Funding and investments

Chapter 5

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Revenue
Cáin agus Custaim na hÉireann
Irish Tax and Customs

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5.1. General

The tax advantages of exempt approved schemes are controlled by imposing limits on benefits. The other important control is to prevent excessive funding of the scheme. The basic requirement is that scheme assets should not amount to more than what is required to provide the benefits which the scheme has a commitment to pay.

5.2. Actuarial reports

It is the duty of scheme trustees and administrators to monitor the scheme's funding. In the case of self-administered schemes, appropriate actuarial advice should be obtained at commencement and at regular intervals thereafter. Actuarial reports are not required for insured schemes where contributions are invested exclusively in a policy or policies that provide benefits according to a predetermined scale of premium rates. Particular attention should be paid to employee's additional voluntary contributions (AVCs).

5.3. Surpluses

There is no objection to a scheme holding a reasonable reserve. In any case where a valuation discloses a surplus in excess of 10% of the value of the fund assets, the matter should be brought to the attention of Pensions Branch, Large Cases – High Wealth Individuals Division. Cases will be reviewed on an individual basis. It is important to prohibit the build-up of monies in a tax-exempt fund that could not be used for the purposes of providing relevant benefits.

Normally, a scheme surplus should be dealt with by augmenting benefits within approvable limits or by reducing or suspending contributions to the scheme. In exceptional cases, part of the surplus might have to be refunded to the employer and taxed as a trading receipt.

5.4. Investments

Revenue's interest in scheme investments is to ensure that schemes are "bona fide established for the sole purpose of providing relevant benefits" (section 772(2)(a) Taxes Consolidation Act 1997 [TCA]). Certain investments may prevent approval or prejudice ongoing Revenue approval. These could include investments used for tax avoidance purposes and assets not used to provide "relevant benefits".

Specific investment rules for small self-administered schemes are detailed in Chapter 19.

Exemption from income tax of rental income by schemes in possession of residential properties

Pension schemes may acquire a residential property as an investment asset of the scheme. Such schemes are allowed to claim an exemption on income tax on rental income received from these properties. This exemption is provided for under section 774(3) TCA for occupational pension schemes in relation to rents.

Finance (No. 2) Act 2023 inserted a new section 790F into Part 30 TCA which provides that, from 1 January 2024, such an exemption shall not apply unless the person chargeable (within the meaning of section 790F TCA) has registered the tenancy with the Residential Tenancy Board (RTB).

Where such a requirement applies –

a) Revenue may request by written notice that the person chargeable provide, within 30 days of such notice, evidence that the qualifying lease has been registered with the RTB, under the provisions of Part 7 of the Residential Tenancies Act 2004, and

b) a copy of an entry in respect of the published register provided under section 132 of the 2004 Act, by the person changeable, will be accepted by Revenue as evidence of this registration.

Transactions deemed to be pensions in payment

Where scheme assets are used in connection with a transaction which would, if the assets in question were those of an approved retirement fund (ARF), be regarded as giving rise to a distribution under ARF legislation (see Chapter 23.6) then the use of those assets is treated as a pension paid under the scheme and is subject to tax. The amount to be regarded as a pension payment is calculated in accordance with ARF provisions. Any amount treated as a pension payment is no longer regarded as a scheme asset. The transactions detailed in Chapter 23.6 include the following:

- Loans, or the use of ARF assets as a security for a loan, made to:
    - the beneficial owner or a connected person, or
    - a close company where the beneficial owner or a connected person is a participator[1],
- Acquisition of property from the beneficial owner or connected person.
- Sale of ARF asset to the beneficial owner or connected person.
- Acquisition of residential or holiday property for use by the beneficial owner or connected person.

[1] This provision was inserted by section 18 Finance (No. 2) Act 2023, and only applies to loans made after the passing of the Act.

- Acquisition of property which is to be used in connection with any business of the beneficial owner, or of a connected person.[2]

- Acquisition of shares in a close company in which the beneficial owner, or connected person, is a participator.

A close company means a company under the control of five or fewer participators, or of participators who are directors. Please refer to section 430 TCA for a complete definition.

A participator in relation to any company, means a person having a share or interest in the capital or income of a company. Please refer to section 433 TCA for a complete definition.

"Connected persons" and "relative" are defined in section 10 TCA.

5.5. Borrowing

Section 772 (3E) TCA provides that:

> A retirement benefits scheme shall neither cease to be an approved scheme nor shall the Revenue Commissioners be prevented from approving a retirement benefits scheme for the purposes of this Chapter because of any provision in the rules of the scheme which makes provision for borrowing by the scheme.

The following rules apply to scheme borrowing:

1. Only assets purchased by the borrowing may be used to provide security to the lender.

2. Assignment of rental income to the lender is not permitted.

3. Life cover on the amount of the debt may only be provided outside the scheme.

4. Cross-collaterisation is not permitted (that is, an asset being used as security for a loan cannot also be used as collateral for another loan).

5. Interest only loans and loans for a period of more than 15 years are not permissible. The loan should be repaid in full prior to normal retirement age.

6. Use of other scheme assets to clear residual debt is not permissible.

[2] Where property is acquired for residential or holiday purposes, or for use in connection with any business, the distribution arises on the date such use commences. The amount of the distribution is the aggregate of the value of the ARF assets used in connection with the acquisition and any expenditure on improvement or repair of the property.

5.6. Geared property investment vehicles

In relation to investments made via geared investment funds and unit trusts, it is possible to link a scheme investment to a particular property, within a collective investment fund, provided that all acquisitions, disposals and lettings are on an arms' length basis.

5.7. Calculation of maximum contributions

To standardise benefit and funding calculations, the following methodology and capitalisation factors shown in Table 1 should be used. Current annuity rates form the basis for the calculation.

The methodology to obtain the maximum ordinary annual contribution to be paid by or on behalf of an individual employee (combined employer and employee) is as follows:

$$\text{Contribution} = \frac{\text{B X CF – (value of assets plus retained benefits)}}{\text{Term in years to normal retirement date, minimum 1 year}}$$

$$\text{Or} \quad = \frac{\text{N/60ths pension X CF- value of assets}}{\text{Term in years to normal retirement date, minimum 1 year}}$$

whichever is the greater.

B is the revenue maximum pension based on current remuneration but with service to normal retirement date.

CF is the maximum benefit capitalisation factor as detailed in the table below.

N/60ths pension is the pension that can always be provided from a scheme regardless of retained benefits.

This maximum ordinary annual contribution includes administration costs but not the cost of death-in-service benefits. The cost of death-in-service benefits may be added to the amount calculated using the above formula.

The maximum ordinary annual contribution for a group scheme would be the sum of the individual maximum allowed contributions.

Tax relief in respect of contributions in any one tax year is subject to the limits for employee contributions, as detailed in Chapter 3. Relief for employer contributions under section 774 TCA is discussed in Chapter 4. The limits on tax relieved pension funds also apply, as discussed in Chapter 25. Care must be taken to ensure that overfunding does not occur, as surplus funds may have to be refunded to the employer and taxed as a trading receipt. Details of maximum retirement benefits are contained in Chapter 6.

Additional voluntary contributions (AVCs) can be made if the total of employer contributions and employee normal contributions do not exceed the above limits and the total employee contribution limits as outlined in Chapter 3.

In the case of defined benefit plans where the value of pension assets are not readily available or earmarked at an individual level the following formula applies:

$$\text{Contribution} = \frac{\text{B X CF – (SchB X SchCF plus retained benefits)}}{\text{Term in years to normal retirement date, minimum 1 year}}$$

SchB is the scheme pension based on current remuneration but with service to normal retirement.

SchCF is the Scheme benefit capitalisation factor.

Example 1

A male employee with a dependant spouse has a salary of €100,000 and has 15 years until his intended retirement at age 60. He has accumulated assets of €1,000,000 in his pension plan. The maximum normal annual contribution the employer and employee can pay in total is:

$$\frac{2/3 \text{ X } €100{,}000 \text{ X } 32.4^{*} - (€1{,}000{,}000)}{15} = \frac{€1{,}160{,}000}{15} = €77{,}333 \text{ or } 77.3\% \text{ of salary.}$$

*This factor is taken from Table 1, line 1.

Example 2

A male employee has 20 years until retirement at age 65. His gross salary is €60,000, his pensionable salary is €50,000 and he has an AVC fund of €120,000. His scheme provides a 50% spouse's pension and fixed increases of 3% per annum.

	Salary / pensionable salary	**Benefit**	**Pension**	**Capital-isation factor**	**Value of benefits**	
Revenue maximum benefits	60,000	66.66%	40,000	28.4*	1,136,000	A
Scheme benefits	50,000	66.66%	33,333	22.6**	753,326	B
Current AVC fund plus value of retained benefits					120,000	D
Maximum benefit to be funded by AVCs					262,674	E=A-B-D
Maximum AVC rate as % of salary					21.9%	(E/20) / 60,000

* This factor is taken from Table 1, line 6.

** This factor is taken from the Table 5, allowing for a 50% spouse's pension and 3% pension increases.

Example 3

A married male civil servant has 20 years until retirement with 40 years' service at age 60. He has accumulated AVCs worth €100,000. The public sector scheme provides a spouse's pension of 50% and parity increases.

	Salary / pensionable salary	**Benefit**	**Pension**	**Capital-isation factor**	**Value of benefits**	
Revenue maximum benefits	60,000	66.66%	40,000	32.4*	1,296,000	A
Scheme benefits	60,000	50%	30,000	28. 3**	849,000	B
Gratuity					90,000	C
Current AVC fund plus retained benefits					100,000	D
Maximum benefit to be funded by AVCs					257,000	E=A-B-C-D
Maximum AVC rate as % of salary					21.4%	(E/20) / 60,000

*The factor 32.4 is from Table 1, line 1.

**The factor 28.3 is from Table 5 for a scheme providing 50% spouse's or civil partner's pension and the earnings indexed figures are used as the public sector scheme provides parity increases.

Table 1: Capitalisation Factors

The capitalisation factors to be used are as follows:

NRA	Female no spouse or civil partner	Female with spouse or civil partner	Male no Spouse or civil partner	Male with spouse or civil partner
60	27.5	30.0	24.4	32.4
61	26.8	29.2	23.6	31.6
62	26.0	28.4	22.8	30.8
63	25.3	27.5	22.0	30.0
64	24.6	26.7	21.2	29.2
65	23.8	25.9	20.4	28.4
66	23.1	25.1	19.6	27.6
67	22.4	24.3	18.9	26.8
68	21.6	23.5	18.1	26.0
69	20.9	22.6	17.4	25.2
70	20.2	21.8	16.7	24.4
71	19.5	21.0	16.0	23.6
72	18.9	20.2	15.4	22.8
73	18.2	19.4	14.8	22.0
74	17.5	18.6	14.2	21.2
75	16.9	17.8	13.7	20.5

Table 2: Sample Maximum Contribution Rates

Applying the above factors produces the following table for maximum annual contribution rates, assuming no pre-existing retirement benefits and an NRA of 60.

Current age	Female no spouse or civil partner	Female with spouse or civil partner	Male no spouse or civil partner	Male with spouse or civil partner
30	61%	67%	54%	72%
35	73%	80%	65%	86%
40	92%	100%	81%	108%
45	122%	133%	108%	144%
50	183%	200%	163%	216%

Table 3: Pension Increases linked to Consumer Price Index (CPI) and/or subject to a cap

The formulae in the tables above are easy to apply when there is a fixed rate of pension increase. If increases are in line with an earnings index the figures can also be taken from the table. In other cases, increases are related to the CPI but with such increases being capped at a fixed amount or uncapped. The table below shows the fixed increase to be used where the scheme provides increases linked to CPI.

Increases

CPI subject to annual cap of	Fixed increase
Under 1.5%	The actual cap
2%	1.50%
3%	1.50%
4%	1.75%
5% or over	2.00%

Table 4: Scheme Factors for females

Intermediate factors can be derived by interpolation:

Female – 0% spouse or civil partner

NRA	0%	1%	2%	3%	Earnings index
60	17.0	19.3	22.1	25.5	27.5
61	16.8	19.0	21.6	24.9	26.8
62	16.5	18.6	21.1	24.2	26.0
63	16.2	18.2	20.6	23.6	25.3
64	15.9	17.9	20.2	23.0	24.6
65	15.7	17.5	19.7	22.3	23.8

Female – 50% spouse or civil partner

NRA	0%	1%	2%	3%	Earnings index
60	17.5	19.9	22.9	26.5	28.7
61	17.2	19.5	22.4	25.8	27.9
62	17.0	19.2	21.9	25.2	27.1
63	16.7	18.8	21.4	24.5	26.3
64	16.4	18.4	20.8	23.8	25.5
65	16.1	18.0	20.3	23.1	24.8

Female – 100% spouse or civil partner

NRA	0%	1%	2%	3%	Earnings index
60	18.1	20.6	23.8	27.7	30.0
61	17.8	20.3	23.3	27.0	29.2
62	17.5	19.9	22.8	26.3	28.4
63	17.3	19.5	22.2	25.6	27.5
64	17.0	19.1	21.7	24.9	26.7
65	16.7	18.7	21.2	24.2	25.9

Table 5: Scheme Factors for males

Male – 0% spouse or civil partner

NRA	0%	1%	2%	3%	Earnings index
60	15.9	17.7	20.0	22.8	24.4
61	15.5	17.3	19.5	22.1	23.6
62	15.2	16.9	18.9	21.4	22.8
63	14.9	16.5	18.4	20.7	22.0
64	14.5	16.0	17.8	20.0	21.2
65	14.2	15.6	17.3	19.3	20.4

Male – 50% spouse or civil partner

NRA	0%	1%	2%	3%	Earnings index
60	17.3	19.6	22.5	26.1	28.3
61	17.0	19.2	22.0	25.4	27.5
62	16.7	18.8	21.5	24.7	26.7
63	16.4	18.4	21.0	24.0	25.8
64	16.1	18.0	20.4	23.3	25.0
65	15.7	17.6	19.9	22.6	24.2

Male – 100% spouse or civil partner

NRA	0%	1%	2%	3%	Earnings index
60	18.8	21.7	25.2	29.7	32.4
61	18.6	21.3	24.7	29.0	31.6
62	18.4	21.0	24.3	28.4	30.8
63	18.1	20.7	23.8	27.7	30.0
64	17.9	20.3	23.3	27.0	29.2
65	17.6	20.0	22.8	26.4	28.4