

The Pension Scheme
Practical Notebooks

English

Tax adjustment

Article 42

As a pensioner or future pensioner from one of the Co-coordinated Organisations, you receive or you will receive every month your pension pay slip. It indicates the amount of your pension together with an amount which represents the monthly “tax adjustment”, which may vary and even be negative.

This results from application of Article 42 of the Pension Scheme Rules. Pensioners (and future pensioners) wish to be better informed on the way this amount is determined.

This booklet aims to answer the questions related to the conditions of granting, to the formula of calculation and to the payment of tax adjustment. It has no legal value by itself, only the Pension Scheme Rules themselves are legally binding.

1. What is meant by “tax adjustment”?

It is an *extra payment* made under the Pension Scheme because of the fact that the pension is liable to the income tax.

For a more complete definition please refer to Article 42 of the Rules which sets out the amount and conditions of the adjustment. The procedure of granting and mode of calculation - which depend on the provisions of the different national tax regulations - are set out in the Implementing Instructions relating to Article 42.

The International Service for Remunerations and Pensions, under the supervision of the taxation authorities of member countries, calculates the amount of the adjustment, which varies with family status* and the country of taxation. The International Service for Remunerations and Pensions updates its information on the legislative and regulatory provisions of countries’ taxation which govern possible alterations in the corresponding adjustments.

* Only two family alternatives are recognized in calculating the adjustment: unmarried, and married, no children. Pensioners who have neither spouse nor dependants are regarded as “unmarried” and all others as “married, no children”.

2. Are all pensioners entitled to tax adjustment?

For a pensioner to be entitled to tax adjustment, his pension has to be liable to income tax in a member country of the Organisation from which he retired.

It may be noted here that a pensioner living in a non member country of the organisation, where he is liable to tax, will not be granted tax adjustment.

3. What defines the amount of the tax adjustment?

The tax adjustment which is added to the basic benefits is defined in the Rules as:

“50 per cent of the amount by which the recipient’s pension would theoretically need to be increased, were the balance remaining after deduction of the amount of national income tax or taxes on the total to correspond to the amount of the pension calculated in accordance with these Rules”.

The amount of this payment is therefore based on the tax which he would have to pay solely on the taxable income arising from the Pension Scheme, excluding all other income.

4. Does the tax adjustment have to be declared?

Pensioners are reminded that the tax adjustment paid to them **has to be declared** and is therefore taxable.

5. In what currency and in which country is the tax adjustment paid?

The tax adjustment can only be paid in the currency of the member country of the Organisation where the recipient is assessed for income tax.

Example: If a pensioner whose benefits are paid into a bank account in France states that he is taxable in the United-Kingdom, the amount of the tax adjustment due to him, calculated on the basis of the British tax scale, will be paid in the United-Kingdom, in sterling pounds.

When the pension is paid in a different currency from the currency of the country where the recipient is assessed for income tax, the calculation of the tax adjustment is based on the monthly pension converted at the official market rate.

6. By what formula is the tax adjustment calculated?

Taking the taxable amount paid by the Organisation* as the starting point (*any other taxable personal income is not considered for calculation of tax adjustment*) a theoretical gross amount is calculated that leaves, after deduction of national income tax, an amount equivalent to the pension calculated in accordance with the Rules. The tax adjustment actually paid is half what the tax would be on that theoretical gross amount.

It is easier to follow this principle by working out an example:

a)	if the amount of the pension to which the pensioner is entitled is	29 100 €
b)	the theoretical gross amount necessary to yield a) after tax would be	30 868 €
c)	because the tax on the theoretical gross amount under b) is	1 768 €
d)	under Article 42 of the Pension Rules, the annual tax adjustment to which the pensioner is entitled [50 % of c)] is	884 €
e)	and therefore the adjusted pension paid by the Organisation to the pensioner [a) + d)] amounts to	29 984 €
f)	the tax on the adjusted pension e) will be	1 641 €
g)	and the net pension remaining to the pensioner after taxation [e) - f)] will be	28 343 €

But while the principle of adjustment is the same in all member countries, the differences in national tax legislation lead to different calculations for each tax country.

* Family allowances shall be assimilated to pensions in determining the taxable income insofar as similar allowances are taxable under the national tax legislation of the country concerned.

7. The tax is annual; the tax adjustment is monthly - why?

The implementing Instructions under Article 42 of the Pension Rules provide for the tax adjustment to be paid to pensioners:

- i)* in the form of an advance, for the current tax year,
- ii)* in monthly payments, and
- iii)* at the same time as the pension.

It was decided that the advance should be 90% of one-twelfth of the amount which would be due for the tax year concerned.

As a result:

- i)* advances are paid during the tax year whereas in fact, in some countries, the tax is not actually paid by the pensioner until the following tax year;
- ii)* **before the definitive tax scales are approved**, the advances are calculated on the basis of the last tax scales in force;
- iii)* upward or downward corrections are made as soon as the tax scales for the current year are made known.

8. Is there also a tax adjustment on back payments?

When back payments are made retroactively following an increase in the scales, these are taken into account for the tax adjustment during the year of payment.

9. Sometimes the amount of the tax adjustment varies during the year - why?

Pensioners' rights may vary during the year, following a change in salary scales or because of a change in family status. The tax adjustment is affected by all such variations when they affect pensioners' benefits.

10. How does it happen that there are “overpayments” and therefore “negative” adjustments?

In most member countries the taxation scales used in calculating tax adjustments are known only after the tax year is over^{*}. However, as explained in point 7, the advances on tax adjustment are paid monthly with and on the benefits for the current period. As a consequence, there may be a certain time lag between the dates at which the payments are made and the date when the regularization is worked out.

In France for example, the final tax adjustment tables applicable to pensions paid in year n will only not be available around April until the year $n+1$. Consequently the monthly advances paid out from 1st January of year n to 30th April of year $n+1$ will have been based (up to a level of 90%) on the income tax scales for the year $n-1$. It will therefore not be until May of year $n+1$ at the earliest that corrections to the tax adjustments relating to pensions of year n will be possible.

Tax scale brackets are sometimes adjusted. When the time comes to regularize the adjustment, it could happen that the 90% advance already paid may in fact exceed the full entitlement. The Organisation is then obliged to recover what has been overpaid and this will affect not only the year in question but also the advances made for the next year.

^{*} The tax year is established in accordance with the legislation of each country and may vary from one to another.

11. What happens to the tax adjustment in the first year of the pension payment if the commencement of eligibility does not coincide with the beginning of the tax year?

A projection is made of the monthly taxable pension for the remaining months of the tax year concerned.

If this figure is below the tax threshold in the country concerned there is no basis for paying a tax adjustment.

If, however, it is above that threshold, the tax adjustment is calculated and paid normally as described above.

- Example:*
- First pension payment due in September
 - Monthly pension = 1 200 €
 - Number of months of payment for the current tax year (September to December) = 4
i.e. 1 200 € x 4 = 4 800 €

The latter sum is the total taxable income for the fiscal year concerned and below the tax threshold, so there will be no tax adjustment payment for the period, but only as from the following January.

12. What happens if a pensioner moves from one taxing country to another during the year?

The income in each of the two countries is considered separately. The taxable income and the tax adjustment concerned, if there is one, are calculated for the first country and then again, for the second country.

13. What happens in the case of disabled pensioners receiving income from another source?

In order to ensure equal treatment for all pensioners, the calculation relating to tax adjustment is made in principle on the gross amount of the pension, before any deduction of income received from another source. The disabled pensioner is required to declare both the benefits he receives from the Organisation and any income received from other sources.

14. What happens when the pension payment ceases during the year (in case of death for example)?

The amount of the taxable benefits already paid during the fiscal year is considered as annual income and the final calculation of the tax adjustment due is based on that.

Any overpayment will be the subject of a refund request by the Organisation in the pension termination statement.

15. What happens when there is more than one pension?

- 1) For pensions paid to spouses the tax adjustment for each spouse is calculated and paid separately, even if such payments are due by one and the same Organisation.
- 2) If more than one benefit is paid separately either by a single Organisation or by different Organisations to one recipient, the tax adjustment is calculated separately for each of the benefits.
- 3) Survivor's pensions and orphan's pensions (paid to minors) are not added together for purposes of calculating the tax adjustment, unless legal provisions stipulate the contrary.

16. What administrative formalities have to be complied with?

The coordinated Organisations provide the tax authorities of the member country concerned with the names and addresses together with the total amount of the taxable benefits and the relevant tax adjustment of those who are subject to income tax in that country.

Non-acceptance of the tax adjustment does not absolve the Organisation of its duty to declare the benefits to the national tax authorities.

Pensioners for their part must prove that they have made a tax declaration or been taxed on their pensions and adjustments, failing which they will lose their right to the adjustment and be required to reimburse the sums improperly received.

To meet this obligation they are required to produce:

- i)* proof of having made a tax return or
- ii)* a copy of their tax assessment.

The documentary evidence required is specified by the national tax authorities. In order to fill their tax returns, all pensioners are provided, at the end of each fiscal year, in time for the completion of their returns, with a statement giving details of the amount received which are subject to tax.

This statement gives the amount of the pension and allowances and of the tax adjustment, and also a breakdown of these amounts by tax year, for those countries which allow such treatment of back payments.

The pensioner must also inform his Organisation or the International Service for Remunerations and Pensions of any change in his family or residence for taxation purposes when such changes occur. A change of address and date of removal from the tax rolls must therefore be notified to the Organisation without delay.