**Approved Retirement Funds:**
**Tax on Deemed Distributions**

## Background

Included in the Finance Act is the introduction of a deemed distribution tax on Approved Retirement Funds (ARFs) with effect from 2007. It is intended that with effect from 2007 ARFs will be deemed to have distributed 1% of their fund value each year and that this deemed distribution will rise to 3% by 2009. The deemed distribution will be taxed at the ARF holders marginal tax rate and applies to those over aged 60 at the beginning of the year.

This tax is clearly designed to enable the government to accrue some tax from those retirees who may not be using their Approved Retirement Funds to provide them with an income in retirement. High net worth individuals can use their ARFs to continue to enjoy tax free investment returns and might have no intention of ever drawing down money from such Funds. For such individuals their pension account/ARF might not be about planning for an income in retirement

The IAPF understands the problem that the Minister of Finance has identified and is seeking to grapple with. It is clearly not appropriate that some wealthy individuals may be using the tax advantages available to pension's savings for anything other than retirement planning.

However it is clear that any deemed distribution tax levied on ARFs should be allowable as a carry forward tax relief on subsequent draw downs or otherwise the deemed distribution tax becomes a double taxation.

## Problem with Deemed Distribution Solution

The IAPF notes that the Minister has favoured the deemed distribution approach to tackling the "failure to draw down" issue. From the Department of Finance's point of view the advantage of this approach is that it reduces the period of deferment before which the State will start to receive income tax from the pension's savings. While this approach is instinctively justifiable in the case of a high net worth individual its implications for an ordinary working person could be draconian.

As an example take the case of a person retiring on a low salary with a Pension Account worth perhaps 4 times their salary at age 65. This person would probably take a tax free lump sum of once salary and (assuming they were entitled to do so) invest the balance of 3 times salary in an AMRF and ARF. Their logical retirement plan would be to live off their state pension while drawing down

part of their tax free lump sum for a number of years. During this period they might also work part time (perhaps from age 65 to 70) in the expectation that they would not then have to draw down any of their AMRF/ARF moneys until age 70. It seems clear that the Minister would not wish to discourage such flexible and sensible retirement planning by imposing a deemed distribution tax on their pensions savings between 65 and 70.

It seems obvious that any deemed distribution tax should most certainly not apply to AMRF moneys. The Minister may be aware that the IAPF has argued for many years that the €63,500 limit beyond which pension moneys can be invested in ARFs as distinct from AMRFs is much too low. We attach a copy of an extract from our 2005 budget submission as an example. The Minister might take this opportunity to revise this threshold up to a more appropriate level and then exempt AMRFs from the deemed distribution tax. If the Minister does not consider this approach to be appropriate we would suggest that he at least consider introducing a de minimis limit so that the deemed distribution tax might not apply to ARFs below a certain value provided the member is then aged less than 70 say.

Some mechanism needs to be found to ensure that a tax designed to discourage the abuse of pensions savings by high net worth individuals does not prevent ordinary people from planning appropriately for their retirement income. Any deemed distribution tax should not be applied below certain de minimis money limits particularly below certain ages.

In addition any deemed distribution tax levied on an Approved Retirement Fund should be allowable as a carry forward tax relief on subsequent draw downs in order to avoid double taxation.

**Note: AMRFs/ARFs are currently not available for members of group pension arrangements but that it is IAPF policy that the availability of AMRF/ARFs should be urgently extended to all defined contribution pension arrangements.**

24 July 2006

**Excerpt from IAPF Budget Submission 2005**

## 5. Approved Retirement Funds and DC Schemes

The IAPF believes that members of a defined contribution pension schemes who have full flexibility regarding the investment of their fund prior to retirement should have similar flexibility post retirement rather than being forced into annuity purchase at times when interest rates and the subsequent low bond yields and high cost of annuity products may significantly reduce the purchasing power of their retirement savings.

The IAPF believes that it is illogical that the Finance Act should distinguish between stand-alone PRSA products that operate on a defined contribution basis and trust based defined contribution schemes by only attaching ARF retirement options to PRSA products. Such a policy puts hundreds of thousands of workers at a disadvantage for no logical reason.

The IAPF believes that it is important to underpin minimum income security within the ARF framework and believe that the AMRF limits ought to be increased to take account of inflation since the scheme's introduction in 1999.

### Submission

**The IAPF recommends that the ARF (Approved Retirement Fund) and AMRF (Approved Minimum Retirement Fund) retirement options be extended to Defined Contribution (DC) schemes.**

**The IAPF also recommends that AMRF limits should be increased from the original levels set in 1999 and index linked going forward.**