



Representative Association of Commissioned Officers
Cromhlachas Ionadaitheach na nOifigeach Coimisiúnta



Mr. Kevin Duffy.
Chairman Public Service Pay Commission.
Stephens Green House,
Dublin 2.

03 April 2017

RACO Submission to the PSPC

Reference 'A': DPER Pension Report dated 30 March 2017.
'B': RACO submission to PSPC dated 13 March 2017.
'C': Report by Trident Consulting (Independent Actuarial Consultants)
dated 03 April 2017

Dear Chairman,

1. RACO's submission to PSPC was presented on 23 November 2016 in accordance with the Terms of Reference and invitation to contribute. At our meeting on 19 December 2016, RACO discussed our submission with the Commission while also submitting an additional paper highlighting key differentiators between the conditions of service of Defence Forces Commissioned Officers relative to that of Public Servants and Private Sector Employees. RACO identified that key differentiators of military service are particularly relevant where the PSPC may be evaluating pay & superannuation arrangements.
2. RACO's follow-on submission to the PSPC on 13 March 2017 supported our position (Trident Actuary Report 28 February 2017) regarding the impact of forced early retirement from the workforce at ages well in advance of 66-68. RACO emphasised the monetary impact, both pay and pension pay, that places a Defence Force Officer at a distinct monetary disadvantage to equivalent grade Public Servants and Private Sector earners.
3. RACO also identified that the Single Pension Scheme for new entrants since 2013 failed to recognise the impact of forced early retirement and the impact of career average earnings. The impact of these factors on Defence Forces Officers are punitive and questions again the failure of our unique Industrial Relations arrangements that precluded our Association from consultation and negotiation, similar to arrangements afforded to unions affiliated to the ICTU. Also of great disappointment is the obvious failure of our employers, the Department of Defence, to represent the Defence Forces interests where they clearly recognise the impact of forced early retirement (CCR 421 – previous submission dated 13 March 2017) but did not secure the necessary terms of agreement to minimise the monetary impact of the SPC model. *The current trend in voluntary exit are proof of the impact of inadequate policies.*

4. Our previous submission, reinforced by independent actuary consultant's report (RACO Trident Report dated 28 February 2017), identified the following significant differentiators which RACO have requested the PSPC to consider;
- a. Forced early retirement age *is not a benefit to the individual*. Forced early retirement age are a prerequisite of military organisation and only of benefit to the Defence Forces organisation to ensure military personnel are "fit for the duties they perform". Government policy directs compulsory retirement at ages from 54-60 for Defence Force Officers.
 - b. Compulsory retirement ages from 54-60 fail to provide a career earning potential equivalent to other Public Servants who serve to 66-68 years. This earning potential deficit, relative to Private and Public Sector equivalents, can be anywhere in the region of 10%-19% negative depending on the rank. This earning potential shortfall comes at a point where 30-year mortgages and the ability to support a child's 3rd level education is *seriously compromised by forced early retirement ages*.
 - c. In total, a Defence Force Officer is projected to receive **€1.02m to €1.77m** lower remuneration over their lifetime factoring pay plus pension (less pension contributions) than an equivalent grade public servant retiring at 68 years of age.

Pre-01 January 2013- Final Salary Based

- i. **13% less** for a final salary member where the supplementary pension arrangement is not applied.
- ii. **10% less** for a final salary member allowing for the payment of the supplementary pension where meeting the Defence Sector criteria as outlined in CCR 421- Annex 'C' (see Ref 'F').

Post 01 January 2013- Single Pension Scheme Member

- i. **19% less** for a single scheme member where the supplementary pension arrangement is not applied.
- ii. **15% less** for a single scheme member allowing for the payment of the supplementary pension where meeting the Defence Sector criteria as outlined in CCR 421- Annex 'C' (see Ref 'F').

In an organisation suffering from the high loss and continued exodus of specialist and career professionals, the cost benefit of retaining such military expertise which can take 2-5 years to safely develop, is a factor that should be considered by the PSPC. The medium and long term remuneration issues identified in our submissions to the PSPC will undoubtedly magnify the current manning crisis.

5. Evaluation of DPER's Pension Report dated 30 March 2017

Factoring RACO's previous submissions relative to the most recent Pensions Report released by DPER (30 March 2017), the following observations are submitted to the PSPC for reflection when considering Defence Forces pay and superannuation arrangements for Commissioned Officers;

- a. **Pay:** The failure of the DPER Report to factor the pay element and the "total remuneration" (pay and pension) where Defence Force personnel are forced to retire early from the workforce is seen by RACO as a very significant omission from this report when evaluating the respective sectors.

The reports omission on the pay element questions the validity of the reports application to Defence Force members considering the very significant impact with respect to our unique forced early retirement and impact on career pay. DPER have failed to recognise the significant negative monetary implications of Defence Force service timelines. RACO, in our submissions to the PSPC, identified the monetary impact (pay & pension) of forced early retirement on Defence Force personnel – see submission dated 07 March 2017.

- b. **PRD:** The position of DPER not to factor the PRD is considered by RACO as an unfair reflection of the "real" or total employee contribution to their superannuation arrangements. Given the exclusion of annual salary comparison in the DPER report, the PRD must in our opinion be treated as a pension contribution. The alternative would be to treat it as a pay cut if total earnings were being compared. Unless the PRD is being considered for immediate removal, DPER's report and the exclusion of PRD value from Public Sector Pay, is seen by our Association as a clear anomaly. Irrespective of the legal classification, PRD is, without any doubt, a significant loss of pay to those concerned.

- c. **Applying current market conditions without sufficient recognition that future market conditions will differ.** Without the time to fully assess the assumptions used in the DPER report, we would query the long-term validity of a post-retirement discount rate of 2% p.a. plus the assumption of pay parity pension increases. It appears unlikely that changes in market conditions over coming years will trigger an adjustment of pension costs and hence pay. Secondly, if public servants are being told through the DPER report that future pension increases on a pay parity basis reflect Government policy, then this should be formalised

- 6. In support of our observations, please find attached Trident Consulting Report dated 03 April 2017. Trident Independent Actuarial Consultants, were commissioned by RACO to analyse DPER's Report as it reflects on the

circumstances in respect to Defence Force Officers. This report is attached (see ref 'B') and constitutes our Association position and response to DPER's Report dated 30 March 2017.

7. The Trident Report findings again challenge the perception of Public Service pay & superannuation benefits as they apply to Defence Force Commissioned Officers. These findings reinforce the negative impact of "forced early retirement" on the financial viability of career service in the Defence Forces. This report identifies clear and unique financial distinctions with respect to the implications of "forced early retirement" on commissioned officers relative to other Public Servants and Private Sector Employees and the continued failure by Government policy to recognise, factor and address these obvious anomalies in pay and pension arrangements of our members. *RACO have been excluded from pay and pension negotiations where those unions affiliated to the ICTU have direct influence.*
8. In summary, it is clearly evident that forced early retirement age *is not a benefit to the individual* but is, in fact, a significant negative factor on those who commit to Defence Forces career service. Mandatory retirement from the workforce at ages which preclude continued employment in other sectors are a factor which should be recognised in the design of pay & superannuation arrangements of military service. When benchmarked against other Public Servants, not only in career salary but additionally with respect to the rate of pension pay on retirement, the financial implications are stark. Unless addressed in the short term, *these issues will certainly impact on the future viability of career service in the Defence Forces and the retention of expertise in which the Defence Forces has heavily invested.*
9. **RACO request the PSPC to reflect on the significant impact of recent Government policies on the remuneration (pay & pension) of Defence Force Officers. The failure of DPER to recognise and factor the negative retirement age conditions of military service is ill-considered and punitive to those who serve in the Defence Forces. The failure to balance and provide for this financial inequity in the Single Pension Scheme, either by accident or design, must be addressed if the Defence Forces are to retain a professional workforce capable on delivering state outputs. Recent HR issues in this context reinforce our Associations position.**
10. RACO request that the PSPC factor these key service issues when evaluating Defence Force pay and superannuation arrangements in the context of the Public and Private Sector. The negative remuneration (pay & pension) impact of Defence Forces officers separates our service terms & conditions from the average Public Servant or Private Sector employee. *DPER's review of pensions failed to identify this significant finding.* Attracting and retaining the best candidates for the commissioned ranks of the Defence Forces must be cognisant of the increased and rigorous demands of military service, limitations imposed by commitment to a career in military service relative to conditions offered by other more attractive Public Service and Private Sector appointments.

11. RACO wishes to thank the Chairman and Members of the PSPC for their invitation to discuss the associations submission and their engagement on issues identified in our submissions. The Association is available to discuss any matter relating to our submissions at your convenience.

Yours sincerely,



P.P. (Earnán Naughton)
Commandant
o/ General Secretary RACO

Response to the
Department of Public
Expenditure and Reform
Technical Paper by the
Defence Forces
Commissioned Officers

3 April 2017

1. Introduction and purpose of report

The purpose of this report is to respond to the Department of Public Expenditure and Reform Technical Paper entitled “Actuarial Review of Pension Provision in the Irish Public Service and a Comparison with the Private Sector” commenting in particular on matters of concern to the Defence Forces Commissioned Officers.

We note that this report was issued by DPER on 30th March 2017, with responses required by 3rd April 2017. It is unusual in our experience for interested parties to be given such a short timeframe to comment on a paper which is potentially of importance.

We note further that the pensions of Defence Force Officers are not directly valued in the report. Given the accelerated accrual that applies to Defence Force Officers, we have analysed the **Fast Accrual: Garda** category as the most directly comparable, although there are differences between the two.

For the purposes of our calculations, the rank of Commandant is used with a forced retirement age of 58. The rank/grade equivalent with the Public Service is as follows;

Commandant = [HEO+APO] / 2

2. Earnings Compensation

Our most fundamental objection to the report is the exclusion of annual salary as part of the career earnings compensation. Given the early forced retirement ages of the Defence Force Officers, a shorter career span has the following consequences:

- Lower career earnings.
- Lower pension entitlement as pension is based on lower retirement earnings.
- The ability to borrow money for house purchase is curtailed by calculations of ability to pay over a shorter time horizon. This may become more of a problem going forward as the average age of home formation has increased significantly in recent years.

We have not factored into our report issues such as curtailed ability to borrow money but such factors should be taken into account by decision makers.

Based on a forced retirement age of 58 for the rank of Commandant in the post 2004 category, and the assumptions per our report of 1 March 2017, we estimate that a Defence Force Officer is projected to receive €495,000 less remuneration over their lifetime taking into account pay plus pension less pension contributions (ignoring future salary and pension increases) than an equivalent public servant who retires at age 68. This ignores the supplementary pension.

Allowing for future salary inflation and pension increases, the (undiscounted) differential is €1.31m.

Adjusting the annual position for the present value of money, the total value of remuneration for this accelerated accrual employee retiring at age 58 is 13% less than that of an equivalent public servant retiring at age 68.

Looking at total earnings for a similar Officer who is a member of the post 2013 scheme, they are projected to receive €665,000 less remuneration (ignoring future salary and pension increases) over their lifetime taking into account pay plus pension less pension contributions than an equivalent public servant who retires at age 68. Allowing for future salary inflation and pension increases, the (undiscounted) differential is €1.77m.

Adjusting the annual position for the present value of money, the total value of remuneration for this accelerated accrual employee retiring at age 58 is 19% less than that of an equivalent public servant retiring at age 68.

3. Review of Pension Costs

We have compared the post-2004 and post-2013 Garda costs from the DPER Report with pension costs arising based on the assumptions in our report of 1 March 2017 for a Commandant retiring at age 58.

There are a number of differences between the Garda details and those appropriate for the Defence Force Officer, being:

	DFO Accelerated Accrual - Trident	Garda Fast Accrual - DPER
Retirement Age	58	55
Age at Entry	24	25
Salary Scale Post 2004	€18,442 at 24 to €77,266 at 58	€28,400 at 25 to €60,000 at 55
Salary Scale Post 2013	€16,854 at 24 to €73,325 at 58	€28,400 at 25 to €60,000 at 55

The salary scale for the Defence Force Officer approximates to 4.3% p.a. increases over a career, with that for the Garda being 2.5% p.a. over their career. These differences will impact on the comparison of pension costs below.

Post 2004 Pension Cost Comparison

The pension costs can be compared as follows:

Post-2004	DFO Accelerated Accrual - Trident	Garda Fast Accrual - DPER
Total Cost (% of Salary)	30.50%	57.00%
Normal Employee Contribution	5.00%	4.00%
PRD	5.20%	4.00%
Employer Contribution Rate	20.30%	49.00%

Retirement at age 58 (our assumption) versus age 55 (DPER) would for example be a significant element of the difference. 34 years' service to earn a full pension (our assumption) versus 30 years would be a further element.

The supplementary pension has been ignored in the DPER report and therefore we reflect above our costs ignoring the supplementary pension.

This represents a material differential, with the employer contribution rate for the Garda costs per the DPER report being almost 2.5 times as high as our DFO pension costs. If we look at the DPER costs where pension increases are linked to CPI rather than pay parity (CPI being consistent with our pension increase assumption), the DPER costs reduce by 8%, giving a net employer contribution rate of 41%.

It is inappropriate in our view for continued uncertainty regarding the basis of future pension increases. If pensions are to be valued on a pay parity basis, then a commitment to provide such increases should be given.

Given the exclusion of annual salary comparison in the DPER report, the PRD must in our opinion be treated as a pension contribution. The alternative would be to treat it as a pay cut if total earnings were being compared.

Post 2013 Pension Cost Comparison

The pension costs for the post-2013 pension scheme can be compared as follows:

Post-2013	DFO Accelerated Accrual - Trident	Garda Fast Accrual - DPER
Total Cost (% of Salary)	17.90%	19.00%
Normal Employee Contribution	5.70%	5.00%
PRD	5.00%	4.00%
Employer Contribution Rate	7.20%	10.00%

The differences are narrower in this comparison.

The difference in assumed retirement age is likely to represent a significant component of the difference in cost.

In both comparisons above, there are differences in assumptions, retirement ages and sample members analysed; in the short timeframe to review the report, there hasn't been sufficient time to assess the relative impact due to these differences.

At this point in time, we are not satisfied that the DPER report is a reliable foundation for the Defence Forces bearing in mind the potential for small differences in assumptions (age at recruitment, retirement age etc.) to have a significant impact on calculations.

Potential benefits at retirement should also be borne in mind. The reduced nature of the accelerated accrual that applies for Defence Force Officers in the post-2013 scheme means that benefit adequacy at forced early retirement ages is a material concern for members of this scheme.

4. Assumption Review

While the timeframe is too short to undertake a full comparison of the impact of the DPER assumptions versus ours (per our 1 March 2017 report), I would comment that general salary increases of 3% p.a. with a salary scale in addition seem high in our opinion. The inflation assumption at 2% p.a. could also be seen as high – the rate we have used of 1.5% p.a. seems equally justifiable.

Pension increases have been assumed to keep pace with pay parity and I would question the likelihood of this in practice given our understanding of Government policy. On the other hand, if public servants are being told through this report that future pension increases on a pay parity basis reflect Government policy, then this should be formalised.

Costs have also been provided in the DPER report where pension increases are linked to CPI instead. This seems a more reasonable assumption to us and we have referred to this reduced cost above for the post-2004 scheme.

We would urge long term assumptions to be used for the purposes of establishing the value of pensions as it is impractical to adjust public service pay at short intervals to take into account differences for example in long-term interest rates. Without the time to fully assess the assumptions used in the DPER report, we would query the long-term validity of a post-retirement discount rate of 2% p.a.

5. Comparison of Costs with Private Sector Pension Costs

The notional employer contribution rate for the “private sector equivalents for the public sector posts considered” in the DPER report for the post-2004 group has been calculated as 22% of salary. This is based on a retirement age of 65. This may be appropriate if total earnings over a member’s lifetime were being considered but as this is not the case, the pension costs should be tailored accordingly with the same retirement age used for a more direct comparison. This could increase the contribution requirement sizeably.

Furthermore, we note that the private sector contribution rate deemed to be appropriate for comparison purposes represents 30% of the notional DB employer contribution rate and 70% of the DC employer contribution rate. This 30%/70% split is based on statistics provided by the

Pensions Authority regarding pension scheme membership of private sector employees. Presumably, this statistic is based on current membership of a pension scheme; as we are looking at pension costs over a member's career, it may be more appropriate to consider accrued benefits also. This would be likely to increase the proportion of DB membership.

In terms of the DC employer contribution rate assumed of 7% of salary, does this reflect death in service costs, for a more direct comparison of costs? Also, does it reflect future increases in contribution rates in schemes where the rates increase with age and/or service? It is the average contribution rate over the member's career that is appropriate. Furthermore, given the assumptions made in the DPER report regarding future financial circumstances together with increasing longevity, the likelihood is that DC contribution rates will come under pressure to increase. These increases have been reflected in the DPER public sector costs and it seems an unfair comparison to exclude them when assessing an appropriate DC contribution.

6. Summary

It is essential in our opinion that career earnings are considered in totality, rather than isolating pension accrual costs which are higher due to the accelerated accrual of forced early retirement but also as they are paid for a shorter period. The material reduction in career earnings due to forced early retirement has to be considered to enable a fair comparison.

Our concerns with regard to various other assumptions are outlined above.

Please advise if you have any queries.

Yours sincerely,



JOHN O'CONNELL &

RITA-ANNE KEYES

Fellows of the Society of Actuaries in Ireland

3rd April 2017