Social Security

International Update:

Recent Developments in Foreign Public and Private Pensions

August 2009

Europe

Baltic States

In an effort to stem rising budget deficits, the governments of Estonia, Lithuania, and Latvia have implemented temporary measures to reduce the financial burden of their public pension systems. In **Estonia**, a law went into effect on June 1 that reduces employer contributions to mandatory second-pillar individual accounts and increases contributions to the state-run first pillar through 2012. In addition, employees may choose to reduce their second-pillar contributions during this period. Under the new law, the employer contribution rate to the second pillar will be 0 percent of gross payroll through 2010, and it will increase to 2 percent in 2011 and to 4 percent in 2012, where it will remain fixed. Because the total employer contribution rate of 20 percent to the first and second pillars remains the same, the first-pillar contribution rate will increase to 20 percent through 2010, and then it will decrease to 18 percent in 2011 and to 16 percent in 2012. Employees who choose to reduce their second-pillar contribution rate in this period will contribute 0 percent through 2010, 1 percent in 2011, and 2 percent in 2012. Finally, employees who choose to continue their contributions throughout this period will receive employer contributions of 6 percent to their second-pillar individual accounts and 14 percent to the state-run first pillar from 2014 through 2017. However, this measure may be postponed a year if the national growth rate falls below 5 percent. Under the previous rules, employers contributed 4 percent to second-pillar individual accounts and employees contributed an additional 2 percent, for a total of 6 percent. According to the government, reallocating employer contributions to the state-run system will increase state revenues by approximately 1.6 billion kroons (US$145.4 million) this year and by approximately 3 billion kroons (US$272.8 million) in 2010.

Similarly, on July 1 the government of **Lithuania** reduced the contribution rate to second-pillar individual accounts and increased the rate for the first-pillar pay-as-you-go system. The contribution rate to second-pillar individual accounts was reduced from 3 percent to 2 percent of gross salary through 2010 and will increase to 5.5 percent in 2011, to 6 percent in the 2012–2014 period, before stabilizing at 5.5 percent in January 2015. This marks the second time this year that Lithuania has reduced the contribution rate to the second pillar; in January it was reduced from 5.5 percent to 3 percent. Contributions to second-pillar individual accounts are drawn from a total employer/employee contribution of 26.35 percent (23.85 percent from the employer, 2.5 percent from the employee). The government expects the reallocation of contributions to increase state revenues by approximately 99.2 million litas (US$41.0 million) this year and by approximately 194.3 million litas (US$80.3 million) in 2010.

Finally, on July 1 the government of **Latvia** reduced the amount of monthly pension benefits to pensioners by 10 percent and to working pensioners by 70 percent. The reductions will be in effect until the end of 2012. The measure is a part of a larger package of spending cuts required to unblock approximately €1.2 billion (US$1.7 billion) in aid from the International Monetary Fund and the European Union. The government is hoping to save approximately 500 million lats (US$1 billion) through these measures.

Sources: "State Social Insurance System of the Republic of Lithuania," State Social Insurance Fund Board, 2009; "Estonian Gov't Takes Contribution Holiday," *IPE*.com, April 16, 2009; "Lithuania: Pension Contribution Cuts May Be Taken To Court," *Baltic Business News,* April 19, 2009; "Lithuanian President Signs into Law New Cut in Pension Contributions," *Baltic Business Daily*, May 8, 2009; Watson Wyatt Worldwide, *Global News Briefs*, June 2009; "Latvia to Cut Pensions, Salaries to Avert Crisis," *Reuters,* June 11, 2009; "Budget Amendments Come Into Force Today," *Latvian News Agency*, July 1, 2009.

The Americas

Colombia

On July 16, President Uribe signed into law a financial reform bill with provisions that modify the country's system of individual retirement accounts. Law

1328 broadens the system's investment rules and provides coverage for workers who do not meet the requirements for a minimum benefit under the public pay-as-you-go (PAYG) system or the individual account system.

Beginning in 2011, pension fund management companies (AFPs) will be required to offer three types of funds with varying degrees of risk: conservative-, moderate-, and high-risk investments. Currently, AFPs are permitted to offer only one type of fund with limited investments. The government will design and set up regulations for these multifunds that include the following:

- A new administrative fee structure.
- Allowable investments and management rules for these investments.
- Required minimum rates of return.
- Information that AFPs must provide to account holders.
- Incentives for various groups (such as labor unions and consumer organizations) to set up low-cost financial education programs in conjunction with institutions (such as universities).

Another provision of Law 1328 sets up Periodic Economic Benefits (Beneficios Económicos Periódicos, or BEP) for workers who have reached the normal retirement age for the public system (age 60 for men and age 55 for women, raised to 62 and 57, respectively, in 2014), but do not qualify for a minimum benefit under the PAYG or individual account system. BEP will be financed by the solidarity pension fund, which was previously set up to subsidize only low earners covered by the social insurance system. The solidarity fund receives monthly contributions from higher earners (those who earn more than 16 times the minimum wage) and the government. Total BEP benefits awarded may not exceed 50 percent of the value of the solidarity fund. No implementation date for the BEP has been announced.

In Colombia, a worker may choose between the public PAYG system and the individual account system and may switch membership every 5 years up to the last 10 years before retirement. However, less than 40 percent of the labor force is currently covered by either system. Of those covered workers, only about 45 percent make regular contributions, and some 40 percent of contributors will not qualify for a retirement pension under current rules because they have not made enough contributions. In addition, about 40 percent of workers earn the minimum wage or less. The minimum pension is equal to the country's minimum wage.

Sources: *Social Security Programs Throughout the World: The Americas, 2007*; "Pensiones en Colombia: Análisis y Propuestos," BBVA, el 6 de mayo de 2009, "Económico Periódico Para Quienes No Alcancen Pensión," elespectador.com, el 2 de junio de 2009; "Los Multifondos Entrarán en Operación en 2011," *La República*, el 9 de julio de 2009; Ley 1328, el 15 de julio de 2009; "Sanciona Uribe Ley de Reforma Financiera para Mejorar Pensiones," Agencia Mexicana de Noticias, el 16 de julio de 2009.

Asia and the Pacific

Bilateral Agreement

On July 16, Australia and New Zealand signed a Memorandum of Understanding to allow portable retirement savings between the two countries. This arrangement will permit New Zealand workers to transfer their Australian superannuation funds to their KiwiSaver accounts after they return to New Zealand and, conversely, allow Australian workers to transfer KiwiSaver accounts to Australian superannuation funds after they return to Australia. Both countries must develop and pass legislation in order to implement the portability measures. The agreement is part of the Single Economic Market initiative to encourage the movement of "people, trade and capital" between the two countries.

The legislation is expected to include the following stipulations:

- Funds in a KiwiSaver account (including any government subsidy) may be transferred to a superannuation scheme regulated by the Australian Prudential Regulation Authority. To qualify, an individual must be immigrating permanently to Australia.
- Australian retirement savings may be transferred to a KiwiSaver account.
- KiwiSaver providers are not required to transfer funds to or from Australia. However, KiwiSaver account holders may transfer their funds to a provider that offers this service.
- After the fund transfer, the date an individual could access the funds varies. New Zealand KiwiSaver funds transferred to Australia may be withdrawn at age 65, and Australian superannuation funds transferred to New Zealand may be

withdrawn at age 60 provided the individual meets certain qualifying conditions.

Until the agreement enters into force, New Zealanders must leave their superannuation funds in Australia until age 65, and Australians may withdraw their KiwiSaver funds (except for the member tax subsidy) a year after they emigrate permanently.

Australia's Tax Office estimates there are A$13 billion (US$8.6 billion) in "lost accounts"—superannuation accounts that have not been claimed by any individual, with up to 25 percent belonging to New Zealanders who have left Australia permanently.

In Australia, since 1992, employers are required to contribute 9 percent of an employee's earnings to a superannuation account. However, New Zealand's KiwiSaver, introduced in 2007, is voluntary. But once workers set up a KiwiSaver account, both employees and employers must contribute a percentage of employee gross earnings: employees, at least 2 percent and employers, 2 percent.

Sources: "Q and A on Retirement Savings Portability," New Zealand Tax Policy, July 2009; "Trans-Tasman Superannuation Portability Nears," SCCONZ, July 15, 2009; "Ministers Take Single Market Forward, Sign up to Trans-Tasman Retirement Savings Portability," Minister of Finance, press release, July 16, 2009.

Reports and Studies

U.S. Census Bureau

The U.S. Census Bureau recently released *An Aging World: 2008*—a report commissioned by the National Institute of Aging—which examines the phenomenon of rapid population aging and the challenges it presents to both developed and developing nations. According to the report, the proportion of the global population aged 65 or older will double between 2008 and 2040, from 7 percent to 14 percent. Population aging will be especially rapid in the developing world, with a rate of growth more than double that of developed nations.

Some of the report's key findings include the following:

- Within 10 years, there will be more people aged 65 or older than children aged 5 or younger for the first time in world history.
- The fastest growing portion of the world's population is the "oldest old," people aged 80 or older. This group is projected to increase by 233 percent between 2008 and 2040, compared with increases of 160 percent for the population aged 65 or older and 33 percent for the population from all age groups.
- Increasing childlessness among recent cohorts of women raises questions about the provision of care when these cohorts reach advanced ages. In the United States, the percentage of women who are childless increased from 10 percent in 1970 to 20 percent in 2006.
- The old-age dependency ratio—the share of those aged 65 or older as a proportion of those aged 20 to 64—is projected to increase in all countries between 2005 and 2040, and it will more than double in Italy, Japan, Spain, and Turkey. This will put increasing pressure on health and pension systems.

The full report is available online at http://www.census.gov/prod/2009pubs/p95-09-1.pdf.

Sources: *An Aging World: 2008*, U.S. Census Bureau, June 2009.

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