Staff Paper 2014

Expenditure Review of State Pension and Related Supplementary Benefit Schemes

Irish Government Economic and Evaluation Service

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Summary

- The main schemes are State Pension (Contributory) and State Pension (Non-Contributory); combined they accounted for €4.93 billion in public expenditure in 2013 (or 25% of total expenditure on social protection schemes and services).
- In 2013, there were over 420,000 people in receipt of one of these two payments compared with 201,000 in 2003 – a 115% increase.
- State Pension (Contributory) has experienced particularly high growth in recipients over the period, at 189% (from 114,000 in 2003 to 330,000 in 2013). It must be noted that there was a rationalisation of customers between 2006 and 2007, which caused the numbers on State Pension schemes to increase in 2007. This change was noticeably seen in the growth in State Pension (Contributory) numbers and expenditure.
- The analysis highlights that under a 'no change' scenario, the expenditure on these two schemes could reach around €7.5 billion by 2026. This is an increase of **€2.36 billion** on the current allocation in 2014 of €5.1 billion in nominal terms, and represents an estimated annual increase of **€195 million per year** out to 2026.
- In addition to the primary payments, by 2026 we estimate that expenditure on Supplementary Benefits such as the Household Benefits, Free Travel and Fuel Allowance would increase to around €800 million up from an estimated €515 million in 2014.
- Looking at Poverty Rates from the EU-SILC data, it is clear that the Government policies have had an impact in protecting people of pension age over other age cohorts. The at-risk of poverty rate for those aged 65 plus dropped 4.5 percentage points between 2007 and 2012, compared to a drop of 1.1 percentage points for those 17 or younger and a 1.4 percentage point increase for working age people.
- It is of key importance to the state that the State Pension provision is maintained at a sustainable level. Given that the estimated increase per year due to demographics alone is in the region of €200 million, there are serious concerns about the sustainability of such future expenditure levels. In addition, with Ireland coming under the scope of the new EU 'Sixpack' framework, the state will no longer be able to allow extra expenditure to cover increasing demographic pressures on an

aggregate level. This means that the sustainability of State Pensions will likely have to be achieved through the use of structural reforms to the scheme or through increased taxation or expenditure reductions in other areas.

- This paper presents a range of policy options for consideration in an Expenditure Review context. Options for Structural Reforms which would help make pension-related expenditure sustainable in the medium-term and better balance resources to those most in need are detailed below:
  - Bringing forward increases in the Pension Age **-** An option is to bring forward the increases in the age for State Pension eligibility scheduled for 2021 (to age 67) and 2028 (to age 68) by say, 3 years to 2018 and 2025 respectively.
  - Increase the number of yearly contributions for a full State Pension under the Total Contributions approach.
  - Introduce a Qualified Adult Increase on State Pension (Non-Contributory) for those spouses/civil partners aged 66 or over.
  - Reductions in the basic rates of the State Pension (Contributory) and/or the State Pension (Non-Contributory). The combined savings of a €1 reduction to the State Pension schemes and a pro-rata reduction for qualified adults is in the region of **€22.8 million**.
  - Discontinuation of the Over-80's allowance for new entrants to save an estimated **€2 million** in the initial year but savings would increase over time to **€72 million** in a full year.
  - Applying the fuel allowance means test for new recipients of the Household Benefits Package would achieve savings of around **€23 million** if introduced.
  - Discontinuing the Free TV License to coincide with the introduction in 2015 of the new Household Broadcasting Charge would save **€54 million.**
  - Aligning/limiting the Gas/Electricity Allowance to the 6 month long winter Fuel Allowance payment saving in the region of **€87 million**.
  - Reforming the Free Travel Pass – with options presented for savings ranging between **€3 million and €62 million.**
  - Means-testing the universal Living Alone Allowance, which would save an estimated **€27 million.**
  - Increasing PRSI revenues to support the Social Insurance Fund (SIF), which primarily funds Contributory Pensions and related supplementary benefits. The latest actuarial review of the SIF highlights that the SIF revenue needs to increase by 187% in the longer term (out to 2066) to become self-funding.

1. Introduction and Overview

Recently, the numbers on State Pension schemes in Ireland has grown considerably, with the population projections for the future suggesting that this growth will continue. This paper looks at the two State Pension schemes – State Pension (Contributory) and State Pension (Non-Contributory), to assess if they are economically sustainable in their current form or whether reform is necessary to ensure their sustainability. The two schemes under review together amounted to €4.9 billion in 2013 – which represents a quarter of total voted and Social Insurance Fund expenditure on social protection schemes and services. Pension schemes represent the largest area of Department of Social Protection expenditure.

1.1 Scheme Details

State Pension (Contributory) - €3.98 billion in 2013

State Pension (Contributory) is a contributory-based weekly payment made to people aged 66 or older who have made the required PRSI contributions during their working lives. To qualify for the maximum payment the recipient must have made at least 520 PRSI contributions (10 years) and have at least an average of 48 contributions made per year. The payment is not-means tested as it is based solely on contributions. The maximum weekly rate is €230.30 and recipients can also claim for an adult dependent (€206.30) i.e. a spouse, civil partner or cohabitant, or a child dependant (€29.80).

State Pension (Non-Contributory) - €0.95 billion in 2013

State Pension (Non-Contributory) is a means-tested weekly payment to people aged 66 or older who do not have the required PRSI contributions to claim State Pension (Contributory) but whose means are low enough to qualify for state pension assistance. To qualify the recipient must (i) not qualify for a State Pension (Contributory) payment, (ii) pass a means test and (iii) meet the habitual residence condition. The means for State Pension (Non-Contributory) are more generous than those for working age schemes, with the first €20,000 of capital and €200 in weekly earning exempted from the means test. The maximum weekly rate is €219, and recipients can also claim for an adult dependent (€144.70) and a child dependant (€29.80). Once the adult dependent reached 66 years of age they no longer become entitled to the increase for qualified adult payment, however they can apply for State Pension (Non-Contributory) in their own right.

2. Contextual Analysis

2.1 Rationale

The rationale behind the payment of the State Pension schemes is to provide an income support for people who are aged 66 and over, who are more than likely out of the labour force. These payments are a key component in the state's welfare system. The "Old Age Pension" precedes the foundation of the State, having been set up by the United Kingdom Government in 1909.

2.2 Trend Analysis: Growth in Number of Recipients and Rates

Table 1 below shows the degree to which the total cost to the State of the State Pension schemes have increased over the period 2003 to 2013. It shows that there has been a 236% increase to the total cost of these two schemes, from just over €1.5bn in 2003 to just under €5.1bn in 2014. In particular, the expenditure on State Pension (Contributory) alone more than quadrupled in this 11 year period.

Table 1: Payment trends, 2003 to 2014

	2003	*2004*	*2005*	*2006*	*2007*	*2008*	*2009*	*2010*	*2011*	*2012*	*2013*	*2014*
	€ m	*€ m*	*€ m*	*€ m*	*€ m*	*€ m*	*€ m*	*€ m*	*€ m*	*€ m*	*€ m*	*€ m*
State Pension (Non-Con)	565	600	631	728	920	973	1,001	977	972	963	952	940
State Pension (Contributory)	947	1,050	1,153	1,581	2,755	3,118	3,368	3,452	3,623	3,800	3,981	4,142
Total	1,512	1,650	1,784	2,309	3,675	4,091	4,368	4,429	4,595	4,764	4,933	5,082

Source: 2012 statistics book published by Department of Social Protection and 2014 REV.

As Tables 2 and 3 below show, underlying the growing cost base over the period is a combination of regular rate increases introduced up until 2009 and increasing numbers of recipients due to population growth in pension aged people. There was an approximate 50% increase in the weekly rates of the two State Pension schemes between 2003 and 2014, with these two schemes exempt from any rate reductions following the economic downturn. By comparison the Consumer price index increased by 17.8% between 2003 and 2013. If the State Pensions had matched the CPI increase from 2003 to 2013, then the State Pension (Contributory) would only pay €185.40 in 2013 and the State Pension (Non-Contributory) would only pay €169.70.

In addition to the State Pension payments, there is also an entitlement to the over 80's allowance once a person reached 80 years of age. This is an additional payment of €10 per week on top of the State Pension payment. Also there is a top-up of €7.70 per week for those who are Living Alone, approximately 147,000 people on State Pensions qualify for this payment.

Table 2: Trend in rates, 2003 to 2014		
Year	***State Pension (Contributory) € p.w.***	***State Pension (Non-Contributory) € p.w.***
2003	157.30	144.00
2004	167.30	154.00
2005	179.30	166.00
2006	193.30	182.00
2007	209.30	200.00
2008	223.30	212.00
2009	230.30	219.00
2010	230.30	219.00
2011	230.30	219.00
2012	230.30	219.00
2013	230.30	219.00
2014	230.30	219.00

Source: 2012 statistics book published by Department of Social Protection and 2013 Social Welfare Rates of Payment 2013

In 2003, there were 201,000 people in receipt of one of the two payments; by 2013 this number was 424,000 - a 115% increase in the number of recipients. It must be noted, however, that there was a simplification of scheme arrangements for the over 66's between 2006 and 2007, which caused the numbers on State Pension schemes to increase in 2007, while numbers on other related schemes reduced[1]. This change can be noticeably seen in the growth in State Pension (Contributory) numbers and expenditure.

Table 3: Trend in volume, 2003 to 2013											
	2003 '000	***2004 '000***	***2005 '000***	***2006 '000***	***2007 '000***	***2008 '000***	***2009 '000***	***2010 '000***	***2011 '000***	***2012 '000***	***2013 '000***
State Pension (Non-Con)	87	85	84	97	98	98	98	97	97	96	96
State Pension (Contributory)	114	118	125	140	238	250	265	280	297	312	329
Total	201	204	209	237	335	348	363	378	394	408	424

Source: 2012 statistics book published by Department of Social Protection.

[1] The Social Welfare Law Reform and Pensions Act 2006, Sections 11 and 12 provided for transfer of recipients aged 66 and over from 28th September 2007: **(i)** To State Pension (Non-Contributory) from Widow/ers' (Non-Contributory) Pension, Blind Person's Pension (aged 66 and over), Deserted/Prisoners Wife's Allowance and One-Parent Family Payment. **(ii)** To State Pension (Contributory) from Invalidity Pension or State Pension (Transition) when the recipient reaches the age of 66.

Figure 1: The effect of volume and rate increases on State Pension expenditure, 2003-2013

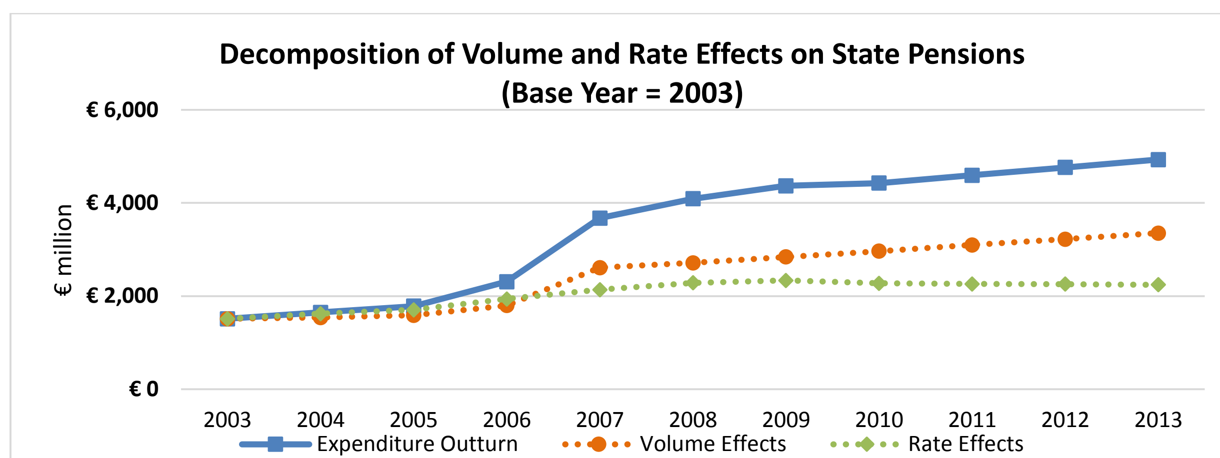
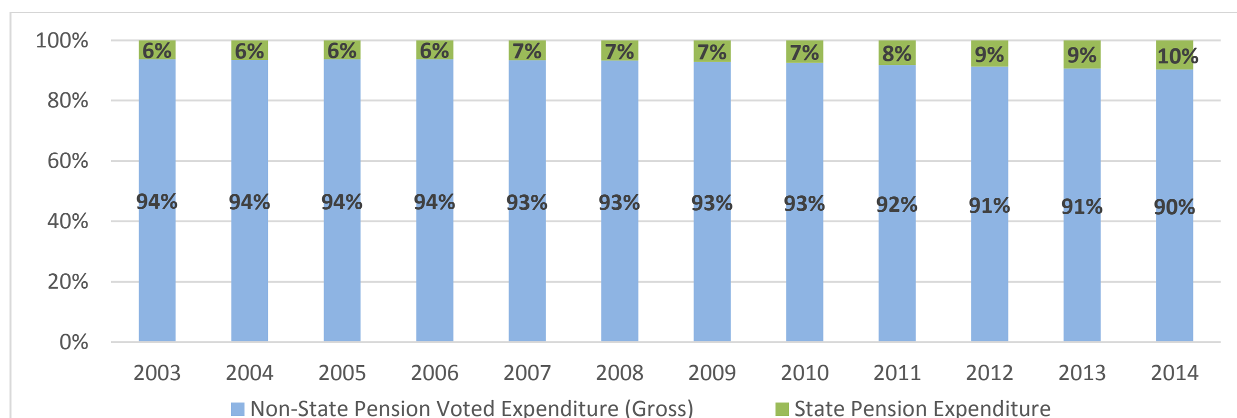


Figure 1 above shows the impact that the increases in rates and growth in recipient numbers have had on the expenditure on these schemes. We can see that the growth in recipients has been the primary driver of the increase in expenditure since 2008.

2.3 State Pensions as a Percentage of Gross Voted Expenditure, GDP and GNP.

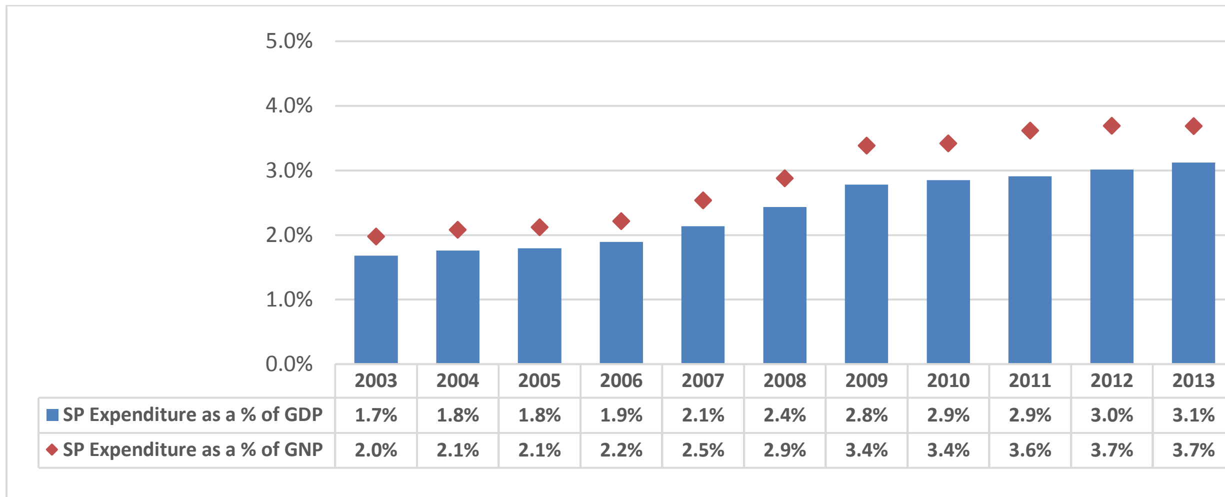
As detailed in figure 1 above, Pensions expenditure has consistently grown over the past eleven years. This is in contrast to most other areas of Government expenditure, particularly since 2009. While a significant amount of consolidation has been achieved across all Government Expenditure areas, State Pensions have been largely exempt from the consolidation effort. For this reason, we looked at the share of gross voted expenditure on State Pensions versus all other expenditure to see if State Pensions has grown relatively. Figure 2 clearly shows that State Pensions receives a significantly larger share of voted expenditure than it did in previous years. In particular since 2010, the share of State Pensions to total gross voted expenditure has grown from 7% to 10%. This trend is likely to continue given the expected growth in pension numbers in future years.

Figure 2: State Pensions as a percentage of Gross Voted Expenditure



In addition to looking at the comparison of State Pensions to Gross voted expenditure, we also looked at the comparison to our domestic and national product. Figure 3 below shows that spending on State Pensions compared to the GDP and GNP of the state has grown significantly. State Pensions in 2013 is 3.1% of our GDP, up from 1.7% in 2003. Similarly, State Pensions as a percentage of our GNP has grown by 1.7 percentage points in this period, up from 2% to 3.7%.

Figure 3: State Pensions as a percentage of GDP and GNP



	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
SP Expenditure as a % of GDP	1.7%	1.8%	1.8%	1.9%	2.1%	2.4%	2.8%	2.9%	2.9%	3.0%	3.1%
SP Expenditure as a % of GNP	2.0%	2.1%	2.1%	2.2%	2.5%	2.9%	3.4%	3.4%	3.6%	3.7%	3.7%

Source: CSO; Revised Estimates Volumes 2004 – 2012

2.4 Changes to the State Pension in recent years

Due to concerns about the sustainability of the State Pension schemes it has been necessary to introduce long-term measures on these schemes. The following two changes have been initiated with the goal of improving the sustainability of the two State Pension schemes:

2.4.1 The Social Welfare and Pensions Act 2011 made a number of changes to the qualifying age for State pensions. The qualifying age will rise to 67 in 2021 and 68 in 2028. So:

- For those born on or after 1 January 1955 the minimum qualifying State pension age will be 67.
- For those born on or after 1 January 1961 the minimum qualifying State pension age will be 68.

As part of this process, the State Pension (Transition) is no longer available to people who reach 65 on or after 1st January 2014. In addition, rate of Invalidity Pension for those aged 65 was reduced to €193.50. This brings it into line with payments for those aged below 65. The rate of payment increases to €230.30 at age 66, to match the State Pension (Contributory). This is estimated to save in the region of €140 million.

2.4.2 The Social Welfare and Pensions Act 2012 changed the level of contributions required to claim a contributory State Pension. If a claimant reaches pension age on or after April 6 2012, they will now need to have 520 full-rate contributions (10 years contributions) to claim State Pension (Contributory). Alternatively, if a claimant reached pension age on or after 6 April 2002, they needed to have 260 full-rate contributions (effectively 5 years contributions) and if the claimant reached pension age before 6 April 2002, they needed 156 qualifying full-rate contributions (3 years contributions).

2.4.3 The Social Welfare (Consolidated Claims, Payments and Control) (Amendment) (No. 8) (Reduced Rates) Regulations 2012 made a number of changes to the rates of payment for the State Pension (Contributory) scheme, based on the average number of yearly contributions over the working career. Table 4 below details the changes in the rates of payment for State Pension (Contributory) recipients from September 2012. The Regulations effectively reduced the payments to new entrants that had an average of less than 40 PRSI contributions per year. This was estimated to have full year savings of €17 million.

Table 4: Rate changes on State Pension (Contributory) from September 2012

State Pension (Contributory) rates for people who qualify for pensions from 1 September 2012

Yearly average PRSI contributions	Personal rate per week, €	Increase for a qualified adult (under 66), €	Increase for a qualified adult (over 66), €
48 or over	230.30	153.50	206.30
40-47	225.80	146.00	196.00
30-39	207.00	139.00	186.00
20-29	196.00	130.00	175.00
15-19	150.00	100.00	134.00
10 to 14	92.00	61.00	83.00

Source: Citizens Information – State Pension (Contributory) website

From 1 September 2012, the rate band 20-47 was replaced by the bands 20-29, 30-39 and 40-47. This means that those with average yearly contributions lower than 40 would receive a lower amount of State Pension (Contributory). For example, new entrants who had an average of 33 contributions per year would now receive €207 per week, as opposed to €225.80 per week before this reform.

2.5 Further proposed changes under the National Pensions Framework

Under the National Pensions Framework a number of other changes to the qualifying conditions for the State Pension (Contributory) were envisaged from 2020). Legislation is required before these changes come

into effect. The main change proposed is the introduction of a total contributions approach to replace the current yearly averaging system. This means that the amount of pension paid will be directly proportionate to the number of social insurance contributions and/or credits recipients have made over their working lives.

So if the person was born after 1 January 1954 and when they reach pension age, they will need a total of 30 years contributions and/or credits to get the maximum State Pension. They will be able to get the minimum State Pension if they have paid 520 full-rate contributions (10 years). The minimum pension will be one third of the maximum rate. The recipient can then get a further 1/30th of the pension for each additional year of contributions that they have made. The maximum number of credits that can be used in calculating the entitlement to State Pension will be 520 (or 10 years).

2.6 The OECD review of the Irish Pension System

In 2013, DSP commissioned the OECD to review the Irish pensions system. Their report supports the proposals under the National Pensions Framework with regard to the total contributions approach. It also recommends one of two options for more fundamental reform of the State Pension system which is to either move to a universal basic pension scheme (with strict means-tests for HHB and free travel) or a single means-tested pension as follows:

Option 1: a universal basic pension scheme

- A universal basic pension scheme for the entire population would be based on residency requirements, provide a single flat-rate benefit and cover all of the Irish population, regardless of their life-time work or contribution status. It could be financed by taxes, contributions or a combination of the two.
- A basic pension scheme could be complemented with either mandatory private pension provision or auto-enrolment into private pension schemes. Participation could be targeted at workers above a certain income level as workers on low earnings would already be receiving a comparatively high replacement rate through the basic pension.
- The household benefits package and free travel scheme could either be transformed into a cash supplement and merged with the basic pension or it could be awarded to pensioners who need the extra benefit as a means-tested cash supplement.
- Setting the level of such a basic pension for all citizens in order to meet the twin goals of social adequacy and financial sustainability would require more detailed analysis, including the costing of alternative revenue scenarios.

Option 2: a single means-tested pension

- An alternative would be a single means-tested pension financed out of general revenue. The household benefits package, the free travel scheme, and other means tested "advantages" would be included in the pension amount.
- The main design issues to be addressed under such a scheme would again be the appropriate level of the means-tested benefit, at what schedule the benefit should be withdrawn for higher earnings, what type of administrative arrangements would be needed and how much this scheme would cost under alternative scenarios.
- Combining the public and the private pension pillars, a means-tested scheme would function in combination with mandatory participation in private pension plans. In a voluntary scheme, even with an auto-enrolment mechanism, there would be disincentives to contribute to a private pension, unless a certain amount of pension savings were exempted from the means-test for low earners.

2.7 Poverty statistics 2007 – 2012

As highlighted in the sections above, the rates of State Pension payments have been protected to a large extent since the beginning of the downturn in 2008. During this time, the levels of social welfare payments to other age cohorts have been reduced significantly to help reduce the fiscal deficit in expenditure. The table below highlights the impact this has had on the different age cohorts between 2007 and 2012. Since 2008, those aged 65 and above have had the lowest at-risk of poverty rate of all the cohorts and they have consistently been below the state average. The at-risk of poverty rate dropped 4.5 percentage points between 2007 and 2012, compared to a drop of 1.1 percentage points for those 17 or younger and a 1.4 percentage point increase for working age people. Between the years of 2009 to 2011, the at-risk of poverty rate was below 10%. Throughout these years the at-risk of poverty rate for those aged 0 to 17 has remained consistently high at around 18-19% and the at-risk of poverty for working age people has increased significantly from 2008 to 2012. This highlights the results of the Government focus on protecting those of pension age, but also highlights the impact on other age cohorts from following such a policy.

Table 5: At-Risk of Poverty rate by age groups

	2007	**2008**	**2009**	**2010**	**2011**	**2012**
Aged 0-17	19.9%	18.0%	18.6%	18.4%	18.8%	18.8%
Aged 18-64	15.0%	13.3%	13.0%	14.2%	15.9%	16.4%
Aged 65 +	16.6%	11.1%	9.6%	8.7%	9.7%	12.1%
Total	**16.5%**	**14.4%**	**14.1%**	**14.7%**	**16.0%**	**16.5%**

Source: CSO EU-SILC data

We also looked at the at-risk of poverty rates by household composition type (table 6) to see if different groups of retired households were impacted differently. We can see that the two groups of retired

household types are very similar in terms of at risk of poverty rates at around 13% in 2012. These cohorts fare significantly better than single adult families of working age and other households with children.

Table 6: At Risk of Poverty Rate (%) by Household Composition and Year

	2010	**2011**	**2012**
1 adult aged 65 years and over	8.0%	9.1%	12.9%
2 adults, at least 1 aged 65 years and over	8.6%	8.9%	13.0%
1 adult aged less than 65 years	19.2%	24.3%	27.1%
2 adults, both aged less than 65 years	12.6%	12.5%	12.4%
3 or more adults	8.8%	11.7%	13.4%
1 adult, with children under 18 years	24.7%	28.4%	29.1%
2 adults, with 1-3 children under 18 years	14.4%	14.6%	13.9%
Other households with children under 18 years	20.7%	21.2%	21.5%

Source: CSO EU-SILC data

2.8 Population Projections to 2026 and implications for State Pension schemes

The trend in both volume and expenditure has increased quite markedly in recent years as highlighted in the analysis above. This trend in volume is expected to continue to increase as indicated in the CSO "Population and Labour Force Projections, 2016-2046" paper published in April 2013, with those aged 65 and over estimated to increase to 855,000 in 2026 from around 570,000 in 2013. Using these growth projections, we have calculated an estimate of the likely cost of State Pension schemes expenditure if everything else remained unchanged. The analysis highlights that under a 'no change' scenario, the expenditure on these two schemes could reach around €7.5 billion by 2026 in nominal figures. This is an increase of **€2.36 billion** on the current allocation in 2014 of €5.1 billion, and represents an estimated annual increase of **€195 million per year** out to 2026. For completeness, we also calculated an estimate of the real increase in State Pension scheme costs if the payments were to remain the same and prices were to increase by an average of 2% per year. We found that the costs of these schemes would increase by around €700 million in real terms between 2013 and 2026. This increase in real costs is due to the population of retirees increasing faster per annum than the price increases (average of 3.2% versus 2% respectively).

What will be of particular concern is that the expenditure figures above take account of the increase in qualifying age for State Pension schemes from 66 to 67 in 2021. This measure is estimated by us to reduce expenditure in 2026 by €150 million on what would have been spent if no reform had been put in place.

With these levels of expected growth in the medium term, it is vital that State Pension provision is maintained at a sustainable level. Under the new EU 'Sixpack' framework, stricter controls have been put on what countries are allowed to spend and demographic pressures will likely have to be dealt with through structural reforms to ensure expenditure limits are not exceeded. For these reasons, pension expenditure has to be considered as a priority area for reform in the coming years.

2.9 Supplementary Payments

In addition to the basic weekly State Pension payments, claimants on these schemes also may be entitled to supplementary payments once they meet certain criteria. The main schemes are the Household Benefits Package, Free Travel and Fuel Allowance.

Household Benefits Package

The Household Benefits package is a universal scheme for those aged 70 and over irrespective of means. Additionally those on State Pension aged between 66 and 70 are entitled to the Household Benefits Package if they live alone or only with excepted people[2]. The Household Benefits Package comprises of 3 schemes (formerly 4) with 2 allowances which provide a free service to claimants. The 3 schemes are:

Allowance 1: Choice between scheme (i) or (ii)

The Electricity Allowance (Cash or Credit)

The Electricity Allowance is a cash credit paid each month. It is applied directly as a credit of €35 on the bill for Electric Ireland customers. If the electricity provider is **not** Electric Ireland, the Electricity Allowance is paid directly to the client to use towards their electricity bill.

Natural Gas Allowance (Cash or Credit)

Depending on the supplier, the Natural Gas Allowance of €35 can be paid as a cash credit on the gas bill or on the first Tuesday of each month to an account in a financial institution or a post office.

[2] Excepted people include:

- A qualified adult (if he or she earns less than €310, including income from a social welfare payment)
- Dependent child(ren) under the age of 18 or under the age of 22 if in full-time education.
- A person who is so incapacitated as to require constant care and attention for at least 12 months.
- A person(s) who would qualify for the allowance in his/her own right
- A person who is providing you or someone in your household with constant care and attention if you or that person is so incapacitated as to require constant care and attention for at least 12 months.

Allowance 2: **The Free Television Licence**

Once a person qualifies for the Household Benefits Package, they become eligible for a Free Television Licence from the next renewal date of your television licence. The licence is equal to €160 per annum.

Allowance 3: Water Support Payment

In addition to the two current allowances that are in place, the Government decided in May 2014 to introduce a new allowance funded through the Household Benefits Package which will provide an extra €100 per annum for the purpose of alleviating the costs of the new water charges. This will take the form of a cash payment for those who already qualify for the Household Benefits Package and will come into effect from 1 January 2015.

Free Travel

The Free Travel scheme is a universal scheme available to everyone aged 66 and over living permanently in the State. Free travel is available on Iarnród Éireann, Bus Éireann, Dublin Bus, Dart and Luas Services and on certain private bus and ferry services. It is also possible to travel free of charge on certain cross-border services between Ireland and Northern Ireland. There are no restrictions on the times at which the Free Travel Pass can be used. Therefore, there is no need for unrestricted passes, permitting free travel at peak times.

In addition to the main travel pass, if the person with the Free Travel Pass is married, in a civil partnership or cohabiting, they are entitled to a Free Travel Pass which allows their partner to accompany them free of charge when travelling (Spousal Pass). Also, some people who are unable to travel alone may get a Free Travel Companion Pass. This allows the holder to be accompanied by any person over 16 years of age, free of charge. The cost of the Free Travel pass is estimated at an average of €100 per annum per pass holder.

Fuel Allowance

The Fuel Allowance is a means-tested supplementary payment which people on Pension schemes may apply for. The fuel allowance is worth an additional €20 per week for 26 weeks from October to April and assists those with a heating need to pay for fuel. Accordingly, it is worth **€520 per annum** for those who qualify.

Means test for Fuel Allowance

The Fuel Allowance means test is linked to the maximum rate of the State Pension (Contributory). A person on a State Pension can have a weekly income of €100 above the maximum State Pension (Contributory) and still be eligible for a Fuel Allowance. In addition, a person can have capital/savings providing they are less than €58,000, and also be eligible for a Fuel Allowance. For example:

- The assessable income limit for a single person under 80 is €330.30 (€100 plus €230.30). If they are over 80, then an extra €10 is added to the appropriate DSP payment rate.

Living Alone Allowance

The living alone allowance is an extra payment for those who are living alone. The payment is worth an additional €7.70 per week. This is not means-tested and is only paid to people who receive a qualifying DSP payment which includes State Pension (Contributory and Non-Contributory). As table 6 above shows, single people aged 65 or over face lower at risk of poverty rates than the average household type and significantly lower rates than single adult households of working age.

Expenditure on Supplementary Benefits

Table 7 details the numbers on the two State Pensions schemes that are in receipt of the supplementary payments listed above. In addition, the approximate rate/value per annum of these benefits are detailed below. From this, it is estimated that the secondary benefits for the State Pension schemes cost an additional **€270 million** per annum on top of the €4.9 billion cost of the primary pension scheme payments.

Table 7: Supplementary payments

	Value per annum	Numbers in Receipt	
		State Pension (Contributory)	State Pension (Non-Contributory)
Free Electricity	€420	145,633	53,638
Free TV license	€160	168,264	56,906
Gas Allowance	€420	21,367	2,522
Free Travel	€100*	266,637	95,977
Fuel Allowance	€520	66,600	53,400
Living Alone Allowance	€400	62,234	32,969

Source: 2012 Statistical Information on Social Welfare Services.

* This is an estimate of the average cost per person per annum. The value per person will vary depending on usage. Usage data in relation to the Free Travel Pass is not currently available.

Trends in Expenditure on Supplementary Benefits

In recent years, the measures that have been taken to reduce secondary payments, with the ultimate aim of focussing primarily on primary payment, have meant that expenditure on Supplementary Benefits has reduced in recent years. Table 6 shows the trends in the last 10 years on these schemes, with the expenditure falling from the peak of €711m in 2011 to €515m in 2014 (a 28% reduction). The table does not include expenditure on the Living Alone Allowance which is estimated to amount to €72m in 2014.

It is clear, however, that spending on Supplementary Benefits has increased significantly from 2003 to 2014, with a 51% increase in expenditure in this time. It is important to note that not all of this expenditure relates to people on State Pension schemes. About 70% of all spending on Household Benefits and Free Travel relates to pensioners, the rest relates to people in receipt of Illness and Disability payments. In the case of the Fuel Allowance scheme, about 40% of recipients are of retirement age, with the remainder of claimants on a range of working age schemes (including Long-Term Jobseekers, Lone Parents and those with Illness or Disability).

The table below does not include the new proposed Water Affordability element of the HHB which will be introduced from 1 January 2015 and which will give rise to additional costs on the HHB of €42m. This will take the form of a cash payment for those who already qualify for the Household Benefits Package.

Table 8: Payment trends, 2003 to 2014

	2003 € m	***2004 € m***	***2005 € m***	***2006 € m***	***2007 € m***	***2008 € m***	***2009 € m***	***2010 € m***	***2011 € m***	***2012 € m***	***2013 € m***	***2014 € m***
Electricity Allowance	75	88	104	108	147	157	166	172	179	177	158	153
TV License	44	48	46	49	52	56	56	58	58	58	59	54
Telephone Allowance	83	86	89	90	99	112	120	119	112	114	48	3
Gas	5	6	6	9	15	16	18	20	21	21	19	20
Free Travel	50	52	55	58	64	68	73	74	76	76	77	77
Fuel Allowance	83	85	82	130	158	170	200	229	266	211	211	208
Total	**341**	**364**	**383**	**444**	**536**	**579**	**632**	**671**	**711**	**656**	**572**	**515**

Source: 2012 Statistical Information on Social Welfare Services. Revised Estimates Volume 2014.

The universality of many of the Supplementary Benefits is an obvious concern. It means that resources are not as tightly focused on the most vulnerable as they could be and this raises valid value for money concerns for the State. Furthermore, there are sustainability concerns, given that the population is expected to rise so markedly in the medium-term. At this time any proposal to remove universal entitlement to such payments must be considered. The supplementary benefits must also be considered as viable options to offset demographic pressures building in the area of pensions expenditure generally.

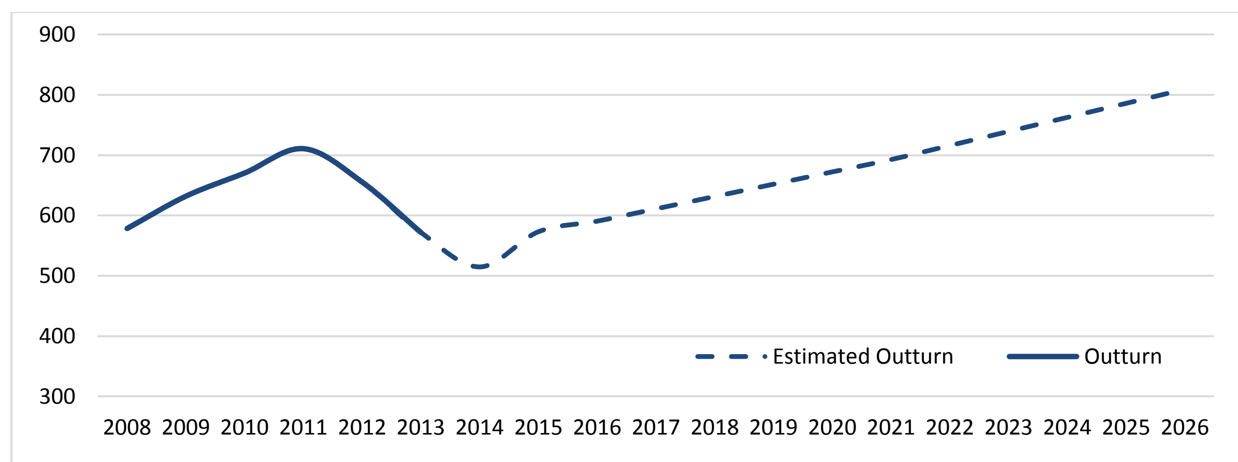
A range of expenditure reductions have been implemented in the area of pensions-related supplementary payments since the beginning of the crisis. These are summarised in the following table.

Table 9: Savings on Supplementary Benefits in recent Budgets

2014	Savings that year (€m)	Full year savings (€m)
Telephone Allowance discontinued for all recipients, from Jan 2014	44	47
Reduction in the annual payment to RTÉ for the Free TV Licence from €59.17 million to €54.17 million	5	5
2013		
Introduction of changes to the electricity/gas element of the package	20	23
Reduction in the value of the Telephone Allowance element of the Household Benefits package for new and existing recipients.	61	61
2012		
Reduction in expenditure on the electricity/gas allowances	15	15
Reduction in the length of the fuel season by 6 weeks from 32 to 26 weeks for new and existing recipients	51	51
2011		
Efficiency savings in the energy and communications elements of the Household Benefits Package	30	30
Total	**226**	**232**

The Budget measures listed above have been necessary to offset the significant expenditure pressures on Supplementary Benefits that had been growing significantly between 2006 and 2011. The graph below shows the impact of the savings measures from 2011 onwards but also shows the likely trajectory expenditure will take if no further Budget measures are taken. By 2026, we estimate that expenditure would increase to around €800 million up from an estimated €515 million in 2014. This includes the measure agreed by Government in May 2014 to provide a €100 per annum water allowance to recipients of the Household Benefits Package.

Figure 4: Estimated Expenditure Growth on Supplementary Benefits 2008 - 2026



Source: DPER Calculations using CSO Population Projections

3. Options for Structural Reform

As detailed above, the levels of people of retirement age is expected to grow in the medium term (and long-term), and it is of critical importance to the state that expenditure on pensions related schemes and supports are maintained at a sustainable level and that scarce resources are targeted in a more balanced way. Given that the estimated increase per year due to demographics alone is in the region of €200 million, there are serious concerns about the sustainability of expenditure in this area over the medium to long-term. Given the scarcity of resources, it is important that the State prioritises how its allocation is distributed to ensure that those most at need receive the greatest assistance. In addition, with Ireland coming under the scope of the new EU 'Sixpack' fiscal rules framework, the State will no longer be able to provide additional expenditure to cover increasing demographic pressures on an aggregate level. This means that the sustainability of State Pensions will likely have to be achieved through the use of structural reforms to the scheme or through increased taxation or expenditure reductions in other areas. There is a spectrum of options for improving the sustainability of state pensions and related expenditure. These range from options involving very fundamental reform of the state pensions system to those involving further adjustments to current schemes and arrangements to contain expenditure and target resources more effectively. These are articulated below.

In terms of fundamental reform, the OECD, as outlined in Section 2.5 above, have presented two possible options for long-term reform of the state pension system in order to address sustainability issues, replacement of the current state pension schemes with either *a universal basic pension scheme* or *a single means tested pension*. However, estimates of the cost savings associated with either option were not included by the OECD. DSP are currently considering all of the recommendations contained in the OECD report and will be bringing proposals to Government later this year.

Secondly, as highlighted in Section 2.4, the National Pensions Framework proposed the introduction of a total contributions approach in 2020 to replace the current yearly averaging system. This would involve switching from the current system to a total contributions system, where a person is required to make 30 years of contributions to claim the full State Pension. This measure still requires Government approval and is still subject to further discussion. DSP have indicated that estimated savings achieved by this reform have not been calculated. The possibility of introducing this ahead of 2020 should also be examined.

The following are options for consideration in the context of this Expenditure Review (within the framework of existing arrangements) which would assist in improving state pension sustainability and which would advance the welfare reform objective of ensuring limited resources are targeted in a balanced and fair way:

1. **Bringing forward increases in the Pension Age**

   An option is to bring forward the increases in the age for State Pension eligibility scheduled for 2021 (to age 67) and 2028 (to age 68) by say, 3 years. This would mean the increase from age 66 to age 67 would take place in 2018 and the increase from 67 to 28 would take place in 2025. It is estimated that this measure would yield savings in the region of **€140 million** in the three years from 2018 to 2021 and we estimate we would be spending **€170 million** less on State Pensions in 2026 than it would under the original reform[3]. Obviously there would be concerns about impacting on peoples expected dates of retirement, given that 2021 has been published as the date for the reform. However, given the expenditure pressures in the pension's area, it is a proposal that should be considered. It must be noted that while this measure will save on pension's expenditure, the full savings for DSP may not be achieved. This is because some people are likely go onto Jobseeker's at age 65 if they are not entitled to get a State Pension payment. This means some of the savings on State Pensions will be offset by an increase in Jobseekers expenditure. It is hard to quantify the numbers that would either join Jobseekers or keep working, however under a pessimistic scenario where everyone retires at 65 and joins Jobseekers, we estimate the savings in the initial year would be in the region of **€48 million.**

2. **Increase the number of yearly contributions for a full State Pension under the Total Contributions approach.**

   As detailed in Section 2.5 above, the State Pension Contributory scheme will switch from a yearly average contributions approach to a total contributions approach in 2020 as part of the National Pensions Framework. Currently, it is envisaged that once a claimant has 30 years contributions they will be entitled to receive the full state pension. However given the projected costs on State Pension schemes in future years, the option to increase the years in the total contributions approach must be considered. Therefore we are proposing that the required years to claim the full State Pension under the total contributions approach should be increased to either 35 or 40 years.

   Based on the 40 years approach, this would mean that a person would receive one quarter of the full State Pension once they have contributed the minimum of 10 years contributions (520 weekly contributions). They would then receive 1/40th of the full State Pension for each additional year of contributions. We have asked the Department of Social Protection to cost this.

[3] The population of people of retirement age is expected to grow by an average of over 3% per year in the medium term. Under a no reform scenario we would expected State Pension expenditure to increase by a similar percentage

3. **Introduce a Qualified Adult Increase on State Pension (Non-Contributory) for those spouses/civil partners aged 66 or over**

   Currently anyone over 66 who is not entitled to State Pension (Contributory) can apply in their own right for the State Pension (Non-Contributory), which is means-tested. This means that a couple who are both aged 66 and over can receive the full €219 per week based on their means. We are proposing that, similar to other social welfare schemes, one person should apply for non-contributory pension in their own right and the other would receive a qualified adult increase. Similar to other social welfare schemes, the rate for the Qualified Adult Increase is set at around 70% of the primary rate as couples benefit from economies of scale. This would mean that the new Qualified Adult Increase would be set at €153.30 per week. We estimate the savings to be €3.4 million per 1,000 impacted but we don't currently have the numbers that would be impacted by such a measure and we have asked the Department of Social Protection to cost this measure for us. If this only applies to new entrants then the savings will be significantly lower than applying to the current stock.

4. **Reduce the basic rates of the State Pension (Contributory) and/or the State Pension (Non-Contributory)**

   The option to reduce base rates must be considered in the context of ensuring the sustainability of the State Pension schemes. As can be seen in Table 10, a €1 reduction to the primary rates for the two pension schemes will generate savings of €19.7 million. If a pro-rata reduction is also applied to the increase for a qualified adult payment, then a further €3.1 million in savings can be achieved. The combined savings of a €1 reduction to the State Pension schemes and a pro-rata reduction for qualified adults is in the region of €22.8 million. Given that this paper estimates the expenditure on State Pensions is likely to increase by €195 million per year in the medium term, **a cut of €8.50 per week on the two State Pension schemes will only offset those demographic pressures for one year.**

Table 10: Indicative Cost of Each €1 Change in Personal and IQA Rates

Payment	Personal €m	Qualified Adult €m	Total €m
State Pension (Contributory)	€14.8	€3.0	€17.8
State Pension (Non-Contributory)	€4.9	€0.1	€5.0
Total	€19.7	€3.1	€22.8

Source: Department of Social Protection

5. **Discontinue the higher rate for Over-80s**

   Currently those aged over 80 get an additional €10 per week on top of the basic State Pension payment. Between 2008 and 2013, the numbers in receipt of the Over-80's allowance increased by 20% from 115,000 to 138,000. This caused expenditure to increase by an estimated €12 million for this allowance

in 6 years alone (we estimate expenditure to be €72 million in 2013). The expenditure on this allowance is likely to increase in the medium to long-term and we estimate expenditure will be in the region of €100 million by 2026, an increase of €28 million on 2013 figures. We recommend that as this is not means-tested and targeted at those most in need, then there is justification to discontinue the payment. This would save an estimated **€72 million.** The alternative to this option would be to discontinue it for new entrants. From looking at recent years there are about 3,800 new claimants each year, meaning this would save **c. €2 million** in the initial year this was introduced, but the saving would ramp up over time.

6. **Household benefits package savings options**

As things stand, expenditure on the Household Benefits Package is estimated to be €272m in 2015 (inclusive of the new Water Affordability measure recently agreed by Government). There are a range of options for further savings and reform in this area as follows:

i. **Introduce the Fuel Allowance Means test for the Household Benefits Package** - This would remove the universal element of this package and would ensure that limited resources in this area would go to those most at need and that resources are targeted in a more balanced way. As discussed above, the threshold for the fuel allowance means test is set at €100 above the State Pension (Contributory) weekly payment, therefore any person in receipt of a State Pension and less than €100 of an occupational pension would still qualify. We estimate that approximately 191,000 people would be affected by this change, and that this **would generate savings of around €127 million if introduced**. An alternative to this would be to introduce the fuel allowance means test for new entrants only. This would achieve savings of around €23 million if introduced and has the advantage of not taking the Household Benefits Package off people who currently avail of it.

ii. **Abolish the Free TV License** - The new Household Broadcasting Charge will be introduced in 2015. It may be timely to abolish the TV license aspect of the Household Benefits Package as part of the move to the new Charge which is expected to generate extra funding streams to fund broadcasters. While this would mean an increased payment of €160 per year being borne by those on the Household Benefits Package, it would ensure that they would retain the gas/electricity allowance part of the package. **Abolishing this payment would save €54 million.** The direct impact on RTE could be minimal as compliance with payment of the TV license among the general population is running at around 84%. If 84% of those currently in receipt of the Free TV license paid the €160 fee from 2015 onward, it would generate €55m for RTE. Alternatively, to means test the free TV License would save an estimated €25 million and around 190,000 people would be affected. The third possible reform in this area would be to maintain the free TV License but only

for those people also in receipt of the Living Alone Allowance. This cohort are most in need of this allowance as they are most at risk of social exclusion. This would save in the region of €25m.

iii. **Halve the Gas/Electricity Allowance by aligning to the 6 month long winter Fuel Allowance payment** – Following the rationale of the fuel allowance season, there are only certain times of the year where people face higher than usual energy bills. Therefore, it could be argued that an energy subsidy could be limited to the six month winter season only. This measure would deliver savings in the region of **€87 million** and would impact on all persons in receipt of the Household Benefits Package.

7. Reform the Free Travel Pass

Free travel is also a universal scheme available to those aged 66 plus and has also faced criticism for not being targeted at those most at need. There is also no reliable data on the level and nature of usage under the scheme by beneficiaries so it is hard to gauge the value of the Pass to recipients or the degree of abuse/misuse through inadequate control. The introduction of the Public Service Card should address the issue going forward. Nevertheless, there a range of possible measures which could be considered which would tighten up the scheme and reduce expenditure. An interdepartmental group is currently reviewing the Free Travel scheme and will publish their findings in due course. The main options for reform detailed below reflect the views of this paper alone:

i. **Spousal and Companion Passes –** There are strong arguments in terms of both equity, economy and combating abuse of the Scheme for abolishing both the spousal and companion passes. For example, a Spousal pass may be provided regardless of the spouse's age or financial position – the spouse may well be in full time employment. Furthermore, the impact of abolishing the Spousal pass is not as serious as it might seem. More than half of beneficiaries are aged over 66 and, therefore, entitled to a Free Pass in their own right. Therefore, only those aged under 66, i.e. of working age, would lose out. Given the need to ensure that scarce resources are targeted solely at those in genuine need of assistance, it is difficult to justify maintenance of these aspects of the Scheme. Those with greatest medical need and who are genuinely unable to travel alone are likely to have a full time carer who will continue to be eligible for a free travel pass in their own right. Abolition of the Companion Pass would save **€3 million.** Abolition of the spousal pass would save a further **€11.5 million**.

ii. **Apply a fuel allowance means test to Free Travel Recipients** – The purpose of this would be to remove the universal aspect of the Free Travel scheme and to ensure that finite resources are targeted at those most in need of assistance. The drawback of this would be the increased

administrative burden on DSP that would result from means-testing 1.2 million current recipients plus new people applying to join the scheme. However, we estimate that applying the means-test to all customers could save around **€29 million** and would mean that resources are better targeted.

iii. **Introduce an annual charge of €50 for use of the Free Travel pass** – An annual charge of €50 would bring in almost **€62 million** if levied on all 1.2 million Free Travel cards. This equates to €1 per week and it could be argued represents a modest contribution given the value of the benefit derived from the pass by many recipients.

Table 11: Reform options for the Free Travel Scheme

Reform Option		Numbers Affected	Indicative Saving:
Abolish Free Travel	Primary Recipients	771,147	€62.5 million
	Spouses	375,616	€11.5 million
	Companions	90,692	€3 million
	Total	1,237,455	€77 million
Fuel Allowance Means Test	Primary Recipients	280,000	€17.4 million
	Spouses	135,000	€8.4 million
	Companions	35000	€2.9 million
	Total	450,000	€28.7 million
Annual Charge of €50	Spouses	375,616	€18,780,800
	Companions	90,692	€4,534,600
	All Recipients	1,237,455	€61,872,750

The impact of any measures adopted to reduce expenditure on the Free Travel Pass on the finances of CIE Group would need to be further considered.

8. Reform the Living Alone Allowance

As discussed in Section 2, the Living Alone Allowance is a non-means tested payment that is paid out to those living entirely alone. It provides for an additional €7.70 per week on top on the qualifying payment. As also highlighted above, single people aged 65 or over face lower at risk of poverty rates than the average household type and significantly lower rates than single adult households of working age. Between 2008 and 2013, the number of pensioners on this allowance increased by 10,000 or 7% and there are now around 145,000 pensioners availing of the allowance. We would recommend that this allowance be means-tested to ensure that finite resources are targeted at those most in need. The options are laid out as follows:

i. **Means testing for all –** There are currently 145,000 availing of this allowance. If we apply the fuel allowance means test to this cohort we estimate about 47% of this cohort will lose entitlement[4] and therefore about 67,700 will lose entitlement to the Living Alone Allowance. This would generate savings of around **€27 million** if introduced.

ii. **Means-testing for new entrants –** The alternative would be to means test just new entrants for the allowance. We estimate that this would mean around 700 people per year would not be entitled to get this payment, saving **€300,000** in the initial year but with savings ramping up over time.

9. Revenue raising measures

One alternative to reducing expenditure allocated towards State Pensions would be to increase PRSI contributions to fund the Social Insurance Fund (SIF). The latest actuarial review of the SIF, undertaken for DSP by KPMG, looked at the necessary levels to fund the SIF at breakeven without the need for a subvention from other exchequer funds. These are detailed in table 12 below. KPMG use 2013 as the base year for their calculations for the breakeven scenarios and they look at four separate time periods. They estimate that if we require the SIF to be self-funded to 2018, then PRSI revenue needs to be 128% of the current revenue, factoring in predicted growth in wages and employment. On a longer term period from 2013 to 2066, the SIF would require increases in revenue to be 187% greater than a no change scenario. This means the short-term employee (employer) PRSI rates would increase to 5.1% (13.8%) to fund the SIF out to 2018, and the long term employee (employer) rate would increase to 7.5% (20.1%) out to 2066.

Table 12: Increase in PRSI revenue required to balance the SIF

Starting	No Subvention	Indicative Class A rates
Equalised Contributions for 5-year period (2013-2018)		
2013	128%	Employee: 5.1% Employer: 13.8%
Equalised Contributions for 10-year period (2013-2023)		
2013	132%	Employee: 5.3% Employer: 14.2%
Equalised Contributions for 20-year period (2013-2033)		
2013	139%	Employee: 5.6% Employer: 14.9%
Equalised Contributions for whole projection period (2013-2066)		
2013	187%	Employee: 7.5% Employer: 20.1%

Source: KPMG actuarial review of the SIF 2010; published September 2012; Assumed top rate for employer.

[4] This is the same percentage of Household Benefits recipients that qualify for the fuel allowance.