

# Pension Post



## Gross v net income replacement in retirement

**Tony Gilhawley of Technical Guidance Ltd looks at gross and net income replacement in retirement.**

### Tax benefits for the over 65s

When a client hits age 65, and later when they pick up the State Pension, a number of tax reliefs and benefits kick in

- ▶ An additional age tax credit of €245 per person - for a married couple, this is an additional €490 tax credit
- ▶ Income tax exemption if total income (including the State Pension) is less than €18,000 pa for a single person or €36,000 pa for a married couple. Even if the client's income goes over this figure, there is marginal relief on income up to double the limit, which can reduce the client's income tax bill
- ▶ No USC on the State Pension
- ▶ A reduced rate of USC of 2% for the over 70s whose income (other than the State Pension) is less than €60,000 pa
- ▶ No PRSI on the State Pension, private pensions and annuities. PRSI applies to ARF and AMRF withdrawals, but only up to age 66 currently

## Net income replaced

The resulting tax savings for the over 65s can be significant.

Take an example of a married couple, one income. Let's take a 50% target gross income replacement in retirement, inclusive of the State Pension (Contributory) at the assumed maximum rate of €461.30 per week, so that the balance of retirement income will come from private pensions, annuities and/or ARF/AMRF withdrawals<sup>1</sup>.

### Married couple, one income

Under 65								
Gross income	€50,000	€60,000	€70,000	€80,000	€90,000	€100,000	€110,000	€120,000
Income tax, USC and PRSI	€10,002	€14,877	€19,752	€24,951	€30,151	€35,351	€40,551	€45,751
Net income	€39,998	€45,123	€50,248	€55,049	€59,849	€64,649	€69,449	€74,249
Over 65								
Gross income (50%)	€25,000	€30,000	€35,000	€40,000	€45,000	€50,000	€55,000	€60,000
Income tax, USC and PRSI	€0	€0	€0	€1,740	€3,840	€5,940	€8,040	€10,140
Net income	€25,000	€30,000	€35,000	€38,260	€41,160	€44,060	46,960	€49,860
<b>Net income replacement</b>	<b>63%</b>	<b>66%</b>	<b>70%</b>	<b>70%</b>	<b>69%</b>	<b>68%</b>	<b>68%</b>	<b>67%</b>

A few surprising facts emerge

- ▶ A 50% gross income replacement in retirement is much more like 2/3rds net income replacement, when allowance is made for the various tax reliefs and benefits applying to retirees over age 65
- ▶ The retiree in this example only starts to pay taxes when their retirement income (inclusive of the State Pension) exceeds €36,000 pa. Up to that level of retirement income, they pay no taxes at all
- ▶ €60,000 income for a working couple under age 65 gives rise to a total tax liability of €14,877; however a retired couple over age 65 with €60,000 income, pays taxes of €10,140 pa (€4,700 pa less than the under 65 couple with the same income)

<sup>1</sup> No PRSI is assumed and the lower 2% USC rate is assumed to apply throughout.

The figures for a single person are broadly similar

## Single person

Under 65								
Gross income	€50,000	€60,000	€70,000	€80,000	€90,000	€100,000	€110,000	€120,000
Income tax, USC and PRSI	€13,452	€18,327	€23,202	€28,401	€33,601	€38,801	€44,001	€49,201
Net income	€36,548	€41,673	€46,798	€51,599	€56,399	€61,199	€65,999	€70,799
Over 65								
Gross income (50%)	€25,000	€30,000	€35,000	€40,000	€45,000	€50,000	€55,000	€60,000
Income tax, USC and PRSI	€1,455	€2,622	€3,812	€5,912	€8,012	€10,112	€12,212	€14,312
Net income	€23,545	€27,378	€31,188	€34,088	€36,988	€39,888	€42,788	€45,688
<b>Net income replacement</b>	<b>64%</b>	<b>66%</b>	<b>67%</b>	<b>66%</b>	<b>66%</b>	<b>65%</b>	<b>65%</b>	<b>65%</b>

## Conclusion

Assuming the current taxation system remains the same, retirees over 65 will benefit from a significant reduction in tax on their income. This means that a 50% target gross income replacement in retirement will replace about 2/3rd of their net income, the difference being the tax 'bounce' which the over 65s get.