retirement prior to age 65 in order to make up the shortfall in total pension (see Paragraph 3.3.60 and Appendix 11.3).

22.9.40 However, the supplementary pension is not payable where a former public servant in receipt of an integrated pension is employed subsequent to retirement in any capacity which involves a Social Insurance contribution. Submissions argued that this was unfair when compared with the position of public servants who are not subject to integration (i.e. those in modified PRSI class). The latter's pension entitlements are, except in certain exceptional circumstances, unaffected by subsequent re-employment.

22.9.41 The Commission favours continuation of the existing arrangements in relation to supplementary pension. These arrangements are now applied to all public service groups following the extension of full PRSI to new entrants in April 1995. We consider that it is appropriate that a supplementary pension should be paid where no Social Insurance benefit is payable. (It would appear that most private sector schemes do not pay supplementary pensions in such circumstances.) We also consider that payment of supplementary pension should cease where a retired public servant enters into further insurable employment prior to age 66.[281]

Two-thirds pension

22.9.42 One submission raised the question of providing an option to public servants to avail of a two-thirds pension entitlement instead of the existing pension and lump sum arrangement.

22.9.43 We compare the pension benefits in public service (80ths) schemes with private sector (60ths) schemes in Section 11.4 and Appendix 11.1. We conclude that the retirement benefits in the public service are on a par with the vast majority of private sector defined benefit (60ths) schemes which adopt a 1:9 commutation rate for lump sum (1:9.8 in the case of female employees), i.e. for every £1 of pension surrendered, an equivalent lump sum of £9 is purchased. Because pension increase arrangements are more favourable in public service schemes compared with private sector schemes, the cumulative value to the pensioner over time of public service benefits compared with private sector benefits will normally be more favourable. We found also that for the small number of private sector schemes which adopt more favourable commutation rates than 1:9, resulting in a more favourable outcome compared with the public service in terms

[280] In the LGSS, those in modified PRSI class have three years to pay contributions owing before compound interest is applied.

[281] Social Insurance Old Age (Contributory) Pension is payable at age 66, regardless of whether or not the individual concerned has retired.

of pension and lump sum at point of retirement, the differences in pension increase arrangements mean that over time the cumulative value of public service benefits will normally outstrip that of private sector benefits.

22.9.44 Better benefits means higher costs. Thus, it would represent a major increase in public service pension costs to replace the existing 80ths structure for pension and lump sum with a 60ths structure (with commutation), while continuing existing pension increase arrangements.

22.9.45 On the other hand, we recognise that some public servants might desire the option to forego lump sum in favour of a higher retirement pension. Accordingly, we have recommended in Paragraph 19.10.7 that a facility be made available under SPEARS to use any or all of the lump sum at retirement to buy additional pension benefit. This would be a new option for public servants, and would be available at no additional cost to the State.

Small or temporary organisations

22.9.46 In Chapter 14, we address the question of the most appropriate pensions structure to be adopted for public service schemes. We reached a particular view in relation to small or temporary organisations, as set out in Paragraph 14.8.5. In accordance with that view, we recommend that, where it might be deemed appropriate, there should be an option to consider the introduction of funded defined contribution type schemes on a basis that was mutually acceptable to the organisations concerned and to the relevant public service unions. The rates of contribution by employer and employees should be designed so as to provide benefits which are comparable with standard public service pension benefits. Public servants in such schemes who subsequently move to areas of the public service where defined benefit pension terms apply should have the option of transferring the balance on their defined contribution accounts into SPEARS (if introduced) or the main pension scheme (see Chapter 19).

Issues outside the Commission's terms of reference

22.9.47 A number of issues were raised in submissions which we found on examination to be outside our terms of reference. These included a submission seeking an increase in the maximum allowable limit for payment of contributions into a defined contribution pension scheme for General Medical Service Scheme Doctors. The doctors concerned are self-employed and so cannot be considered to be public servants for the purposes of our terms of reference. In addition, a number of submissions raised the issue of the delayed consolidation of a restructuring pay award to pensioners in An Post. As commercial state companies are outside our remit, we are not in a position to comment on this matter.

22.10 Conclusions and summary of recommendations

22.10.1 In this Chapter, the Commission has considered a wide range of issues coming within the scope of public service occupational pension arrangements. Many of these were raised in the submission process. While a number may appear minor within the overall scale of public service pensions, each one is of major importance to the individuals or groups concerned.

22.10.2 Our approach has been to examine each issue from the perspective of the five requirements to be met by public service pensions (see Section 13.5): adequacy and comprehensiveness, viability, flexibility, fairness and cost. These factors have guided our recommendations in each case.

22.10.3 In summary, the recommendations which we make in this Chapter are as follows:

(i) continuation of standard employee contribution rates for new entrants across all public service groups (Paragraph 22.2.10);

(ii) adjustment which might be made in the pay determination process to reflect the value of public service relative to private sector pension arrangements to take employee pension contributions into account (Paragraph 22.2.14);

(iii) abolition of schemes of notional added years for professional, technical and other grades; consideration to be given to the offer of other forms of recruitment incentive (Paragraph 22.3.12);

(iv) public service transfer arrangements (other than between public service organisations) to be the same as those applying to private sector schemes (Paragraph 22.4.8);

(v) discussions to take place with the UK authorities regarding transfer of public service pension entitlements between both jurisdictions (Paragraph 22.4.12);

(vi) depending on the direction of future public service reform, pension terms of non-established employees to be amended to bring them into line with those of established employees (Paragraph 22.7.4);

(vii) changes to be made in the rules for averaging variable allowances for pension purposes (Paragraph 22.9.14);

(viii) removal or modification of pension scheme terms which now are considered outdated or unduly complex (Paragraph 22.9.16);

(ix) reduction of compound interest rate charged on refunds of marriage gratuities, outstanding employee contributions, etc. from 6% per annum to 4% per annum, with the rate to be reviewed as a matter of course (Paragraph 22.9.34);

(x) more flexible arrangements for refund of marriage gratuities (Paragraph 22.9.35);

(xi) consideration of defined contribution pension structure for small or temporary organisations (Paragraph 22.9.46).

CHAPTER 23

Partial Funding of Public Service Pensions

23.1 Introduction

23.1.1 Like Ireland, most countries meet their obligations for state social security and public service pensions out of general revenues on a pay-as-you-go basis. Some countries use a funded approach under which contributions raised today and in the past are invested, with the income stream from the resulting fund being used to pay pension costs each year. Private sector companies, too, use a funded approach and are required by law to do so.

23.1.2 Faced with concerns about the long-term sustainability of pay-as-you-go pension provision, many countries have been examining the option of a move to funding or part funding their future pension commitments. In Ireland, the debate has been partly influenced by the fact that the country is currently enjoying budget surpluses, with the national finances expected to remain in a healthy state, assuming no external shocks, for some time to come. In addition, there is the prospect of *windfall gains* arising from the privatisation of State assets. The experience of consistently high returns on equity investment over the past number of years is also relevant. This combination of factors means that, in the short-term at least, the investment of resources with the aim of part financing future pension costs has come to be considered a viable and affordable proposition.

23.1.3 In July 1999, the Government announced its decision to provide resources on a planned basis to secure the pensions in retirement of a progressively ageing population. Under this initiative, an annual provision of 1% of GNP is being set aside each year to pre-fund part of the future cost of Social Welfare and public service pensions and this is supplemented by an allocation of a tranche of the proceeds of the Telecom Éireann flotation. Enabling legislation for a temporary holding fund was passed in December 1999, and substantive legislation to establish pension funding on an ongoing basis, the National Pensions Reserve Fund Bill, 2000, was published in June 2000. The Government has stated that the funding may meet about one-third, only, of the extra costs which demographic change promises over the period to mid-century. When announcing the pre-funding initiative, the Government referred to the ongoing work of the Commission on Public Service Pensions and to the report on the National Pensions Policy Initiative (May 1998).

23.1.4 The Commission viewed the debate on pension funding as an integral part of our review, and we made a number of preliminary comments in this regard in our Interim Report (August 1997). As already noted, the Government has, in the meantime, decided to pre-fund part of the future cost of public service (and Social Welfare) pensions. In the circumstances, and having regard to our terms of reference, our approach, as set out in this Chapter, is as follows:

- to review the various arguments for and against funding in order to reach definitive conclusions on the funding of public service pensions;
- to examine and discuss the objectives to be met by a partial fund for public service pensions; and

- to make specific recommendations on the partial funding of public service pensions in the context of the Commission's overall recommendations on the public service pensions framework.

23.1.5 We have concluded for the reasons outlined below that the optimal funding solution, insofar as public service pensions is concerned, is to fund the future cost of pension increases, and we recommend accordingly. A component in our recommendation is the payment by serving public servants of a new employee contribution, to be lodged to the pension fund, in respect of pay-related pension increases under public service pension schemes (see also Chapter 16).

23.1.6 The Commission is convinced that funding for pension increases is the option best placed to deliver a public service pension fund that is independent, is capable of addressing the expected peak in pension costs, will ensure discipline and integrity as regards inflows and outflows, and will help secure the viability and stability of the public service pensions framework over the long-term.

23.1.7 The Government decision of July 1999 envisaged the setting up of two funds, one for Social Welfare pensions and one for public service pensions, while the National Pensions Reserve Fund Bill provides for a single fund to cover both sets of liabilities. However, in the press statement accompanying the publication of the Bill, the Minister for Finance indicated that the legislation could be amended at a future date to provide for two funds if, following our Report and following the necessary consultation process about the Report's recommendations, there were agreement between all parties that there should be separate funds.

23.2 Funding public service pensions

23.2.1 As a first step, we review the arguments in favour of funding public service pensions as an alternative to continuing the existing pay-as-you-go approach. Our approach in this Section is to review the arguments at a general theoretical level. In Section 23.4, we address more practical and immediate considerations relating to the partial funding of public service pensions.

Arguments in favour of funding public service pensions

23.2.2 **Transparency and cost discipline:** Funding helps to make pension costs transparent to employers and employees. Under pay-as-you-go, the recruitment of additional personnel and improvements in pension terms may have little impact on short-term pension costs but they can result in a disproportionate increase in medium- to long-term expenditure. The use of notional funding and the accounting for pensions costs on an accruals basis may be of help in this regard (see Chapter 24), but they may be viewed as artificial. Funding helps to infuse an atmosphere of realism and responsibility into the consideration of pension claims.

23.2.3 To the extent that employees contribute to the fund, these advantages are further reinforced.

23.2.4 **Spreads the State's pension costs:** A pension fund can help to smooth expected peaks in the State's future pension costs. The State would spend more money upfront (through a large initial capital injection and/or through annual contributions) and would then benefit from returns from the fund in later years. The total cost of pensions would not change — that would remain as the total outflow to pensioners — but the strain upon the State's finances would be reduced.

23.2.5 **Security:** In the private sector, pension funds are established independently of the employer. They provide security to pension scheme members and to pensioners that assets will be available with which to meet future pension commitments in the event of the employer going out of business. Arguably, the existence of a public service pension fund would provide similar security to public servants and pensioners that the State would continue to meet its long-term pension commitments. Or the fund would give assurance that the State would not at a future date cut back benefit terms or weaken conditions of eligibility so as to reduce the entitlements of public servants still in employment.

23.2.6 **State's credit rating:** For the State, putting a pension fund in place as an alternative to allowing the continuing build up of unfunded pension liabilities would be viewed positively by international organisations such as the OECD and IMF, as well as credit rating agencies. Thus, it could have the advantage of improving the State's credit rating, thereby reducing the cost of interest payments on the national debt.

23.2.7 **Approach of other countries:** While pay-as-you-go applies in most EU countries, a number of countries maintain or have recently introduced some form of pension funding, whether full funding of defined benefit schemes (ABP in the Netherlands, the UK local government scheme), funding related to a defined contribution scheme or component in public service terms (Denmark, Sweden), or a reserve fund with which to meet future pension costs (France, Germany, Finland).

23.2.8 **Funding and investment:** Many economists argue that at a macroeconomic level funding increases real investment in the economy. The belief is that when pensions come to be paid, the economy would be more productive than it would otherwise have been. Even if a large portion of the fund were held in external assets — to meet fund return and diversification objectives — the building up of a stock of high-yielding assets outside the State would be an important means of providing for a future with a higher proportion of retired people in the economy.

23.2.9 **Saving in State's net outgoings:** This would arise insofar as returns over time to the pension fund were in excess of returns that the Government would have obtained on the same monies through alternative spending (on education, infrastructure, repaying part of the national debt, tax relief, etc.). Over the past ten years, real returns to pension funds in Ireland have averaged 10.9% per annum.[282] However, this has been a period of exceptional stock market growth. Real returns to pension funds over the ten year period to 31 December 1988 was estimated at 9.1% per annum and over the 25 year period from 1964, at between 3.8% and 4.4% per annum.[283] As discussed in Paragraph 14.4.4, the volatility of stock markets in particular can have a very significant impact on pension fund performance.

23.2.10 If high rates of return to a State pension fund were maintained, then it would certainly be the case that there would be net savings to the State as a result of establishing the fund. If, instead, more modest rates of return were to emerge in the future, the argument that a fund would generate savings is obviously much less clear cut, particularly when considering what the alternative usage of the monies contributed to the fund might have been. This might have included government investment in infrastructural projects, education, training, and health care. Alternatively, the Government might have reduced taxation, and in effect returned the money to the private sector. A crucial difficulty is the measurement of the economic returns which would be received on each of these options and the extent to which increased investment via pension funding leads to disinvestment elsewhere.

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[282] Mercer Ltd., *Pension Pooled Fund Survey*, June 2000. The real rate of return is the annual return in excess of annual price inflation.
[283] William M. Mercer Fraser Ltd, *Pension Fund Investment Returns* (undated).

Arguments against funding public service pensions

23.2.11 Here we set out the arguments against replacing the pay-as-you-go approach to financing public service pensions with a funded approach.

23.2.12 **Funding does not guarantee security:** For the private sector, the primary objective of funding is to secure the pension benefits independently of the company which, no matter what its size and history, has in a commercial environment no guarantee of a continued existence. The State, on the other hand, operates in a completely different environment. Its financial obligations and commitments are met through taxation, which can be raised or lowered as necessary. As a democratic State operating under the rule of law, the possibility that it would at some future date renege on its statutory pension commitments to its former employees is so slight as to be negligible. Thus, there is no *necessity* to have a pension fund. The existence of a fund would provide no greater level of assurance that future pensions would be paid, or that they would be paid in accordance with existing terms and conditions, particularly if the State were facing an unprecedented financial crisis, or, indeed, had ceased to exist. In circumstances where the State had ceased to exist, then any fund would also cease.

23.2.13 **Transparency of costs under pay-as-you-go:** As already noted, many of the arguments in relation to a lack of transparency in the pay-as-you-go approach are capable of being addressed through the adoption of an accruals approach to accounting for pension costs under government financial systems.

23.2.14 **Cost stability:** It has been argued that pension funding leads to stability in costs. However, it might be suggested instead that the more important point is that the development of future pension costs should be known and preparations made to ensure that adequate resources will be available in future years to meet those costs. Government economic planning should factor in future public service pension costs, just as it does future Social Welfare, education, and health care requirements. Proper management of the economy should ensure that economic growth is sufficient to meet those costs. For example, the use of budget surpluses now to reduce the national debt would bring about savings in interest payments which would be available in future years to meet part of the increased cost of pensions.

23.2.15 **Budgetary system:** Pay-as-you-go is in keeping with the Government's budgetary system generally: arguably, it is not appropriate for government to seek to apply resources available today — whether through taxation, borrowing, sale of state assets, or use of budget surplus — to provide for pension costs which will occur at some future date. In addition, it might be asked why such an approach should be adopted for pensions but not for other liabilities which it is clear will arise in the future (e.g. for health care costs).

23.2.16 **Double payment by current generation:** The establishment of a pension fund would involve today's taxpayers having to contribute twice — to pay the pension costs which have arisen in the past as well as setting aside resources to pay future pension costs. This would run contrary to the intergenerational contract which is integral to pay-as-you-go systems: today's workforce meets the cost of past pensions on the promise that when they retire their own pensions will be paid for by the next generation of workers. Thus, the establishment of a pension fund would involve intergenerational transfers, at the expense particularly of today's generation of taxpayers.

23.2.17 **Limiting budget flexibility:** The move towards pension funding could significantly limit budget flexibility in future years. In the context of today's budget surpluses, a commitment of a certain percentage of pensionable pay may appear affordable. However, true pension funding is irrevocable and non-discretionary. Finding the contribution in circumstances where the public finances had returned to a deficit situation might necessitate cutbacks in other areas of government expenditure or increased taxation or borrowing.

23.2.18 Share out of resources: On a broader level, a pension fund would limit the scope of future governments in relation to the allocation of resources within society. Arguably, there are groups in society that have greater needs than pensioners, for example, young low income families with mortgages, education and other commitments, and those who are long-term unemployed or otherwise socially or economically disadvantaged. Pension funding, in that it would *lock away* resources for the benefit only of pensioners, would add greater weight to the claims of pensioners at the expense of the claims of all other groups, and could cause distortion in the equitable share out of resources within society.

23.2.19 High administrative charges: Compared with pay-as-you-go schemes, a typical large pension fund faces a complex regulatory environment and substantial administrative charges. The fund has to meet the transaction costs associated with its investment decisions, as well as pay fees for the services of investment advisors, investment managers (including domestic and foreign managers and specialist managers for particular sectors), property managers and advisers, actuaries, accountants, legal and tax advisors, custodians, etc. In addition, the regulatory environment for pension funds is complex, and funds have to address issues such as corporate governance, ethical investment, indemnification of trustees, etc. Generally speaking, State pay-as-you-go social security systems operate efficiently and at a very low cost, in terms of the expense to benefit ratio, whereas private sector schemes tend to have a higher expense to benefit ratio.[284]

23.2.20 Funding and investment: The argument that pension funds lead to an increase in real investment is a matter of debate amongst economists. There is no simple direct link between an increase in the flow of money into funded pensions and increased capital formation. The factors that determine the level of capital formation are many and disparate. Even the evidence that is most favourable to the view that funding pensions leads to additional capital formation suggests that it is a blunt and inefficient instrument to that end. Investment in pension funds can lead to disinvestment elsewhere in the economy. Thus, the conclusion must be that funding pensions schemes does not necessarily create additional resources that will significantly ease the cost of future pensions.

23.2.21 Investment mandate: The objectives of a pension fund are to maximise investment returns and to maintain a diversified portfolio of assets as a means of minimising risk. At the end of 1999, Irish pension funds' investments consisted of 40% Irish assets (21% Irish equities) and 60% foreign assets.[285] Funds expected that with implementation of the Euro, the portion of Irish equities in the portfolio would fall over time.[286] A State pension fund, if structured in the same way and having the same objectives as a private sector pension fund, would need to follow a broadly similar investment strategy; indeed, the Irish equity market would be unable to sustain any substantial new pension fund investment while maintaining existing levels of return. To the extent that a State pension fund would come under external pressure to invest in domestic

[284] Daykin, C., *Funding the Future? Problems in Reform* (Politeia, 1998), p. 25. A survey of funded pension schemes in Ireland for 1994 found that administrative costs amounted to 5% of total contributions (10.5% of total expenditures); the Department of Social Welfare estimated that the administrative costs of the Retirement Pension and the Old Age (Contributory) Pension ranged from 1% to 2% per cent of expenditures (Hughes, G., and Whelan, B.J., *Occupational and Personal Pension Coverage 1995*, ESRI 1996, pp. 109-110).

[285] IAPF, *Asset Allocation Survey* 1999 (May 2000).

[286] IAPF, *Investment Fund Survey* 1999, p. 10.

projects and firms selected otherwise than in accordance with normal pension fund investment objectives, this could result in reduced rates of return to the fund and so negate a primary argument for setting up the fund in the first place.

23.3 Cost of fully funding public service pensions

23.3.1 Having reviewed the arguments for and against funding, we now examine the cost implications for the State of introducing full funding of public service pensions.

23.3.2 If a formal public service pension fund were to be established along private sector lines, the initial annual contribution to the fund would be approximately 19% of pensionable pay, i.e. £780 million (€990 million) per annum at 1997 salary rates. This would be additional to current annual expenditure on pensions, i.e. £636 million (€807 million) in 1997, which is met on a pay-as-you-go basis. Over time, the funding rate would decline to 16% of pensionable pay, i.e. £650 million (€825 million) per annum at 1997 salary rates, as the proportion of public servants in full rather than modified PRSI class increased.[287]

23.3.3 In addition to this annual contribution, full funding along private sector lines would require the State to set aside funds to meet its accrued pension liabilities. As indicated in Section 6.5, the value in 1997 of the State's accrued liabilities in respect of public service pension schemes was of the order of £20 billion (€25.4 billion). For a public service pension fund to meet the full amount of those liabilities, the market value of its assets might have to be somewhat higher than that figure. The scale of the fund envisaged is made clear when we compare it with the market value of total Irish pension funds as at the end of 1997, which stood at just over £26 billion (€33 billion).

23.3.4 Of course, it would be possible to move to full funding on a phased basis. Thus, rather than having to find the £20 billion (€25.4 billion) and more necessary to meet the State's accrued pension liabilities, funding could be introduced for new entrants only or for the future service of current public servants. With the former, the amount of the State's annual contribution to the fund in the first few years would be quite low, building up as the number of new entrants increased. Under the latter, funding for future service, the contribution rates would be as indicated in Paragraph 23.3.2 .

23.3.5 A difficulty with both scenarios is that the fund in each case would be of little value in reducing the State's expenditures on public service pensions during the period of the expected peak in pension costs, i.e. the years 2017-2032. This is because the State would continue to be required to pay a major proportion of its pension costs on a pay-as-you-go basis, with the contribution to the fund being additional to those costs. While payments by the fund would bring about a reduction in the State's pay-as-you-go expenditure over time, the *break-even* point (i.e. the date at which the State's contribution to the fund plus pay-as-you-go expenditure would be lower than its existing projected pay-as-you-go expenditure on pensions) would occur later than this period.

23.4 Full v. partial funding

23.4.1 The Commission has given careful consideration to the question of whether or not the State should fully fund public service occupational pension schemes along private sector lines. We have weighed the arguments in favour of funding and pay-as-you-go, and examined the cost implications for the State of a move to full funding. On balance, while we favour making some

[287] Department of Finance, "Report of the Budget Strategy for Ageing Group" (July 1999), Paragraph 8.2.2.

advance provision for future public service pension costs (see below), **we recommend against the full scale funding of public service pensions** for the following reasons:

- pension funds in the private sector are based on the requirement to provide security of benefits to pension scheme members. This consideration is not a major factor in the public service, where the State is the ultimate guarantor of benefits;
- taken in isolation, the economic arguments in favour of funding are not conclusive. In addition, many of the arguments in relation to the lack of cost transparency under pay-as-you-go are capable of being addressed through the introduction of appropriate changes to government financial management systems;
- as we have shown, the cost of establishing a full fund would be substantial. A commitment to full funding would have to be placed side by side with the Government's other long-term commitments and goals, including its existing pre-funding initiative for Social Welfare and public service pensions, and expected future demands in respect of health-care costs, investment in infrastructure, etc.;
- a major consideration must be the need to address the expected peak in pension costs which will occur in the next fifteen to thirty years. Full funding would, in fact, exacerbate the position;
- the Government's Budgetary Strategy for Ageing Group, which investigated, inter alia, the long-term effect on the national finances of various pension funding options, concluded that the enormity of the extra cost involved would rule out the full funding of public service pensions.[288]

23.4.2 However, while we have ruled out full funding, we consider that there are strong arguments in favour of **adopting a mixed financing approach whereby part of the State's liabilities for public service pensions would be met on a funded basis** with the balance, perhaps the most significant part, being met on a pay-as-you-go basis. We outline these arguments below.

23.4.3 Firstly, partial funding would bring much improved transparency and discipline into pension costs. With the existing pay-as-you-go approach, benefits, not costs, tend to become the main focus of attention. In a funded system, the contribution rates would bring home to public servants the value of their pension entitlements and the costs of improving them, while the State, too, would become more conscious of the real cost of recruitment. Reforms to financial management systems would assist in ensuring transparency in pension costs, but might be seen as artificial, depending on how they were implemented. In that context, partial funding would represent a clear and effective means of introducing improved discipline into public service pension costs, and would strengthen the management of pension costs and liabilities into the future.

23.4.4 Secondly, the establishment of a partial fund for public service pensions would have the advantage of helping to smooth the pensions bill in the future, thereby averting destabilising shifts in future government taxation/spending patterns. In addition, it would ensure diversification of state expenditure at a time when the economy is at or near full employment and revenue is buoyant.

23.4.5 Thirdly, partial funding would help minimise the risk resulting from a too heavy reliance on pay-as-you-go as the basis for financing future pension costs. A balanced approach to financing state pension costs, involving the introduction of part funding where pay-as-you-go is the only approach currently applying, has been put forward by a number of international organisations as

[288] Department of Finance, "Report of the Budget Strategy for Ageing Group" (July 1999), Paragraph 8.2.2.

part of a strategy to tackle the challenges of ageing.[289] Consistent with this approach, the Pensions Board recommended the establishment of a fund for Social Welfare pensions as a means of securing the sustainability of the national pensions system; the fund would achieve this by levelling the financing burden over time thereby avoiding the otherwise significant strains which would be likely to occur over the decades ahead.[290]

23.4.6 Our conclusion is that full funding is not practical, necessary, or advantageous. However, the case for establishing a partial public service pension fund is convincing, primarily as a means of ensuring improved transparency and discipline in public service pension costs, smoothing the expected peak in the pensions bill, and bringing a balanced approach into the long-term financing of pension costs. The next step is to consider what form this partial funding should take.

23.5 Objectives of a partial pension fund

23.5.1 In this Section, we develop a set of objectives which we believe a public service pension fund should be capable of meeting. In summary, these are as follows:

Objective 1: insofar as possible, the fund should be capable of addressing the expected **peak in pension costs** in a flexible way that is consistent with the Government's long-term planning for the effects of demographic ageing generally;

Objective 2: in order to fully realise the economic benefits of funding, the fund should be structured so as to **maximise investment returns**;

Objective 3: the **discipline and integrity** of the fund should be secured as regards contributions, investment returns, and payments from the fund in respect of future pension costs;

Objective 4: pension funding should be **integrated** into the public service pensions framework and be capable of adjustment to meet future changes in that framework.

23.5.2 In considering how these objectives can be met, we need to address what type of fund for public service pensions should be established, i.e. a true *pension fund* or a *budgetary reserve fund*. We discuss both approaches below.

23.5.3 We note that the Government's pre-funding initiative relates to both Social Welfare and public service pensions, and that it is proposed in the National Pensions Reserve Fund Bill to establish a single reserve fund in respect of both sets of liabilities. We also note that the Minister for Finance has indicated that provision could be made for a separate fund for public service pensions if agreement were to be reached on this between the relevant parties (see Paragraph 23.1.7).

23.5.4 In our view, public service occupational pension schemes are more broadly comparable to occupational pension schemes in the private sector than to the Social Welfare system, notwithstanding the role of government as the ultimate source of finance for both.[291] We consider that the specific nature of occupational pension schemes derives from the industrial relations arena in which occupational pension issues are determined and from the property right claim which occupational pension scheme members — including public servants — have upon their

[289] See, for example, summary of actions proposed by the World Bank, IMF, OECD and G10 in European Commission Directorate General II Economic and Financial Affairs, *Ageing populations: the long-term sustainability of public finances in the EU and some microeconomic issues,* Issue paper for the Economic Policy Committee (30 April 1999), Annex 3.
[290] The Pensions Board, *Securing Retirement Income*, 1998, p. 112.
[291] We discuss this point further at Paragraphs 23.5.37-23.5.40 below, and at Paragraphs 4.4.3-4.4.4.

pension entitlements. Thus, we would suggest that different funding considerations should apply to public service and to Social Welfare pensions, reflecting the different nature of the respective pension commitments under both systems.

23.5.5 At this point, it is useful to examine briefly the main features of a pension fund approach and of a budgetary reserve fund approach to pre-funding pensions.

23.5.6 **Pension Funds** are a recognised financing method used in many countries to meet the costs of the occupational pension schemes of companies in the private sector, including the commercial state sector and, in some countries, of the occupational pension schemes of certain public service groups and organisations. A pension fund for a defined benefit occupational pension scheme normally involves the following:

- it is established under trust separate from and independent of the employer. The trustees of the fund are required to ensure that the fund is adequate to meet the future benefit promise;
- the scheme is funded on a *balance of cost basis*. This means that the members usually pay a fixed periodic contribution, often a certain percentage of pensionable salary,[292] and the employer contributes the balance determined by the scheme actuary as necessary to provide for the benefits promised under the scheme;
- the trustees are required to invest the fund in a prudent manner in a portfolio of assets, including equities, government gilts, and property, both domestic and foreign;
- at the date of each regular actuarial valuation, the scheme actuary must be in a position to certify that the fund assets at that date are sufficient to meet the accrued pension liabilities in respect of serving staff, pensioners, and deferred pensioners, on the assumption that the fund is to be wound up;
- the employer has no discretion to interfere with the operation of the fund.

23.5.7 Pension funds are normally subject to detailed government regulation. Generally, this has the aim of safeguarding the entitlements of pension scheme members, as well as limiting and controlling the extent of the tax relief often provided to pension funds as a means of encouraging pension savings. In Ireland, pension funds are regulated under the Pensions Act, 1990 and are usually subject to approval by the Revenue Commissioners under the Finance Act, 1972.

23.5.8 In the context of the State and its budgetary procedures, an alternative means available to it to provide for future liabilities and/or to apply existing financial surpluses or windfall receipts is the establishment of a **Budgetary Reserve Fund** (or a *buffer fund*). Such a fund could be used to supplement the pay-as-you-go system so as to smooth expected peaks in pensions expenditure and/or to moderate the effects of long-term increases in the pensions bill on the national finances. While there are no *hard and fast* rules, a reserve fund might have the following features:

- it could be established as temporary in nature, to be built up in time of financial prosperity with the aim of smoothing costs over a longer-term period;
- government could decide from time to time how much to contribute to the fund, and establish broad investment parameters for the fund (independent trustees could be appointed to oversee implementation of the investment mandate);

[292] Some pension schemes do not require an employee contribution. In Paragraph 8.9.3, we note that almost one-third of schemes in large private sector firms in Ireland do not require a direct contribution to the pension fund from the members.

- the arrangements for making expenditures from the fund would probably be established in advance;
- the fund would be considered as part of government resources, whether or not it was managed at arm's length by an independent body.[293]

23.5.9 We now consider the four objectives for a public service pension fund identified in Paragraph 23.5.1, and examine how effectively each is capable of being addressed under a pension fund and a budgetary reserve fund approach.

Objective 1: addressing the peak in pension costs

23.5.10 As outlined in Chapter 6, public service pension costs are expected to quadruple in constant (1997) price terms over the next thirty years from £636 million (€807 million) per annum in 1997 to £2.4 billion (€3 billion) per annum in 2027. In GNP terms, expenditure is projected to grow from 1.6% of GNP in 1997 to a peak of 2.4% of GNP in around 30 years' time, before falling back to about 1.8% of GNP in around 45 year's time.

23.5.11 If the only objective of the Public Service Pension Fund were to meet the peak in pension costs, the ideal fund would have the characteristics of a budgetary reserve. The fund could be built up during the period in which annual pensions expenditures were less than, say, 2% of GNP, and drawn down thereafter in order to cap total expenditures at 2% of GNP during the period of the peak.

23.5.12 In the current budgetary environment, it would be desirable that any funding proposal enable the State to contribute to the fund a portion of the annual budget surplus as well as windfall receipts arising, for example, from privatisation. This would enable the State to draw resources from the fund in later years in order to reduce the cost pressures arising from the effects of demographic ageing.

23.5.13 Our understanding, based on the "Report of the Budget Strategy for Ageing Group", is that funding for future pension costs along these lines would be relatively straightforward if the Government's budgetary position were measured by reference to the traditional Exchequer Borrowing Requirement (EBR). However, difficulties arise when the wider General Government Balance (GGB) is considered.

23.5.14 Under the EU *Stability and Growth Pact*, budget positions must not exceed a deficit of 3% of GNP. The relevant measure under the European System of Accounts is not the EBR but the GGB, which has a wider definition than the former. Under the GGB approach, only transactions between government and non-government sectors count.

23.5.15 Thus, it would appear that if a fund for public service pensions were established as part of a Government reserve fund, payments into the fund when made would not be treated as expenditure in calculating the GGB and so would not reduce the present GGB surplus; and later withdrawals to meet pension costs, when made, would not be regarded as receipts and so would not improve the GGB at that time.

23.5.16 Accordingly, a fund of this nature would not make any *direct* contribution to protecting the future GGB position. It would, however, have a beneficial effect on the longer-run GGB to the extent that allocating resources to such a fund would constrain other expenditure in the nearer term.

[293] The National Pensions Reserve Fund Bill, 2000 adopts a budgetary reserve fund approach to meeting future pension liabilities of the State. Generally, the provisions of the fund envisaged in the Bill incorporate the features which we identify in this Paragraph.

23.5.17 On the other hand, provided a public service pension fund were properly structured, the State's contributions to it should count as expenditure for purposes of calculating Ireland's GGB, while the future use of the accumulated resources of the fund to meet the public service pension costs for which it was established would directly assist the GGB.

23.5.18 For this type of fund to be successful from a GGB perspective, however, it must be a properly constituted pension fund operating under the normal conditions which apply to pension funds generally. For example, the obligation to make payments into the fund would have to be permanent, the level of contribution to the fund would be determined on an actuarial basis, there would have to be an independent investment mandate for the management of the resources of the fund, etc.[294] The logic behind this GGB approach appears rather opaque in this context but to change the technical interpretation at this stage would require concerted action by EU member governments.

23.5.19 In order to provide maximum budgetary flexibility, a fund of this nature should also be capable of handling the investment of amounts in addition to the actuarially determined contribution (for example, the lodgement of part of the proceeds of privatisation). We address this further in Section 23.7.

Objective 2: maximising investment returns

23.5.20 The reduction in the long-term cost of pensions which may be brought about by funding is marginal at best (we discuss this point at Paragraphs 23.2.9-23.2.10). To realise fully the economic benefits of establishing the fund, we consider that every effort should be made to maximise its investment return.

23.5.21 Were a definite timeframe envisaged for a partial fund, this might serve to limit to some extent its investment strategy by comparison with a private sector pension fund. For example, in the period prior to final drawdown and termination of the fund, it would probably be required to hold a larger balance in gilts and cash reserves at the expense of long-term equity holdings. This would have a negative impact on the investment returns to the fund. It might be noted that the US Social Security Trust Fund, which was established as a buffer or reserve fund to support social security pensions, is held exclusively in US government gilts, although there are proposals to expand its portfolio to include equities.

23.5.22 Under the Pensions Act, 1990, trustees of pension funds are required to ensure that proper investment of scheme assets takes place. This is generally taken to mean that trustees should adopt the *prudent person test,* i.e. they must exercise a high degree of diligence in making investment decisions, having regard to the liabilities of the scheme and the interests of the beneficiaries. This sets the context in which trustees make investment decisions.

23.5.23 Trustees will generally have regard to criteria of risk tolerance, diversification of investment portfolio, and return and liquidity of assets in making their investment decisions, taking into account the profile of the liabilities they are seeking to match.

23.5.24 Typically, the investment objective of trustees is to achieve a reasonable level of return compared to salary growth and, in doing this, to minimise the risk of any substantial loss that might make the scheme insolvent or lead to volatility in the contributions required from the employer and/or employees.

[294] Department of Finance, "Report of the Budget Strategy for Ageing Group" (1999), Paragraph 5.1.4.

23.5.25 Trustees will seek to maintain asset portfolios which are appropriately diversified across a range of asset types and within each market and, as far as possible, to minimise currency risk by investing in assets which will match the currency of their pension liability exposure. In an Irish context it has been argued that, against the background of a strong preference for equity investment, these objectives are difficult to reconcile.[295] However, with the advent of the Euro, pension funds now have the opportunity to invest, at no currency risk, in a wide range of assets in the markets of the other Euro participants. As noted at Paragraph 23.2.21, Irish pension funds now expect that the portion of Irish equities in their portfolios will fall over time. [296]

Objective 3: securing the discipline and integrity of the fund

23.5.26 Elsewhere, we have pointed to the advantages of pension funding in ensuring a disciplined approach to managing pension scheme costs and of recognising the impact of changes in pension scheme terms and coverage. We consider in Chapter 24 the introduction of accrual accounting for pension costs under government financial systems. In the context of the partial funding of public service pensions, it would be important that the funding recommendation would be capable of delivering improved pension cost discipline. Most importantly, the fund should be designed so as to counteract pressures which might arise at some future date to introduce benefit improvements that would not, in the absence of the fund, have been considered.

23.5.27 From the perspective of cost discipline, a certain value could be envisaged in establishing a partial pension fund which would finance a particular defined element or elements of public service pension benefits, with the contribution rate calculated on a strict actuarial basis. Under this approach, there would be a direct connection — through the contribution rate charged on employers and employees — between the funded benefit(s) and the overall state of the fund. The contribution rate would fall to be adjusted with each actuarial review and on any change in benefit rules and pension scheme coverage. While an employee contribution would not be a necessary requirement of such an arrangement, its inclusion would help to reinforce the cost discipline inherent in funding.

23.5.28 Under an accrual accounting approach to recording pension costs, departments/agencies, as well as employees, would be charged contribution rates in respect of the full package of benefit entitlements. It could be envisaged that one element of the contributions received might be passed on to a public service pension fund. Thus, through the combined *funded* and *unfunded* elements in the contribution, departments/agencies and employees would, in effect, be paying the full accruing pension costs of serving public servants in the same way as for a fully funded private sector scheme, even though public service pensions would only be partially funded. We illustrate a practical example of this arrangement in Paragraph 24.4.6.

23.5.29 The funding of a specific pension benefit in accordance with the normal actuarial approach in private sector schemes would *automatically* enforce a discipline as regards payments into the fund and withdrawals from it. Each department/agency (as well as public servants themselves) would be required to make contributions, with effect from the *vesting date*[297] of the fund, based on the full actuarial cost of the particular benefit for serving employees. Payments from the fund would arise in respect of the element of actual expenditure on pensions related to

[295] Deloitte & Touche, Peter Bacon & Associates, *The Scope for Increasing Investment Opportunities for Irish Pension Funds in the Economy of Ireland* (July 1996), pp. 17,18.

[296] IAPF, *Investment Fund Survey*, 1999, p. 10.

[297] In this context, the *vesting date* would mark the commencement of the pension fund's liability to meet the future cost of that portion of the funded pension benefit which was earned or accrued after the commencement date.

the benefit in question which was accrued after the vesting date of the fund. No other payments or withdrawals would arise.

23.5.30 In the period during the setting up of the fund, it would be possible for the Government to make *additional contributions* in respect of the past accrued pension liability for the particular benefit being funded, without compromising the strict actuarial basis of the fund. In practical terms, these contributions would have the effect of moving the vesting date of the fund to a date earlier than its actual establishment, and of making the benefit fully funded more quickly than would be the case if contributions were made for the accruing cost only. In this way, substantial fund assets could be accumulated at an early stage, with the result that the Government would be in a position to draw greater resources from the fund in the years of the peak in pension costs (this is illustrated in Section 23.7). As a further option, assuming budgetary resources permitted, the Government could decide to fund other pension benefits in addition to that selected at the outset.

23.5.31 In the past, funds established by previous governments were taken over by the Exchequer in times of financial difficulty. We consider that every step should be made at this stage to ensure that a similar outcome does not befall the Public Service Pension Fund. Adopting a sound actuarial approach to partial funding would be one such step.

23.5.32 We have noted the situation which developed in the 1980s in relation to the Dutch public service pension fund, the ABP, when successive governments cut contributions as a means of reducing public expenditure (see Paragraph 9.5.10). To prevent the possibility of this recurring, it was agreed with effect from 1996 that the fund should be made subject to the same minimum funding requirements as apply to pension funds in the private sector. This ensured that it was no longer possible for governments to cut back contributions as they had previously done.

23.5.33 A similar approach could be adopted for a public service pension fund. The fund could be made subject to the same requirements, including the minimum funding requirement, as apply to funded pension schemes under the Pensions Act (subject to appropriate modifications to recognise the special nature of the fund, for example, that only a specific benefit was to be funded). In addition, the fund could be made subject to the Revenue rules and granted tax relief as an exempt approved pension scheme under the Finance Act, 1972.

23.5.34 Both the fact that the purpose of a public service pension fund would be the financing of a specific benefit, and that the fund would operate in broadly the same way as pension funds in the private sector, should help ensure clarity about the contribution to and payments from the fund, as well as limiting the possibility that the fund could be called upon at a future date for a purpose other than that for which it was designed, for example, to finance a general improvement in pension benefits.

Objective 4: funding as part of an integrated set of recommendations

23.5.35 It would be a particular advantage if the structure and design of the partial fund were capable of being integrated into an overall package of recommendations on a new public service pensions framework, and were capable of adjustment to meet future changes to that framework. If configured in this way, the fund would contribute to the overall objective of securing the viability and stability of public service pensions over the long-term.

23.5.36 The pay-as-you-go approach to financing public service pensions sits comfortably with what might be called the *traditional view* of occupational pensions as extended earnings payments made at the discretion of the State. In the past, it was not considered that public servants earned or accrued their occupational pension by virtue of their public service employment and, accordingly, no pension liability was recorded in government financial systems. While many countries required serving public servants to contribute towards the cost of their pension, these contributions were not invested and pensions expenditure in respect of retired public servants and their dependants was viewed simply as a call to be met from the annual budget like the provision of any other state service. The fact that many countries do not pre-fund future public service pension costs reflects this traditional view of occupational pensions, at least in part.

23.5.37 However, occupational pensions in the public service and in the private sector have come increasingly to be regarded as deferred pay and as a property right. This *modern view* of pensions has, to a large degree, been adopted by domestic law (including the Pensions Act) and EU law. It is now considered that employees earn their occupational pension during the course of their employment, as if part of their pay were being withheld or deferred for later payment in the form of a pension. Thus, it is not generally possible for employers to seek to reduce accrued pension entitlements without obtaining the prior agreement of the individuals affected. The modern view of occupational pensions is reflected in the fact that in most employments pension terms are a matter for negotiation and agreement between unions and employers. This applies equally to the public service, notwithstanding the fact that pension terms are laid down in legislation.

23.5.38 The practical implications of the modern view of pensions are capable of being met under the pay-as-you-go approach. The establishment of a budgetary reserve fund for public service pensions — in effect, the continuation of pay-as-you-go under a different format — would not appear to present any particular complications in this regard. The fund would merely represent a new element in the Government's budgetary processes. However, employees, unions and pensioners, who might look to pension fund practice of private sector and commercial state companies, could have quite different expectations concerning the nature and purpose of the fund.

23.5.39 In contrast to the pay-as-you-go approach, a pension fund maintains a close connection between the benefits promised under the pension scheme and the financing of those benefits. The purpose of the fund is to meet the full actuarial cost of accrued benefits, and contribution rates are determined accordingly. The fund's primary investment mandate is to maximise returns so as to meet the benefit promise and to maintain contribution rates at a reasonable level. Employers, employees and pensioners have a shared interest in the fund and in ensuring that it remains solvent. In most cases, employees make a pension contribution. Employee and pensioner representatives may be present alongside the employer as trustees of the fund.

23.5.40 The combination of features in a pension funding environment means that employers and unions must consider the implications for the fund and for contribution rates of any proposed change in pension terms. Thus, in the context of the public service, the existence of a true pension fund might ensure a greater appreciation of cost discipline than has characterised the existing pay-as-you-go approach to date.

23.5.41 In funded private sector and commercial state company schemes, representatives of the pension scheme members are often included on the trustees of the fund. Regulations covering the nomination and appointment of member trustees have been drawn up under the Pensions Act. The case for inclusion of members' representatives on the trustees of a public service pension fund might be seen as strengthened if an explicit employee contribution were made to the fund. Member trustees might be perceived as strengthening the fund's independence and security over the long-term.

Criteria for a public service pension fund

23.5.42 In light of the above discussion, the Commission considers that in order to meet the funding objectives identified in Paragraph 23.5.1, the fund for public service pensions should have the following structure and features:

- a single partial pension fund for public service schemes as a whole, established under legislation, permanent in nature, and closely replicating private sector pension funding arrangements;
- fixed contribution system — fixed arrangements regarding the elements of pension costs to be funded. Fund to be made responsible for a set class of pension benefits with provision to be made for regular actuarial review;
- fund to be built up over the short-term through the injection of additional lump sum contributions so as to be of greater assistance in meeting the peak in pension costs in the period after 2017;
- fund to be subject to the Pensions Act provisions regarding minimum funding requirement, etc., and to qualify for favourable tax status as an exempt approved scheme under the 1972 Finance Act;
- independent trustees or board, with employer and member representatives, to be accountable to the Minister for Finance and to the Oireachtas for the carrying out of their powers and responsibilities in accordance with the relevant legislation, regulations and policy guidelines;
- investment mandate, appointment of investment manager(s), etc. to be at the discretion of the fund trustees or board, subject to the provisions laid down in legislation.

23.5.43 The Commission believes that it is feasible to recommend the establishment of a fund to meet the **future cost of public service pension increases** which would incorporate these structural requirements and meet the funding objectives identified.

23.6 Fund to provide for pension increases

23.6.1 Because pensions are increased in public service schemes in line with increases in the salaries of serving employees, as opposed to the practice of the best private sector schemes of increases in line with the Consumer Price Index (CPI), subject to an annual limit, a case can be made for a special financing arrangement to meet the costs involved. The case is strengthened if an explicit employee contribution is to be introduced to meet part of the cost of pay-related pension increases.

23.6.2 Part of the rationale behind the creation of pension funds is to provide security to pensioners and serving employees. An area of concern for both groups has been the question of pensions increase policy. In Chapter 16, the Commission recommends the continuation of pay-related pension increases into the future (on the basis of a public service earnings index), subject to the introduction of an additional 1% employee contribution towards the cost involved. The establishment of a public service pension fund to finance pay-related pension increases, to which the 1% contribution would be lodged, would be seen as providing pensioners and serving public servants with a greater level of assurance and security that this system of pension increases would be continued in the long-term.

23.6.3 We examine the cost implications of establishing a public service pension fund to provide for pension increases in the following Section. First, we consider the funding of pension increases in relation to future service. We then consider two alternative scenarios in which the Government would make additional lump sum contributions to the fund in respect of the past service liability for pension increases for serving staff. The application of lump sum contributions in this way would allow the Government, without compromising the actuarial basis of the pension fund, to build up fund assets during the years in which budgetary resources were available with the aim of drawing down additional resources from the fund in the years of the peak in public service pension costs.

23.6.4 In its Report, the Budget Strategy for Ageing Group noted that the Commission was carrying out an actuarial costing of the pre-funding of public service pension increases. The Group stated that it favoured the establishment of a fund on this basis, concluding as follows:

> *A decision to proceed with pre-funding of public service pension increases would have a number of advantages. The annual amounts needed are in line with what we see as being affordable* [see Section 23.7 below]. *Moreover, such a fund would meet the current requirements of the European System of Accounts. Even more important, it would allow flexibility to Government to also pay occasional lump sum amounts into the fund — either from the proceeds of privatisation or from unanticipated budget surpluses — in respect of past service in line with normal pension funding arrangements, with a view primarily to reducing the Exchequer burden of public service pensions over the longer term.*[298]

23.7 Modelling the funding of pension increases

23.7.1 The actuarial model used by the Commission's consultants to assess the impact on the public finances of funding pension increases is based on the commencement of the fund in 1997. This was necessary in order to be consistent with the base year used in the full actuarial review of public service pension scheme costs (see Chapter 6).[299] The model would have produced broadly similar results to those indicated had it been possible to assume a more recent commencement date.[300]

23.7.2 The fund examined provided for future increases to pensions in payment for public servants currently in service. The liability in respect of future increases can be broken down into two components: the accrued liability in respect of service completed; and the future service liability in respect of service yet to be given.

23.7.3 To illustrate the above, consider the example of a public servant who joined at age 20 and is now aged 45. He or she has accrued entitlements to future pension benefits in respect of the 25 years' completed service. These accrued pension benefits have attaching entitlements to increases in the course of payment when they become payable.

[298] Department of Finance, "Report of the Budget Strategy for Ageing Group" (July 1999), Paragraph 8.4.3.
[299] Commission on Public Service Pensions, "Further Actuarial Review of Impact of Changes to Pension Scheme Terms" (October 1999), Report prepared by Mercer Ltd.
[300] The Budget Strategy for Ageing Group prepared an estimate of the impact of funding pension increases assuming a fund vesting date of 1 January 2000.

23.7.4 Similarly, as this public servant completes service in the future, he or she will continue to accrue entitlement to pension benefits in respect of this additional service. These pension benefits in respect of future service will also have attaching entitlements to increases in the course of payment when they become payable.

23.7.5 In assessing the impact of establishing a fund on this basis, we need to address the following three questions:

- how big should such a fund be if it were to fully cover the accrued liability for increases to pensions in payment?
- what is the ongoing contribution rate required to meet the future service liabilities for increases to pensions in payment?
- if increases to pensions in payment for current public servants were met by this fund, what impact would this have on the State's actual benefit expenditure projections?

Methodology and assumptions

23.7.6 The same methodology and assumptions were used in the calculations as are set out in Chapter 6 for the actuarial valuation of public service pensions. It was necessary to make an additional assumption regarding future price inflation, as its absolute level affects the size of the fund required. It was assumed that future price inflation would be 2% per annum. In order to highlight the sensitivity of the results to this particular assumption, the impact of future price inflation of 3% per annum was calculated separately.

Accrued liability for pension increases

23.7.7 On the basis of the methodology and assumptions used, the accrued liability of the State in 1997 in respect of future increases to pensions in payment for serving public servants amounted to approximately £3.3 billion (€4.2 billion).

23.7.8 If all other assumptions remained unaltered and a future price inflation figure of 3% per annum rather than 2% per annum were used, the State's accrued liability would have amounted to approximately £3.9 billion (€5 billion).

23.7.9 It is important to note that the accrued liability figure of £3.3 billion (€4.2 billion) is the discounted present value of expected pension increase payments for serving public servants in respect of accrued service. If assets were set aside in a pension fund to meet this liability, a market value adjustment would be made in order to ensure consistency in the way that the assets and liabilities were valued. Depending on the state of the markets at the time of the fund's establishment, this could mean that the fund assets would have to be somewhat higher than the value of the accrued liabilities.

Ongoing contributions required to meet future service liabilities for increases to pensions in payment

23.7.10 A contribution rate was calculated that would spread the cost of the future service liabilities for increases to pensions in payment as a stable percentage of public servants' salaries over their future service if the underlying assumptions were borne out in practice. This rate is expressed as a percentage of gross salaries plus pensionable allowances.

23.7.11 Given the fact that new entrants' benefits are integrated with the State Social Insurance pension, the funding rate should decline over time as the proportion of public servants with integrated benefits increases.

23.7.12 It must be emphasised that this funding rate is sensitive to the methodology and assumptions underlying the calculations. What happens in practice where private sector funds exist is that actuarial valuations of the liabilities and assets of the fund are undertaken at three yearly intervals. The recommended ongoing funding rate is adjusted, as appropriate, at these valuations to take account of the actual financial and demographic experience of the fund.

23.7.13 Using the methodology outlined above, the funding required to meet future service liabilities for increases to pensions in payment is 5.1% of gross salaries plus pensionable allowances.[301] (In the projections below, it is assumed that the funding rate will decline uniformly over a 40 year period from 5.1% to 4% of pensionable pay.) Based on a figure for pensionable pay of approximately £4 billion (€5.1 billion), the annual contribution in 1997 would have been around £200 million (€250 million).

23.7.14 To illustrate the sensitivity of the above funding rate to the assumed rate of future price inflation, if an assumption of 3% per annum rather than 2% per annum had been used, the funding rate would be approximately 6.1% rather than 5.1%.

Impact of the fund on existing benefit expenditure projections

23.7.15 Following the establishment of the fund, the State would be liable to meet the contribution to the pension fund in respect of the future service liabilities for increases to pensions in payment.[302] (This would be additional to the normal pay-as-you-go cost.) To ascertain the overall impact of the fund on the State's cash outgoings, it is necessary to factor in the expenditure from the fund in respect of the cost of pension increases accruing after the date of establishment.

23.7.16 The impact of the fund would be negative for a number of years as the expenditure from the fund would be less than the annual contribution required. The break-even point would be reached around 2027; in that year the expenditure from the fund (i.e. the pension increases arising from service after 1997) would be greater than the State's contribution to the fund. After 2027, the difference between annual outflows from the fund and the annual contributions needed would gradually increase leading to a continuing improvement in the Government's financial position for a number of years.

23.7.17 However, the above scenario would not mark any progress in dealing with the peak in pension costs expected in the period 2017 onwards.

23.7.18 For this reason, we examined the impact on the fund of the State meeting part or all of the accrued liability of £3.3 billion (€4.2 billion) in respect of future increases to pensions in payment for serving public servants. Two scenarios are examined: initial capital payment in 1997 of (i) £2 billion (€2.5 billion) and (ii) £3.3 billion (€4.2 billion). A price inflation assumption of 2% per annum is made in the following projections.

[301] This contribution rate represents the full actuarial cost of the benefit in question; thus, it includes both the employer and employee contribution.

[302] For the purposes of the model, we have ignored the additional employee contribution towards the cost of pension increases. Including the employee contribution would have the effect of reducing slightly the projections for the new pay-as-you-go cost plus fund contributions.

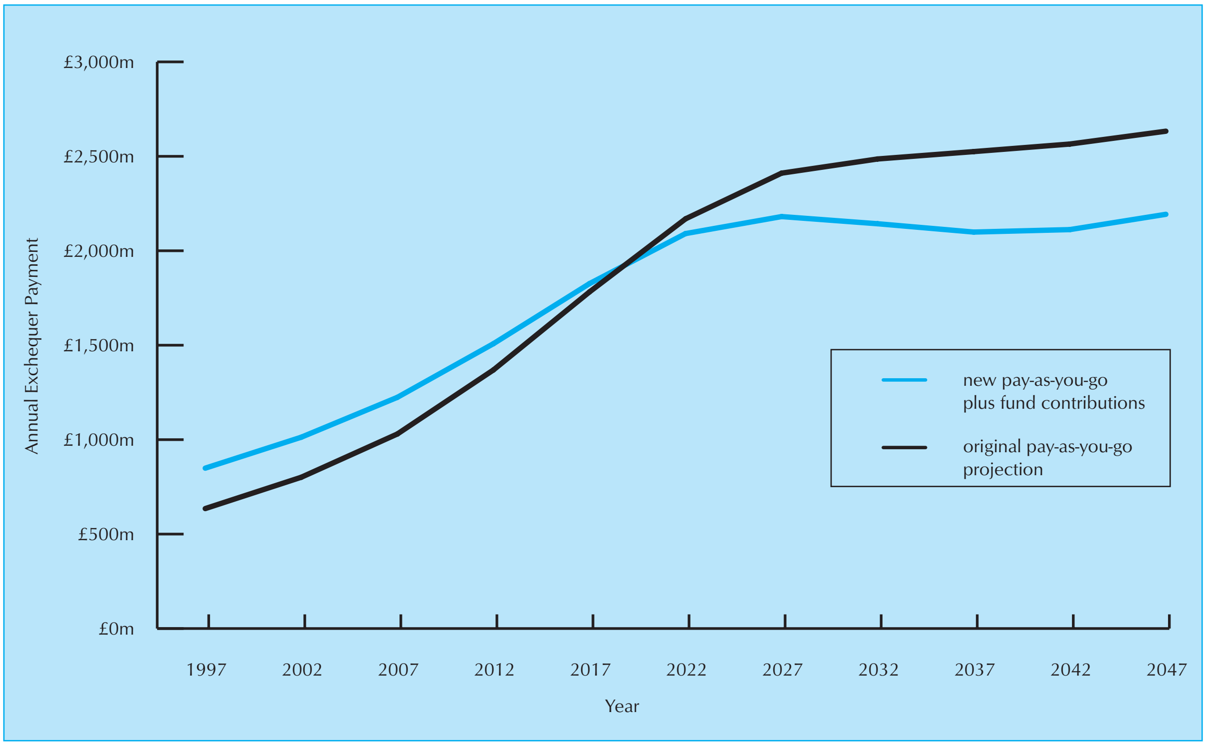
23.7.19 In Section 23.8 following, we examine how the financial implications of these funding scenarios compare with the cost of the pre-funding initiative announced by the Government in July 1999.

Scenario 1: initial contribution of £2 billion (€2.5 billion)

23.7.20 In this scenario, we assume that an initial State contribution of £2 billion (€2.5 billion) is made to the fund. Thus, the fund would meet 61% of the accrued liability for future increases to pensions in payment for serving public servants. The balance would be met on a pay-as-you-go basis.

23.7.21 Table 23.1 presents a comparison of the State's pension expenditure under the old and new arrangement. The original pay-as-you-go projection (see Table 6.3) is shown. A projection of the new pay-as-you-go figures plus the contributions required for the pension fund (from which pension increases will be met) is also shown. The new pay-as-you-go figures include only 39% of the cost of pension increases in respect of the past service of serving public servants, with no provision for future service. It is assumed for the purposes of the Table that the £2 billion (€2.5 billion) State contribution has already been met (i.e. it is not shown as part of the annual Exchequer payment in 1997).

Table 23.1: Comparative Exchequer position — initial fund £2 billion



23.7.22 The break-even point, at which the fund would begin to be of value in reducing the State's pension expenditure, is 2019. By 2032, the annual *saving* on the State's overall pension cost position would be of the order of £400 million (€500 million), in constant (1997) price terms.

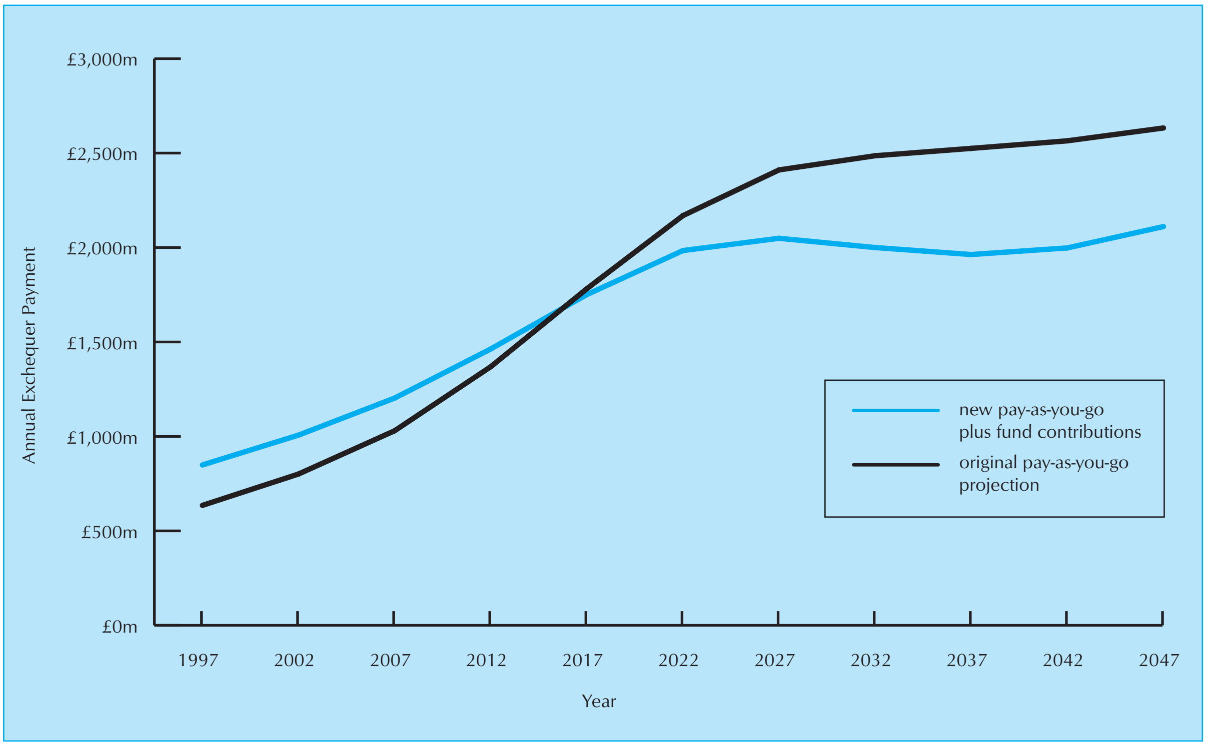
23.7.23 It is projected that in constant (1997) price terms the value of a public service pension fund established on this basis would be approximately £10 billion (€13 billion) in 2016 and almost £20 billion (€25 billion) by 2047.

Scenario 2: initial contribution of £3.3 billion (€4.2 billion)

23.7.24 Here we assume that the Government pays the full past service liability of £3.3 billion (€4.2 billion) into the fund. Under this scenario, the full cost of pension increases for all serving public servants and new entrants would be met from the fund. The cost of pension increases for pensioners would continue to be met on a pay-as-you-go basis.

23.7.25 Table 23.2 shows that the impact on the State's pension costs of this scenario are more pronounced than in the previous case. The break-even point is 2016, and by 2025, the annual *saving* on the State's overall pension cost position would be £300 million (€380 million), rising to over £500 million (€630 million) by 2035, in constant (1997) price terms.

Table 23.2: Comparative Exchequer position — initial fund £3.3 billion

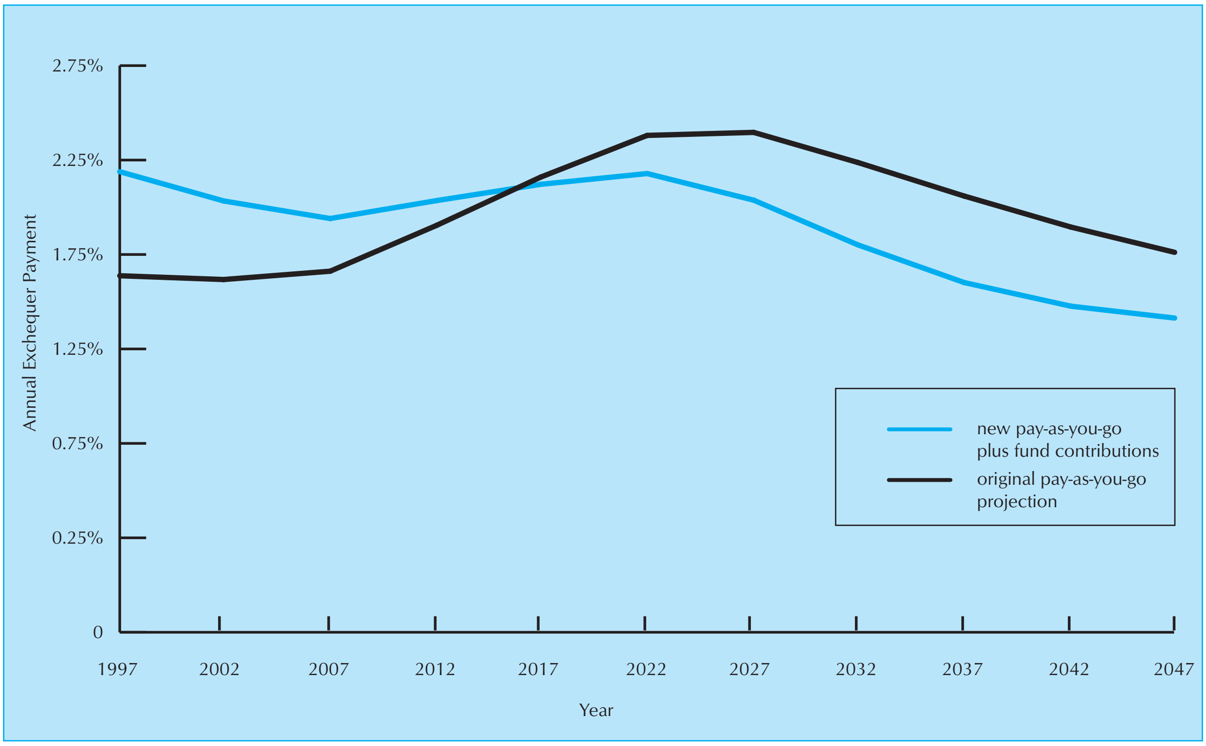


23.7.26 The value of the fund, in constant (1997) price terms, would reach approximately £10 billion (€13 billion) in 2012, and over £20 billion (€25 billion) by 2047.

23.7.27 The impact of the fund is more clearly demonstrated when projected pension costs are expressed as a percentage of GNP, as set out in Table 23.3. Growth in GNP is as assumed in Chapter 6 (see Table 6.1).

23.7.28 In 1997, expenditure on pensions under Scenario 2 would increase from 1.6% of GNP to 2.2% of GNP as a result of the additional contribution to the pension fund (excluding the cost of the £3.3 billion (€4.2 billion) payment). In the years of the expected peak in pension costs, 2017-2032, when expenditure is expected to reach 2.4% of GNP under the original projections, expenditure under Scenario 2 would be lower, not exceeding 2.2% of GNP in the peak period, and retaining a gap of about 0.3% of GNP over the period to 2047.

Table 23.3 — Comparative Exchequer position as % of GNP — initial fund £3.3 billion



23.8 Government's pensions pre-funding initiative

23.8.1 The Commission was concerned to ensure that the financial implications of our funding recommendation were broadly in line with what the Government decision of July 1999 had indicated was affordable over the long-term. Accordingly, we compared the scale of the financial commitment implied in the Government's pre-funding initiative — for public service pensions only — with the annual contribution and lump sum contributions indicated in Section 23.7 as necessary to pre-fund the future cost of public service pension increases.

23.8.2 Legislation enabling the establishment of a temporary holding fund for Social Welfare and public service pensions was passed in December 1999. This allowed the Government to commence funding on the basis of an annual allocation of 1% of GNP and to lodge part of the proceeds of the Telecom Éireann privatisation to meet future pension costs, in advance of making substantive legislation for the permanent, ongoing funding of Social Welfare and public service pensions.

23.8.3 A sum of £2.999 billion (€3.808 billion) was lodged to the temporary holding fund in 1999, made up of 1% of GNP, calculated at £582 million (€739 million), and £2.417 billion (€3.069 billion) from the proceeds of the Telecom privatisation. Provision has been made for a further sum of up to £1.85 billion (€2.35 billion) to be paid into the fund in 2000, of which about £650 million (€825 million) will be the 1% contribution and about £1.2 billion (€1.52 billion) will come from the sale of Telecom.[303] It is intended that these monies, which are managed by the National Treasury Management Agency, will be transferred to the National Pensions Reserve Fund once this is established under legislation.

[303] Reply to Parliamentary Question on 30 March 2000.

23.8.4 The Minister for Finance has indicated that the funding allocation between Social Welfare and public service pensions will be in the ratio two-to-one.[304] This allocation ratio is stated explicitly in the ''Report of the Budget Strategy for Ageing Group''. Applying the two-to-one ratio to the amounts paid, or to be paid, into the temporary holding fund in 1999 and 2000, would imply periodic and lump sum contributions for public service pensions as shown in Table 23.4.

Table 23.4: Implied funding contribution for public service pensions, 1999-2000

Contribution	1999		2000	
	Ir£	*Euro €*	Ir£	*Euro €*
1% of GNP per annum (1/3rd)	194	*246*	217	*276*
Lump sum	806	*1,023*	400	*508*

23.8.5 As stated in Paragraph 23.7.13, we estimate that the annual contribution needed to meet future pension increases is 5.1% of pensionable pay, and that this funding rate will fall uniformly to 4% over a 40-year period. Total pensionable pay in 1997 was calculated at £4 billion (€5 billion). We consider that the comparable figure in 2000 is closer to £5 billion (€6.3 billion), which means that the funding contribution for pension increases for that year would amount to approximately £250 million (€320 million). Assuming the additional 1% employee contribution towards the cost of pension increases was in place,[305] the net cost of the funding contribution to the State in 2000 would be approximately £210 million (€270 million).

23.8.6 The additional funding contribution which would be necessary to meet the accrued liability for pension increases in respect of serving staff was estimated at £3.3 billion (€4.2 billion) in 1997 (see Paragraph 23.7.7). It would be open to the Government to pay any or all of this liability by lump sum contribution over one or a number of years: the greater the lump sum contributions, the greater would be the benefit in terms of smoothing future pension costs. We show two scenarios above, based on lump sum contributions of £2 billion (€2.5 billion) and £3.3 billion (€4.2 billion), respectively.

23.8.7 As the figures indicate, the annual fund contribution implied for public service pensions — around £205 million (€260 million) per annum — is broadly similar to that envisaged under a pension fund for public service pension increases. The implied payment of additional lump sum contributions totalling £1.2 billion (€1.5 billion) to date would be consistent with the payment into a fund for pension increases of portion of the accrued liability for pension increases for serving staff. Thus, the effect of the Government's pre-funding initiative — in terms of its impact on the State's overall expenditure on pensions — would be broadly similar to that indicated in the pre-funding of pension increases. We estimate that in the longer term the periodic contributions envisaged under both approaches would be broadly of the same order.

23.8.8 In conclusion, the figures suggest that if a fund for pension increases were to be created, there would be no additional cost to the State in backdating the establishment of the fund to the beginning of 1999 and of reclassifying the Government's pre-funding payments to date accordingly.

[304] Dáil debate on second and subsequent stages of Temporary Holding Fund for Superannuation Liabilities Bill, 1999 (14 December 1999). It should be noted that the National Pensions Reserve Fund Bill gives no indication of the breakdown or allocation of the fund as between Social Welfare and public service pensions.

[305] In Paragraph 10.5.13, we indicated that an additional 1% contribution by serving employees would realise about £38 million (€48 million) per annum.

23.8.9 Of course, in considering the financial implications of a move to funding pension increases, it should be noted that drawdowns from the fund would occur immediately, rather than from the year 2025 as envisaged under the National Pensions Reserve Fund Bill. (However, the drawdowns would be relatively minor in the initial years, reflecting the very low portion of the liability for pension increases which was being carried by the fund.) Also, a pension fund to meet the cost of pension increases would be permanent in nature, while a reserve fund, in theory at least, would be of limited duration.

23.9 Conclusions and recommendations

23.9.1 The Commission is not convinced of the need to fully fund public service pensions in line with private sector practice. The basic reason for establishing a pension fund in the private sector — to provide security of benefits — does not apply in the public service, where the State is the ultimate guarantor of benefits. In addition, as we have shown, the economic arguments in favour of funding are less than conclusive. Finally, the introduction of full funding would do nothing to address the expected peak in public service pension costs and would limit, to an unreasonable extent, the budgetary flexibility available to future governments.

23.9.2 Nevertheless, we are aware of the major advantage of funding, particularly in bringing transparency into pension costs. With the existing pay-as-you-go approach, benefits, not costs, tend to become the main focus of attention. In a funded system, the contribution rates would bring home to public servants the value of their pension entitlements and the costs of improving them, while the State, too, would become more conscious of the real cost of recruitment. We make recommendations in the next Chapter on the introduction of greater transparency into pension costs under government financial systems. However, we would suggest that if public service pension costs were allowed escalate beyond existing projections, a move towards full funding might be deemed necessary as a more effective means of control.

23.9.3 The Commission sees definite advantages in the idea of partially funding future pension costs. We welcome the Government decision of July 1999 to pre-fund part of the future cost of Social Welfare and public service pensions. This initiative will help to smooth the pensions bill in the future, thereby averting destabilising shifts in future government taxation/spending patterns. In addition, it ensures diversification of state expenditure at a time when the economy is at or near full employment and revenue is buoyant. Finally, as we have argued, funding (whether full funding or part funding) represents an effective approach to ensuring greater transparency and discipline in the management of public service pension costs.

23.9.4 A partial fund for public service pensions could be structured as either part of a government budgetary reserve fund or a private sector type pension fund. The former would have the advantages of simplicity, ease of establishment, and lower cost of administration. The latter would have the advantages of integrity and cost discipline in a pension scheme context.

23.9.5 The type of fund selected would have implications for the ownership and management structure of the fund and, indeed, for the question of whether or not an employee contribution to the fund would be appropriate. A budgetary reserve fund would clearly form part of the public finances and, once established, it would be for the Government to decide on its deployment, subject to legislation. It is difficult to envisage on what basis an employee contribution might be sought for such a fund.

23.9.6 On the other hand, a public service pension fund could be seen as separate from government, being jointly secured by public service employers, serving public servants, and former public servants for the purposes of paying a particular pension scheme benefit. A direct employee contribution would reinforce the independence of the fund from government, in terms of its perception and in reality. In these circumstances, there would be a strong case for creating an independent Board of Trustees or Directors which would act in the same way as pension fund trustees in the private sector and would comprise employer, union and pensioner representatives.

23.9.7 In Chapter 16, we recommend that the existing policy of pay-related pension increases should be continued, subject to the making of an additional 1% contribution by public servants towards the cost involved. We also recommend that the contribution should be lodged, along with an employer contribution, to a new pension fund which would in due course be made responsible for meeting the total cost of pension increases.

23.9.8 Accordingly, we recommend that as part of the process of introducing the new 1% employee contribution, the public service pensions element in the proposed National Pensions Reserve Fund should be adapted to a separate properly constituted pension fund for pension increases, structured on the basis set out in Paragraph 23.5.42. As we have shown, the periodic and lump sum contributions for such a fund would be broadly of the same order as those implied for public service pensions under the Government's pre-funding initiative, while there would be a different profile of fund payments as between the two approaches, reflecting the different drawdown mechanisms involved.

CHAPTER 24

Transparency in Pension Costs and Liabilities

24.1 Introduction

24.1.1 The lack of transparency in public service pension costs has been a matter of concern to the Commission from an early stage in our deliberations. Prior to the establishment of the Commission, there was no clear picture in existence of the expected future cost profile of public service schemes, of the differences in benefit costs of the various public service groups, and of the State's total liability for the pensions of its serving and former employees. Furthermore, there were no agreed arrangements to enable account to be taken of the true cost of improvements in pension terms, to ascertain the cost of early retirement, and to estimate the long-term pension implications of extending pensions coverage and of recruiting additional staff.

24.1.2 In our Interim Report, we suggested that it was necessary to put in place a system which could clearly and quickly identify existing pension liabilities and the impact on those liabilities of increases in public service numbers and of improvements in pension terms. We added that the usefulness of regular actuarial reviews — which we recommended should be put in place — would be enhanced through the introduction of an accruals-based approach to pension costs within government financial management and accounting systems. We commented on the pilot accrual accounting project carried out by the Department of Transport, Energy and Communications (now Public Enterprise), and on the notional funding approach of a number of the unfunded public service schemes in the UK. We concluded that whatever approach was considered, it was important to ensure that there were mechanisms in place to identify pension costs, both immediate and emerging.

24.1.3 In this Chapter, we review the shortcomings in the cash-based approach to recording public service pension costs. We recommend the adoption of a new accounting framework with the objective of extending greater transparency into pension costs and liabilities. We are not in a position to recommend a detailed system of accounting for pension costs, as this must be done in the context of ongoing reform in government financial management systems under the Strategic Management Initiative. However, we would suggest that the framework for improved transparency in pension costs which we propose would facilitate better management of the continuing evolution of public service pension schemes, and would be consistent with the thrust of reforms under the financial management component of the Strategic Management Initiative.

24.2 Shortcomings in the existing cash-based approach

24.2.1 In Chapter 5, we consider the existing system of accounting for public service pensions. At present, payments made to pensioners — pensions, retirement lump sums, death gratuities, etc. — are recorded as expenditures in government financial statements, while pension contributions received from serving staff are recorded as income. Departments and other public service employers are not required to report the accruing cost of pensions for each year of operation, i.e. the costs which will arise at some future date in respect of the pension benefits earned by their employees during the year in question. In addition, no record is made of each employer's accrued liability for the pensions of its employees, nor of the State's total liability for public service pensions.

24.2.2 Section 5.4 details the shortcomings of the existing cash-based approach to accounting for public service pension costs:

- existing systems fail to highlight the long-term cost of pensions and of decisions which would have long-term pension cost implications, e.g. additional recruitment, improvements in pension terms, etc.;

  we have shown, for example, that the additional annual pension cost arising from recruitment to a range of public service grades is equivalent to 15%-20% of salary, and up to 30% of salary in the case of grades which have special pension terms for operational reasons (the new entrant rates are set out in Table 6.8);

- because they report only the current cash cost of pensions, they convey a false impression of the affordability of pension schemes and benefits;

  for example, pensions expenditure represents around 16% of pensionable pay at the present time. However, this is expected to increase to 38% of pensionable pay in 2027, before falling somewhat to around 30% in 2047 (see Paragraph 6.10.3);

- they fail to bring home to employers and employees the true cost of early retirement;

  we have shown that the capital cost of early retirement for a typical civil servant having 25 years' actual service at age 50, assuming the grant of 5 notional added years, would amount to 4.35 times his or her retiring salary (see Paragraph 10.4.13). The cost of early retirement on ill health grounds is only slightly less. We have shown also that the application to civil servants of the special terms which apply to the Garda Síochána would cause a doubling in the cost of civil service pensions (see Paragraphs 6.6.5-6.6.7);

- these deficiencies make it difficult to delegate responsibility to departments and agencies for important categories of management decision making in accordance with the modernisation of the public services under the Strategic Management Initiative;

- the failure to report the full cost of public service pension benefits impacts adversely on the value which employees place on those benefits;

  while public servants make pension contributions (both implicit and explicit), the corresponding, but larger, implicit contribution being made by the State towards the future cost of the pensions earned might not be appreciated;

- the lack of transparency in pension costs and accumulated liabilities is open to criticism by international organisations such as the IMF and the OECD;

  the State's accrued liability in respect of public service pension schemes in 1997 was estimated at approximately £20 billion (€25.4 billion) (see Paragraph 6.5.1).

24.2.3 We have suggested a number of actions to address these deficiencies (see Paragraph 5.4.4): regular actuarial reviews of public service schemes, actuarial valuations of the cost of proposed changes to scheme terms, and the recording of accruing pension costs under government financial management systems.

24.2.4 As regards the latter, an accruals-based approach to pension costs applies to the accounts of private sector and commercial state companies. The primary objective of the relevant accounting standard is to ensure that:

(i) financial statements reflect the assets and liabilities arising from an employer's retirement benefit obligations and any related funding, measured at fair value;

(ii) the operating costs of providing retirement benefits to employees are recognised in the accounting period(s) in which the benefits are earned by the employees, and the related financing costs and any other changes in value of the assets and liabilities are recognised in the accounting periods in which they arise; and

(iii) the financial statements contain adequate disclosure of the cost of providing retirement benefits and the related gains, losses, assets and liabilities.[306]

24.2.5 We believe that the introduction of an accruals-based approach to accounting for public service pensions, broadly along private sector lines, would offer a number of advantages. From the perspective of cost discipline, an accruals approach would ensure that the true cost of pensions would be charged to the accounts of the department or organisation which had primary responsibility for the delivery of a particular public service. It would foster an awareness of the medium- to long-term effects of additional recruitment, improvements in pension terms, and of early retirement. This would enhance the future management of pension schemes at a time of escalating costs. In addition, the employer contribution would more clearly indicate the *overall* cost and value of public service pensions to both employer and employees.

24.3 Implications of reforms in government financial management systems

24.3.1 We have considered the question of transparency in public service pension costs and liabilities against the backdrop of ongoing developments in government financial management systems. In this section we briefly review the relevant developments.

24.3.2 Predating the Strategic Management Initiative, there has been a move in government accounting systems away from simply recording compliance with spending limits to recording full costs and measuring achievement. In the Strategic Management Initiative process itself, public service financial management systems have been criticised as over-centralised, short-term in orientation, and more concerned with control of inputs than with efficient and effective delivery of outputs. This led to the Report of the Working Group on Financial Management, *Financial Management in a Reformed Public Service* (1999), which supported the delegation of financial authority to line departments, and the development of a *Generic Model* for an enhanced financial management system based on an accrual accounting approach to management accounting.

24.3.3 According to the Working Group, the essential features of the Generic Model will include:

- integrated standard accounting modules which will capture data on an accruals basis and will facilitate accruals and cash-based reporting (it will also be capable of recording all direct and indirect costs, including notional costs);
- the development of management accounting based on an accrual accounting approach, which will underpin and strengthen performance management and focus on results;

[306] Accounting Standards Board, *Financial Reporting Exposure Draft No. 20 Retirement Benefits* (November 1999), p. 13.

- changes in the presentation of the annual departmental Appropriation Accounts; and
- appropriate IT support for the Generic Model.

It is envisaged that implementation of the Generic Model will be done over a five year period.

24.3.4 A possible approach to accounting for public service pension costs on an accruals basis is the pilot project carried out by the Department of Transport, Energy and Communications (now Public Enterprise) over the period 1995-96 (see Paragraphs 5.4.8-5.4.10). The accounting policies adopted in producing financial statements under the pilot project, which is currently being evaluated as part of the roll-out of the Generic Model, were no different in most respects to those adopted by public limited companies. A notional charge for the accruing cost of pensions in respect of serving employees was recorded in the Department's Operational Statement, while the Department's estimated unfunded pensions liability was disclosed separately in a note to the financial statements.

24.3.5 The proposed framework for improved transparency in pension costs which we outline below is based generally on the approach to pension costs adopted in the pilot project. Without prejudice to the review of the pilot project mentioned above, it is, in our view, consistent with the reforms in government financial management systems which are currently in the course of development and implementation.

24.4 Proposed framework for improved transparency in pension costs

24.4.1 The Commission considers that the Generic Model for an enhanced financial management system, which is to be brought on stream over the next five years, should encompass the accounting for pension costs on a transparent basis.

24.4.2 While we are not in a position to recommend a detailed system of accounting for public service pension costs, we would suggest that the system embody the features set out below. The funding of pension increases which we recommend in Chapter 23 is a relevant consideration. A possible model for a new system of accounting for pension costs, consistent with this framework, is set out at Appendix 24.1.

24.4.3 Under the framework proposed, departments and public service employers should be required to include a charge in their annual accounts/operational statements for the accruing cost of pensions in respect of their serving employees. The charge would be based on rates broadly equivalent to the new entrant contribution rates (see Section 6.6). The inclusion of pension charges in this way would ensure that the annual accounts reflected the full cost, including the future pension cost, of each organisation's employees.

24.4.4 In order to arrive at appropriate contribution rates for the accruing cost of pensions, it would be necessary to use the concept of a notional pension fund.[307] Under this arrangement, employer and employee contributions would be credited to the notional fund, and investment return to the fund added each year. In valuing the notional assets of the fund, certain assumptions would be made about the balance of the portfolio held in different asset classes, investment

[307] The purpose of a notional fund is to enable the determination of the appropriate employer contribution rate. This rate can be updated every few years through an actuarial valuation of the notional fund, i.e. a comparison between the value of the assets and the value placed on the accrued liabilities at the date of the valuation. This enables the employer contribution rate to be adjusted upwards or downwards to reflect the changing position of the notional fund, thereby ensuring that it remains in equilibrium.

return, etc. In practice, the actual experience of the Public Service Pension Fund (see Chapter 23) would be a useful guide in the selection of assumptions.

24.4.5 It would appear that experience to date of the benefits of introducing accruals information into departmental financial statements has been mixed. Despite the costs involved, in resource terms and technology, it has been suggested there is no *ownership* of the information produced; it has been seen as an external requirement which has been imposed on departments.[308] For this reason, we would suggest that to make the charge for accruing pension costs as meaningful as possible, it should require an actual cash transaction, rather than being recorded simply as a notional charge.

24.4.6 In any event, assuming the Public Service Pension Fund is established in accordance with our recommendations in Chapter 23, the contribution for pension increases – which is to include both an employer and an employee contribution – would require actual payments to the fund. Thus, as noted in Paragraph 23.5.28, we would envisage that the accruing cost of pensions would be made up of two components, the *funded* element (i.e. pension increases) and the *unfunded* element (i.e. the balance of benefits payable under the scheme). Taking the example of a civil servant, and assuming a total charge for the accruing cost of pensions of 16% of pensionable pay and allowances, which includes a contribution for pension increases of 5.1%, the breakdown of accruing pension costs would be as follows:

Table 24.1: Example of annual charge (funded and unfunded element) for the accruing pension cost of serving public servants

Annual accruing pension cost	% of remuneration
Charge for pension increases, to be paid to the Pension Fund	5.1%
Accruing cost of unfunded element	10.9%
Total charge for pensions earned in year	16.0%

In this example, we have not broken down the contributions into the separate employee and employer components.

24.4.7 The rates charged for accruing pension costs should be linked to the actuarial review of public service pension schemes and of the Public Service Pension Fund, which should be carried out on a regular basis, ideally, every three years.

24.4.8 For departments and public service employers which pay pension benefits direct from their own resources, the aim should be to recognise the accruing cost of providing those benefits, rather than the actual pay-as-you-go cost.

24.4.9 Departments and public service employers should be required to disclose the estimated unfunded pensions liability for their staff separately in a note to the financial statements.

24.4.10 Financial statements should be prepared annually by each public service pension scheme and appended to the annual report of the scheme. As provided for in the Pensions Act, 1990, the availability of the annual report and financial statement should be brought to the attention of all public servants who are members of the scheme.

[308] Department of Finance, Financial Management Working Group, "Role of Accrual Accounting in the Generic Model" (6 November 1997), p. 5.

24.4.11 In order to enhance the visibility of accruing public service pension costs, it would be appropriate if a statement on the cost of the pension earned in the previous year were included in the annual statement of pension entitlements issued to each individual public servant (see Paragraph 25.5.6).

24.4.12 In future, any proposed changes to pension terms should be actuarially costed, and agreement should be reached between public service employers and unions about how any additional cost, in terms of an increase in contribution rates, should be met. The costings should be prepared by the Public Service Pensions Office (see Paragraph 25.4.11), in a form agreed by both management and unions.

24.5 Practical implications of improved transparency in the accounting for pension costs

24.5.1 In this Section, we set out briefly what we consider would be the practical implications of implementing transparency in accounting for pension costs along the lines envisaged above. We address three headings — recruitment, early retirement and remuneration. Of course, we cannot be sure about the detail of how the new accounting system for pensions would be implemented, and what variation there might be in the manner of its implementation across the different parts of the public service, particularly, as between centralised areas, such as the civil service, Garda Síochána, Defence Forces, and much of the education sector, on the one hand, and decentralised areas, such as the local authorities, health service, and universities, on the other. We believe that it is essential that the design of the new system should take account of relevant developments in relation to financial management systems in the various parts of the public service.

Recruitment

24.5.2 Under the new system, a decision to recruit new employees would mean finding the resources necessary to meet not just the additional salary and employer PRSI costs associated with the additional staff but also the employer contribution towards the accruing cost of pension. This would help to ensure that the pension implications of additional recruitment — which has been a major impact on long-term pension costs (see Section 6.9) — was factored into the recruitment decision. It would also ensure that the true cost of the delivery of improved public services was recognised by management, politicians and taxpayers.

Early retirement

24.5.3 It is a stated goal of the Strategic Management Initiative to devolve authority and accountability with the goal of achieving results and improving performance. Part of this process will likely involve a greater input by local managers in the deployment of staff resources, subject to implementation of appropriate accountability arrangements. In the context of early retirement (organisational restructuring, excess staff numbers, or Approved Early Retirement under Paragraph 15.15.21), accountability could be achieved by requiring the relevant department or organisation to meet the additional capital cost involved from within their own resources. Obviously, the operation of such an arrangement would need to be examined in detail before it could be introduced.

Remuneration and pensions package

24.5.4 Under the proposed accounting framework for pension costs, departments and organisations would pay the accruing cost of pensions for their serving employees. Thus, the remuneration package of each group of public servants would include in a transparent way not only the pay and employer PRSI cost but also the pension cost carried by the employer. This arrangement would help make the pension cost clear to both employers and employees.

24.5.5 We would envisage that the inclusion of the accruing cost of pensions in employer costs would give greater scope to employers and unions to address the wider package of pay and pensions, and ensure, where relevant, that the pension implications of any proposed changes were taken into account (through increased employer and/or employee contribution rates). In certain cases, a change in pension arrangements – such as making a new allowance pensionable – would involve a past service liability, and arrangements would need to be agreed on how this liability would be met.

24.6 Conclusions and recommendations

24.6.1 At present, because they are financed on a pay-as-you-go rather than a funded basis, public service pension costs are recognised in government accounting systems only when the pension benefits ultimately become payable, thereby disregarding the accruing cost of pensions for serving employees. Decisions about the recruitment of employees, improving benefit terms, making new allowances pensionable, extending pensions coverage, as well as early retirement, have obvious pension cost implications but, usually, the full extent of these costs will only impact at some future point. Often, the department or agency which gives rise to the additional pension cost is different to that which must meet that cost in due course. Thus, as the pension cost does not affect its bottom line there is little incentive for the employer concerned to manage and control the increase in costs.

24.6.2 In order to address these deficiencies, the Commission recommends the adoption of an accruals-based approach to accounting for pension costs under government financial systems. We recommend that implementation of accrual accounting for pension costs should take account of the framework proposed by the Commission (see Section 24.4) and be addressed in the context of ongoing reforms to government financial management systems.

24.6.3 Accrual accounting would help to make pension costs more fully transparent and would bring to bear some of the disciplines associated with funded pension schemes. In practical terms, it could enable departments and agencies to be given greater flexibility to make decisions having long-term pension implications, on the basis that the costs involved would be met from within their own resources. For example, the recruitment of new employees would mean having to pay for the accruing cost of their pension benefits as well as salary and PRSI costs; the cost of granting a pensionable allowance to an individual would include the consequent cost of pensioning the allowance.

24.6.4 The Commission also recommends that in future negotiations on changes to pension terms for any public service group or for the public service as a whole, actuarial costings of the proposed changes, specifically, the impact on contribution rates, should be obtained from the Public Service Pensions Office (see Paragraph 25.4.11). It would then be a matter for management and unions to agree how the increase in contribution rates would be apportioned as between employers and employees.

24.6.5 We recommend that actuarial reviews of public service pension schemes and of the Public Service Pension Fund should be carried out on a regular basis, ideally, every three years.

APPENDIX 24.1

Suggested system of accrual accounting for public service pension costs

The system of accounting for public service pension costs suggested by the Commission is as follows:

(i) a new charge, entitled the *Accruing Pension Liability Charge* (APLC), would be payable by all departments and bodies employing personnel who are pensionable under public service pension schemes. The payment would be in respect of the employer's share of the actuarially-calculated cost of pension provision for future service of existing staff in the department or body, including the cost of pension increases (which would be pre-funded — see Chapter 23);

(ii) the APLC rates, expressed as a percentage of pensionable pay, would be calculated on an actuarial basis on a grade or salary banded approach. They would be reduced by the explicit contribution being made by serving employees towards the cost of their pensions, e.g. the employee contribution of $1\frac{1}{2}$% for the spouses' and children's scheme would be deducted from the total pension charge for a pre-April 1995 civil servant in modified PRSI class (currently about 20% of salary);

(iii) the APLCs would be subject to review every three years as part of the actuarial review of public service pension schemes (and of the fund for pension increases);

(iv) the APLCs and employee contributions collected by departments and agencies would be paid on a monthly or quarterly basis to a central Public Service Pensions Vote. From its annual income, the Vote would be responsible for meeting the full pay-as-you-go cost of all public service pensions, including the cost of pension increases (for which it would receive reimbursement from the Public Service Pension Fund);

(v) charges in respect of pension costs would be included as part of employee costs in the departmental operating cost statement (Appropriation Account) and the accounts of agencies covered by the APLC mechanism. The total charge for the year would be disclosed in a Staff Numbers and Costs note;

(vi) departments and agencies which pay APLCs would not show in their balance sheets the corresponding total pension liability in respect of their current employees, pensioners and deferred pensioners. Instead, this liability would be disclosed in the report of the actuary that formed a part of an overall pension scheme statement;

(vii) for departments and agencies which pay pension benefits direct from their own resources, the aim would be to recognise the accruing cost of providing those benefits, rather than the actual pay-as-you-go cost, which would in future be met by the Public Service Pensions Vote;

(viii) the Public Service Pensions Vote would operate in accordance with normal government financial procedures — thus, any projected shortfall in income would be met by voted estimate, and any balance on the Vote at year end would be surrendered to the Exchequer;

(ix) a separate public service pensions financial statement — paralleling those to be prepared by the Public Service Pension Fund — would be prepared and presented annually, separate from the Appropriation Accounts.

CHAPTER 25

Reforms to Management, Administration and Communication Systems

25.1 Introduction

25.1.1 The management, administration and communication of occupational pension schemes is a complex and technical area. In many of the larger funded private sector schemes, standards of service provision and administration are being continuously updated, driven by a range of factors such as the changing regulatory environment, developments in information technology, employee interest, and an increased emphasis on occupational pension as a valuable feature of employment. In some cases, pension schemes are outsourcing their administration functions.

25.1.2 Public service schemes have not experienced these same developments to any significant extent. One of the consequences of the pay-as-you-go system is a pensions administration system that is geared primarily towards the calculation and payment of pension, rather than the provision of management information on pension costs or the communication of benefit entitlements and scheme options to serving employees. This has had implications for the resourcing of pension administration units across the public service.

25.1.3 In this Chapter, we make recommendations on a new structure for the management and administration of public service pensions. We consider that the most important task to be addressed by the new structure is to plan the introduction of a new computerised pension system capable of linking pension data across all public service employments. Such a system would provide the management information required for pension costing as well as the data at individual level which is necessary for effective pension communication.

25.2 Overview of current arrangements

25.2.1 In Chapter 4, we discuss the existing arrangements for the management, administration and communication of public service pension schemes. We identify a number of deficiencies, as follows:

- **processing of pensions:** while pensions appear to be processed reasonably efficiently and effectively across all schemes, there are delays in relation to such matters as pension increases, transfer of service, etc.;
- **pension administration for serving public servants:** the recording of pensionable service is deficient, particularly in non-centralised parts of the public service and for atypical employees. Arrangements for the transfer of service between schemes are cumbersome with the lack of computerised pension systems a particular weakness;

- **scheme documentation:** in some parts of the public service, scheme documentation issued to serving staff and to new entrants is not kept fully up to date;
- **communication:** there is inadequate communication of benefits and of the pension choices available to individual public servants. In an environment in which public servants are being encouraged to take a more proactive interest in their pension entitlements, a new *active* approach to communication is necessary;
- **appeal system:** while most schemes allow a member to appeal the employer's determination of his or her pension entitlements, questions arise in relation to the effectiveness of the appeals process;
- **development of pension policy:** to an increasing degree, unfunded statutory occupational pension schemes in the public service are being treated for the purposes of Irish and EU law in the same way as private sector schemes, and are subject to much the same regulatory framework (other than in relation to funding). The range of issues affecting pension schemes has widened considerably while at the same time the complexity of scheme administration and the level of compliance required has increased. In these circumstances, a more centralised approach to pensions policy in the public service may be considered necessary. The existence of a large number of separate, independent pension schemes means that there is duplication of effort in amending pension terms affecting all schemes;
- **negotiation of pension terms:** the existence of different industrial relations structures creates a potential for changes in pension terms in one part of the public service to be implemented without full consideration being given to their possible impact on all other public service schemes.

25.3 New requirements for public service pensions management and administration arising from the Commission's Report

25.3.1 If implemented, the measures recommended by the Commission would impact upon all existing public service pension schemes. The most important recommendations would involve:

- amendments to pension schemes to incorporate the recommended changes to pension terms;
- the establishment of an independent Public Service Pension Fund for the purpose of meeting the cost of pension increases across all pension schemes;
- the development of a single Public Service Earnings Index for the determination of future rates of pension increases for all schemes;
- the adoption of a new, transparent approach to accounting for pension costs under government financial systems;
- a proactive approach to the communication of scheme benefits and options, involving the provision of better, more regular and more user-friendly information to all public servants; and
- the introduction of a public service wide additional voluntary contribution arrangement, known as SPEARS, to be marketed and administered by external providers.

25.3.2 The combination of additional responsibilities and functions arising from implementation of these recommendations, both at a global and a scheme-specific level, would place considerable strains on existing public service pensions management and administration systems. Accordingly, the question of how current resources might be strengthened and/or restructured to meet the anticipated demands must be considered.

25.3.3 We examined whether existing pension administration structures, assuming the commitment of additional resources, would be capable of dealing with the changed pensions environment. We concluded, however, that a reform of pension administration structures was necessary, specifically, a move to a more centralised approach. This conclusion was based on our belief that an integrated, central input would be needed to guarantee successful implementation of the measures recommended across all public service schemes and public service employers. Also, we considered that a centralised approach would ensure greater consistency in the administration of pensions, and that the future development of public service pensions policy would be more effectively coordinated.

25.3.4 We would not intend that the new centralised structure would eliminate the need for the input of those departments and organisations that are currently involved in the administration of public service pensions. We envisage that public service employers would have a major responsibility in ensuring that correct and updated data were recorded for all employees, that correct charges were applied for the accruing cost of pensions, and that pension entitlements were correctly established.

25.3.5 In addition to considering management and administration structures for public service pensions, we also examined whether replacement of the large number of separate pension schemes with a smaller number of schemes, or alternatively, the creation of a single public service pension scheme, would be of benefit to future management and administration.

25.3.6 The Commission noted that a 1965 report on UK public service pensions addressed this issue. Discussing the multiplicity of schemes then in existence, the report suggested three possible options:

- amalgamation of closely similar schemes;
- centralisation and mechanisation of the routine work of record-keeping in the main groups of schemes; and
- a single public sector scheme.

The report commented that any or all of these options would continue to allow for variations in pension terms amongst public service groups arising from differences in conditions of employment. Major changes in benefits would apply uniformly, again as at present, but with the difference that since they would not have to be negotiated separately for each scheme, they could be operated at the same time for everybody.[309] Notwithstanding the views expressed in this report, it would appear that no concrete action was taken to implement any of the options suggested.

25.3.7 In our view, there would be major advantages in amalgamating closely similar public service schemes or introducing a single occupational pension scheme to cover all public servants. For administrative convenience, the new scheme or schemes could be applied to new entrants, at least in the first instance.

[309] Rhodes, G., *Public Sector Pensions* (George Allen & Unwin Ltd.), 1965, p. 209.

25.3.8 The Commission recommends that the question of amalgamating closely similar public service schemes or of creating a single occupational pension scheme for all public servants should be examined as part of the implementation of new management and administration structures.

25.4 Proposed structure for management and administration of public service pension schemes

25.4.1 We recommend the introduction of a new centralised structure for the future management and administration of public service pensions. The structure would involve four groups or parties: the Minister for Finance, an Inter-Departmental Committee on Public Service Pensions, a Public Service Pensions Office and a number of Pension Support Units.

We envisage that the responsibilities of each would be as outlined in Appendix 25.1, and summarised below.

Minister for Finance

25.4.2 The Minister for Finance, through the Pensions Section of the Department, would maintain formal responsibility for overall coordination of public service pensions policy.

Inter-Departmental Committee

25.4.3 A new Inter-Departmental Committee would be established, chaired by the Department of Finance, to advise on policy matters such as the implications for public service pension schemes of new pensions legislation, judgements of the European Court of Justice, etc.

25.4.4 Given the importance of reforming pensions IT systems in the public service, we consider that the committee would have a role in ensuring that the strategy devised by the Public Service Pensions Office (PSPO) was being implemented (see Section 25.5).

25.4.5 Representatives of the public service unions and of the PSPO could be asked to join the Inter-Departmental Committee. The expanded committee might then exercise a general role in relation to staff side pension claims, as well as considering other proposals affecting public service pension arrangements. The expanded committee might be titled the *Public Service Pensions Partnership Committee*.

25.4.6 The objective of the Pensions Partnership Committee would be to ensure that the wider implications, including the long-term cost implications, for all public service pension schemes of a proposed change in pension terms in any one area of the public service were fully considered, and that the basic principles of the public service pensions framework were not compromised as a result of the change. It would not be intended that the Pensions Partnership Committee form part of the standard industrial relations machinery.

25.4.7 The Commission notes that under the *Programme for Prosperity and Fairness* (*PPF*), a Working Group of the public service unions, relevant Government Departments, and other appropriate bodies is to be established to advise on the implementation of the relevant Government decisions arising from our Report with a view to introducing, as quickly as possible, any proposed changes in public service pension arrangements, including those for low paid workers. The Commission hopes that through that process the full range of pension issues addressed by this Report can be dealt with. The Commission envisages that the Working Group should have completed its task by the expiration of the *PPF*.

25.4.8 The Commission recommends that all parties should agree to forward claims under consideration to the PSPO for costing. This would facilitate implementation of our recommendation at Paragraph 24.6.4.

25.4.9 The Commission considers that if a Public Service Pensions Partnership Committee were to be established along the lines set out in Paragraphs 25.4.5-25.4.6, it should not become effective until the *PPF Working Group* has completed its task.

Public Service Pensions Office

25.4.10 To deal with the complex range of practical, technical issues arising under the new public service pensions framework, we propose that a Public Service Pensions Office should be set up under the aegis of the Minister for Finance. This body would provide the relevant pensions, actuarial, legal, and IT expertise necessary for the efficient administration of public service pension schemes.

25.4.11 The PSPO would oversee the regular actuarial review of public service pensions, provide costings to management and unions of the effect of proposed changes to pension terms, prepare pension scheme documentation and booklets, liaise with SPEARS providers, etc.

25.4.12 The PSPO would be responsible for the development of a pensions IT/database strategy for the public service, and would work with the Pension Support Units to ensure its implementation. We envisage that the PSPO would also act as the independent executive to the Public Service Pension Fund, and could provide a similar service to the trustees/commissioners of SPEARS. The PSPO would work closely with the Pension Support Units attached to Government Departments. In due course, responsibility for the Pension Support Units might be assigned to the PSPO.

Pension Support Units

25.4.13 The existing pension administration sections in the Departments of Finance (civil service), Health and Children (health service employees), Education and Science (teachers and support staff), Justice, Equality and Law Reform (Garda Síochána), Defence (Defence Forces), and the various non-commercial state-sponsored bodies would become known as Pension Support Units. The Department of the Environment and Local Government has currently a policy, regulatory and an advisory role only in relation to the pensions of the local authorities. Rather than have separate Pension Support Units based in each of the local authorities, we would suggest that a central Unit in or under the aegis of that Department and responsible for the administration of the pensions of all local authorities would represent a more efficient and effective use of resources.

25.4.14 The Pension Support Units would be responsible for ensuring correct recording of data on the pension entitlements of serving public servants, the setting up of new pension cases, provision of scheme documentation and answering queries from individual public servants and pensioners. The Units, along with the PSPO, would implement the new pensions IT/database strategy developed by the PSPO.

25.4.15 We would envisage that additional resources would be required by all Departments to enable their Pension Support Units to carry out the full range of tasks envisaged.

25.4.16 As outlined above, the Commission believes that a move to a centrally coordinated information and management system is necessary to address the various deficiencies which we have identified. However, we would emphasise that local input and responsibility on the part of departments and organisations would be essential to ensure the success of the new system.

25.5 Information technology and scheme communication

25.5.1 In our view, the most pressing requirement is to plan the introduction of a computerised pensions administration system for the recording of pensionable service, pensionable pay and allowances, and other relevant pension data. The introduction of such a system would be necessary to ensure the accuracy of information on benefit entitlements communicated to individual employees. It would also be crucial in the introduction of greater transparency in the accounting for pension costs and in the establishment of the Public Service Pension Fund.

25.5.2 It would be essential that the system be capable of sharing data between the major public service employers. A single central database which could be regularly updated by the various Pension Support Units would be one possible approach. The new system should also be capable of catering for the greater flexibility in public service employment, particularly the wider prevalence of part-time and temporary employment, and the increasing range of options for job-sharing, work-sharing, term time, career breaks, etc.

25.5.3 The system would be operated across every public service employer. Its introduction would be a specialised task, requiring the coordination of the individual requirements of a range of departments and public service employers, including Health Boards, hospitals, local authorities, VECs, third level bodies, and non-commercial state-sponsored bodies.

25.5.4 The Commission recommends the development of a specialised, computerised pensions administration system, and that introduction of the new system should be overseen by the interdepartmental committee and implemented by the PSPO, with appropriate expert assistance.

25.5.5 We consider that the task of putting in place a system capable of meeting the needs of a modern, flexible and transparent pensions administration structure would be considerable. The accompanying costs for such a project would be sizeable, particularly if, as will almost certainly be the case, outside consultancy advice is required.

25.5.6 Consistent with our recommendations in relation to pension flexibility, we recommend the implementation of an active policy of pension scheme communication, involving the provision of user-friendly documentation, an annual statement of pension entitlements, and a statement of the options available to public servants to improve their overall level of benefits and to plan for their retirement (including information on SPEARS).

25.6 Appeals mechanism

25.6.1 We have discussed in Section 4.3 the arrangements which apply to appeals in relation to pension benefits. While most schemes have an appeal mechanism in place, questions arise as to their effectiveness, due to the fact that personnel who are involved in processing an appeal will often be those who advised on how to handle the case in the first instance.

25.6.2 The Commission considers that a more transparent and independent appeals system would be to the benefit of scheme administrators and aggrieved parties. We believe that the essential criteria of any appeals system would include:

- *accessibility:* simple instructions about how to make a complaint should be made available. This should clearly identify the designated complaint handlers and explain how they will operate;
- *independence:* complaints which have not been resolved by the original decision maker should be examined objectively by persons not involved with the original decisions or actions. The examination should have regard not only to the rules governing the scheme but also to considerations of equity and good administrative practice;
- *confidentiality:* all complaints should be treated in confidence;
- *effectiveness:* the appeals system should have the authority to address all the issues giving rise to the complaint. Where the examination finds that the fault lies with the public body, the system must have the power to provide appropriate redress;
- *flexibility:* where rules are necessary to ensure consistency, too much rigidity in the appeals system should be avoided and there should be a degree of discretion given to those involved in the system to adjust to changing needs.

25.6.3 We recommend the appointment of a suitably qualified individual — supported by an executive to be provided by the Minister for Finance — as an external ombudsman for public service pensions. Account should be taken of the existing remit of the Public Service Ombudsman in implementing this recommendation. In the event that a National Ombudsman for Pensions is appointed who it is intended should have a remit in relation to all pension schemes, consideration should be given to subsuming the functions of the ombudsman for public service pensions into those of the National Pensions Ombudsman.

25.7 Conclusions and summary of recommendations

25.7.1 In some parts of the public service, the pension scheme is small and is specific to a particular company or organisation; in others, it is a large *umbrella* type scheme applying to the sector as a whole. Thus, there are a large number of schemes and a wide range of organisations involved in different aspects of their administration. Notwithstanding the complexity of these structures, it would seem that on the basic requirement of any pension administration system — paying pensions in the correct amount and on time — public service pensions are administered reasonably efficiently and effectively across all parts of the public service.

25.7.2 However, there are deficiencies in the system, foremost among which is the recording of information and the absence of proactive communication of the pension scheme. The records held of employees' service are incomplete in many areas. The focus of pension administration and personnel sections has traditionally been the calculation of benefits at the point of retirement and on death-in-service. Insufficient effort is made to communicate benefit entitlements to employees during service, to appraise them of options to enhance their pension, and to open up retirement choice. In addition, scheme documentation is not kept up to date in some parts of the public service.

25.7.3 The fragmented structure of public service pensions, involving a large number of independent schemes, can present problems for the management and negotiation of pension terms. In addition, questions arise as to the effectiveness of the appeal mechanisms available under public service schemes.

25.7.4 From our examination of pension arrangements abroad, we note that a centralised approach to pensions management and administration features in a number of countries (see Appendix 9.5). We were particularly impressed with the professionalism of pensions administration in the ABP organisation in the Netherlands.

25.7.5 In summary, the Commission's recommendations on pension scheme management, administration and communications are as follows:

(i) the amalgamating of closely similar pension schemes or the creation of a single Public Service Pension Scheme to be examined (Paragraph 25.3.8);

(ii) the introduction of a centralised structure for the administration and management of public service pension schemes (Paragraph 25.4.1);

(iii) the full range of issues addressed in the Commission's Report to be dealt with by the Working Group to be established under the *PPF* (Paragraph 25.4.7);

(iv) all parties to agree to forward claims to the Public Service Pensions Office for costing (Paragraph 25.4.8);

(v) the development of a specialised, computerised pensions administration system (Paragraph 25.5.4);

(vi) the implementation of an active policy of pension scheme communication (Paragraph 25.5.6);

(vii) the appointment of an external ombudsman for public service pensions (Paragraph 25.6.3).

APPENDIX 25.1

Recommended structure for public service pensions management and administration

1. Minister for Finance

- role to be exercised by Pensions Section (Public Service Pensions), Department of Finance;
- responsible for overall public service pensions policy, as advised by the Inter-Departmental Committee on Public Service Pensions and, if established, the Public Service Pensions Partnership Committee (see below);
- the Public Service Pensions Office (PSPO) (see below) would be a separate, stand-alone office or unit attached to the Department.

2. Inter-Departmental Committee on Public Service Pensions

- comprising representatives of the Departments of Finance, Defence, Education and Science, Environment and Local Government, Health and Children, Justice, Equality and Law Reform; chaired by the Assistant Secretary in the Department of Finance who has responsibility for public service pensions policy;
- in certain circumstances, the committee could be expanded to include representatives of the public service unions and of the PSPO. The expanded committee, having the same Chairperson, could be known as the Public Service Pensions Partnership Committee;
- discusses overall policy strategy;
- considers and approves proposed changes in pension terms;
- coordinates integrated response on behalf of public service pension schemes (e.g. in relation to new pensions legislation);
- liaises with the trustees/commissioners of the Public Service Pension Fund on matters which affect the funding of pension increases;
- ensures implementation of the IT/database strategy developed by the PSPO.

3. Public Service Pensions Office

- established as a separate office or unit attached to the Department of Finance;
- has access to relevant professional expertise — actuarial, legal, pensions, and IT — either in-house or by consultancy;
- develops pensions IT/database strategy for the public service as a whole;
- provides central service (including training) to staff of Pension Support Units (see below);
- provides relevant technical expertise, e.g. in relation to interpretation of scheme rules, drafting amendments to schemes, etc.;
- supports the industrial relations process through the provision to both management and unions, on an independent basis, of actuarial costings and technical advice in relation to proposed changes in pension terms;

- oversees regular actuarial review of public service pensions and provides necessary costings and technical support for new approach to accounting for pension costs;
- provides independent executive support to the trustees/commissioners of the Public Service Pension Fund and, possibly, to the trustees/commissioners of SPEARS;
- liaises with SPEARS providers;
- oversees operation of Public Service Earnings Index (for pension increases);
- prepares pension scheme documentation and information booklets;
- liaises with the Pension Support Units; in due course, the PSPO could take over responsibility for the work of the Pension Support Units.

4. Pension Support Units

- linked to relevant Government Departments;
- records relevant data in relation to serving public servants;
- deals with set-up and payment of new pension cases, processing of pension increases;
- implementation of pensions IT/database strategy;
- communication with pension scheme members, including provision of scheme documentation, answering queries, etc.

PART VII

Conclusions

CHAPTER 26

Conclusions and Overview of Recommendations and Impact on Costs

26.1 Introduction

26.1.1 Under our terms of reference, the Commission was required to examine and report on the pension arrangements of public servants having regard to the present and future cost of pensions, claims for improvements in scheme benefits, changes in working environment and conditions of employment, and the operational needs of the public service.

26.1.2 From the outset, the Commission was faced with the challenge of having to address the problem of the escalating cost of public service pensions against the background of a desire for greater flexibility and improved pension terms within the public service itself. These expectations have, no doubt, been fuelled by the present conditions in the Irish economy. The problem is that the cost of improvements in pension terms might appear small in comparison with current GNP but could be much larger as time progresses.

26.1.3 Many countries in Europe are now confronting the same problems that we may confront in the future. In responding to these problems, they have sought to limit improvements in pension terms and/or to restrict conditions of entitlement. Our objective was to find ways of *heading off* these cost problems through early reform of pension schemes and, in this way, ensuring minimum disruption in the longer term.

26.1.4 Our approach has been to outline the strengths and deficiencies of existing pension terms and arrangements in the public service, taking the public service in other countries and the private sector as comparators. The size of the public service pensions bill has been quantified in a comprehensive manner, including projections of its future profile. This statistical base has made it possible to estimate accurately the impact of changes in pension terms on existing and future pensions outgoings.

26.1.5 The Commission concluded that a change to a completely new pension scheme such as a defined contribution scheme was neither necessary nor desirable at this time. Likewise, no compelling case was apparent for changing the system of financing public service pension costs from pay-as-you-go to full funding.

26.1.6 However, significant modifications in present arrangements were possible that, in the Commission's view, would enhance the viability and stability of public service pensions in the long-term.

26.1.7 In this Chapter, we present an overview of our recommendations and of the cost implications of implementing the major recommendations.

26.2 Overview of Commission recommendations

26.2.1 The Commission's approach in determining our recommendations has been:

(i) to find ways of smoothing the expected peak in costs, including the use of pension funding;

(ii) to limit any recommended scheme improvements to cost neutral changes, or to cost increasing changes considered absolutely necessary for operational reasons or on grounds of equity and fairness, with a view to preventing as far as possible any net enlargement of the rise in the pensions bill;

(iii) to estimate the impact on long-term costs of all major suggested changes in pension terms;

(iv) to permit as much individual flexibility as possible, consistent with the overall framework of the pensions system, in order to allow employees to provide for benefit improvements by means of personal contributions (the new flexibility to be facilitated through better communication systems);

(v) where a disimprovement in benefit terms is considered necessary, to confine the change to new entrants only, while having due regard to intergenerational equity.

26.2.2 The main recommendations are summarised below:[310]

- **retirement age and early retirement:** pension changes to facilitate new work patterns in the lead-in to retirement; the introduction of cost neutral early retirement from age 50; a change to a standard retirement age of 65 (new entrants); the introduction of a limited early retirement facility called Approved Early Retirement; changes in the application of special early retirement terms to certain groups for operational reasons (new entrants);
- **pension increases:** a change in the method of applying pay-related pension increases through the use of a CSO Public Service Earnings Index; the introduction of a new contribution by public servants of 1% of remuneration/net remuneration towards the cost of pay-related pension increases;
- **integration with State Social Insurance benefits:** a change in the pension calculation formula aimed at improving occupational pension for those retiring on relatively low levels of pay; a change in the way in which integration is applied in the case of part-time public servants;
- **pension savings:** the development of a new centralised AVC-type arrangement called the Scheme for Public Employees' Additional Retirement Savings;
- **other pension terms:** the removal of notional added years facilities for professional, technical and other grades (new entrants);
- **partial funding:** the establishment of a fund to meet the cost of public service pension increases;

[310] Reservations were expressed by some members of the Commission in relation to several of the recommendations. These are marked separately below.

- **cost transparency:** the adoption of an accruals-based approach to accounting for pension costs;
- **scheme management and administration:** the introduction of a centralised structure for the management and administration of public service pension schemes, including the establishment of a Public Service Pensions Office.

A full list of the 57 recommendations made by the Commission is given at the start of the Report.

26.2.3 The package of recommendations represents a comprehensive reform of the existing public service pensions framework, with the focus of reforms coming under the following headings:

- viability;
- flexibility;
- adequacy and fairness;
- management and development.

We summarise below the main recommendations of the Commission under each of these headings. In cases where reservations were expressed by Commission members, we have marked the recommendation with "*(R)*".

26.3 Viability

26.3.1 The Commission carried out a full actuarial review of public service pension schemes and ascertained the long-term cost projections of schemes. We commented on the affordability of the escalating pensions bill and how it must be seen in the context of other cost pressures (including Social Welfare pensions and health care) arising from demographic ageing.

26.3.2 Our recommendations on pension terms take account, amongst other things, of the continuing improvement in life expectancy in Ireland. The effect of improved life expectancy is that occupational pensions are being paid for a longer period, thus adding substantial additional costs onto pension schemes. Accordingly, we recommend an increase in the age of retirement for new entrants to the public service to 65. *(R)*

26.3.3 The Commission sees definite advantages in the idea of partially funding future pension costs as a means of securing the viability of public service schemes. We welcome the Government decision of July 1999 to pre-fund part of the future cost of Social Welfare and public service pensions. This initiative will help to smooth the pensions bill in the future, thereby averting destabilising shifts in future government taxation/spending patterns. In addition, it ensures diversification of state expenditure at a time when the economy is at or near full employment and revenue is buoyant. Finally, as we have argued, funding (whether full funding or part funding) represents an effective approach to ensuring greater transparency and discipline in the management of public service pension costs. The Commission's specific recommendation on partial funding is that a properly constituted independent pension fund should be established for the purposes of financing annual increases in pensions.

26.3.4 One of the Commission's objectives was the establishment of a consistent pension system for all public servants, with differences in pension terms to be based on particular operational requirements. Accordingly, we recommend certain changes in the special pension terms held by particular groups for operational reasons. Developments in operational requirements since these terms were first introduced necessitate these changes, which will affect new entrants only. *(R)*

26.3.5 The Commission recommends the introduction of an additional early retirement facility, called *Approved Early Retirement*, in respect of public servants aged 55 or over with 20 or more years' service who consider that they are unable to make a fully satisfactory contribution, and where management accept that their early retirement would improve the general level of efficiency and effectiveness of the service in question. Approved Early Retirement would be initiated either by management or the individual public servant, and would be subject to agreement by both parties. Pension benefits under Approved Early Retirement would consist of the immediate payment of pension and retirement lump sum with no actuarial reduction.

26.3.6 In the case of teachers and nurses, where special early retirement facilities have been in operation for the past few years on a pilot basis, the Commission recommends the continuation of these facilities for a further five years. We recommend also that they, along with the Approved Early Retirement facility, be subject to review in five years' time, and that this review take into account the implementation of new performance management systems in the public service.

26.3.7 We recommend the adoption of a new accounting framework with the objective of extending greater transparency into pension costs and liabilities. Such a framework would help ensure that the pension cost implications of changes in pension terms, recruitment, early retirement, etc. were properly recognised. It would also ensure that a more realistic approach would be adopted to managing the future development of pension schemes. We believe the implementation of such an accounting framework should be done in the context of ongoing reform in government financial management systems under the Strategic Management Initiative.

26.3.8 Finally, we recommend that the cost of any further proposed changes in pension terms should be ascertained in advance on an objective basis, with agreement to be reached between unions and employers as to how the additional cost should be met.

26.4 Flexibility

26.4.1 Greater pension flexibility is desirable from the perspective of both the employer and the employee. On this there is general agreement. There is also agreement that the cost of such enhanced flexibility should be objectively quantified.

26.4.2 To meet this demand, we recommend greater flexibility as regards retirement with respect to the following:

- the option to retire from age 50 (age 55 in the case of new entrants) with actuarial reduction of benefits to cover the longer period over which benefits will be paid;
- safeguarding the accrued pension entitlements of public servants who wish to work part-time, work at a lower level of responsibility, or work reduced levels of unsocial hours in the period prior to retirement;
- some relaxation of the abatement of pension rules in order to facilitate the re-employment of public servants with required expertise/skills on a contract basis after retirement.

26.4.3 A number of shortcomings were identified in existing provisions aimed at facilitating retirement choice, viz the schemes for purchase of notional service and union-sponsored schemes of additional voluntary contributions (AVCs). Accordingly, we recommend the introduction of a new AVC-type facility to be known as the Scheme for Public Employees' Additional Retirement Savings (SPEARS). This facility would enable public servants to contribute towards additional pension benefits and death cover, and to make good some of the shortfall in pension resulting from a decision to retire early.

26.4.4 SPEARS would be open to all employees in the public service and would be portable between public service employments. Contributions to SPEARS would be tax deductible. Central tendering arrangements should ensure that individuals availing of SPEARS would benefit from low rates of charges and fees.

26.4.5 A major benefit of SPEARS would be its flexibility. It would offer options which are not available under existing arrangements. Individuals could make contributions by periodic deduction or by lump sum. They could change their contribution arrangements or the investment mandate for their funds as their circumstances change. SPEARS would provide employees with a flexible facility to purchase an additional pension from the State, at a properly costed rate, which would attract pension increases in line with public service pension increases generally.

26.4.6 The Commission also recommends greater scheme flexibility in relation to dependants' benefits:

- the nomination of beneficiary for the receipt of gratuity in the case of death-in-service; and
- the payment of a survivor's pension to a financially dependent partner in circumstances where there is no legal spouse and where a valid nomination has been made. *(R)*

26.4.7 An essential feature of the new public service pensions framework is that the details of benefit entitlements and options should be actively communicated. Accordingly, the Commission recommends that public servants should be provided with an annual benefit statement setting out their accrued pension entitlements and their prospective benefits at retirement age. This would enable them to have a better appreciation of the value of their entitlements and of the contributions which they must make in order to achieve their retirement and pension objectives.

26.5 Adequacy and fairness

26.5.1 It is important that pension terms are applied fairly and transparently and that they are adequate by reference to past and current pay conditions. We consider that the benefits and conditions of public service pensions compare well with good pension schemes in the private sector and in the public service abroad.

26.5.2 Employees in full PRSI class who retire on relatively low levels of pay receive low or sometimes zero occupational pension even if the level of pensionable service is high. This is because of integration with the pension provided by the Social Welfare system. The Commission accepts the logic of this situation. Nevertheless, we are aware of the negative perception arising from this situation amongst the affected groups. One way of dealing with the problem is the recommendation in our Report which would have the effect of increasing the rate of pension where pensionable remuneration at retirement is below an amount equal to three times the rate of Social Welfare Old Age (Contributory) Pension (OACP), i.e. £288 (€366) per week, based on the May 2000 rate of £96 (€122) per week. Pensioners whose pensions are integrated and whose pensionable remuneration (updated to current values) is less than the cut-off amount would also benefit from this change. We believe this recommendation is justified on the basis of the long-term benefit of removing a major source of contention and grievance for the public service groups affected.

26.5.3 With integration, the OACP is merged (or coordinated, or integrated) with the occupational pension to provide a combined pension which is both reasonable, by reference to pensionable pay and the period in employment, and affordable to both employees and employers. In effect, integration avoids *double pensioning* that tranche of income which is already *pensioned* by the employer's and employee's PRSI contributions. The Commission accepts that integration is a fundamental component in the public service pensions framework and is strongly of the view that it should be continued. In relation to our recommendation at Paragraph 26.5.2, it should be noted that the pension of all other public servants, i.e. public servants retiring on pensionable remuneration in excess of three times the rate of OACP, would remain unchanged.

26.5.4 The Commission also saw the need to improve the pensions position of those in atypical employment. Accordingly, we recommend that temporary and part-time public servants should be granted access to pension schemes. We also recommend an improvement in the method of integration of pension for part-time public servants. Finally, we recommend that the period of reckonable service required to qualify for preserved benefits should be reduced from five to two years.

26.5.5 While the Commission does not recommend a new general option to join public service spouses' and children's contributory pension schemes, as sought in a number of submissions, we do recommend the establishment of a limited appeals mechanism to examine the exercise of past options, subject to a number of specific criteria.

26.5.6 The existing system for increasing pensions in line with pay has become a source of concern in recent times, in light of changes to pay determination and administrative difficulties. In addition, major variation in the nature of the pay agreements as between different public service groups has resulted in the application of very different rates of pension increase. For these reasons, the Commission recommends that a CSO Public Service Earnings Index should be developed for twice-yearly calculation of a single rate of pay-related increase to be paid to all public service pensioners. The implementation of the index should involve consultation with public service employers, unions and pensioner representatives. Furthermore, the Commission recommends that, in view of the value to public servants of a guaranteed system of pay-related pension increases, all serving public servants should make an additional explicit 1% contribution of remuneration or net remuneration, as appropriate, towards the cost of pay-related pension increases *(R)*. The Commission also recommends that the State explicitly guarantee the new system of pension increases by means of legislation and through the establishment of a Public Service Pension Fund for pension increases.

26.5.7 Finally, under the general heading of adequacy and fairness, we recommend the establishment of an independent appeals mechanism for public service pensions. This would lead to an increased confidence amongst public servants and pensioners in the quality of pensions administration and decision making.

26.6 Management and development of scheme

26.6.1 The Commission considers that there are a number of areas in which improvement is necessary in current arrangements for managing and administering public service pensions. Addressing these would, in our view, help to address employee dissatisfaction in relation to pension terms — early retirement, in particular — as well as ensuring greater transparency in the cost and value of pensions.

26.6.2 Our recommendations on the adoption of a new accounting framework, if implemented, would help to ensure transparency in pension costs and facilitate better quality decision making as far as pensions are concerned.

26.6.3 Several of our recommendations, if implemented, would change the way public service pensions are managed and administered in the future. These include the Public Service Pension Fund, the Public Service Earnings Index, and SPEARS. In addition, pension scheme administrators would have to adopt a more proactive approach to communication of benefits and options, make more effective use of information technology, and operate a new system of accounting for pension costs.

26.6.4 In view of the above developments and considerations, we recommend the introduction of a centralised structure for the administration and management of public service pension schemes, involving the Minister for Finance, an Inter-Departmental Committee on Public Service Pensions (and, perhaps, involving the public service unions in a Public Service Pensions Partnership Committee), a Public Service Pensions Office (PSPO), and a number of Pension Support Units.

26.6.5 The Commission hopes that the full range of pension issues and recommendations in this Report will be dealt with by the Working Group to be established under the *PPF* to implement the relevant decisions arising from Government consideration of our Report. We recommend that all parties should agree to forward claims under consideration to the PSPO for costing.

26.6.6 We recommend the development of a specialised computerised pensions administration system, the introduction of which should be overseen by the interdepartmental committee and implemented by the PSPO, with appropriate expert assistance.

26.6.7 Consistent with our recommendations in relation to pension flexibility, we recommend the implementation of an active policy of pension scheme communication, involving the provision of user-friendly documentation, an annual benefit statement, and a statement of the options available to public servants to improve their overall level of benefits and to plan for their retirement (including information on SPEARS).

26.7 Overview of cost of Commission recommendations

26.7.1 Assessing the financial implications of the Commission's recommendations is an unusually complex task. Some proposals would add to pensions expenditure (benefits), others would reduce it, and the different proposals have different time profiles. Some of our proposals would affect expenditure in the short-term only and are rapidly self-liquidating through the passage of time, others could have enduring long-term implications for the pensions bill that are impossible to quantify precisely. For example, the Commission is confident that our recommendations on pensions administration, taken in their entirety, would introduce a more flexible and more effective way of dealing with public service pensions that could have a significant long lasting impact on pensions expenditure, on productivity in the public service and through these on overall economic performance. But exact estimation of this impact is obviously impossible. Where appropriate, specific recommendations have been costed, and the broad methodology of such costing exercises is explained in this Report.

26.7.2 In Table 26.1, we illustrate the broad impact of the Commission's main recommendations in terms of their impact on costs and savings, both in the short- and long-term.

Table 26.1: Assessment of impact of main recommendations on cost of public service pensions

Short-term costs	Short-term savings
Approved Early Retirement New integration formula Pensions for part-timers Funding of pension increases Pensions administration	1% contribution for pension increases

Long-term costs	Long-term savings
Approved Early Retirement New integration formula Pensions for part-timers Pensions administration	Increase in retirement age Changes in special terms Removal of professional added years 1% contribution for pension increases Improved administrative efficiency Funding of pension increases

26.7.3 A number of the Commission's recommendations would not have any direct implications for the future cost of pension benefits. Some recommendations involve new ways of carrying out existing functions, perhaps in a way that would be more effective than the existing approach. Others involve initiatives which would improve pension scheme flexibility or the quality of service offered to public servants and to pensioners.

26.7.4 For example, use of the Public Service Earnings Index as the basis for calculating future rates of pension increases would not result in any change in the overall cost of pension increases in the long-term; however, it would reduce administrative costs by allowing departments and agencies to pay a single rate of increase automatically to all pensioners, rather than having to examine the particular implications of each pay agreement for different pensioner groups.

26.7.5 The recommendations in relation to cost transparency and pension scheme management and administration would increase the cost to the State of administering pension schemes, but should also contribute to improved management of schemes and to better communication of scheme entitlements. The development of SPEARS would likely give rise to additional costs, particularly if the State decided to meet part of the scheme's promotional costs. However, this must be balanced against the administrative costs which the State currently bears in relation to the schemes for purchase of notional service.

26.7.6 Certain scheme recommendations might appear to represent benefit improvements, but at a wider level could also realise savings. For example, there would be an additional capital cost to the State for each individual availing of the Approved Early Retirement facility. However, the terms of the new facility require employers to establish that each early retirement would improve the general level of efficiency and effectiveness of the service in question. Clearly, this aspect of the facility must be carefully monitored and controlled if it is not to give rise to additional costs.

26.7.7 The recommended introduction of a 1% contribution towards the cost of pension increases offers a real long-term saving in future pension costs.

26.7.8 In the case of pension funding, the Commission's recommendation to fund the cost of pension increases must be compared with the Government's decision of July 1999 to pre-fund future Social Welfare and public service pension costs. As we have shown in Chapter 23, the State contribution to the Public Service Pension Fund would not be very different from the implied contribution to which the Government has already committed itself under its pre-funding initiative.

26.7.9 We present below a more detailed analysis of the cost impact of each of the major recommendations contained in our Report. In the case of several recommendations, this has been a difficult or impossible task, because of deficiencies in the available data and because retirement behaviour may change substantially as a result of implementation of these recommendations. Thus, in some cases, we can only comment on the likely effect on future pension costs.

Presentation of cost

26.7.10 In considering the impact on future costs of proposed changes in pension terms, the question arises as to the best means of presenting the effect of each change, i.e. the consequences for cashflow projections, the State's accrued liabilities, and/or new entrant contribution rates. In practice, the most appropriate approach is to express the cost of any recommendation in a way which reflects the time period over which the cost will occur. For example, a change in retirement age affecting new entrants only will have no impact on the State's accrued liabilities, and minimal impact on cashflow projections for up to the next 40 years; however, it will cause a reduction in new entrant contribution rates.

26.7.11 In some cases, it is possible to measure the cost of the recommendation as a capital cost, expressed as a factor of the salary of the individual public servant. This is the approach which we have adopted in costing the effect of early retirement.

Flexible approach to retirement (Paragraphs 15.15.8, 15.15.12)

26.7.12 Pension changes to facilitate new work and retirement flexibility in the lead-in to retirement and the relaxation of pension abatement on re-employment after retirement would result in a minor change in future pension costs.

Increase in age of retirement (Paragraph 15.15.17) and changes in special terms applying to certain groups for operational reasons (Paragraph 15.15.33, 21.6.6)

26.7.13 The introduction of a standard retirement age of 65 would bring a gradual reduction in pension costs which would become fully apparent in around 30 to 40 years' time; in the longer term, the saving would be quite significant. The impact of the change would vary throughout the public service; for example, at present, the new entrant rate for an established civil servant is 16.3%; this would fall to 14.3% if the retirement age were increased to 65.

26.7.14 The recommended changes in special terms affecting new entrants to the psychiatric services, Garda Síochána, prison service, fire service, teachers, and the Defence Forces would have little effect on costs for about 20 to 30 years and would result in a gradual reduction in costs thereafter. The level of savings could be significant. For example, the introduction of standard pension terms for the psychiatric services would cause a reduction in the new entrant rate (male) from 17% to 12.8% of pay. The actual level of savings would depend on future recruitment patterns and on what the retirement patterns would have been under the current system.

Cost neutral early retirement (Paragraph 15.15.14)

26.7.15 No additional costs would arise from implementation of this proposal. Any public servant opting for actuarially reduced early retirement would receive a smaller pension for a longer period. There would be slightly higher pensions expenditure in early years matched by lower payments in later years; the effect would depend on the numbers who opted for this facility.

Approved Early Retirement (Paragraph 15.15.21)

26.7.16 The costs associated with this proposal would depend on the numbers who were allowed to retire and also on their pay and service at retirement. There might be advantages to the public service in terms of increased productivity and there would also be savings if all retirees were not replaced immediately; no monetary value has been placed on these potential benefits. With early retirement, additional costs would arise from the pension being paid for a longer period, the lump sum being paid earlier and the accrual of pension benefits of the replacement staff.

26.7.17 The capital cost of early retirement pension terms for sample grades expressed as a multiple of salary is shown below (these figures make no allowance for the benefits to management mentioned above). In each case, it is assumed that the individual is aged 55 and has 30 years' service at the time of early retirement.

Table 26.2: Cost of Approved Early Retirement (as a multiple of salary)

Grade	Multiple of salary
Civil Servant	1.71
Teacher	1.60
General Nurse	1.69

26.7.18 Details of the measurement of the cost impact of early retirement are provided in Section 10.4.

Pay-related pension increases based on a new Public Service Earnings Index (Paragraph 16.6.5)

26.7.19 There would be no change in average pension costs arising from implementation of this proposal as the new method of increasing pensions would provide for the average increase that would have been granted under the current system. There would be some small costs involved in setting up the index. However, there would be a small saving in administrative costs arising from a change to an index method of increases.

1% contribution towards the cost of pension increases (Paragraph 16.6.5)

26.7.20 This contribution would be levied on remuneration, including pensionable allowances, for public servants in modified PRSI class and on net pensionable remuneration for public servants in full PRSI class, whose pensions are subject to integration. The income from this 1% contribution is estimated at £38 million (€48 million) in the year 2002, rising to £58 million (€74 million), in constant (1997) price terms, by 2047. The saving to the State resulting from the additional contribution would fall as a percentage of annual pensions expenditure in the period under review.

Integration and low levels of occupational pension (Paragraph 17.6.5)

26.7.21 The cost of this proposal, if applied to both serving staff and current pensioners, would result in an increase in pension costs of around £2 million (€3 million) in the first year rising, in constant (1997) price terms, to an annual increase of around £13 million (€17 million) in about 40 years' time, assuming the level of OACP gains at the same rate as average pay in the public service.

Pensions and atypical employment (Paragraphs 18.6.7, 18.6.13)

26.7.22 We estimate that the recommendation to change from full to pro rata integration in relation to the pensions of part-time employees would have minimal effect in the short-term, and would, in time, bring an increase in pension costs of the order of £11 million (€14 million) per annum in about 40 years' time, in constant (1997) price terms. The proposed change would result in an increase of £32 million (€41 million) in the State's accrued liabilities. It should be noted that this estimate relates only to part-time employees still in service.

26.7.23 The reduction in the qualifying period for a preserved pension from five to two years would give rise to some minor costs in about 30 years' time. The extra cost would arise in respect of public servants who leave with more than two and less than five years' service.

Pension scheme flexibility (Chapter 19)

26.7.24 The Commission has recommended that the State should consider meeting part of the administrative costs of SPEARS, in particular, the cost of promoting the scheme. Such a move would involve some additional costs to the State. However, the Commission's recommendation is presented in the context of the phased removal of the schemes for the purchase of notional service. The removal of these schemes would result in savings in administrative costs.

Removal of schemes of notional added years (Paragraph 22.3.12)

26.7.25 Savings from the removal of schemes of notional added years for new entrants would result in around 30 years' time. The savings would depend on the numbers recruited in future who would have been awarded added years. The estimated impact on the new entrant contribution rates for a few sample grades is as follows:

Table 26.3: Impact of removal of notional added years on new entrant contribution rates

Group	Existing	Without added years
Local authority officers	18%	16%
Consultants in health sector	21%	17%

Funding (Chapter 23)

26.7.26 The funding of public service pensions would not, of itself, reduce the cost of pension schemes, except to the extent that the returns on the monies lodged to the fund would be greater than the returns which the Government would otherwise have obtained (a comparison that is difficult to quantify conclusively). However, funding would enable the State to smooth the expected peak in pension costs.

26.7.27 Having established the new fund, the State's expenditures on public service pensions would be greater in the early years when account is taken of contributions to the fund; net pension payments would be lower in the long-term as part of future pension payments would be met by the fund.

26.7.28 The National Pensions Reserve Fund Bill, 2000 provides for the establishment of a Reserve Fund to meet part of the future cost of Social Welfare and public service pensions from 2025 onwards. The Commission has recommended that the portion of the fund that relates to public service pensions should be established as a separate Public Service Pension Fund to meet the cost of pension increases. Thus, the cost impact of the Commission's recommendation must be assessed against the (implied) funding commitment for public service pensions which has already been indicated by the Government. This involves considering both contributions and drawdowns.

26.7.29 On the contribution side, both the National Pensions Reserve Fund and the Commission's recommended fund for pension increases would involve the making of periodic contributions and additional lump sum contributions. We have shown in Section 23.8 that, in the short-term at least, the annual fund contribution implied in the former ($\frac{1}{3}$% of GNP) is broadly similar to that envisaged in the latter (5.1% of pensionable pay falling to 4% over a 40 year period). We estimate that in the longer term the contributions envisaged under both approaches would be broadly of the same order.

26.7.30 As regards lump sum contributions, the State has to date implicitly contributed £1.2 billion (€1.5 billion) to pre-fund public service pensions (see Table 23.4), in addition to the annual contribution. This is broadly consistent with payment of lump sum contributions in respect of part of the accrued liability for pension increases for serving staff, as examined by the Commission in the two scenarios set out in Section 23.7.

26.7.31 On the drawdown side, it is envisaged that the National Pensions Reserve Fund would not be available for payment to the Exchequer until the year 2025. The precise arrangements for payment from the Fund are to be drawn up, subject to certain legislative safeguards, by the Minister for Finance in consultation with the Minister for Social, Community and Family Affairs. The Commission envisages that consistent with the actuarial approach underpinning the proposed fund for pension increases, drawdowns would commence immediately. However, the amounts involved would be small in the initial years, reflecting the very low portion of the liability for pension increases being carried by the fund. The drawdowns would be correspondingly higher, the greater the level of additional lump sum contributions.

26.7.32 In conclusion, the Commission envisages that the periodic and lump sum contributions to a public service pension fund to meet the cost of pension increases would be broadly of the same order as that implied for the pre-funding of public service pensions in the National Pensions Reserve Fund. There would be a very different profile of fund payments as between the two approaches, reflecting the different drawdown mechanisms involved.

Accruals-based approach to accounting for pensions costs (Chapter 24)

26.7.33 The proposed changes in accounting for pension costs would involve some additional staff costs.

Improved pensions administration and communication systems (Chapter 25)

26.7.34 It would be necessary to commit extra resources in order to implement this proposal. The recommended centralised structure for the future administration of public service pensions would require some additional staff. Extra resources would also be associated with the proposed specialised computerised pensions administration system and with the proposed improvement of pension scheme communications.

26.8 Final comments

26.8.1 The recommendations of this Report have implications for all parties having an interest in public service pensions — the Government, public service employers, trade unions, pensioner associations, individual public servants and pensioners — as well as for the taxpayer. They may also have implications for the commercial state sector, the private sector and for the overall competitiveness of the economy generally. The recommendations which we make are the fruits of a comprehensive examination of Irish public service pension schemes, a detailed evaluation of scheme structures and benefits, and a considered analysis of how best to reconcile the legitimate concerns of the major stakeholders. Against this background, we are satisfied that the recommendations represent an integrated and cohesive long-term strategy for public service pensions, and we would place particular emphasis on the importance of maintaining the integrity and cohesion of the package of measures outlined in this Report. We are aware that, taking account of the range of entitlements currently applicable to serving staff in the public service, the changes which we propose — primarily in respect of new entrants — are less beneficial in some respects, and more beneficial in others, but it is essential that the balanced nature of our recommendations be recognised and respected.

26.8.2 This is a time of increasing pressure and of cutbacks in pension terms in many Western economies. The public service pension bill, financed on a pay-as-you-go basis out of general revenues, is a matter of general concern. Ireland's public service pensions are no exception. However, because the overall demographic situation is more favourable than in other countries, the national finances will be in a stronger position than others to cope with the consequences of ageing for some time. It is important that this breathing space is put to constructive use. The Commission is confident that our recommendations will help secure the long-term viability and stability of public service occupational pension schemes in Ireland.

Dermot McAleese
Chairperson

Brian Aylward	Anne Maher
Rosheen Callender	Joe McGovern
John Cullen	Dan Murphy
Brian Geoghegan	Senator Joe O'Toole
Eamonn Heffernan	Anne Vaughan

Conor McGinn
Secretary
14 November 2000