

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.

Of the 26 LAC countries five of them provide additional basic relief under the personal income tax. Generally, this takes the form of an extra tax allowance or tax credit.

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 13 LAC countries. Overall, 17 LAC countries have some concession for older people or pension income under their personal income taxes. In only nine is the tax treatment of pensions and pensioners the same as it is for people of working age.

Virtually all LAC countries levy employee social security contributions on workers. However 16 of these countries do not levy social security contributions on pensioners. The rate of contributions in the ten 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 charts show the percentage of income paid in taxes and contribution by workers and pensioners.

Starting with pensioners, countries have been ranked by the proportion of income paid in tax at the replacement rate that an average earner would see in retirement (as set out in the indicator of “Gross pension

replacement rates” above). In 16 of the LAC countries, such a pensioner would not pay any income tax in retirement. This is either because pensions are not taxable or the basic income-tax reliefs offered to older people are above the pension level. Pensioners with the gross replacement rate for an average earner would pay 3.8% of their income in taxes and contributions.

The other two bars in the charts aim to show directly the impact of different tax and contribution treatment of earnings and pensions. The longer bar shows the amount of taxes and contributions paid by a worker with average earnings. This averages 9.7% in LAC countries and 26.2% in the OECD countries listed.

The middle bar shows how much a pensioner would pay with the same income: that is, a pension worth the same as average earnings. This averages 4.1% in LAC countries, some 5.6 percentage points less than what a worker pays with the same level of income.

The difference between this 4.1% rate for pensioners with an income equal to average earnings and the 3.5% 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.

References

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.

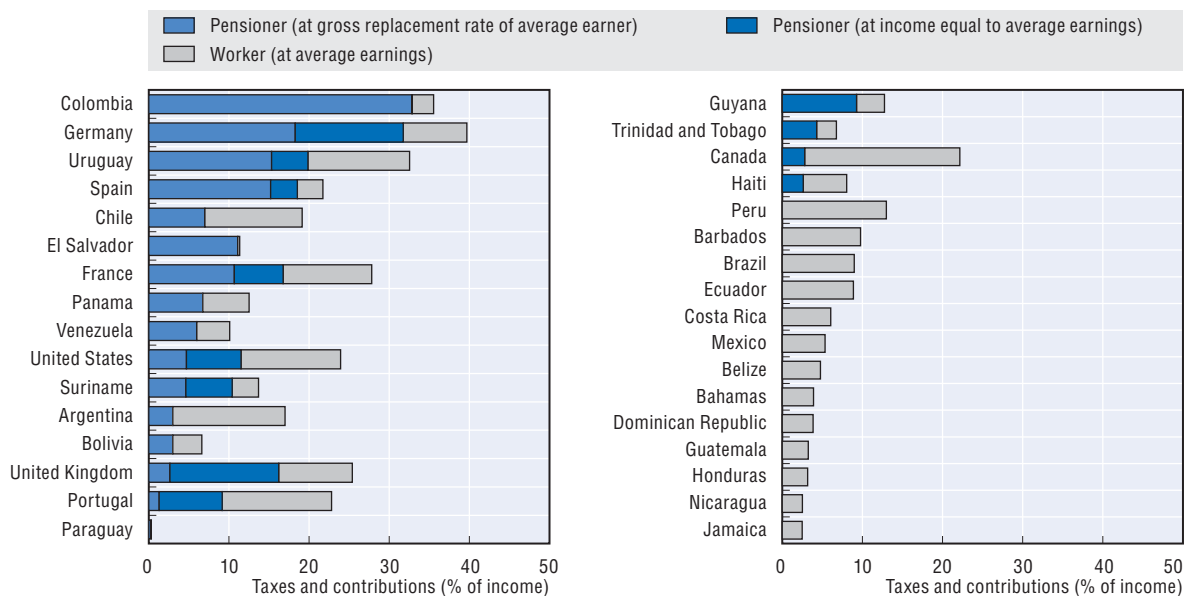
3.6. Treatment of pensions and pensioners under personal income tax and social security contributions

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	Allowance/credit	Public scheme	Private scheme	Pensions
	✓		Low	Mexico	✓		None				None
			None	Nicaragua		✓	None		✓		None
✓			None	Panama		✓	None		✓		Low
			None	Paraguay		✓	None		✓		Low
	✓		Low	Peru		✓	None		✓		None
	✓		None	Suriname		✓	None		✓		Low
✓			Low	Trinidad and Tobago			None				None
			Low	Uruguay	✓		None				Low
			None	Venezuela		✓	None		✓		Low
	✓		None	Canada	✓	✓	✓		✓	✓	None
	✓		None	France			Low				Low
			Low	Germany		✓	✓		✓	✓	Low
	✓		None	Portugal	✓		None				None
			None	Spain		✓	None		✓		None
			None	United Kingdom	✓		None				None
✓	✓		None	United States	✓	✓	None		✓		None

Source: On-line country profiles available at www.oecd.org/els/social/pensions/PAG.

StatLink <http://dx.doi.org/10.1787/888933161919>

3.7. 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/10.1787/888933161483>



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