

Flexible retirement and post-retirement employment – current status and planned changes

Many employees would like to have a flexible transition into retirement. There are multiple options, from early retirement to gradual retirement to deferred retirement. Planning to leave gainful employment is complex and needs to be done well in advance. Tax aspects are often an essential part of retirement planning.

This technical article focuses on flexible retirement from the point of view of tax and social security law and outlines the planned changes in this regard. It also considers voluntary employment beyond the ordinary retirement age.

Pension payments from the OASI perspective (pillar 1)

According to current rules, pensions from the old-age and survivors' insurance (OASI) are paid, on request, once the ordinary retirement age is reached. OASI pensions are taxed in full. If the request is submitted later, the OASI pension is paid retroactively for the last 5 years from the start of entitlement without increase and interest.

The OASI pension can be drawn in advance by up to two years before reaching the ordinary retirement age; in return, the OASI pension amount is reduced by 6.8% for each year of advance payments. Those who claim their retirement benefits early continue to be subject to the compulsory OASI contributions until they reach the ordinary retirement age. Anyone who is not in gainful employment after the early retirement must pay contributions as a non-employed person. Depending on the constellation, contributions are covered via the spouse or via a residual income-earning activity.

On request, the OASI pension can also be deferred by 1–5 years. This will lead to a pension increase of 5.2%–31.5%. From a tax perspective, a pension deferral can be attractive under certain circumstances, provided that a lower marginal tax rate can be expected in the future.

The current OASI law does not envisage a gradual retirement.

Retirement from an occupational pension plan perspective (pillar 2)

Once the ordinary retirement age is reached, according to current rules, the retirement assets from the occupational pension plan are paid out as either a pension or a lump sum, depending on the regulations of the pension fund. A lump-sum payment is more tax-efficient since it benefits from a substantially reduced rate and is taxed separately from all other income, whereas the pension payments are taxed in full as income. If voluntary buy-ins to pillar 2 were made previously, a lockup period of three years must be observed before the pension assets should be withdrawn; this lockup clause also applies in the event of early retirement at the request of the employer.

Depending on the structure of the pension plan regulations, early withdrawal of the pension assets in the form of a lump sum or pension is possible from the age of 58.

Retirement can be deferred until the age of 70 if the pension plan regulations provide for such an option and if the person remains gainfully employed. In this case, the taxation of the pension benefit is also deferred.

Gradual retirement is currently not explicitly regulated in the occupational pension plan, but is permitted in practice. Depending on the administrative practice of the cantonal tax authorities of the canton of residence, the following cumulative requirements must be met from a tax perspective:

- Working hours are reduced significantly, permanently, and demonstrably (usually by at least 20%–30% and for at least 1 year).
- The reduction in working hours comes with a reduction in salary and insured earnings.
- The retirement benefits paid correspond to the reduction in working hours.
- The pension plan regulations must allow partial retirement.

The staggered payout of retirement assets offers tax benefits since splitting the payments breaks the tax progression. Partial retirements that only serve to withdraw pension assets in

installments are considered as abusive from a tax perspective. But according to current practice (e.g., in the Canton of Zurich), two capital withdrawals are not deemed objectionable. Other cantons, such as Bern, allow up to three capital withdrawals.

Withdrawal from the restricted private pension plan (pillar 3a)

According to current rules, the accumulated capital in pillar 3a can be withdrawn at the earliest five years before reaching the ordinary retirement age irrespective of whether employment is discontinued or continued. The withdrawal of pillar 3a assets is taxed in the same way as a lump-sum withdrawal from an occupational pension plan, i.e., privileged and separated from other income.

If there are several pillar 3a accounts, a staggered withdrawal is recommended from a tax perspective in order to break the tax progression. Withdrawals from occupational pension plans and restricted private pension plans made in the same tax year are added together to determine the tax rate.

Working after the ordinary retirement age

The income of gainfully employed individuals who work beyond their ordinary retirement age is taxed in full. There is no tax-free allowance.

Anyone who is gainfully employed after reaching the ordinary retirement age continues to pay social security contributions on their income according to current rules, but only on income above the tax-free amount of CHF 1,400 per month or CHF 16,800 per year per employment. Contributions to unemployment insurance, on the other hand, no longer apply. The social security contributions do not lead to a higher retirement pension and they need therefore to be considered as solidarity contributions.

Depending on the pension plan regulations, it is possible to remain insured under the occupational pension plan even after reaching the ordinary retirement age.

A person who continues to work can continue to make contributions to pillar 3a up to five years after reaching the ordinary retirement age. Without ties to a pension fund, up to 20% of the

income earned (maximum CHF 34,416) can be paid in annually; with ties to a pension fund, the annual contribution is capped at CHF 6,883 (as of 2022).

If a lump sum was withdrawn from the pension fund after reaching the ordinary retirement age but gainful employment is continued, contributions to pillar 3 are possible in principle, and are tax-efficient. However, such a constellation could be classified as tax avoidance, so the combination of withdrawing pillar 2 funds and paying into pillar 3a should be exercised with caution.

OASI reform: flexible retirement

On September 25, 2022, the Swiss will vote on the OASI reform (OASI 21). In addition to setting the retirement age at 65 for both men and women, there are proposals to make retirement more flexible. The OASI pension can be drawn beginning in any month between the ages of 63 and 70. In the case of deferred retirement, the pension amount will increase; in the case of early retirement, it will decrease. A gradual retirement with partial pension payments is also possible (reduction in gainful employment of at least 20%).

Those who work beyond the ordinary retirement age and continue to pay OASI contributions can improve their retirement entitlement up to the level required for a full pension, and by doing so close any gaps in contributions. The provision is that the income after the ordinary retirement age must be at least 40% of the previous income and the OASI contributions must be no less than the statutory OASI minimum.

Moreover, the flexibilization of the occupational pension plan with partial pensions will be stipulated by law. Pension funds will have to offer at least three steps for the payout of retirement assets from the occupational pension plan. In the event of lump-sum withdrawals, the regulations can provide for only three partial pension payouts. It is not clear at this stage whether the tax authorities will adjust their practice and whether, from a tax perspective, three-step lump-sum withdrawals will be possible in all cantons.

Outlook – Changes proposed by the Economic Affairs and Taxation Committee with regard to gainful employment after the ordinary retirement age

In addition, the Economic Affairs and Taxation Committee of the National Council (EATC-N) submitted a motion in June 2022 instructing the Federal Council to encourage gainful employment

beyond the ordinary retirement age by granting tax benefits. Various options are to be examined, including (i) the introduction of a "pensioner deduction" once minimum working hours or a minimum income have been reached, (ii) the exemption of OASI retirement pensions from income tax once minimum working hours or a minimum income have been reached, or (iii) a reduction in income tax on part or all of the income earned through employment. How the financial incentives for post-retirement employment should be shaped leaves much room for maneuver and will certainly be the subject of many discussions before any implementation takes place.

We will keep you informed of further developments.

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