Spotlight

Hewitt

A retirement and investment update from Hewitt Ireland

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Budget 2009 – part II

In light of the continuing sharp deterioration In the public finances, the Minister for Finance announced a further set of budgetary measures In the Dáil today (7 April 2009). There was much speculation and press comment in advance of the Budget that the tax reliefs granted in relation to pensions would be reduced or eliminated, with particular focus on the tax free lump sum at retirement, and the marginal rate of relief granted (up to a cap) on contributions paid.

The Minister announced no immediate changes in the tax treatment of pensions but commented "*The Commission on Taxation is examining various aspects of pension tax treatment including the treatment of lump sums and I expect to be dealing with their recommendations in the 2010 Budget next December*".

The Minister opened his Budget speech by outlining 6 essential steps to renewal

- Stabilize public finances
- Restore the banking system
- Regain competitiveness
- Protect jobs and invest in training
- Stimulate economic confidence
- Restore our reputation abroad

If no action were taken to increase revenues or cut spending, the deficit in 2009 would be 12.75% of GDP. The borrowing requirement will be reduced to 10.75% of GDP by a combination of tax increases of €1.8bn and a reduction in expenditure of €1.5bn. The Minister announced that the European Commission has accepted the Government's proposal to "address our structural problems" within a 5 year timeframe. He also indicated that additional taxation of €1.75bn would be raised in 2010 and €1.5bn in 2011, and that he would be considering options such as taxation of child benefit, carbon and property taxes and "elimination of unnecessary reliefs". Further increases might be required in the later years of the 5 year plan depending on the performance of the economy.

The main immediate taxation changes are

- Doubling the rates of the income levy, coupled with lowering the thresholds, so that it now applies to annual earnings of €15,000 (2%) and reaches 6% at approximately €175,000
- Raising the limit on earnings for employee PRSI to approximately €75,000 p.a.
- Increasing the health levy to 4% on earnings up to approximately €75,000, and 5% thereafter
- Increasing the rates of capital gains tax and capital acquisitions tax from 22% to 25%
- Increasing the rate of Deposit Interest Retention Tax (DIRT) to 25%
- Introduction of 1% levy on life assurance premiums from 1 June 2009
- Restriction of mortgage interest relief to the first seven years

The Minister announced a range of cutbacks in public expenditure but no changes in the main Social Welfare benefits, although he hinted that there might be reductions in future if negative inflation continues. He also announced a new early retirement scheme for public servants aged 50 or over which will come into effect from 1 May 2009 and will be reviewed in the 2010 Budget. Early retirement pensions will be paid with no actuarial reduction together with 10% of the retirement lump sum, with the balance of the lump sum payable at the normal retirement age of 60 or 65. The key point is that those retiring early would not be replaced, therefore cutting the overall public service pay and pensions bill. He also announced some "tweaking" of the recently introduced public service pension levies to exempt the first €15,000 of earnings, and introduce a higher rate of 10.5% for earnings over €60,000, at a cost of €100m in 2009.

The Minister also made reference in his speech to discussions which have been taking place with the pensions industry in relation to an initiative to enable pension funds to invest in infrastructural and development projects. In the Summary of Budget Measures, it is stated that legislation would be introduced to enable the assets (€1.7bn) and liabilities (€3bn) of the pension schemes of certain universities and non-commercial State agencies to be transferred to the Exchequer, with the assets being managed as part of the National Pensions Reserve Fund.

In the section of his speech dealing with regulation, the Minister confirmed that the Central Bank will be responsible for "financial supervision and financial stability oversight, providing for full integration of the prudential supervision and stability of individual institutions as a whole" and would be provided with significant additional resources and expert staff.

In what is probably the most controversial part of his speech, the Minister announced the establishment of the National Asset Management Agency (NAMA) to take on the so-called toxic assets of the banks so that the banks can resume lending activity. The assets to be transferred could have a nominal value of €80bn to €90bn, but would be substantially written down by the banks before being acquired by NAMA, in return for which the Government would issue bonds to the banks. The Department of Finance has issued a detailed Q&A about the operation of NAMA, which states that the establishment of NAMA is a priority for Government, with the relevant legislation to be enacted "before the summer".

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