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Do Tax Incentives for Saving in Pension Accounts Cause Debt Accumulation? Evidence from Danish Register Data ☆

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Abstract

This paper applies a quasi-experimental research design on a Danish 2010 policy that reduced tax incentives for saving in annuity pension schemes to show significant substitution of savings from retirement accounts to gross debt repayments. We find that for every 1 Danish currency unit reduction in retirement savings 31 cents goes to debt repayments. Taking into account all types of savings, we find full crowd-out. Consistent with previous findings, we document that the effect is driven by a minority, about 23 percent, who actively rebalance their savings.

Keywords: Crowding-out, Pension Savings, Household Debt

Tax-favoured pension accounts have attracted attention over the years because of their importance to individual savings behaviour. Many developed countries use tax subsidies to affect individual saving rates and economists strive to determine the outcomes of such policies. Recent empirical work suggests that savings in tax-favoured retirement accounts are fully crowded out (Chetty et al., 2014). It is less clear, however, whether savings in pension accounts are crowded out by savings in non-retirement accounts or debt repayments. Imagine that tax incentives for saving in pension schemes are reduced from one day to the next and taxpayers respond by shifting savings from retirement accounts to the now-highest after-tax-return account. Given that debt usually carries higer interests than savings, outstanding debt should be repaid before saving in non-retirement accounts. A growing interest in the development of household

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