

Standard Fund Threshold Regime and Personal Fund Thresholds - Guidance Note

(This summary Guidance Note has been compiled by Revenue for information only and does not purport to be a legal interpretation of the statutory provisions governing the Standard Fund Threshold regime which are contained in Chapter 2C of Part 30 of, and Schedule 23B to, the Taxes Consolidation Act (TCA) 1997.)

At the outset, it should be noted that the Standard Fund Threshold (SFT) regime will have no tax consequences for the vast majority of individuals with pension arrangements, whether in the private or public sector.

1. What is the SFT Regime?

The SFT regime imposes a limit or ceiling on the total capital value of pension benefits that an individual can draw in their lifetime from tax-relieved pension arrangements, where those benefits come into payment for the first time on or after 7 December 2005. There are tax consequences where the limit is exceeded.

The limit was set at €5 million when first introduced on 7 December 2005. It was subsequently reduced to €2.3m from 7 December 2010 and was further reduced to its current level of €2m, with effect from 1 January 2014, by section 18(2) of the Finance (No. 2) Act 2013.

In certain cases, individuals can avail of a higher limit or threshold (called a “personal fund threshold” or PFT).

2. How does the SFT regime work?

On each occasion that an individual becomes entitled to receive a benefit under a pension arrangement for the first time (called a “benefit crystallisation event” or BCE) they use up part of their SFT or PFT, as the case may be. At each BCE, a capital value has to be attributed to the benefits that crystallise and the value is then tested against the SFT or the individual’s PFT, as appropriate, by the pension scheme administrator.

When the capital value of a BCE, either on its own or when aggregated with earlier BCEs, exceeds the SFT, or an individual’s PFT, the excess (called a “chargeable excess”) is subject to an immediate tax charge at 41% (called “chargeable excess tax”). Any chargeable excess tax due has to be paid upfront by the pension fund administrator and recovered from the individual.

In addition, when the remainder of the excess is subsequently drawn down as part of a pension (or, for example, by way of a distribution from an Approved Retirement Fund or vested Personal Retirement Savings Account) it is subject to tax at the individual’s marginal rate. The effective income tax rate on a chargeable excess can, therefore, be as high as 65%, excluding any liability to USC and PRSI.

3. What is a PFT?

If the capital value of an individual’s pension rights on 1 January 2014 exceeds the SFT limit of €2m, the individual can protect that higher capital value from any risk of incurring chargeable excess tax in the future, when the pension benefits are taken, by notifying Revenue of that higher capital value and obtaining a PFT certificate from Revenue for that amount.

4. How is a PFT calculated?

A PFT is the sum of the capital values of an individual's "uncrystallised" pension rights on 1 January 2014 in respect of all of his or her pensions arrangements, i.e. pension rights that the individual was building up on that date but to which he or she had not yet become entitled. This would include rights under defined benefit (DB) and defined contribution (DC) occupational pension schemes, AVCs, retirement annuity contracts, Buy-out-Bonds and PRSAs, etc. If the individual had already become entitled to pension benefits from any pension arrangement between 7 December 2005 and 31 December 2013 (called "crystallised rights"), the capital value of those rights have also to be included in the PFT calculation.

Where, on **1 January 2014**, the overall capital value of an individual's crystallised and uncrystallised pension rights exceeded the SFT of €2 million, that higher amount will be the individual's PFT, subject to it not exceeding the previous SFT of €2.3m.

5. How are uncrystallised pension rights determined for PFT purposes?

In the case of uncrystallised rights arising under DC arrangements, the capital value for PFT purposes is the value of the assets in the arrangement that represent the member's accumulated rights on 1 January 2014, i.e. the value of the DC fund on that date.

Because members of DB arrangements do not have an individual "earmarked" fund, the capital value of uncrystallised rights arising under such arrangements has to be determined using a formula. In these situations, the capital value is determined by taking the gross annual pension the individual would be entitled to under the rules of the DB arrangement if he or she retired on 1 January 2014 at his or her salary and service on that date and on the assumption that the individual had attained normal retirement age on that date. The gross annual pension is then multiplied by 20 (the standard valuation factor) to arrive at the capital value of the DB pension rights for PFT purposes. Future service after 1 January 2014 cannot be included in this calculation.

If the individual's DB arrangement provides for a separate lump sum entitlement (otherwise than by way of commutation of part of the pension), e.g. most public service schemes, the value of the lump sum entitlement (calculated on the same assumptions as above) is added to the capital value of the DB pension to arrive at the overall capital value.

6. How are crystallised pension rights determined for PFT purposes?

In the case of crystallised rights i.e. pension benefits that have already come into payment between 7 December 2005 and 31 December 2013 by, for example, the commencement of a pension or annuity, the receipt of a pension lump sum or the proceeds of a pension fund being placed in an Approved Retirement Fund (ARF), an Approved Minimum Retirement Fund (AMRF) or retained in a vested PRSA, the capital value is determined as follows.

For defined contribution arrangements, the capital value of the crystallised pension rights is the value of the cash/assets that were used to, for example, purchase an annuity for the individual or that were transferred to an Approved Retirement Fund. In the case of a pension lump sum, the value will simply be the cash amount of the lump sum paid to the individual.

For defined benefit arrangements **with a lump sum commutation option**, the capital value of the crystallised pension rights is the gross amount of pension that would have been payable to the individual (before any commutation for a lump sum) in the first 12 months from the date the individual became entitled to it, multiplied by 20 (the standard valuation factor). **Note** it is not the annual amount of pension actually **paid** to the individual in the first 12 months (which could reflect the fact that part of the pension was commuted for a lump sum), nor the **current annual rate** of the pension being paid (which may reflect adjustments in the pension rate since it was first awarded). Rather, it is the amount of pension that **would have been payable** in the first 12 months from the date the individual became entitled to it on the assumption that there had been no commutation of part of the pension for a lump sum or no adjustments made in relevant pension

payable. Any lump sum actually paid is, therefore, ignored in computing the capital value of the crystallised pension entitlements in such cases as it is already reflected in the pension capital value.

In the case of defined benefit arrangements with separately accrued lump sums, the capital value of the crystallised pension rights is the amount of pension actually paid to the individual in the first 12 months from the date the individual became entitled to it multiplied by the standard valuation factor of 20 plus the cash value of the separate pension lump sum paid at that time.

The following simple examples illustrate the above concepts.

Example 1

Paul is a member of a DC pension arrangement. The value of his pension fund on 1 January 2014 (i.e. his uncrystallised pension rights) is €1m. He had not become entitled to any pension rights since 7 December 2005. As the value of Paul's uncrystallised rights on 1 January is below the SFT of €2m, he cannot claim a PFT and the maximum allowable pension fund for tax purpose that Paul can build up is €2m.

Example 2

John is a member of a private sector DB pension arrangement. His pension fund administrator has indicated that, under the rules of the scheme, his accrued pension rights at 1 January 2014 would entitle him to a gross annual amount of pension (before any commutation for a lump sum) of €60,000, based on his salary and service on that date and on the assumption that he had attained normal retirement age on that date. The capital value of John's uncrystallised pension rights on 1 January 2014 is, therefore, €60,000 multiplied by the standard valuation factor of 20, i.e. $€60,000 \times 20 = €1.2m$. He had not become entitled to any pension rights since 7 December 2005. As the value of John's uncrystallised pension rights on 1 January 2014 is below the SFT of €2m, he cannot claim a PFT and the maximum allowable pension fund for tax purpose that John can build up is €2m.

Example 3

Mary is a member of a DB pension arrangement. Her pension fund administrator has indicated that her accrued pension on 1 January 2014 based on her salary and service on that date and on the assumption that she had attained normal retirement age on that date, is €95,000 before any commutation for a lump sum. Mary also has DC pension arrangements with a value on 1 January 2014 of €300,000. The capital value of Mary's uncrystallised pension rights on 1 January 2014 is, therefore, €2.2m, i.e. DB rights of $€95,000 \times 20 = €1.9m$ + DC rights of €300,000. She had not become entitled to any pension rights since 7 December 2005. Mary can apply to Revenue for a PFT of €2.2m and that represents the maximum allowable pension fund for tax purpose that Mary can build up. Any future accrual of pension benefits by Mary in her DB arrangement and any future increase in the value of her DC arrangement, either through further contributions or fund growth, will give rise to a chargeable excess and be subject to chargeable excess tax.

Example 4

Jean is a member of a DC pension arrangement the value of which is €1.8m on 1 January 2014 (i.e. her uncrystallised rights). Jean had already drawn down pension benefits under a separate scheme on 1 July 2009 which had a capital value for BCE purposes of €0.7m at that date (i.e. her crystallised rights). The combined value of Jean's crystallised and uncrystallised pension rights on 1 January 2014 is, therefore, €2.5m. This exceeds the SFT of €2m, so Jean is entitled to make a PFT application. However, Jean's PFT will be restricted to a maximum of €2.3m (the current SFT limit). Jean's maximum allowable pension fund at retirement is, therefore, €2.3m. The pension benefits she drew down in July 2009 have already used up €0.7m of her PFT leaving her with a PFT balance of €1.6m for use against her uncrystallised pension rights when she draws them down.

Whether Jean ultimately has a chargeable excess will depend on how her remaining DC pension arrangement performs up to the point when she takes her benefits. On the assumption that the value of her uncrystallised pension rights remains at €1.8m, she would have a chargeable excess at retirement of €200,000 (i.e. €1.8m - €1.6m).

7. How is a PFT notification made?

Previously, the PFT notification procedure was paper-based. However, with effect from 1 July 2014, the new electronic based notification system must be used. The new system can be accessed through the Revenue On-Line Service (ROS) or PAYE anytime. If not already registered, an individual will have to register as a user of one of these services in advance of accessing the new system.

8. Is there a time limit for making a PFT notification?

Yes. The time limit for making a PFT notification is 12 months after the date on which the electronic system is made available. A PFT notification must, therefore, be made before 2 July 2015.

However, regardless of the 12 month time period, where an individual is retiring or taking benefits from a pension arrangement earlier than 2 July 2015, the PFT notification must be made before benefits are taken (i.e. before the first BCE occurs). Otherwise the pension fund administrator is required to apply the SFT limit of €2m.

9. What has to be included in a PFT notification?

In making the notification, an individual will be required to provide certain identifying information and information about the various pension arrangements he or she has, or is a member of, including the capital value of the individual's pension rights under each arrangement as at 1 January 2014. To that end, he or she will have to obtain in advance from the administrator of each pension arrangement a statement certifying the amount of the individual's pension rights on 1 January 2014 relating to that arrangement, calculated in accordance with the provisions of the legislation. In the case of a DB arrangement, the individual will also have to indicate the annual amount of pension accrued at 1 January 2014 underpinning that calculation, as certified by the administrator.

Where an individual had become entitled to pension benefits under a pension arrangement between 7 December 2005 and 31 December 2013 (i.e. crystallised rights), the capital value of those rights at the date they crystallised must also be included in the PFT notification, with supporting certifying statements from the pension administrator.

The new electronic system has "drop-down menus" and information icons at each step explaining what is required.

10. Is there a limit on the PFT that can be claimed?

Yes. Regardless of the overall capital value of an individual's pension arrangements, in no case may a PFT exceed €2.3 million, i.e. the amount of the SFT that applied from 7 December 2010 to 31 December 2013. The electronic notification system will automatically apply this limit.

11. How is a PFT Certificate generated?

Once an individual accesses the electronic PFT notification system, inputs all relevant information, satisfies the criteria and submits the notification, a PFT certificate will be automatically generated and can be printed.

It is important to note that it will not be possible to submit an electronic PFT notification more than once. It is essential, therefore, that care is taken to ensure that the correct information and details are inserted before submitting the notification. If, having used the system to obtain a PFT certificate, it transpires that there was an error in the information entered or information was inadvertently excluded, the individual should contact Financial Services (Pensions) District of Revenue by email at:

lcdretirebens@revenue.ie

or by post to:

Financial Services (Pensions)
Large Cases Division,
Revenue Commissioners,
Ballaugh House,
73-79 Lower Mount Street,
Dublin 2.

12. What should an individual do with the PFT Certificate?

This PFT certificate is an important document which should be carefully retained. A copy of the certificate should be provided by the individual to the administrator(s) of his or her pension arrangement(s) in advance of pension benefits being drawn down from the arrangement. This will allow the administrator to apply the PFT to the capital value of the individual's pension benefits for the purposes of determining whether a chargeable excess arises on which tax needs to be paid.

In the absence of a certificate, the administrator is obliged to apply the SFT limit of €2m to the capital value of the benefits.

13. What if an individual already holds a PFT certificate with a value in excess of €2.3m?

If an individual already holds a PFT certificate from Revenue issued in accordance with the legislation as it applied before the Finance (No. 2) Act changes (which restricted a PFT to a maximum of €2.3m with effect from 1 January 2014), he or she retains that certificate, notwithstanding that it is for a capital value in excess of €2.3m. There is no need to make a new PFT notification under the electronic notification system.

14. What if an individual has already received a PFT certificate, or made a PFT notification, since 1 January 2014?

If an individual made a PFT notification under the previous paper-based system on or after 1 January 2014, and has already received, or is awaiting, a certificate from Revenue, there is no need to make a new PFT notification under the electronic notification system.

However, a PFT notification made on or after 1 July 2014 using the previous paper based process will not be accepted.

15. Are there any implications for an individual who had retired or drawn down all their pension rights before 1 January 2014?

No. If an individual has already retired and become entitled to all of his or her pension rights before 1 January 2014 and were not contributing to a pension scheme on that date (i.e. building up additional pension rights on that date) the new lower SFT limit and PFT procedures does not apply.

16. Is it necessary to retain records?

Yes. Section 787P(3) TCA 1997 places an obligation on both the member of the pension arrangement and the administrator(s) of the arrangement(s) to retain the certifying statements, referred to earlier, for six years and make them available to Revenue on being required by a notice in writing to do so. In the case of the member of the pension arrangement the records must be retained for six years after the date of the final BCE relating to all of his or her pension arrangements. In the case of the administrator(s) it is for six years after the date of the last BCE arising to the member under the pension arrangement of which he or she is administrator.

17. Are there penalties for failure to retain records?

Yes. Penalties arise if a person fails to comply with any of the obligations imposed on them under the relevant legislation.

The penalty is €3,000 for each failure.

18. Things to be aware of

- PFT Notifications may be audited by Revenue.
- A false declaration on a PFT Notification form may leave you liable to prosecution.