Chapter 7

Retirement savings taxation

Contents

7. RETIREMENT SAVINGS TAXATION

SUMMARY

It is not possible to draw an overall conclusion about the relative ranking of the concessionality of the Australian retirement income taxation system owing to the lack of data and to methodological issues with the various studies on this subject.

There is no report by the OECD or other international organisations identified by this study that provides an overall comparison of the concessionality of taxation of retirement savings regimes. This is due, in part, to the lack of relevant revenue statistics data as well as the interaction of taxation and expenditure systems. This chapter therefore focuses on the taxation of private retirement savings.

The examination of the relative concessionality of countries' taxation arrangements for private retirement savings relies on two studies by Whitehouse (1999) and Yoo and de Serres (2004).

Both papers indicate that the Australian retirement savings taxation regime, like those of other countries, is concessional compared to the taxation treatment of other savings (for example, a bank account).

The Yoo and de Serres paper also highlights the extent to which revenue is forgone in delivering these tax concessions. Australia has the fourth largest amount of revenue forgone per unit of contribution in the OECD-10.

The two papers have contradictory results about the effective tax rates facing private pension savings. Whitehouse (1999) indicates that the concession offered by Australia's taxation of retirement savings is the third highest in the OECD-10. In contrast, Yoo and de Serres (2004) indicate that Australia has the second highest effective tax rate applying to private pension savings out of the OECD-10. This contradiction cannot be reconciled because of methodological issues with both papers.

These methodological issues reduce the reliability of their results on the effective tax rates and their usefulness for international comparisons. In particular, Yoo and de Serres (2004) use different bases for determining the tax rate, depending on the taxation regime applied, and Whitehouse (1999) measures concessionality against a benchmark derived from a country's own marginal tax rates.

Whilst there is no standard 'international model' of retirement savings taxation, eight countries out of the OECD-10 use an EET tax model. This group of eight can be further broken down into those who impose tax at normal marginal tax rates and those who offer a more concessional taxation treatment of benefits. The two exceptions to the EET approach are Australia and New Zealand. However a key finding is that the most important point about the overall concessionality of the taxation arrangements is the rate(s) of tax imposed.

When compared with the OECD-10, Australia is broadly mid-range for the generosity of its contribution limitations and provides above average concessions in terms of the availability and taxation treatment of lump sum payments.

7.1 INTRODUCTION

This chapter differs significantly from most of the other chapters in this review because there is no authoritative primary data source upon which to rely. OECD revenue statistics do not capture taxes on retirement savings in a consistent or transparent manner across countries. Rather, depending on the retirement income system used, the tax burden will be spread (at varying rates) across various parts of the direct income tax base. Without separate data it is not possible to examine the ratio of taxes to GDP, the tax mix or any of the other indicators used in other chapters. In any case, an international comparison of the taxation of retirement savings arrangements is problematic as both the structure of retirement income arrangements and the taxation regimes which countries apply to them vary widely.

Box 7.1: The structure of retirement income arrangements

Retirement income arrangements can be defined in different ways. Perhaps the most commonly used typology is the so-called 'three pillar' approach set down by the World Bank. These pillars are described as:

> a publicly managed system with mandatory participation and the limited goal of reducing poverty among the old [the 'first pillar']; a privately managed mandatory savings system [the 'second pillar']; and voluntary savings [the 'third pillar'].

In practice, arrangements can be much more varied than might be implied by describing them as falling within a particular pillar. Arrangements within a pillar can vary as easily as those between pillars. For instance, the OECD notes that safety-net arrangements (which would be a 'first pillar' arrangement) can broadly be of four different types.

Retirement income systems are also generally composed of a mix of various forms of income secured from various pillars. The pillar which is the chief focus of retirement arrangements can vary significantly from country to country. This focus will often impact upon a country's policy in relation to the taxation of private retirement savings.

This chapter does not compare these disparate systems, but focuses on the taxation regimes imposed on private retirement savings vehicles (that is, second and third pillar arrangements which are not government-controlled or managed) through an examination of the concessionality of regimes (this requires consideration of all elements of the taxation regimes, not only a comparison of tax rates applying at particular points). This partial analysis limits the drawing of robust comparisons or conclusions about the taxation of overall retirement savings.

As is the case in relation to other taxes, there are limitations to such comparisons that do not take into account the different contexts in which the taxes are imposed. For example, the different extent to which countries rely on private retirement savings vehicles can reduce the value in making international comparisons. That is, a country that has little reliance on the use of private retirement savings vehicles as the primary retirement income vehicle (perhaps due to a universal public pension regime paying large benefits) may be able to afford to offer highly concessional tax treatment to them.

Further, any study which focuses purely on the taxation arrangements (that is, the rates and incidences of taxation) ignores the costs incurred in providing concessions to such savings. Retirement income arrangements are also strongly affected by variable factors such as retirement age and life expectancies (which affect the period of time spent in retirement) and indeed broader social constructs including the level of expected individual responsibility for retirement income provision and social or family support structures. This will impact on policy decisions about the appropriate level of taxation of retirement savings (including decisions about tax concessions).

Discussion of the taxation treatment of retirement savings tends to focus on the taxable or tax exempt status (and tax rates) which applies to contributions, earnings and the payment of benefits. However, limiting the discussion to these elements has the potential to be misleading. Keenay and Whitehouse (2003) have noted the importance of avoiding 'comparing the rates and structures of retirement benefits across countries without also considering the effect on older people of systems of personal income tax and social security contributions'. Many countries, including Australia, offer significant personal income tax concessions to retirees (under various qualifying conditions) such that the overall tax burden is significantly less than if the same level of income was derived by a non-retiree. In general, such concessions are not captured in international comparisons of taxation treatment of retirement savings.

Lastly, even where comprehensive studies of international tax treatment are undertaken they generally have to homogenise the regimes they are looking at (for instance, by ignoring particular concessions or the impacts of other sources of income) to allow the drawing of comparisons.

After examining the concessionality of the taxation of private retirement savings, some descriptive comparisons of particular aspects of retirement savings regimes are considered. The limitations which governments apply to the level of contributions to, and benefits flowing from, the retirement savings system are examined, along with the availability and taxation treatment of lump sums.

7.2 APPROACHES TO TAXING RETIREMENT SAVINGS

There are three points at which retirement savings vehicles (much like any other savings vehicle) can be subject to taxation. Taxation can be imposed on:

- contributions (before or after income tax and social security contributions);
- investment income and capital gains derived from contributions; and
- payment of benefits.

Taxation can be imposed (or not) at each of these three points, giving rise to eight theoretical taxation models. Even regimes which impose taxation at the same points can produce different outcomes as a result of different tax rates, exemptions, credits, other offsets or even government subsidies which may apply.

Box 7.2: Defining different taxation regimes

In academic literature retirement savings taxation regimes are generally described by a three letter name indicating at what point (or points) taxation is imposed. The presence of a 'T' reflects the imposition of taxation. It does not reflect the overall burden of the tax imposed (that is, a system that imposes 1 per cent, 1 per cent and 1 per cent, would be described as TTT, as would a system that imposed 30 per cent, 30 per cent and 30 per cent).

A model that exempts contributions and earnings but taxes benefit payments is referred to as an 'exempt-exempt-taxed' (EET) model or expenditure tax model. The comprehensive income tax model instead taxes contributions and earnings but not benefits. This model is described as a 'taxed-taxed-exempt' (TTE) model.

From a theoretical stand point, a TEE model produces an equivalent retirement income outcome to an EET model (for the same value of 'T'). Similarly, an ETT model produces an equivalent retirement income result to a TTE model. The table below highlights the retirement income equivalence of the TEE/EET and ETT/TTE regimes (as demonstrated by the value of the net pension). In practice, Whitehouse notes that the systems may not have the same effect because of the point at which the tax exemption occurs.

Table 7.1: Theoretical pension taxation regimes

	EET	TEE	TTE	ETT
Contribution	100.00	100.00	100.00	100.00
Tax	-	25.00	18.00	-
Fund	100.00	75.00	82.00	100.00
Net investment return	61.05	45.79	39.60	48.30
Fund at retirement	161.05	120.79	121.60	148.30
Tax on pension	40.26	-	-	26.69
Net pension	120.79	120.79	121.60	121.60
Net present value of tax	25.00	25.00	24.49	24.49

Source: Derived from Whitehouse (1999).
Note: Assumes 10 per cent annual return (nominal), five-year investment term, discount rate of 10 per cent, 25 per cent tax rate for EET/TEE scenarios and 18 per cent for TTE/ETT scenarios.

Table 7.2 outlines in detail the diverse approaches to the taxation of private retirement savings across the OECD.

Out of the OECD-10, eight countries use a form of expenditure tax treatment. This group of eight can be further broken down into those who impose tax at normal marginal tax rates (Canada, the Netherlands, Switzerland and the United States) and those who offer a more concessional taxation treatment of benefits (Ireland, Japan, Spain and the United Kingdom). The two exceptions to the expenditure tax approach are Australia and New Zealand. New Zealand utilises a comprehensive income tax model, whilst Australia imposes tax at each of the three stages (though at concessional rates).

Table 7.2 illustrates that there is no standard 'international model'. Around a quarter of the countries examined by Yoo and de Serres (2004) do not apply an EET model of taxation. Of those countries that do apply a form of expenditure tax model, more than half deviate from the 'pure' expenditure tax treatment by taxing pensions at a lesser rate than that applying to other income.

Table 7.2: Tax treatment of private pensions in 2003

	Contributions	Fund		Pension payments	
		Income	Value	Annuities	Lump sums
Australia					
individuals	M	7.1%	E	M/PC	PE/16.5%
employers	15%	7.1%	E	M/PC	PE/16.5%
Austria					
individuals	M/PE	E	E	M/PE	M/PE
employers	E	E	E	M	M
Belgium					
individuals	M/PC	E	0.17%	M/PC	10%
employers	E	E	0.17%	M/PC	16.5%
Canada	E	E	E	M	M
Czech Republic					
individuals	M/PE/S	E	E	15%/PE	15%/PE
employers	E/S	E	E	15%/PE	15%/PE
Denmark	E	15%	E	M	40%
Finland	E	E	E	M	M
France	E	E	E	M/PE	M/PE
Germany	E	E	E	M/PE	M
Greece	E	E	E	M	M
Hungary					
individuals	M	E	E	E	E
employers	E	E	E	E	E
Iceland	E	E	E	M	M
Ireland	E	E	E	M/PE	M/PE
Italy	E	12.5%	E	M/PE	M/PE
Japan	E	E	E	M/PE	M/PE
Korea	E	E	E	M/PE	M/PE
Luxembourg					
individuals	E	E	E	M	M/PE
employers	20%	E	E	E	E
Mexico	E/S	E	E	M/PE	M/PE
Netherlands	E	E	E	M	M
New Zealand					
individuals	M	33%	E	E	E
employers	21%	33%	E	E	E
Norway	E	E	E	M	Not allowed
Poland	E	E	E	M	M
Portugal					
individuals	M/PC	E	E	20%/PE	M/PE
employers	E	E	E	20%/PE	M/PE
Slovak Republic	E	E	E	15%	15%
Spain	E	E	E	M	M/PE
Sweden	E	15%	E	M	M
Switzerland	E	E	E	M	M
Turkey	E	E	E	E	5%/PE
United Kingdom	E	E	E	M	M/PE
United States	E	E	E	M	M

Source: Derived from Yoo and de Serres, OECD *Economic Studies*, No. 39, (2004).
Notes:
(1) 'Private pensions' refers to mandatory or voluntarily funded, privately managed, pension schemes.
(2) Tax deductible contributions are subject to a certain limit in most countries.
(3) The effective tax rate on earnings shown for Australia assumes a portfolio of 60 per cent interest-bearing assets and 40 per cent equities.
(4) Where a country's tax regime differentiates between the tax treatment of employer and employee contributions, each has been shown.
(5) E = exempt.
(6) M = taxed at marginal income tax rates.
(7) PC = partial credit.
(8) PE = partial exemption or deduction from taxation.
(9) S = subsidy.

7.3 MEASURING THE CONCESSIONALITY OF THE TAXATION SYSTEM

Retirement savings attract taxation concessions in many countries. There are a number of arguments used to justify the more generous taxation treatment of retirement savings (when compared with other savings vehicles):

- the state should ensure that people maintain a 'reasonable' standard of living in retirement (and the provision of taxation concessions overcomes any short-sightedness on the part of the individual who may otherwise choose to consume immediately rather than save for future consumption);
- the cost of social security benefits is reduced by encouraging individual provision for retirement, particularly where means-tested social security benefits are an important source of retirement income, as in Australia; and
- the favourable taxation treatment increases long-term savings, which has beneficial impacts on the level/stability of capital available for investment (Whitehouse 1999).

Box 7.3: Benchmarking concessionality

There is no consensus on the benchmark to be used to determine whether a particular retirement savings taxation regime is concessional. The methods of calculating tax expenditures vary from country to country.

According to Yoo and de Serres (2004), a savings taxation regime is generally considered concessional if it deviates (favourably) from the 'comprehensive income tax' model. A pure comprehensive income tax regime will see savings made from after-tax money, any earnings subject to income tax, and a tax free withdrawal of assets. A real-world example of the application of a comprehensive income tax model would be the taxation treatment of a bank deposit in Australia: the deposit is made from after-tax money, any earnings (interest) are subject to taxation, and savings are withdrawn tax free.

Whitehouse (1999) argues that the (more generous) expenditure tax model is a more appropriate benchmark than the comprehensive income tax model as it is neutral between immediate consumption and consumption in retirement.

Whitehouse's research indicates that Australia is considered to be concessional against the more generous expenditure tax benchmark (Chart 7.1 illustrates).

There are very few studies comparing the taxation of private retirement savings. The two papers already mentioned are the most recent and often cited papers on this matter. However, there are significant limitations in their approach to determining the concessionality with which countries tax private retirement savings.

Whitehouse has ranked the relative generosity of OECD countries' taxation of pensions (using the effective generosity of expenditure tax treatment and comprehensive income tax treatment as benchmarks). The Whitehouse paper was published in 1999 and there may have been subsequent changes to taxation regimes since then (for instance Whitehouse indicates that Japan was a TET system at the time he was writing; Yoo and de Serres indicate that in 2004 Japan was applying an EET system).

Table 7.3 shows the relative concessionality of the taxation treatment applied by countries compared to the tax regimes that would apply if the country imposed an expenditure tax regime or a comprehensive income tax regime to retirement savings.

Table 7.3: Pensions taxation in practice

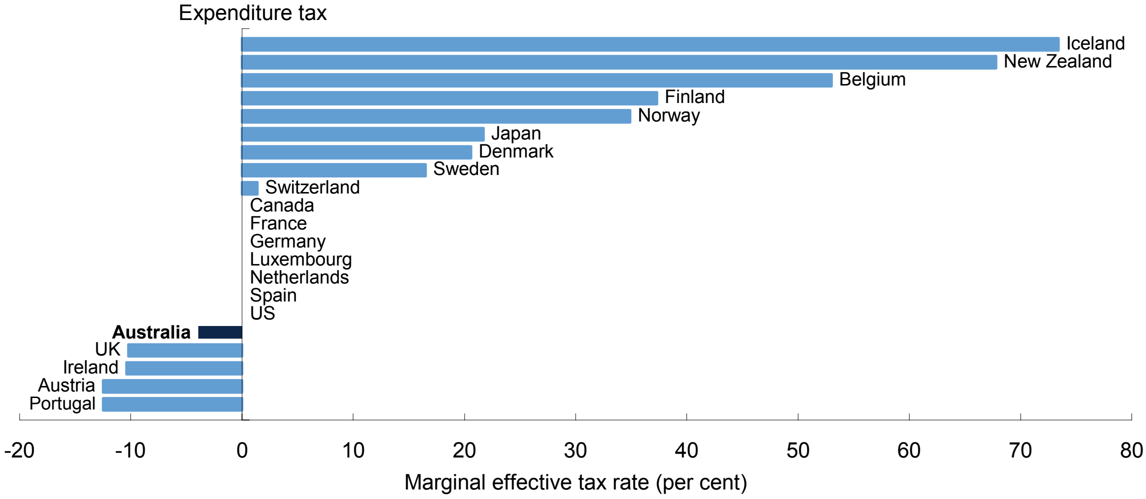
More concessional than expenditure tax	Expenditure tax	Between expenditure and comprehensive income tax	Less concessional than comprehensive income tax
Australia	Argentina	Denmark	Belgium
Austria	Canada	Finland	Iceland
Czech Republic	Chile	France	Japan
Hungary	Columbia	Norway	New Zealand
Ireland	Costa Rica	Sweden	
Korea	Germany		
Portugal	Luxenbourg		
United Kingdom	Netherlands		
	Poland		
	Spain		
	Switzerland		
	United States		
	Uruguay		

Source: Derived from Whitehouse (1999).
Note: Table shows, from left to right, the most concessional regimes through to the least concessional.

Whitehouse's findings suggest that the points at which taxation is imposed by a country do not necessarily provide an insight into the overall comparative generosity of its taxation treatment of retirement incomes. This is particularly relevant for Australia, given our unique approach to the taxation of superannuation.

Chart 7.1 refines the information presented in Table 7.3 by comparing all countries against an expenditure tax model. The chart indicates the effective marginal tax rate for an average worker's wage (as measured by the OECD), on pension savings (to be read as 'private retirement savings') for 21 OECD countries. Those countries to the left of the 'expenditure tax' axis have a concessional taxation regime compared to an expenditure tax benchmark. In contrast, those to the right tax more heavily than a pure expenditure tax regime. Australia is one of five countries (out of 21) ranked as providing a more generous taxation treatment.

Chart 7.1: Marginal effective tax rates on pension savings
Selected OECD countries, tax rate at average production worker earnings level



Source: Derived from Whitehouse (1999).

In the Whitehouse findings Australia is fifth out of 21 OECD countries in terms of the relative concessionality of the retirement savings taxation regime and third out of the OECD-10. The caveat to these results is that each country is compared against an EET case calculated against its own taxation regime. The figures reflect the difference between a country's retirement savings taxation arrangements and its own marginal tax rates.

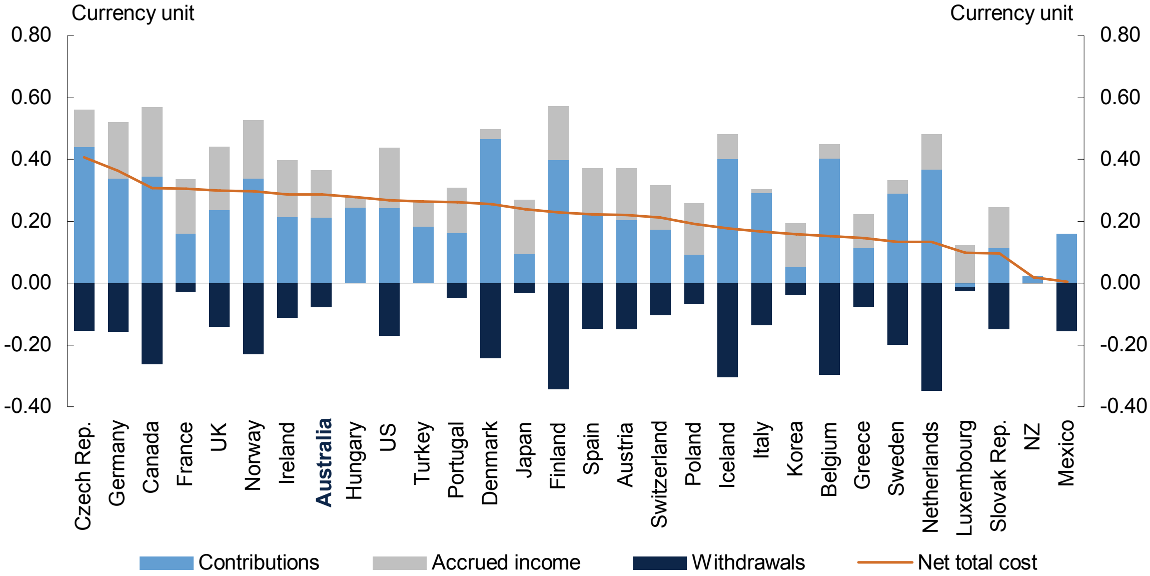
Chart 7.2 illustrates the total revenue cost to countries incurred per unit of contributions (for example, per dollar). According to Yoo and de Serres, Australia is eighth in terms of the revenue forgone per dollar of contributions across the OECD countries and fourth (behind Canada, Ireland and the United Kingdom) when compared against the other OECD-10 countries.

Yoo and de Serres also rank countries on the basis of the effective tax rates on private pensions (and compare this against the effective tax rate on a benchmark savings product). Their results are set out in Chart 7.3. Compared to the OECD-10 comparators, Australia (it is argued) has the second highest effective tax rate on private pension savings.

A further conclusion which might be drawn from Chart 7.3 is the extent of the concession which countries provide to retirement savings in contrast to the taxation treatment of benchmark savings (as measured by the gap between the two bars for each country). On such a measure Australia would be first amongst the OECD-10 and second across the entire OECD.

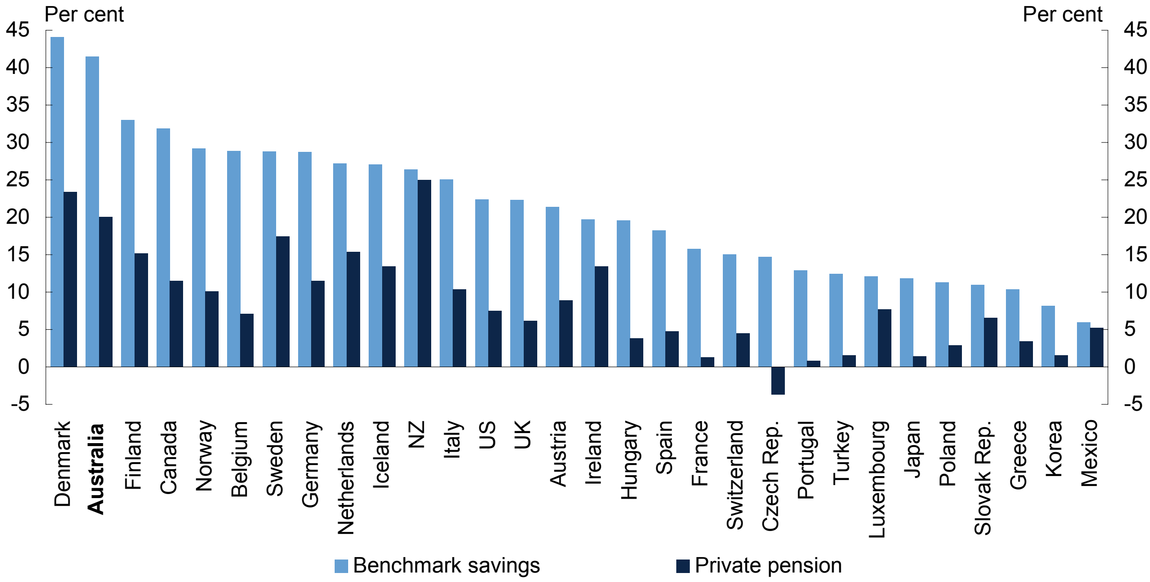
It is important to note that the relative rankings of countries in the Yoo and de Serres study are very sensitive to a number of the assumptions and methodological choices made, as discussed in Box 7.4.

Chart 7.2: Net tax cost per unit of contribution, age group average



Source: Yoo and de Serres (2004).

Chart 7.3: Effective tax rates on private pension and benchmark saving, age-group average



Source: Yoo and de Serres (2004).

Note: Based on the employer-sponsored schemes (except Italy and Korea) and lump sum payments. However, for countries in which tax treatment between the employer's and the employee's contribution is the same, the distinction between employer-sponsored and individual pension schemes is meaningless.

The effective tax rate is measured as the difference between the net present value of the pre-tax and post-tax assets in proportion to the net present value of the pre-tax assets, for 6.5 per cent of return (and discount rate).

Box 7.4: Issues of methodology

Many studies are sensitive to the assumptions underlying their methodology.

In comparing the marginal effective tax rates on pension savings against an expenditure tax (EET) benchmark, Whitehouse relies on the value of 'T' in his benchmark being the same as that faced in working life. However pensioners are unlikely to face the same marginal tax rate in retirement as they did in their working life (particularly given the tax concessions many countries offer to their pensioners and their generally lower income levels).

Yoo and de Serres use different tax bases for different regimes (for example, the tax base for an EET regime is different to that for a TEE regime). These differences in the tax base prevent comparison between different regimes (that is, a TTT regime cannot be effectively compared to an EET regime) though the relativities within regimes are valid.

The Yoo and de Serres paper is also very sensitive to the way in which the present-day value of benefits is determined. The assumption in the paper is that, in today's terms, if a person contributes a dollar, they will withdraw only a dollar at the benefits stage. Changing the way this is calculated does not affect the relativities between EET systems, but has a significant impact on the comparative results for TTE and TTT countries compared against the EET regimes. That is, if the outcome of the contribution is improved (by assuming that a dollar contribution delivers more than a dollar of benefits) the relative standing of the TTE and TTT countries is improved.

Both the Yoo and de Serres methodology and the Whitehouse methodology are also sensitive to assumptions about the tax rate faced in retirement. Both use a simplified treatment (though different between the papers) to deal with the complex arrangements that apply in retirement. As noted previously, this tendency to homogenise taxation regimes is a common feature of international work on retirement savings.

While Australia provides taxation concessions to retirement savings (compared both to a benchmark savings product and to an expenditure tax regime), the data are not available to enable robust cross-country comparisons.

7.4 COMPARATOR TABLES

The treatment of particular aspects of retirement savings arrangements can also inform consideration of the various taxation regimes. Following are comparative tables outlining the limitations which apply to contributions to and benefits from retirement savings vehicles and the availability and tax treatment of lump sum payments.

The information in the tables suggests that Australia's limitations on contributions are broadly in the middle of the OECD-10 and that our taxation treatment of lump sums provides above average concessions (although not much can be drawn from considering the treatment of one point in the contributions/earnings/benefits cycle).

7.4.1 Limits on concessionality

Countries frequently limit the amount of concessionally taxed retirement savings that can be accumulated by an individual. There are two key ways of imposing such limits: contribution limits (a flow limitation) and benefit limits (a stock limitation). The imposition of contribution and benefit limits provides governments with a level of comfort about the level and distribution of the costs associated with providing tax incentives to encourage retirement savings. Contribution and benefit limitations can either be used individually or in combination, dependent in part on how they are applied.

Table 7.4 sets out some high-level international comparisons of the mechanisms used to limit concessionality.

The data in the table might seem to indicate that Australia imposes significant limitations on the amount of concessional benefits which can be received compared to the rest of the OECD-10. However, of the five comparator countries that impose no benefits limits, New Zealand imposes a comprehensive income tax arrangement and the remaining four impose marginal tax rates on end benefits (though in two cases with possible credits or exemptions), thus imposing effective benefits caps if high marginal tax rates in retirement are to be avoided. In addition, the United States and Switzerland also impose strict contribution limits (rather than merely limiting tax deductibility for contributions). This range of treatments provides an example of how different forms of contributions and benefit limitations can be used either individually or in unison to achieve similar outcomes, namely the effective limitation of the level of tax concessions provided.

Table 7.4: International limitations on private pension contributions and benefits

Country	Contribution limits	Benefit limits
Australia	Age-based contribution limits (ABLs) impose a cap on tax deductibility for employers (and eligible self-employed). In 2005-06, the ABL is A$14,603 for those under 35, A$40,560 between 35 and 49 and A$100,587 for those aged 50 and over. Self-employed individuals do not receive the same dollar-for-dollar deduction available to employers. For the self-employed the first A$5,000 is deductible, as is 75 per cent of the remainder of their contributions up to the ABL. Excessive contributions receive no tax deduction and therefore face a higher effective tax rate.	Benefit limitations apply, called Reasonable Benefits Limits (RBLs). In 2005-06, these limits are set at A$1,297,886 for the pension RBL and A$648,946 for the lump sum RBL. The pension RBL is greater to encourage pension uptake and applies if at least 50 per cent of benefits are taken as an income stream (subject to it meeting certain requirements). Excessive benefits are subject to tax at the rate of 38 per cent (where they have already faced the 15 per cent 'contributions' tax).
Canada	Contributions to employer registered pension plans limited to C$19,000 in 2006 (applies to total employer/employee contributions). Contributions to registered retirement savings plans (RRSP) limited to the lesser of 18 per cent of prior year's earnings or C$18,000 (in 2006). Members of employer pension plans face a reduction based on prior year's contributions. Deductions capped at these absolute levels. Unused RRSP contribution limit can be carried forward indefinitely.	Limits apply to Defined Benefit (DB) plans. Pension cannot exceed 2 per cent per year of service multiplied by pensionable earnings (and capped at a maximum of C$2,111.11 per year of service).
Ireland	Age-based contribution limits cap tax deductibility for individuals (as a percentage of net relevant earnings). Salary limit of €254,000 applies.	From 7 December 2005, a benefits limit applies. Maximum allowable balance set at €5 million (transitional rules apply for balances which exceeded this limit as at 7 December). Excessive benefits are subject to tax at the rate of 42 per cent when drawn down.
Japan	Complex limitations apply depending upon whether a person has other corporate pensions and upon their employment status (that is, if self-employed). Monthly contribution limits range from ¥18,000 to ¥68,000.	None
Netherlands	None. Uncapped tax deductibility is available for contributions. Ability to make voluntary contributions may not exist (the company running an employment-based scheme may allow voluntary contributions, but this is not a requirement).	None for accumulation funds, but DB funds limited to pension benefits of 100 per cent of salary.
New Zealand	None	None
Spain	Maximum deductible amount is €8,000 per year for employee and same amount for employer. Taxpayers over 52 get an additional allowance of €1,250 with a maximum limit of €24,250 for members aged 65 and over. Some capacity to carry forward deductibility (for up to five years).	None
Switzerland	All contributions deductible except for certain third-pillar contributions which receive only a minimal deduction.	None
United Kingdom	Tax deduction contribution cap applies. From 6 April 2006, deduction limited to greater of 100 per cent of person's United Kingdom earnings or £3,600. If an employer contributes more than £215,000 for a person in a year, then the excess is taxed at 40 per cent.	From 6 April 2006 lifetime allowance (LTA) limits concessional benefits to £1.5 million (for the 2006-07 United Kingdom financial year). Any excessive benefits taxed at a rate of 55 per cent if taken as a lump sum or at 25 per cent if taken as an income stream.

Table 7.4: International limitations on private pension contributions and benefits (continued)

Country	Contribution limits	Benefit limits
United States	Strict contribution limits apply to contributions to individual retirement accounts (IRAs). In 2005 contributions were capped at US$4,000 (US$4,500 for those aged 50 and above). Whilst there is some ability to offset excess contributions against unused limits in future years, penalties and additional tax can apply. Strict contribution limits also apply to 401(k) plans. In 2005 contributions were capped at US$14,000 worth of deferred income. People aged 50 and above can make additional contributions of US$4,000.	None

Source: Various, see Chapter 1 (1.4.1).

7.4.2 Availability and tax treatment of lump sums

Table 7.5 provides a summary of international arrangements concerning access to lump sums from private savings (a relatively common payment type in Australia). The table also notes any limitations which apply to lump sums and details of the relevant taxation treatment.

An examination of the treatment of lump sums is relevant given the tendency of Australian retirees to take their benefits in this way. Additionally, a comparison of pensions is less useful as it is not possible to review comprehensively the range of tax concessions that other countries offer to their retirees. In any event, pension income tends to be taxed at marginal rates.

Table 7.5: International practice — lump sums from private retirement savings vehicles

Country	Taxation arrangements
Australia	Tax rates on lump sums vary based on the constituent components. They may contain up to eight different components taxed in seven different ways. The first A$129,751 (2005-06 value) of the most common component (that is, post-June 1983 taxed element) faces a zero per cent tax rate.
Canada	Lump sum is taxed at marginal rates.
Ireland	Lump sum only available when assets in a personal retirement savings plan first become available to the contributor. Lump sum is limited to a maximum of 25 per cent of the value of the benefit. Lump sum is received tax free.
Japan	Lump sum is 50 per cent taxable at marginal rates.
Netherlands	Lump sum payments no longer available.
New Zealand	Lump sum generally received tax free, but certain employer contributions attract a five per cent fund withdrawal tax on distribution to fund member.
Spain	Lump sum is taxed as employment income. 40 per cent tax reduction available if at least two years elapsed since first contribution.
Switzerland	Lump sums only available for voluntary additional savings. Pensions payable in all other circumstances. Subject to preferential rate which varies but roughly amounts to one third of individual's rate.
United Kingdom	From 6 April 2006 lump sums are restricted to the lesser of 25 per cent of the value of the benefit and 25 per cent of unused lifetime allowance. Lump sum is received tax free.
United States	Taxed at marginal rates.

Source: Various, see Chapter 1 (1.4.1).
Note: Table assumes access at normal point of retirement/access. Different (less generous) tax regimes tend to apply to early access.

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