SGI Sustainable Governance Indicators

2014 Pensions Report

Pension Policy

BertelsmannStiftung

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 economic 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 conditions. Swiss politicians did initiate a discussion of pension reform some years ago, but were unable to reach a compromise supported by a majority of the country's political forces. At the time of writing, policymakers were discussing proposals for reforming various elements of the pension system simultaneously, allowing for the partial compensation of losers by providing them with gains in other areas.

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.

Australia

Score 9

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 to reduce poverty. However, the negative consequence of the means tests is that pensioners tend to be either affluent or relatively poor. Currently, the Age Pension is still the dominant source of income for retirees, but over time the balance will shift to the private pension system, which was only introduced on a wide scale in 1992, and has only had the current minimum 9% contribution rate since 2002. 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. The mean-tested element of the pension was also tightened for unearned income, but for employment earnings it was relaxed to encourage employment participation of retirees. The pension rate was also increased for single pensioners, for whom the pension was increased from 25% to 27.7% of average male earnings. A new pensioner cost of living index was also announced to preserve the real value of the age pension.

In terms of intergenerational inequity, the gradual nature of the shift since 1992 from a pay-as-you-go public pension towards 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, the changes to the Age Pension announced in 2009 and 2010 had the effect of giving more money to fewer people, thus simultaneously enhancing the financial sustainability of the pension while improving its ability to prevent poverty. While reliance on the Age Pension will continue to be high for many years into the future, in broad terms the pension system is highly sustainable, with private pensions increasingly taking on more of the financial burden. This trend is expected to continue with a further increase in the minimum rate of pension contribution, which will gradually rise by 0.25% per year from July 2013 to July 2019, when it will reach 12%. Overall, the government has demonstrated a sustainable outlook on retirement income, encouraging employer and voluntary pension arrangements in order to minimize the costs to the taxpayer.

Denmark

Score 9

The pension policy in Denmark is well-diversified with regard to 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% for most employees. As for the third pillar, in Denmark additional private pensions schemes are available through insurance companies, pensions fund and banks.

In Denmark, pension savings are tax subsidized. The return is taxed at 15%, which is below the normal capital income tax rate (33%). Moreover, contributions are deductible in taxable income, while pensions are taxable income. However, for most the tax rate that applies to the deduction when one is working is higher than the one that applying when a pensioner is not working, due to progressive elements in taxation, and hence the subsidy. 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.

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.

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.

While the 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 reflects the effects of the early-retirement scheme. The scheme is much debated and politically controversial. The scheme has been reformed a number of times and now includes incentives to delay retirement until age 62. The most recent reform will result in an increase in the earlier retirement age, and a reduction in the early retirement period from five to three years.

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 2019–2023, and the statutory pension age by two years over the period 2024–2027. After these transitions periods, the statutory ages are linked to longevity via an indexation mechanism targeting an average retirement period of 19.5 years. 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.

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. Still, the aging of Finland's population creates problems in terms of labor-force maintenance and fiscal capability, and the ongoing economic crisis in Europe has added considerably to these problems. A reform of the pensions system in 2004 – 2005 aimed for a more flexible pension policy and for the creation of incentives to keep older workers employed. While these reforms were successful, recent government attempts to raise further the retirement age has met considerable opposition from political and labor market organization forces, and has so far (at the time of writing) failed. Since flexible retirement often promotes later retirement and thereby add to system adequacy as well as sustainability, these developments give cause for concern.

Citation:
Nicholas Barr, "The Pension System in Finland: Adequacy, Sustainability and Systems Design", Finnish Centre for Pensions, Helsinki 2011.

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.

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. In 2012, the federal government increased the age for receipt of full OAS benefits from 65 to 67, with a phase-in period starting in 2023. This measure will add to the fiscal sustainability of the OAS.

Czech Republic

Score 8

The Czech pension system has developed from a gradual and partial reform of the structure that existed before 1989. The average state pension in 2010 was 52% of average earnings, and 95% of all pension payments are covered by the state. This system is reasonably equitable and will be financially sustainable for some years with a dependency ratio currently at 21.5%. Long-term sustainability can be achieved by gradually increasing the retirement age. This is relatively uncontroversial. As of 30 September 2013 a new age limit for retirement and the duration of insurance was set up. The aim was to equalize the retirement age for men and women at 67 years, and establish the minimum insurance length at 35 years after 2018. The government has made further changes which came into force in January 2013, aimed at diversifying funding within a two-pillar scheme. The second pillar includes a voluntary private element. Entering the new pillar of the pension scheme is voluntary but irreversible. Only citizens under 35 years of age can enter the new scheme at any time; however, older citizens need to opt-in in the first half of 2013 only. General interest in participating in the new scheme has been very low. It was highest in the 35–44 age group, where 8% opted for the voluntary contributions. Deep skepticism was expressed about this scheme by some members of the expert commission that advised on it, by opposition and governing political parties and by international agencies. Some major private pension companies have opted out on the grounds that financial returns for them are likely to be small and that the system may be changed by a future government.

Netherlands

Score 8

Since 2007 pension age has incrementally increased from 61.0 to 63.7 in 2012, in which year 75,000 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 the recovery 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. Bills for strengthening the governance of pension funds (pensioners in the government board, oversight commissions, comparative monitoring) are being prepared.

Citation:
Ministerie van Sociale Zaken en Werkgelegenheid (2012), 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)

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, with regard to equity in the system, 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 struggles with a comparatively high degree of poverty among the elderly. While the respective rate has been significantly reduced over the last 15 to 20 years, 14% to 16% of UK pensioners were considered to be at risk of poverty in 2010. This demographic trend threatens to worsen in the future, unless policy action to the contrary is taken soon.

The overall figures cover huge 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 very 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). So far, the government has been unwilling to tackle this issue and has committed itself to maintaining pensioner benefits.

The United Kingdom has a three pillar system in which the second (employer) 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 big effect on the incomes of those already retired. In addition, young men who were among the long-term unemployed during the 1980s now find themselves reflected in the pension system. New entrants into private pension schemes are being offered less attractive terms than their predecessors. The Pensions Act 2010 raised the state pension age 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.

Chile

Score 7

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.

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 exists (third pillar), but they has remained quite marginal in terms of coverage and assets.

Poverty among the elderly is modest compared to many EU countries, and has decreased even further in recent years. However, the situation is not entirely without problems. First, a significant increase in poverty among elderly in 2011 – 2012 occurred because the level of wages and salaries that rose sharply during the economic boom in 2007 – 2008 came down. Thus, the working population is less wealthy today. Second, old age pensions are quite low (€334 in 2013) and the average increase in 2011 – 2012 composed just 0.2%, which clearly underperforms inflation (about 4% to 5% per year). Thus, although elderly people do quite well compared to some other social groups, they still have to struggle to make ends met.

The modest living standard of current pensioners is part of the price that the country is paying in order to secure financial stability of the pension system. Current pension payments comprise 6.5% to 6.6% of GDP and contributions roughly 5.5%. Thus, the annual deficit of public pension insurance is about 1% of GDP, and according to the forecast this remains at that level for coming 10-20 years. However, there are some demographic and labor market factors that may increase the risk of debt. Increasing life expectancy and low birth rates worsen the dependency ratio and the current measure aimed at postponing retirement will be insufficient. Thus, Estonia faces the challenge of how to implement new mechanisms that allow for an aging demographic without endangering the three pillar structure.

Citation:
Analysis on Possibilites of Sustainable Financing of Social Insurance. (in Estonian) http://www.praxis.ee/fileadmin/tarm o/Projektid/Tervishoid/Eesti_sotisa alkindlustussuesteemi_jaetkusuutlik u_rahastamise_voimalused_luehiversi oon.pdf

Germany

Score 7

Germany has engaged in a significant number of pension reforms in recent decades. All these reforms have improved the long-run sustainability of the pension system, leaving it in a favorable condition compared to systems in France or the southern European countries, for example. However, given the increasing political power of pensioners, the long-term nature of this success cannot be guaranteed. During the period under review, age-related poverty was identified as an important area requiring additional reform. While German pensioners have a low risk of poverty today, projections indicate that this risk will grow over the coming decades.

Seeking to address this challenge, Minister for Social Affairs Ursula von der Leyen introduced a proposal in August 2012 that aimed at reducing poverty among elderly citizens. It was intended to create a supplementary pension that would increase pension benefits for those with minimal pensions to a maximum level of €850 a month. This proposal met with considerable opposition from within the ministers' own party, partly because it was deemed insufficient to the problem. The obstacles to obtaining a supplementary pension under the proposal were high. Benefit recipients would have to be insured for 45 years, including training or unemployment periods, and would have to have contributed to the pension system for 35 years. Additionally, recipients would be required to have made private supplemental provisions. Ultimately, the proposal was not passed, meaning the problem still needs to be tackled in the coming legislative period.

Due to differences of about 15% in per-capita income, average pensions in the former East Germany differed by 11% from those granted for the same performance in the former West Germany in 2009. This uneven treatment has been an issue ever since reunification, particularly due to the observed levels of poverty among the elderly. In their 2009 coalition agreement, the Christian Democratic Union (CDU), Christian Social Union (CSU) and Free Democratic Party (FDP) promised to align pension levels in the former East and West. However, this task had not been implemented by the end of the period under review.

The question of whether the country's pension system puts an unacceptable burden onto the younger generation is controversial. A double burden on the younger generation in an era of falling fertility is unavoidable. Even today, the country's the old-age dependency ratio is the second-highest in the European Union at 31.2%. This is expected to rise to nearly 60% by 2060. However, previous reforms (mainly sustainability-oriented measures such as the increase in the retirement age to 67) have made the pension system quite robust with respect to withstanding demographic and economic changes and containing costs.

Iceland

Score 7

Iceland's pension policy is partly based on a tax-financed, means-tested public social-security program, and partly on occupational pension funds and voluntary savings encouraged through the provision of tax incentives. The pension funds, which feature employee contributions of 4% of total wages and an employer contribution of 8% of wages, are aimed at giving retirees a pension equivalent to 56% of their average working-life wages. Employees can opt to pay a further 4% of their wages, with a 2% employer contribution, 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, the economic collapse caused heavy losses for most if not all of the country's pension funds, as they had invested in the stock of Icelandic banks that collapsed in 2008, as well as in additional companies that went bankrupt. These losses, overall totaling about a third of GDP, have caused most pension funds to cut payments to their members, imposing a further reduction in the living standards of the elderly. That said, the pension funds have made significant strides following their 2008 losses, and still 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 (LSR), the largest pension fund, has a huge unfunded gap that the state will have to finance through future tax revenue. Second, politicians have a history of raiding the pension funds, as if they believed the funds to have a social responsibility beyond that of providing pensions. Thus, there is a pending danger that the pension funds will be induced to bring part of their foreign exchange holdings to Iceland in order to relieve the balance-of-payments problems that have faced Iceland following the crash.

Citation:
ÓlafurÍsleifsson (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 has embarked on several reforms to its pension policy, profoundly changing the pension system with respect to employer-based pensions and the national insurance. These changes have had great influence, across all relevant dimensions.

With respect to poverty prevention, the reforms introduced a new defined-benefit (DC) pension plan, with contributions invested in the capital market instead of in government bonds. In so doing, the comprehensive reform transformed a system of significantly underfunded pension funds driven by collective bargaining into a system of mainly individual defined-contribution accounts with various levels of collective risk sharing. However, these actions in large part saw the government renounce responsibility by imposing transferring liability to the individual level.

Beginning in 2008, according to an agreement signed by the New Histadrut trade union and the Coordination Office of the Economic Organizations, the Pension for Every Worker process went into effect. Once approved by the government, every salaried worker in the economy became entitled to participate in pension set-asides jointly carried out by employees and employers.

Moreover, at the end of 2008, the Israeli government implemented a reform that introduced a requirement for life-cycle strategies in pension savings products. According to the reform, various investment tracks with age-based investment profiles would be established, serving as default options for savers who failed to make an investment choice on their own initiative. However, under the reforms, the new pension system is regulated rather than operated by the state. The system is therefore subjected to free-market rules; though by law, every worker is entitled to a pension, private pension funds can decide who to accept.

As pension assets are now held by external management entities, they are supervised and regulated by not managed by the state itself. Furthermore, in the last two years, Israel has increased the legal maximum for insurance contributions (including that for pension insurance), with the aim of improving fiscal stability. Thus, it appears that the system as it stands today is fiscally sustainable.

Citation:
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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, 30% of all people over 65 are at risk of poverty. 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 precrisis levels as of 1 January 2012.

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%.

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%. Although 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, 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.

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. Luxembourg in 1999 started a program of health care insurance (assurance dépendance) that offers a broad scope of services and requires no out-of-pocket expenses. 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. Old-age poverty is lower than that of 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 2012 reforms were seen as insufficient as the plan was based on GDP growth of 3% and employment growth of 1.5%. The OECD has argued that more substantive reform is necessary, and that incentives to retire early should be abolished.

Citation:
Hartmann-Hirsch, C. (2010), The State of the Luxembourg's Welfare State: the Effects of the Crisis on a Corporatist Model Shifting to a Universalistic Model. Working paper no. 2010-44: http://www.statistiques.public.lu/cataloque-publications/workingpapers-CEPS/2010/44-2010.pdf
OECD (2010), Economic Survey of Luxembourg: http://www.odc.public.lu/actualites/2010/05/Rapport_OCDE_2010/Policy_brief_2010_EN.pdf
OECD (2012), Economic survey of Luxembourg: http://www.oecd.org/eco/surveys/LUX_Overview_Eng%202012.pdf
Pension reform: http://www.gouvernement.lu/dossiers/social_emploi/reforme-systeme-pension/
Inspection Générale de la Sécurité Sociale (2012), Rapport general sur la sécurité sociale, Luxembourg: Ministère de la Sécurité sociale
Luxembourg (2020), Programme national de réforme du Grand-Duché de Luxembourg dans le cadre du semestre européen 2013: http://www.odc.public.lu/publications/pnr/2013_PNR_Luxembourg_2020_avril_2013.pdf

Poland

Score 7

Pension policy featured prominently in Prime Minister Tusk's 2011 State of the Nation address. Despite massive protests, the government in May adopted a gradual increase in the retirement age from 65 years to 67 years until 2020 for men and from 60 years to 67 years until 2040 for women. In 2013, the retirement age will start to increase, by three months per year. In contrast, the government only partly succeeded in limiting pension privileges of the military and of judges, and postponed the announced reforms of the social insurance system for farmers (Kasa Rolniczego Ubezpieczenia Społecznego, KRUS). The increase in the retirement age has made the Polish pension system more sustainable. After the temporary redirection of 5% of an individual's gross salary from the mandatory but private second pension pillar to the first pillar that went into effect in May 2011, the debate over the future of the second pillar still looms. Statements by various government officials, most notably Finance Minister Jacek Rostowski, have increased uncertainty over the pension scheme and over old age income.

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. Long-term projections in 2010 suggested that, without any reforms, public pension expenditure was likely to reach 11.2% of GDP in 2020 and 18.4% of GDP in 2050. The Pahor government undertook a first attempt at increasing the retirement age, and was rejected by over 70% of the voters at a June 2011 referendum initiated by the unions and the parliamentary opposition. The Janša government launched similar reforms, this time backed by and coordinated with the social partners. Adopted unanimously by the National Assembly in December 2012, these reforms gradually increase the full retirement age for both men and woman to 65, or after 40 years of pensionable service for workers of at least 60 years of age. The increase in the retirement age will be felt most strongly by women, who were previously eligible for a full pension at the age of 63 or after 38 years of pensionable service. Men already had to work until the age of 65, but were able to retire without any discounts at 58 when they had paid contributions for 40 years. The changes in retirement age were complemented by other measures, such as the introduction of incentives for people to continue working after qualifying for official retirement and some changes in the pension formula that slowed future pension growth.

Citation:
Skledar, Štefan, 2013: Retirement Age Increases as Reforms Take Effect. European Industrial Relations Observatory Online (http://www.eurofound.europa.eu/eiro/2013/01/articles/si1301011i.htm).

United States

Score 7

The United States has had major difficulties developing sustainable pension policies. 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 $110,000 per year. The wage replacement rate of the public system is on average 45%, below the OECD average – with higher rates for people with lower incomes. Benefits from company-based and private accounts raise the wage-replacement rate to 80% for those who participated in these programs. But

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 failure to make full payments. 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 elderly poverty rate 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 very early by international comparison.

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.

Belgium

Score 6

Pension policy was a sacred institution that few politicians would dare consider reforming until the formation of the most recent government at the time of writing. A protracted political crisis amid the economic crisis forced coalition parties to implement drastic reforms that succeeded in cutting a number of loopholes in the system, closing down much of the early retirement options that were available, and improving the long-run sustainability of the system.

There are three important costs associated with this reform. First, it will likely further increase the risk of poverty for the elderly (pensions are typically low for people who did not have a "complete career," earned low wages or were self-employed and could not invest in a complementary private pension scheme). Second, it is not equitable inter-generationally, as it significantly reduces the return to pension contributions for younger generations. Extremely low interest rates also mean that complementary private pension schemes will be less rewarding for today's workers than for those currently retired. Third, it has not earned popular support, and thus begs politically to be re-reformed when public finances will permit. The long-run fiscal sustainability of the pension scheme is thus far from being guaranteed.

Bulgaria

Score 6

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 still not paying out many pensions.

The pension system is the major instrument for reducing poverty among the elderly. Data by the National Statistical Institute for 2010 indicate that the pension system reduced the share of the 65 and above age group at risk of poverty from 79% before transfers to 31% after transfers. From a comparative perspective, however, senior citizen poverty remains high. The Bulgarian pension system also suffers from a lack of intergenerational fairness and fiscal sustainability. Given the present demographic dynamics and the existing setup of the system, both the implicit public pension debt and the real pension burden will increase significantly over time.

Reforms of the pension scheme have begun, but have proven problematic in political terms. The GERB government adopted a pensions reform package in 2011, providing for an increase in the minimum retirement age (then 63 years for men and 60 years for women) by four months from January 1, 2012; a similar increase was to be applied on the first day of each of the following years, until the retirement age reached 65 years for men and 63 for women. The reforms were highly controversial, partly because the GERB government imposed them in spite of an earlier agreement with trade unions and business organizations to delay the increase of the retirement age till 2021. The reform package was vetoed by the socialist President Purvanov, but the National Assembly overturned his veto.

Citation:
National statistics institute, data for Bulgaria from Eurostat on the EU-SILC survey:
http://www.nsi.bg/ORPDOCS/SILC_1_en.xls

Ireland

Score 6

The Irish system of pension provision rests on three pillars: a public 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.

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 at the same rate since the onset of crisis, despite the general fall in incomes and a period of falling prices in 2010-11.

Ireland ranks among Europe's best – alongside the United Kingdom and the Netherlands – for 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).

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 pensions crisis unless the age at retirement 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 the current generation of pensioners enjoying the state pension or public sector pensions did not contribute adequately 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.

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 Party government, the National Party-led government has only implemented minor modifications. KiwiSaver is a popular option, and as of May 2012, nearly two million 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 Co-operation 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 and from some media voices to gradually increase the age of pension eligibility from 65 to 67 years.

Citation:
OECD Economic Survey: New Zealand (Paris: OECD 2011).

South Korea

Score 6

The average age of Korea's population is rising much faster than is the case in many other OECD countries. The share of the population that is 65 or more years old will increase from 7% in 2000 to 37% in 2050. This relatively quick demographic shift is taking place in part because 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. Korea now has the lowest birth rate of any OECD country and one of the lowest in the world. Old age remains a major source of poverty in Korea, as pension payments are low and most older people today lack coverage under a pension system that did not cover a large share of the workforce until the expansion of the program in 1999. The government has also failed to enforce mandatory participation in the system, and many employers fail to register their employees for participation. The pension system is currently fiscally sustainable and needs only small subsidies. This is because the pension 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 the contributors who have entered since 1999 retire. 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. Korea's pension funds also seem to be vulnerable to government interference. For example, in 2008 the government told the National Pension Fund to invest a larger share of its assets in Korean stocks, seeking to stabilize the stock market during the global financial crisis. Its financial sustainability is now hotly debated.

Spain

Score 6

Spanish pension policy largely achieves the goal of poverty prevention (7), but only partly the goals of fiscal sustainability (5) and intergenerational equity (5). The pension system represents the largest single piece of public spending (€120,000 million) and, in contrast with 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. Thus it seems that the goal of poverty prevention has been accomplished and now the elderly are perhaps less economically vulnerable than active but unemployed workers or other young inactive people without social benefits.

It cannot be said that the Spanish pensions system ensures equity among pensioners, the active labor force and the adolescent generation. The system actually does not have intergenerational equity as an aim since it is not explicit which burden carried by which generation should be the fair one. The model 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 as that generation did for the previous generation. To be sure, there are accumulated reserves and the rights of new retirees have always been respected so far, but the model is based on the expectancy that the following generation will be able to cover the necessities of the previous one and, therefore, it depends on maintaining growth and increasing productivity to compensate for the aging of the society.

This aging process is leading to an unsustainable population pyramid – worse in Spain than anywhere else in Europe – which, in combination with the impact of the crisis, reopened in 2011 – 2013 the debate about the long-term fiscal sustainability of the pension 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 is about to implement a radical reform (based on a report authored by a consultative committee of experts in 2013) which will accelerate the delay in the retirement age and will render more difficult the induced early retirement (an onerous mechanism frequently used in the past).

At the same time, the contribution period taken into account to calculate the amount of the pension will be significantly longer, thus encouraging Spaniards to complement their public pension plans with private schemes. The most crucial point is the cancellation of the pension indexation which can cause long-term effects on poverty and inequality. Nevertheless, even before this reform now in progress was announced, the Spanish pension policy had already introduced recent changes oriented to improving fiscal sustainability. Law 27/2011 on the updating and modernization of the social security system, which was approved under the socialist government, considered a delay of the official retirement age from 65 to 67 years old and also introduced the evolution of the life expectancy and the economic growth as parameters to bear in mind in future revisions of the system – which would take place in principle every five years.

Citation:
www.lamoncloa.gob.es/ConsejodeMinistros/Enlaces/280111-enlacepensiones.htm

France

Score 5

The French pension system is complex. It includes the so-called general regime, which applies to all private employees and is complemented by additional voluntary systems, in particular in large companies. 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 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 a French pensioner is 58.

Over the past 10 years, governments have tried to introduce reforms on several fronts, usually against fierce opposition: an increase in pension contributions; an increase in the number of years of contribution, to 42.5 years; and in 2008, a reduction of peculiarities or privileges granted to “special regimes.” These reform delays 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. And at the same time, deficits in the system continue. The Socialists, who had opposed limited reforms under the Sarkozy administration, are now forced to face drastic changes to improve the sustainability of the pension system overall. 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.

Italy

Score 5

Under the Monti government, Italy's pension policy has undergone an important reform which has very significantly improved its sustainability by a steep increase of the age of retirement to 67 years, and by reducing benefit levels for higher income groups. As a consequence no major reform will be needed in the next few years in spite of the serious demographic imbalance between an increasingly elderly population and the relatively smaller size of the younger generations. 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 worsened by the increasingly late or even entirely absent entry into the labor force of the younger cohorts due to the economic crisis.

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.

The role of complementary pension schemes is still too low and the fiscal policies adopted to encourage their diffusion have not been sufficiently bold.

Japan

Score 5

Given the rapid aging of the country's 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 reform is thus needed. For instance, national budgetary contributions to the system have risen in recent years from 1.5% of GDP to more than 2% despite concerns about the deficit. Thus, fiscal sustainability has not been fully recovered, although the gap is not expected to increase again soon.

After taking office in 2009, the DPJ-led government proved unable to pass legislation overhauling the pension system despite a January 2012 announcement that pension reform should be part of an encompassing reform of the tax and social-security system. The new LDP-led government has focused on reforms improving industrial competitiveness, although it has maintained its support for the 2012 bipartisan reform agreement.

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
NIRA Policy Review, Public Pensions and Intergenerational Equity, No. 59, Tokyo 2013 Kenichiro Kashiwase et al., Pension Reforms in Japan, IMF Working Paper WP/12/285, 2012
NIRA Policy Review, Public Pensions and Intergenerational Equity, No. 59, Tokyo 2013

Latvia

Score 5

The state pension system guarantees a minimum pension. The amount cannot be smaller than the state social-security benefit (LVL 45, or LVL 75 for those disabled from childhood) to which an additional sum added depending on the length of service. The minimum pension can fall between LVL 49.5 and LVL 76.5, less than half the minimum wage (LVL 200 as of January 2013). If this amount does in fact fall under the minimum wage, the recipient qualifies for public assistance. The average pension in 2012 was LVL 190, with only 1% of pensioners receiving under LVL 50. According to the Central Statistics Bureau, the at-risk-of-poverty rate for retired persons has risen from 11% 2011 to 16% in 2012.

Since the introduction of a three-tier pension system, which consists of the state compulsory pension scheme, the state-run mandatory funded pension scheme and the private voluntary pension scheme, the system has become more sustainable, and treats the various age groups in society more equitably. The European Commission Fiscal Sustainability Report 2012 concludes that the Latvian notional defined contribution pension system has low sustainability risks, given its expected reliance on second-pillar funds. Optimistic projections presume that Latvia will ultimately restore a 6% contribution rate to the second pillar (which was reduced during the economic crisis). In 2013, the rate had reached only 4%, and plans were to further delay reintroduction of the 6% rate until 2016.

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

Malta

Score value_6

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 and following recommendations from two distinct commissions, the government has enacted some reform measures. In 2007, the retirement age was modified and is in the process of rising to 65 for all pension recipients. However, the debate about sustainability and equity continues to dominate, especially because of pressures from the European Union, which claims that Malta's current system is unsustainable and that the pension age should rise further to make it so, as a result of the rising percentage of the population reaching pensionable age (21% in 2011). 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 (10% of pensioners are at risk of poverty).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.

Malta has no second or third pillar pension structures in place. Previously unsuccessful pension reform had indicated the introduction of a mixed pension provision, but as of the time of writing no progress has been made on this issue. There are no mandatory occupational pension schemes; although many individuals buy into a retirement scheme privately to boost their future state pensions, the global financial crisis resulted in a loss of confidence by investors as the banks and companies providing such schemes struggled. The state so far provides no public subsidizes for private pension plans. There is also no tax exemption for those who buy into private pension schemes, and hence no concrete incentives for people to do so.

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

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 as the population ages and the current system – while improving – might not be strong enough 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 entitlement, which the federal government is following.

Slovakia

Score 5

Slovakia introduced a three-pillar pension system along World Bank lines in 2004. During its first term 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 increased once more the role of the state in provisioning for the elderly, have improved the short-term financial situation of the public pension scheme and have made the pension system more redistributive. At the same time, however, they have weakened the nexus between contributions and benefits and have infringed upon intergenerational fairness and long-term sustainability.

Turkey

Score 5

The social security and general health insurance law, passed in 2006 and effective 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 reform's overarching goals of poverty prevention, intergenerational equity and fiscal sustainability were only partially met. According to the World Bank (2013), the reforms did improve pension coverage and should provide savings, yet the reforms were insufficient to ensure a pension system balance over the long run. Turkey's spending on pensions (7% of GDP) is still low compared to other OECD countries. More than half of pension spending is financed through budget transfers. The main reasons for this are the high system dependency ratio and generous eligibility rules, such as early retirement and low minimum years of service. As of 2013, the government again enacted pension reforms to address some of these issues. Reforms included the introduction of government-matching contributions and of transfers from defined benefit plans to defined contribution plans. As part of this transfer plan, employees will be able to claim a tax deduction of up to 15% on pension contributions. The reform was aimed at widening system coverage and making the system more progressive, and could be an important step in strengthening private savings and making pensions far more attractive.

However, these adjustments are to be phased in over a long period of time, at a rate that may be too slow to counter the effects of a maturing population. As a result, pension system deficits are expected to remain around 3% of GDP until the middle of the century.

Citation:
World Bank (2013) "World Bank Group - Turkey Partnership - Country Program Snapshot, Washington D.C.: World Bank.
Turkey: Regulating the pension system, Today's Zaman, 11.11.2012.

Croatia

Score 4

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 (World Bank, 2011). Given the ageing 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 not fiscally sustainable and intergenerationally fair. The public pension fund has shown a persistent deficit, which represents a significant risk to the stability of the system. Despite rules aimed at raising the retirement age and at penalizing early retirement, early retirement is widespread due to the stagnant labor market. No effective policy to raise the actual retirement age and to increase the employment rate exists.

Citation:
World Bank, 2011: Croatia: Policy options for further pension system reform. Zagreb (http://siteresources.worldbank.org/INTCROATIA/Resources/Croatia_Policy_Notes-Pension.pdf)

Cyprus

Score 4

Persons over 65 are the demographic with the highest risk of poverty in Cyprus, where the relative median income ratio is the EU's lowest. Expenditure on pensions as a percentage of GDP is the second-lowest in the EU-27. The existence of a 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. In addition to employer-based and social-insurance pensions, employees within the public sector also receive a gratuity upon retirement. Private-sector workers typically have access only to the government social-insurance program, along, in some cases, with private-sector provident funds. The social-insurance fund does not offer an adequate, secure or sustainable pension income; the program is facing major financial sustainability challenges due to demographic changes and structural weaknesses. Provident funds, where they exist, have serious weaknesses in terms of their effectiveness as retirement-income vehicles.

Although pension programs have been expected to face additional serious problems in the future, social actors, in particular trade unions, have been reluctant to agree to reforms. However, changes to government and private pension schemes took place in August 2011, aimed at reducing the cost of the system to the government as well as at improving equity with private-sector employees. The economic crisis led to cuts in benefits, including pensions, and changes to the retirement age and other provisions are expected in the future. Reductions in salaries and benefits will mean further reductions in pensions, increasing the risks of poverty for the elderly.

Citation:
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Greece

Score 4

The Greek pension system is a pay-as-you-go corporatist system. It is based on a multitude of occupational pension funds and it is also clientelist in the sense that, due to pressure from the strongest groups – such as the liberal professions and the public sector employees – the state has subsidized certain relatively privileged funds instead of others.

Greece does not attain the first objective of pension policy because the majority of pensioners receive the minimum pension. These are pensioners with a job record consisting of periodic short-term jobs or with few insurance contributions corresponding to a short span of working life. According to the World Bank, 14.50% of Greek senior citizens are relatively poor, ranking the country among the five European countries with the worst ratios of poverty for senior citizens. Women are included among the poorest of pensioners if they have never entered the labor market. This is the case for housewives who have no insurance contributions at all and rely on a very low-level non-contributory pension.

Pension policy does not serve intergenerational equity either. Between 1990 and 2010 there were repeated failed attempts to reform the pension system in order to stabilize the rising pension expenditures that threatened to derail fiscal policy. This failure was caused by the mobilization of 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.

A combination of high replacement rates, early retirement opportunities – particularly for married women with under-age children and public sector workers – and low insurance contributions has rendered the pension system financially unsustainable. 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.

Social insurance funds relied more and more on loans and subsidies from the state budget. A reform passed in June 2010, after the crisis broke out, and implemented in 2011 was a first step toward streamlining the pension system. The reform involved lowering replacement levels, raising contributions, preventing early retirement and merging dozens of small social insurance funds into a few larger ones.

Hungary

Score 4

Hungary introduced a three-pillar pension system along World Bank guidelines, with a strong mandatory second pillar in 1997. Between 2010 and 2011, the Orbán government abolished the second pillar. It then used the nationalized capital, worth almost 10% of GDP, for reducing the budget deficit and for financing tax cuts, thereby drastically reducing the sustainability of the pension system. The final nail in the coffin of the second pillar was the decision in late 2011 to permanently divert pension contributions of the 3% of individuals that, despite considerable pressure, had decided to remain in the second pillar to the first pillar. To further improve the short-term fiscal situation of the pension system, the Orbán government also eliminated some options for early retirement. In doing so, it partly relied on retroactive legislation and thus deprived workers who had already retired of their pensions. At the same time, however, the Orbán government has allowed women who have worked or raised children at home for 40 years to retire without any reductions in benefits and has anxiously avoided any pension cuts for this group. The crackdown on the pension system's second pillar and on early retirement has strongly increased uncertainty over income in old age in Hungary.

Portugal

Score 4

Pensions policy has been one of the most scrutinized aspects of Portugal's 2011 bailout, and has been one of the domains in which the government has sought to reduce public expenditure. To that end, a number of cuts and measures have been enacted. A 2013 study indicated that on average the government has saved more than €2.5 billion on pensions since 2011, reducing each pensioner's income by an average of €733.

While these cuts have hit the highest pensions especially hard, they have also affected poorer pensioners – damaging the goal of preventing poverty among the elderly. A study indicated that in 2010 – 2011 three out four pensioners in Portugal received a pension of €500 or less, and that the risk of poverty among the elderly is higher in Portugal than elsewhere in the European Union. This effect is likely to be aggravated, as cuts in pensions were compounded by the recession and rising unemployment, which weakened overall family income.

The government has sought to reinforce the fiscal stability of the pension system. To that end, the age of retirement is planned to increase from 65 to 67 years (although as of May 2013 that had not yet been implemented), and the government has also reduced future public sector pensions. Nevertheless, this stability was made difficult by the diminishing population – as both birth rates and immigration fell – and by the economic recession and unemployment, which inevitably reduce social security revenue.

The current pensions system does not appear to ensure intergenerational equity. While the government has maintained this as a goal of its reforms, there is little or no evidence of this being achieved.

Citation:
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Romania

Score 4

In Romania, low fertility rates combined with the massive outmigration of working-age citizens have contributed to a rapidly ageing population. Forecasts for 2050 predict that 43% of the population will be over the age of 65 – an dramatic increase from 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 sectors, where workers on 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.

The inconsistencies of pension policy as well as the volatile budgetary and economic situation and the low employment rates in the Romanian economy have severely inhibited the fiscal sustainability of the pension system. Fiscal imbalances will be exacerbated at least in the short term by a January 2013, decision by Parliament to raise pensions, bringing the total pensions budget up to €11.5 billion. This politically highly popular move will, however, soon be accompanied by a raise in the retirement age for women to 60 years and men to 65, which should help with longer-term sustainability.

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