Ref: P18/065/06

To: All Personnel Officers

Cc: Secretaries General/ All Heads of Departments/Offices

18 February 2011

**Budget and Finance Act 2011:**

**Reduction in the maximum allowable pension fund on retirement for tax purposes (the Standard Fund Threshold or SFT)**

 **– Implications for Civil / Public Service Officials and Administrators**

**Introduction**

1. The purpose of this letter is to highlight the potential implications of the Budget and Finance Act 2011 amendments, outlined in paragraph 2 following, for certain civil/public servants and also for Departments/Offices in their role as pension administrators. In general, the amendments will not have implications for persons who earn less than €200,000 and have no other pension benefits additional to and independent of their civil/public service occupational pension.
2. Chapter 2C of Part 30 of the Taxes Consolidation Act 1997 (TCA) and Schedule 23B TCA provide for a maximum allowable pension fund on retirement for tax purposes. This legislation was amended in this year’s Finance Act on foot of changes announced on Budget Day 2011 (7 December 2010) and legislated for by way of Financial Resolution on that day. This Department’s previous letter of 27 October 2006 in this general matter (reference P18/065/06) also refers.
3. Paragraphs 7 to 13 below and Appendix 1 outline the potential implications of the changes for certain individuals, the actions they may need to take at this time and generic examples describing the possible impacts. Some relevant Questions and Answers are set out at Appendix 3. These details should be brought to the attention of relevant staff in your Department and in the agencies under its aegis. Paragraphs 14 to 30 set out the implications for and requirements on Departments.

**General position**

1. The maximum allowable pension fund on retirement for tax purposes, known as the Standard Fund Threshold (SFT), is set at €2.3 million as on and from Budget Day 2011 (7 December 2010). This compares with an SFT of €5,418,085 that applied before the Budget. The new lower SFT will apply to all individuals the capital value of whose pension rights on Budget Day 2011 is equal to or less than €2.3 million. Individuals with accrued pension rights whose capital value exceeds €2.3 million on Budget Day will be able to avail of that higher capital value by claiming a Personal Fund Threshold (PFT) from the Revenue Commissioners.
2. The PFT is the aggregate of the capital value of pension benefits which the individual has already become entitled to on or after 7 December 2005 and prior to 7 December 2010, if any, (i.e. “crystallised” pension rights) plus the capital value of any ‘‘uncrystallised’’ pension rights which the individual had on 7 December 2010 (in other words, pension rights which the individual was building up but had not drawn down on that date). Where this capital value amount exceeds the SFT amount of €2.3 million, that higher amount will be the individual’s PFT, subject to the PFT not exceeding the previous SFT of €5,418,085. An individual who already claimed a PFT arising from the introduction of the maximum allowable pension fund provisions from Budget Day 2006 (7 December 2005) may retain it.
3. On each occasion, on or after 7 December 2005, that an individual becomes entitled to receive a benefit (e.g. a pension, retirement lump sum etc.) under a pension arrangement (referred to in the legislation as a “benefit crystallisation event” or BCE) they use up part of their SFT or PFT. When the capital value of a BCE (either on its own or when added to BCEs that have been taken earlier) exceeds an individual’s SFT or PFT, as appropriate, a “chargeable excess” arises equal to the amount by which the fund threshold is exceeded. The whole of the amount of the chargeable excess is subject to an upfront income tax charge of 41%. This charge is without prejudice to any other income tax charge that might arise on the balance of the chargeable excess as and when benefits are actually taken from the pension arrangement e.g. by way of regular pension payments.

**Implications for certain civil/public servants**

1. While the Budget and Finance Act 2011 changes will not affect the majority of public servants, they may impact on certain public servants, in particular those whose pensionable remuneration amounts to or exceeds €200,000 per annum and/or who have pension arrangements additional to and independent of their public service occupational pensions. Such individuals should establish if they may need to apply to Revenue for a PFT certificate.
2. Tax legislation (paragraph 1 (2) of Schedule 23B to the TCA) provides a formula for calculating the capital value of uncrystallised pension rights under Defined Benefit pension schemes as on Budget Day, in order to establish entitlement to a PFT. Basically, the formula provides for a capital value to be determined by establishing the annual pension entitlement that would arise to an individual on the assumption that he/she retired on Budget Day (7 December 2010) having reached normal retirement age and on the basis of their service and salary levels as on that date. The annual pension entitlement so established is multiplied by a factor of 20 to arrive at the capital value. In the case of public sector Defined Benefit schemes, the value of the retirement lump sum entitlement on 7 December 2010 (calculated on the same assumptions) would also be added. The capital value on 7 December 2010 of any Additional Voluntary Contributions (AVCs) to pension saving for the purpose of supplementing pension benefits may be added. AVCs are generally defined contribution (DC) type arrangements and the legislation provides that the capital value of pension rights in DC arrangements is established by simply taking the value of the fund on Budget Day.[[1]](#footnote-1) AVCs made for the purposes of enhancing death-in-service benefits should not be included.
3. The capital value of pension rights which had come into payment to the individual since 7 December 2005 (i.e. crystallised rights), if any, would also have to be calculated and added in order to establish if a PFT arises.
4. A PFT has to be claimed by way of notification to, and certification by, the Revenue Commissioners. In general, individuals will have a period of 6 months from Budget Day to send details of their pension schemes and the calculation of their PFT to the Revenue Commissioners. Where retirement takes place within that 6 month period, the PFT application should be made in advance of retirement taking place. There is provision, however, for a late notification. The Revenue Commissioners will then certify the PFT as appropriate. A PFT Notification form along with general guidance is available from the Revenue website at [www.revenue.ie](http://www.revenue.ie).
5. **Post-cut rates of pay** should be used as the basis for pensionable remuneration in calculating PFTs, except where a decision to retire before 1 March 2012[[2]](#footnote-2) has already been taken at the time of application for a PFT and the decision has been formally intimated by the individual concerned to the Personnel Officer in his/her Department or Office. In all other cases, if it transpires that an individual subsequently decides to retire before 1 March 2012, a revised PFT may be sought from Revenue at least one month before retirement or before 31 January 2012, whichever is the earlier.
6. Once a PFT is granted, if the capital value of the individual’s pension rights grows, for example, within a Defined Benefit scheme on foot of increased pensionable income or service, then a chargeable excess will arise on drawdown of those rights equal to the amount by which the value of those rights exceeds the PFT. Any excess will be subject to the one-off up-front income tax charge of 41%.
7. Examples of the impacts of the changes are set out at Appendix 1 to this letter together with some Questions and Answers at Appendix 3.

**Implications of changes for Departments/Offices as Pension Administrators**

1. As already set out above, where the relevant SFT or PFT threshold is exceeded when a BCE takes place, an up-front income tax charge of 41% on the “chargeable excess” arises. Under the legislation, the pension administrator of the relevant pension scheme and the individual are jointly and severally liable for the tax charge. It is, therefore, essential that the pension administrator is aware of, and accounts to the Collector General of Revenue for, any tax due from the individual. Such tax is due at the time by which the return is due to be made to the Collector General, i.e. within three months of the end of the month in which the BCE occurs. The pension administrator is the person normally tasked with administration of the scheme and, in the case of Civil Service schemes, will be the trustee of the scheme.
2. Given the joint liability, it is vital that Government Departments and Offices and public service employers take full account of the relevant legislative provisions in dealing with all staff retiring, and make them aware of these provisions.

**The Process**

1. In order to assess if any potential liability to the tax arises, **every officer**, or former officer claiming retirement benefits from the Civil/Public Service, must complete the attached declaration form (Appendix 2).
2. **No pension payments can be approved unless a properly completed declaration form is on file.**

**Tax Computation:**

1. Once the completed declaration form has been received, it will be necessary to establish a capital value for the retirement benefits an individual is entitled to from the Civil/Public Service scheme and to add this to the capital value of any other retirement benefits the officer has declared in the relevant declaration form.
2. The legislation (paragraph 3 of Schedule 23B of the TCA) gives details as to how the capital value is to be calculated in respect of differing types of pension benefits. In general, in the case of Defined Benefit schemes (the most usual model in the public service), the capital value is calculated by multiplying the person’s annual pension on retirement by 20 and then adding that figure to the actual value of the lump sum (before any tax that might be payable on the lump sum).
3. The tax due, if any, is 41% of the amount by which the total capital value of all retirement benefits in payment/paid at the time the Civil/Public Service benefits fall due for payment exceeds €2.3 million or, if the individual has a PFT, the value on the PFT Certificate issued by the Revenue Commissioners.
4. An important point for pension administrators to bear in mind is that in a situation where an individual becomes entitled to receive a benefit under a pension arrangement (e.g. a BCE takes place) and the capital value of that BCE, on its own or when added to previous BCEs, exceeds €2.3m, then unless the individual produces a PFT certificate to the pension administrator, the pension administrator is obliged under legislation to apply the tax charge of 41% on the “chargeable excess” over the standard SFT of €2.3m. The legislation also permits the pension administrator to appropriate all or part of an individual’s pension entitlements to reimburse for any tax paid by the pension administrator.

**The Tax**

1. Once it is established that a tax liability exists, the pension administrator should inform the individual and request immediate payment of the tax due. In the normal course, payment would be expected to be made out of the lump sum.
2. In the event that the individual does not pay the tax due, the pension administrator, being jointly liable with the individual for the tax, must pay the full amount to the Revenue Commissioners.
3. In such circumstances pension administrators should deductthe amount of tax due from any pension entitlements the officer may have. In that regard, the legislation (section 787Q(6)(b) TCA) requires the individual to allow such an “appropriation” of his or her benefits. If the amount of lump-sum[[3]](#footnote-3) is not sufficient to meet the tax liability arising (or if there is no lump sum), pension administrators should make arrangements with the person liable so that recoupment is made over a reasonable period. Should the individual die before the tax paid is fully recovered, the relevant Department/Office should assess the situation and, if warranted, seek to recover the balance outstanding from the estate.
4. Further detailed guidance will issue in due course from the Office of the Revenue Commissioners in relation to the records to be kept and the returns to be made to the Revenue Commissioners.

**The Accounting: (Civil Service pensions – Superannuation Vote etc.)**

1. If it is necessary for the pension administrator to discharge tax liability on behalf of an individual, the amount should be accounted for on a gross basis, i.e. the total amount should be paid from Vote 7, and any off-set or recovery of monies directly from the individual or from his or her lump-sum or pension, or from the estate of the individual if deceased, should be treated as an Appropriation-in-Aid to Vote 7. Separate records should be maintained for each individual case which will provide a clear audit trail.
2. Similar arrangements to those at the preceding paragraph should be put in place for areas of the Public Service not covered by the Superannuation & Retired Allowances Vote for the Civil Service superannuation schemes.

**Circulation:**

1. Please bring the contents of this minute to the attention of all officers of your Department or Office, and of all relevant public service bodies under the aegis of your Department for dissemination to their staff. You should alert this Department of ongoing problems relating to the implementation of these changes, and advise the Department of the measures you intend to take to resolve those problems.
2. Queries relating to this Circular about accrual of service should be addressed in the first instance to the relevant personnel officer. Queries about tax aspects of the Circular (e.g. what qualifies for PFT) should be addressed to the relevant office of the Revenue Commissioners.
3. Questions and Answers have been made available to help provide elaboration and further clarification on these Finance Act changes. Further Q&As will be provided as necessary.
4. This minute does not purport to be a legal interpretation of the changes referred to, which are fully set out in the relevant legislation.

Yours sincerely,

*Tony Jordan*

Principal

Budget, Economic and Pensions Section

**Appendix 3**

**Questions and Answers**

Q1. How do I establish the capital value of my Defined Benefit pension on 7 December 2010?

A. First of all you should establish from your pension fund administrator(s) what gross annual pension(s) you would have been entitled to under the rules of the defined benefit arrangement(s) if you had retired on 7 December 2010 at your pensionable remuneration and service on that date and on the assumption that you had attained normal retirement age on that date. The gross annual pension is then multiplied by 20 (the standard capitalisation factor) to arrive at the capital value of your defined benefit pension(s) on 7 December 2010.

If the defined benefit arrangement provides a separate lump sum entitlement (otherwise than by way of commutation of part of the pension) e.g. civil service schemes, the value of the lump sum entitlement (calculated on the same assumptions as above) is added to the capital value of the defined benefit pension to arrive at the overall capital value. Again, the pension scheme administrator will be able to advise you of the value of the lump sum that would be payable under the scheme rules on 7 December 2010.

***Q2. How do I take account of a pension benefit that came into payment since 7 December 2005 in my current PFT Notification?***

A. You need to include in the calculation of the PFT the capital value of pension benefits taken by you on or after 7 December 2005, if any. These are known as “benefit crystallisation events” (BCEs) and could arise by way of, for example, a pension or annuity coming into payment, the receipt of a pension lump sum or the proceeds of a pension fund being placed in an Approved Retirement Fund (ARF) or Approved Minimum Retirement Fund (AMRF).

In the case of pension benefits that arose from defined contribution arrangements, you need to contact the pension fund administrator to establish the value of the cash/assets that were used to, say, purchase your annuity or that were transferred to an ARF for you. In the case of a pension lump sum the value will simply be the amount of the lump sum paid to you.

In the case of a pension paid under a defined benefit arrangement the capital value of the pension is the amount of pension paid to you in the first 12 months (ignoring any increases over that period) from the date you became entitled to it, multiplied by 20 (the standard capitalisation factor). Note it is not the current annual rate of the pension being paid to you. You will also have to add the value of any separate pension lump sum paid to you at that time.

***Q3. Do severance payments count as retirement benefits for the purpose of calculating an SFT or PFT****?*

A. No. Severance payments would not be regarded as pension benefits from a tax perspective.

***Q4. I am in the middle of my contract as a Secretary- General. If “added years” service is credited to me at the end of my contract, are those “added years” included in the calculation of my PFT as at 7 December 2010?***

A. Unlike pension and retirement lump sum entitlements that accrue to individuals over time at specified rates, “added years” in this context are discretionary benefit enhancements available only if certain conditions are met and Government decisions are made. In these circumstances, “added years” cannot form part of the accrued pension rights that have been built up at 7 December 2010 for the purpose of calculating a PFT.

***Q5. If, as a Secretary-General Level II, I intend to retire by end-February 2012, at what level of pensionable remuneration should the capital value of my uncrystallised pension rights be calculated on Budget Day 2011 for the purpose of my PFT?***

A. **Post-cut rates of pay** should be used as the basis for pensionable remuneration in calculating PFTs, **except** where a decision to retire before 1 March 2012 has already been taken at the time of application for a PFT and has been formally intimated by the individual concerned to the Personnel Officer in his/her Department or Office, in which case the pre-cut rate of pay may be used.

If it is the case that an individual, after applying for a PFT on the basis of a post-February 2012 retirement date and using the post-cut rate of pay in the calculation, decides instead to retire before 1 March 2012 and formally notifies this intention to his/her Personnel Officer, a revised PFT using the pre-cut rate of pay may be sought from Revenue at least one month before retirement or before 31 January 2012, whichever is the earlier.

Q6. As I intend to retire by end February 2012, my public service pension will be subject to the “pension reduction”, is that reduction taken into account in any way in the calculation of the PFT?

A. No. An average reduction of 4% in the pensions paid to certain existing public servants and to those retiring on or before 29 February 2012 was introduced in Budget 2011 with effect from 1 January 2011. As the pension reduction measure was introduced with effect from a date after 7 December 2010, it has no impact on the calculation of an individual’s PFT. The amount of the reduction should be taken into account, however, in calculating the capital value of the individual’s pension rights at retirement (see example 2 in Appendix 1).

Q7. I am making AVCs to maximise death-in-service benefits. Can the current value of these AVCs be included in the calculation of my pension rights for PFT purposes and at the point of retirement?

A. No. AVCs being made purely and exclusively to provide for enhanced death-in-service benefits should not be included in the calculation of uncrystallised pension rights used to establish the value of a PFT or the capital value of pension rights at retirement. Only AVCs made to supplement retirement benefits should be included. These are generally defined contribution type arrangements whose capital value is essentially the value of the AVC fund on 7 December 2010 and at the date of retirement. .

Q8. I have plans for my retirement lump sum. What if the tax due on the excess of my retirement lump sum over €200,000 and the tax charge on any chargeable excess arising over my PFT take up a considerable amount of the lump sum? Is there any possible alternative to paying the chargeable excess tax due from my lump sum – can it be paid over a period?

A. From the Exchequer’s point of view it is important that any tax due on a chargeable excess be discharged as quickly as possible and the retirement lump sum is the most obvious means of doing this. There may be circumstances where alternative arrangements including recovering the tax over a short period from the pension in payment can be considered – but this will be the exception rather than the rule.

Q9. I am on modified PRSI (a pre-1995 recruit to the public service) while my colleague in the same grade is in the “integrated” pension scheme having joined post-1995. His entitlement to a State Pension (Contributory) does not count towards the SFT or PFT, yet he may end up with the same overall pension benefits as me and I may exceed the SFT and be faced with tax on a chargeable excess and he may not. Is that equitable?

A. The SFT or PFT, as appropriate, are thresholds that apply to pension benefits derived from tax-relieved pension arrangements. The State Pension (Contributory) does not fall into this category and the SFT or PFT are not relevant insofar as the State Pension is concerned.

Q10. If pension benefits (BCEs) from more than one pension scheme come into payment on the same date, which pension administrator will have to account for tax if a chargeable excess arises?

A. The legislation provides that where more than one pension benefit (BCE) arises on the same day in relation to an individual, the individual must decide which is deemed to arise first and inform the administrators accordingly. Each pension fund administrator is then required to operate independently to establish if the capital value of the pension benefit (BCE) that he is responsible for, either on its own or when added to prior BCEs in respect of the individual, gives rise to a chargeable excess and to deduct tax accordingly. So the pension fund administrator dealing with the BCE that is deemed to arise second in the sequence will have to take account of all prior BCEs (including the one dealt with by the administrator of the BCE deemed to arise first) to establish if a chargeable excess arises as respects the second BCE. Depending on the circumstances each might have to account for tax on a chargeable excess e.g. if the capital value of the first BCE either on its own or when added to prior BCEs exceeds the SFT or PFT a chargeable excess will arise on the amount by which the SFT/PFT is exceeded and the administrator will have to apply tax at 41% on the excess. By definition, if the first BCE has given rise to a chargeable excess then the second BCE will be fully exposed to the 41% charge and the administrator of the second BCE will have to account for that tax.

***Q11. Can I change the capitalisation factor because I am age 75?***

A. No. The legislation only provides for the standard capitalisation factor of 20 to be used.

Q12. What happens in the case of an individual whose pension is subject to a pension adjustment order? Does the portion of the pension being allocated to the other party form part of the latter’s SFT/PFT?

A. No. Under the requirements of the legislation where an individual is a member of a relevant pension arrangement which is, or becomes, subject to a pension adjustment order (PAO), then in calculating the capital value of the PFT or any subsequent Benefit Crystallisation Event (BCE) the benefits designated to the other party under the PAO are to be included in the calculations as if the PAO had not been made. This is the case whether the benefits under the PAO are to be paid, in due course, by way of a designated benefit from the individual’s pension scheme or whether a transfer amount has been applied to provide the other party with an independent benefit in accordance with the Family Laws Acts. The corollary is that the PAO benefits are not included in any PFT/BCE calculations in respect of the other party.

*These Q&As may be supplemented from time to time, and will be posted on the internet at www.revenue.ie.*

1. The assets in a DC fund may be cash or non-cash, and if the latter, the market value of the assets on the relevant date must be established. The AVC fund administrator will provide this information [↑](#footnote-ref-1)
2. The Government decided in Budget 2011 to extend from end-December 2011 to end-February 2012 the period over which pensions could be calculated by reference to pre-cut rates of pay. This change will be made by Statutory Instrument. [↑](#footnote-ref-2)
3. Note that section 790AA TCA already places a lifetime limit on the amount of a tax-free retirement lump sum that can be taken by an individual from 7 December 2005. This limit was set at 25% of the old SFT and amounted to about €1.35 million. Budget and Finance Act 2011 provides that the maximum lifetime retirement tax-free lump sum is €200,000 as on and from 1 January 2011. Amounts in excess of this tax-free limit are subject to tax in two stages (except for specified exclusions). The portion between €200,000 and €575,000 is taxed at the standard rate of 20% while any portion above that is taxed at the individual’s marginal rate of tax. The figure of €575,000 represents 25% of the new lower SFT of €2.3 million. [↑](#footnote-ref-3)