

qualify for alternative unique preferential tax treatment. The “personal pension” deduction is but one option in the special subset of opportunities to minimize income taxes.

In addition to restraints on forms of investment, “personal pension” deductions generally severely limit or outright prohibit the withdrawal of funds before some specified retirement age. This is an undesirable feature from the saver’s point of view, as retirement funds normally would provide a concurrent contingency fund.

Younger participants in the “personal pension” program are faced with a longer period of locked-in funds, yet there is no compensating adjustment in the tax inducement mechanism to reflect this variable feature. Consequently, one may postulate that participation in such a program—*ceteris paribus*—is directly related to the age of the taxpayer; that is, inversely related to the number of illiquidity years between contribution and retirement age. An analysis of Canadian participation, summarized in an appendix, does not reject this hypothesis.¹² The tests indicate that personal pension contributions are significantly related to the age of the taxpayer.¹³ Individuals initiating a retirement program late in life will have few remaining years to accumulate an adequate fund to supplement social security.¹⁴

As a final note, preliminary analysis of Canadian participation data indicates that individuals covered by company contributory pensions will reduce “personal pension” contributions accordingly, and to some degree the two programs are substitutes.¹⁵ If this observation is valid, an expansion of the contributory pension movement will offset some increases in personal saving attributable to the “personal pension” deduction (at least among employees eligible for both programs).

The introduction of new income tax inducements, then, may not significantly increase the rate of personal retirement saving. Certainly this is the experience of the “personal pension” deduction instituted on a limited basis in the United States and as a universal taxpayer deduction in Canada. An appreciation of the true relative net yield advantages to participation, coupled with investment and liquidity constraints, may explain this small taxpayer response. Individuals generally have existing alternatives that discount the superficial attractiveness of the “personal pension” deduction.

¹² The U.S. individual income-tax returns do not record the age of the taxpayers, but Canadians are requested to report their birth year on their respective returns. I gratefully acknowledge the interest and cooperation of the Canadian Department of National Revenue (Taxation Division) in providing detailed information on taxpayer participation, subject to departmental policies regarding the disclosure of the taxpayer’s identity.

¹³ The age distribution of the Canadian labor force is skewed to the younger workers, and this bias tends to reinforce the above participation data. Canada, “Census of Canada, 1961, Labour Force: Employment Status by Age and Sex” (catalog 94-502), Bulletin 3.1/2, Mar. 31, 1964.

¹⁴ I assume in this paper that the intent of a “personal pension” deduction is to increase the rate of personal saving. While propensities to save may be relatively constant over time, motives for saving may vary through the life cycle. Retirement saving, therefore, may be an increasing function of age, regardless of the “personal pension” deduction. If this program is to be successful, however, the effect of the deduction presumably will be to increase the rate of retirement saving at all age levels. The negligible rate of participation in the Canadian program by taxpayers under age 40 (adjusted for income) tends to support the illiquidity hypothesis—that there is more to this program than increases in net (after-tax) yields.

¹⁵ The subsample of taxpayers studied declared company pension and personal pension contributions significantly under any statutory ceilings, and therefore were free to add to the amount of “personal pension” contribution at their discretion.