Moalem Weitemeyer Bendtsen
Advokatpartnerselskab

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Bill to amend the Pension Taxation Act

On 1 March 2009 the Government and Dansk Folkeparti (the Government's cooperative partner) (hereinafter referred to as the "Parties") entered into an agreement concerning the package of measures to be implemented in the spring, version 2.0.

Among other issues, the agreement contains a bill to amend the Pension Taxation Act. This draft bill contains two proposals regarding the taxation of pension plans. These proposals suggest imposing a cap on pension annuity payments, together with raising the age limit for the withdrawal of capital pensions.

Governing law on pension annuity payments

According to the governing rules in the Pension Taxation Act, pension plans with current payments must be entered into with a pension fund or a life insurance company.

Under governing law, the Pension Taxation Act contains fiscal benefits for contributions and premiums to instalment insurance, so long as a number of conditions have been met. These conditions are, that the insurance amount is paid out in equal instalments over a period of no less than 10 years; that the plan must be set up before the policy-holder reaches retirement age; that the policy-holder must be insured and own the insurance; that pension payments cannot occur prior to the policy-holder reaching retirement age and no earlier than five years after the policy has been drawn up; that the point of maturity for the final instalment cannot be agreed upon to be later than the first policy-day, 25 years after the policy-holder reaches retirement age.

The above also applies to pension savings, however with necessary modifications due to the fact that it is a savings plan.

Insofar as the above conditions have been met, the fiscal benefits consist of the full deduction of contributions and premiums to instalment insurance for pension purposes, at the time of the measurement of personal income. The same is applicable for payments to pension annuity for pension purposes. Under circumstances such as when contributions and the like are made by the employer of the tax payer, there is no right of deduction.

In situations where the pension plan has been drawn up as part of an employment relationship, and where the employer pays contributions and premiums, the contributions are not to be included in the measurement of taxable income.

Under governing rules, there is no cap on the size of contributions and the like to instalment insurance and pension savings for pension purposes. The private plans are, however, subject to the rules regarding the distribution of the right of deduction, whereas these rules do not apply to pension annuities which are part of an employment agreement. The rules applicable to the distribution of the right of deduction mean that contributions and the like to privately entered schemes cannot be fully deducted in the relevant calendar year, but are to be distributed throughout a number of years.

Governing law on term annuities

An annuity is a pension which is paid out to the pension saver, for instance on a monthly basis. It is for the most part a lifelong policy, though it can also be a term policy. A term annuity is conditional on the life of the policy-holder, meaning that the policy-holder is guaranteed of a continuous income for a set amount of years conditional on the policy-holder being alive.

A term annuity can be with or without warranty coverage. If it is without warranty coverage and the policy-holder dies, the payments for the remainder of the agreed-upon period will not be made payable to the surviving relatives. The opposite is effective in the case of a term annuity with warranty coverage.

The contents of the bill

With this draft bill, the Parties have proposed the implementation of an annual cap concerning the amount to be used for insurance annuity and pension savings for pension purposes with the right of deduction or the right of exemption. The cap is proposed to be set at DKK 100,000, to be regulated annually according to the regulating price index in the Personal Taxation Act Section 20.

Furthermore, it has been proposed that payments to term annuities shall be included under the cap of DKK 100,000. According to the Parties, this is because these pension plans contain similarities with instalment insurance plans. Provided that the annuity has the nature of a life long retirement pension, the payments shall not be included.

The bill proposes that lifelong annuities are not included. According to the bill, the reason is that it contains a considerable insurance element.

The right of deduction for payments to pension plans with current payments, including certain annuities of a lifelong nature, are not affected by the bill, with the exception of term annuities, see above.

The cap of DKK 100,000 also applies to self-employed businesses, though the bill will not apply in this connection until 2015. This means that until 2015, self-employed businesses can pay up to 30% of their profits to a term or pension annuity. Thus, wage earners and self-employed businesses will have equal rights as from 2015, except that the favourable rules on early retirement pension are maintained, cf. the Pension taxation Act Section 15 A. According to these rules, a self-employed business can place DKK 2.5 million on a term, insurance or pension annuity for pension purposes if the business is closing down.

As a consequence of the cap of DKK 100,000 on deductable payments to pension annuity plans, it is proposed that the deduction allocation rules are repealed, insofar as the term, insurance and pension annuities are concerned in connection with payments above DKK 100,000.

If you have any questions or require any further information on the package of measures to be implemented in the spring, version 2.0, please contact attorney Dan Moalem (dmo@mwblaw.dk), attorney Lasse Dehn-Baltzer (ldb@mwblaw.dk) or attorney Henning Hedegaard Thomsen (hht@mwblaw.dk).