State should cap pension relief instead of cutting it

COMMENT

Gerry Hassett

Incentives exist because people respond to them. People are more likely to do things if you make it attractive enough. Taking away incentives may save money – but what if it comes at the cost of people no longer doing what you need them to do?

When the famous Special Savings Incentive Account (SSIA) scheme stopped offering a €1 bonus for every €4 saved, people closed them and did something else with their money.

Taking away a very useful and far-sighted incentive – tax relief on pension contributions – would cost Irish taxpayers far more in the long run than it would save today.

Right now, the government needs people with no pension to save for their retirement. If these people don't save enough, the state will have to pick up the tab.

To make it worth their while, the government currently offers a great incentive. If you're a top-rate taxpayer, the government gives you a top-up of €69 for every €100 you save.

It makes sense. The state gives you an incentive now that will make its burden easier in the future. It's a win-win for everyone. You get a top-up today; the state benefits because you won't be as much of a burden when you retire.

Cutting the current incentive would mean that, if you're a top-rate taxpayer, your government top-up will drop from €69 for every €100 saved to €25. Put another way, it will force you to pay 35 per cent more just to maintain your existing contribution level.

In the short term, this could save money. In the long term, it could cost a lot more.

People won't respond to a reduced incentive by paying more into their pensions. Irish Life research shows that 43 per cent of our pension customers will respond in a different way – by giving up on their pension altogether or reducing the amount they save.

Cutting the incentive could have a devastating impact on retirement planning. The burden on the state could increase to breaking point.

Of course, it's tempting to say that everyone knows the state needs money today and that we can worry about the problems of tomorrow some other time. But it doesn't have to be like this.

Irish Life, Ireland's biggest pension provider, has a better idea than cutting pension incentives that can raise just as much money for the government. Instead of hitting 500,000 middle-income earners with reduced incentives, leave these incentives intact and adopt a different approach.

We believe that the government could raise the same amount by capping the pension tax relief for 30,000 high earners.

This would mean middle-income earners won't lose out and can continue saving for their retirement with the incentive they currently get.

It would mean the government gets the savings it's looking for without putting at risk existing incentive arrangements that are working and delivering real benefits to the state.

Capping reliefs is a much more equitable solution to the government's problem. It's a system that works in Britain. It makes scarce relief available to everyone in the middle-income band and closes perceived loopholes for the wealthy.

Gerry Hassett is chief executive of Irish Life Financial Services, Ireland's biggest pensions company