iapf
representing pension savers

Response to the Consultation on the Standard Fund Threshold

February 2024

We welcome the opportunity to respond to the Consultation issued by the Department of Finance on the operation of the Standard Fund Threshold.

While it is understandable that there should be a limit on the level of tax incentivised pension savings, the operation of the Standard Fund Threshold (the Lifetime Allowance) does lead to practical issues and difficulties, and we will outline some of these in our response. We also believe it is noteworthy that the UK recently abolished their equivalent of the Standard Fund Threshold because of those practical issues and, primarily, its impact on retention and recruitment of staff in the public sector.

1. The lack of any indexation of the current €2m limit since its introduction in 2014 means it is impacting on individuals that it was not originally meant to impact on. This is having a knock-on effect on individuals leaving the workforce in order to avoid any excess tax that may be payable should they continue to work.

2. A review of the fairness between DB and DC members is required, for the purchasing power of a DC fund varies in line with annuity rates. DC members can also breach the Standard Fund Threshold, not because of additional contributions they have made, but because of the investment returns they have achieved. It does seem unfair that they suffer an excess tax because of this and also it does not seem that it should be the existence of the Standard Fund Threshold that would drive an excessively cautious investment strategy.

3. The use of the current valuation factors can be complex, even more so where people have benefits over different employments and a mix of DB and DC benefits, often with differing retirement ages (which is becoming the norm). This can also mean that the individual's current employer or pension provider is less likely to be aware of any prior pension benefits they might have which can often create circumstances where the individual is unaware that they are potentially accruing benefits in excess of the Standard Fund Threshold.

4. For many pension schemes, particularly in the public and semi-state sectors, there is no ability for members to opt out of their scheme. Where employees are aware of the Standard Fund Threshold, this often triggers early retirement rather than breaching it. Again, this would seem to be an unintended outcome. There seems to be a perception that people think all their pension will be subject to the excess tax once they exceed the Standard Fund Threshold.

5. The excess tax should be reviewed – there is an argument that it does not need to be as high as 40% to still have the intended impact i.e. to act as a disincentive but not excessively penalise those who end up with higher benefits, who often have little effective way of avoiding the limit. An excess tax of 20% could continue to provide that disincentive but be less penal.

6. There is also a particular issue in relation to public servants and the PRSI class their pension benefits are accrued in. For those who are class D their entire pension is from the company pension scheme whereas for those who are class A their pension comprises both the company pension and the state pension. Most of these pension schemes are based on the total member pension payable is the same regardless of class A or class D. However, the current SFT regime does not include the state pension element in its calculation thus penalising the D class member when compared to the A class member resulting in a significantly higher tax liability. It is recommended that when calculating the SFT liability for D class members that an allowance be made equal to the value of the state pension payable thus equalising the SFT liability.

7. The current SFT regime means that where a Pension Adjustment Order (PAO) applies to a member's pension benefits, the same threshold that applies to the capital value of the pension (€2m) for an individual is still applied to the total capital value of the pension before it is divided under the terms of the PAO between the 2 parties, despite the 2 parties now being deemed as separate entities. So, where an individual has €3 million in a pension with a PAO to pay half to their spouse, the chargeable excess is €1m and the tax on this (40% of everything over this €2m) is divided between both parties in proportion to the split of the pension under the PAO. It would seem more equitable, given the circumstances that, with a pension each of €1.5m, that they would each be able to apply their own €2m threshold to their portion of the pension and thus, in the example above, no tax would be payable as both would be under the €2m threshold.

Our Recommendations

- Careful consideration needs to be given to the rationale for a Standard Fund Threshold and how the appropriate amount is determined. The link between the value of a DB pension and the equivalent DC fund needs to be equitable.
- Consideration should be given to reducing the rate of excess tax to a level that would still disincentivise excess funding but be less penal, particularly as many people cannot avoid doing so. A level of 20% could, in our view, achieve this.
- Any Standard Fund Threshold should be indexed to maintain its value and act as a deterrent to individuals inadvertently breaching it. A good starting point would be to index in line with wages since 2014.
- A more simplified basis of calculating the Standard Fund Threshold, particularly where there are multiple employments should be considered.
- There should be a fairer way of valuing the benefits of pre and post 1995 public servants.
- If a Standard Fund Threshold is to continue to apply there may be no need for annual earnings or age-related contribution limits.
- Address the complex issues created when pension benefits are split as a result of a Pension Adjustment Order
- Ensure the review is completed in a timely manner as some individuals are now postponing retirement in order to await the outcome of this review.