A Levelling of the Pensions Taxation Playing Field in Ireland to Everyone's Benefit

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1. Introduction

The primary purpose of this whitepaper is to cover the current inequities in the tax treatment of public and private sector pensions and provide relevant facts about the existing model. We also look at solutions to resolve these inequities. For the avoidance of any confusion, we want to make clear that this paper is not suggesting that the current favourable pension tax regime relating to the public sector be curtailed. We are instead proposing that this regime be extended to all pension participants. It is only appropriate to ask why we have one regime for public sector pensions and another less beneficial regime for the private sector.

The content shared in this whitepaper has been prepared for the purpose of informing the discussion on any current and potential changes to the Irish pensions taxation treatment mainly impacting the private sector. The information may not be suitable for use in any other context, for any other purpose or by any other party and we accept no responsibility for any such use. Any reliance placed on this material for another purpose, or by other parties is entirely at their own risk.

The material in this paper is based on information provided by various sources, as referenced in this paper. In preparing this paper, we have relied upon data supplied by third parties, or available in the public domain. While we have made every effort to ensure that the information is correct and reasonable care has been taken to ascertain the reliability of data, we do not guarantee the accuracy or completeness of this data.

We do not intend to go over the ground covered in earlier reports but want to focus on the fact that there exist significant anomalies in the tax treatment between public sector pensions and private sector pensions. This could give rise to the accusation of discriminatory treatment between the two regimes. We outline at the end of this Paper a number of possible reforms of the current private sector pension regime which could be considered by the government to reduce or eliminate inequities with the public sector pensions.

2. Executive Summary

The pandemic and other challenges are having a significant impact on pension savings. The current situation is not sustainable in the medium-long term as the number of retirees with quality jobs vs new lower paid entrants keeps increasing. Many of these new employees, in the current challenging environment, are aiming to rely on the state pension mainly as their source of income when reaching retirement. Ireland has an "Exempt-Exempt-Taxed" ("EET")[1] system of pension taxation where tax relief is provided on contributions and the investment returns on pension savings are not taxed. Then, the actual pension drawdown is taxed at the individual's appropriate tax rate. This type of system, is similar to other countries in the OECD (Half of OECD countries apply a variant of the "EET") regime, causes a long-run net cost to the Exchequer which varies as a regime matures.

2.1. Background and Challenges of the Current Pension Landscape

Latest CSO statistics suggest that male and female life expectancy in Ireland is approx. 81.5 years on average[2]. We have more active lives and are living longer after retirement. This means we will need to provide ourselves with an income for a longer period of time post-retirement.

To address this the Government launched "A Roadmap for Pensions Reform" 2018 to reduce the low rates of supplementary pension. This document outlined proposals for pension auto-enrolment which have currently been deferred due to the COVID-19 pandemic. Also, in 2020 we had the Report of the Interdepartmental Pensions Reform & Taxation Group[3] which has further examined the Irish pensions landscape and has made recommendations to both simplify and make pensions more 'user friendly'. All of this shows the desire of the Government to increase pensions coverage from its current low level.

According to CSO data, around 45% of the working population in Ireland do not have supplementary pensions or are not members of any pension arrangements. Unfortunately, most pensioners in the future will suffer undesirable reductions in living standards after leaving the workforce. Research by Standard Life also shows that just under half of people of working age have an occupational pension due to fewer young employees entering pension schemes than workers retiring.

2.2. Need for Reform and Consistency

Public Sector Pay Commission[4] considers pensions the main cause of the remuneration gap between the public and private sector. Commission chairman Kevin Duffy[5] said that finding appropriate "comparators" for public sector pay was "difficult and time consuming". It is critical

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[1] OECD Brief - The tax treatment of retirement savings in private pension plans
[2] https://www.cso.ie/en/releasesandpublications/er/ilt/irishlifetablesno172015-2017/
[3] Report of the Interdepartmental Pensions Reform & Taxation Group - 2020
[4] https://paycommission.gov.ie/?s=pension
[5] https://www.irishtimes.com/business/economy/pensions-the-key-to-gap-between-public-and-private-sectors-1.3077273

for both public and private employees to take control of retirement planning and make decisions regarding their pensions. Saving for a pension is one of the few areas where individuals can still get tax relief, but there are disparities between both sectors' pensions tax regimes, and it is critical that these are resolved.

The statistics regarding pension coverage as outlined in 2.1 are concerning but when coupled with an ageing population it becomes apparent why encouraging individuals to make independent pension provision is so high on the government's agenda. In terms of our ageing population the projections are stark.

The percentage of retirees will grow substantially over the coming decades[6]. The Irish Fiscal Advisory Council[7] covers in its Long Term Sustainability Report, that Ireland is no longer a predominantly young society and we are going to get older. In fact, it projects that between now and 2050, the number of 65-79 year olds will increase by 88%. The number of people aged 80 and over will increase by 241%. Under current policies, ageing-related costs will add to the debt burden.

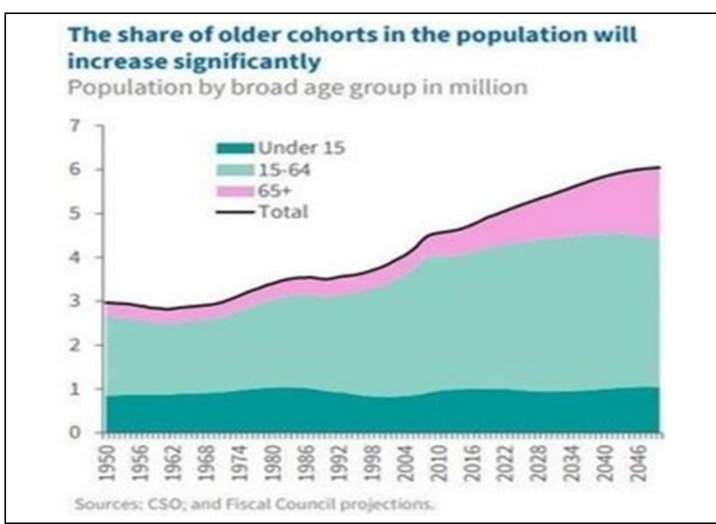
So, there is an urgency on the government to address inequities and to introduce the auto-enrolment scheme, similarly to other countries in the EU, in parallel with the state pension.

[6] Population Ageing and the Public Finances in Ireland - September 2021 - Department of Finance | Annual Report on Public Debt in Ireland
[7] Irish Fiscal Advisory Council 2020 - Long Term Sustainability Report Website

3. Ireland is Ageing Very Quickly Creating a Domino Effect on Pensions

The rate of supplementary pension coverage in Ireland is around 55% of the working population (CSO, Pension Coverage Survey 2020) and it is estimated that this reduces to less than 35% when the private sector is considered in isolation. We will very soon go from being one of the youngest populations in Europe to one of the fastest ageing populations. We'll hit the EU average in about 15 years' time. By 2050, our population will be older than any other EU state is today.

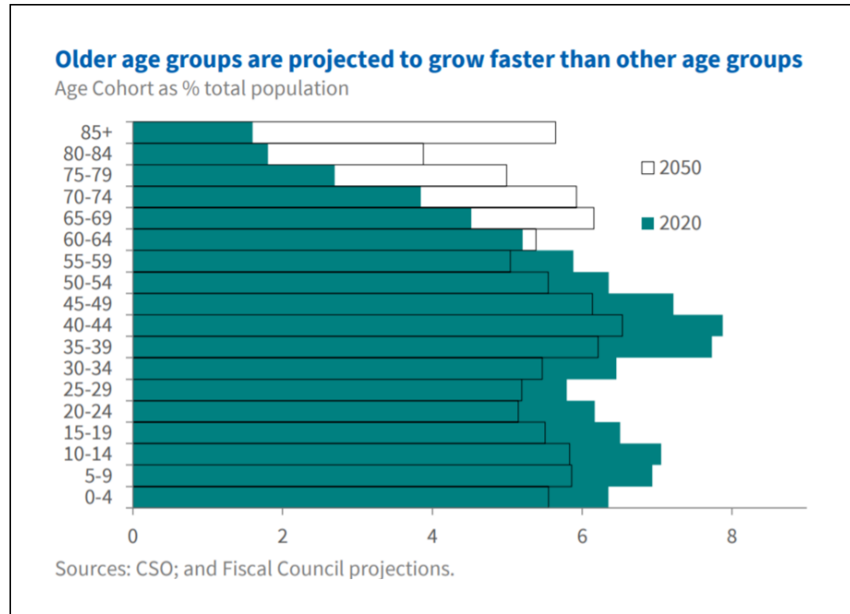
The more telling 'dependency ratio', which measures the percentage of people aged 65 and over compared to the numbers aged 15-64, will rise from 22% today to 47% by 2050. In simple terms, this means the numbers at work will be fewer and the number of older people who will be supported by the taxes paid by those in employment will be far greater.



Graph: Irish Fiscal Advisory Council.

The rise in public spending on health and pensions primarily reflects an ageing population. Older people will represent a higher share of the population, with the share of ages 65+ increasing from 14 per cent in 2020 to almost 27 per cent by 2050.

IFAC calculates that based on current policies continuing as they are, the public finances will slip into deficit from 2026 just to keep up with increased pension payments and healthcare costs.



Graph: Irish Fiscal Advisory Council.

The rise in public spending on health and pensions primarily reflects an ageing population. Older people will represent a higher share of the population, with the share of ages 65+ increasing from 14 per cent in 2020 to almost 27 per cent by 2050.

There is an urgency on the government to address inequities and to introduce the auto-enrolment scheme, similarly to other countries in the EU, in parallel with the state pension. The current situation is not sustainable in the medium-long term as the number of retirees with quality jobs vs new lower paid entrants keeps increasing. Many of these new employees, in the current challenging environment, are aiming to rely on the state pension mainly as their source of income when reaching retirement.

In terms of pension coverage, the vast majority of Public Servants are members of some form of the State Superannuation Scheme; it is in the private sector that coverage remains low. We do not intend to go over the ground covered in earlier reports but want to focus on the fact that there exist significant anomalies in the tax treatment between public sector pensions and private sector pensions. This could give rise to the accusation of discriminatory treatment between the two regimes.

We outline at the end of this Paper a number of possible reforms of the current private sector pension regime which could be considered by the government to reduce or eliminate tax inequalities with the public sector pensions. For the avoidance of any confusion, we will now restate the following, this paper is not suggesting that the current favourable pension tax regime relating to the Public Sector be curtailed. We are instead proposing that the Public Sector regime be extended to all pension participants. It is only appropriate to ask why we have one tax regime for public servant pensions and another bluntly less favourable regime for the private sector. This is obviously inequitable. In addition, it could lead to the suspicion that those who 'write the rules' ensured that they were well protected. How could such a conclusion be arrived at?

- A system for valuing Defined Benefit pensions that is unrealistic in the context of real-world annuity rates. The public sector superannuation scheme has all the characteristics of a Defined Benefit Scheme.
- An encashment option only applying to the public service
- Ability to pay CET over a 20-year period only applying to the public service
- Mandatory ASC in the public service does not count towards the €115,000 tax relief limit whereas in both the public and private sector mandatory employee contributions do count against the threshold.

We will go through these anomalies in greater detail and will outline at the end of this Paper a number of possible reforms of the current private sector pension tax regime which could be considered by the government to reduce or eliminate inequities between the public and private sector pensions.

The options must be considered carefully to avoid significant pressure on the government's budget. However, we consider that lack of action to encourage private workers to contribute to their pension could have significant negative potential consequences for some individuals with undesirable changes in behaviour in relation to private pension provision.

Research shows several potential benefits to society when private pension provision is incentivised. An Irish Longitudinal Study on Ageing (TILDA)[8] report identified that a retiree's level of retirement income is positively associated with quality of life in older age. All aspects of quality of life (control, autonomy, self-realisation, and pleasure) increase consistently with household income

[8] https://tilda.tcd.ie/

4. Overview of Private Sector and Public Service Pensions

As outlined earlier, it is in the private sector that pensions coverage remains low. So, the task is to improve pensions coverage in the private sector. There is a need to address the low proportion of employees in Ireland with supplementary pension cover.

4.1. Public sector occupational pension schemes

Employees can join their public sector pension scheme which operates on a defined benefit model but largely financed from general taxation on a pay-as-you-go basis but supplemented by members' contributions. In the public sector, private pension tax relief acts as a subsidy to a compulsory superannuation contribution.

A public sector pension of €66,000 for someone aged 65 would[9], if bought in the marketplace, cost €3.3 million to purchase. A private sector worker aiming to secure a pension of €24,000 annually from age 65 would have to contribute €15,750 annually from age 25 in order to do so. Since 2008, the public service pension bill has risen by 75 per cent and last year costing €2.8 billion.

The Public sector Superannuation regime could be broadly described as being equivalent to a defined benefit scheme that provides a set level of pension at retirement, the amount of which normally depends on members service and earnings at retirement or in the years immediately preceding retirement.

In the public service there are 4 key dates. These are pre-6th April 1995 entrant, 06th April 1995 to 31st March 2004 entrant, 01st April 2004 to December 2012 entrant and Single pension scheme entrant from 01st January 2013 onwards. It is beyond the scope of this paper to go through each incarnation in depth but rather we will give a brief synopsis. For public servants who joined prior to 6 April 1995, a pension of 1/80th of final earnings is payable for each year of service. A gratuity (cash sum) of 3/80ths of final earnings is also payable. Those who joined on or after 6 April 1995 the key difference is that pensions are integrated with the State pension. A new scheme for joiners to the public service (the 'Single Scheme') has been introduced for new entrants from 1 January 2013 that provides pensions based on career average revalued earnings, rather than final earnings. All incarnations to all intents and purposes are similar in that they provide a benefit promise. This benefit promise is of course similar to the private sector defined benefit promise. Key difference of course being that the cost of providing public sector pensions falls mainly (see ASC section later) on the exchequer i.e., the taxpayer. For more information see the website http://www.cspensions.gov.ie/

4.2. Private sector occupational pension schemes

Private employees can join a pension scheme / company pension plan, these are set up by employers and can provide benefits including a tax-free lump sum (within certain limits), and

[9] https://www.irishtimes.com/opinion/editorial/public-v-private-a-glaring-inequality-in-pension-provision-1.2815201

pension income in retirement. In the private sector, private pension tax relief is designed to act as a financial incentive to encourage voluntary supplementary retirement provision. Those in "non-pensionable" employment can contribute to a personal plan or PRSA.

Company Pension Defined Benefit schemes promise a fixed benefit on retirement, some schemes have provisions for the employer to top up the fund if necessary. DB schemes in the private sector typically provide for an annuity calculated as 1/60th of final salary multiplied by number of years of service, up to a maximum of 40 years' service. This is usually reduced by commuting some pension income for a lump sum on retirement. Standard defined benefit schemes in the private sector, which were integrated with social welfare, provided for a two-thirds final pensionable salary benefit when integrated with the State old age pension. However, DB schemes are not providing the comfortable retirement private sector employees anticipated in comparison to public service employees.

Employers have closed defined benefit schemes as they see it as an increasing expense. Standard defined benefit schemes in the private sector, which were integrated with social welfare, provided for a two-thirds final pensionable salary benefit when integrated with the State old age pension.

Company Pension Defined Contribution schemes: The majority of company pension schemes and all Personal Pension Products and PRSA's are defined contribution i.e., the amount being contributed is defined but the final benefits are not. These benefits will be dictated by final fund size which of course will be impacted by contribution amounts and investment performance. In addition, now most private sector employees are members of defined contribution schemes.

With Defined Contribution schemes unlike Defined Benefit schemes, the final pension will depend on how much was paid and how the fund performed, and so there is no certainty on retirement income. This contrasts with Private sector defined benefit schemes which tend to provide for a lump sum of 3/80th's of final salary multiplied by number of years of service, and an annuity of 1/60th of final salary multiplied by number of years of service, both of which are usually subject to a maximum of 40 years' service.

Of late there has been a shift to defined contribution schemes. This has resulted in a substantial transfer of risk to households and may have deep implications[10]. This might result in suboptimal risk allocation in the economy due to a lesser diversification of risks and lower capabilities of households to manage risks.

The private sector defined contribution pension provision has been impacted by falling global interest rates. The current environment and macro-economic strategies such as quantitative easing and low interest rates has an adverse effect for pension funds. Lower yields have made the purchase of retirement income more expensive.

[10] European Systemic Risk Board, 2020 – Paper - Pension schemes in the European Union: challenges and implications

The options at retirement may include:

- Taking a tax-free lump sum, subject to limits set by Revenue.
- Receiving a pension (sometimes provided by an annuity).
- Transferring some or all of the retirement savings to an Approved Retirement Fund (ARF) or Approved Minimum Retirement Fund (AMRF);
- Taking a taxable lump sum and
- Providing for dependants.

There are considerable inequities in the tax treatment of public and private sector pension arrangements. These include but are not limited to Chargeable Excess Tax, ASC (Additional Superannuation Contribution), Encashment Option, Defined Benefit Multiplier basis. We shall look at each in turn.

5. Tax Charge on High Value Pension Funds

State pensions are paid without tax being deducted, but if an individual is in receipt of additional income, they may become taxable. However, when in receipt of additional pension income, the individual's tax-free allowance is reduced when a state pension is being paid. All pensions (annuities) are taxable as income under the PAYE system and are also subject to the Universal Social Charge, but not PRSI. Approved Retirement Funds (ARF's) however are subject to PRSI until age 66.

Chargeable excess is subject to income tax at a fixed rate of currently 40% jointly on Administrator and retiree. Threshold amounts applying to an individual will be either the Standard Fund Threshold ("SFT")[11], which is the maximum tax-relieved pension fund value an individual is permitted, currently set at €2 million or a Personal Fund Threshold greater than €2 million and less than €2.3 million.

For those in the private sector, chargeable excess tax on excess Defined Contribution benefits is taken in one go from their fund at retirement and no refund is provided if the retiree dies shortly afterwards.
In contrast, where public sector employees have benefits valued in excess of the threshold limit, they can opt to pay the chargeable excess tax in instalments over a period of up to 20 years, by deduction from gross pension, with outstanding instalments written off on death within the 20-year repayment period.

There is a limit on the amount of pension you can get from an occupational pension scheme at normal retirement age - broadly this is 2/3rds of your final remuneration, if you have completed 10 years' service and have no benefits from a previous scheme.

5.1. Tax on Lump Sums at Retirement

As per the Pensions Manual[12], a maximum of €200,000 can be taken as a tax-free pension lump sum amount. This is a total lifetime limit even if lump sums are taken at different times and from different pension arrangements. Lump sums between €200,001 and €500,000 are taxed at the standard chargeable amount (SCA) of 20%, with any balance over this amount taxed at marginal PAYE rate and subject to the Universal Social Charge and PRSI, if drawn down before age 66.

Lump Sum Tax Credit: There is a credit against chargeable excess tax liability for any standard rate tax paid on lump sums from 1st Jan 2011. This has the effect of extending the 'Threshold' amount. For example, if an employee pays max standard rate tax on lump sums of €60,000 since 1st Jan 2011 their Threshold limit before chargeable excess tax starts to apply is €2,150,000. In effect an extra €150,000.

[11] https://www.revenue.ie/en/tax-professionals/tdm/pensions/chapter-25.pdf
[12] Pension Manual - Taxation of Retirement Lump Sums Chapter 27

Therefore, the chargeable excess tax system can be looked on as having 3 components.

- A threshold amount, not subject to chargeable excess tax.
- Nil rate band of chargeable excess over the Threshold.
- The excess over the nil rate band liable to 40% chargeable excess tax.

5.2. Chargeable Excess Tax Payment (CET)

The Finance Act 2006 introduced a limit on the value of an individual's pension fund which may attract tax relief, and this may vary from year to year. This limit is called the standard fund threshold (SFT) with a value currently of €2 million. In certain circumstances, a higher threshold called the personal fund threshold (PFT) may apply for up to €2.3 million[13]. When the capital value of a Benefit crystallisation event (BCE) exceeds an individual's SFT or PFT, a chargeable excess arises equal to the amount by which the fund threshold is exceeded. This is an immediate tax charge at the higher rate of income tax for the year in question when it is drawn down from the fund[14].

The whole of the chargeable excess is subject to an upfront income tax charge[15], the pension scheme administrator is required to deduct and pay this tax to the Collector-General.

The amount of retirement benefit deemed to be crystallised for chargeable excess tax purposes is referred to as the 'BCE amount'. The BCE amount for lump sums taken, transfers to AMRF/ARF, transfers to buy an annuity and the amount retained in a vested PRSA is the open market value of the sum involved, i.e., the cash amount involved.

In the case of lump sums and gratuities the amount is the gross sum before deduction of any tax due on the lump sum. However, there are two separate regimes in operation as to the payment of any CET liability. One for the Public Sector and one for the Private Sector. We shall look at both in greater detail but first a brief synopsis. In the private sector, chargeable excess tax on excess defined contribution benefits is taken in one amount within 3 months of liability becoming due from their fund at retirement and no refund is provided if the retiree dies shortly afterwards.

Where public sector workers have benefits valued in excess of the Threshold limit, they can use up to 20% of net gratuity less any standard rate tax deducted from it. Any balance over 20% of the net gratuity is paid by the public service retiree. However, they can opt instead of using 20% of their net gratuity to instead pay the chargeable excess tax in instalments over a period of up to 20 years. This is by a deduction from their gross pension, with outstanding instalments written off on death within the 20-year repayment period.

So firstly, we shall look in greater detail at public service options re payment of CET:

- The relevant legislation provides that the tax paid by the pension administrator is a debt owing to the administrator from the individual. There are several options available to individual civil/public servants for reimbursing the administrator for the chargeable excess tax paid and clearing the debt under section 790AA. It also includes allowing any balance

[13] https://www.oireachtas.ie/en/debates/question/2019-11-12/119/

[14] Revenue - Pensions - Chapter-25

[15] Pensions Manual - Chapter 25 - For the years of assessment 2015 to 2021 the higher rate of income tax is 40%. For earlier years when the SFT and PFT applied, the higher rate was 41% from 2007 to 2014 and 42% in 2005 and 2006, depending on when the BCE occurred.

of the tax to be recovered from the gross annual pension of the individual over a period to be agreed with the administrator of up to 20 years[16].

- If the individual dies before the debt owing to the administrator is fully discharged (i.e., before the chargeable excess tax is fully recovered) the outstanding debt is released.

- The private sector has no facility to pay CET over a 20-year period. Instead under 787S TCA 1997 Payment of tax due on chargeable excess; the administrator of a relevant pension arrangement shall, within 3 months from the end of the month in which the benefit crystallisation event giving rise to the chargeable excess occurs, make a return to the Collector-General.

- In addition, in the private sector there are different rules re CET payment depending on whether a DC or a DB pension. In the event of any chargeable excess tax on DC benefits it is taken in one amount from their fund at retirement and no refund is provided if the retiree dies shortly afterwards. For a retiree with DC benefits, it is more tax beneficial to have a chargeable excess tax liability taken from their gross retirement benefits rather than net lump sum or by personal reimbursement from other personal funds.

Inequities in the tax treatment or public and private sector pension arrangements:

- Public sector workers can avail of the option to pay any CET liability over a 20-year period by a gross deduction in their pension benefits. This is in effect an interest free loan to pay an immediate tax bill over a 20-year period. In addition, should the pensioner die within the 20-year period the debt ends. A further advantage allowed by this facility is available for those with a combination of public and sector benefits. In such a scenario it may well be advisable to draw any private sector pensions first and if the additional public sector benefits create a CET, then they have the option to pay this CET over 20 years.

- Those in the private sector do not have these options. When facing a CET liability, they do not have 20 years to pay their bill but instead have 3 months to pay on clearly less favourable terms. A tenuous argument has been put forward that in the public sector the CET liability is paid up front by the employer e.g., the HSE. This argument simply is illogical as it is all taxpayer money paid by both those in the public and predominantly private sector.

- This differing treatment regarding the collection of CET between the public and private sector is clearly discriminatory and the same payment facility should be extended to the private sector. However, as we shall cover in the next section there are further advantages bestowed on the public sector in respect of CET for those who have dual public and private benefits.

[16] https://www.revenue.ie/en/tax-professionals/documents/notes-for-guidance/tca/part30.pdf (787Q (7) TCA)

6. Encashment Option

The Revenue's Pension Manual under Dual Private/Public Pension Scheme Encashment Option Chapter 29[17] covers the public service encashment option. This benefits those who work in the public service and also have substantial private pensions.
There are further tax implications when the remaining excess is drawn down as a pension. The provisions in section 787TA TCA allow an affected individual a once-off opportunity to encash their private pension rights, in whole or in part, from age 60 (or earlier, where retirement is due to ill health) with a view to eliminating or minimising the chargeable excess that would otherwise arise when the public sector pension crystallises.

It also states that where the encashment option is exercised in respect of a private pension scheme, the encashment amount does not constitute a "benefit crystallisation event" (BCE) in the hands of the individual for SFT or PFT purposes. In addition, where a private pension scheme has already been drawn down and is the subject of an encashment option, BCEs that occurred at the time of draw down are, depending on the circumstances, disregarded. A benefits encashment amount cannot be used as a contribution to, or the payment of a premium in respect of, a relevant pension arrangement. An encashment amount or deemed encashment amount is not regarded as a taxable distribution from an ARF or AMRF or as a withdrawal from a PRSA.

Benefits encashed do not count as a BCE for the purposes of the Thresholds etc.

- The encashment amount currently suffers tax called encashment tax at higher rate income tax and USC at a fixed rate of 2.00%. i.e., In total 42.00% currently.

- The net encashment proceeds are then paid to the individual.

The part of the private benefits that is over the Threshold is referred to in the legislation as the 'specified amount'. This is the amount which can be encashed. There are two types of encashment:

- **Total:** where all the private pension benefits are encashed. This occurs where the public service benefits on their own will exceed the Threshold amount.

- **Partial:** where the public sector benefits on their own will be under the Threshold but the addition of the private benefits brings the individual over the Threshold.

[17] https://www.revenue.ie/en/tax-professionals/tdm/pensions/chapter-29.pdf

Inequities in the tax treatment or public and private sector pension arrangements:

Public sector workers under s787TA Taxes Consolidation Act 1997, who also have personal pension benefits can avail of the above facility to encash their private benefits before retirement from the public service, so that the encashment is not a benefit crystallization event for the Threshold limit system.

Under this facility those with a mixture of public and personal pension benefits could potentially (depending on circumstances) eliminate a future CET liability by availing of the encashment option before accessing their public sector pension. By doing this any amount encashed does not count towards the threshold limit. Private sector workers do not have a similar facility to cash out any excess private pension benefits outside the Threshold limit.

7. Additional Superannuation Contribution (ASC)

Additional Superannuation Contribution (ASC)[18] was introduced on 1st January 2019, it replaced the Pension Related Deduction (PRD). Whereas PRD was a temporary emergency measure, ASC is a permanent contribution in respect of pensionable remuneration.

The Additional Superannuation Contribution[19] applies to individuals who are accruing pensionable benefits in respect of their current employment. Unlike the PRD, the ASC only applies employees who are members of a public service pension scheme and are accruing pensionable benefits in respect of their current employment. Thus, for example, anyone retained in a non-pensionable position under temporary Circular 21/2017 which allows for certain Civil Servants to be retained beyond their Compulsory Retirement Age of 65 years until they reach the age of eligibility for the Contributory State Pension, will not be liable for ASC.

ASC only applies to gross pensionable remuneration. A key difference between ASC and PRD is that ASC is chargeable on pensionable income and not taxable income. It is only chargeable on pensionable remuneration. Pensionable remuneration includes:

- Basic Pay (excluding non-pensionable overtime) due to the public servant in respect of that period

- Allowances, emoluments, and premium pay (or its equivalent) which are treated as pensionable pay

ASC will apply only to individuals who are in receipt of pensionable pay and applies to a person who is a member of a public service pension scheme or, receives a payment-in-lieu of pension or is entitled to an ex-gratia retirement gratuity (annual or lump sum) on retirement

ASC Treatment: ASC qualifies for tax relief but not Universal Social Charge (USC) relief. There is employer PRSI relief in respect of ASC, it does not qualify for employee PRSI relief. INTO and other unions secured reductions to the Additional Superannuation Contribution (ASC) which is payable by public servants when negotiating the PSSA (Public Sector Stability Agreement). The reduction became effective from 1 January 2020 and is the subject of DES Circular 0072/2019.

There is an annual earnings threshold below which no ASC is paid. From January 1, 2020, this threshold increased from its current €32,000 to €34,500. Therefore, €2,500 less income is exposed to the 10% ASC charge. This means that members pay €250 (€2,500 X 10%) less ASC in 2020 than they did in 2019.

To recognise the reduced value of such pensions, INTO and other unions secured a rate reduction (in addition to the above increase in threshold) for these members. The annual rate of ASC – from

[18] https://assets.gov.ie/7407/5ee8f7cf2f9e4030b65144424aae4a1d.pdf
[19] https://www.gov.ie/en/publication/c552ee-asc/

the threshold up to €60,000 earnings – was 6.66% for Single Scheme members in 2019; in 2020 the rate was 3.33%.

Inequities in the ASC tax treatment relating to both public and private sector pension arrangements:

Public sector workers obtain separate income tax relief (not limited by age related or the €115,000 earnings limit) on the Additional Superannuation Contributions (s790CA Taxes Consolidation Act 1997). On the other hand, both public and private sector workers are restricted to the age related and €115,000 net relevant earnings on all their personal contributions whether mandatory or voluntary. Mandatory contributions arise whereby pension scheme membership requires a certain level of employee contributions. Voluntary contributions arise where member through personal choice opts to make an additional contribution.

Why unlike the ASC are mandatory contributions in both the public and private sector outside of the scope of s790CA TCA 1997?

This is clearly discriminatory and the same regime applying to ASC contributions should be extended to both the public and private sector in respect of mandatory contributions. This would allow greater scope for those wishing to make additional voluntary contributions. In addition, we believe it is now appropriate for the Minister for Finance to recommence indexing the pensions earnings tax relief cap in s790A of €115,000. As it has not increased in line with average earnings, the real value of retirement provision which can be made by those in the private sector has been reduced, as retirement provision to be effective must be linked to earnings.

8. Challenges to the Long-term Viability of the Current Old Age Pension Model

Ireland faces challenges on the financial sustainability of its pension system as the population ages.[20] The OECD Reviews of Pension Systems compares the set-up and performance of retirement income arrangements in Ireland to those in OECD countries with comparable systems, proposes changes in the key parameters of the Irish state, occupational and private pension schemes and it outlines options for more profound structural reforms of the retirement income system. However, the challenging environment during the pandemic has made day-to-day the priority with millennials and employees in general questioning the benefits of contributing to a pension, in particular in the private sector where there is not the same job quality and security as in the public sector.

COVID-19 may have been the first pandemic or major challenge new employees have experienced and unfortunately it will not be the last one. If private employees do not appreciate the benefits of additional contributions to their pension's schemes, it will be difficult for them to survive with the state pension.

As noted in the IFAC Report we have an ageing population and thus the difficult question must be asked as to the long-term viability of the current old age pension model. This led to the inevitable question, are individuals basing their retirement future on an old age pension which may well be radically different in the future? We now have those answers in the form of a department of finance report titled "Population Ageing and the Public Finances in Ireland" - September 2021. This document makes stark reading. We shall quote briefly from the executive summary:

"The old-age dependency ratio in Ireland – a proxy for the number of retirees as a fraction of the number of workers – is set to near-double over the next 30 years, from 24 per cent at present to 47 per cent by the middle of this century (53 per cent by 2070).
To put it another way: there are currently around 4 persons of working age to support each person aged 65 and over; by 2050, the equivalent figure will be just over 2.

Such shifts in the demographic structure of the population will involve increased outlays in demographically sensitive components of public expenditure, such as pensions and healthcare. Analysis set out in this document shows that age-related expenditure is set to increase by 8 percentage points of GNI* by the mid-point of the century. In other words, this means by 2050 the annual cost of age-related expenditure is set to be €17 billion higher, in today's terms, than in 2019.

[20] Pensions Authority - OECD Report - Review of the Irish Pensions System 2014

Revenue increases will not be sufficient to fund all of these additional expenditure pressures. This is because growth in the productive capacity of the Irish economy is expected to slow significantly, as demographic trends weigh on additional labour supply. As public revenue evolves in line with economic growth, slower revenue growth will make it more difficult for the public finances to absorb the increase in age-related spending."

Consequently, it is quite clear that individuals need to take control of their own retirement destiny. This may well be in the form of compulsion i.e., auto-enrolment and incentives such as a favourable tax regime. However, not alone does the pensions tax regime need to be favourable it also needs to be fairly applied. At the moment this is quite simply not the case as major inequalities exist between the public and private sector pension tax regimes.

In our view, public sector employees are major beneficiaries of the inequality involved, in particular at senior level of the current pension relief system. Resolving inequities in the taxation treatment of public and private sector pensions is possible and necessary to change the perception that contributing to a pension is a costly luxury in particular after COVID-19. The Government tax incentives allow individuals to save towards their retirement. However, new entrants and existing employees understand that taxes will come down the line: apart from the lump sum that can be taken tax free up to a certain threshold, the payments are treated as income for tax purposes with the tax being levied at currently 20% or 40%. In addition, employees will also have to pay USC and, up to the age of 66 PRSI levied on ARF drawdown.

The design and institutional set-up of DC pension plans has been acknowledged by government as needing to improve in line with the OECD Roadmap for the Good Design of DC Pension Plans. In addition, the current inequities between the public and private pensions regime should be removed. This is to ensure that all citizens are treated equally to this end the Government could consider the following below:

- A review of the SFT Threshold amount. The limit referred to as the Standard Fund Threshold has been reduced several times from its initial (2005) €5m value to its current €2m value. The original chargeable excess tax system provided for automatic annual indexation of the SFT in line with an earnings index, and indexation was therefore applied in 2007 and 2008. However, since 2009 automatic indexation of the SFT has been replaced with optional indexation by the Minister for Finance in line with "an earnings adjustment factor which may be designated in writing by the Minister for Finance in December of the year of assessment preceding the relevant year".

  The Minister has chosen not to index the SFT limit since 2009. However, we contend that this is not the case. The SFT by successive minister's own inaction has been increased for those participating in defined benefit pension schemes. How has this happened? Public sector workers in the main will retire with a Defined Benefit Pension (Superannuation Scheme). Both Public and Private Sector Defined Benefits are tested against the SFT. However effectively two tests are carried out in this respect:

1. The first relates to benefits accrued up to 31/12/2013 which is at a fixed factor of 20 and the second relates to any benefits accrued from 01/01/2014 which are tested against Revenue Capitalisation Factors contained in Chapter 5 Revenue Pensions Manual. With reference to Example 3 Chapter 5 which relates to a married male civil servant who will have 40 years' service at age 60, with 20 years' service and €100,000 in AVC's with a 50% spouses' pension and pay parity equates to a Capitalisation Factor of 28.3 times.

   This Capitalisation Factor equates to an annuity rate of 3.534% and the question is very simple, would the annuity rate relating to this level of benefit for the private sector be 3.534%? The answer is of course in the negative. The Capitalisation Factors are valued at multiples for the Threshold limit system which are substantially below open market annuity rates.

2. Furthermore, pensions accrued prior to 1st January 2014 are converted into equivalent capital at 20:1, equating to an annuity rate of 5% whereas the real open market multiple would be substantially higher. The end result being that in real terms there are effectively two different SFT regimes. For those with defined contribution pensions it is simply based on their fund value whereas for those with defined benefit pensions it is based on Capitalisations Factors that are 12 years out of date and as such inaccurate.

Result is that those with defined benefit style pensions are effectively in receipt of a higher SFT limit and correspondingly less exposure to CET. Specifically in the case of the public sector when coupled with the inequities already outlined in respect of the CET regime and the Encashment regime mean very simply that the Public Sector pensions regime enjoys substantial tax advantages over the private sector. This inequality needs to be resolved. As a starting point we believe that as a minimum indexing the Standard Fund Threshold (SFT) limit should recommence from 2022 onwards, in line with the growth in average public service earnings.

- Allowing private sector workers with Defined Contribution benefits likely to be in excess of the Threshold limit to use s787TA encashment option (available currently only to public service employees with private pension benefits) to encash the excess.

- Providing a facility for private sector workers with retirement benefits in excess of the Threshold limit to pay chargeable excess tax in instalments from their ARF over 20 years, with outstanding instalments written off on death within the 20-year repayment period.

The Public sector workers ability to obtain separate income tax relief (not limited by age related or the €115,000 earnings limit) on the Additional Superannuation Contributions (s790CA Taxes Consolidation Act 1997) should be extended to all members of company pension schemes in both the public and private sector who are compelled to make a member contribution.

In addition, government should recommence indexation of the pension's earnings tax relief limit. With earnings and profit growth returning to the economy (public service salaries have been increased under the Public Service Stability Agreement (2018-2020), it is appropriate for the Minister for Finance to recommence indexing the pensions earnings tax relief cap in s790A of €115,000.

If not increased in line with average earnings, the real value of retirement provision which can be made by sole traders and partnerships is being reduced, as retirement provision to be effective must be linked to earnings. We suggest that the current pensions earnings limit for tax relief of €115,000 be increased in line with minimum public service salary increases as agreed under public service pay agreements.

A review of the current age-related limits is merited. Why? Because age related limits which set maximum allowable amounts which are not aligned with the real cost of funding even a modest level of pension in retirement are counterproductive.

This is demonstrated by the 'pensions calculator' function on the Pensions Authority website[21]. Please see Appendix 1 at the end of the whitepaper, this is a useful tool to show the level of funding required to meet an individual's pension target. It informs of the actual cost of achieving their own retirement income objectives.

It can make stark reading; you can play around with different variables. However, as an example a 50-year-old looking to fund a pension of €12,088 p.a. at a retirement age of 68 would need to be contributing 41.30% of salary. If funding were delayed till age 55 the cost rises to 60.80%.

This clearly demonstrates that the current age-related funding limits need to be reviewed. Consideration should also be given to both an increase in the limits to support higher contributions at an early stage in the life of pension contributors and an ability to carry unused relief.

Projected Retirement Pension	€12,912 p.a.
Projected Pension Shortfall to be funded	**€12,088 p.a.**
Total Target Pension in retirement	€25,000 p.a.

All figures shown are in **present day** terms

[21] The Pensions Authority - Pension Calculator

Based on the assumptions used by this calculator, you are not expected to meet your Target Pension of €25,000 p.a. in retirement.You need to increase your contributions to 41.3% of Salary a year in order to meet your Target Pension. Alternatively, you could consider reducing your Target Pension in retirement or retiring at a later age.

The sooner you start contributing to your pension the less you pay. See below your additional contribution requirement to meet your Target Pension depending on the age at which you start contributing.

You should keep your contributions to your pension under regular review.

Consideration should also be given to both an increase on the limits to support higher contributions at an early stage in the working life of the employees. This is an option used in other countries to support funding contributions in a "lumpy fashion"; which is required for workers and entrepreneurs alike who may have different capacity to save for retirement at different stages of their working life.

Several experts recommend allowing set back of unused relief for a period of at least 10 years to smooth the deductions for pension contributions across earnings during the whole working life.

9. Conclusion and Final Thoughts

We have stated earlier but we will now restate the following, this paper is not suggesting that the current favorable pension tax regime relating to the public sector be curtailed. We are instead proposing that this regime be extended to all pension participants. It is only appropriate to ask why we have one pension taxation regime for public servant pensions and another bluntly less favorable regime for the private sector. This is obviously inequitable. In addition, it could lead to the suspicion that those who 'write the rules' ensured that they were well protected. How could such a conclusion be arrived at?

Public Sector	Private Sector
• The ability to pay CET over a 20-year period in the form of an interest free loan which ceases on death.	• Those in the private sector when facing a similar CET liability, do not have 20 years to pay their bill but instead have 3 months to pay on clearly less favorable terms.
• An encashment option which can in whole or part remove pension benefits outside the Threshold limit and thus removed from CET regime.	• Private sector workers do not have a similar facility to cash out any excess pension benefits outside the Threshold limit.
• Mandatory ASC in the public sector not counting towards €115,000 tax relief limit.	• Mandatory contributions to all Company Pension Schemes both private and public, unlike the ASC regime are counted against the €115,000 tax relief limit thus limiting scope for additional voluntary contributions.
• Those in both the public and private sector with defined benefit style pensions are effectively in receipt of a higher SFT limit and correspondingly less exposure to CET due to the failure to review capitalization factors	• In contrast those who are members of defined contribution pension schemes (predominately private sector) by virtue of this failure to review capitalization factors have effectively a lower SFT limit and correspondingly a greater exposure to CET.

We will again reference Department of Finance Population Ageing and the Public Finances in Ireland September 2021 Report:

“Simulations show that, in a hypothetical scenario in which there were no further policy responses, the fiscal costs associated with population ageing would add around 20 percentage points to the debt-to-GNI* ratio by 2050. Beyond 2050, the fiscal position is expected to deteriorate significantly, with the debt-to-GNI* ratio reaching 180 per cent by 2070. A no-policy change approach is, accordingly, unsustainable.’

This warning comes from our own Department of Finance, and when read in conjunction with The IFAC Report, there is a clear need for change. This is not only to safeguard retirees’ future but indeed the long-term sustainability of the public finances.

As outlined earlier, this could be a combination of compulsion i.e., Auto-Enrolment and incentives in the form of an attractive and crucially an equally applied pensions tax regime. By extending the current public service favorable tax regime to the private sector as outlined above, apart from obviously remedying an inequitable pensions regime it would reinforce the belief that we are all in this together.

Considering a changing environment and in the interest of equality, it is difficult, if not impossible to justify the continuing existence of a two-tier pension’s tax regime.

10. References in Order of Appearance:

1. Revenue Pensions Manual
2. s790CA Taxes Consolidation Act 1997
3. Roma Burke and Tony Gilhawley in their paper “Private Pension Tax Relief - A paper on the Irish pensions taxation landscape” (November 2018)
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6. Report of the Interdepartmental Pensions Reform & Taxation Group - 2020
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8. https://www.oireachtas.ie/en/debates/question/2021-04-28/673/
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25. https://www.esrb.europa.eu/pub/pdf/occasional/esrb.op17~554f755910.en.pdf
26. Pensions Authority - OECD Report - Review of the Irish Pensions System 2014
27. The Pensions Authority - Pension Calculator

11. Appendix 1 - Information about the Pensions Authority

The Pensions Authority regulates occupational pension schemes, trust RACs and Personal Retirement Savings Accounts (PRSAs).

Their website provides access to a comprehensive range of information and guidance material to help understand pensions in Ireland. The information is organised under five separate personas to assist access to the most relevant information for each person.

Other supports such as Understanding Your Pension, Pension Calculator, Model Disclosure Documents, Trustee e-Learning and the Trustee Handbook are all accessible on their website.

Their information and guidance help those involved in managing pensions such as trustees, administrators, employers and advisors understand their obligations under the Pensions Act 1990, as amended, and how to meet them.

If you can't find the information you are looking for or have a specific question, you can email their enquiry service at info@pensionsauthority.ie

A useful resource is their pension calculator. This calculator allows to estimate the contributions employees should be paying to their pension to provide a Target Pension ? in retirement.

Your age:	18 – 70	45
Your current annual gross salary: ?	69000 €	
Your intended retirement age: ?	50 – 70	68
Target Pension as a % of pre-retirement salary: ?	0% 55% 66%	37950 € per annum
Are you currently in a pension scheme: ?	Yes / No	
Current fund value:	155555 €	?
Your monthly contributions, if any:	5 % OR €	?
Your monthly employer contributions, if any:	4 % OR €	?

Calculate

The results of this example are as follows:

How your Annual Target Pension is Made Up	Your Personal Pension From 68
Projected Pension from your Current Pension Arrangement (click ? for a breakdown of your Projected Pension from your Current Pension Arrangement)	€11,860 p.a.
Current State Pension	€12,912 p.a.
Projected Retirement Pension	€24,772 p.a.
Projected Pension Shortfall to be funded	**€13,178 p.a.**
Total Target Pension in retirement	€37,950 p.a.

IMPORTANT NOTE
Your accumulated retirement fund is converted to an annual pension using a long term average conversion rate. The actual conversion rate at retirement may differ from the conversion rate used in your illustration.

All figures shown above are in **present day** terms

Based on the assumptions used by this calculator, you are not expected to meet your Target Pension of €37,950 p.a. in retirement.You need to increase your contributions to 29.5% of Salary a year in order to meet your Target Pension. Alternatively, you could consider reducing your Target Pension in retirement or retiring at a later age.

The sooner you start contributing to your pension the less you pay. See below your additional contribution requirement to meet your Target Pension depending on the age at which you start contributing.

You should keep your contributions to your pension under regular review.

Start your pension early. The longer you leave it, the more you pay!

Additional contributions required to provide your Target Pension in retirement

The Age You Start Your Contributions	Age 45	Age 50	Age 55	Age 60
Yearly as % of Salary :	24.5% p.a.	33.2% p.a.	48.9% p.a.	84.9% p.a.
Yearly contributions :	€16,905 p.a.	€22,908 p.a.	€33,741 p.a.	€58,581 p.a.
Gross per Month :	€1,409	€1,909	€2,812	€4,882
Less Tax Reliefs	(€460)	(€575)	(€690)	(€805)
Net Contributions Per Month :	€949	€1,334	€2,122	€4,077