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Tax Relief for Pension Contributions: Application of Earnings Limit

Background

Section 790A of the Taxes Consolidation Act 1997 provides that for the purposes of giving income tax relief to an individual on contributions made to certain pension products^[1] an aggregate earnings limit is to apply.

This article illustrates the operation of the earnings limit where an individual has both earnings from employment and income from self-employment and makes contributions to both an occupational pension scheme/statutory scheme and a personal pension plan.

Tax relief for pension contributions

Tax relief for pension contributions is subject to two main controls.

The first control is an age-related percentage limit^[2] of an individual's remuneration/net relevant earnings. This provides that the maximum pension contribution in respect of which an individual may claim tax relief may not exceed the relevant age-related percentage of the individual's remuneration/net relevant earnings in any year.

The second control places an overall upper limit on the amount of remuneration/net relevant earnings that may be taken into account for the purposes of giving tax relief. The earnings limit is set at €150,000 for 2009^[3]. This limit applies whether an individual is contributing to a single pension product or to more than one pension product.

Contributions to a single pension product

In a situation where an individual is contributing to a single pension product, the *maximum* tax relievable pension contribution is the relevant age-related percentage of *the lower* of:

- the individual's remuneration/net relevant earnings and
- the earnings limit.

In effect, this means that tax relief on pension contributions is limited :

- where an individual's remuneration/net relevant earnings exceeds the earnings limit, to the lower of the actual contributions made and the relevant age related percentage of the earnings limit, and
- where remuneration/net relevant earnings is less than the earnings limit, to the lower of the actual contributions made and the relevant age related percentage of the individual's remuneration/net relevant earnings.

For example, an individual aged 50 with earnings of, say, €200,000 in 2009 and making contributions to an occupational pension scheme may claim tax relief on the lower of the actual contributions paid and 30% of the earnings limit of €150,000 (i.e. €45,000).

So if the individual is making contributions of 40% of salary (i.e. €80,000), tax relief would be limited to contributions of €45,000 (i.e. the lower of €80,000 – the actual contribution –

and €45,000 – 30% of €150,000). If he is making contributions of 20% of salary (i.e. €40,000) he could claim tax relief on the full amount (as this is lower than 30% of €150,000).

Similarly, an individual aged 40 with self-employed income (net relevant earnings) of, say, €100,000 in 2009 and paying premiums to a Retirement Annuity Contract or making contributions to a PRSA, may claim tax relief on the lower of:

- the actual premiums/contributions paid and
- 25% of €100,000.

So if he is paying premiums/contributions of €30,000, the amount on which tax relief could be claimed would be limited to €25,000. If the premiums/contributions paid were €25,000 or less, relief could be claimed on the full amount.

Contributions to more than one pension product

Where an individual has two sources of income (e.g. earnings from employment and profits from self-employment and is making pension contributions to an occupational pension scheme and to a personal pension plan (i.e. RAC and/or PRSA)) a single aggregate earnings limit of €150,000 applies in determining the amount of tax relievably contributions.

The following examples illustrate the operation of the earnings limit in such situations.

Example 1

Mary has earnings from employment of €100,000 in 2009. She also has self-employed income of €100,000. She is aged 28 and is required to make a contribution of 10% of salary (i.e. €10,000) to an occupational pension scheme established by her employer.

(Given Mary's age, the maximum allowable tax relievably contribution she can make in respect of her employment earnings is a contribution of 15% of her salary i.e. €15,000).

What is Mary's scope for making further tax relievably pension contributions?

As Mary is already making pension contributions in respect of her employment earnings of €100,000, she has, in effect, "used up" €100,000 of the aggregate earnings limit of €150,000.

Clearly, she has not fully used her capacity to make tax relievably pension contributions in respect of her employment earnings and she could check with her scheme administrator/pension advisor to see if she has scope to secure extra benefits through Additional Voluntary Contributions (AVCs). If such scope exists, she could make tax relievably AVCs of up to an additional 5% of her employment earnings (i.e. up to €5,000).

In relation to her self-employed income, because Mary has "used up" €100,000 of the aggregate earnings limit of €150,000 in contributing to her occupational pension scheme, her capacity to make tax relievably contributions to a personal pension plan (e.g. RAC and/or PRSA) in respect of her self-employed earnings is restricted to a maximum of 15% of €50,000 (i.e. €7,500).

This is the position irrespective of whether Mary decides to make an AVC or not.

Example 2

Michael, aged 51, has earnings from an employment of €180,000 in 2009. He also has self-employed income of €100,000.

Michael makes pension contributions as follows:

- a contribution of 10% of salary (i.e. €18,000) which he is required to make to an occupational pension scheme established by his employer, and
- 15% of self-employed earnings (i.e. €15,000) to a PRSA.

Based on his age, the maximum amount of pension contributions which Michael is entitled to claim tax relief on in respect of the occupational pension scheme for 2009 is the lower of his actual contributions (i.e. €18,000) and 30% of the earnings limit of €150,000 (i.e. €45,000). As Michael's contributions are €18,000 he can claim relief on that amount.

However, no tax relief is due in 2009 for Michael's contributions to the PRSA as he has used up all of his aggregate earnings limit in contributing to his occupational pension scheme.

As in Example 1, Michael may have scope to make AVCs and, if so, could increase the amount of tax relivable contributions in respect of his earnings from employment by up to €27,000 (i.e. maximum tax relivable contribution permissible is €45,000 (€150,000 x 30%) less €18,000 contribution made to occupational pension scheme).

1. Occupational & Statutory Pension Schemes, Retirement Annuity Contracts, PRSAs and Qualifying Overseas Pension Plans

2.

Age	Limits
Up to 30 years	15% of remuneration/net relevant earnings
30 – 39	20%
40 – 49	25%
50 – 54	30%
55 – 59	35%
60 and over	40%

3. "Earnings limit" was €254,000 in 2006, €262,382 in 2007 and €275,239 in 2008.