

Key results

The personal tax system plays an important role in old-age support. Pensioners often do not pay social security contributions. Personal income taxes are progressive and pension entitlements are usually lower than earnings before retirement, so the average tax rate on pension income is typically less than the tax rate on earned income. In addition, most income tax systems give preferential treatment either to pension incomes or to pensioners, by giving additional allowances or credits to older people.

Slightly more than half (18 out of 34) OECD countries provide older people with additional basic relief under the personal income tax. Generally, this takes the form of an extra tax allowance or tax credit. In many cases – Canada and the United Kingdom, for example – this additional relief is phased out for older people with higher incomes.

A significant number of countries offer tax relief for particular source of retirement income. Relief from income tax for public pensions, either full or partial, is available in 11 OECD countries. For example, between 15% and 50% of income from public pensions (social security) in the United States is not taxed, depending on the total income of the pensioner. Another four countries offer reliefs for private-pension income. In Australia, for example, benefits derived from pension contributions and investment returns that have been taxed are not taxable in payment for over 60s. (This therefore applies to the mandatory defined-contribution scheme and voluntary contributions to such plans.)

In contrast Sweden taxes earned income from work less than pensions. The Earned Income Tax Credit is targeted to low and mid-income earners and work as a tax deduction on work income. The tax deduction is larger for the over 65s in order to strengthen incentives work and to prolong working lives.

Overall, 23 OECD countries have some concession for older people or pension income under their personal income taxes. In only eleven is the tax treatment of pensions and pensioners the same as it is for people of working age.

Virtually all OECD countries levy employee social security contributions on workers: Australia and New Zealand are the only exceptions. In addition to these two countries, a further 17 do not levy social security contributions on pensioners. The rate of contributions in the 15 countries that do levy social security contributions on retirees is always lower than the rate charged on workers. Typically, older people do not pay contributions for pensions or unemployment (for obvious reasons). However, pensioners can be subject to levies to pay for health or long-term care and, in some cases, are liable for “solidarity” contributions to finance a broad range of benefits.

Empirical results

The figures show the percentage of income paid in taxes and contribution by workers and pensioners.

Starting with workers, countries have been ranked by the proportion of income paid in tax at an average earner level. This is then compared to the replacement rate that an average earner would see in retirement (as set out in the indicator of “Gross pension replacement rates” above). In eight OECD countries and all the other major economies, such a pensioner would not pay an income tax in retirement. In others, such as the Slovak Republic and Turkey, this is because pensions are not taxable. In Ireland it is because the pension income would be less than the basic income-tax reliefs offered to older people. Pensioners with the gross replacement rate for an average earner would pay 10.9% of their income in taxes and contributions.

The figure aims to show directly the impact of different tax and contribution treatment of earnings and pensions. The amount of taxes and contributions paid by a worker with average earnings averages 26.7% in OECD countries and 10.2% in other major economies.

The last comparison shows how much a pensioner would pay with the same income: that is, a pension worth the same as average earnings. This averages 16.9% in OECD countries, some 10 percentage points less than workers pay with the same level of income.

The difference between this 17% rate for pensioners with an income equal to average earnings and the 11% paid in taxes and contributions paid on incomes equal to the gross replacement rate for an average earner illustrates the impact of progressivity in income-tax systems.


Further reading

Keenay, G. and E.R. Whitehouse (2003), “The Role of the Personal Tax System in Old-age Support: A Survey of 15 Countries”, *Fiscal Studies*, Vol. 24, No. 1, pp. 1-21.

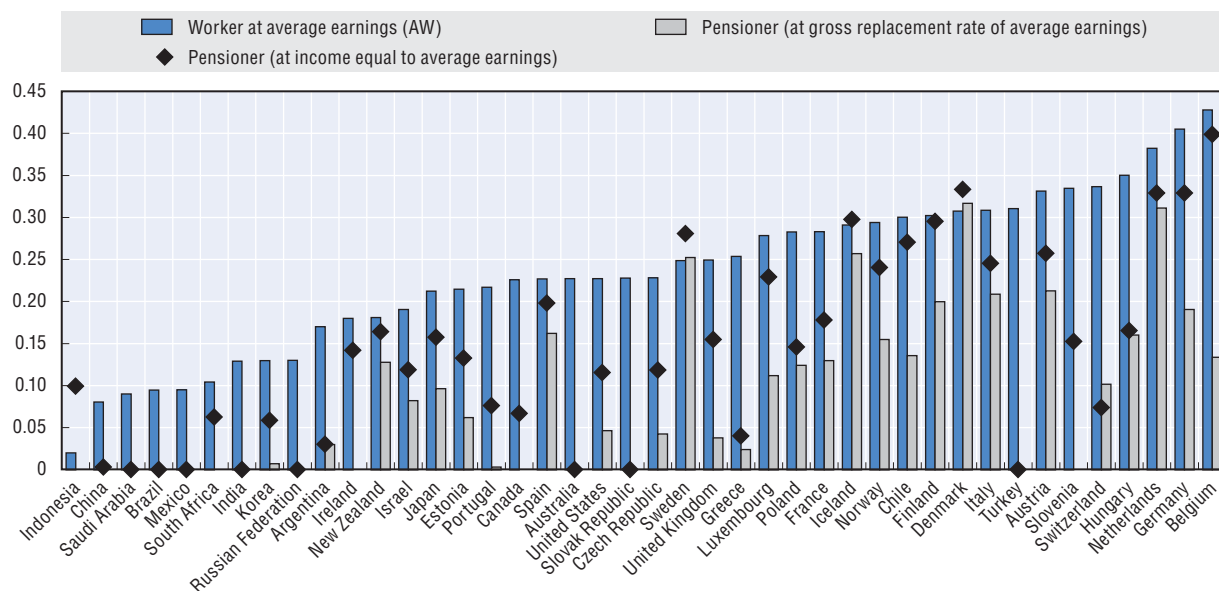
4.5. Treatment of pensions and pensioners under personal income tax and social security contributions

	Extra tax		Full or partial relief for pension income		Social security contributions		Extra tax		Full or partial relief for pension income		Social security contributions
	Allowance/credit	Public scheme	Private scheme	Pensions	Allowance/credit		Public scheme	Private scheme	Pensions		
OECD members						OECD members (cont.)					
Australia	✓	✓	✓	None		New Zealand					None
Austria				Low		Norway	✓	✓			Low
Belgium		✓		Low		Poland					Low
Canada	✓	✓	✓	None		Portugal					None
Chile	✓			None		Slovak Republic		✓			None
Czech Republic	✓	✓		None		Slovenia	✓				Low
Denmark				None		Spain					None
Estonia	✓			None		Sweden	✓				None
Finland		✓		Low		Switzerland					Low
France				Low		Turkey		✓			None
Germany		✓	✓	Low		United Kingdom	✓				None
Greece				Low		United States	✓	✓			None
Hungary				None							
Iceland				None		Other major economies					
Ireland	✓			Low		Argentina		✓			None
Israel	✓			Low		Brazil		✓			None
Italy	✓		✓	None		China					
Japan	✓			Low		India	✓				None
Korea	✓	✓		None		Indonesia					None
Luxembourg	✓			Low		Russian Federation					Low
Mexico	✓			None		Saudi Arabia					Low
Netherlands	✓			Low		South Africa	✓				None


Source: On-line country profiles available at www.oecd.org/pensions/pensionsataglance.htm.

StatLink  <http://dx.doi.org/10.1787/888932907300>

4.6. Personal income taxes and social security contributions paid by pensioners and workers



Source: OECD pension models; OECD tax and benefit models.

StatLink  <http://dx.doi.org/10.1787/888932907310>



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