SGI Sustainable Governance Indicators

2015 Pensions Report

Pension Policy

Bertelsmann Stiftung

Indicator

Pension Policy

Question

To what extent does pension policy realize goals of poverty prevention, intergenerational equity and fiscal sustainability?

41 OECD and EU countries are sorted according to their performance on a scale from 10 (best) to 1 (lowest). This scale is tied to four qualitative evaluation levels.

10-9 = Pension policy achieves the objectives fully.

8-6 = Pension policy achieves the objectives largely.

5-3 = Pension policy achieves the objectives partly.

2-1 = Pension policy does not achieve the objectives at all.

Switzerland

Score 10

The Swiss pension system is based on three pillars, each with its own logic of financing and redistribution. The underlying concept is that pension income should not fall below the subsistence level, and should provide 60% of average pre-retirement income. The first pillar guarantees a basic income. The minimum benefit level for a couple as of 2013 was CHF 28,080 (about €23,400) per year, while the maximum benefit was CHF 42,120 (about €35,100). Employers and employees finance this through contributions. It is a pay-as-you-go system, and is highly redistributive, since the maximum benefit level for couples (provided to high-income earners) is just 1.5 times that of the minimum benefit level, while contributions are proportional to income.

The second pillar is a funded system financed through contributions by employers and employees. Contributions and benefits are proportional to income. Employees whose income from the first pillar already covers about 60% of their wage income are not entitled to this system. Many pension programs, particularly in the public sector, are very generous, and provide pension incomes (first and second pillars combined) that exceed 60% of previous income.

The third pillar takes the form of personal tax-deductible savings of up to CHF 6,739 per year (about €5,600). This system benefits high-income groups, since they can afford to put aside these sums and have the highest returns on these savings given the tax advantages.

Demographic changes will present major challenges to the first pillar over time. Provided there is no major change in GDP or productivity growth rates, the ability to sustain this pillar will be strained unless the average age of retirement (currently 65 for men and 64 for women) is increased or benefit levels fall. However, given the solid basis of the pension system overall, Switzerland faces less pressure than many other European countries to adapt to demographic change.

However, Switzerland has tried to modernize its system at a relatively early stage. After several previous reform failures, the Social Democratic minister for social policy embarked in 2013 on a strategy for achieving compromise that has previously proved successful in other areas. This consists of compensating those who are going to lose as a result of policy changes with gains in other areas. This implies that the reform is necessarily a package of policies. However, at the time of writing, this reform plan was in jeopardy. Trade unions and left-leaning politicians opposed the plan, since they did not want any reduction of benefit levels or criteria – such as increasing the retirement age for women from 64 to 65 – while employers and bourgeois politicians had offered support only for those elements of the package they liked, effectively destroying the package's balance. As of the time of writing, the actors had not yet moved toward effective negotiation and compromise.

With regard to poverty prevention, the pension system is highly efficient. Every citizen can claim additional payments if he or she is not entitled to the first pillar's minimum pension. The system as a whole has a high degree of intergenerational equity, as it rests on three different pillars, and only the first pillar is based on intergenerational payments.

Financial sustainability will be a potential problem over time, but remains stronger than in comparable countries such as Germany.

Denmark

Score 9

The pension policy in Denmark is well-diversified in accordance with the World Bank's three-pillar conceptual framework. Concerning the first pillar, Denmark has public pensions in the form of a universal base pension with a means tested supplement. For the second pillar, labor market pensions are negotiated in the labor market but mandatory for the individual. With these pensions, the contribution is split between employers (2/3) and employees (1/3). Moreover, the contribution rate has been increased over the years and is now 12% or more for most employees. As for the third pillar, it is comprised of both tax-subsidized pension arrangements (tied until retirement) offered by insurance companies, pension funds and banks as well as other forms of savings (for most households in the form of housing wealth).

In Denmark, pension savings are tax subsidized. The return is taxed at 15.3%, which is below the normal capital income tax rate (33%). Moreover, contributions are deductible in taxable income, while pensions are taxable income. For some high income groups this adds an additional subsidy since deductions on contributions are higher than on the outpayment due to progressive elements in taxation. The tax principle causes problems in relation to portability when, for example, Danish pensioners decide to move to another country. This principle was changed for so-called capital pensions (a payment released as a lump sum) starting in 2013, motivated by the implied forward shifting of tax revenue contributing toward meeting budget targets.

The combination of the different pillars of the pension scheme creates a pension scheme that both protects against low income for the elderly (distributional objective) and ensures that most have a pension, which is reasonable in relation to the income earned when the pensioner was active in the labor market (consumption smoothing). The Danish pension scheme ranks first in the Melbourne Mercer Global Pension Index. The division of work between the public and private pensions systems, however, has its problems. The means testing of public pension supplements has the effect that the net gain from additional pension savings or later retirements can be rather low for a broad segment of income earners. Moreover, the system is very complicated. The system is still maturing since contribution rates to the labor market pensions have been raised since the late 1980s. This implies a substantial lag before workers can retire with a pension based on current contribution rates. It has also been debated whether the high level of forced pension savings contributes to high debt levels and thus accounts for the fact that Danish households have very high debt levels, although they have positive net-wealth. Due to the different exposure and liquidity of assets and debt this may constitute a systemic risk factor. As the system matures some of the abovementioned problems may be more important. A Pension Commission was appointed in 2014 to overhaul the pension system.

In addition to the public pension scheme, the early retirement scheme is important. It allows retirement at the age of 60 and offers a benefit until the statutory pension age of 65.The scheme is voluntary and contribution-based, but it is highly subsidized. The scheme was introduced in 1979 as a labor market initiative to cope with youth unemployment, but has since become an integral part of the welfare package. The scheme has been much debated since its introduction and reformed a number of times. Among others, incentives have been introduced to delay retirement until age 62. The most recent reform will result in an increase in the earliest retirement age (and eventually tie it to life-expectancy) and a reduction in the early retirement period from five to three years.

While labor force participation is generally high in Denmark, even for citizens aged 50 to 55, it is low for those aged 60 to 65, which in part can be explained by the early-retirement scheme. The problems of an aging population are also affecting Denmark.

The financial consequences of increasing longevity are large, and have been at the core of policy debates for some years. A so-called welfare reform was approved with broad parliamentary support in 2006. This scheme increases the statutory age for early retirement by two years over the period from 2019 to 2023, and the statutory pension age by two years over the period from 2024 to 2027. After these transitions periods, the statutory ages are linked to longevity via an indexation mechanism targeting an average retirement period of 14.5 years plus a possible three years on early retirement. This reform is a significant response to the challenge of Denmark's aging population, and in combination with other recent reforms, will ensure the sustainability of its public finances.

Citation:
Basispensioner, rapport udgivet af udvalg nedsat af Penge- og Pensionsudvalget, København 2012.

Finland

Score 9

The Finnish pension system has two pillars: a residence-based, national pension and an employment-based, earnings-related pension. Private pension schemes also exist. Successfully managed by social partners as well as by the government, overall pension policy and the mixture of public and private pension schemes has been able to effectively provide support for Finnish citizens. Finland has been able to avoid the classic problem of poverty in old age. The average pension by the end of December 2013 was €1,760 per month for men and €1,376 per month for women. The total number of pension recipients was 623,210 men and 762,540 women. Still, the aging of Finland's population creates problems in terms of labor-force maintenance and fiscal capability, and the economic crisis in Europe has added considerably to these problems. A reform of the pensions system between 2004 and 2005 aimed to introduce greater flexibility into pension policy and create more incentives to encourage workers to stay in employment later in life. While these reforms were successful, further reforms are scheduled for 2017. In September 2014, social partners agreed on further gradual raise of the lowest retirement age to 65 (with exceptions for labor intensive occupations at 63), flexible retirement and amendments of the accumulation rate. The results of these negotiations gives cause for cautious optimism regarding the financial sustainability of the pension system.

Citation:
Nicholas Barr, "The Pension System in Finland: Adequacy, Sustainability and Systems Design", Finnish Centre for Pensions, Helsinki 2011.
"Earnings-related Pension System in Graphs and Figures", Finnish Centre for Pensions, 2014.
Vuoden 2017 työeläkeuudistus.
http://www.etk.fi/fi/service/el%C3%A4keuudistus_2017/1628/el%C3%A4keuudistus_2017. Finnish Centre for Pensions 2014.

Netherlands

Score 9

Since 2007 pension age has incrementally increased from 61.0 to 63.9 in 2013, in which year 73,000 pensioners stopped working. The Dutch pension system is based on three pillars. The first pillar is the basic, state-run old-age pension (AOW) for people 65 years and older. Everyone who pays Dutch wage tax and/or income tax and who is not yet 65 pays into the AOW system. The system may be considered a "pay-as-you-go" system. In comparison to other European countries, this pillar makes up only a limited part of the total old-age pension system in the Netherlands. Because the current number of pensioners will double over the next few decades, the system is subject to considerable and increasing pressure. The second pillar consists of the occupational pension schemes which serve to supplement the AOW scheme. The employer makes a pension commitment and the pension scheme covers all employees of the company or industry/branch. The third pillar comprises supplementary personal pension schemes which anyone can buy from insurance companies.

This system, like most European systems, is vulnerable to a rise in the aging population and disturbances in the international financial market. As of 2013, the government will stepwise increase the age of AOW retirement so that in 2018 the retirement age will be 66 and in 2021, 67. For supplementary pension schemes the retirement age will rise to 67 in 2014. As a result of the financial crisis and very low interest rates, pension fund assets have been shrinking. At the same time, however, the liquidity ratio of pension funds must be maintained at a minimum of 105%. The timeframe for recovery after a decrease of the minimum liquidity ratio was increased by the Dutch national bank from three to a maximum of five years. In spite of this, quite a few pension insurance companies had to decrease benefits from -0.5% to as much as 7% per year. Interim framework bills for strengthening the governance of pension funds (conditions for indexation of pension benefits, pensioners in the government board, oversight commissions, comparative monitoring) were adopted by parliament in the summer of 2014. A more definitive reform of the Dutch pension system will be proposed following a website-facilitated national dialogue on pensions in four deliberative meetings between govenment and all stakeholders.

Citation:
Ministerie van Sociale Zaken en Werkgelegenheid (2014), Toekomst Pensioenstelsel (www. Rijksoverheid.nl/onderwerpen/pensioen/toekomst-pensioenen)

CBS (2013), Ruim 40 procent van werknemers bij pensionering 65 jaar of ouder (www.cbs.nl/nl-NL/the,as/dossiers/vergrijzing/publicaties)

Rijksoverheid, Wetsvoorstel 'Wet aanpassing financieel toetsingskader', 25-06-2014 (rijksoverheid.nl)

Norway

Score 9

Norway's pension system is well-positioned to sustain the aging of the population expected in coming decades. With birth rates that have been persistently high by European standards, the demographic burden is less than in most comparable countries. Future pensions are essentially guaranteed by the massive savings accumulated in the petroleum fund, now renamed the Government Pension Fund – Global (Statens pensjonsfond – Utland).

A pension reform passed in 2009 came into effect in 2011. This has further strengthened the sustainability of the system. The crux of the reform was to introduce more choice and flexibility into the system in terms of retirement, while adding new mechanisms of gradual demographic adjustment. One major goal, in addition to improving financial sustainability, was to redesign contribution and benefit rules so as to encourage employment and discourage early retirement. This reform was carefully prepared, starting with the appointment of a cross-party pension commission in 2001; this body reported its findings in 2004, leading to a five-year process of political implementation that culminated in the 2009 reform, which drew widespread approval. During the process, the proposed reform was criticized as being "too little, too late," but that criticism has largely subsided today.

Pensions are by international comparison generous and equitable, and are set to remain so. The universal basic minimum pension is large enough to essentially eliminate the risk of poverty in old age. The recent reform has strengthened the link between contributions and benefits for earnings-related pensions, while improving the system's intergenerational equity. The population has broad confidence in the adequacy of future pensions from the state system, and there has hence been no significant move toward private-sector pension insurance.

Australia

Score 8

Australia has two explicit pension systems, the public age pension and private employment-related pensions. The age pension is funded from general taxation revenue, and because it is means-tested, it effectively acts as a social safety net. However, pensioners enjoy additional benefits, for example, access to universal health care, concessions on pharmaceutical and other government services as well as tax concessions.

Currently, the age pension is still the dominant source of income for retirees. Nearly 80% of pensioners receive a means-tested pension from the government. The result is that Australian pensioners' income is the lowest in the OECD when compared to the income of the working population. However, over time the balance will shift to the private pension system, which was only introduced on a wide scale in 1992, and only reached a minimum contribution rate of 9% of earnings in 2002. The minimum contribution rate increased to 9.25% on 1 July 2013 and to 9.5% on 1 July 2014. It was scheduled to further increase by 0.5% per year until it reached 12% on 1 July 2019, but in 2014 the Abbott government deferred further increases until 1 July 2021.

The aging population has increased the anticipated pressures on the pension and in response, in the 2009 – 2010 budget, the government indicated that it would progressively increase the age of eligibility for the age pension from 65 to 67 years by July 2023. In its 2014 budget, the Abbott government announced plans to further increase the age of eligibility to 70 years by 2035 and to index the pension to consumer price inflation rather than male average weekly earnings from 1 July 2017. However, the government has been unable to pass the required legislation in the Senate.

In terms of intergenerational inequity, the gradual nature of the shift since 1992 from a pay-as-you-go public pension toward a private pension system supplemented by a public pension has meant that relatively little inequity has resulted between generations. As reliance on private pensions grows over time, intergenerational equity will continue to improve.

Lastly, concerning the fiscal sustainability of the pension system, while reliance on the age pension will continue to be high for many years into the future, in broad terms the pension system is relatively sustainable, with private pensions increasingly taking on more of the financial burden. Concerns have been raised, however, about the sustainability and equity of maintaining the tax-free status of private retirement income. The current absence of significant constraints on how private pension assets are used is also of concern, with some evidence that retirees run down private pension holdings too quickly and become reliant on the age pension.

Citation:
OECD, Pensions at a glance. Paris, OECD 2013, p. 68-70.

Canada

Score 8

The basic components of Canada’s public pension retirement-income system are the demogrant Old Age Security (OAS), the income-tested Guaranteed Income Supplement (GIS) and the contribution-fed, earnings-based Canada/Quebec Pension Plan (CPP/QPP). Other tiers of the pension system include employer pension plans (both defined-benefit and defined-contribution plans) and government incentive programs for individual saving such as Registered Retirement Saving Plan (RRSPs) and Tax-Free Saving Accounts (TFSAs).

The effectiveness of the Canadian pension system as a tool to reduce poverty among the elderly depends on the poverty measure used. Using Statistics Canada’s Low-Income Cutoff (LICO) measure of poverty, an absolute definition, the poverty rate for persons 65 and over was 5% in 2009, down from 10% in 1995 and 20% in 1981. In contrast, Statistics Canada’s Low-Income Measure (LIM), a relative poverty definition, was 12% for the elderly in 2009, up from 4% in 1995.

Intergenerational equity is not a major concern for the Canadian pension system. It is true that the early recipients of CPP benefits in the phase in-period of the plan received considerably more than they contributed from an actuarial perspective. There is now a much closer relationship between contributions and benefits on an individual basis, so intergenerational transfers are much less significant. The combination of the OAS/GIS and the CPP/QPP provides a relatively high base income for low-income earners. At the same time, the CPP/QPP is designed to replace only 25% of the average wage. This means that middle-income workers with no employer pension plan or private savings may encounter problems in replacing a sufficient proportion of their pre-retirement earnings. The federal government has recognized this weakness in the pension system and in 2012 responded by creating the Pooled Registered Pension Plan (PRPP) to encourage more employee saving in workplaces without registered pension plans. However, utilization rates for this new program have been very low. Many pension experts believe that expansion of the CPP/QPP, either on a voluntary or mandatory basis, is the most appropriate path for the provision of adequate pensions for all Canadians. The CPP is currently considered to be actuarially sound and fiscally sustainable at its current rate and benefit structure, due to large increases in contribution rates implemented in the late 1990s. The fiscal sustainability of the OAS/GIS is tied to the sustainability of the federal government's overall fiscal balance, and is fostered by the indexation of benefits to the CPI rather than to nominal wage increases.

Czech Republic

Score 8

The Czech pension system has developed through a gradual and partial reform of the pay-as-you-go system that existed before 1989. Sustainability of the pension system with an increasingly aging population has pointed to the need for reform (Loužek 2014). A "small pension reform" (2012) extended the retirement age, equalized the retirement age for men and women and increased the minimum insurance length to 35 years after 2018. The controversial "large" pension reform that came into force in January 2013 under the Nečas government aimed at diversifying funding within a two-pillar scheme. The second pillar includes a voluntary private element which could channel part of the compulsory contributions paid to the pension system to newly established private companies. Entering this new pillar is voluntary, but irreversible. General interest in participating in the new scheme has been low, but highest among those aged 35 to 44, in which 8% opted for voluntary contributions. Social partners have expressed negative attitudes toward this reform, and the ČSSD party warned in the 2013 election campaign that it would scrap the system should it win the election. In November 2014, the Sobotka government decided to close the second pillar by January 2016.

Loužek, Marek, 2014: Pension reform in the Czech Republic after 2010, in: Post-Communist Economies 26(1): 89-102.

Sweden

Score 8

Sweden's pension system succeeds in preventing poverty among senior citizens, but those living only on the very basic pension have problems making ends meet. In fact, Sweden has twice as many pensioners living at or below the poverty line as in Denmark and three times as many as in Norway, two comparable Nordic countries. Pensioners living on a baseline pension with limited savings and no private pensions insurance are eligible for additional support from social welfare programs, however.

The stability of the pensions system was a problem for a long time but appears to have improved over the last several years, due to major reforms of the whole pension system in Sweden. One result of the pension reforms is a new public-private mix, strengthening capital funded occupational and private pension schemes. The distributional principles appear to be sound but the volatility of the stock market during the most recent past has meant a major source of uncertainty about how stable and sustainable the system will be in the future.

Lastly, in regard to equity in the system, the results are mixed. Ideally, a pension system ensures equity among pensioners, the active work force and the adolescent generation. If equity refers to basically similar living conditions, Sweden's system fails in this respect. If equity however refers to a provision of baseline material goods related to needs, the performance of the system looks better. Some studies state that the new Swedish pension system does not undermine inter-generational equity, as long as the entry into the labor market for the adolescent generation is not blocked. Therefore, high and persistent youth unemployment rates threaten this aspect of equity in the long run.

United Kingdom

Score 8

The United Kingdom has a three-pillar system in which the second (employer-based) is the mainstay of the pension system. Private pension-system funds were hardest hit by the financial crisis, and some need capital injections from employers, but this has not had a significant effect on the incomes of those already retired. New entrants into private pension schemes are being offered less attractive terms than their predecessors. The Pensions Act 2010 raised the age of state pension eligibility to 66 (from 65 for men and 60 for women). Coalition reforms have shifted pressure from pension funds to individual pensioners, and are thus likely to change living conditions for British pensioners substantially in the years to come. However, compared with many other countries, the UK pension system is fiscally sustainable.

The United Kingdom used to have a comparatively high degree of poverty among the elderly, but this has improved as pension provision has expanded, partly through specific additional payments for purposes such as winter heating. The overall figures disguise inequalities within the group of pensioners, however. Lifelong housewives, for example, fare much worse than those who have the benefit of adding occupational or private pensions to their income from the state pension system. On average, children are at a much higher risk of poverty than pensioners, whose share among the poor continues to shrink. But at the same time, they constitute the largest group just above the poverty line, indicating a tight but sufficient pension policy. Most pensioners are, however, on reasonably comfortable incomes and, if anything, recent debate has been about cutting some of the fringe benefits of better-off pensioners (such as free bus travel). To date, the government has been unwilling to tackle this issue, and has committed itself to maintaining pensioner benefits.

Estonia

Score 7

Estonia's three-pillar pension system has been in force since 2002. In terms of pension payments, the situation is still transitional because most of the current pensioners do not have the mandatory funded pillar, and their benefits depend on the social-insurance contributions made by current employees to the first pillar. Voluntary privately funded pensions also exist (third pillar), but have remained marginal in terms of coverage and assets.

Poverty rates among the elderly are modest compared with many OECD countries, and has slightly decreased in recent years. However, old-age pension benefits are still quite minimal (€353 per month in 2014), and elderly people still struggle to make ends meet.

Despite modest pension expenditures (roughly 5.5% of GDP), the sustainability of Estonia's pension system is at risk. State pension-insurance expenditure will exceed social tax revenue by close to €363 million in 2014, and according to the state budget strategy, this deficit will reach €474 million in 2017. A report by the National Audit Office revealed that the performance of mandatory fully funded schemes has not met expectations. The actual returns on the funds have amounted to zero on average. Furthermore, the present pension system does not encourage people to work longer, or even until retirement age (the average retirement age is almost eight years lower than the formal age of pension eligibility). Early retirement is also incentivized through numerous special pension schemes that previous reform plans have sought to abolish. However, these reforms have been put on hold. Thus, Estonia faces an urgent challenge, and must increase the efficiency of the three-pillar structure in order to serve its aging population in a sustainable manner.

Citation:
State Audit Office (2014) Sustainability of the state's pension system. Does the state guarantee the effective functioning of pension pillars?http://www.riigikontroll.ee/Suhtedavalikkusega/Pressiteated/tabid/168/ItemId/704/amid/557/language/en-US/Default.aspx (accessed 01 Nov.2014)

Iceland

Score 7

Iceland's pension policy is based on a tax-financed, means-tested social security program supported by tax incentives to encourage participation in occupational pension funds and voluntary savings schemes. The pension funds, which are based on employee contributions of 4% of total wages and employer contributions of 8%, are designed to provide a pension equivalent to 56% of an individual's average working-life wage. In addition, employees can opt to pay a further 4%, with a further employer contribution of 2%, into a voluntary savings program.

In the past, it has appeared that Iceland's pension policy was both conducive to poverty prevention and fiscally sustainable. However, Iceland's pension funds experienced heavy losses as their investment in, among other stock, Iceland's banks depreciated substantially following the collapse of the banking sector in 2008. These losses, which totaled about a third of GDP, caused most pension funds to reduce their payments to members and further reduced the living standards of pension recipients. That said, the pension funds have recovered since 2008 and have an overall assets-to-GDP ratio that is among the highest in the OECD group.

Two main issues confront the pension system. First, the Pension Fund of State Employees, the largest pension fund, has a huge funding gap that will have to be financed through future tax revenue. Second, given that pension funds have previously been used to fund additional social programs, there is a danger that the government will use the funds to relieve Iceland's foreign exchange and balance-of-payments deficits.

Citation:
Ísleifsson, Ólafur (2012),"Vulnerability of pension fund balances," Stjórnmál og stjórnsýsla, Vol. 8, No 2., pp. 543-564. http://www.stjornmalogstjornsysla.i s/wp-content/uploads/2012/12/a.2012.8.2.17.pdf

Israel

Score 7

Over the past two decades, Israel initiated several reforms of pension policy, profoundly changing the system with respect to employer-based pensions and national insurance. The reforms introduced a new defined-benefit (DC) pension plan, with contributions invested in the market instead of government bonds. In so doing, it significantly transformed the underfunded system driven by collective bargaining into a system of mainly individually defined-contribution accounts with varied levels of collective risk sharing. In the last two years, Israel increased the legal maximum for insurance contributions (including that for pension insurance), with the aim of improving fiscal stability and the system's overall sustainability.

One of its main consequences was shifting more responsibility to individuals. This risk was partly resolved by an agreement that was struck between the "New Histadrut" trade union, the Coordination Office of the Economic Organizations and the government. Once approved by the government in 2008, it insured a steady pension contribution to every salaried employee with two-thirds of the fund financed by his or her employer. In 2014, the contribution was set at a minimum of 17.5% of the monthly salary and is expected to yield high turnovers in the future. Thus, it is meant to secure the future of Israel’s moderately aging population. However, it also reduced available income for poor households and does not fund supplementary income that is critical for the extremely poor.

At the end of 2008, the Israeli government implemented a reform that introduced a requirement for life-cycle strategies in pension savings products. The reform initiated the establishment of different investment tracks with age-based investment profiles, serving as default options for savers who failed to make an investment choices by themselves. Since the new system is regulated rather than operated by the state, it is subjected to the rules of the free market; even though legally every worker is entitled to a pension, private pensions have discretion over client selection.

Citation:
Achdut, Leah and Spivak, Avia, “The pension system in Israel after 15 years of reforms,” Policy Studies 8, 2009: http://www.vanleer.org.il/sites/files/product-pdf/research_polilcy8.pdf (Hebrew)

Arlozerov, Merav, “The matter at hand: Pension that leads to poverty at old age,” TheMarker website, 15.2.2012 (Hebrew).

Bowers, Liora, “Pensions, Poverty and the elderly in Israel”, Taub center policy brief, January 2014: http://www.themarker.com/markets/1.1642036 (Hebrew).

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http://www.oecd.org/finance/private-pensions/49498122.pdf

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“Social situation report: 2011,” Adva center, December 2011:
http://www.adva.org/uploaded/social-HEB-site2.pdf (Hebrew).

“The Taxing system: Main recommendations,” Trachtenberg committee paper via Haaretz website:
http://www.haaretz.co.il/hasite/images/images/taxes.pdf (Hebrew).

Lithuania

Score 7

Lithuania’s pension system does not adequately protect recipients against old-age poverty. The share of the population over 65 years of age who are poor or suffer from social exclusion is well above the EU average; indeed, since the crisis, 35.7% of all people over 65 are at risk of poverty in 2012. During the financial crisis, the

Lithuanian authorities were forced to cut social expenditures (including pensions), thus increasing the risk of poverty for some retired people. However, pensions were restored to their pre-crisis levels as of 1 January 2012, and policymakers later decided to compensate pensioners for pension cuts made during the crisis within a period of three years.

In terms of intergenerational equity, Lithuania's three-pillar pension system, which mixes public and private pension programs, should ensure equity among pensioners, the active labor force and the adolescent generation. The 2004 pension reform added two privately funded pillars (a statutory pillar that receives a portion of mandatory state social-insurance contributions, and a voluntary pillar that is funded through private contributions) to the pay-as-you-go (PAYG) state insurance fund. However, this system as a whole suffers from instability and uncertainty; for instance, during the financial crisis, the government cut the share of social-security contributions going to the second-pillar private pension funds from 5.5% to 1.5%. Beginning in 2013, this contribution was increased to 2.5%. Also in 2013, another change to the private-savings system was introduced that reduced the contribution level to 2%. Furthermore, it allowed individuals either to stop their private contributions or to gradually top up 2% from the social-security contributions to the state insurance fund. Beginning in 2020, the share of contributions transferred from the state social-security fund to private funds is expected to be increased to 3.5%. However, during debates on the draft 2015 budget some government-coalition policymakers said that a complete overhaul of the private-savings systems may be necessary if budget forecasts prove to be too optimistic, and that there is thus a need to find additional revenue sources in 2015. Comments of this nature have led the population to distrust the pension system, complicating the task of accumulating adequate retirement savings.

In terms of fiscal stability, Lithuania's pension system faces unfavorable demographic change ahead. The old-age dependency ratio is projected to more than double by 2060 as the working-age population shrinks by a projected 35.8%. The parliament approved a gradual increase in the age of pension eligibility to 65 years in 2011, and in 2012 changed the pension-system's second pillar to provide for a possible gradual increase in the share of social contributions received by private funds (however, only 33% of those who participated in the previous pension scheme decided to join a new scheme). The unsustainable PAYG pillar continues to pose a risk to the sustainability of public finances overall. Therefore, a comprehensive reform of the state insurance fund, including pensions as well as other social expenditures, remains necessary in order to ensure its long-term sustainability while safeguarding its ability to protect people from poverty. In addition, the statutory retirement age should be better aligned with increasing life expectancies in Lithuania.

Citation:
COMMISSION STAFF WORKING DOCUMENT on the assessment of the 2014 national reform program and convergence program for Lithuania: http://ec.europa.eu/europe2020/pdf/csr2014/swd2014_lithuania_en.pdf.

Luxembourg

Score 7

Luxembourg's pension plans offer one of the highest replacement rates within the OECD (2012) and provide a high living standard for the elderly. In 1999 Luxembourg started urgent reforms of the social security system that offers a broad scope of services and requires no out-of-pocket expenditure for benefits such as health care. The country's package of services for the elderly (health care insurance and other allowances) is one of the most substantial and generous in the world. The rate of old-age poverty is lower than that for families, and even more so if single-parent families are considered. Pensioners must contribute financially to the health care insurance system, however, and are fully taxed.

In 2012, the country's pension fund comprised a still-growing reserve of 3.8 times annual expenses. Luxembourg's old-age dependency ratio in the private sector was at its most ideal in 2008 with 38.6 pensioners to 100 contributors, yet in 2011 fell to 40.1 pensioners per 100 contributors. For civil servants in 2005 the ratio was 51.6 pensioners per 100 contributors. The public sector, of which 90% is Luxembourg nationals, is suffering from an inevitable ageing effect; furthermore, in this sector wages and pensions are significantly higher than in the private sector.

Luxembourg also offers by far the highest minimal pension benefit with a monthly sum of €1,661.58 as of 2013. In light of the long-term sustainability of such a system, the OECD and the European Commission have urged radical pension system reform. In 2012 the government introduced a number of changes, including a gradual increase in the number of contribution years to 43 to earn the same level of benefits, as well as a reduction in benefits for those who have only contributed to the system for 40 years; indexing pension payments only to inflation rather than to nominal wages, in the event that reserves proved insufficient; and a gradual increase in the rate of pension contributions from 24% to 30% of gross wages and other income. Yet the pension reforms, which came into force on 1 January 2013, are benefiting from the favorable macroeconomic environment. The reforms were based on an estimated GDP growth rate of 3%, which is unlikely to be continued in the future. GDP growth was estimated at 3.2% and employment growth at 1.9% in 2014. Further measures must be taken to guarantee long-term financial stability through 2050.

Citation:
Inspection Générale de la Sécurité Sociale (2013), Rapport general sur la sécurité sociale, Luxembourg: Ministère de la Sécurité sociale
http://www.gouvernement.lu/3680390/cg.pdf
http://www.mf.public.lu/publications/programme/15th_update_stability_growth_programme.pdf
http://www.odc.public.lu/publications/pnr/2013_PNR_Luxembourg_2020_avril_2013.pdf
http://www.oecd.org/fr/luxembourg/47536647.pdf
http://www.oecd.org/eco/surveys/LUX_Overview_Eng%202012.pdf

Poland

Score 7

Poland introduced a three-pillar pension system following World Bank recommendations in 1999. Starting in 2011, pension contributions were partially redirected from the second – obligatory, but private and funded – to newly created subaccounts in the first, public pillar. In addition, the sustainability of the first pillar was improved in 2011 by the adoption of an increase in statutory retirement ages, which will be phased in between 2013 and 2020 (for men) or 2040 (for women). Further changes were adopted in late 2013. By making participation in the second pillar voluntary, and by reducing the share of the pension contribution to be paid to the second pillar, the weight of the second pillar was further reduced. The Treasury and Treasury-guaranteed bonds held by the pension funds in the second pillar were transferred to the social-security administration and converted into future pension claims, thereby substantially reducing the (explicit) public debt. Finally, pension funds were banned from investing in government bonds, but given more scope for holding foreign securities. These reform measures have helped improve the financial situation of the first pillar and have helped reduce the public debt; however, they have been controversial with respect to their constitutionality and their treatment of the property rights associated with second-pillar assets.

Citation:
IMF, 2014: Republic of Poland: Selected Issue. Country Report No. 14/174., Washington, D.C., 59-82 (http://www.imf.org/external/pubs/ft/scr/2014/cr14174.pdf).

Slovenia

Score 7

Slovenia has a traditional pay-as-you-go (PAYG) pension system with modest pensions, whose intergenerational fairness and financial sustainability in face of an aging society has suffered from a low employment rate for the elderly. A substantial pension reform was adopted in December 2012. This instituted a gradual increase in the full-retirement age to 65 for men and woman, or 60 for workers with at least 40 years of pensionable service. In addition, it introduced incentives for people to continue working after qualifying for official retirement, and implemented changes to the pension formula that will slow future pension growth. No further changes were adopted under the Bratušek government.

United States

Score 7

The Social Security retirement system is one leg of the pension system, complementing a private system of company-based saving plans (so-called 401k plans) that receive tax subsidies, and a variety of private retirement accounts. Social Security is funded by mandatory employee and employer contributions, totaling

12.4% of wages, on wages up to $117,000 per year. The wage replacement rate of the public system is on average 45%, below the OECD average, though with higher rates for people with lower incomes. Benefits from company-based and private accounts raise the wage-replacement rate to 80%. However, 78 million Americans have no access to company-based retirement plans. In addition, the financial crisis has hit the asset base of pension funds, resulting in current or future failures to make full payments by many private employers. The Social Security funding shortfall has been politically intractable, with Democrats blocking benefit cuts (including reductions of scheduled benefit increases) and Republicans blocking increases in the payroll tax. Along with the related health-care program for the aged, Medicare, the Social Security retirement program is at the center of the country's long-term fiscal difficulties.

With respect to the three goals of pension systems, the U.S. pension system is partially successful in reducing poverty among the elderly. (The poverty rate among the elderly is high by OECD standards, but not as high as the general U.S. poverty rate.) The system is hard to assess with respect to intergenerational equity. Historically, each succeeding retirement cohort has received generous subsidies from current workers, but the growth of the elderly population threatens coming retirement cohorts with potential losses of expected benefits. The system is currently at risk with respect to financial sustainability.

Austria

Score 6

Within the short term, Austria's pension system is still considered to be reliable and secure. However, the system's ability to respond to demographic changes is open to question. The population is aging and the birth rate declining, yet the logical response – prolonging the period a person has to work before being entitled to a pension – is politically difficult to implement. Austrians still retire early by international comparison; nevertheless some progress has been made in terms of increasing the effective retirement age in the last years.

Thus, while the pension system itself is still considered stable, more efficient responses to the coming demographic changes must be found. Longer life expectancies have not yet found an equivalent in longer periods of working. This represents a significant burden for future generations, as pension expenditures consume a significant amount of government resources, to the disadvantage of the younger generations. According to recent calculations by the Austrian audit court, by 2015 pension payments will consume around 47% of net state tax income. In comparison, state expenditures for schools and universities (primary, secondary and tertiary education) amounted to around 18% of net tax income in 2012. The system therefore largely fails to achieve the objective of intergenerational equity.

The different interests behind the different positions remain the same: Employers and right-of-center parties argue that without a significant increase in the statutory pension age, the outlook for the next generation is dire; labor unions and left-of-center parties argue that individuals who have worked hard for decades should be guaranteed the best-possible quality of life in their later years and without having to work significantly longer.

Belgium

Score 6

Pension policy always has been a touchy issue. Reforms were continuously delayed until the financial crisis hit the country and forced the previous government to initiate a bunch of reforms to restrict early retirement. In comparison to what had been achieved over the last 20 years, this is a major achievement. Yet, the implicit pension debt is much higher than the present public debt with current pension schemes.

Potentially good news is seen in the fact that the previous government called a national conference on pensions. A set of experts and politicians met regularly for more than a year to produce a report on the state of play and make concrete proposals, based on sound research and evidence from other countries. The new government seems keen on implementing a large set of these proposals.

There is, however, a negative aspect to be considered: pension generosity will clearly fall, while minimum pension levels are already very low, producing relatively high poverty rates among the retired. Public pensions are often topped by private pension funds (especially for medium- and high-income categories in the private sector), but the economic crisis has dented their expected returns. Poverty among the retired can thus be expected to increase over the next decades.

Next to this private sector pension system, civil servants benefit from a distinct and more generous system. This system is actuarially too generous, which calls for a tightening there. But tackling that issue has always been politically difficult, and it remains unclear if the new government has the capacity to effectively address that issue.

Chile

Score 6

Chile's pension system combines a redistributive means-tested pillar financed by general taxation with a self-financed pillar based on individual contributions and individual pension accounts, which are managed by private pension fund managers and invested both domestically and abroad. The redistributive pillar was extended and broadened very substantially by a 2008 pension reform that implemented means-tested pension subsidies, guaranteeing a pension floor to all older citizens that is very high relative to the country's minimum and average wages. The reform also provided pension benefit entitlements to women based on the number of children they have had, with no ceiling on the number of children. It is a matter of some debate whether the Chilean pension system guarantees intergenerational equity or prevents poverty caused by old age. It can be argued that both public and private pension systems are fiscally sustainable (like those of Norway, the best-funded system among all OECD countries), and thus provide both intergenerational and intragenerational equity across income groups. Nevertheless, the system largely fails to guarantee poverty prevention among large parts of the socioeconomically weaker and older population who depend on the support of their families or have no pensions at all if they worked in unstable and/or informal employment. Thus, the pension system has (because of the capitalization logic) virtually zero redistributional effect.

Ireland

Score 6

The Irish system of pension provision rests on three pillars: a state old-age pension, occupational pensions and individual pension plans. The substantial proportion of the population that is employed in the public sector enjoys relative generous occupational pension entitlements.

In May 2011, an annual levy of 0.6% was imposed on the value of pension assets. In the 2014 budget, this levy was increased to 0.75%. The proceeds were earmarked to fund a “jobs initiative” program, and applied only to private-sector pension funds. In the 2015 budget, the minister announced that the levy, which was widely regarded as discriminatory and unfair, would be phased out.

Poverty prevention:

The state pension is not income related. It provides €920 a month for a fully qualified individual, regardless of previous earnings, with increases for qualified dependents. This is about one third of average earnings among the employed population. The nominal value of this pension has been held constant since the onset of the crisis, despite the general fall in incomes and a period of falling prices in 2010 – 2011 and again in 2014.

Ireland ranks among Europe’s best – alongside the United Kingdom and the Netherlands – with regard to the size of existing private pension funds relative to GDP. About 55% of the workforce has made some pension provision for their retirement outside the main state scheme. However, these schemes have come under very severe pressure following the stock market crash of 2007 and the fall in annuity rates (which increases the liabilities of these schemes). The trend of a shift from defined-benefit to defined-contribution schemes continued over the review period.

Fiscal sustainability:

The state pension scheme is largely a pay-as-you-go system. Its sustainability depends on the ability of the state to raise the funds required to meet ongoing commitments through taxes and social insurance levies. Although Ireland's population structure is now relatively young, it will age rapidly over the medium term. This has led to repeated predictions of a pension-system crisis unless the retirement age is raised significantly and the amount earmarked for pensions from income taxes and social insurance levies is steadily increased. Pensions for those employed in the public sector were until 2009 almost entirely funded from general tax revenue. Significant changes to the funding of public sector pensions were made in 2009 and in the Public Service Pensions Act, 2012. These will, over time, make the system more sustainable.

Intergenerational equity:

The pension reforms introduced over the past four years will eventually increase the equity of the Irish pensions system across generations. At present, inequities arise because those in the current generation of pensioners who enjoy the state pension or public-sector pensions did not contribute sufficiently through taxation and direct pension contributions to fund the level of pensions they receive. Those now in the workforce are unlikely to enjoy comparable levels of pension when they reach retirement age. Furthermore, although some adjustments have been made to pensions since the crisis of 2008, these have been smaller than the adjustments to the after-tax income of those who are in employment. Finally, Irish pension law gives retired members of defined-benefits schemes priority among the claimants to the schemes' assets. The deficits that have emerged in these schemes imply that active members are contributing to support pensions that exceed what they are likely to actually receive when they reach retirement age. The possibility of changing these provisions has been discussed recently, but no change has yet been made to the program.

Citation:
Data on poverty levels among the retired are from the Survey on Income and Living Conditions,2011 Results: http://www.cso.ie/en/media/csoie/releasespublications/documents/silc/2011/silc_2011.pdf

New Zealand

Score 6

New Zealand's pension system is tax-based. It is relatively efficient, as it prevents poverty in old age with a relatively low level of public spending, measured as a percentage of GDP. The most recent innovation in this area is KiwiSaver, introduced in 2007, a publicly subsidized and private pension plan offered on a voluntary basis. KiwiSaver enjoys broad political support by both the government at the time of writing and the major opposition party. Although introduced by a Labour government, the National-led government has only implemented minor modifications. KiwiSaver is a popular option, and as of September 2014, more than 2,400,000 people had joined the program. In the longer term, however, demographic changes mean that more effort must be made to encourage private savings as part of a strategic plan to address public sector affordability issues and intergenerational equity challenges. The economic downturn and rising unemployment make it a difficult time to encourage further private saving, and yet intergenerational equity and affordability suggest the urgent need to further focus on reforms. The Organization for Economic Cooperation and Development (OECD) has suggested improving fiscal sustainability through the raising of the retirement age, while slowing the pace of growth in benefit payments, and through removing subsidies, especially to high-income members. So far, the government has resisted pressure from some economic and social forecasters, party leaders and media voices to gradually increase the age of pension eligibility from 65 to 67 years; indeed, prior to the 2014 election the Prime Minister threatened to resign rather than adopt a retirement age of 67 years as government policy. One proposal coming from a government support party, United Future, was to encourage a higher retirement age by increasing the pension rate for those retiring at 70, while allowing retirees to take the pension at lower rates from the age of 60.

Citation:
OECD Economic Survey: New Zealand (Paris: OECD 2013).
Joining KiwiSaver, http://www.kiwisaver.govt.nz/statistics/monthly/joining/ (accessed October 13, 2014).

South Korea

Score 6

The average age of South Korea’s population is increasing much faster than in many other OECD countries. The share of the population that is 65 years or older is expected to increase from 7% in 2000 to 37% in 2050. This relatively quick demographic shift is taking place in part because South Korea has been very successful in reducing infant mortality rates and increasing life expectancy, while failing to maintain birth rates near the replacement rate. Since 1996, the fertility rate has dropped from 1.6 babies per woman – just below the OECD average – to 1.2. South Korea now has the lowest birth rate among OECD countries and one of the lowest in the world.

Old age remains a major source of poverty in South Korea, as pension payments are low and most elderly people today lack coverage under a national pension system that did not cover a large share of the workforce until its expansion in 1999. The government has also failed to enforce mandatory participation in the system, while many employers fail to register their employees for participation. Furthermore, most irregular workers and self-employed are not covered by the system.

The national pension system is currently fiscally sustainable and needs only small subsidies. This is because the system is organized in the form of a pension fund and contributors currently far outnumber pension recipients. However, given the risks involved in pension funds, it is not clear what level of subsidies the fund will require once those who entered into the system since 1999 retire. According to the first national pension financial review in 2003, the fund was projected to run out of money by 2047. Growing concerns about the long-term financial sustainability of the pension fund led to a drastic reform in 2007. The earnings replacement rate was reduced from 60% to 50% in 2008 and will be further reduced to 40% by 2028. The government hopes that pay promoting private pension plans can offset this reduction in the national pension benefit. Beginning in 2016, the government will make it mandatory for businesses with 300 or more employees to provide retirement pensions to their employees. This requirement will gradually be extended to all businesses by 2022.

Three older and much smaller pension funds for government employees (insolvent since 2001), military personnel (insolvent since 1973) and teachers (expected to be insolvent from 2033 on) are already running deficits and have to be subsidized by the government. Given the low fertility rate and the aging population, the country's pension funds will almost certainly need more subsidies in the future. Faced with the increasing fiscal burden of relatively generous civil servant pension schemes, Park Geun-hye has been pushing ahead with reform of the government employee pension plan to increase the pension age from 60 to 65 and reduce pension benefits.

South Korea's pension funds are vulnerable to government interference. For example, in 2008 the government told the National Pension Fund to invest a larger share of its assets in South Korean stocks, seeking to stabilize the stock market during the global financial crisis. Its financial sustainability is now hotly debated.

Citation:
Kimm, Seong Sook (2013), Pension Reform Options in Korea,
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OECD, Pensions at a Glance, 2013,
http://www.oecd-ilibrary.org/finance-and-investment/oecd-pensions-at-a-glance_19991363
Government to Promote Private Pension Plans, Ministry of Strategy and Finance, Aug 27, 2014
http://english.mosf.go.kr/pre/view.do?bcd=N0001&seq=3671&bPage=1

Spain

Score 6

Spanish pension policy targets its objectives both through a public pension scheme and by offering favorable tax relief for those enrolled in private pension schemes. It largely achieves the goals of poverty prevention and fiscal sustainability, but only moderately meets standards of intergenerational equity.

The pension system represents the largest single piece of public spending (more than €120,000 million). Despite the cuts suffered in salaries and subsidies as a result of the austerity measures or labor market reform, Spanish pensioners have maintained their purchasing power during the crisis years. Moreover, whereas the poverty rate of the total Spanish population is at 20.5% (and 26.5% among children), the rate among the elderly is only 12.5%. Thus, it seems that poverty prevention among older generations has succeeded and that the elderly are less economically vulnerable than active but unemployed workers or other young inactive people without social benefits.

It cannot be said, however, that the current system ensures equity across generations – pensioners, the active labor force and youth. As a matter of fact, intergenerational equity is not an explicit goal and fair burden-sharing is not explicitly defined. The model (with the exception of those publicly subsidized – through favorable tax treatment - private pension plans) is instead based on the pay-as-you-go methodology in which current contributors to the insurance system pay the expenses for the current generation of recipients. Although there are accumulated reserves and the rights of new retirees have always been respected so far, the model is based on the (doubtful) expectancy that the following generation will be able to cover the necessities of the previous generation. In other words, it is doubtful that Spain will be able to maintain a sufficient employment-population ratio or increase productivity to compensate for societal aging.

These shifting demographics and a longer life expectancy are leading to an unsustainable population pyramid that is worse in Spain than anywhere else in Europe. Combined with the impact of the crisis, these developments have refueled debates over the long-term fiscal sustainability of the Spanish social security system. Pessimistic forecasts show a growing deficit and an increase in the weight of pensions in relation to GDP from 8% in 2005 to 15% in 2050.

Concerned about this problem, the current government has launched a reform (based on a report authored by a consultative committee of experts and implemented through Law 23/2013) which will increase retirement age from 65 to 67 and will render more difficult induced early retirement (an onerous mechanism frequently used in the past). At the same time, the contribution period taken into account to calculate pension amounts will be significantly longer, thus further encouraging Spaniards to complement their public pension plans with private schemes. The most crucial point is the replacement of the pension indexation by a new Pension Revaluation Index (PRI), which uses a formula that implicitly introduces economic growth as a parameter. The PRI may have long-term effects on poverty, but it improves the system's fiscal sustainability and, to some extent, equity. The new system was used for the first time in 2014 for the determination of the 2015 PRI, when contributory pensions are bound to grow by the minimum 0.25% threshold.

Citation:
Independent Authority for Fiscal Responsibility. 2014. Opinion on the determination of the 2015 Pension Revaluation Index. Madrid: AIReF www.airef.es/system/assets/archives/000/000/138/original/Opinion_on_the_determination_of_the_2015_Pension_Revaluation_Index.pdf?1417513934

Bulgaria

Score 5

Bulgaria has a mixed pension system consisting of three pillars: a public pay-as-you-go pillar financed by social-insurance contributions, an obligatory fully funded private-pension-fund pillar and a voluntary third pillar. The second pillar was started in 2002 for people born after 1959, and is not yet paying out many pensions.

While the pension system substantially reduces poverty among the elderly, the poverty rate among senior citizens remains high from a comparative perspective. The Bulgarian pension system also suffers from a lack of intergenerational fairness and fiscal sustainability. Given the present demographic dynamics and the existing system's configuration, both the implicit public-pension debt and the real pension burden will increase significantly over time. These problems have been aggravated by the Oresharski government's decision to terminate the gradual increase in the retirement age originally adopted in 2011.

Croatia

Score 5

Like other East-Central European countries, Croatia introduced a three-pillar pension system with a mandatory second pillar in the late 1990s. The average effective replacement rate for pensions is around 40%, partially due to the fact that many pensioners retire early. As a result, pensioner poverty is rather high in Croatia. The rules for calculating benefits are generally equitable. However, war veterans enjoy strong privileges, and inequalities between cohorts have been introduced through irregular supplements that have reflected the electoral cycle. As a consequence of the aging of the population, the low general employment rate and the decline in the effective retirement age from 61 in 2004 to 59 in 2013, the system is neither fiscally sustainable nor intergenerationally fair. The public pension fund has shown a persistent deficit, which represents a significant risk to the stability of the system. After some dithering, the Milanović government has started to address these problems. The Pension Insurance Act of January 2014 raised the statutory retirement age from 65 to 67 and the early retirement age from 60 to 62. Under the new rules, early retirement cannot be taken without penalty until 41 years of service have been completed, and eligibility begins only at 60 years of age. Moreover, an amendment to the Act on Social Welfare has allowed the continuation of pension payments even if a retiree takes on a part-time job. Pensions under certain "special schemes" that are above a certain threshold have been temporarily cut by 10% and indexed to GDP growth. New rules covering disability pensions have been introduced, and the occupational-rehabilitation system has been changed. Disability-pension beneficiaries must now undergo a compulsory medical assessment every three years, and are subject to random control assessments.

Cyprus

Score 5

Statistics released in September 2014 by the government show significant improvements in some age groups, particularly in those over 65, the demographic that used to be at highest risk of poverty in Cyprus and had the EU's lowest relative median income. Changes to various benefits schemes between 2012 and 2014 were expected to modify the ratio of pensions expenditure to GDP, which was the EU-27's second-lowest until 2012. However, the broad variety of pension programs and rules means that some groups, such as public employees, may be in a better position than others. The public-service pension system provides for different retirement ages for employees in various sectors. Debate is underway on prospective changes to employer-based and social-insurance pensions, as well as on a gratuity that employees of the public sector receive upon retirement. Private-sector workers typically have access only to the government social-insurance program, as well as private-sector provident funds in some cases. A number of funds were drastically affected by the bail-in of 2013, but mismanagement has also taken a toll. The social-insurance scheme, which has not been able to offer an adequate, secure or sustainable pension income, is also being reformed with regard to retirement age, contributions and more.

The guaranteed minimum income (GMI) scheme and special allowances have offered some remedy for the economic crisis' worst ills, and have compensated for benefits and pensions cuts affecting vulnerable groups. Pensioners are expected to benefit significantly from the GMI, in particular people living alone, a category that includes more women than men.

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1. http://www.socialwatch.eu/wcm/Cyprus.html
2. The Cypriot Pension System: Issues and Reform Options -Alejandro Sergio Simone- International Monetary Fund- Cyprus Economic Policy Review, Vol. 5, No. 2, pp. 3-34 (2011)
3. http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=tps00103&plugin=1
4. At Risk of Poverty Statistics 2008-2013, Cyprus Statistics Service, 2014, http://www.mof.gov.cy/mof/cystat/statistics.nsf/All/FC36371E3D9CE0B4C2257893002FF33A/$file/EUSILC-POVERTY-A2008_13-EL-160914.xls?OpenElement (in Greek)

France

Score 5

The French pension system is relatively generous, and largely prevents poverty of the elderly. But it is also complex, which is a problem for equity: First, the so-called general regime applies to all private employees and is complemented by additional voluntary systems, in particular in large companies. Second, some professions are affiliated to "special regimes" which are characterized by shorter periods of contribution and higher generosity in pension payments. These systems usually cover employees working in public companies or groups highly subsidized by the public budget (coal mines, public transport, sailors and fishermen, for example). Finally, public servants usually benefit from higher payments as their pension payments are based on a final salary, and not on an average. Early retirement is a common practice, and despite of the raising of the retirement age to 62 years, the average age of entry into pension is 58.

In order to meet the (mainly) demographic challenges and to assure the sustainability of the pension system, French governments have tried to introduce reforms on several fronts over the last 10 years, usually against fierce opposition: an increase in pension contributions; an increase in the number of years of contribution, to 43 years; and in 2008, a reduction of peculiarities or privileges granted to "special regimes." These reforms are bound to create social problems for the younger generations, who are penalized by their late entry in the labor market, their unstable job careers and the necessity to contribute for a longer period of time. At the same time, deficits in the system continue. The Socialist Party (PS), which had opposed limited reforms under the Sarkozy administration, are now forced to face drastic changes to improve the sustainability of the pension system. It is important to note that France's pension system is entirely publically run, and there are practically no pension funds except for a few limited exceptions. Furthermore, the Socialists who had fought fiercely against the rise of the pension age had to find an excuse for swallowing it when coming to power. They have introduced the concept of "penibility", a very complex and bureaucratic mechanism allowing workers to go to pension at 60 if they fill the criteria and measures set up for every industrial or service sector. The consequence of this new mechanism is twofold in addition to its costs: it introduces further uncertainty about the actual pension age and puts in place a highly complex and cumbersome system of measurement of penibility.

Germany

Score 5

Germany has engaged in a significant number of pension reforms in recent decades. All these reforms have improved the long-term sustainability of the pension system, leaving it in a favorable condition when compared to some other European countries. While German pensioners today have a low risk of poverty, projections indicate that this risk will grow over the coming decades as a result of previous reforms.

Far-reaching pension reforms were adopted by the new government in 2014 which have reversed the course of previous reforms (which had managed to preserve the pay-as-you-go system). The recent reforms were hotly disputed, with critics claiming they would undermine the long-term sustainability of the pensions system, lead to higher social security contributions, and burden younger generations and business with higher financial costs.

First, the government reduced the retirement age from 65 to 63 for workers who have contributed to the pension system for at least 45 years. This allows workers to retire at 61, registering as unemployed for two years and then drawing a full pension at 63. Second, it provided a catch up for housewives with children born before 1992 relative to those with children born after 1992. An additional pension point will be added to the former group, which now can claim two points (instead of one), while the latter group can claim three. Finally, pensions for invalids were improved. The calculation will now include two additional years of (fictive) contributions. All in all, the costs of these reforms will amount to approximately €160 billion by 2030. Public subsidies for the pension fund will increase from €400 million to €2 billion euros in 2022.

The reforms go against the measures undertaken in recent decades to raise the participation rate of older workers, reduce early retirement, moderate the increase of the contribution rate and balance the pay-as-you-go system for the future.

Citation:
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http://www.deutsche-rentenversicherung.de/Rheinland/de/Inhalt/5_Services/05_Fachin¬forma-tionen/00_rundschreiben_/2014/4_2014.html.

Italy

Score 5

The Monti government introduced a key sustainability-oriented reform of Italy's pension policy by increasing the retirment age to 67 years and by reducing benefit levels for higher income groups. Thanks to this reform, no further major reforms of the retirement system will be needed in the next few years – despite the demographic imbalance between the aged and the young. The current situation, however, is less positive from the point of view of intergenerational fairness, as the younger generations will receive smaller amounts upon retirement. This problem is exacerbated by the late entry into the labor force of younger cohorts, which itself is a consequence of the economic crisis. In addition, the growing number of permanently unemployed also face receiving little to none in terms of a pension. The high percentage of public spending on pensions also diverts financial resources from other welfare policies such as family policy. Ensuring pensions comes with high costs for the rest of society.

The problem of poverty prevention which exists today for a relatively limited share of the population will be much more significant and relevant for the young cohorts of today when they reach retirement age.

Supplementary pension schemes have to date played only a minimal role in the pension system and fiscal policies adopted to encourage them have not been sufficiently bold.

Japan

Score 5

Given the rapid aging of the population, Japan's pension system faces critical challenges. The last major overhaul was based on 2004 legislation and became effective in 2006. Under its provisions, future pension disbursements will rise less than inflation, payments (after an intermediate period) will commence at age 65 instead of age 60, contributions will top out at 18.3% of income, and a payout ratio of 50% is promised. However, the program’s assumed relationship between future payment levels, contributions and the starting age for receiving benefits is based on optimistic macroeconomic forecasts. After the global financial crisis, these assumptions seem increasingly unrealistic, and further reforms are needed. According to the mid-2014 estimates of the Ministry of Health, Labor and Welfare (arguably based on somewhat optimistic assumptions), the payout ratio will drop to 50.6% in 2043 and stay around that level.

The LDP-led government that assumed office in late 2012 has focused on reforms improving industrial competitiveness. In its 2014 Revitalization Program, it proposed to shift the asset portfolio of the Government Pension Investment Fund somewhat away from bonds (and from Japanese Government Bonds (JGBs) in particular) towards other assets like stocks. Some legal prerequisites for organizational changes are still lacking. While the government reasons this will allow for increased profitability and hopes for a positive effect on the stock market, many observers are concerned about the higher risks involved. However, whether the current emphasis on JGBs is indeed so much less risky may also be questioned.

Japan has a higher-than-average old-age poverty rate, although the previous pension reform contributed to reducing this gap. Intergenerational equity is considered to be an understudied topic among Japanese reformers, although it is recognized that declining birth rates will create new problems for the 2004 reform.

Citation:
Kenichiro Kashiwase et al., Pension Reforms in Japan, IMF Working Paper WP/12/285, 2012

The Japan Times, Public pension reforms, Editorial, 06.06.2014, http://www.japantimes.co.jp/opinion/2014/06/06/editorials/public-pension-reforms/#.VFJTlhY-etE

Malta

Score 5

Pensions represent 21.5% of GDP, with the figure projected to rise by some 10 percentage points over the next 50 years. The debate over pension reform started 12 years ago, but until recently, the only concrete step to have been taken was an increase in the age of pension entitlement from 61 to 65. The EU believes that sustainability cannot be achieved overall unless the retirement age is raised to a still-higher level. According to a report from the National Statistics Office, half the money spent on social expenditures goes toward old-age pensions. Of the other 27 EU member states, only Italy and Poland spend more on pensions.

The Maltese pension system could be described as an exclusive form of public pensions. It is based on a pay-as-you-earn system, as well as a means-tested non-contributory system. Until recently pensions were not linked to inflation, and considerable erosion in real value had been allowed to occur over the years.

Although partially rectified, the real value of pensions cannot make up for decades of loss. Furthermore, given the low tax ceiling, pensioners were required to pay some income tax on their pensions, thereby suffering a further erosion of value. The 2013 budget raised the tax ceiling, which will go some way to help to redress this situation, as will the revision of supplementary assistance for those aged 65 and older, in cases where household income falls below the risk-of-poverty threshold.

The parliament recently voted to introduce a third pillar to the pension system, and to provide fiscal incentives to encourage people to invest in private-sector pension schemes. As occupational pension schemes are also mandatory, it will be some time before this third-pillar reform will in fact reduce stress on pension expenditures.

Citation:
http://www.oecd.org/countries/malta /43469300.pdf
http://www.academia. edu/360125/Welfare_Regimes_Explorin g_the_Maltese_Social_Policy_Model
National Strategy Report on Pensions, Malta 2005
Borg Betrand, Pension Trap for those over 37. Times of Malta 30/05/12
Third Pillar Pensions: A First Step Times of Malta 4/12/14
Addressing the Pensions Dilemma Times of Malta 17/10/14

Mexico

Score 5

Mexico is slowly shifting from a pensions system based on contributions and corporate identity to one that is more universalistic in character, operated by government-approved financial agencies called Afores. Some Mexican states have in recent years introduced noncontributory old-age pensions based on universal eligibility. A pension reform plan is now underway to introduce a universal old age pension for Mexicans over the age of 65. Mexico is in a relatively advantageous position to introduce reform in that its birth rate peaked in the 1970s, which has led to a reduction in children’s demands on the public sector. At the other end of the demographic balance, Mexico still has a relatively low proportion of old people. As a result, Mexico’s dependent population is fairly low. This happy position will eventually change for the worse. More substantial reforms will be needed as the population ages and the current system – while improving – might not be robust enough in the future to cope with an older population. Historically, Mexico’s pensions policy has been based on the principle of contributions, which has not provided adequate, or any, safety net for the elderly poor. However, some parts of Mexico, notably the capital district, now have a limited old-age pension system based on a universal entitlement.

Slovakia

Score 5

Slovakia introduced a three-pillar pension system along World Bank lines in 2004. In 2012, the Fico government adopted a number of measures aimed at strengthening the first (public, pay-as-you-go) system to the detriment of the relatively strong second (private, fully funded) pillar. First, it changed the distribution of the pension contribution from an even nine percentage points each for the first and second pillars to 14 percentage points for the first pillar and only 4 percentage points for the second. Secondly, it "opened" the second pillar by allowing people to enter or leave it between September 2012 and January 2013. Finally, it replaced the compulsory membership of school graduates in the second pillar with the voluntary entry of citizens under 35. In addition to this rebalancing of the pillars, the government changed the rules for the investment of private pension funds and increased the contribution rates for self-employed people. These changes have once again increased the role of the state in providing for the elderly, and have given the pension system a more redistributive nature. While the reforms have improved the public pension program's financial situation, the expected increase in public pension spending through 2060 is still much higher than the EU-27 average. In the period under review, the Fico government did little to address this problem.

Citation:
European Commission, Assessment of the 2014 national reform and stability programme for Slovakia, COM 2014/426 final, 2.6.2014; http://ec.europa.eu/europe2020/pdf/csr2014/swd2014_slovakia_en.pdf.

Turkey

Score 5

Turkey's social security and general health insurance law, passed in 2006 and implemented in October 2008, radically reformed the country's previous pension and health system. The reforms put an end to the unequal, corporatist character and fragmented structure of the previous system and made the Social Security Institution responsible for managing provisions. With the new changes, the state began to contribute to the system, in addition to employers and employees. The new law specifically set out to cover all social groups, including individuals not formally employed, and guarantees equal access to health care. In addition, those under 18 years of age are covered by health insurance without having to pay premiums. The 2008 reform adjusted pension rules by gradually increasing the retirement age and contribution period, and reducing the accrual rate.

The 2008 social-security reform improved the coverage provided by public pensions, and is expected to yield significant savings, but these are insufficient to ensure pension-system balance over the long term. The World Bank notes that pension spending in Turkey, at around 7% of GDP, is still modest in comparison to high-income OECD countries. This reflects the relatively young population, and the fact that due to the system's high dependency ratio and generous eligibility rules (including early retirement and low minimum years of service), more than half the country's pension spending is financed through budget transfers. The 2008 reform adjusted pension parameters, gradually increasing the retirement age and contribution period, and reducing the accrual rate. But these adjustments will be phased in over a period of several decades, too slowly to counter the effects of expanded coverage and a maturing population. For this reason, pension-system deficits are expected to remain around 3% of GDP until the middle of the century. In 2013, new pension reforms sought to address some of these issues. Reforms included the introduction of government-matching contributions and a shift from defined-benefit plans to defined-contribution plans.

Under the new pension law, which came into force on 1 January 2013, the government matches 25% of individual contributions up to a gross monthly salary of around EUR 410. Participants will gain access to government contributions through a gradual vesting system – 15% after the first three years, 35% after six years, 60% after 10 years and 100% at retirement at the age of 56. The reform was aimed at widening system coverage and making the system more progressive, and could be an important step in making pensions far more attractive.

Citation:
Turkish Statistical Institute, 'Elderly Statistics, 2013', 19 March 2014, http://www.turkstat.gov.tr/PreHaberBultenleri.do?id=16057 (accessed 6 December 2014)
World Bank (2014) "World Bank Group - Turkey Partnership - Country Program Snapshot, Washington D.C.

Greece

Score 4

The Greek pension system is a pay-as-you-go corporatist system, based on a multitude of occupational pension funds (there were approximately 60 pension funds in 2013). In April 2013, it was announced that by the end of 2014, the Greek government planned to merge all pension funds and arrive at a system of only four funds for salaried employees (including the private and the public sector), self-employed (including so-called liberal professions requiring specialized education such as lawyers, doctors and accountants), farmers and persons employed in commercial shipping (ship crews). To date, this reform plan has not been implemented.

Greek pension policy does not successfully prevent poverty among the elderly because the majority of pensioners receive only the minimum pension. According to the World Bank, 14.5% of Greek senior citizens are relatively poor. Greece therefore ranks among the five European countries with the worst ratios of poverty for senior citizens. Women are included among the poorest of pensioners if they rely on a very low-level non-contributory pension.

Pension policy also does not meet intergenerational equity requirements. In response to rising pension spending which threatened to derail fisal policy, successive governments from 1990 through 2010 attempted but failed to reform the pension system. Unions in favor of existing arrangements that primarily served the interests of middle- and old-age groups at the expense of younger generations of workers successfully mobilized to block such reform attempts.

Greece's pension system is financially unsustainable. Reasons for this include high replacement rates, early retirement opportunities (in particular for married women with under-age children and public sector workers) and low insurance contributions. It is telling that in 2011, fewer than 40% of Greeks aged 55 to 64 were still working. The Greek dependency ratio is among the worst in Europe, on a par with Sweden, Germany and Italy, which all have better organized welfare states.

As Eurostat data shows, expenditure on pensions jumped from 13.5% of GDP in 2009 to 17.5% in 2012 (the highest level in the EU-28). The continuous decline of Greece's GDP during a recession stretching over five years (2008-2012) accounts in part for this increase. However, it can also be explained by the increased outflow of middle- and old-age employees who – driven by the fear that the longer they stay in employment, the greater the chance that their pension rights are reformed for the worse – have retired as soon as permitted.

After the crisis broke out, pension reform involved lowering replacement levels, raising contributions, preventing early retirement and merging dozens of small social insurance funds into a few larger ones.

When fiscal consolidation was achieved in 2013, it was hoped that the system would become sustainable. However, a decline in social security contributions, which resulted from growing unemployment combined with lowered salaries and wages from 2010 to 2014, means that the system, if it has stabilized, has done so at a low level with diminished social security contributions and benefits.

Citation:
Eurostat data on government expenditure on pensions is available at

http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=tps00103&plugin=0

Hungary

Score 4

Hungary introduced a three-pillar pension system along World Bank guidelines in 1997, featuring a strong mandatory second pillar. Upon coming to office, the second Orbán government abolished this second pillar. In order to improve the fiscal situation and the sustainability of the pension system, it also eliminated some early-retirement options. The elimination of the pension system's second pillar and the limitations on early retirement strongly increased uncertainty regarding income in old age. The Orbán government failed to address these issues during the period under review.

Latvia

Score 4

The state pension system guarantees a monthly minimum pension. The of the monthly pension is dependent on the of service, but is at least equal to or larger than the state social security benefit of €70, though less than half the monthly minimum wage of €320 (as of January 2014). However, where the amount of an individual's monthly pension is below the minimum wage, the recipient qualifies for public assistance. The average monthly pension in 2013 was €264. According to the Central Statistics Bureau, the at-risk-of-poverty rate for retired individuals has increased from 11% 2011 to 16% in 2012.

The introduction of a three pillar pension system has increased the system's fiscal sustainability and inter-generational equity. The three pillars consist of a compulsory state pension scheme (also known as a notional defined contribution system), a state-run mandatory funded pension scheme and a private voluntary pension scheme.

The European Commission Fiscal Sustainability Report 2012 concluded that the notional defined contribution system had low sustainability risks, given its expected reliance on funds raised through the second pillar. Initial projections that the pre-crisis contribution rate of 6% would be quickly restored are looking overly optimistic. . In 2014, the rate was only 4% and a further delay of the reintroduction of the 6% rate until 2016 is expected.

Citation:
1. European Commission (2012), Fiscal Sustainability Report, Available at: http://ec.europa.eu/economy_finance/publications/european_economy/2012/pdf/ee-2012-8_en.pdf, Last assessed: 20.05.2013.

2. Central Statistical Bureau, Database, Available at: http://data.csb.gov.lv

Portugal

Score 4

The pension program has been one of the most closely scrutinized aspects of government policy since the 2011 bailout, and has been one of the main areas in which the government has sought to reduce public expenditure. To that end, a number of cuts and modifications were enacted, and remained in place during the assessment period.

While these cuts have hit the highest pension-drawers especially hard, they have also affected poorer pensioners – undermining the goal of preventing poverty among the elderly. A study indicated that in 2010 – 2011, three out of four pensioners in Portugal received a pension of €500 or less per month, and that the risk of poverty among the elderly is higher in Portugal than elsewhere in the European Union. This statistic was likely aggravated by subsequent cuts in pensions. However, the 2015 budget unveiled in October 2014 partially alleviates some of these cuts, especially for lower pensions, although it is as yet far from undoing all the cuts of the bailout period.

The government has also sought to bolster the pension system's fiscal sustainability. To that end, the retirement age was increased from 65 to 66 years beginning in 2014, and is expected to remain there through 2015. From 2015 on, the retirement age will increase every year depending on the evolution of average life expectancy. Thus, it is expected to increase by two months in 2016. However, as per the previous report, the diminishing population – as both birth and immigration rates fall – is putting additional pressure on the social security system.

Citation:
Notícias CGA (Caixa Geral de Aposentações) - orgão da administração pública que gere as pensões.

Romania

Score 4

In Romania, low fertility rates combined with the massive outmigration of working-age citizens have contributed to a rapidly aging population. Forecasts for 2050 predict that 43% of the population will be over the age of 65 – a dramatic increase from the comparable figure of 27% in 2011. These demographic pressures, combined with a gradual lowering of the pension age and the widespread recourse to early retirement after 1990, threaten to undermine the pension system's sustainability.

In an economy susceptible to sudden upheavals, the fragility of the pension system exposes different strata of the population to the twin phenomena of poverty and insecurity. The situation is particularly dire in the agricultural sector, where workers of the former agricultural cooperatives were left with very low pensions following the dissolution of these cooperatives after 1990. As a result, many retirees live below or near the poverty limit, and many more rely on support from relatives to supplement their pensions. In part due to their lower pension-eligibility age, women typically have considerably lower pensions than men, and therefore have double the poverty-risk rates.

The inconsistencies of pension policy, the volatile budgetary and economic situation, and the country's low employment rates have combined to severely undermine the pension system's overall fiscal sustainability. Fiscal imbalances will be exacerbated at least in the short term by a January 2013 parliamentary decision to raise pensions, bringing the total pension budget up to €11.5 billion. However, this politically highly popular move will be accompanied by a rise in the retirement age for women to 60 years and for men to 65, which should help with longer-term sustainability.

Pensions will increase by 5% in 2015, with the minimum pension reaching RON 400, and the state's overall disbursement totaling EUR 613 million. These funds are contained in the 2015 draft budget, and will be balanced partially by lower expenses on goods and services and more effective VAT collection. According to the Romanian Pension Funds' Association (APAPR), private-pension funds were managing 30% more money in 2014 than they did in the previous year.

Citation:
European Commission (2014) Assessment of the 2014 national reform programme and convergence programme for ROMANIA http://ec.europa.eu/europe2020/pdf/csr2014/swd2014_romania_en.pdf Accessed [23/12/14]

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