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Relate

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Occupational and personal pensions

The October 2018 issue of *Relate* described the State pension and the changes proposed to the pensions system in the Government's *Roadmap for Pensions Reform 2018-2023*. This issue of *Relate* sets out the various pension arrangements available in Ireland which are additional to the State pension. It explains how occupational and personal pension benefits are calculated, how benefits are taxed, and the tax relief on contributions. It also explains the impact on your pension of a change in circumstances, for example, changing your job or a relationship breakdown. Finally, it sets out how the pensions sector is regulated and how you can make a complaint.

Occupational pensions

An occupational pension is one that is provided by an employer. They are also known as company or employers' pension plans. Occupational pension schemes provide a regular income after retirement. Some also provide a lump sum payment on retirement.

In the private sector, occupational pensions are usually set up as *trusts* and the rules for the operation of the pension are contained in a document known as a *trust deed*. The people responsible for administering occupational pensions are known as *trustees*.

Occupational pensions of public sector and semi-state employees are regulated by legislation. Specific aspects of public sector pensions are outlined below (see page 2).

The trust deed (private sector) or legislation (public sector) sets out in detail:

- What contribution each member must make

- What contribution the employer must make
- Eligibility rules for joining the scheme
- Normal retirement age under the scheme
- Who is responsible for managing any funds in the scheme

There are limits on how much a person can receive as a regular pension income and as a lump sum from an occupational pension.

There is no legal obligation on employers to provide occupational pension schemes. However, if they do not provide one, they must give employees the option of a Personal Retirement Savings Account (PRSA) (see page 3).

Types of occupational pension

Occupational pensions fall into three main categories:

- Defined benefit schemes – which include many public sector pension schemes
- Defined contribution schemes
- Hybrid schemes

Defined benefit schemes

In a defined benefit scheme, each member will receive a set level of regular pension income on retirement. Exactly how much you can expect to receive depends on three factors:

1. The **length of service** you have. Although rules vary, many schemes require 30, 35 or 40 years' service for you to qualify for what is known as a *full pension*.
2. The **proportion of your income** for each year in the scheme. The same proportion applies to all scheme members. Generally, this is expressed as a fraction of relevant earnings for people who are entitled to a full pension (for example, one-sixtieth).
3. Your **earnings either at retirement or at defined points** in your time within the scheme. For example, your pension may be based on an average of earnings across your whole career or on the average of your earnings over your final three years.

Example:

Your defined benefit scheme provides for an annual pension entitlement of one-half of the final salary for members with 40 years' service. You have 30 years' service and a final salary of €40,000.

Your annual pension entitlement will be €15,000.

Calculation: €40,000 x 30/40 (years of service) x 50% (full pension entitlement according to the scheme) = €15,000.

However, the calculation will usually involve a number of other factors, for example, a break in service or employment, which may affect the final amount.

It is normal practice for employees to make a contribution to defined benefit schemes, and the amount is set out in the trust deed or legislation. Any shortfall in the pension fund must be made up for by contributions from the employer. In a very few cases, employees do not have to make any contribution.

Public sector pensions

Many public sector employees are members of defined benefit occupational pension schemes, where their pension is based on salary and length of service – and varies depending on when they joined the public service.

If you joined **before 6 April 1995**, a pension of one-eightieth of final earnings is payable for each year of service. A lump sum of three-eightieths of final earnings for each year of service, or of up to 1½ times final annual earnings, is also generally payable.

If you joined **on or after 6 April 1995**, pensions are coordinated with the State pension, meaning that your State pension entitlements are included in your regular pension income. This is often known as integration. A lump sum of three-eightieths of final earnings for each year of service, or of up to 1½ times final annual earnings, is also generally payable.

If you joined **on or after 1 January 2013**, your pension entitlement will be based on your career-average revalued earnings (that is, your earnings are averaged over your whole period of employment and adjusted for inflation), rather than your final earnings. A lump sum is also generally payable. This is known as the Single Scheme.

Defined contribution schemes

Under a defined contribution scheme, the contribution is fixed but the benefits are based on the value of the fund built up from the contributions. The value of the fund may vary over time. This means that you do not know what level of pension you will get on retirement.

Both you and your employer must pay regular contributions, normally set at a fixed percentage of your salary (for example, 4%). This money creates a pension fund, which is normally invested to ensure that its real value is not reduced by inflation.

Your pension fund at retirement may be worth less than the total value of your contributions, because:

- Investment performance may fall as well as rise
- Management fees are payable to the person or company managing the pension fund

Hybrid schemes

Occupational pension schemes can offer aspects of both defined benefit and defined contribution schemes. This means that you can predict a certain amount of income, as in a defined benefit scheme, whereas the remainder will vary as it will be subject to defined contribution rules.

Personal pension plans

You may prefer not to join an occupational pension scheme, or you may not have the option to do so (for example, if you are self-employed or your employer does not offer such a scheme). In these cases, you can save for retirement by choosing a different type of pension plan. These are normally known as personal pension plans or private pension plans and are managed by a life assurance or investment company.

Types of personal pension plan

The two main types of personal pension plan are:

- Personal Retirement Savings Account (PRSA)
- Retirement Annuity Contract (RAC)

Personal Retirement Savings Account (PRSA)

The most common type of personal pension is a Personal Retirement Savings Account or PRSA. This is a savings plan which also leads to the creation of a pension fund, so you can use both the savings and the pension on retirement. Anyone under 75 can open a PRSA. Most PRSAs are more flexible than occupational schemes and you can generally open one even if you have an irregular income or no income at all. However, it is always recommended that you make regular contributions to a PRSA – to ensure it grows large enough to provide an adequate income on retirement.

PRSAs work on the same basic principles as a defined contribution scheme. You pay part of your income into an account, which, in general, is then invested to ensure that the real value of the fund is not reduced by inflation. The value of the fund can go up or down, depending on investment performance.

PRSAs fall into two categories:

- Standard PRSAs
- Non-standard PRSAs

The main differences are:

- The charges are capped for standard PRSAs but not for non-standard PRSAs
- Types of investment are restricted in standard PRSAs but not in non-standard PRSAs

If your employer offers a PRSA rather than an occupational pension, they must deduct contributions from your salary and send these payments to the PRSA provider. The employer may also contribute to the PRSA but has no obligation to do so.

Retirement Annuity Contract (RAC)

The other main type of personal pension is a Retirement Annuity Contract or RAC. This is similar to a PRSA in that you build up a pension fund on a defined contribution basis. However, only people with what is known as *relevant earnings* may take out an RAC. "Relevant earnings" means income arising from a trade, profession or non-pensionable employment (for example, employment where no occupational pension is offered). You cannot contribute other forms of income to an RAC.

There are no restrictions on the charges or investments for RACs, unlike certain types of PRSAs, but there are important differences in tax treatment. Like PRSAs and occupational defined contribution schemes, the RAC pension fund is generally invested, so the value of the fund can go up or down, depending on investment performance.

Increasing your pension fund above the minimum requirements

Depending on the rules of the scheme or the PRSA, you may be able to pay in more than the specified contribution to increase your pension benefits. Such contributions are normally known as *additional voluntary contributions* (AVCs).

If you are a member of an occupational pension scheme that does not allow for AVCs, your employer must allow you access to a PRSA, so that you have the option of making AVCs.

There are limits on the additional amounts that allow you to claim tax relief. These limits increase with age and are discussed in the taxation section below.

If you are a public sector, civil service or semi-state employee and a member of an occupational scheme, you may be entitled to buy extra notional years of service to increase your eventual pension entitlements. This is known as *notional service purchase* (NSP). You can do this either by paying a lump sum or by making an extra regular contribution from your earnings.

Taking your pension benefits on retirement

Depending on the pension plan, you may have choices to make about how to take your benefits when you are nearing retirement. Each plan will have different rules about when and how you can take your retirement benefits.

Ill health and early retirement

With most pension plans, you can take your pension benefits at any time if you become seriously ill and have to give up work as a result.

Pension plans usually come to an end or mature when you reach a certain age, which is generally between 60 and 70. Some occupational pension plans allow early retirement from age 50, with the employer's consent. You can take benefits from an RAC at any time after 60, or from 50 with a PRSA. Some schemes may apply charges if you take benefits earlier than you had originally planned.

Otherwise when you can take your pension benefits depends mainly on the type of plan you have.

Options on normal retirement

On retirement, you may have the option of transferring all or some of your retirement fund into an annuity (see below) or other approved scheme that will provide a regular pension income.

If you are a member of a defined benefit occupational scheme, the scheme trustees will normally make the necessary arrangements for your pension income.

For personal pension plans, the options available on retirement include:

- Purchasing an annuity
- Investing in an Approved Retirement Fund (ARF) or Approved Minimum Retirement Fund (AMRF)

Annuities

With an annuity, you buy a regular pension income with all or part of your retirement fund. In return for you transferring your retirement fund to a life assurance company, the company will pay you a secure regular income for the rest of your life. The amount of this regular income depends on a number of things, including:

- The amount of your retirement fund
- Your age and state of health
- Whether you are male or female
- Whether your pension will continue to paid to any dependants on your death
- The annuity rate that the life assurance company offers at that time

Approved Retirement Funds (ARFs) and Approved Minimum Retirement Funds (AMRFs)

An ARF is a personal retirement fund where you can keep your pension fund invested as a lump sum after retirement. You can withdraw money from it regularly to give yourself an income. Any money left in the fund after your death can be left to your next of kin. Because an ARF invests in various assets (such as shares, property, bonds and cash), your original investment is not guaranteed. This means there is a risk that your fund could get significantly smaller over time.

If you are under 75 and want to buy an ARF, you must have a guaranteed annual income of at least €12,700. To be considered guaranteed, the income must generally come from an existing pension or annuity. If you do not meet this income threshold, you must purchase an AMRF.

An AMRF is a fund for people under 75 with a retirement income of less than €12,700 a year. You can transfer a maximum of €63,500 from your existing pension fund into the AMRF. You can only withdraw a maximum of 4% of the fund each year. An AMRF operates in a similar manner to an ARF, except you cannot withdraw any of your original capital until you reach 75 (you can only withdraw investment growth). Any remaining money left in the pension fund above €63,500 can be transferred into an ARF.

AMRFs automatically become ARFs when you:

- Reach 75, or
- Have a guaranteed annual income of €12,700 or over, or
- Die

Benefits payable on death

The benefits payable on death depend on the type of pension scheme you are in and other circumstances, such as whether or not you have a partner, spouse, children or other dependants.

Some pension arrangements provide pension benefits to dependants if you die while still in employment. Others pay benefits to your dependants if you die after retirement. The dependants may receive the benefits in a lump sum or as a regular pension income.

If you die before any pension benefits become payable to you under your pension arrangements, then a *death benefit* will be paid to dependants. This could happen, for example, if you die before the date that your benefit under an occupational pension scheme is due. It could also happen if you die before completing your payments into a PRSA or another personal pension arrangement.

Taxation of pensions

When considering the taxation of pensions, there are two issues to consider: the tax relief on pension contributions (the money being paid into the pension fund) and the tax payable on retirement income (the money you receive).

Tax relief on pension contributions

To make contributing to a pension more tax efficient, a number of tax reliefs are available for both you and your employer.

Employee contributions

Income tax relief is available in respect of employee contributions to:

- Occupational pensions
- PRSAs
- RACs
- Certain overseas pensions plans

You are entitled to income tax relief on your pension contributions at the highest rate of income tax you pay. This is currently either 20% or 40%. However, tax relief for employee pension contributions is subject to two main limits:

- An age-related earnings percentage limit (see table below)
- A total earnings limit (the maximum amount of earnings taken into account for calculating tax relief is €115,000 a year)

Age	Contribution limit of income for income tax relief
Under 30 years	15%
30-39 years	20%
40-49 years	25%
50-54 years	30%
55-59 years	35%
60 years or over	40%

For example, if you are aged 42 and earn €40,000, you can get tax relief on annual pension contributions up to €10,000. If you contribute 10% of income (€4,000) to your pension, your taxable income for income tax purposes will be €36,000.

Any additional voluntary contributions (AVCs) you make are added to your standard contributions for the purposes of tax relief.

For example, if you are aged 29 and earn €40,000, you can get tax relief on annual pension contributions up to €6,000. If you make a standard contribution to your occupational pension of 6% (€2,400) and make AVC contributions of 10% (€4,000), your total pension contribution is now 16% (€6,400). However, income tax relief applies to the first €6,000 only because it is capped at that limit.

People in certain occupations, such as professional sports, are subject to separate rules.

Employer contributions

The tax relief thresholds do not apply to the pension contributions of employers to occupational pension schemes.

However, the thresholds do apply to employer contributions to PRSAs or RACs. Therefore, if you and your employer make a pension contribution of 6% each to your PRSA, your pension contributions will be deemed to be 12% of income.

As the holder of the PRSA or RAC, you are responsible for claiming tax relief.

Pension funds do not pay tax on their gains at the point the gains are made, but do pay tax when paying out to you, as described below.

Tax payable on retirement income

Lump sums and regular pension income are treated differently for tax purposes.

Tax payable on lump sums at retirement

When you retire, you can usually take part of your pension fund as a tax-free lump sum. The amount you can take depends on the type of pension plan you have and how much you have taken in tax-free lump sums from other pension plans.

If you receive a lump sum or sums on retirement, the first €200,000 is tax exempt. Any amount after this up to €500,000 is taxed at 20%. Any amount over €500,000 is taxed at the marginal rate and subject to the Universal Social Charge (USC).

The maximum tax-free lump sum payment from an occupational pension is 1½ times your final salary and this amount is dependent on having a certain number of years' service. The maximum that can be taken as a tax-free lump sum from an RAC or PRSA is 25% of the fund.

Tax payable on regular pension income

Regular pension income from defined benefit schemes or annuities is subject to the standard income tax and USC rules and thresholds. Depending on your circumstances, you may also pay PRSI on pension income.

ARFs, AMRFs and PRSAs with some funds remaining (sometimes known as vested PRSAs), are taxed in a slightly different manner because they are funds available to you rather than income yet to be received. Tax in the form of income tax, USC and possibly PRSI is applied to any withdrawals made from ARFs, AMRFs and PRSAs.

Under tax rules, you must withdraw a certain percentage from your ARF or remaining PRSA each year. Tax is levied on this amount each year, regardless of whether you have taken it from your fund or not.

The minimum percentage taxed depends on your age and the amount of your pension fund.

Age for the whole of the tax year	Size of pension fund	Minimum portion taxed
60-69 years	<€2,000,000	4%
Over 70 years	<€2,000,000	5%
Over 60 years	>€2,000,000	6%

Changes in personal circumstances

Treatment of pensions when leaving employment

There are specific rules about what happens if you leave the pension scheme for whatever reason (for example, if you change jobs or become self-employed). If you have less than two years' qualifying employment when you leave your job, you may have to take a refund of the value of your own contributions less tax at the basic rate.

If you have at least two years' employment, your benefits from the pension scheme may be preserved within the scheme or transferred to another scheme. A preserved benefit means you will get a pension when you reach the scheme's normal retirement age. Alternatively, you can ask the scheme trustees to transfer your pension rights to a new pension scheme. Generally, any AVCs are treated in the same way as benefits under the main scheme.

PRSA providers can pay a refund if you have not contributed for two years, have a PRSA worth less than €650 and have given three months' written notice to terminate the PRSA.

Treatment of pensions in separation and divorce

If you and your spouse separate or divorce, it may affect pension entitlements arising from occupational or personal pension arrangements.

The Family Law Act 1995 sets out the treatment of pensions in cases of judicial separation, and the Family Law (Divorce) Act 1996 deals similarly with divorce proceedings. These Acts also apply to civil partners and cohabiting couples (see below).

To provide financially for a spouse and any dependants where a marriage has broken down, you may need to adjust your pension arrangements. This frequently happens in the context of judicial separation and divorce proceedings, as a court order is needed to require the pension administrators carry out any adjustment. This order is known as a pension adjustment order (PAO).

PAOs can take a number of forms, depending on your circumstances. Normally, the PAO designates a part of the pension for payment to a spouse and dependent children. The judge decides how much of the pension should be designated. The designated part of the pension remains in the pension scheme and is payable to your spouse and children when you reach pension age or die.

Where the court does not make a PAO, it may take into account the value of the pension and reflect this when making other financial orders.

Where you hold a number of pensions, a separate PAO must be made for each pension. This applies, for example, where you have:

- Pensions from separate employers which have never been transferred into a single pension
- A separate AVC, PRSA or RAC

After a PAO has been made, it will be unaffected if either you or your spouse later re-marry. You can apply for a PAO after a judicial separation or divorce, but the PAO will not be granted if either spouse remarries before it has been approved.

Treatment of pensions where a civil partnership breaks down

Where a civil partnership is dissolved, a court may make pension adjustment orders (PAOs) as it would in judicial separation and divorce proceedings between a married couple, with one significant difference. With a civil partnership, the PAO extends only to the civil partner and not to any dependants.

Treatment of pensions when a qualified cohabitation arrangement ends

You may be entitled to apply for a PAO if you are a qualified cohabitant – that is, you have been living with another person in a committed relationship for at least five years, or for two years if you have had a child with your partner. As with civil partnerships, a PAO does not extend to any dependants.

Upcoming changes to the pensions sector

Irish pensions sector

Ireland is unlike other European countries in how its private pensions are provided. One of the main features of the Irish pensions sector is the large number of small independent occupational pension schemes in operation. This means that many more individuals are involved as trustees in the running of pensions in Ireland than elsewhere.

In February 2018, the Government published *A Roadmap for Pensions Reform 2018-2023*. It proposes, amongst other things, to reduce the number of small independent occupational pension schemes. Multi-employer schemes and personal pensions will be encouraged, as is commonplace in other European countries.

New EU Directive

At EU level, new legislation has been passed governing occupational pension schemes. The EU Directive on the activities and supervision of institutions for occupational retirement provision (IORP II) came into effect on 13 January 2019. It aims to improve governance and regulation standards that apply to occupational pension schemes. It imposes additional professional standards for people involved in managing pension schemes. It also applies standards on communications and information to be provided to members and prospective members. The Directive is due to be transposed into Irish legislation in early 2019.

The new EU Directive includes:

- A requirement for pension trustees, as a body, to meet certain minimum qualification, experience and probity standards
- Greater obligations on trustees to ensure that certain key people involved in the day-to-day management of pension funds have the necessary qualifications and experience
- A requirement to notify the Pensions Authority when certain key people are being appointed to the day-to-day running of pension funds
- A requirement to have detailed written policies on issues such as risk management and internal audit
- Enhanced powers for the Pensions Authority to intervene in the running of pension schemes
- Minimum standards of communications with members

These new rules are expected to lead to more multi-employer schemes and fewer small occupational pension schemes.

Regulation of the pensions sector

Pensions Authority

The Pensions Authority is the statutory body tasked with overseeing the proper administration of pension schemes and the protection of pension rights for people living in Ireland. It has responsibility for overseeing occupational pensions, RACs and PRSAs, and has a regulatory role in respect of certain aspects of public sector pensions.

Its main functions include:

- Providing information and guidance to members and trustees of pension schemes
- Encouraging people to take part in pension schemes and adequately provide for retirement
- Supervising pension schemes for compliance with the Pensions Act and investigating potential breaches of the Act
- Monitoring defined benefit schemes to ensure sufficient funds are available to meet the ongoing and eventual needs of members
- Approving PRSAs with the Revenue Commissioners
- Keeping a public register of PRSAs and their providers
- Monitoring the operation of pensions legislation and pensions developments generally
- Issuing guidelines on the duties and responsibilities of trustees
- Advising the Minister for Employment Affairs and Social Protection on pension matters

When IORP II is introduced, the Pensions Authority's powers and responsibilities will be further enhanced. Further information on the Pensions Authority and a number of useful information booklets are available at: **pensionsauthority.ie**.

The Pensions Authority does not regulate the providers of annuities, AMRFs or ARFs or State pensions. The Central Bank of Ireland regulates the companies (such as banks, life assurance companies and investment firms) that provide personal pension plans and PRSAs.

Making a complaint about a pension

If you have a complaint about your pension, the action you may take depends on the type of pension.

- **Occupational pension scheme** – Contact your employer, the administrator of the plan, the trustees of the plan, the Pensions Authority, or the Financial Services and Pensions Ombudsman
- **Personal pension** – Contact your pension provider, the Financial Services and Pensions Ombudsman, or the Central Bank of Ireland

The Citizens Information Board provides independent information, advice and advocacy on public and social services through citizensinformation.ie, the Citizens Information Phone Service and the network of Citizens Information Services. It is responsible for the Money Advice and Budgeting Service and provides advocacy services for people with disabilities

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- **PRSA** – Contact the PRSA provider, the Pensions Authority, the Financial Services and Pensions Ombudsman, or the Central Bank of Ireland
- **State pension entitlement** – Contact the Department of Employment Affairs and Social Protection or the Social Welfare Appeals Office, or the Financial Services and Pensions Ombudsman

Financial Services and Pensions Ombudsman

The Financial Services and Pensions Ombudsman (FSPO) is the body responsible for dealing with complaints against pension providers and regulated financial service providers.

Various people can make pensions complaints to the FPSO. You may be:

- A member, an external member or a former member of a pension scheme
- A surviving dependant of a member who has died
- A contributor to a PRSA
- A personal representative of a member or contributor who has died
- A widow, widower, surviving spouse or civil partner of a member or contributor who has died
- A person with an entitlement under a scheme

Complaints can be made about:

- Occupational pensions
- PRSAs
- RACs

There are certain time limits for bringing cases to the FSPO:

- Six years from the date of the action that has given rise to your complaint or dispute
- Three years from the date that you became aware of or should have become aware of the action that has given rise to your complaint or dispute

The Ombudsman has discretion to consider a complaint or dispute outside these timeframes but cannot go back further than 13 April 1996. Further information on the FSPO and its services are available at: **fspo.ie**.

Complaint procedure

Before you can make a complaint to the FSPO, you must first complain to the pension provider. This is often known as *internal dispute resolution* or IDR. In your letter, you should set out all relevant details of the complaint, and provide copies of any relevant documents. You must give the pension provider 40 working days to respond to your complaint. If they fail to resolve the issue, they must send you a *final response letter* setting out the steps they have taken.

After 40 working days, if your complaint has not been resolved and you have not received a final response letter, you can then ask the FSPO to follow up on your behalf to get a final response letter.

If you are not satisfied with the outcome when you receive the final response letter, you can refer your complaint back to the FSPO. They will then deal with the complaint either informally (using mediation) or formally.

To achieve a formal resolution of the complaint, both parties must usually submit a large amount of paperwork. The FSPO will review this information and adjudicate on the matter. If they uphold a complaint, they may direct the pension provider to rectify the problem or pay compensation, or both. If they do not uphold your complaint, they will not direct any action. The FSPO's decision is binding and can only be appealed to the High Court.

There is no charge for using the FSPO. However, if you appeal the FSPO's decision to the High Court and you are not successful, you may have to pay all the legal costs.

The information in *Relate* is intended as a general guide only and is not a legal interpretation