



Relate

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Pensions

People who have been contributing to occupational or personal pension schemes are understandably concerned about whether those schemes will be able to deliver the benefits which are expected from them. Pension funds have been badly affected by the current economic crisis and employers are trying to move away from defined benefit schemes. There are serious concerns about some schemes where the employer is in danger of becoming insolvent or is actually in liquidation. The rules about pensions are complex. Here we try to explain, as simply as possible, the differences between the different kinds of pension scheme, the rules that apply to how you take your benefit from a scheme and what happens if your scheme is in financial trouble.

This article does not deal with social welfare pensions except in so far as they have an impact on other pensions. The general official term for occupational and personal pensions is *supplementary pensions* – in effect, they supplement your State Pension. The primary income of most pensioners in Ireland is the State Pension and for a significant number of pensioners it is their only income.

Government policy on pensions

It is Government policy to provide a basic standard of living for pensioners through direct state support, that is, through the social welfare system, and to encourage people to make supplementary pension provisions for themselves in order to ensure an adequate retirement income. The main way in which you are encouraged to make supplementary pension provision is through tax relief on pension contributions. Most people of working age are likely to qualify for a State Pension (Contributory) when they reach 66. However, many people are not making adequate provision for supplementary pensions.

The Government published a *Green Paper on Pensions* in October 2007. This examined the current system and looked at various options for the future development of both social welfare and supplementary pensions – see *Relate*, November 2007 and January 2008. A public consultation process has taken place and the report of that process has been published. The Government is developing

a National Pensions Framework which will effectively be a White Paper. This will set out the Government decisions on the future development of pensions.

Occupational pensions

Occupational pensions are organised by employers to provide pensions to one or more employees on retirement and to surviving dependants on the death of an employee. There is no obligation on your employer to provide an occupational pension unless there is such a commitment in your conditions of employment. If there is no occupational pension scheme available to you, your employer is obliged to facilitate your access to a Personal Retirement Savings Account (PRSA) – see page 4.

A contributory pension scheme is one in which the employer and employee pay a contribution towards the scheme. The contribution may be a fixed amount but more usually it is a percentage of pay. Sometimes both employer and employee pay a set percentage while in other cases the employee pays a set percentage and the employer pays the amount necessary to ensure that the scheme is properly funded.

In general, occupational pensions are contributory. Some public service pension schemes are non-contributory, or at least they were before the introduction of the pension levy. These are described separately below. There are also some non-contributory schemes in the private sector – in these cases, the employer contributes to the scheme but the employees do not. The employer may pay a contribution into a fund from which benefits are payable or benefits may simply be payable out of current income.

Funded schemes

Virtually all occupational schemes are funded – the contributions are put into a designated fund and the benefits are paid from that fund. The most notable exception is the public service pension arrangement where there is no fund and benefits are paid out of current government expenditure – see below.

Funded occupational pension schemes are generally irrevocable trusts and are governed by trust law and the provisions of the Pensions Acts (and, to a limited extent, by EU law). Each occupational pension scheme has its own set of rules. Members of the schemes have certain rights in respect of information about the scheme.

A National Pensions Reserve Fund (NPRF) has been established to provide a fund for future payments of public service and social welfare pensions. This is different from funded pension schemes. In a funded scheme, you are a member of the scheme and you have a direct interest in, and claim on, the fund. You have no direct claim on the NPRF.

In funded schemes, the pension is separate from the employer's business. The fund is usually controlled by trustees who have specific legal obligations to the members (that is, the current employees, current pensioners and people who have preserved benefits in the fund). The trustees may be called administrators or pension fund managers. Their precise title is not important – if they have control over the funds they are trustees and have legal responsibilities to the members.

Defined benefit schemes

A defined benefit scheme, as the name suggests, defines the benefits you will get on retirement. It may state that you are entitled to, for example, a lump sum of the amount of your annual salary at retirement and an annual pension of 1/80th of your final salary for each year of service. Some schemes may simply provide for a specified amount. The contributions may have to be varied from time to time in order to make sure that the fund can meet the level of benefits. Some schemes have provisions for the employer to top up the fund if necessary. If this provision is not included in the scheme, then there is no obligation on the employer to top up the fund. In some cases, employers do this voluntarily.

Defined contribution schemes

A defined contribution scheme is one in which the contributions are set and the benefits are dependent on the amount in the fund. This means that you do not know what level of pension you will get.

Public service pensions

Public service pensions usually refer to the various schemes which cover the civil service, local authorities, teachers, Gardaí, the public health services and the non-commercial state bodies. Commercial state bodies generally have their own funded schemes which are usually defined benefit schemes – these are subject to broadly the same rules as other occupational pensions. Some are set up on a statutory basis so they are also subject to the terms of the relevant legislation.

The public service pension schemes are virtually all statutory and are virtually all financed on a pay-as-you-go-basis; that

is, there is no fund. Some are contributory and some are non-contributory. The recent introduction of the public service pension levy means that virtually all are now contributory. Some schemes are funded but these are gradually being taken over by the Exchequer. Recently it was decided that the funded schemes for the five older universities and a number of non-commercial semi-State bodies (for example, FÁS and the Arts Council) would be taken over by the Government. This means that their assets and liabilities are transferred to the Exchequer and the pensions will be paid on a pay-as-you-go-basis.

Public service pensions are generally transferable between one public sector employment and another.

There is no legal right to increases in public sector pensions but such increases may be granted by the responsible Minister with the consent of the Minister for Finance. In practice, increases are granted in line with increases in the salaries paid to serving public servants.

Those public servants who have been paying Class A PRSI since 1995 have integrated pension arrangements – see below.

Additional Voluntary Contributions

Occupational pension schemes, including public service schemes may allow you to buy additional years of service in order to meet any shortfall. This may be done as part of the primary scheme or by way of Additional Voluntary Contributions (AVCs) to a separate scheme.

Pension benefits

The benefits that you get from your pension scheme depend on the type of scheme it is and the rules that apply. In general, schemes provide for a payment to you in your retirement and most schemes include provisions for payments to your dependants after your death. Your dependants may include a spouse or partner – this depends on the precise terms of the scheme. Pension schemes may restrict post-death payments to spouses. If your scheme provides for a payment to a partner, then it may not discriminate between same-sex and opposite-sex partners. Most schemes also provide for early retirement on health grounds.

The amount of your pension depends on the scheme but it is common for the amount to be related to your income on retirement. The benefits are, of course, also related to the number of years you have been contributing to the scheme. The scheme may also provide for post-retirement increases in pension – approximately one-third of defined benefit pension schemes provide for such increases for pensioners. Most provide for increases in the pension in line with inflation.

Some provide increases which keep the amount of your pension related to current earnings in the job from which you retired. There may be a legal entitlement to increases linked to inflation but there is generally no legal entitlement to increases in line with earnings. However, it has been the practice to grant such increases in public sector pension schemes and in some of the schemes run by large employers. Schemes may provide such increases even if they are not obliged to do so.

You have to retire to avail of your occupational pension. The age at which you can retire is usually set in your conditions of employment. If you choose to retire early, you may not have enough contributions to get a full pension. You may be able to make AVCs to enable you to get a higher pension. If you are made redundant, you may be able to negotiate extra years contributions to the pension scheme as part of the redundancy package.

Integration of occupational pensions and social welfare pensions

Occupational pensions operate independently of the social welfare pension system and there is no statutory link between the two. However, many occupational pensions take into account the level of social welfare pension received in calculating the level of benefit; these are sometimes called integrated or co-ordinated or abated schemes. This may be done when you start to receive your pension but since 1999 your occupational pension may not be subsequently reduced because your social welfare pension is increased. If you take early retirement, depending on your scheme, your occupational pension may not be reduced until you start receiving your social welfare pension.

Preserving pension benefits

If you leave employment before you have reached pension age, your rights to benefit from the pension scheme to which you have been contributing may be preserved and must be preserved if you have two or more years membership of the scheme. The right to preserve benefits applies to pension rights built up after 1 January 1991. Preserved benefit means that you will be entitled to some pension based on your preserved contributions when you reach normal retirement age. The same does not apply to defined contribution schemes because the benefits payable from such schemes depend on the operation of the fund. Instead of simply leaving your preserved benefit where it is, you may opt to have it transferred to your new employer's pension scheme or to a life annuity contract or, in certain circumstances to a Personal Retirement Savings Account.

Personal Retirement Savings Accounts

Personal Retirement Savings Accounts (PRSAs) are designed to enable people, especially those with no occupational pension provision, to save for retirement. A PRSA is a contract between an individual and a PRSA provider in the form of an investment account.

Everyone under the age of 75 may contribute to a PRSA, even when they are not working. No minimum or maximum limits have been set on how much an individual can pay into a PRSA. Employers who do not have a pension scheme in place, or where certain employees are excluded from a company's occupational pension scheme, must provide these employees with access to at least one standard PRSA. Employers are not obliged to contribute to the PRSA scheme. PRSAs can be transferred, without penalty, from one provider to another.

If you have a PRSA you may start to avail of it at any time after 60 years of age and before 75. You don't have to retire to draw on your fund; once you are over 60 you can draw on your PRSA and keep working. If you are an employee, you can draw on your PRSA on early retirement from age 50. If you become seriously ill you can draw on the fund, regardless of your age at the time. If you die before drawing on your fund, your total contributions are passed on to your estate.

Personal pensions/Retirement Annuity Contracts

Personal pensions are basically insurance policies mainly taken out by self-employed people but anyone with non-pensionable income may take one out. The correct legal term for personal pensions is Retirement Annuity Contracts (RACs). They are governed by tax legislation and financial services legislation. They are not regulated by the Pensions Board.

You may contribute any amount towards your RAC but there are annual limits on the amount which attracts tax relief – see below. The premiums you pay are invested by the insurance provider – you can exercise various choices about where the investment is made. You may transfer your fund from one insurer to another.

You may take your benefit at any time between the ages of 60 and 75; you do not have to have retired. You have a number of options as to how you use the money in your fund.

You may take up to 25% of the fund as a tax-free lump sum. You may buy an annuity – that means you buy an insurance policy which provides guaranteed regular payments for the rest of your life in return for your investment. Alternatively, you may invest your fund (or part of it) in an Approved Retirement Fund (ARF) or an Approved Minimum Retirement Fund (AMRF).

You may place your money in an ARF if you are over 75 or if you have a guaranteed income of at least €12,700 a year for life. (Most people aged 66 or over would have this level of income from the State Pension (Contributory).) If you do not meet this minimum income requirement, you must invest at least €63,500 in an AMRF. You may not access the capital in the AMRF until you reach 75.

If you get an income from the ARF or AMRF, it is taxable in the normal way. If you do not take an income from an ARF, you are assumed to receive 3% of it each December and this is taxed in the normal way.

If you die before taking any benefit from your fund, the accumulated funds form part of your estate and are distributed accordingly. If you die after taking benefit and you have invested in an ARF, then the remaining funds form part of your estate but are regarded as your income in the year of death.

These options are available to some extent to AVCs paid by members of occupational pension schemes (either to their own schemes or to separate schemes). They are also available to PRSAs.

Tax treatment of pensions

The general principle is that you get tax relief on your contributions to a pension scheme – subject to age and income-related limits – and you pay tax on the pension when it is paid out to you.

Employees get tax, PRSI and health levy relief on pension contributions (but not income levy relief). Self-employed people get tax relief only. There is no limit on the amount which employers may contribute and get tax relief. There is a cap on your overall pension fund – this was set at €5 million in 2007 and is indexed annually. If you had a larger fund when this cap was set you may continue to hold and benefit from the larger amount.

All pension schemes must be approved by the Revenue Commissioners in order to attract tax relief. The scheme must meet certain conditions, for example, the maximum pension which may be paid is two-thirds of final salary.

The maximum pension contribution, in any one year, for which you are entitled to tax relief is related to your age and is expressed as a percentage of your earnings. For employees, "earnings" means gross pay for tax purposes, while for the self-employed, it means earnings less allowable expenses.

The current limits are as follows:

Age	% of earnings
Under 30	15%
30 – 39	20%
40 – 49	25%
50 – 54	30%
55 – 59	35%
60 years and over	40%

The maximum earnings that can be considered are €150,000 in 2009 (in 2008 the limit was €275,239). The 30% limit applies, irrespective of age, to certain sportspeople.

The investment income and capital gains of a pension scheme are exempt from income tax and Capital Gains Tax.

You may get a tax-free lump sum of up to one and a half times your final salary up to a maximum of 25% of the fund or, in the case of RACs, up to 25% of the value of your pension fund. You then pay tax on the pension you receive.

Regulation of pensions

Occupational pensions are governed by the law on trusts, by the Pensions Acts and, to a limited extent by EU rules. Occupational pension schemes are generally established under irrevocable trust. Under trust law, trustees of pension schemes have the principal responsibility for ensuring that the entitlements of the members are adequately protected and that they receive the pensions due to them.

Monitoring your pension scheme

Usually membership of your occupational pension scheme is a condition of employment and so you normally have no say in what sort of scheme it is. You have to accept what is there. However, you do have rights to certain information about your scheme.

You must be given certain basic information within six weeks of joining a scheme or within six months if it is a new scheme. This includes information on how contributions are calculated and on what benefits you can expect.

Apart from the initial information, you are also entitled to ongoing information about your level of benefit at the given time and your options in relation to additional contributions. If you do leave your job, you are entitled to a statement from the trustees about what your benefits are and how you can claim them.

Trustees are required to provide members with an Annual Report about how the pension fund is performing. This report must contain both a Trustees' Report and an Investment Report.

The Trustees' Report must give you information about, among other things, the trustees and their advisors, any changes in the constitution or rules of the scheme, and information about increases being paid to existing pensioners. The Investment Report must tell you about the investment policy being pursued and the value of the scheme's assets. The audited accounts of the scheme must also be included in the annual report.

Defined benefit schemes must get an actuarial valuation of the scheme's assets in relation to its liabilities. An actuarial valuation is a technical calculation involving various financial assumptions and assumptions about life expectancy. When this actuarial valuation is made, it must be available for members and trade unions to inspect within three weeks of being asked for it.

Responsibilities of trustees

The trustees are legally responsible for the proper running of pension schemes. They must make sure that the scheme is adequately funded and that the funds are properly invested. They must register their schemes with the Pensions Board within a year of the start of the scheme. If they fail to carry out their duties they may be prosecuted by the Pensions Board and the Board may ask the High Court to replace them.

The Pensions Board

The Pensions Board is the regulatory body for occupational pensions and PRSAs. All pension schemes must register with the Pensions Board. The Board itself is financed by fees payable by the pension schemes. The Board has extensive powers to inspect the books and records of pension schemes, to enter premises and to require people to give explanations. It may apply to the High Court to have pension scheme trustees replaced in order to protect the interests of the members.

The Board has produced a number of leaflets on the operation of the Pensions Acts. It provides information to members of pension schemes as to their rights under the legislation. If you have a complaint, the Board can advise you about your rights.

The Pensions Board
Verschoyle House
28/30 Lower Mount Street
Dublin 2
Tel: (01) 613 1900
Fax: (01) 631 8602

Web: www.pensionsboard.ie

The Pensions Ombudsman investigates and decides on individual complaints relating to occupational pensions and PRSAs.

Office of the Pensions Ombudsman,
36 Upper Mount Street
Dublin 2
Tel: (01) 647 1650
Fax: (01) 676 9577

Web: www.pensionsombudsman.ie

Problems with defined benefit schemes

Minimum funding standard

The Pensions Acts require that defined benefit pension schemes must meet a minimum funding standard. This is aimed at ensuring that the pension schemes have enough assets to enable them to discharge whatever liabilities exist if the scheme is wound up – in effect, to ensure that everyone who is entitled to a pension under the scheme can actually get that pension. Trustees of pension schemes are required to submit a funding certificate to the Pensions Board every three years. If a scheme does not meet the requirements of the funding standard, the sponsors or trustees must submit a funding proposal to the Pensions Board to restore full funding within three years. The Pensions Board can allow a scheme up to ten years to meet the standard in certain circumstances. If necessary, the Pensions Board may order a reduction of benefits.

The Minister for Social and Family Affairs recently told the Dáil that, based on the most recent actuarial funding certificates submitted to the Pensions Board, 75% of defined benefit schemes met the funding standard. Most of those schemes failing the test had a funding proposal in place. However, “the effective date of most of these certificates pre-dates the current market difficulties. Accordingly, the full extent of the problem and the actual level of under-funding will not

be fully apparent until schemes carry out their next actuarial assessment and report the results to the Pensions Board.”

There are currently 1,355 defined benefit schemes subject to the funding standard. It is estimated that more than 90% of these are now in deficit; the shortfall has been estimated at up to €30 billion.

Because of the problems pension schemes are facing, the Government announced some short-term measures in December 2008. These aim to allow pensions schemes more time to recover from their losses. Among other things, these mean that:

- Extra time is being allowed to schemes to put forward funding proposals. Trustees have 18 months to review the situation with sponsoring employers and to bring forward proposals for recovery.
- The Pensions Board may deal as flexibly as possible with applications for approval of funding plans.
- The Board has flexibility to allow more than 10 years for recovery plans in appropriate circumstances.
- The Board may take into account voluntary employer guarantees in approving recovery plans.

It is expected that the National Pensions Framework will include further measures to deal with the problem of underfunded defined benefit schemes.

What happens if an employer becomes insolvent

The assets of the pension scheme are legally separate from the assets of the employer. So, if your employer becomes insolvent, the assets of the pension scheme should not be affected by the insolvency. The insolvency probably does mean that the employer cannot continue to contribute to the fund but the assets which are already in the fund are preserved for the purposes of paying pensions.

Winding up of a defined benefit scheme

If a scheme is to be wound up, all members must be informed within 12 weeks of the decision. The trustees must then inform all members and existing pensioners of the amount of their benefits at the date the scheme ends.

If a defined benefit scheme does not have enough assets to meet the liabilities, there is no obligation on employers to provide for the shortfall. In the past, some employers have contributed to schemes in order to make up the shortfall but there is no legal obligation on them to do so.

The main liabilities of a pension scheme are to its members. These members are mainly existing pensioners, people with rights to a deferred or preserved benefit who have not yet reached pension age (deferred members) and existing employees (active members). The scheme may, of course, also have a range of other liabilities but we are not concerned with those here.

If a defined benefit scheme is wound up, there are rules about the order of priority for claims by members on the fund. Before the passage of the Social Welfare and Pensions Act 2009, the order of priority was as follows:

1. Any benefits secured by members by way of Additional Voluntary Contributions
2. The future benefits to those scheme members who are already in receipt of a pension or have reached normal retirement age (existing pensioners); this includes any future increases to which these existing pensioners may be entitled
3. Benefits to current employees who are members of the pension scheme and former employees with entitlement to preserved benefits; this also includes any future increases
4. Any subsequent benefits not yet discharged

In schemes that are being wound up, the trustees usually provide for the existing pensioners by buying annuities. If there are not enough funds to meet the liabilities in any particular category then each member's entitlement is reduced proportionally.

Social Welfare and Pensions Act 2009

The Social Welfare and Pensions Act 2009, which was passed in May 2009, contains a number of provisions dealing with pensions. The main changes relate to:

- Priority in the winding up of insolvent pensions schemes
- Restructuring of pension benefits within a scheme
- The creation of a pensions insolvency payment fund
- New rules on remittance of pension contributions

It provides for a change in the priority in cases of winding up. Existing pensioners still have priority over future pensioners (existing employees and former employees who have deferred benefits) but any future increases to which existing pensioners may be entitled now have lower priority than future pensioners. So, the order of priority is now:

- AVCs
- Current pensioners
- Future pensioners
- Future increases to both current and future pensioners

This change in order of priority applies to the winding up of schemes after 29 April 2009 and to schemes which were wound up before that date but which had not started to discharge the liabilities.

Restructuring of schemes

The Act also makes provisions for the restructuring of defined benefit pension schemes. Before the Act was passed, defined benefit schemes could have been restructured but such a restructuring could only affect the benefits of those currently in employment. It could not have affected the rights of people who were already retired or of people who were entitled to preserved or deferred benefits. The Government considered that this limitation on the restructuring of a scheme could lead to situations where the scheme would have to be wound up. The Act provides that a restructuring can now also affect people who are entitled to deferred benefits and can affect the post-retirement increases for all members including existing pensioners. The pension payable to existing pensioners cannot be affected but the scheme could be restructured in such a way as to provide that there would be reduced or no future increases for such pensioners. Scheme members are entitled to make representations to the trustees before any such restructuring. The Pensions Board may order such a restructuring in certain circumstances.

The Act also allows pension scheme trustees, with the consent of the Pensions Board, to make amendments which are considered necessary to secure the future viability of the scheme where the only alternative to such changes is the winding up of the scheme. In general, trustees are liable for breach of trust but the Act now provides powers to the courts to grant relief to pension scheme trustees from liability for

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Head Office

Ground Floor

t + 353 1 605 9000

George's Quay House

f + 353 1 605 9099

43 Townsend Street

e info@ciboard.ie

Dublin 2

w www.citizensinformationboard.ie

breach of trust where the court deems that the trustee acted honestly and reasonably with regard to the circumstances of the case.

Failure to remit pension contributions

The Act includes arrangements for greater monitoring and more severe penalties for the failure of an employer to remit employee contributions, which have been deducted from the employee's pay, to the pension scheme.

Pensions Insolvency Payments Scheme

The Act provides that the Minister for Finance may, after consultation with the Minister for Social and Family Affairs, introduce a Pensions Insolvency Payment Scheme (PIPS). The full details of this are not yet available as detailed regulations have to be made before it can come into effect. It is proposed to introduce PIPS for a period of three years, after which it will be reviewed.

The plan is that PIPS would apply to situations where an employer is insolvent and the pension scheme cannot meet all its liabilities. The scheme is intended to make it cheaper to pay for the pensions of retired pension scheme members so that more money is available for the pensions of those yet to retire. Under PIPS, trustees of eligible pension schemes will have the option of paying the Exchequer a sum that will cover the cost of paying the pensions of retired members instead of buying annuities. It is expected that this will, in some cases, be a cheaper option than buying annuities on the open market. Any savings would then be put towards the pensions of those yet to retire, thereby reducing to some extent their pension shortfall. Pension schemes that want to participate in PIPS will have to be certified as eligible by the Pensions Board. They will then have to apply to the Minister for Finance to participate in PIPS. They will then be quoted a price by the National Treasury Management Agency for the cost of paying the pension. Trustees can then compare the cost of participating in PIPS to the cost of annuities on the open market before deciding which option to choose.

PIPS does not involve the Government subsidising the pension schemes. It is intended that there will be no cost to the Government in operating the scheme.

It is not intended at present to extend PIPS to support the underfunded pension schemes in cases where the employer is not insolvent. The National Pensions Framework may include some proposals to deal with these underfunding problems.

EU rules and employer insolvency

EU Directive 80/987/EEC provides that member states must ensure that the necessary measures are taken to protect the interests of employees and of people who have already left employment when an employer becomes insolvent. What exactly this means was considered by the European Court of Justice in Case C-278/05. This dealt with a UK defined benefit pension scheme where the employer had gone into liquidation and the pension scheme was being wound up. The scheme did not have enough assets to meet the claims of all the people who had contributed.

In this case, the ECJ held that

- The directive does not oblige the member states themselves to fund the rights to old-age benefits.
- Inasmuch as the directive states in a general manner that the member states 'shall ensure that the necessary measures are taken', the directive leaves the member states some latitude as to the means to be adopted to ensure protection. A member state may therefore impose, for example, an obligation on employers to insure or provide for the setting up of a guarantee institution in respect of which it will lay down the detailed rules for funding, rather than provide for funding by the public authorities.
- The directive cannot be interpreted as demanding a full guarantee of the rights in question.

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