Factsheet - Changes to tax relief for pension savings from 1 January 2014

Background

From 1 January 2014 the Government reduced the Standard Fund Threshold (SFT) from €2.3million to €2.0 million. Further changes were also made to the way in which pension benefits from defined benefit schemes like the Guinness Ireland Group Pension Scheme and Grand Metropolitan Irish Pension Fund are valued for the purpose of comparing against the SFT.

Whilst most members will not be affected by these changes some members will be, either now or in the future, and so we recommend you read this factsheet.

What is the Standard Fund Threshold (SFT)?

The SFT is the amount of tax efficient pension savings an individual can build up over their working life in Irish pension arrangements. Any pension savings in excess of this amount at retirement will be subject to an additional tax charge.

'Pension savings' includes the value of any defined benefit pension you have built up with Diageo (eg benefits under the Guinness Ireland Group Pension Scheme (GIGPS) or the Grand Metropolitan Irish Pension Fund (GMIPF)). It also includes the value of any other pension benefits you might have, any Additional Voluntary Contributions (AVCs) and any contributions to a Personal Retirement Savings Account (PRSA).

Before 1 January 2014 defined benefits, such as those under the GIGPS and GMIPF, were valued using a factor of 20 so the old €2.3m threshold was equivalent to a pension of €115,000 a year. If an individual also pays AVCs, the actual amount of any AVC fund would need to be added to the value of any defined benefit pension and if the total value at retirement exceeds the SFT, a tax charge will be applied to the excess.

What is the impact of the changes?

The SFT reduced to €2.0m from 1 January 2014. This is equivalent to a pension of €100,000 a year under a defined benefit scheme if the pension relates solely to pension benefits built up before 1 January 2014. It is difficult to calculate the equivalent pension if the pension is built up from benefits accruing both before and after 1 January 2014 because different factors will be used in the calculation. In the appendix to this factsheet we have set out a couple of examples of how the new tax regime works.

Age related factors

The factor of 20 is still to be used for pension built up before 1 January 2014 but for pension built up after this date, an age related factor will be used. This age related factor varies from 37 at age 50 to 22 at age 70. The full list of age-related factors is set out in the table on page 2.

Table of Relevant age-related factors

Age	Factor	Age	Factor
50 and below	37	61	29
51	36	62	28
52	36	63	27
53	35	64	27
54	34	65	26
55	33	66	25
56	33	67	24
57	32	68	24
58	31	69	23
59	30	70 and above	22
60	30		

Some schemes allow members to exchange pension for lump sum at retirement. This is known as commutation. The new legislation confirms that from 1 January 2014 it is the pension **before** commutation that is valued in the calculation.

Personal Fund Threshold (PFT)

Anyone who has built up pension benefits at 1 January 2014 which are in excess of the SFT of €2.0m can apply to the Revenue for a Personal Fund Threshold (PFT) equal to the value of their pension benefits at that date, but capped at the old SFT of €2.3m i.e. their pension benefits, subject to a maximum of €2.3m, will be protected but any benefits above the PFT would be subject to the chargeable excess tax on retirement.

What are the procedures for making a PFT application?

PFT information will have to be provided to the Revenue through a new online process which can be accessed at **https://www.ros.ie/paye-home-v1-web/pft/login**. Full details of the application requirements will be available when an individual applies online. The individual will need to provide basic identifying information about themselves and the various pension arrangements they are a member of. In addition, the individual will have to obtain from the administrator of each pension arrangement, a statement certifying the amount of their pension rights on 1 January 2014, calculated in accordance with the provisions of the legislation. In the case of a defined benefit scheme, the individual will also have to show the annual amount of pension built up as at 1 January

2014. For your Diageo pension benefits, this can be found on your annual benefit statement which was issued in March 2014 (copies are available from the Pension Team in Edinburgh).

Is there a deadline for a PFT application?

The deadline for making a PFT application is 1 July 2015.

Chargeable excess tax

As before, the penalty for exceeding the SFT or PFT is an additional 41% charge on the excess value (the "chargeable excess tax"). This is on top of the normal income tax at the individual's marginal rate and the Universal Social Charge (USC) payable on pension proceeds, giving a net effective tax rate of around 70% on this income. Any chargeable excess tax due has to be paid upfront by the pension scheme administrator and recovered from the individual.

How does the administrator recover chargeable excess tax paid in the case of defined benefit pension arrangements?

The legislation provides for the administrator to recover any chargeable excess tax paid either by way of an actuarial reduction in the individual's pension rights or by arranging to be directly reimbursed by the individual.

Maximum tax free lump sums

Before 1 January 2014, the maximum tax free lump sum that could be taken from a pension scheme was €200,000, while a further €375,000 could be taken subject to the standard income tax rate of 20%. Any excess above €575,000 was subject to marginal rate income tax of 41% and USC of 7%. The €575,000 threshold was 25% of the old SFT.

A consequence of the SFT having been reduced to €2.0m from 1 January 2014, is that the tax free cash threshold has dropped to €500,000. The tax-free amount of €200,000 has remained unchanged but the 20% rate of tax will apply to any amount between €200,000 and €500,000 and marginal rate tax on amounts above €500,000.

What happens next and what action should I take?

We have identified a small number of members who, based on the pension benefits they have with Diageo only, are expected to be impacted immediately or in the very near future by the reduction in the SFT from 1 January 2014. We will contact these individuals by the 18th July setting out the options available to them.

If you have pension benefits outside of Diageo you should contact the administrators of your other pension benefits and get details of the current value of your pension benefits and then send this to the Diageo Pensions Team so that they are able to check your overall benefits against the SFT when you come to retirement. If, having received the information, you believe the total value of all of your Irish pension benefits at 1 January 2014 is in excess of €2m you should contact the Diageo Pensions Team who will be able to assist you with an application for a Personal Fund Threshold (PFT). You are also strongly encouraged to consider consulting an independent financial adviser.

Contact Information

If you have any queries, please contact the Diageo Pensions Team using the details given below.

Diageo Pensions Team
Diageo plc
Edinburgh Park
5 Lochside Way
Edinburgh
EH12 9DT

Tel: 01 471 4422
Email: gmi.pensions@diageo.com

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Appendix to changes to tax relief factsheet

Example 1 - Patrick – total pension below SFT at retirement

Patrick is an active member of a Defined Benefits (DB) scheme, building up further DB pension after 1 January 2014. He has also paid Additional Voluntary Contributions (AVCs). He has no other pension benefits.

Can Patrick apply for a Personal Fund Threshold (PFT) at 1 January 2014?

Pension built up at 1 January 2014	€45,000 a year
Value of AVC fund at 1 January 2014	€60,000
Calculation of value of pension	€45,000 x 20 = €900,000 + €60,000
Total Value of Patrick's pension benefits at 1 January 2014	€960,000

No. Patrick's pension benefits are valued at €960,000. He can only apply for a PFT if the value of his pension benefits is in excess of €2million at 1 January 2014.

At retirement will Patrick be subject to chargeable excess tax on his pension benefits?

Let's say Patrick retires at age 65. The value of his pension benefits will be compared to the SFT at that time. If the value is greater than the SFT he will need to pay a chargeable excess tax.

Summary of his pension benefits

Total annual pension at 65	**€60,000 a year**
Pension built up at 1 January 2014	€45,000 a year
Pension built up after 1 January 2014	€15,000 (€60,000-€45,000)
Value of AVC fund at 65	**€90,000**

Value of pension at age 65 for comparison against SFT

Value of pension built up at 1 January 2014	€45,000 x 20 = €900,000
Value of pension built up after 1 January 2014	€15,000 x 26 = €390,000
Value of AVC fund	€90,000
Total value of pension benefits at age 65	€900,000 + €390,000 +€90,000
TOTAL VALUE	**€1,380,000**

Assuming the Standard Fund Threshold (SFT) remains at €2m Patrick will not have to pay 'chargeable excess tax' as the value of his pension benefits is below the SFT.

Example 2 - Mary – total pension above SFT at retirement

Mary is an active member of a Defined Benefits (DB) scheme, building up further DB pension after 1 January 2014. She has also paid Additional Voluntary Contributions (AVCs). Mary also has a deferred pension of €20,000 with a previous employer.

Can Mary apply for a Personal Fund Threshold (PFT) at 1 January 2014?

Current pension built up at 1 January 2014	€60,000 a year
Pension built up with previous employer at 1 January 2014	€20,000 a year
Value of AVC fund at 1 January 2014	€60,000
Calculation of value of pension equals the sum of	€60,000 x 20 = €1,200,000 €20,000 x 20= €400,000 €60,000
Total Value of Mary's pension benefits at 1 January 2014	€1,660,000

No. Mary's pension benefits are valued at €1,660,000. She can only apply for a PFT if the value of her pension benefits is in excess of €2million at 1 January 2014.

At retirement will Mary be subject to chargeable excess tax on his pension benefits?

Let's say Mary retires at age 62. The value of her pension benefits will be compared to the SFT at that time. If the value is greater than the SFT she will need to pay a chargeable excess tax.

Summary of her pension benefits

Total annual pension from current employer at 62	**€80,000 a year**
Pension built up at 1 January 2014	€60,000 a year
Pension built up after 1 January 2014	€20,000 (€80,000-€60,000)
Total annual pension from previous employer at 62	**€25,000 a year**
Pension built up at 1 January 2014	€20,000
Pension built up after 1 January 2014	€5,000 (€25,000-€5,000)
Value of AVC fund at 62	**€100,000**

Value of pension at age 62 for comparison against SFT

Value of pension from current employer built up at 1 January 2014	€60,000 x 20 = €1,200,000
Value of pension from current employer built up after 1 January 2014	€20,000 x 28 = €560,000
Value of pension from previous employer built up at 1 January 2014	€20,000 x 20 = €400,000
Value of pension from previous employer built up after 1 January 2014	€5,000 x 28 = €140,000
Value of AVC fund	€100,000
TOTAL VALUE	**€2,400,000**

Assuming the Standard Fund Threshold (SFT) remains at €2m Mary has a chargeable excess of €400,000 and will have to pay tax on this amount.

The chargeable excess tax is an additional 41% charge on the excess value of €400,000. This is on top of normal income tax at Mary's marginal rate and the Universal Social Charge (USC) payable on pension proceeds.