Personal Finance

In association with Oakwood Financial Advisors

Impact of recent High Court victory for consultants' pension limits

Following a significant increase in queries from HSE hospital consultants concerned at the impact of pension limits on their entitlements after a recent High Court ruling, **Oakwood Financial Advisors** offer advice and guidance on getting the best outcome

The recent High Court terms of settlement for the reinstatement of pre-2010 and 2013 salary cuts for Health Service Executive (HSE) consultants has brought a renewed focus on revenue pension limits for many hospital consultants due to the potential tax liability which may arise.

Significant tax liability

In many cases, there will be a significant increase in the tax liability due at retirement as a result of the reinstatement of salaries. The retrospective increases in salary for eligible consultants has implications for the calculation of the capital value of their pension entitlements. At Oakwood Financial Advisors we have had a significant increase in queries from consultants concerned at the impact that the current pension limits will have on their retirement planning.

Loss of expertise to health system

What is even more worrying for the health system is that an increasing number of consultants are considering retiring early — in part because of these pension concerns.

The Irish Hospital Consultants Association (IHCA) has been an ardent campaigner over the last several years in trying to raise the pension question with the various stakeholders (HSE and Department of Health) but there has been a lack of political will to address the issue. With the HSE under significant pressure, our creaking health system can ill-afford to lose doctors with so much experience and expertise.

Increased confusion

The reinstatement of consultants' salaries to the pre-2010/2013 levels has also led to confusion for those consultants looking towards retirement. For an area that was already complicated, a recent directive from Revenue has added even more confusion. Revenue has now advised that those individuals who have already been issued with a Personal Fund Threshold (PFT) Certificate in December 2010 and January 2014, may now be eligible to re-apply for a revised PFT at a higher limit.

— Consultants who have already been issued with a PFT as at December 7, 2010 may be eligible to apply on a 'lookback' basis for a revised PFT.

— Consultants who have already been issued with a PFT as at January 1, 2014 may be eligible to apply on a 'lookback' basis for a higher PFT as at December 7, 2010.

— Consultants who were not eligible before to apply for a PFT in either 2010 or 2014 may now be able to apply on a 'lookback' basis.

€2 million (down from €5.4m)

Since January 2014, the limit an individual can have in their accumulated pension pot at retirement is €2m (this has reduced from €5.4m in 2010). For those with defined benefit schemes (HSE consultants employed pre-2013) all benefits accruing after this date are capitalised by a factor of 20, or greater, depending on an individual's retirement age. Once you exceed the current limit of €2m you are looking at a minimum 40 per cent tax bill on pension benefits over this limit. However this can potentially increase up to 68 per cent depending on how benefits are drawn down.

Mitigate tax

Oakwood Financial Advisors would be concerned that too many doctors are considering leaving the HSE because of potential tax charges on their pensions without being fully aware of the options available to mitigate the tax and without examining their overall financial circumstances.

Limit easily exceedable

While €2m sounds like a hugely significant sum, the revised revenue capitalisation factors which apply mean that a consultant on a modest pension (relative to their working salary) can easily find themselves exceeding the PFT. The table illustrates the point.

Professional Added Years (PAY)

While PAY can push you over the revenue limit, they may also allow you to apply for a retrospective increase in your PFT as a result. If dealt with correctly, this may allow you to receive a higher PFT and reduce or negate any potential tax liability.

Be aware of all options

Unfortunately, when addressing these issues, too many doctors are making decisions based on tax charges alone without looking at their overall financial picture. While they could face additional tax charges by staying in the HSE pension scheme, if they leave they may miss out on ancillary benefits, which may mitigate the possible tax charges. It is difficult enough to have a clear understanding of expected pension entitlements at 60 or 65 due to the various elements and rules involved. Now with salary reinstatement, it has become even more complicated for some consultants. Knowing these projected benefits is a key requirement in order to put an informed, prudent financial plan in place.

Avoid double tax

You need to be aware of where you are from an overall limit. Otherwise you may pay on the double at retirement. The right advice has never been more important for HSE consultants with regard to their options towards retirement planning.

> The retrospective increases in salary for eligible consultants has implications for the calculation of the capital value of their pension entitlements

Reducing potential tax bills

The good news is that there is some scope to reduce your tax liability if you do exceed the Standard Fund Threshold:

1. Tax on any pension lump sum (up to €200,000 paid out tax free with a balance up to €500,000 taxed at 20%) can be offset against the tax due on exceeding the limit.
2. For HSE employees the tax liability can be paid as an interest free deduction from their HSE pension over 20 years (no impact on spouse death in retirement entitlement and no recovery on early death) — in essence, this is an interest free loan.
3. One can use a little known encashment option on any personal pension benefits at age 60 before taking HSE benefits. This option is only available to those in the public service.
4. Retire your benefits on a staggered basis drawing your private pension initially in order to crystallise their value now, so that any further growth will not impact on your PFT limit. A plus for individuals with both HSE (or GMS) pension and private pension benefits is that you do not have to retire in order to draw down your private pension benefits.
5. Take early retirement in order to keep under the €2m limit.

Which option to consider needs careful review before making a decision. Expert advice from an experienced advisor, familiar with this area, is essential.

Minimise risk

There are a couple of strategic steps which you can take in order to ensure that you minimise the risk of a significant tax liability when in an overfunded position.

1. Request a breakdown of your current values and expected pension benefits from your pension providers or, in the case of HSE employees, your relevant department. Most hospitals have a contact person for such queries.
2. Gather together the information (or request your financial advisor to do so) and get an experienced financial advisor /pension specialist to review your figures.
3. Ask your advisor if they have the necessary experience in this area to provide the right advice. The majority would lack familiarity with both the GMS and HSE pension schemes.
4. Putting the correct plan in place is critical. Each individual's circumstances will vary, depending on their years of service, salary level and private pension values.

Ronan McGrath, Managing Director, Oakwood Financial Advisors

Worrying trend — incorrect submissions

Due to the volume of requests being submitted to the various HSE pension sections across the country, there has been a worrying increase in incorrect projection of benefit statements. These are being given to doctors who try to estimate if they will have a potential tax liability to deal with on retirement. Issues such as applying incorrect revenue multiples to calculate benefits, or years of service, being omitted, are commonplace.

In one recent case, a consultant was advised, by his pensions department, that he has no liability on retirement. On review, we noted an error in the figures that he received, with the unfortunate result in him having a pending €200,000 tax liability. Better to know now than come retirement when your income streams may be limited.

In another case we reviewed, we calculated a consultant's years of service were not recorded by her pensions dept correctly. This would have resulted in her losing out on the inclusion of Professional Added Years in her benefits. When this was amended it gave her a 20 per cent up lift in her annual annuity payment and a 50 per cent uplift in her lump sum payment.

Peace of mind

Getting the right advice on your retirement planning is very important. Putting a financial plan in place is part of this planning as it gives you peace of mind.

You will know that no unexpected tax bills are due from Revenue and you can look at maintaining the quality of your lifestyle in retirement. You will be able to relax and enjoy the well-earned benefits from your years of hard work. IMT

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Example

Take a simplified example of an HSE consultant looking at retirement in 2019 with a prospective public service pension of €100,000 p.a. (€5,000 assumed to be accrued after January 1, 2014), a related gratuity of €300,000, private pension benefits of €500,000 and a current PFT of €2m.

Currently this individual has a prospective chargeable excess on retirement at age 65 assuming all benefits are taken together of:

HSE pension accrued before January 1, 2014	€95,000 x 20	€1,900,000
+ Pension accrued after January 1, 2014	€5,000 x 26	€130,000
+ Public Service (gratuity) lump sum		€300,000
+ Private benefits		€500,000
Total pension benefits		**€2,830,000**
Chargeable excess		**€830,000**
Chargeable excess liability (tax due)	€830,000 x 40 per cent	€332,000
Less credit for standard rate tax deducted from gratuity		- €45,000
Total tax due		**€287,000 ***

If eligible for Professional Added Years, the PFT can increase up to €2.3m, which reduces the potential tax liability by €120,000 immediately.

* The projected chargeable excess liability (in 2019) is €830,000 x 40 per cent = €332,000 less a credit for €45,000 for standard rate tax deducted from the gratuity and 25 per cent lump sum from private benefits, leaving a net chargeable excess liability of €332,000 - €45,000 = €287,000.